



meridian
ASSET MANAGEMENT (C.I.) LIMITED

INVESTMENT MEMORANDUM

International equities have held steady over the last quarter and show a modest rise. However international bond markets have shown a mixed performance as investors increasingly worry about the vast quantities of debt being taken on by many governments. Foreign exchange movements have been limited but gold continues its strong rise as central banks and other investors have stocked up bolstering its traditional attraction, not always manifested, as a store of value in uncertain times.

The tables below detail relevant movements in markets :

International Equities 31.07.24 - 31.10.24

Total Return Performances (%)				
Country	Local Currency	£	US\$	€
Australia	+1.8	+2.0	+2.1	+1.7
Finland	+0.7	+0.9	+1.0	+0.7
France	-2.0	-1.7	-1.6	-2.0
Germany	+3.5	+3.7	+3.8	+3.5
Hong Kong	+13.4	+13.8	+13.9	+13.5
Italy	+2.7	+3.0	+3.1	+2.7
Japan	-2.4	-3.7	-3.6	-3.9
Netherlands	-11.0	-10.8	-10.7	-11.0
Spain	+5.5	+5.8	+5.8	+5.5
Switzerland	-3.9	-2.2	-2.2	-2.5
UK	-1.6	-1.6	-1.5	-1.8
USA	+3.8	+3.7	+3.8	+3.5
All World Europe ex UK	-2.4	-1.9	-1.8	-2.2
All World Asia Pacific ex Japan	+4.0	+4.8	+4.9	+4.6
All World Asia Pacific	+1.7	+1.8	+1.9	+1.6
All World Latin America	+0.2	-3.7	-3.6	-3.9
All World Emerging Markets	+5.2	+5.8	+5.9	+5.6
All World	+2.6	+2.5	+2.6	+2.3

Source : FTSE All World Indices

FTSE UK Government Securities Index All Stocks (total return) : -1.9%

International Bonds - Benchmark Ten Year Government Bond Yields (%)

Currency	31.07.24	31.10.24
Sterling	3.97	4.44
US Dollar	4.03	4.28
Yen	1.05	0.93
Germany (Euro)	2.30	2.39

Sterling's performance during the quarter ending 31.10.24 (%)

Currency	Quarter Ending 31.10.24
US Dollar	+0.3
Canadian Dollar	+1.2
Yen	+1.7
Euro	-0.2
Swiss Franc	-1.3
Australian Dollar	-0.2

Other currency movements during the quarter ending 31.10.24 (%)

Currency	Quarter Ending 31.10.24
US Dollar / Canadian Dollar	+0.8
US Dollar / Yen	+1.1
US Dollar / Euro	-0.5
Swiss Franc / Euro	+1.2
Euro / Yen	+1.6

Significant Commodities (US dollar terms) 31.07.24 - 31.10.24 (%)

Currency	Quarter Ending 31.10.24
Oil	-9.6
Gold	+16.2

MARKETS

Despite some weakness at the end of the quarter, overall equity markets ended the quarter slightly higher. The FTSE All World Index showed a total return in local currency terms of +2.6%, in sterling terms +2.5% in US dollar terms +2.6% and, in euro terms, +2.3%. Looking at individual countries and areas, firstly in local currency terms, the best performers were the FTSE All World Emerging Markets Index, +5.2%, the FTSE All World Asia Pacific ex Japan Index, +4.0%, and the FTSE USA Index, +3.8%. On the negative side were the FTSE All World Europe ex UK Index, -2.4%, the FTSE Japan Index, -2.4%, and the FTSE UK Index, -1.6%. Turning to sterling adjusted figures, the weakest performer was the FTSE All World Latin America Index where a small positive local currency return, +0.2%, became -3.7% in sterling terms. The FTSE Japan Index also returned -3.7%. The FTSE All World Europe ex UK Index remained in negative territory, -1.9%, a slightly lower return than the FTSE UK's index, -1.6%.

Turning to the international bond market, the feature was the weakness of the UK government bond market, exacerbated right at the end of the quarter by a negative reaction to the UK budget on the 30th October as the market digested the very large borrowing requirements in future years. The gross redemption yield on the ten year benchmark government bond yield rose by 47 basis points to 4.44%. There was also some weakness in the US government bond market with the ten year Treasury bond's gross redemption yield rising by 25 basis points to 4.28%. The yield on the ten year German Bund rose slightly by 9 basis points to 2.39%. Bucking the trend was the yield on the ten year Japanese Government Bond which fell by 12 basis points to 0.93%.

In the foreign exchange markets, movements were fairly limited but nervousness about the UK budget pulled sterling back at the end of the quarter. Against the Swiss Franc, sterling fell by 1.3% and against the euro and Australian dollar it fell by 0.2%. On the other hand, it rose by 1.7% against the yen (weak at the end of the quarter after big electoral losses for the LDP), by 1.2% against the Canadian dollar and by 0.3% against the US dollar.

In the commodity markets, the oil price remains under pressure despite the political turmoil and, as measured by Brent crude, fell by 9.6%. On the other hand, gold has had a strong quarter, rising by 16.2%, helped by central bank purchases amongst other factors as it is being viewed by some as a store of value in uncertain times.

ECONOMICS

This is a time of change. This is a time of opportunity. This is a time of contrition. To no group of people does this belong more than our dear political classes and in this time of change recently elected politicians are steering through their promises and pledges and now sit in the driving seat of government, which these days is a far more difficult place to be than in opposition. Regardless, policy decisions and manifesto commitments are becoming reality. Those who are yet to face the polls offer carefully targeted messaging that may appeal to the heart, if not always the brain. Anything to get across the line. Beyond the pure politics there is a practical need to ensure that their electors live in a country that is competitive, attracts investment and can trade on the best possible terms and, in a global economy with complicated cross border competition, there is a world of difference between getting policy right and getting it wrong. At a time of tendency towards the political extremes and personality politics optimal economic policy risks becoming a secondary goal. Meridian's conundrum is to write this and other monthly economic reviews without opening a Pandora's Box of politicising what is an economic view but in failing to seek to acknowledge today's politics, in act and in implication, would suggest it does not play a significant hand.

Thomas Jefferson's quote that "The government you elect is the government you deserve" makes for a powerful statement and in the twenty first century it can be characterised by voting intentions and the list of voters' key election issues. A YouGov poll in June 2024 asked UK voters what was their single most important issue in deciding how to vote in the July General Election. The cost of living was most often cited, with 26%, second was immigration & asylum (18%), third was the economy in general (16%) and fourth was health. Crossing over to the United States, a pre-election poll of voters carried out by Statista at the end of August went a step further and split its findings into Republican, Democrat and Independent voters. 31% of Republicans said inflation/prices was their number one concern (Democrats 15%), immigration 25% (Democrats 3%), jobs and the economy 15% (Democrats 9%). No other leading issue concerned more than 7% of Republican voters. By contrast, 14% of Democrats cited healthcare (Republicans 2%), abortion was also 14% (Republicans 5%) and climate change & the environment 12% (Republicans 2%). In a month in which United Kingdom's last coal-fired power station and last steel blast furnace both closed it is noticeable that green matters have slipped down the priority list in U.K. and almost all other countries. This memorandum is being written just a few days before the US Presidential and Congressional elections and in the white heat of campaigning all of these concerns are uppermost in the thoughts of all candidates. Perhaps an economist would be encouraged by the thought that the number one concern, both in the United Kingdom and the United States, is inflation and the effect it has had on the cost of living - assuming that victorious politicians will give it the priority it deserves. The tangible effect it has on people's lives should ensure the focus on economic discipline and growth will lead to the right decisions being made, supported by the third most significant issue in both countries - jobs and the economy. Immigration is, no pun intended, a new frontier as a political priority and is red meat to some politicians.

This year of elections is drawing to a close and the natural inclination in this memorandum is to attempt to understand what economic effect a new government's likely direction will have on a country. June's investment memorandum provides a good summary of Meridian's view of national elections in the first half of the year. This is the last memorandum before the outcome of the American elections is known and there is much focus on the race to be President but, equally important, are elections in Congress where all 435 seats in the House of Representatives and a third of the 100 seats in the Senate are also being contested. The battlegrounds for victory are very much aligned with the Statista polling but of most interest here is what will affect the ability of American companies to trade and create jobs and wealth? How will taxation affect consumer spending and investment and what foreign policy changes could affect world trade? Any new policy decisions will need to be taken with due regard to the oversized budget deficit and the level of indebtedness that the country carries. The US has been more successful than most other leading economies in bouncing back since COVID. Its economy grew in real terms by 1.9% in 2022, 2.5% in 2023 and is forecast to grow 2.6% in 2024. The figures for the eurozone are 3.4%, 0.5% and 0.9% and United Kingdom 4.3%, 0.1% and 0.7%. Research by the Federal Reserve explores why the recovery in the United States has been greater than in other similar economies and, as always in economics, fails to draw any concrete conclusions but points to successful government discretionary spending, a much higher level of new business creation and more borrowers, both individuals and corporate, sheltered from the fast rise in interest rates by being on fixed rates. All of these have helped keep consumers spending and also kept the job market remarkably resilient with unemployment only rising above 4% a few months ago; this is a level that compares very well in an historic context. These figures also support Meridian's choice to maintain a high exposure to American companies in portfolios where the mandate allows. In truth, typical U.S. companies held in portfolios are global in their outlook but they will tend to have a higher exposure to the US domestic market than companies based elsewhere and culturally will be very shareholder focused.

Both the Democrats and the Republicans offer policies that are emblematic of their different approaches. The Democrats see a 21% rate of corporation tax as too low and wish to raise it to 28% and double the tax rate American multinationals pay on foreign earnings to 21%. The Republican

Party, or more accurately Donald Trump (the office of President is afforded under 1934 legislation the ability to levy tariffs on other countries with the intention of reducing those countries' tariffs on the United States) threatens to increase tariffs on all imports under his 'Reciprocal Tariff Act' and has mentioned 10% to 20% with particularly aggressive treatment for China. Talking about Europe in October he said "They don't take our cars. They don't take our farm products. They sell millions and millions of cars in the United States. No, no, no, they are going to have to pay a big price.". What is known by any follower of elections is that what is said will happen and what actually happens can be two quite different things and there is more reason to believe that statement when considering the United States because of the rules around the apparatus of government.

The US checks and balances between the executive, judicial and legislative branches of government are carefully designed to ensure that control over power is managed responsibly. Congress is responsible for drafting proposed laws but the President can veto legislation and the Supreme Court can overturn unconstitutional law. Supreme Court Justices are nominated by the President but the Senate can confirm or reject the President's nominees and in extreme circumstances can remove the President. In many ways there is a risk if one party has the Presidency, control of both chambers of Congress and there is a favourable predominance of either liberals or conservatives amongst the nine Supreme Court judges. At present there is a Democrat President, a Democrat Senate but a Republican House of Representatives meaning nobody gets it all their own way. The risk is that any departure from the status quo of split power presents the possibility that a dominant party position may lead to a more extreme legislative programme and decisions that may not be for the greater economic good. There is a lot to be said for a divide across the Presidency and Congress when the antagonistic nature of the Democrat and Republican parties can slow down any rate of change.

Perhaps it is wrong to get carried away with some of the loudest political rhetoric which tends to attract the largest headlines. The ability of one person to change the Constitution of the United States is, by design, limited. All countries craft their Constitutions in such a way that there are inherent barriers to overbearing control from one or a small number of people. Usually this is informed by the history of the country and a good example is Italy whose Constitution was re-written after the Second World War with the intention of avoiding any potential for narrow dominance. The resultant emphasis on legislative power rather than executive power sees two chambers with largely equal powers but the downside to the structure of government that has been created is that the spread of power is invariably wide to the point that its chambers are filled with a large number of parties and minority governments come and go with great frequency. Italy has had 31 Prime Ministers since the Second World War, Britain has had 19 (counting Wilson twice) and this has been swelled somewhat by a rather busy period for the Downing Street removals men in recent years.

The most extreme critics of Donald Trump claim that four more years of his rule would lead to a gradual concentration of powers into his hands through engineered changes to the rules of government which would, in turn, lead to an erosion of democracy and civil rights. This is much less likely than some claim as, firstly and as mentioned above, there are carefully designed checks and balances in the administration of power and, secondly, it would require full control of Congress. For a number of changes to happen, such as amendments to the Constitution of the United States, a two thirds supermajority by each body of Congress is required and in what is likely to be a close election, as is usually the case, the chances of the Republican Party achieving such dominance is close to zero.

The purpose of writing on this subject is clear. At times, politics can be more important than economics and when the largest economy in the world, which is enjoying a growth rate above all other G7 countries, faces an election where significant policy shifts are possible, there are grounds for concern. Again, repeating earlier words, there is much to be said for the status quo but the Congressional Budget Office is not alone in warning about the need to steer policy in a way that addresses the growing mountain of national debt, with every good reason. Debt is manageable but is also a constraint on policy. That will remain to be true well into the future. This is being written in the first few days of November and just after the UK's Labour Party's first budget with the reaction of

debt markets drawing quite a lot of attention. Voters have made their choice and have the government they have chosen for five years. Labour, with its comfortable majority can introduce policy as it sees fit and not worry too much about opinion polls. Bond markets have no loyalty nor obligation and buyers of UK Treasury Gilts that are here today can be gone tomorrow. The mechanics of the market are easy to understand and falling demand means lower prices which means a higher cost of borrowing as buyers of gilts want a greater reward for lending money to the government. The 10 year yield on Gilts is, at the time of writing 4.42%, having risen from below 4.0% in August. It's fair to say that there is an amber flashing light on the dashboard and the government will need to balance the demand for public services with the need to raise taxes in a way that doesn't damage growth. One independent judge on how well they manage that will be the bond markets which have no party loyalty and can easily vote with their feet. Unfortunately, a negative assessment from them is most unwelcome. It has already cost one Prime Minister her job.

Either debt levels will have to change or perceptions around debt levels will have to change. The Global Financial Crisis and COVID have forced nearly all governments to borrow heavily and the United States, UK, France, Italy amongst others have levels of debt not seen since the 1960s and the immense fiscal pressure created by ageing and economically inactive populations is a new headwind to face in this century. Central government funding is one issue, regional funding is another and the Financial Times reported on 23rd October that Hampshire Country Council now spends 83% of its budget on social care. This year it will have a shortfall of £132 million against budget revenue of £1.2 billion.

For a long term investor the choices amongst the mainstream investment categories do not really change. The economics and the politics do. We have lived through a decade of exceedingly low interest rates which, by design, discouraged bank deposits and incentivised borrowing. A devastating burst of inflation in 2022 moved the goalposts and indiscriminately devalued anything offering a fixed rate of interest, such as bonds. Inflation, like COVID, now appears to be beaten (famous last words!) with higher interest rates being the price to pay. This along with the higher levels of debt in circulation means that there is an unusual degree of uncertainty around bond markets and Meridian continues to choose to be largely absent from this market. As we go into the final two months of the year well diversified equity portfolios have had a satisfactory year and there is a reasonable expectation that the growth trend will continue, unevenly, in the medium to long term thanks to, or despite, the decisions of politicians.

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