# Current Positioning
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## The past month summed up

A cheeky Chinese artificial intelligence upstart upended assumptions about winners in the technological space race, with an even broader lesson for investors.

## The rationale

Our central view remains that a healthy US economy remains the driver of global growth and is still the destination for some of the most exciting investment opportunities. However, this could be challenged, particularly as markets begin to digest President Donald Trump's policies and whether they might stifle economic growth, speed it up too much or directly fuel inflation.

Meanwhile, the announcement last month from Chinese artificial intelligence startup DeepSeek reinforces the maxim of Harold Macmillan – "events, dear boy" – that predictions about the future can be rapidly upturned by new information or new actors. In a world of rapidly evolving new technologies, it's important to recognise that perceptions about US hegemony could be challenged by an unexpected threat to the US or by a resurgence of currently unloved regions.

## DeepSeeking missile

DeepSeek, unheard of four weeks ago, upended consensus thinking as news that the Chinese arriviste had effectively produced similar results to ChatGPT for a fraction of the cost reverberated around the tech sector – the NASDAQ index fell by more than 3% on the day while AI bellwether Nvidia, which has become one of the biggest companies in the world on the back of expectations for AI, dropped by a massive 20%, eradicating more than $500 billion of market capitalisation in an afternoon. Importantly, it provided a reminder that in technology those originally tapped to be perpetual winners can turn out to be also-rans. We've previously referenced the experience of the dot-com bubble in the late 90s where those initially feted companies involved in building Web infrastructure were not ultimately the most significant beneficiaries – instead it was those businesses best placed to take advantage of the changes that came out on top. Amazon, Apple, Google and Facebook used the expanding Internet to revolutionise industries such as retail and advertising whilst innovating new technologies and services from smart phones to social media.

So, while the largest technology companies are continuing to pledge billions of dollars into winning the AI race, the shock of DeepSeek has reminded investors that nothing is certain, even for those with the deepest wallets. This is important given the omnipotence of US technology has been the most dominant theme of stock markets since 2023. We have been arguing that while technology remains important, opportunities are present in a much broader range of industries, many emerging from the long shadow and after-effects of the Covid pandemic and subsequent inflation shock: technology was one of the weakest sectors last month whilst areas such as healthcare, industrials and financials showed considerable gains.

## Exceptions to American exceptionalism?

We are always vigilant as to how the status quo could be changing and to challenge our assumptions and those of the market. We have often referred to American economic exceptionalism and we still stand by the idea that a combination of relatively unfettered enterprise, low regulation, a flexible workforce and some of the best universities in the world attracting the most talented people, is a formidable challenge to any other region. That does not make US economic dominance immutable and that steps taken by the Trump administration could prove a challenge rather than additive to US success.

First, while the battle over US inflation looked as though it was being won, inflation still remains above the range of central bank targets (in the US this is 2%). Indeed, the CPI came in at an unexpectedly elevated rate of 3% in January, the highest in more than six months. While it would be unfair to lay any blame for this at the feet of the Trump administration, that doesn't mean that its agenda might not add to the continuing precarious picture.

Tariffs remain front and centre. The recent decision by the US government to impose duties on steel imports could potentially add to the costs for any company using that metal in its processes. That cost can either be passed onto consumers in higher prices or companies can seek to absorb it, thereby narrowing their margins and their profits; rarely positive for share prices. The inflationary pressure from a tariff move are not a given, but with high prices already front and centre in US minds, even a relatively small increase might have a larger knock-on effect to sentiments which can become self-reinforcing. Frustration at the prospect of tariffs has already led senior executives such as Ford CEO Jim Farley to question the wisdom of such policies, while concern over their inflationary qualities means that investors now just expect a single rate cut in the US this year, meaning growth-damping interest rates stay higher for longer.

Is the US economy sufficiently robust to weather any shocks? Most likely yes, although nothing is certain. Even though recent job numbers came in lower than expected, a simultaneous reduction in the unemployment rate showed continuing tightness in the US labour market. The planned deportation of illegal immigrants from the US, a policy that has already started and which seems to have widespread support from the public, will shrink that market further, possibly triggering stronger wage inflation which might reverberate throughout the economy. On the opposite side of the equation, the prospect of massive layoffs across the US Federal government, which employs about 3 million individuals and is the target of cost-cutting measures by the world's richest man and Trump acolyte Elon Musk, could see many workers on the street. That would put a considerable dent in consumer spending across a populace already jaundiced by their perception of relentless price increases.

It’s important to note that these represent potential challenges to our positive central thesis. We are not planning action on what at present represents conjecture. However, we recognise that a new administration with a strong mandate and a penchant for bold, unorthodox policies could shift market direction quickly.

## Stagflation

In comparison to the US, the UK has a relatively modest impact on the global investment environment. For us however it has a rather higher significance, given our exposure to sterling and UK government bonds. While the country just about avoided a contraction in the fourth quarter, instead posting a very modest gain in GDP of 0.1 percent, warnings about the future are coming loud and clear. The Bank of England in early February cut its UK growth forecast for 2025 by half to just 0.75%, whilst forecasting inflation would be 3.7% towards the end of the year, a prediction with more than a whiff of stagflation – a brutal combination of a moribund economy sitting alongside higher inflation. This is doubly uncomfortable because higher inflation necessitates interest rates being kept elevated for longer, whilst those elevated rates act as a brake on the economy.

From an investment viewpoint, this justifies our move last year into UK gilts at the shorter end, which are less vulnerable to ongoing inflation and higher interest rates, and therefore should provide stability even amid a rather unsettling time for the UK.

## Conclusion

The DeepSeek announcement surprised the market but has validated our decision to maintain a balanced portfolio made up of companies exposed to a breadth of industries and end markets. While our equity investments are biased towards the US, we believed that a complacent consensus pinpointing AI winners had developed – we were not prepared to capitulate absolutely to that dominant narrative that has now been called into question.

The unexpected nature of the news however does reinforce our determination to constantly question current assumptions. While for the moment investing in Europe seems relatively unattractive, with sluggish economies and strong geopolitical challenges in the form of a populist surge in upcoming elections and the war in Ukraine, a sudden unexpected outcome could change the narrative for what are relatively inexpensive shares. Likewise, while China is deemed essentially uninvestable amid a slump and financial crisis that the government seems unwilling or unable to tackle with sufficient vigour, a change in this area could also open up the possibility of increased value at attractive prices. We remain vigilant for threats and opportunities.

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