

InCred Insights Mid-Year 2025 Outlook: The Great Recalibration

July 2025

Introduction

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Dear investor

The first half of 2025 started with euphoria in markets which was quickly replaced with panic as deep uncertainty around President Donald Trump's tariffs swiftly set in. All-time highs in the S&P500 were superseded by a 20% fall, peak to trough, the greatest since the pandemic. With pauses in the implementation of tariffs, market momentum returned. Even the US actively entering conflict between Israel and Iran did not dull the enthusiasm of markets. A new sense of optimism has returned reflecting the potential of the technological revolution that is taking place around artificial intelligence, and at the start of July, the S&P500 reached new heights. Reassuringly, the outlook for corporate earnings remains stable.

But by historic standards, the valuation of the US equity market remains relatively extended. At the same time, the US economy is slowing, tariff risks remain, and tensions in the Middle East are not fully resolved. The US dollar has meaningfully weakened, and its slide is set to continue. The year-end S&P500 forecasts, across institutions, reflect this uncertainty.

In this climate, how should investors respond? We have called this publication *The Great Recalibration* because we see certain resets that are occurring in economics and markets – which we share – and believe it is necessary for investors to respond practically within their portfolios. We offer five observations about the current environment with tangible actions for investors to consider.

At InCred, we remain cautiously optimistic about the outlook, and we hold the view that it is a moment to remain fully invested. At the same time, we are convinced that this is a time for an active and disciplined approach. We are here to work with you in optimising the risk-return profile of your portfolio – if you would like to discuss the current economic and market dynamics, and how these relate to your circumstances, please contact us.

We hope you enjoy reading our publication.

With best wishes,

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The first half of 2025: From euphoria to panic to optimism

The first half of 2025 brought a wide range of investor emotions – from euphoria to panic to optimism. The year started with healthy optimism as markets strutted into 2025 on a wave of positivity with momentum in corporate earnings, pleasing economic growth and the prospect of central bank interest rate cuts. Corporate America felt particularly confident – capital expenditure surged and there was anticipation around President Trump's promised tax cuts and deregulation. By late February, the S&P500 reached an all-time high of 6,147 – up 4.5% in just 33 trading days, the equivalent of a 30%+ annualised return!

"Liberation Day": The cause of panic

This initial euphoria, however, proved to be short-lived. The first US tariff announcements came in February – a 20% levy on Chinese imports – which seemed manageable. But by 2 April on his "Liberation Day", President Trump announced far reaching US tariffs on around 90 countries at levels from 10% to 145% in the case of China. With the threat of US inflation and the potential for recession, markets panicked with the S&P500 plummeting 20% peak to trough, delivering its steepest decline since the pandemic. The CBOE Volatility Index – a measure of risk linked to the S&P500 – accelerated past 60, a level only recently seen in March 2020, during the Global Financial Crisis of 2008-9 and on Black Monday in 1987. Within days, container ships departing China for the US began a dramatic slowdown and corporate earnings started to be reassessed as the economic damage was analysed.

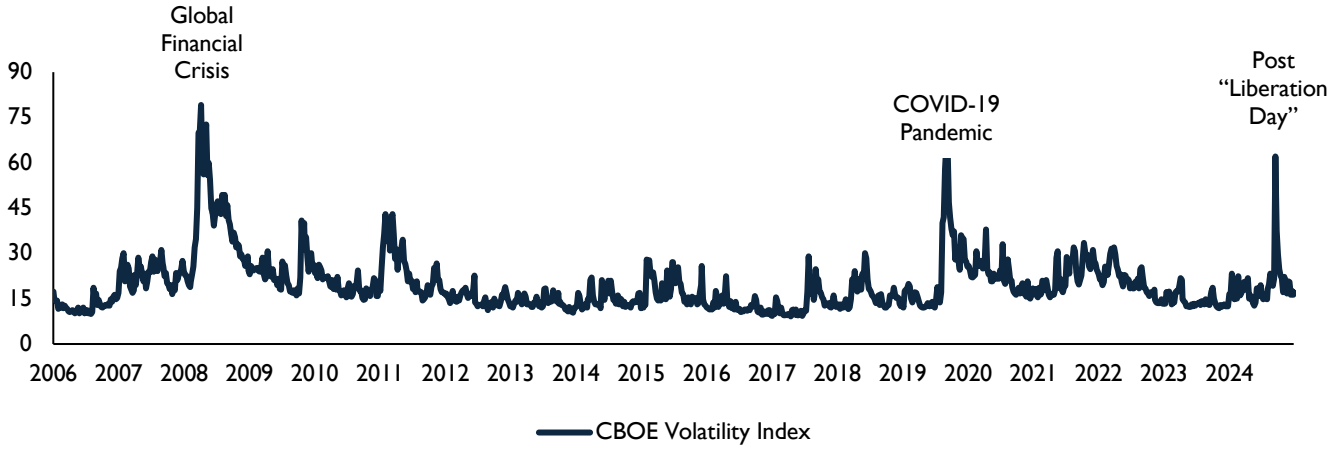


Figure: Historic levels of CBOE Volatility Index (2006 – 2025)
Source: Bloomberg

By 9 April, in the face of this economic and market turmoil and under political pressure, President Trump announced a 90-day pause on the higher tariffs for most countries. Diplomacy then prevailed over the following weeks with trade talks and agreements – including with China – ensuing, and further volatility being avoided. With 90-day paused recently extended by a month, it certainly seems that economic disaster has been averted – although risks clearly do remain. We may never know the degree to which President Trump calculated this outcome, but he has succeeded in recalibrating the way the world trades with the US potentially raising additional revenues of $3 trillion over the next decade.

Technological advance: The driver of optimism

And finally, optimism. During June, with tariffs out of focus, the attention of markets turned back to the seismic technological paradigm shift that is happening in the world with the advance of artificial intelligence with global spending soaring 60% to $360 billion. Robust earnings from technology stocks – including the so-called "Magnificent Seven" drove markets with equities clawing back virtually all their losses. And even as geopolitical tensions flared in the Middle East between Israel and Iran – including with US intervention – markets remained resolutely positive. By 2 July, the S&P500 hit a new all-time high of 6,279.

The greatest decline in the US dollar since 1973

Whilst it has been a positive period for US equities, it has not been for the **US dollar** which suffered its greatest decline since 1973. This results from a convergence of factors:

- **Diminished US growth expectations** in comparison to other economies with a decline in the perception of US exceptionalism
- **Unpredictability in economic and fiscal policy** which has also challenged the US dollar's safe haven status
- **Rising US debt** and questions over its long-term sustainability
- **Expectations of interest rate cuts**, especially if President Trump brings forward the appointment of the new chair of the Federal Reserve

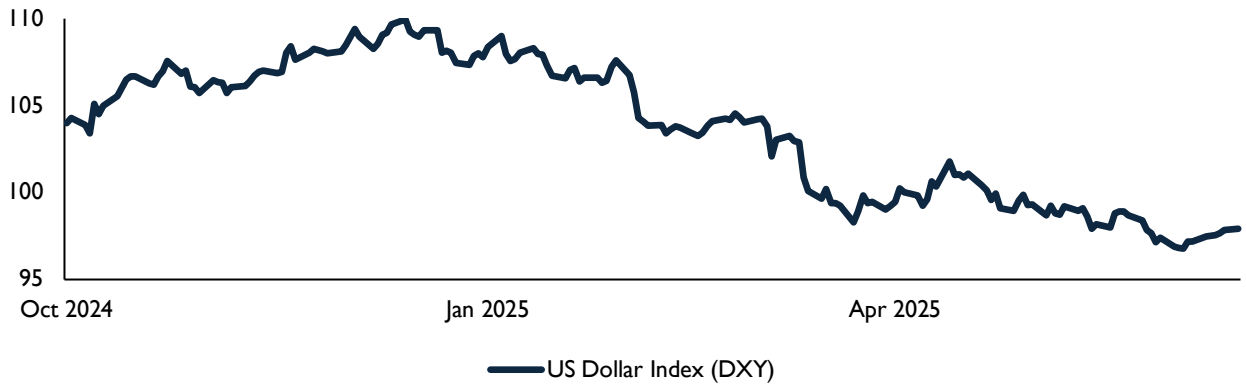


Figure: US dollar versus basket of major currencies (October 2024 – July 2025)
Source: Bloomberg

But a weaker dollar is not necessarily bad. President Trump has argued that a strong dollar hurts US exports and manufacturing and has advocated for other countries revaluing their currencies. That said, it is important for investors to understand the implications of this on their own circumstances.

The first half of 2025 amounted to a colorful period with a broad range of investor emotions. We are convinced that it is necessary to look at what will happen next with these experiences in mind.

The second half of 2025: The Great Recalibration

We have titled this outlook *The Great Recalibration*. In the Cambridge Dictionary, to recalibrate is defined as "a change in the way you do or think about something." It is our conviction that with all that has happened in politics, economics and markets in the first half of 2025, that a change in approach may be required for some in the second half.

As we see it, it is no longer satisfactory to simply have indiscriminate market risk / exposure – to be "risk-on". But in this climate investors must be "risk optimised" ensuring (1) that levels of risk are appropriate for the environment and (2) that the relationship between risk and return is understood and optimal. We are convinced that this is a time for active and disciplined approach.

In this context, we wanted to start by sharing some key themes that we think will influence the second half of 2025:

The economic impact of US tariffs

The trade policy uncertainty that dominated the first half of 2025 has partially abated with the effective US tariff rate now expected to settle at between 15% and 18%. This is substantially lower from the near 30% initially expected but significantly above the pre-Liberation Day 3% and the highest level since the 1930s. The Trump administration seems to have successfully walked the tightrope of adopting a protectionist stance, raising additional revenues, whilst maintaining an environment supportive of markets. Back in the March edition of InCred Insights, we argued that Trump was a pragmatist not an ideologue – this perspective seems to have prevailed. That said, with the now original 90-day deadline extended by one month to 1 August, tensions remain – in particular with key trading partners, Japan and South Korea.

The economic impact, while moderated, remains material. US inflation is projected to rise to approximately 3.0% in 2025, up from pre-tariff estimates of 2.4%. Consumer prices face upward pressure, with apparel prices rising 8% from the April tariffs alone. However, the *stagflationary* shock appears manageable, with the consensus viewing the probability of US recession at just 25% over the next 12 months.

Continued volatility in the Middle East

The fragile ceasefire between Iran and Israel following June's "Operation Rising Lion" represents a significant geopolitical risk that could disrupt global energy markets. While the immediate crisis has subsided, the underlying tensions remain unresolved, and the potential for renewed conflict poses ongoing risks to oil prices and global inflation.

While a broader regional war is certainly not our base case, the durability of the cease fire is uncertain. Specifically, both sides have set out red lines on the future of Iran's nuclear programme which are mutually incompatible, and which narrow the route to a lasting settlement – this could lead to future flare-ups and tensions which would spark volatility in energy prices. BlackRock records this as one of its top risks on its Geopolitical Risk Indicator.

Renaissance in Europe

Perhaps the most underappreciated development of 2025 has been Germany's decision to reform its constitutional debt brake, unleashing significant fiscal capacity for infrastructure and defence spending. Defence spending across the eurozone is projected to surge from 1.9% of GDP in 2024 to 2.8% by 2027, potentially reaching 3% based on military requirements. This fiscal expansion represents a fundamental shift in European economic policy, providing a crucial growth driver as the region adapts to heightened security threats and reduced reliance on US protection.

The implications extend beyond defence. Germany's infrastructure spending surge, combined with monetary easing – encouragement of lending and spending in an economy – from the ECB, creates a powerful combination supporting European growth prospects. This development challenges the narrative of European stagnation and positions the region as a potential beneficiary of global capital flows seeking alternatives to US assets.

Delicate balancing act in China

China has responded to US trade tensions pragmatically with intentional support for its economy. Measures have included ramped up government spending on infrastructure and public projects, targeted subsidies for key sectors such as consumer electronics and autos, relaxation of certain bank reserve requirements, and easing of lending regulations to certain industry sectors. Critically, the government has stabilised the property sector with sector specific support. The US-China trade negotiations, while fragile, have reduced the immediate risk of escalating trade warfare and provided breathing room for economic adjustment. An appropriate and balanced outcome to those negotiations is needed in the second half.

Japan is an outlier, but US trade talks are critical

Japan remains the main exception when it comes to monetary policy in developed markets with the Bank of Japan maintaining a relatively hawkish stance with further rate hikes likely in the second half or early 2026. There has also been structural reform in Japanese quoted companies with encouragement of share buybacks which are at record level and extensive corporate governance reform.

Whilst the wide valuation gaps between Japanese equities and western counterparts has significantly narrowed, considerable investor optimism remains with the prospect of higher levels in equities and the yen. This is predicated on a swift and reasonable resolution to US – Japan trade talks which are particularly important for Japan’s export-heavy sectors such as autos and technology.

Implications for markets

In this recalibration, and considering the themes above, we now turn to what we think might happen in markets and across the different asset classes.

Equities

US: Upside more limited but reasons for optimism remain

Representing 72% of global developed equity market capitalisation, the performance of US equities is central to the performance of the overall equity allocation in any portfolio. With the S&P500's 29% recovery since its lows in April, we need to be circumspect about its likely returns during the second half – after all, we find ourselves in an environment of slower growth, some inflationary pressure and relatively high valuations.

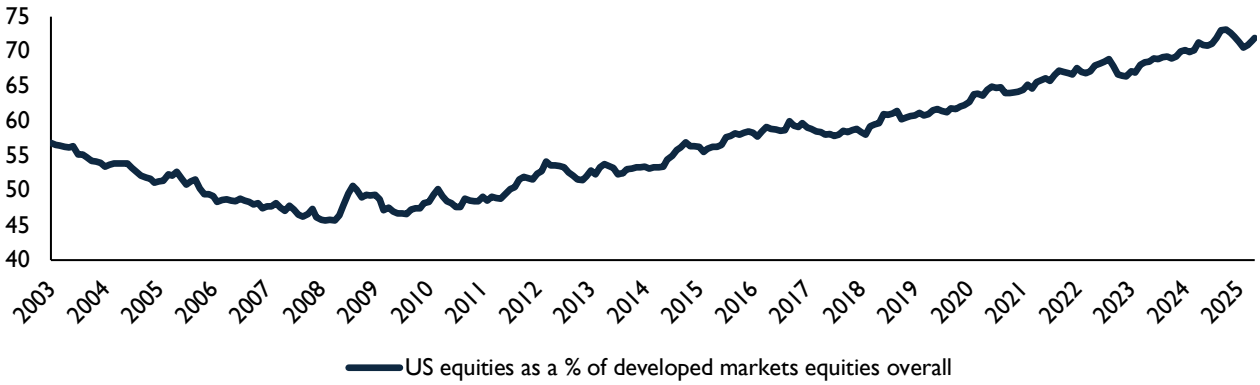


Figure: Value of US equities as % of total global developed markets (2006 – 2025)
Source: Bloomberg

Focusing on the valuations of US equities, a useful measure is the price-to-earnings (P/E) ratio – essentially, a measure of how much an investor is willing to pay for each dollar of a company's profit. A higher P/E ratio shows that an investor is willing to pay more – showing either higher expectations of growth or perhaps that a company is expensive / overvalued. If we look at the average P/E ratio of the S&P500 – looking at share price versus expected profits for the next year (i.e. the forward P/E ratio) – you will see that equities near the peak of their valuations over the last twenty years (the dark blue line on the graph).

This is reinforced by looking at the averages for the preceding five and ten years (the orange and green lines respectively):

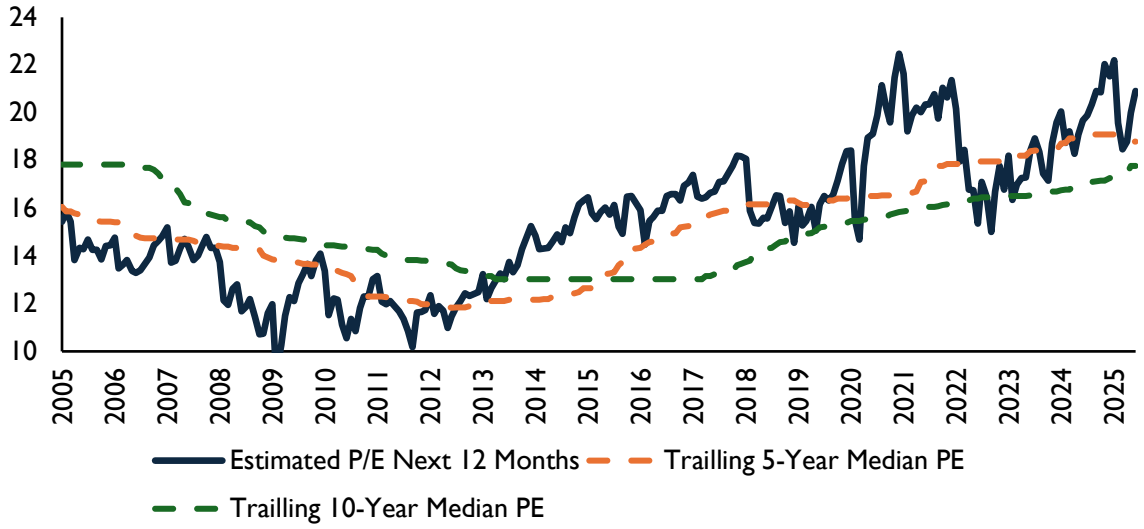


Figure: 12 months forward price to earnings ratio for S&P500 (2005 – 2025)
Source: Bloomberg

Whilst at a superficial level the graph suggests that the S&P500 (currently at 6,270) is expensive, the year-end views of global banks reveal a neutral / stable view on the outlook for the US market:

Firm	2025 year-end S&P500 target
Deutsche Bank	6,550
Societe Generale	6,400
Citigroup	6,300
UBS Global Wealth Management	6,200
Goldman Sachs	6,100
Barclays	6,050
JP Morgan	6,000
BNP Paribas	5,900
Bank of America	5,600
HSBC	5,600
Average	***6,070***

Source: Bloomberg (3 July 2025), UBS CIO H2 2025 Outlook

Looking beyond these forecasts, there is additional evidence that – if anything – US equities could enjoy positive momentum in the second half:

- **Possibility of positive earnings surprises:** If you examine the underlying analysts' forecasts for each individual constituent member of the S&P500 on a bottom-up basis, these point to a year end index level of approximately 6,650.

- **Impact of reported earnings in the first quarter:** Actual reported earnings in the first quarter exceeded expectations. All things being equal, this should have led to increased earnings estimates for the full year, but this did not happen. Rather, earnings estimates overall have been cut for the full year. If growth remains resilient, there is a potential for positive earnings surprises supporting valuations.

- **Valuations of technology companies:** While headline PE ratios for some mega cap tech names are above market averages, they are not excessive when adjusted for growth rates, profitability, and cash flow. When adjusted for expected growth, many AI leaders trade at levels historically associated with fair value. Unlike the dot-com era of the early 2000s, today's leaders are highly profitable, with healthy margins and strong free cash flow generation.

- **An earlier than expected naming of next Federal Reserve Chair:** If the next candidate is viewed as particularly *dovish* (favouring of lower interest rates) that could provide a short-term boost to equity markets.

We maintain a neutral outlook for the US – balancing the risks associated with valuations with the dynamics of the technology sector and the stable earnings outlook.

Europe: Attractive opportunities but discretion essential

European equities represent an attractive opportunity for the second half. Valuations remain reasonable relative to historical norms and those of other regions, while the fiscal expansion in Germany and continued accommodative policies from the European Central Bank provide supportive tailwinds. The combination of less expensive valuations, improving policy support, and potential benefits of US dollar weakness creates an attractive risk-reward proposition. Consistent with our views throughout the first half, we continue to particularly favour companies with exposure to defence, infrastructure, and energy transition themes. The European defence industry stands to benefit substantially from increased government spending, while infrastructure companies should profit from Germany's fiscal expansion.

China: Improving outlook but caution warranted

An improving outlook exists for China equities. As already mentioned, its government has implemented substantial fiscal and monetary stimulus measures, and regulatory change. Recent economic data shows resilience with GDP growth tracking toward 5% year-on-year, while retail sales have strengthened thanks to subsidies and improving consumer sentiment. The property sector, while still under pressure, has received targeted government support thus preventing broader financial instability.

The pragmatic approach to US-China trade negotiations has significantly reduced the risk of further tariff escalation, with various pauses and ongoing discussions providing breathing room. Overall, we adopt a neutral stance on Chinese equities as policy support and undemanding valuations are offset by ongoing property sector weakness, regulatory uncertainty, and potentially slower long-term growth prospects. The market is expected to remain range-bound but selective opportunities do exist in consumer and technology-orientated sectors. While China's willingness and capacity for policy intervention remain key stabilisers, the main risks include renewed trade tensions, slow transmission of economic stimulus to the real economy, and persistent property sector woes.

Emerging markets: Tariff risks remain, outlook improving in India

Emerging market equities present a solid investment opportunity for the second half, supported by improved fundamentals and reduced tail risks. The partial de-escalation of US-China trade tensions has significantly lowered the probability of widespread trade disruption, creating a more favourable environment for emerging market economies. These markets are benefiting from attractive valuations relative to developed markets, with the valuation gap remaining historically wide despite recent narrowing. **India** stands out as a particularly favoured market due to strong domestic growth, robust corporate earnings, and its position as a beneficiary of global supply chain diversification.

The continued weakness of the US dollar provides additional tailwinds for emerging markets assets. Although investors should remain mindful of risks including potential geopolitical uncertainties, and the possibility of renewed US protectionism. We therefore argue for selective and actively managed approaches to emerging markets exposure.

Japan: Structural reforms lead to more attractive investing environment

Japan equities present good long-term opportunities despite some near-term headwinds. The country's structural transformation is accelerating, with corporate governance reforms creating meaningful value for shareholders. Share buybacks are outpacing last year's record levels. Japan's economic fundamentals show increasing resilience, with real wage growth returning to support domestic consumption. The Bank of Japan's policy divergence – raising interest rates whilst other central banks lower them – should continue supporting Japan's attractiveness to global investors. Although there will be considerable focus on whether a positive US-Japan trade agreement can be achieved. We believe that exposure to Japan offers defensive characteristics and diversification benefits in portfolios.

US fixed income

The outlook for **US fixed income** is stable in the second half, in the context of slowing growth and likely US interest rate cuts. After a peak in 10-year Treasury yields at around 4.5%, yields will move lower as the Federal Reserve begins reducing interest rates, likely in September.

Investment-grade corporate bonds enter the second half with spreads (over government bonds) modestly above long-term averages. Corporate balance sheets remain relatively strong with low levels of leverage and high levels of liquidity. The combination of interest rate cuts, likely spread tightening and investor demand will support stable returns for investors.

High yield offers attractive all-in yields of approaching 7.5%, with spreads around 3% over government bonds. This provides solid compensation for credit risks, especially in an environment with modest levels of default. We maintain that exposure to high yield is best achieved through diversified funds with active management but continue to believe that US private credit offers superior risk adjusted returns.

With interest rate cuts on the horizon and a stable environment for credit risk, we encourage investors to maintain a full weighting to US fixed income in their portfolios – although we prefer short to intermediate maturities in the current climate and maintain a neutral position on duration.

Currencies

The **US dollar** is poised for modest weakness in the second half. The US dollar index, which tracks the US dollar against a basket of major currencies – including the euro, yen, pound, Swiss franc – fell by approximately 10.8% in H1 2025, the steepest six-month drop since 1973. The pivot towards US interest rate cuts – which could be as much as 1% by year end – will erode interest-rate advantages over major peers, diminishing carry-driven inflows. Whilst the US dollar remains a safe-haven currency, confidence was, at times, challenged following "Liberation Day", and recent months have seen flows out of US assets elsewhere. Purchasing power models also point to further realignment. Consequently, we see further weakness in the dollar and recommend that investors review their exposure carefully, employing hedging if appropriate.

The outlook for the **euro** in the second half of 2025 is shaped by a complex mix of global and regional dynamics. The euro is expected to remain relatively resilient, trading in a range of 1.15–1.20 against the US dollar, supported by the ongoing US dollar weakness. The European Central Bank has already enacted several rate cuts, and at least one further cut is anticipated, which should continue to support domestic consumption and business activity. Fiscal policy is becoming more prominent, with Germany's release of its debt brake and increased infrastructure and defence spending providing a positive tailwind for European growth. However, the region still faces headwinds from US tariffs, which may weigh on exports and manufacturing, as well as political uncertainty in key countries like France and Germany. Despite these challenges, the eurozone's structural reforms and resilient consumer sector are expected to help cushion the impact, making the euro an attractive diversification tool for global investors.

We maintain a positive position on the **Japanese yen**. The *hawkish* stance of the Bank of Japan is supportive of the yen with the potential for further rate hikes in late 2025 or early 2026. Additionally, Japan's improving real wage growth could boost domestic consumption, further underpinning the currency. The notable headwind relates to the US-Japan trading relationship and if a satisfactory agreement on tariffs cannot be reached, this could temper the yen's appreciation.

The US dollar's recent weakness provides a supportive backdrop for **emerging markets currencies**. However, volatility remains elevated due to ongoing US trade policy unpredictability, geopolitical risks, and uneven global growth. Countries with high external debt or political instability may face renewed depreciation pressures. Overall, selective opportunities exist, especially where domestic fundamentals are strong and reforms are progressing, but investors should remain cautious amid heightened sensitivity to global shocks and the potential for policy surprises.

Gold

We maintain a neutral position on **gold**. Central bank demand remains a key support, with forecasts indicating purchases will stay robust—potentially exceeding 1,000 metric tons for the year, well above historical averages. This sustained interest is driven by ongoing concerns over US fiscal deficits, a weaker dollar, and questions about the independence of US monetary policy.



Figure: Price of Gold per troy ounce in USD (2000 – 2025)
Source: Bloomberg

Current year-end forecasts typically range from $3,500 to $3,700 per ounce, with upside risk in the event of heightened recession fears or further geopolitical disruptions. However, if global growth surprises to the upside and policy uncertainty diminishes, we see gold trading in its current range. While gold's role as a portfolio diversifier is intact, especially amid elevated policy and geopolitical uncertainty, we do not believe that outsized positions are warranted at this time.

Alternative investments

We continue to adopt a positive stance across hedge funds and private markets, on the basis that the asset classes offer portfolio diversification benefits and an attractive risk-return relationship:

Hedge funds

In the current environment, we especially favour funds adopting market neutral and equity long-short strategies. These strategies aim to provide a strong diversification benefit by delivering positive, steady, and market agnostic returns.

- **Market neutral** funds balance long and short positions to eliminate broad market exposure, aiming to profit from pricing inefficiencies between individual securities. This approach results in low correlation to traditional assets and helps preserve capital during market downturns.

- **Equity long-short** strategies, meanwhile, combine selective buying of undervalued stocks with short selling of overvalued ones, offering both upside participation and some downside protection. At the moment, these strategies are particularly compelling - higher interest rates and greater dispersion between winners and losers have created more opportunities for skilled managers to generate excess returns.

In addition to these strategies, we continue to invest in well-managed **multi-strategy** funds with strong track records.

Private credit

Private credit has emerged as an increasingly promising opportunity. As companies delay initial public offerings and remain privately held longer, they rely more on bespoke financing from non-bank lenders, expanding the private credit universe and allowing investors to access a growing pool of loans. Yields on private credit typically run in the mid- to high-single digits – often around 8 to10% – offering a significant income premium over comparable public-market debt. Robust covenant protections, lower default rates and more conservative leverage profiles than high-yield bonds help mitigate downside risk. Additionally, banks' retreat from certain loan markets creates structural lending opportunities.

Private credit also provides diversification benefits, as returns are driven by company specific underwriting rather than broad market movements. For long-term portfolios seeking enhanced yield and controlled risk, private credit stands out for its combination of income, security and growth potential.

Private real estate

Private real estate is particularly attractive at present due to several converging factors. First, valuations have repriced significantly, with private commercial property prices down roughly 18 to 20% from peak levels, creating historically advantageous entry points as the market recovers from higher financing costs. Second, expected lower interest rates should bolster returns. Third, income generation is enhanced by inflation-linked leases and mid- to high-single-digit yields, offering an inflation hedge and a meaningful premium over public-market alternatives. Fourth, the sector delivers diversification benefits: low correlation to equities and bonds reduces portfolio volatility. Finally, structural tailwinds – constrained new supply, ESG-driven asset repurposing, and secular demand for data centres and industrial logistics—support both income growth and capital appreciation.

Private infrastructure

Private infrastructure offers resilience, income stability and exposure to powerful secular trends. Investors benefit from long-term, inflation-linked contracts – whether through regulated utilities or digital assets like data centres –providing mid-single-digit to high-single-digit cash yields and a natural hedge against rising prices. Valuations in private deals often trade at discounts to listed peers. Structural tailwinds – including decarbonisation, digitalisation and energy-security initiatives – are driving robust demand and underpinning steady growth prospects. Government fiscal support for critical infrastructure and privatisation of public assets further expands the investable universe.

With historically low default rates, covenant protections and lower volatility than public markets, private infrastructure offers diversification benefits – its returns correlate weakly with equities and bonds while delivering consistent returns through economic cycles.

We continue to believe that private markets offer useful diversification benefits in a portfolio context. Exposure is best achieved through highly diversified funds offered by top tier global managers who have access to the broadest range of transactions.

From "risk-on" to "risk optimised": Five observations for the second half of 2025

In light of the recalibration that is taking place in economics and markets, we believe thoughtful and active management of investment assets has never been more important. It is our conviction that we have moved from an environment where simply being "risk-on" (i.e. just having market exposure) was sufficient to enjoy decent returns to circumstances where it is necessary to be "risk optimised". That is really analysing how a portfolio is constructed and ensuring it is fit for the current environment. To achieve this, there are five observations that we encourage investors to consider:

I. Stay diversified

Diversification is a foundation of portfolio construction and involves mitigating risk by allocating capital across a broad spectrum of asset classes, sectors, and geographical regions. It recognises that markets are inherently unpredictable, and the performance of individual investments can vary widely due to company-specific, sectoral, macroeconomic or geopolitical factors.

Empirical research demonstrates the effectiveness of this approach. Simply expanding a portfolio from a single stock to a basket of twelve stocks reduces – what is known as unsystematic or idiosyncratic – risk by as much as 88%. In practical terms, this means that the majority of risk unique to individual companies is effectively neutralised through disciplined diversification.

Moreover, constructing a portfolio that blends equities, fixed income, and cash substantially dampens portfolio volatility. For example, an asset allocation – such as 50% US equities, 20% non-US equities, 25% bonds, and 5% short-term cash investments – has historically delivered average annual returns approaching 9% p.a. But most importantly, this diversified mix narrows the range of potential extreme outcomes, offering a smoother investment journey compared to more concentrated portfolios. Historically, this allocation would have reduced portfolio volatility – a measure of overall portfolio risk – from over 18% to nearer 13%, a significant reduction. By embracing diversification, investors position themselves to weather market turbulence and achieve more consistent, long-term financial objectives.

As part of a diversified portfolio, we advocate particularly for the inclusion of **private credit** and **private infrastructure**, **gold** (see V. below for further explanation) and **hedge funds** pursuing market-neutral or equity long-short strategies, or multi-strategy funds. All of these assets will improve the risk-return characteristics of a portfolio.

II. Consider increased capital protection

Virtually every portfolio will already have some instruments that offer a degree of capital protection, such as government bonds. In this environment – where upside in equities may be more limited – we consider **structured products** to offer attractive risk-return qualities. Structured products are investment instruments that combine traditional assets – such as stocks or bonds – with derivatives to create customised risk-return profiles. These products are designed to meet specific investor objectives – such as enhancing yield, providing downside protection, or offering exposure to certain market scenarios. By tailoring features like maturity, participation rates, and capital protection, structured products allow investors to manage risk and reward more precisely than with conventional investments. These are especially appealing in uncertain or more fully valued markets,

where traditional strategies may offer limited upside or heightened risk. In particular, we believe that there are two types of product that could be relevant in current markets.

- **Reverse convertibles** are a type of structured product that offer higher yields in exchange for taking on pre-determined additional risk. Typically, these instruments pay attractive coupon rates regardless of modest declines in the underlying asset, such as an equity index. However, if the underlying falls below a predetermined barrier during the investment term, the investor may receive shares or a reduced payout instead of full principal repayment. Reverse convertibles are best suited for investors with a neutral to slightly bearish outlook who are willing to accept some risk to the principal in return for enhanced and known income level.

- **Capital protected notes** are structured products designed to safeguard the invested capital while still allowing for some participation in market gains. At maturity, these notes return all or a specified portion of the initial investment, even if the underlying asset has declined. In exchange for this protection, the upside is typically capped or subject to a participation rate, meaning investors may not capture the full extent of any market rally. Dividend income may also be forgone to pay for protection. Capital protected notes are ideal for those seeking growth potential with the reassurance that their capital is shielded from significant losses, making them particularly attractive during periods of market uncertainty or elevated valuations.

An alternative is to consider **hedging strategies** through options. Options offer a flexible and efficient means for investors to hedge against potential market declines, particularly when valuations are elevated and market volatility is a concern. The most direct approach involves purchasing put options on the index, which provide the right to sell at a predetermined price and thus limit downside risk if the market falls sharply. This strategy is akin to buying insurance for a portfolio, though it comes at the cost of the option premium. For those seeking to reduce hedging costs, strategies like collars – where a put is purchased and a call is sold – can cap both downside and upside, providing a defined risk-return profile. It is important that investors seek professional advice on structured products and hedging strategies.

III. Be prepared for a weaker US dollar

With US dollar weakness likely to continue, an appraisal of currency exposure is essential. As already observed, with US equities representing 72% of developed markets equities, significant exposure to the US dollar is inevitable in diversified portfolios. Our clients are generally located in Europe, the Middle East, Asia and Africa but often adopt the US dollar as their reference currency and have significant exposure to the US dollar in portfolios. In this context, an evaluation of currency exposure is critical covering the following areas:

- **Assessment of current currency exposure:** What is the currency mix of your existing consolidated investment portfolio, across different institutions? What is the currency exposure across business assets, real estate and other assets?

- **Assessment of future currency requirements:** Are there known liabilities and/or income requirements in a particular currency and when?

- **Decision on target currency mix:** Given current exposure and future requirements, what is a reasonable current mix in a US dollar weakening environment?

- **Implementation of currency strategy:** In light of analysis, it may make sense to introduce an intentional hedging strategy for part of the US dollar exposure. This could involve currency forwards or options, structured currency solutions or using hedged share classes when buying investment funds. Historically, gold has also provided a hedge against a weakening US dollar.

Finally, it is wise to view every investment opportunity with a currency lens in mind – whether a portfolio investment or a real asset. If appropriate, proper assessment of the cost of a hedging strategy can then be assessed – and any return projections can take account of currency risk.

IV. Think long-term and stay invested

Attempting to time the market by moving in and out based on predictions or emotions can severely undermine long-term investment returns. This is because a small number of the market's best-performing days account for a disproportionate share of total gains, and these days are nearly impossible to predict.

Consider the last 20 years. $10 million fully invested in the S&P500 in 2005 would have grown to approximately $71.7 million by 2024, reflecting the power of compounding and the market's long-term upward trajectory. However, if that same investor missed only the 10 best days, their ending value would be reduced by more than half. Missing even more of the best days would have reduced the investment to a fraction of its potential, with annualised returns falling sharply and, in some scenarios, barely keeping up with inflation – on average 2.5% p.a. over this period – or even turning negative:

	End value	Annualised return
Remained fully invested	$71.7m	10.4%
Missed 10 best days	$32.9m	6.1%
Missed 20 best days	$19.7m	3.5%
Missed 30 best days	$12.9m	1.3%
Missed 40 best days	$8.9m	-0.6%
Missed 50 best days	$6.4m	-2.2%
Missed 60 best days	$4.7m	-3.7%

Figure: Impact of being out of the market on $10m investment in S&P500 (2005 – 2024)
Source: S&P500 total return data

The evidence is clear from historical data - staying invested through all market ups and downs is essential for capturing the full potential of long-term growth. Attempts to sidestep volatility often result in missing the very days that drive overall returns, turning a sound long-term investment into a missed opportunity.

V. Be protected against geopolitical shocks

Gold is widely recognised as a safe haven during geopolitical shocks, often outperforming other assets when uncertainty rises. Five-year analysis by the World Gold Council revealed that during weeks when the Geopolitical Risk Index (GPR) surged by over 100%, gold averaged a weekly return of 1.6%, while global equities declined by 0.8% on average.

Similarly, Citigroup quantified that each 10% rise in the GPR correlates with a 3.7% appreciation in gold. Historical data shows that gold prices rise following periods of conflict and unrest:

Event	% Increase in gold price	Period
Russia-Ukraine conflict (2022)	5%	February to March 2022
COVID-19 pandemic (2020)	38%	January to August 2020
Arab Spring (2011)	7%	January to March 2011
9/11 attacks (2001)	6%	11 September 2001
	25%	September 2001 to 2002
Gulf war (1990)	8%	August to October 1990

Figure: The impact of geopolitical events on gold price (1990 – 2024)
Sources: Bloomberg, World Gold Council

The European Central Bank states that "gold generally offers a safe haven in times of stress, particularly during episodes of high geopolitical risk or policy uncertainty". In this context, we recommend a full weighting to gold in diversified portfolios. As already mentioned, gold also can provide a hedge to a weakening US dollar.

Some have described **Bitcoin** as the "digital gold", and it certainly shares some characteristics with gold – scarcity and decentralisation – but its safe-haven status is still being debated, particularly during acute crises when it can move in tandem with other risk assets. For those with an understanding of its nature and risks, a weighting could however make sense.

Next steps

We hope that you have found our analysis and outlook stimulating. As we look into the second half of 2025, we urge you to review the positioning of your portfolio – are you "risk-on" or "risk optimised" in your strategy? Are there asset classes or product types that are absent from your portfolio? Is this a time to recalibrate your approach?

At InCred, we remain cautiously optimistic about the outlook, and we hold the view that it is a moment to remain fully invested. At the same time, we are convinced that this is a time for an active and disciplined approach. We are here to work with you in optimising the risk-return profile of your portfolio – if you would like to discuss the current economic and market dynamics, and how these relate to your circumstances, please contact us.

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Summary of our key views

Asset Class		Summary of view
Equities	US	Valuations elevated but earnings strength and Fed dovishness could support modest upside. Maintain neutral to slightly positive stance.
	Europe	Attractive valuations and fiscal stimulus offer strong upside. Favour defence, infrastructure, and energy transition sectors.
	China	Policy easing offsets structural headwinds. Neutral view with selective opportunities in technology and consumer sectors.
	Emerging Markets	Weaker dollar and easing trade tensions benefit emerging markets. India leads with strong growth and corporate earnings.
	Japan	Structural reforms and Bank of Japan divergence support long-term upside. Positive outlook dependent on trade resolution with US.
US Fixed Income	Government	Stable outlook in rate cutting climate. Remain invested.
	Investment Grade	Stable outlook with rate cuts expected. Strong corporate balance sheets justify full portfolio allocation.
	High Yield	Attractive yields and modest default risk support selective exposure. Prefer actively managed, diversified funds.
Alternative Investments	Hedge Funds	Favour market neutral and equity long-short strategies.
	Private Credit	Strong yield premiums and downside protection make this a top pick. Ideal for income and diversification in long-term portfolios.
	Private Real Estate	Falling valuations and inflation-linked income create attractive entry points. Logistics and data centers show promise.
	Private Infrastructure	Inflation-linked contracts and secular trends drive resilient returns. Supports long-term portfolio diversification.
Currencies	US Dollar	Rate cuts, rising debt, and eroding safe-haven appeal point to further weakness. Review hedging strategies.
	Euro	Supported by ECB easing and German stimulus, but politics and tariffs present headwinds, but a valuable diversifier.
	Japanese Yen	Hawkish Bank of Japan and wage growth support appreciation. US trade tensions are a risk.
	Emerging Markets	Selective opportunities supported by weak USD. Remain cautious due to geopolitical and policy volatility.
Commodities	Gold	Neutral view supported by central bank demand. Allocation remains a hedge against geopolitical and inflation risk.

Important information

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