Tech, Trump and China: three forces for the year ahead

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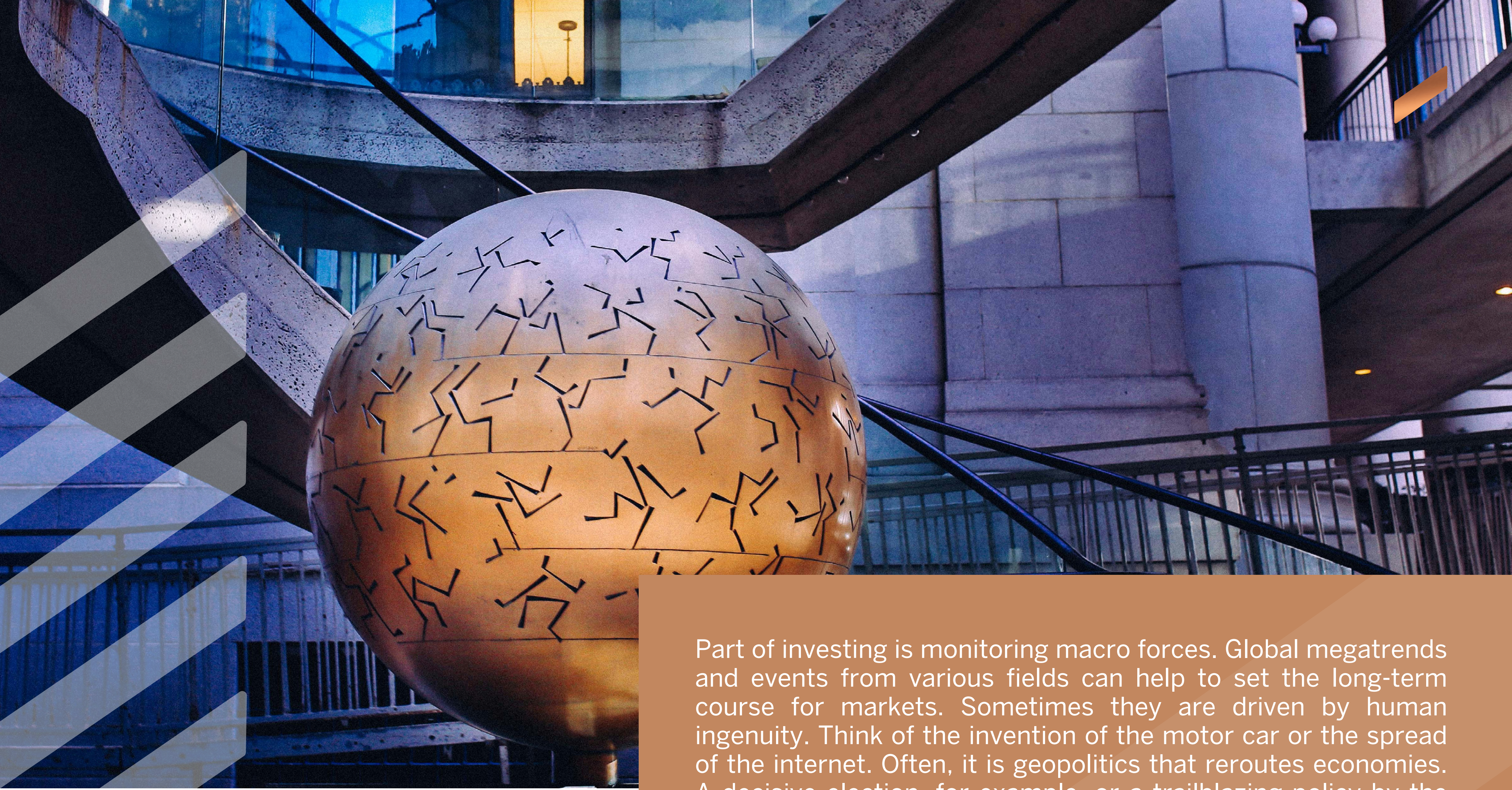
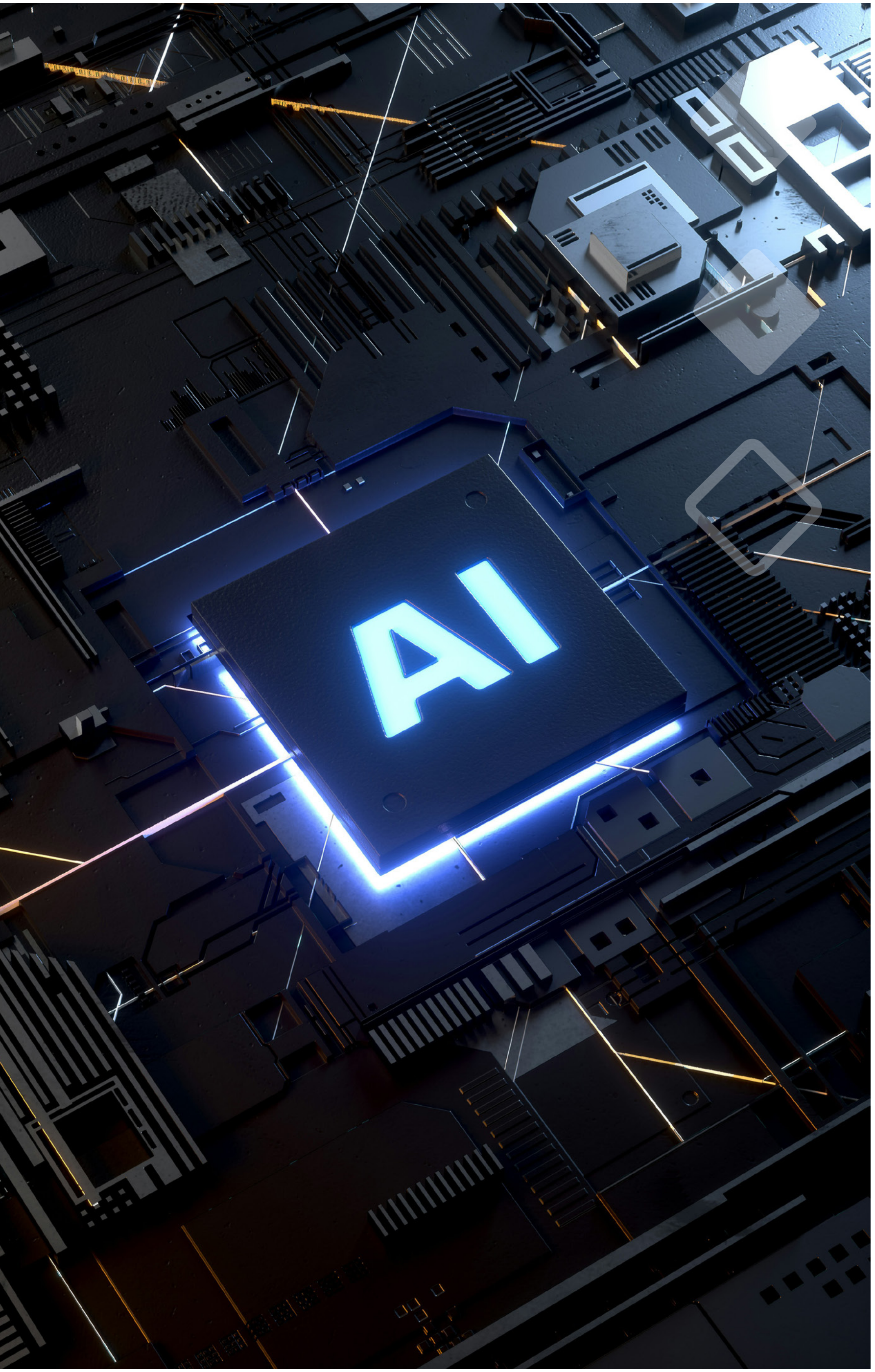


Part of investing is monitoring macro forces. Global megatrends and events from various fields can help to set the long-term course for markets. Sometimes they are driven by human ingenuity. Think of the invention of the motor car or the spread of the internet. Often, it is geopolitics that reroutes economies. A decisive election, for example, or a trailblazing policy by the government of a commercial powerhouse.

In 2025, multiple technological and geopolitical tides demand the attention of the watchful investor. Here are three that deserve our attention.



Technology marches on

The tech trend of recent years shows no sign of abating. Enthusiasm for artificial intelligence (AI) and generative artificial intelligence (GenAI), in particular, is steadily turning into real business applications, income and profits.

That said, a handful of companies are reaping the majority of the rewards. Meta is a good example. It invested heavily in AI models and infrastructure to improve recommendation algorithms on Facebook and Instagram, and better deliver targeted adverts.

The results have been significant. By the end of 2024, users were spending nearly 10% more time on Meta's platforms and advertising pricing was up 11% compared to a year before.

Nvidia has been another big AI winner. It leads the AI revolution by supplying the "picks and shovels". Its graphics processing units (GPUs) are the brains behind AI's computing power. Its Q3 2024 revenue of $35.08 billion was up 94% from the year before, and $2.58 billion more than the company's August forecast.

Companies like Amazon, Alphabet and Microsoft are at earlier stages of monetising AI and GenAI. Much of their share price performance in 2024 was, in fact, generated by improvements in core business activities.

For Amazon, e-commerce sales have been strong and Cloud revenues have recovered from the 2022/23 market slowdown. This revenue growth and improved operating efficiency have led to record operating margins, up four times over two years to 10%, and record levels for free cash flow generation.

It is worth watching these businesses as they raise their AI game. The signs are there to suggest they are driving this hard. As Microsoft said on a recent earnings call: "Our AI business is on track to surpass an annual revenue run rate of $10 billion next quarter, which will make it the fastest business in our history to reach this milestone."

The Trump effect

Donald Trump's decisive victory has been seismic for markets. Investors have generally taken the news as a positive. Although it will take time for the new Trump presidency to take shape, we have strong signals of major policy shifts ahead.

The US President-elect's promised economic policies look set to create friction between growth and inflation. On the one hand, he wants to supercharge the US's economic growth with tax cuts and a "drill baby, drill" approach to energy. On the other hand, he has threatened large and widespread tariffs on imported goods, and the expansionary policies alongside the tariffs would lead to inflationary pressure.

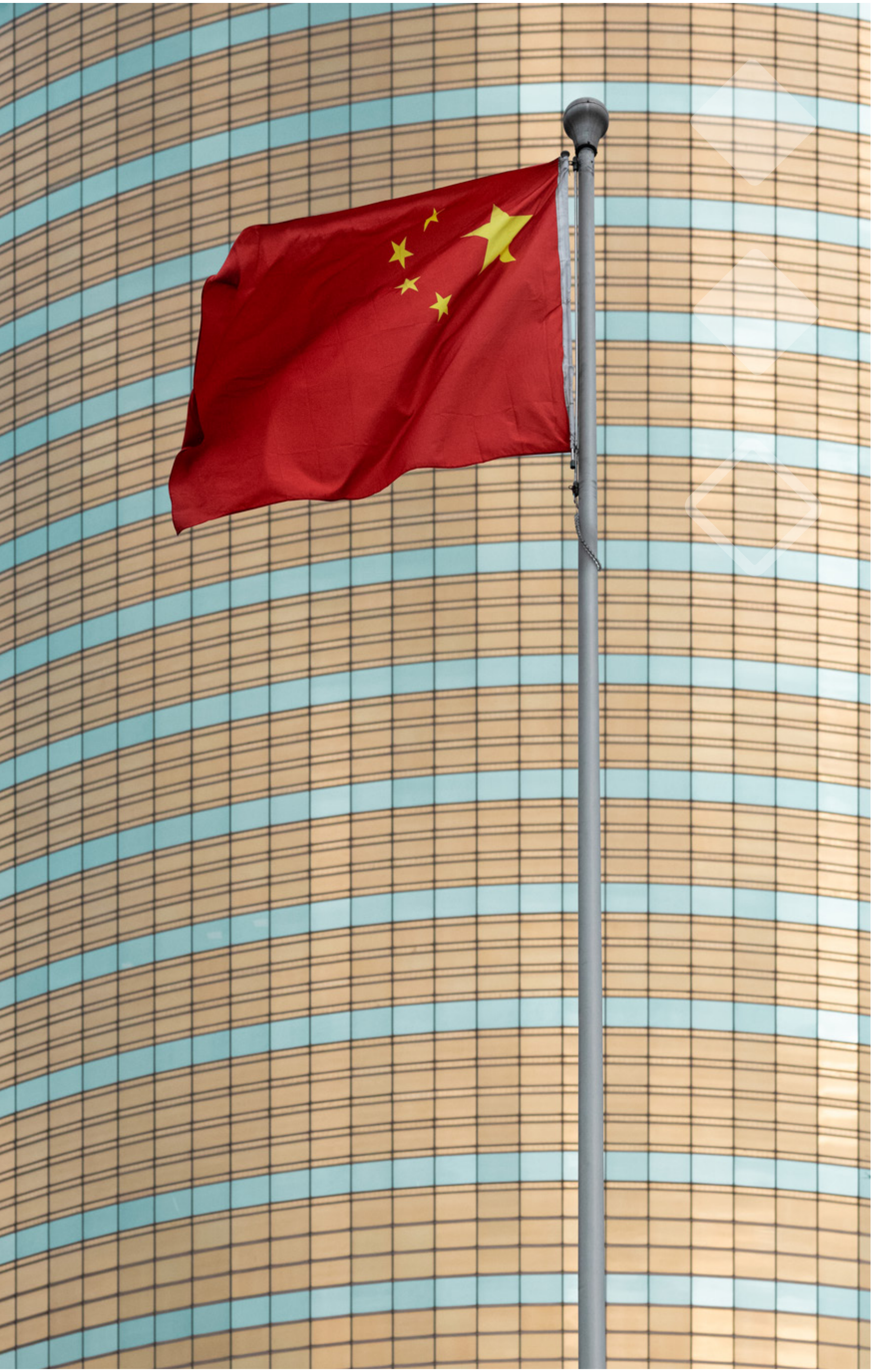
Add to this equation Trump's plans for mass deportation of illegal immigrants. This would place another upward push on prices.

There are important nuances to apply to this calculus. First, Trump tends to use threats of tariffs as a negotiating tool. Sometimes that works, and he gets what he wants without implementing the tariffs.

Second, it is possible that growth, lower taxes and efficiency gains will outweigh inflationary forces. The new Department of Government Efficiency, in the hands of Elon Musk and Vivek Ramaswamy, has the potential to eliminate a great deal of wasteful spending and free up capital.

Finally, we may see US companies lowering gross margins. This will help dampen inflationary results by limiting price rises for the consumer. Similarly, companies around the world, including China, may soak up some of the tariffs by cutting their margins.

As the Trump administration becomes a reality, investors will have a keen eye on the way rhetoric turns to action. Will threatened tariffs materialise? Can he cut the budget deficit? How closely will inflation expectations match what policymakers forecast? And will the US dollar continue to benefit from Trump 2.0?



China: comeback or come down?

China – the global economic miracle of recent decades – has begun to show signs of weakness. The decline in property prices has markedly hit the wealth of households and local governments. Youth unemployment has been at record levels since the Covid-19 pandemic, and confidence is low, due in no small part to lower-than-expected increases in wages.

In response, fiscal and monetary authorities have launched a vast raft of expansionary policy changes. These include lower interest rates, lower capital requirements for banks, and easier access to credit. We will be watching data on credit extension by banks as a good indicator of the success of these steps. Employment growth, confidence indicators and real wage growth will also be key.

It follows, from the Trump analysis above, that any trade disruptions between the US and China have the potential to feed into asset prices.

We don't anticipate a rapid change in fortunes for China's economy. Instead, any recovery is likely to be gradual.

In sum, our client portfolios remain positioned for robust long-term performance, accounting for all three of these forces, and more. Please feel free to reach out with questions about our analysis and what it means for your investments.

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