

A photograph of a young couple sitting on the ground in a forest, surrounded by fallen autumn leaves. The woman, on the left, is wearing a white cable-knit sweater and a dark grey scarf, and is smiling at the man. The man, on the right, is wearing a dark blue sweater and a light blue scarf, and is looking down at a beagle dog lying between them. The background is a soft-focus forest with yellow and orange autumn foliage.

Window on the World

OCTOBER 2025



As we head into the final quarter of the year, the U.S. Government is in shutdown, which means a lot of services stop operating, from Nasa to the National Parks. And, in the U.K., the focus is on the forthcoming Budget on 26 November. History typically shows that the former has a limited impact on the economy or markets, but there is still the potential for extended disruption. Ahead of the U.K. Budget, the Government has been testing the waters with a series of potential measures to boost the fiscal coffers, which have seemingly been scrapped when met with scepticism. These two developments, coupled with a moderation in economic activity and elevated valuations in capital markets such as the U.S., signal that some volatility can be expected going into year-end.

Third quarter review 2025

	Total Returns (%)			
	1 Month	3 Months	12 Months	YTD
UK Equities	1.8	7.5	17.5	17.7
US Equities	3.6	8.1	17.6	14.8
European Equities	3.4	4.6	14.1	16.1
Japanese Equities	2.9	11.0	21.5	15.3
Emerging Market Equities	7.2	10.9	18.1	28.2
UK Gilts	0.7	-0.8	-1.9	1.7
UK Corporate Bonds	0.9	0.7	3.7	4.2
UK High Yield Bonds	0.3	2.9	9.3	7.4
US Corporate Bonds	1.4	2.6	3.9	7.0
US High Yield Bonds	0.8	2.4	7.2	7.1

Source: Bloomberg, Verso Investment Management, as of the end of September 2025. Returns in local currency

Despite the uncertainty investors have faced this year, global equity markets delivered strong gains in the third quarter of 2025. Expectations for lower interest rates, combined with resilient corporate earnings and continued enthusiasm for AI, have underpinned investor confidence. This builds further on the rebound from the lows back in April and means that most equity indices have delivered strong double-digit returns year-to-date in local currency terms. Although equities have pushed higher, the economic data paint a more complex picture of moderating growth, sticky inflation, and increasing regional differentiation. Something equity markets for now have been happy to look through.

In the U.S., economic data continues to point towards relative resilience – supported by steady consumer spending and business investment – a better picture than many investors were expecting when tariffs started to be unveiled and reforms began. That said, the labour market does look to be softening, with payroll growth slowing and hiring intentions weakening, so we'll have to wait and see how this progresses over the fourth quarter and into 2026. This softening led the Federal Reserve to cut interest rates for the first time this year in September, despite inflation remaining above its 2.0% target at 2.6%.

Investors believe this is the first step in a prolonged period of cuts in U.S. interest rates – consequently, the market now anticipates four further cuts in the next 12 months – putting downward pressure on Government bond yields and acting as a further catalyst for U.S. equities (+8.1%). While market leadership in the U.S. has remained quite narrow, towards the end of September, we did see a move higher in areas such as small-cap equities and cyclical sectors, which are typical beneficiaries of lower interest rates.

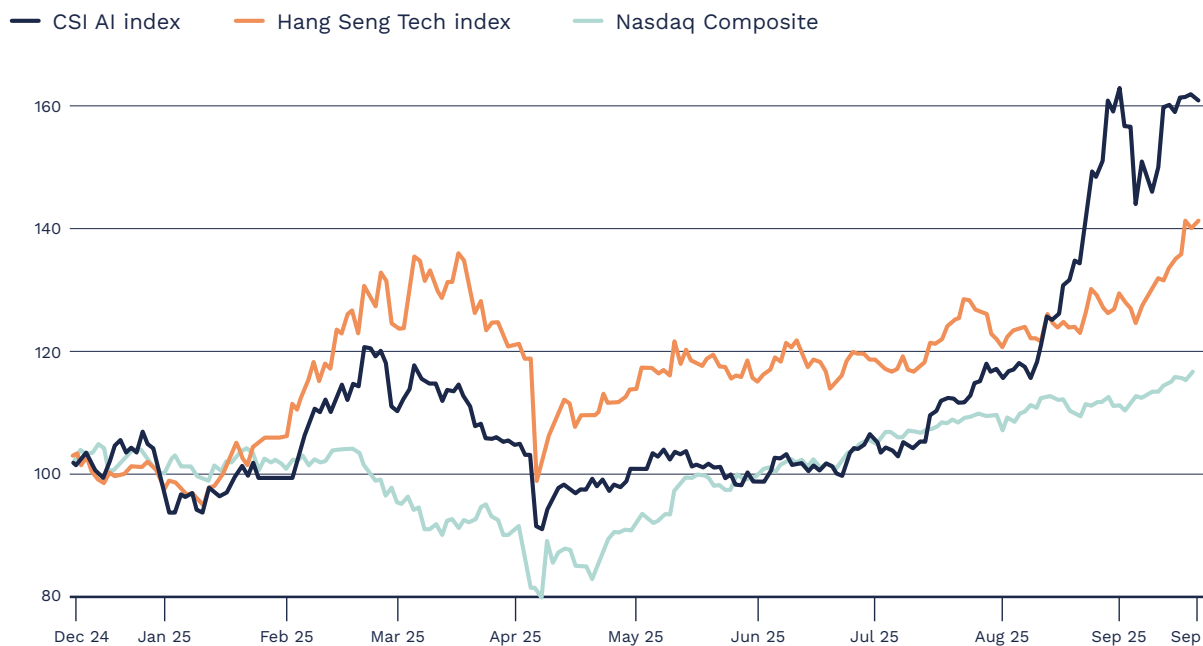
As the Budget approaches in the U.K., the domestic economic backdrop remains difficult, with weakening economic activity, a challenging fiscal situation, and sticky inflation. So, there's plenty of speculation about what the Chancellor may do to raise more revenue for the Government. However, these concerns did not prevent the Bank of England from cutting interest rates to 4.0% in August, although they have cautioned that further cuts this year are not guaranteed. This stance has continued to put some upward pressure on longer-dated Government bond yields, resulting in a negative return from U.K. gilts over the quarter. U.K. corporate bonds fared better, as did U.K. equities (+7.5%), with the latter benefiting from the international nature of the U.K. equity market and a weaker pound.





Emerging markets performed well in the three months ending September, with Chinese equities rallying sharply. Policy support for domestic chipmakers and an acceleration in AI spend fuelled the rally. In addition, the wider market has also been supported by easing trade tensions with the U.S. and hopes that an “anti-involution” policy, which aims to remove unproductive assets from the economy, would help shore up the domestic economy.

CHINESE TECH STOCKS OUTSTRIP US COMPETITORS



Note: Indices rebased
Source: Bloomberg

Despite European equities lagging their international peers in the third quarter, they remain one of the strongest-performing equity markets year-to-date. Political instability in France and weaker economic data weighed on sentiment; the victory of the pro-EU party in Moldova at recent elections was a small boost for the region. In Japan, the stepping down of the Prime Minister did not derail the market, which proved to be the strongest performer in Q3, thanks to a weaker yen, resilient macro data, and ongoing corporate governance reforms.

Tech spending is now a key driver of U.S. economic activity

It won't have gone unnoticed that the global technology sector is experiencing a significant boom, which has been driven primarily by substantial investment in AI. In a little over three years, when ChatGPT was first brought to market, interest and investment in this area have exploded, with many of the largest technology companies in the world investing heavily to maintain their leadership. Some are predicting that over the next five years, capital spending in this area could exceed \$5 trillion.

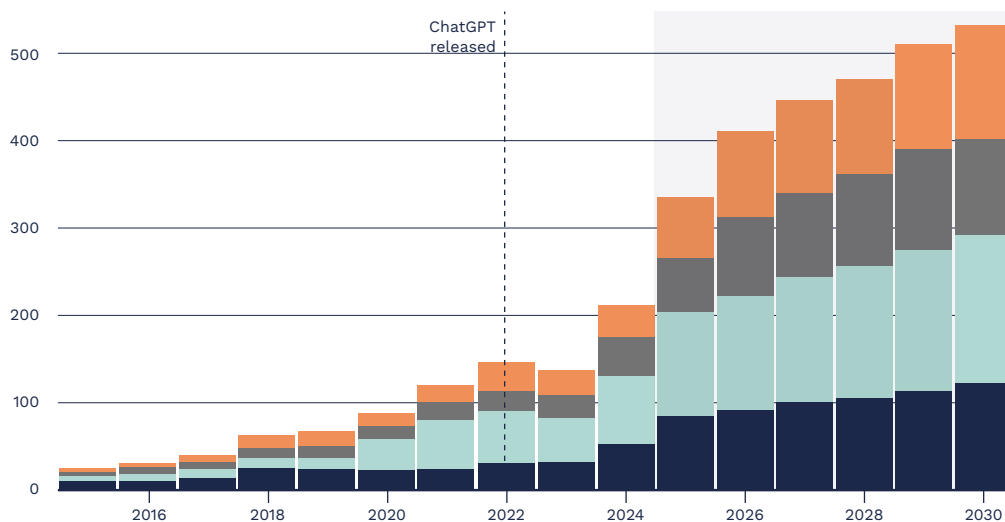


CAPITAL EXPENDITURE ON AI BY ALPHABET, AMAZON, MICROSOFT AND META HAS MORE THAN TREBLED IN THREE YEARS TO OVER \$320BN THIS YEAR

AI drives surge in Big Tech capital spending

Capital expenditure. \$bn

■ Alphabet ■ Amazon ■ Microsoft ■ Meta



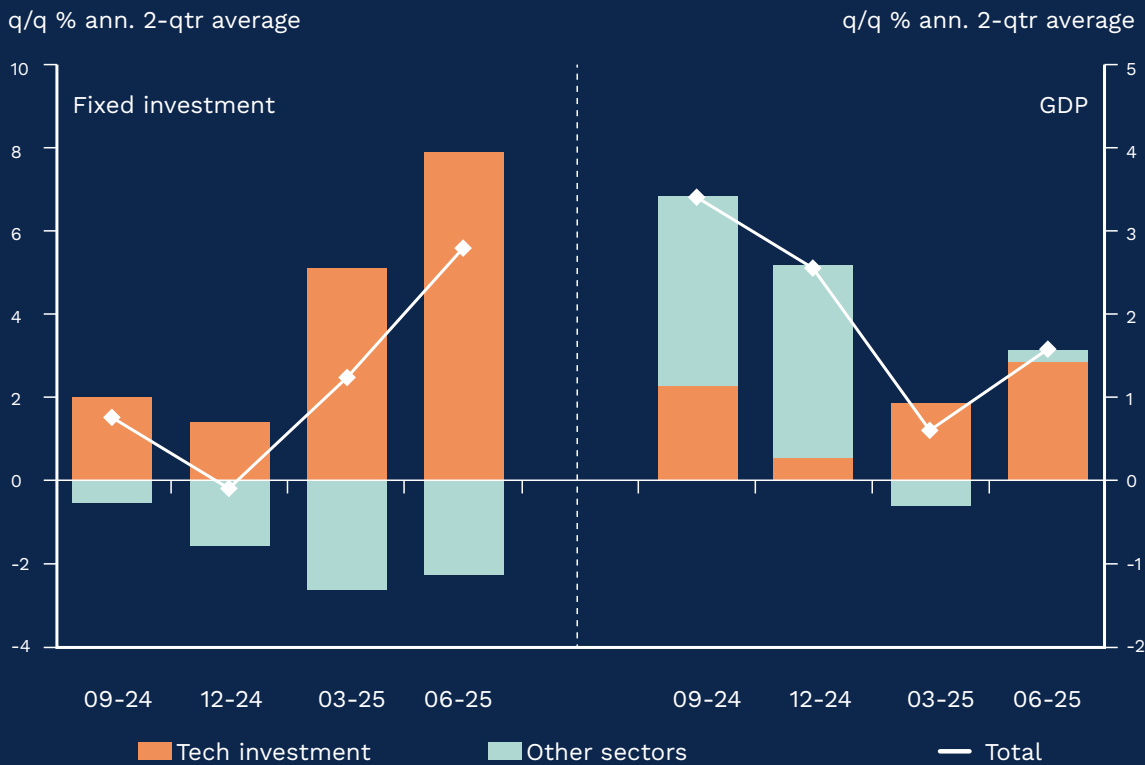
Source: 10-k filings, S&P Global Market Intelligence • Forecasts = shaded area

This surge in investment is having a meaningfully positive impact on the U.S. economy, with spending on AI infrastructure – including chips, data centres and software – acting as a key driver of U.S. growth in the first half of 2025. Oxford Economics (an independent research organisation) calculates that investment in this space grew at an annualised 20 to 40% pace in this period, matching levels seen in the TMT bubble of 1999 to 2001. It accounted for all of the increase in U.S. fixed investment in this period, and also the bulk of U.S. growth in the first half of the year. Put another way, without this investment splurge, the U.S. economy would have flatlined.

Understandably, this heavy investment has helped to fuel optimism about AI, driving technology stocks to new highs, and generating significant concentration in the U.S. equity market. In turn, this is having a positive wealth effect on the U.S. consumer, with the typical U.S. household’s exposure to equities at or close to historic highs. This ongoing AI investment, coupled with signs of a pickup in retail spending and a fiscal boost in 2026, likely lays the groundwork for a reacceleration in U.S. growth as we move into 2026.



US: TECH SHARES IN INVESTMENT AND GDP GROWTH





For those investors who remember the TMT bubble, it won't come as a surprise that parallels between the high levels of expenditure and valuations and the bubble of 1999 to 2001 are being drawn, but it is not clear at this stage if we are at the beginning of the cycle, or close to the end. Nevertheless, it's important to be cognisant of the parallels and consider the impact on the global economy if there were a meaningful downturn in the technology sector.

Oxford Economics has taken this analysis further and modelled two scenarios, the first being a U.S.-centric decline in the technology sector, resulting in a contraction in business investment. Under this scenario, U.S. stocks would decline, led by the technology sectors, and the resulting 1%

drop in GDP would take the economy close to a technical recession. Their second scenario evaluates a more extensive drop in international equity markets and economies, as a result of the slowdown in the U.S. economy. Here, they predict global growth could decline by more than 1% and probably take some economies into recessionary territory.

With all models like this, there are considerable uncertainties, and there are no clear signs that the technology sector will come to a shuddering halt any time soon. Nevertheless, we remain attuned to developments in the sector and will continue to assess its impact on the global economy and markets as we move through the rest of this year.

Positioning and outlook

As we enter the final quarter of the year, most equity markets are at all-time highs, tariff uncertainty and fears have receded from elevated levels, and the Federal Reserve is expected to ease monetary policy further. Given the strong run that most equity markets have delivered year-to-date, and with valuations looking stretched in certain areas, the prospect of a pick-up in market volatility is likely rising. So, as we head into the autumn, we think there could be a few storms to come. As such, we continue to emphasise the importance of regional diversification across equity markets, and a balanced allocation to fixed income, focused on low-duration Government bonds and investment-grade credit, which lowers risk.

Over the course of the quarter, we have been reducing our equity exposure in strong equity markets and taking our allocations across our portfolios back to a neutral stance. Within the U.K., we have dialled back exposure to both equities and Government bonds, recognising the risks around the economy as we head into the Budget. We have allocated the proceeds from the reduction in U.K. gilts to emerging market debt and investment grade credit, providing further diversification benefits while picking up more attractive absolute yields. In equities, we continue to retain a preference for the “rest of world” over the U.S., where valuations are less demanding and where we think we’ll see investors focusing towards the end of the year.



Rory Smith
Chief Investment Officer





versoim.com / info@versoim.com / 020 7380 3300

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Registered in England No. OC351100 at Cannon Place, 78 Cannon Street, London, EC4N 6HL
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