Market Memo – 6th of April 2025

by Léon Kirch, Chief Investment Officer, Managing Partner

Dear Clients and Partners,

A few key takeaways:

- **Tariff Shock**: Trump's sweeping tariffs mark a major policy shift, raising US recession risks (JPMorgan puts odds at 60%) and unsettling global markets.
- **Debt & Rates Strategy**: With U.S. debt at $36.56T and interest payments outpacing defense spending, tariffs may be a tactic to lower rates.
- **Fed on Hold**: Despite market hopes, the Fed is likely to stay sidelined in 2025 amid sticky inflation and limited room to ease.
- **Market Turmoil**: S&P 500 is down 13.7% YTD, Nasdaq down 19% — worst 2-day drop since 1950. Europe remains relatively resilient.
- **Selective Positioning**: Underweight U.S. equities; overweight German mid-caps and quality European names poised to benefit from fiscal stimulus.
- **Opportunistic Buys**: Gradually building positions in NVIDIA and Novo Nordisk as long-term fundamentals remain compelling.
- **Fixed Income Stance**: Favouring short-duration, high-quality bonds; selectively re-engaging in longer maturities.
- **Long-Term Lens**: Navigating volatility with discipline — focused on fundamentals, not headlines or fear.

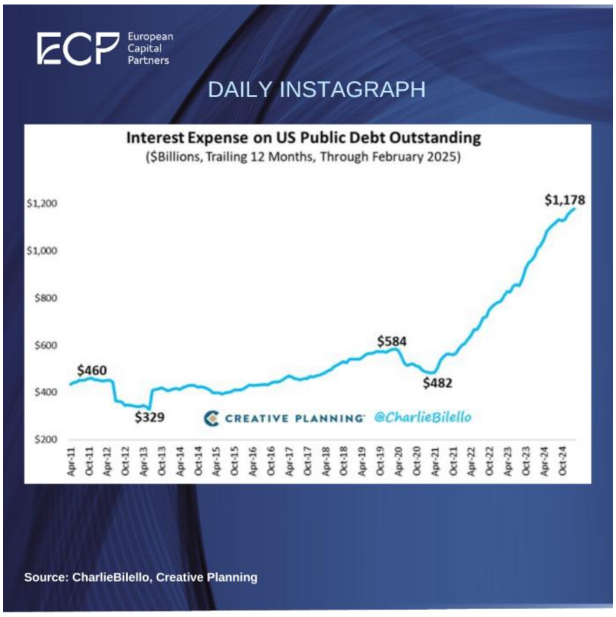
The Trump administration — we now call the new alchemists of economics and finance — may have unleashed the genie from the bottle with their sweeping tariff announcements. Tariffs have pushed U.S. trade policy back to levels not seen since 1908.

While the symbolism is powerful, the implications are far-reaching and financial markets are the first to feel the heat. 2025 equity performance so far has been shaped by a sharp questioning of overconcentrated exposure to U.S. markets and the Magnificent 7, alongside geopolitical disruption and increasingly unpredictable policy shifts. Amid the noise, we remain focused on the fundamentals — and on serving you with the calm, disciplined approach you've come to expect.

The Alchemists of Finance

Some observers suggest that Trump's tariff strategy is less about protectionism and more about engineering a slowdown to push interest rates lower — a deliberate attempt to manage the cost of refinancing the $9 trillion in U.S. debt maturing by 2026.

The United States carries a staggering $36.56 trillion in total debt. Over the past 12 months, the country has spent $1.178 trillion on interest payments alone - surpassing the $886 billion allocated for defense. This stark reality underscores the critical importance of U.S. interest rate policy, both in the short and long term.



With the 10-year Treasury yield now below 4%, the strategy may be working — at least in the short term.

Still, it feels like a successful operation where the patient may not survive. Now is not the time to experiment with economic alchemy.

Recession risks are rising. JPMorgan now puts the probability of a U.S. recession over the next 12 months at 60% — the highest level they've forecasted since early 2020. This view is informed by several converging indicators: a significant tightening of financial conditions, weakening consumer confidence, contracting manufacturing activity, and early signs of deterioration in the labor market. Moreover, the recent surge in trade tensions and associated market volatility have further increased downside risks to growth. JPMorgan notes that if tariffs remain in place — or escalate — the drag on corporate margins and consumer purchasing power could be substantial. In such a scenario, they caution that the U.S. economy could slip into a recession even without a traditional trigger like a housing collapse or credit crunch.

Are these tariff announcements simply negotiation tactics? A dramatic opening move designed to force new trade terms and extract concessions? It's possible. Trump's track record suggests a preference for brinkmanship: raise the stakes, stir the headlines, and then use the pressure to reset the terms of engagement. By opening with maximalist tariff measures, the administration may be aiming to force trading partners into bilateral negotiations on terms more favourable to the U.S., under the guise of 'America First' industrial policy.

This strategy isn't unprecedented — similar tactics were used during the first term to strike deals with Mexico, Canada, and China. But this time, the stakes are higher. The global economy is more fragile, and any prolonged disruption to supply chains or trade volumes could have systemic consequences. The markets, in turn, are left guessing: is this part of a carefully choreographed playbook, or the first act of something more disorderly?

Regardless, the risk is that confidence erodes before clarity arrives.

And where is the Fed?

There is growing debate around the balance between fiscal dominance and monetary independence in the U.S. Belgian economist Bruno Colmant recently outlined a scenario in which political pressure pushes the Federal Reserve to support debt issuance at real negative yields.

In such a world, inflation-adjusted returns would steadily erode purchasing power, and the dollar's global appeal could suffer. While we don't share the more dramatic conclusions, we do agree that the monetary playbook is shifting. Rising debt, persistent inflation, and a realignment of geopolitical interests are rewriting the rules. Many investors are hoping the Fed will ride to the rescue. But that may be a misread.

Despite mounting stress, we expect the Fed to remain on hold for the rest of the year. Market pricing for significant easing may be overly optimistic. With inflation proving sticky and the labor market softening only gradually, the Fed has little room to maneuver.

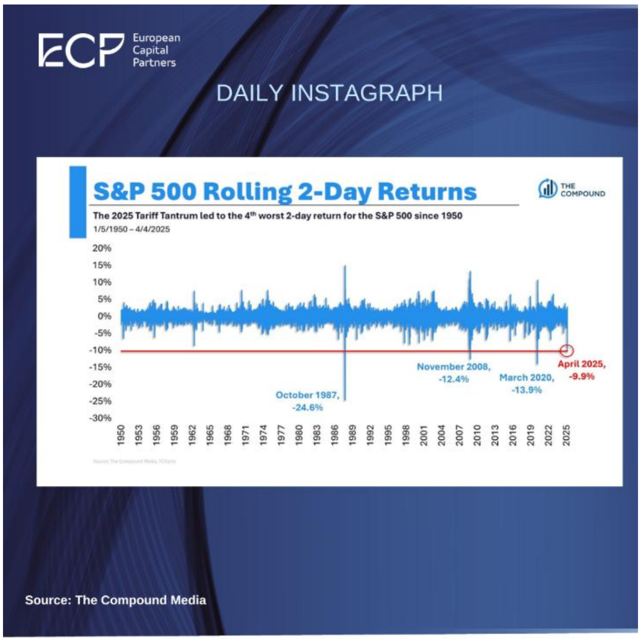
In short, monetary policy may not be the safety net markets are counting on.

Markets at a Glance

The headlines are loud. Sentiment is swinging. Volatility is back.

The S&P 500 is down approximately 13.7% year-to-date, with the Nasdaq off more than 19%. Thursday and Friday last week marked the 4th worst 2-day return for the S&P500 since 1950.

In contrast, European markets have shown relative resilience, supported by early-year rotations into undervalued equities.



To put things in perspective, the drawdown of the S&P 500 during the global financial crisis was 56.7% and during the Covid crash was 33.9%. As illustrated in the graph on the right side, these drawdowns were temporary. While the sea of red is painful in the short run, equity markets have always rebounded relatively quickly.

U.S. government bond yields have dropped meaningfully, with the 10-year Treasury now under 4%, down from 4.8% in January. The dollar has weakened significantly, with EUR-USD trading around 1.0956.

Meanwhile, the U.S. high-yield market has seen its sharpest sell-off since 2020. Junk bond spreads have widened by a full percentage point to 4.45%, reflecting concerns about slowing growth and rising credit risk. As the Financial Times noted, corporate credit is acting as the "canary in the coal mine."

Investor concern is real: tariffs could undermine earnings, weaken demand, and accelerate defaults — particularly for lower-rated issuers.

Our Positioning

In the face of mounting uncertainty, our positioning remains deliberately conservative, selective, and guided by long-term fundamentals.

We have USD exposure mainly through our stock investments. Despite the current volatility, we believe the U.S. dollar remains the world's reserve currency and deserves its place in our asset allocation.

We remain underweight U.S. equities (compared to MSCI World), particularly in sectors most exposed to global supply chains and policy volatility. Conversely, we maintain a constructive view on select European companies with strong balance sheets, pricing power, and stable demand.

We have increased our exposure to German mid-cap companies within our European Value Fund throughout 2025. These companies — often global leaders in engineering, industrial technology, and niche manufacturing — stand to benefit from the policy orientation of the new Merz government. With Germany set to ramp up infrastructure and defense spending, the businesses we are invested in are well positioned to capture both public and private investment flows over the coming years.

In times of market stress, price action tends to overwhelm business fundamentals — and this year is no exception. Some high-quality companies are being punished alongside weaker names, creating potential opportunities for patient investors.

Take NVIDIA, for instance. The stock is down over 37% from its peak in January, despite the company continuing to deliver industry-leading performance and maintaining its dominant position in AI chipsets. What we still believe is a formidable business now trades at around 20.7x forward 12 months earnings — a valuation that, while not cheap, is increasingly supported by secular demand trends and strong earnings visibility. Analysts estimate earnings to grow at 31% a year over the next 5 years.

In Europe, Novo Nordisk has also been caught in the broader market downdraft by a mix of internal issues and the current environment. The stock is down around 58% from its highs in June 2024. It now trades at approximately 16 times 12 months estimated forward earnings, which, given the company's growth prospects in obesity and diabetes treatments, strikes us as a compelling entry point. The fundamentals remain robust: double-digit revenue growth, a strong balance sheet, and expanding global demand for its GLP-1 therapies.

These examples remind us that markets can overshoot — in both directions. Our focus remains on understanding the long-term value of the businesses we look at and take action once Mr Market offers us an opportunity to invest. We have been building carefully positions in both names this year.

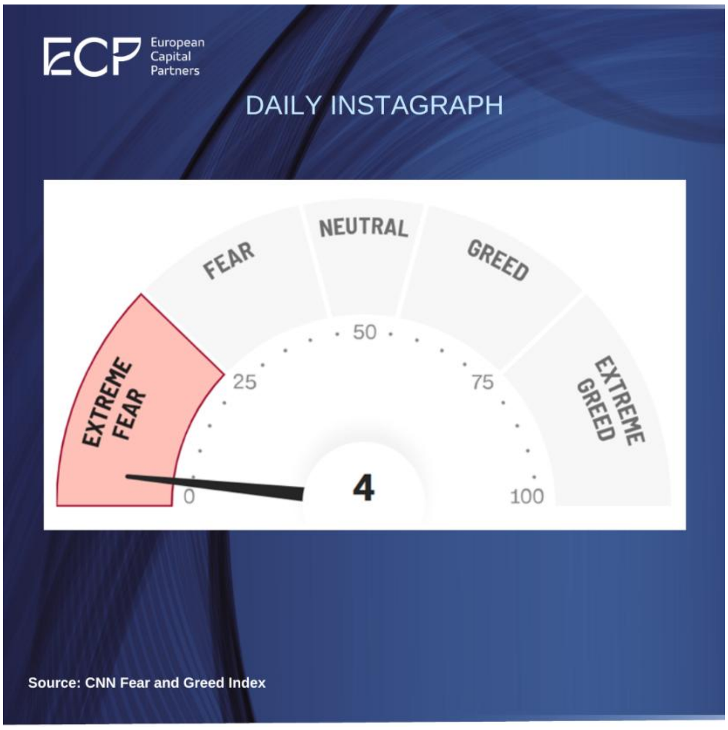
In fixed income, we continue to favour shorter duration and high credit quality. Recent moves in the yield curve and spreads have created opportunities to re-engage at the longer end, and we are doing so cautiously, with a focus on real yields and inflation protection.

Mr. Market and the Long View

As Warren Buffett once wrote:

"Ben Graham, my friend and teacher, long ago described the mental attitude toward market fluctuations that I believe to be most conducive to investment success. He said that you should imagine market quotations as coming from a remarkably accommodating fellow named Mr. Market who is your partner in a private business. Without fail, Mr. Market appears daily and names a price at which he will either buy your interest or sell you his.

Even though the business that the two of you own may have economic characteristics that are stable, Mr. Market's quotations will be anything but. For, sad to say, the poor fellow has incurable emotional problems. At times he feels euphoric and can see only the favorable factors affecting the business. When in that mood, he names a very high buy-sell price because he fears that you will snap up his interest and rob him of imminent gains. At other times he is depressed and can see nothing but trouble ahead for both the business and the world. On these occasions, he will name a very low price, since he is terrified that you will unload your interest on him."



The widely followed CNN Fear & Greed Index shows extreme fear in the market, the closest description we can have to a Mr Market being currently depressed.

We believe successful investing requires engaging with Mr. Market on your terms — with discipline, patience, and perspective.

We continue to believe that free trade is a long-term driver of global prosperity. Tariffs, in our view, are a blunt policy instrument that may provide short-term leverage but come with longer-term costs. In the best-case scenario, they result in higher consumer prices and a cooling economy. In the worst case, they risk tipping the global system into stagflation — the toxic combination of inflation and stagnation.

The Trump administration is likely well aware of the fine line it is walking. It is applying pressure to shift the terms of trade more favourably toward U.S. industry, with the underlying goal of offloading the costs onto trading partners. The strategy may produce results in negotiation — but it also increases the chances of policy error.

We are not there yet, but the trajectory bears close monitoring.

Closing Thoughts

2025 continues to challenge assumptions — about inflation, interest rates, geopolitics, and even the rules of global trade. But through the noise, our focus remains steady.

We invest not in headlines, but in businesses. Not in forecasts, but in fundamentals.

Moments like these reward clarity, consistency, and conviction. As fear rises, opportunities begin to take shape — often quietly.

We are actively monitoring developments in trade, monetary policy, and corporate credit, and adjusting where needed — but always guided by our principles, not the mood of the moment.

Thank you for your continued trust.

Warm regards,

Léon Kirch
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