

CIO Letter | How to deal with a world of multiple disruptions and changing geopolitical dynamics

Dealing with a changing investing environment

An increasingly uncertain and increasingly disrupted world poses new challenges for investors

After an extended period of relative calm, financial markets have been confronting a growing number of disruptions and sea changes since at least early 2022: the war in the Ukraine, the disruption from AI after the launch of ChatGPT in late 2022 and the unorthodox trade and fiscal policies of that President Trumps return to the White House brought.

While these challenges in themselves call for caution, another trend that has benefited many investors for so long looks poised to reverse: the strength of the USD and the outperformance of US assets. US assets have outperformed non-US assets for the last 14 years, longer than any other up-cycle since 1970. It appears to be approaching an inflection point as the up move looks increasingly stretched and President Trump keeps pushing every lever at once that can be associated with triggering a trend reversal (details see CIO Letter of September 5, 2025).

Passive investing and the growing market concentration exacerbate the problem

The proliferation of passive investing in recent years is adding to the challenges. Today, more than 50% of equity assets are being managed passively, but when adding the sizable amount of "quasi" active funds that follow the indices closely, the share of passive investing is significantly higher.

Why is this an issue? Because for passive investors, valuation simply doesn't matter, contact with the underlying asset is increasingly being lost as passive products mechanically overweight already overvalued stocks and underweight undervalued stocks. As a result, they amplify momentum driven price distortions, effectively **acting as momentum plays in disguise**. That would not be a problem

if 5% to 10% of funds were managed this way as in 2010, but with so much money now in passive funds amplify the issue.

And when those flows reverse -- perhaps due to reversing financial flows for fears of recession, margin calls, a bubble bursting or demographic changes -- the aforementioned momentum effect reverses and amplifies the decline. Passive strategies and the staying power of their investors will be sorely tested then.

A further consequence of the above is that popular indices are much more concentrated than ever before. Investors may think they are diversified buying indices like the S&P500 when, in reality, they are becoming ever riskier as their concentration and dependence on individual names or sectors grow.

Implications and opportunities

The above means that the deviations from fair value will grow bigger and may last for longer because the active crowd willing to step in and buy bargains has grown ever smaller in recent years. All this said, the mean-reverting nature of asset valuations, particularly equities, is well-documented in investment research. Valuations will eventually revert to fair value but given the above dynamics at play it just might take longer.

While this may all sound very scary, we see such structural distortions first and foremost as an opportunity for the disciplined investor able to take a long-term view as more assets look detached from their fundamentals resp. intrinsic value.

Consequently, we will focus even more on fundamental research to find the diamonds buried in the sand. This applies as much for researching equities as for evaluating entire asset classes. Hence, the case for our approach of focusing on long-term fundamentals and only investing where we see a sufficient return after inflation has never been stronger.

Implications for our Multi-Asset-Class Mandates

Since the late 1980's/early 1990's institutional investors adopted an increasingly disciplined approach to investing. They applied a rigorous benchmark approach based on a Strategic Asset Allocation (SAA) with often limited leeway for deviations. Most of those asset class buckets were increasingly filled with passive components which was a major force behind the proliferation of passive that we discussed in the prior section.

This approach produced solid results for the post 30-40 years, a period of relative calm after the fall of the iron curtain and thanks to steady economic progress. The equilibrium in markets on which SAA was based may no longer exist in this multi-polar world facing multiple, overlaying disruptions from geopolitics, trade wars, AI and threats to the dominance of USD and US-assets. A more flexible approach will be needed in such an investing environment, in our view.

A growing number of the most sophisticated investors are applying more flexibility in managing their assets.

Already well equipped to deal with the challenges

We at Lloyd have always aspired to only invest money where we could see a sufficient long-term return after inflation with an acceptable risk. Therefore, we were never shy of utilizing the ranges in our asset allocations to the full to achieve that. This allowed us to move the portfolio where we see bargains while avoiding over-priced investments that will not produce the desired returns with an acceptable risk.

Our positioning in recent years in bonds, gold and real estate are good examples to explain what exactly we mean. For years, we have held the absolute minimum in bonds with a short maturity in our MAC-portfolios as we forecast only unsatisfactory real returns for them. The rapid printing of money by the central bank made the problem worse as printing a lot of money tends to result in rising inflation, sooner or later. This in combination of ultra-low interest rates and growing inflationary risks was a toxic mix. To counter those risks we invested the funds not allocated to bonds to a large position in gold and later in Swiss

and Japanese real estate. Such hard assets tend to provide good long-term protection against rising inflation. Later on, as the view grew that the uptrend in the USD, that had lasted for almost 15 years, could come to an end, we decided to invest more funds into stronger "hard" currencies, such as the Swiss Franc. However, because the 10-year Swiss Government bond only yielded 0.07%, we invested the allocation that was initially earmarked for Swiss Franc bonds into Swiss real estate that yielded 2.3% and offered some moderate capital gains over time.

Japanese real estate was another example. After having avoided Japanese investments outside the selected equity investments, the Yen had grown into the most undervalued major currency when compared to its purchasing power parity (PPP). At the same time, Japanese real estate had worked off its massive overvaluation from the late 1980's in a 35-year underperformance to become one of the few major real estate markets trading at a (slight) discount to fair value, yielding 4.5%. This made it much more attractive than USD Bonds. Hence, we added our first investment in Japanese real estate to diversify away from USD-assets.

While we think we are already well equipped to deal with the growing challenges of more aggressive deviations from intrinsic values and growing index concentrations, we now want to go a step further.

To fine tune our proven approach, we will move from managing the deviations from asset class benchmarks to managing target returns based on simplified "reference portfolios" for each strategy with an appropriate active risk budget. That should liberate us even more in our decision-making process. To manage risk, we will work even more intensively with scenario analysis and stress tests so that the portfolio is better prepared for the uncertain world we see ahead.

As we adapt our approach, deviations from comparable portfolios at competitors managed by the "traditional way" could potentially grow, while the likelihood of achieving the long-term absolute investment returns of our Multi-Asset-Class Strategies should increase. As a result, the new approach will

require patience from our clients to allow the time necessary for the investments to generate their long-term returns.

Implications for our pure equity strategies

While the challenges for Multi-Asset-Class strategies are very broad based and across most asset classes the implications for our pure equity strategies are as profound.

While the most important challenge will likely be dealing with a potential AI-boom and bust scenario (see our CIO Letter of Dec. 1, 2025), the impact on sector and regional performance trends from a potential reversal of the dominance of US-assets could be as significant (CIO Letter of Sept. 5, 2025).

However, since there is no free lunch in financial markets and we are faced with an array of disruptions and challenges not seen in a very long time, equity investors need to decide if they want to prioritize managing the downside or going for the opportunities that these multiple disruptions will ultimately present.

While we should be able to mitigate the risk of catastrophic losses through our focus on quality and valuation, volatility and temporary underperformance may not be avoided.

We feel that our investment approach based on bottom-up research and taking a long-term view while only investing in quality businesses that we can understand at an attractive is particularly suited for the challenging road ahead. The reason is because it focuses on the key drivers of long-term returns, which are paying an attractive price for growing cash flows stemming from offering outstanding products and services combined with good management resulting in superior profitability and balance sheet strength.

Summary:

Given the growing number of disruptions, the ongoing changes in the political and economic world order along with the potential reversal of long-term asset flow and currency trends suggest that the next few years could prove highly challenging for investors. Some of the recent trends in the financial industry, most notably the growing rise of passive investing

and the resulting rise in market concentration, add to the challenges.

Clearly, while investors face a more uncertain investing environment, there is also a growing number of opportunities arising from what is happening. Not only is the AI-opportunity large and growing, but the large number of quality names outside AI that have been out of favor for so long offer many attractive investment opportunities for the patient long-term investor willing to do the work to identify the diamond lying in the mud.

Of course, in an environment like this the challenge for investors is to balance the opportunities with the rising risks. If one thing is clear, there is no free lunch in financial markets, particularly in the challenging investing environment investors will be faced with in the coming years.

Consequently, being in the right strategy is the first and most important step. Therefore, we have structured our products offering along the key dimensions. On the equity side the Focused Equity Strategy seeks to invest in outstanding businesses with a significant margin of safety (globally). The International offers the same but excluding US stocks. The Growth Equity Portfolio (GEP) targets quality innovators and growth companies that can outgrow the market for a long time at the right price. While the GEP allows investors to benefit from innovations it does so with a clear focus on quality and visibility. While this may not avoid short-term volatility, it should avoid catastrophic losses at the portfolio level.

The Multi-Asset-Class (MAC) Mandates are focusing on achieving certain long-term target returns from a diverse set of sources without strictly following a benchmark. Through this, MAC-Mandates will not be held hostage by the tyranny of such benchmarks and short-term comparisons with their structures and performance.

Understanding those strategies and their risks and opportunities are key elements to making the right choices. We will be at your disposal any time to explain their construction and behavior in great detail.

We feel that our investment approach based on bottom-up research and taking a long-term view while only investing in quality assets that we can understand and where we see a sufficient return after inflation is particularly suited for all our strategies for the challenging road ahead.

Disclaimer / Important Information

This document has been prepared and distributed by Lloyd Capital LLC based on various reliable research information. Although it may contain contributions of research analysts or quote research reports, it is not investment research or a research recommendation for regulatory purposes as it does not constitute substantive research or analysis. Some of the articles quoted in this document may have been published on Bloomberg by various trustful research providers and may be found on the research providers' website, including the necessary disclaimers and disclosure statements. It is directed to a professional audience including prospects and not intended for distribution to, or use by, any person or entity that is citizen or resident of, or located in any jurisdiction where such distribution, publication, availability or use would be unauthorized or otherwise contrary to applicable law or regulations. Information, tools and material presented in this document are provided for information purposes only and are not to be used or considered as an offer or solicitation to buy, sell or subscribe any securities or other financial instruments. Any information including facts, opinions or quotations, may be condensed or summarized and is expressed as of the date of writing.

The information contained in this document has been provided as a general market commentary only and does not constitute any form of regulated financial advice, legal, tax or other regulated service. It does not take into account the financial objectives, situation or needs of any persons, which are necessary considerations before making any investment decision. Lloyd Capital LLC does not advise on the tax consequences of investments and you are advised to contact a tax advisor should you have any questions in this regard. The information provided is not intended to provide a sufficient basis on which to make an investment decision and is not a personal recommendation or investment advice. It is intended only to provide observations and views of Lloyd Capital LLC at the date of writing, regardless of the date on which the reader may receive or access the information. Observations and views contained in this document may change at any time without notice and with no obligation to update. The information may change without notice and Lloyd Capital LLC is under no obligation to ensure that such updates are brought to your attention. Accordingly, Lloyd Capital LLC accepts no liability for any loss arising from the use of this document.

Lloyd Capital LLC partners, affiliates and/or their employees may have a position or holding, or other material interest or effect transactions in any securities mentioned or options thereon, or other investments related thereto and from time to time may add to or dispose of such investments. To the extent that this document contains statements about future performance, such statements are forward looking and subject to a number of risks and uncertainties. Information and opinions presented in this document have been obtained or derived from sources which in the opinion of Lloyd Capital LLC are reliable, but Lloyd Capital LLC makes no representation as to their accuracy or completeness. Lloyd Capital LLC accepts no liability for a loss arising from the use of this document. Unless indicated to the contrary, all figures are unaudited. All valuations mentioned herein are subject to Lloyd Capital LLC valuation policies and procedures. It should be noted that historical returns and financial market scenarios are no guarantee of future performance. The price and value of investments mentioned and any income that might accrue could fall or rise or fluctuate. Past performance is not a guide to future performance. If an investment is denominated in a currency other than your base currency, changes in the rate of exchange may have an adverse effect on value, price or income. Investments may have no public market or only a restricted secondary market. Where a secondary market exists, it is not possible to predict the price at which investments will trade in the market or whether such market will be liquid or illiquid. The retention of value of a bond is dependent on the creditworthiness of the Issuer and/or Guarantor (as applicable), which may change over the term of the bond. In the event of default by the Issuer and/or Guarantor of the bond, the bond or any income derived from it is not guaranteed and you may get back none of, or less than, what was originally invested. Parties other than the Issuer or Guarantor (as appropriate) (for instance the Lead Manager, Calculation Agent or Paying Agent) do neither guarantee repayment of the invested capital nor financial return on the investment product, if nothing is indicated to the contrary. The distribution of this document and the offer and sale of the investment in certain jurisdictions may be forbidden or restricted by law or regulation. This document is not directed to, or intended for distribution to or use by any person or entity who is a citizen or resident of, or is located in, any jurisdiction where such distribution, publication, availability or use would be contrary to applicable law or regulation. This document has been furnished to the recipient and should not be re-distributed without the express written consent of Lloyd Capital LLC. For further information, please refer to your contact person at Lloyd Capital LLC.

This material may not be published or reproduced, in all or in part, without the prior written express consent of Lloyd Capital LLC.

Copyright © 2026 Lloyd Capital LLC. All rights reserved.