

A Message From Our Chief Investment Officer

Squeeze the Lemon Dry

Morningstar Wealth

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Key points

- Lower interest rates making cash less attractive
- Rebound in US majors back to peaks
- Korean equities the star performer
- Knowing when to hold or to fold

Away from the glare of tariffs, one thing is very clear about 2025: interest rates are coming down.

When we look at the number of countries raising interest rates vs lowering them, Japan is a rarity among developed economies in raising rates. Across Asia Pacific, the Americas and Europe central banks are making money cheaper and dropping the return from cash. Interest rates remain above inflation rates in most countries and the pace of rate cuts might have been faster but for the uncertainty about tariff effects. Tariff impacts appear so far to be dissipated as suppliers either sacrifice margin, uncover efficiencies or simply bump up prices in all their export markets.

Government bonds still offer a decent extra return vs cash and inflation, supporting income seeking investors and those transitioning to retirement seeking shock absorbers to deal with bumpy markets.

Equities continued their rally, with 2024 superscalar stars back in the spotlight. The easing of inflation fears and bond yields not rising further, has no doubt supported these more highly valued companies and perhaps reduced fears of large inflation/growth shocks from tariffs. At current share prices, the US is less attractive, and we continue to favour opportunities outside the spotlight of US tech companies and AI related plays.

What's been notable this year is the outperformance of emerging market equities, with Korea a standout, up 30% to 30 June⁽¹⁾. Such high returns occurred despite the backdrop of a failed attempted at a coup in December 2024, ferocious competition in critical semiconductor industry, curbs on sale of AI chips to China and sharply rising tariffs. We increased exposure in Morningstar multi asset portfolios to Korea last year, as the market sold off.

Getting the most out of investment opportunities is a key element of successful investing, knowing what to invest in, when to buy and when to sell. Overstaying your welcome can lead to large losses but cashing out too early can be just as impactful in terms of missing out on extra gains.

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Looking back over the past 40 years, the classic signs it's time to sell include asset prices rising a lot over an extended time frame to levels that are very high vs metrics like cashflows, dividends and asset values, universally bullish investors with outsized exposures and unsustainably high sales and profits. Examples include telco, media and technology companies in late 1999, emerging market and financial service firms in 2007 and mining companies in the early 2010s during the commodity boom.

Conversely, it's been better to hold or even add to exposures, when investors are fixated on the downside, fundamentals are improving from a low base, asset price gains are small over longer horizons and prices reflect low rather than high expectations of future profits. Here examples include Oil and Gas companies in 2020, Chinese equities in 2024 and IT companies in 2003.

Korea ticks far more of the checklist for buying and holding than selling out. The overhang of bad news has kept foreign investors largely absent until very recently and their exposures lower than usual. Gains while large of late are small over longer periods, reflecting poor 2024 outcomes. Valuation levels still remain attractive, for example the largest company, Samsung, trades close to book value. The fundamental picture for earnings is supported by semiconductor specialisations, an array of strategic industries including defence and a more pro-business administration implementing shareholder friendly reforms.

Along with Brazil, Korea is an example of the potential for gains from specialised research and contrarian risk taking. Getting the most out of opportunities while staying diversified remains key to navigating this period of rapid change.

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