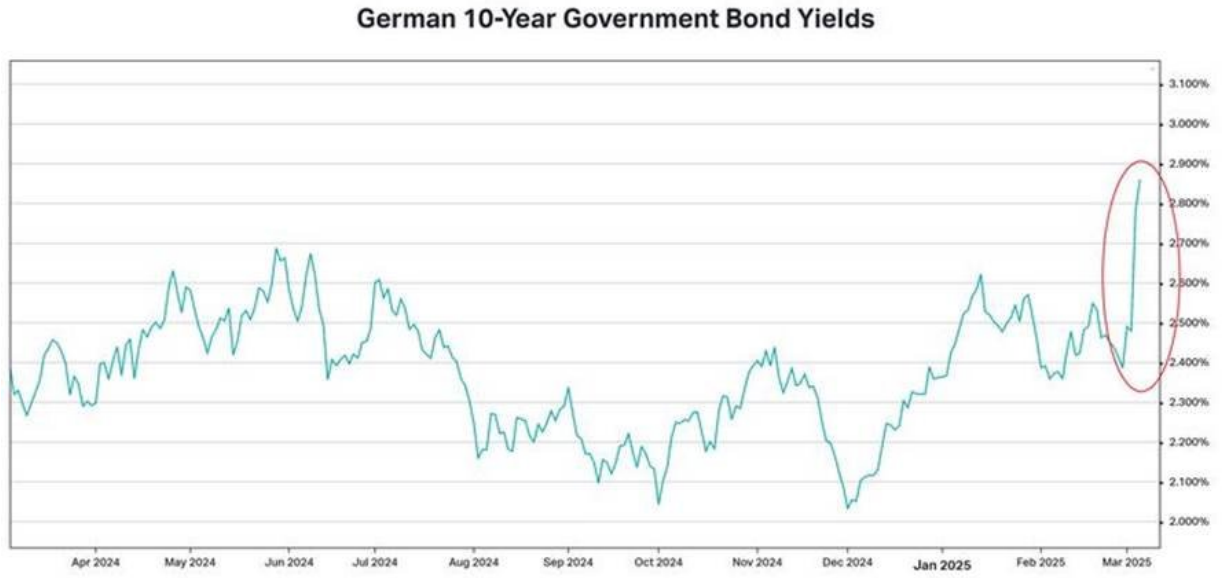
Insights, Tacit Thought | Weekly Investment Insights

What is actually going on in investment markets outside the USA?

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For UK investors, rising bond yields bring back the memory of the 2023 mini budget which led to instability and lost our then Prime Minister and Chancellor their jobs in very short order. The context of then and now is very different and is driven more by global developments than by a domestic finance strategy.

This week bond yields in Europe have risen significantly, driven primarily by German yields.



In tandem, European equities have actually risen and now trade at multi-year highs alongside a strengthening Euro. All whilst the threat of US tariffs and the standoff regarding the future of Ukraine is in full focus on most news channels. So why is this?

Firstly, context is important. German bond yields have been lower than those of the developed world as Germany has been deemed to be more prudent with its government finances than countries such as the UK and France.

The German debt brake, or Schuldenbremse, is a constitutional rule enacted in 2009 to limit public debt. It mandates that federal and state budgets must be balanced, allowing only structural deficits of 0.35% of GDP at the federal level and forbidding net new borrowing at the state level. This rule aims to ensure fiscal discipline, promote sustainable public finances, and enhance economic stability. The debt brake reflects Germany's commitment to maintaining a robust financial position and to avoid excessive government borrowing.

The incoming German Chancellor, driven by the American approach to Ukraine and international relations, has now tabled a material change to this long-standing German consensus. This, as we wrote last week, is an economic reaction to world events. In technical economic jargon this is termed a fiscal stimulus. If a country has the headroom to expand its fiscal stimulus this does not lead to an episode such as the mini budget in the UK. Furthermore, when it is coupled with monetary easing and lower short-term headline interest rates, it is a very powerful economic tailwind.

The reason for writing about this today is not to downplay the changes to the global economic order but to illustrate the actions and reactions which we must consider when setting investment strategy. Binary outcomes are very rarely what we experience, and history shows that economies and companies are very good at adjusting to a new normal albeit with increased volatility and anxiety. People, on the other hand, generally worry more and react emotionally rationally but intellectually irrationally when considering investment decisions. Our job is to deal with cold fact and reason in managing investments through this changing environment, and not to become emotionally biased.

At times such as this, when most news flow is predominantly negative, we aim to provide some balance to this negativity. If the news flow was all positive, we would remind our readers of the risks of group think and herd behaviour.

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