

INVESTMENT COMMENTARY

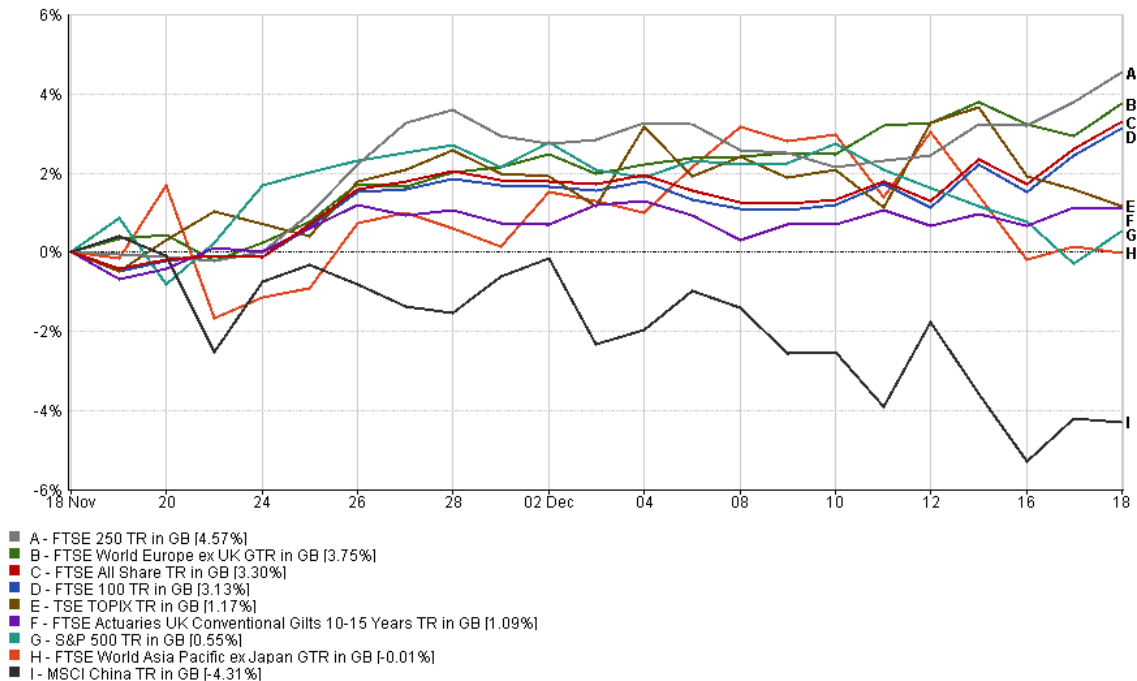


18 DECEMBER 2025

OVERVIEW

The last month has seen some good returns from investment markets with both the US Federal Reserve (Fed) and the Bank of England (BoE) reducing interest rates. Equity markets have had a strong year – who would have guessed that the FTSE All Share Index would have returned over 22% year to date out-performing the US S&P 500 index in sterling and in local currency terms? The volatility in global equity markets around Liberation Day tariffs coupled with investor sentiment oscillating between the benefits of AI developments and worries over high levels of AI expenditure have impacted on US equity market returns given its concentration in AI-related companies.

ONE MONTH INVESTMENT MARKETS STERLING TOTAL RETURNS



18/11/2025 - 18/12/2025 Data from FE fundinfo 2025

YEAR TO DATE INVESTMENT MARKETS STERLING TOTAL RETURNS



31/12/2024 - 18/12/2025 Data from FE fundinfo 2025



As expected, the Fed cut interest rates by 0.25% once again to a range of 3.5% to 3.75% - a three-year low. The Fed meeting showed divisions as Fed members were split as to whether to tackle a weakening jobs market or persistently above target inflation. Three of the twelve Fed members objected to the 0.25% cut – one wanted a 0.5% cut whilst the other two wanted to keep interest rates on hold. Jay Powell, the Fed Chair, commented that further cuts would be dictated by fresh data. The economic data on which the Fed's decisions are based is still distorted due to the impact of the recent government shutdown.

The decision to cut interest rates was taken against a backdrop of weakening retail sales figures and softening consumer confidence. Worries about rising prices, employment prospects and housing affordability weighed on consumers' confidence and their willingness to spend. Inflation currently sits at around 2.7% with the Fed expecting this to fall to 2.4% by the end of 2026. The unemployment rate in November rose to 4.6% - the highest level in four years – with 64000 jobs added in November and 105000 jobs lost in October. It is likely there will be a further one or two more interest rate cuts in 2026. The Fed seemed to be indicating one cut - perhaps as their growth prediction of 2.3% in 2026 points to a resilient economy. The other factor which will influence future interest rates decisions is who will be leading the Fed after Jay Powell steps down as its Chair in May 2026.

The US equity market rallied in the aftermath of the rate cut but concerns about valuations of technology stocks have held back market sentiment. As has been seen at various points during the year, investors questioned when the vast capital expenditure on AI development, much of it funded from debt, would actually begin to produce returns which warrant such elevated valuations. 'Oracle' - a cloud computing provider and key to the build out of AI data centres, saw its shares correct sharply after the company announced a further significant increase in capital spending. 'Oracle' has taken on vast amounts of debt to support its plans. 'Broadcom', a chip designer, saw its share price fall after reporting strong results, as much of the good news was seemingly priced in. The AI theme is not waning, instead it would appear that investors are becoming more disciplined in looking at levels of borrowing, free cash flows and valuations of these AI-related companies. In other words, more attention is being focused on traditional valuation measures.

The UK economy continues to struggle, with GDP contracting by 0.1% in October after a similar level of contraction in September. Over the three months to October, GDP fell by 0.1%. Budget uncertainty and higher taxes appeared to be taking their toll on UK economic growth and housing market confidence. As we said in our 'Budget Commentary,' there were no substantive growth initiatives in the latest Autumn Budget. The unemployment rate continues to tick up – reaching 5.1%. Private sector wage growth slowed in the three months to October to 3.9% (from 4.2% in September), although in the public sector it exceeded 7%. Retail sales in November fell

unexpectedly by 0.1% following a drop of 0.9% in October. The Consumer Price Index (CPI) remains above target, but it fell more than expected to 3.2% in November from 3.6% in October. Against this backdrop of a fragile economy, teetering on recession, and inflation falling, at its latest meeting, the Monetary Policy Committee (MPC) of the Bank of England (BoE) voted to reduce Bank Rate by 0.25% to 3.75% to support the weakening economy. It is likely that soft economic growth and lower wage growth are likely to weigh further on the rate of inflation as demand in the economy is likely to slow. The MPC was split in its decision voting 5-4 in favour of a cut. The BoE Governor, Andrew Bailey, had the deciding vote. The members voting against a cut remained concerned about stubbornly above target inflation driven by continuing high pay growth and lack of productivity gains. The Governor commented that there was “scope for additional monetary easing” but the MPC needed to see inflation settle in a “enduring way”.

Banking shares rallied after the Budget as there were no windfall taxes and the Chancellor avoided further problems in the gilt market by raising taxes, albeit many of her tax increases will only take effect over the next three years. Areas of the market with greater exposure to the domestic economy have seen weakness. For example, the hospitality sector is facing higher business and employment costs, coupled with above target inflation. A freeze in income tax thresholds and moderating pay rises are likely to lead to weaker consumer confidence and spending, which would negatively impact on sectors reliant on consumer discretionary expenditure such as travel, dining and clothing. Many such companies are found in the mid and smaller cap sections of the UK equity market. With interest rates falling, the pound has also fallen in value which has given a boost to the shares of companies (mainly larger ones), which derive the majority of their earnings overseas.



The European Central Bank (ECB) has continued to keep its main deposit rate at 2%. Currently the ECB believes that the eurozone economy is proving resilient in the face of US trade tariffs, with GDP growth at 1.4% pa in the third quarter of 2025 and inflation close to target at 2.2%. The ECB's accommodative monetary policy is supporting lending growth and domestic consumption. Fiscal stimulus from Germany, in particular, should help to drive growth in the next few years. The European Union (EU) is seeing ever increasing levels of cheaper imports from China, as the latter seeks markets for its high levels of loss-making manufactured goods. Germany's manufacturing sector is being negatively affected and the EU is now likely to implement policy responses to diversify its own export markets and to protect its industries from competition, for example, channelling defence orders to European suppliers, putting quotas on steel imports and potentially by erecting further tariff barriers against China.



As expected, the Bank of Japan (BoJ) increased its key interest rate by 0.25% to 0.75% - the highest level in thirty years - at its December meeting. Although still above target at 3%, the BoJ believes that the economy is moving towards a sustainable inflation rate of 2%, although the tight labour market may continue to put pressure on the inflation rate in the shorter term. The Japanese economy is weak – contracting by 2.3% pa in the third quarter of 2025 due to lower consumer spending and falling export levels.

The Japanese equity market has performed strongly over the year as AI and defence related companies have driven returns. The prospect of higher interest rates has been supportive of the financials sector. Solid earnings and further enhancements to shareholder-remuneration policies have underpinned market performance. Fiscal stimulus policies should prove supportive of the economy.

The Chinese economy continues to face deflationary pressures. The consumer price index (CPI) rose to 0.7% in November - only the second time this year that it has been positive. However, the Producer Price Index fell 2.2% - the 38th consecutive month of decline – which acts as an indicator as to where CPI is heading. The prolonged housing slump has led to weak consumer confidence, falling retail sales and lack of domestic consumer demand. The Chinese authorities have supported loss making manufacturing so there is an over-supply of goods. Consequently, a massive flow of cheap Chinese goods is being exported (Europe and other Asia Pacific countries being the chief recipients) as evidenced by China's trade surplus of over \$1trn in the first eleven months of 2025. Lower interest rate and the stimulus measures announced by the Chinese authorities to date have been insufficient to produce a much-needed rebound in mortgage activity and confidence in the housing market. Such a weak housing market does not support the consumer-led growth the Chinese authorities wish to see.

FINANCIAL SERVICES COMPENSATION SCHEME

INCREASE IN DEPOSIT PROTECTION LIMIT

The Prudential Regulation Authority (PRA) has confirmed that bank customers will benefit from an increase in the maximum amount they would be reimbursed if their bank, building society or credit union were to fail.

The deposit protection limit which applies to the Financial Services Compensation Scheme, will be increased to £120000 from £85000 should a bank, building society or credit union fail. The new higher limit applies from 1 December 2025.

In addition, the limit applicable to certain temporary high balance claims, for house purchase and life insurance policies for example, will increase from £1 million to £1.4 million.

OUR VIEW



Compiled by Angela Cooper, MD - Investment Services.

Angela runs Cartlidge Morland's Investment Management team, with over 30 years' experience in investment research working for investment companies, leading UK national IFAs and wealth managers. Angela graduated from the London School of Economics and is a Chartered Insurance Practitioner.

We continue to maintain fully diversified portfolios and have been taking gains from technology, Asia Pacific and US larger cap equity funds, in particular. We are conscious of the stock concentration of the US index fund given the dominance of US mega-tech companies and AI enthusiasm also supporting performance of some Asia Pacific markets. We are using some of the gains to top up US funds with less exposure to these companies through US equity income and US smaller companies funds. We are also rebalancing and diversifying Japanese equity exposure where risk parameters allow.

We are cautious about the prospects for UK Smaller Companies funds given the weak UK economy with domestic demand likely to soften further. We have reduced exposure to this area of the UK market but will continue to monitor it for signs of improvement.

A stalling economy is bringing lower inflation to the UK and it may be that the monetary response by the Bank of England, in the form of lower interest rates, can bring necessary stimulus. Government policy is offering little that is supportive of growth though increased spending, well-targeted or otherwise, should bring some benefit. Higher employment costs are undermining the labour market alongside government policy which appears unsupportive of businesses and their owners. UK economic prospects are dimmed but as

the globally-facing FTSE 100 companies generate over 70% of their revenue overseas they should benefit from a slowly improving global economy. In international terms, UK valuations do not seem high. Christine Lagarde, President of the ECB, is talking of upgrading EU growth forecasts and the Fed is speaking of the US economy continuing to grow at more than 2% p.a. These factors promise a profitable environment for companies meaning that equity prospects apparently remain fair, for all the mega-tech valuation dangers lurking. Fixed interest will be supported by lower interest rates/inflation and by stable credit quality.

With best wishes for Christmas and for 2026!



80 Coleman Street London EC2R 5BJ t: +44 (0)20 7709 5560 e: enquiries@cartlidgemorland.com www.cartlidgemorland.com

This material is not intended to be relied on as a forecast, research or investment advice, and is not a recommendation, offer or solution to buy or sell any securities or to adopt any investment strategy. Cartlidge Morland's current views and suggestions in this document are based on research which is obtained from a variety of sources. Whilst these sources are believed to be reliable, the information obtained cannot be guaranteed to be accurate and may be condensed or incomplete. Past performance not a guide to the future. The value of investments and income arising may go down as well as up.

Cartlidge Morland is a trading name of The Cartlidge Morland Partnership, an appointed representative of Cartlidge Morland Ltd, which is authorised and regulated by the Financial Conduct Authority.