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### The lived experience – and how this shapes the mindsets of investors

*Markets drew lessons from lived experience and old scars that split investors into believers in the AI boom in one camp, and believers in the other.*

Many readers – and this writer – will have stayed up or got up to watch England’s remarkable victory over Mexico in the World Cup. Others will have recorded it, watched a delayed feed or caught up later. But one of the reasons that live sporting events (and the clubs that contest them) continue to command high prices for media distribution is that there really is no substitute for experiencing them in real time. And, of course, it is why match tickets can be sold at eye-watering prices.

On a more sombre note, I recently watched the film ‘Dunkirk’. It certainly strengthened my conviction that I never want to be involved in kinetic warfare, the grim physical kind, fought with bombs, bullets and bodies rather than code or coercion. But whatever emotions the big

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#### Quick take:

- Market history can be modelled, but living through shocks still shapes how investors behave.
- Past market scars help explain why Japanese households remain heavy holders of cash.
- The AI capital spending boom still divides opinion, with bulls seeing a durable growth engine and bears warning of a profitless bubble.

screen stirred in me, I know they can be nothing compared to what the participants experienced.

I have a similar feeling about financial markets. It doesn’t matter how many books you read on historic events or how much data you dissect in fancy models; the real-time lived experience counts for a lot. And the further we get away from historic events, the fewer investors remain who recall not only how they unfolded, but how they felt in the moment: the shock of the 1987 stock market crash, Black

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Wednesday, the euphoria of the dot.com boom at the turn of the century, and the gut-wrenching collapse of equity markets during the global financial crisis of 2007-09.

### Bearing market scars

None of that is to say that having experienced something in the past guarantees the successful interpretation of current events. Research has shown that investors' formative experiences can control their actions well into the future, usually to their detriment. Famously,

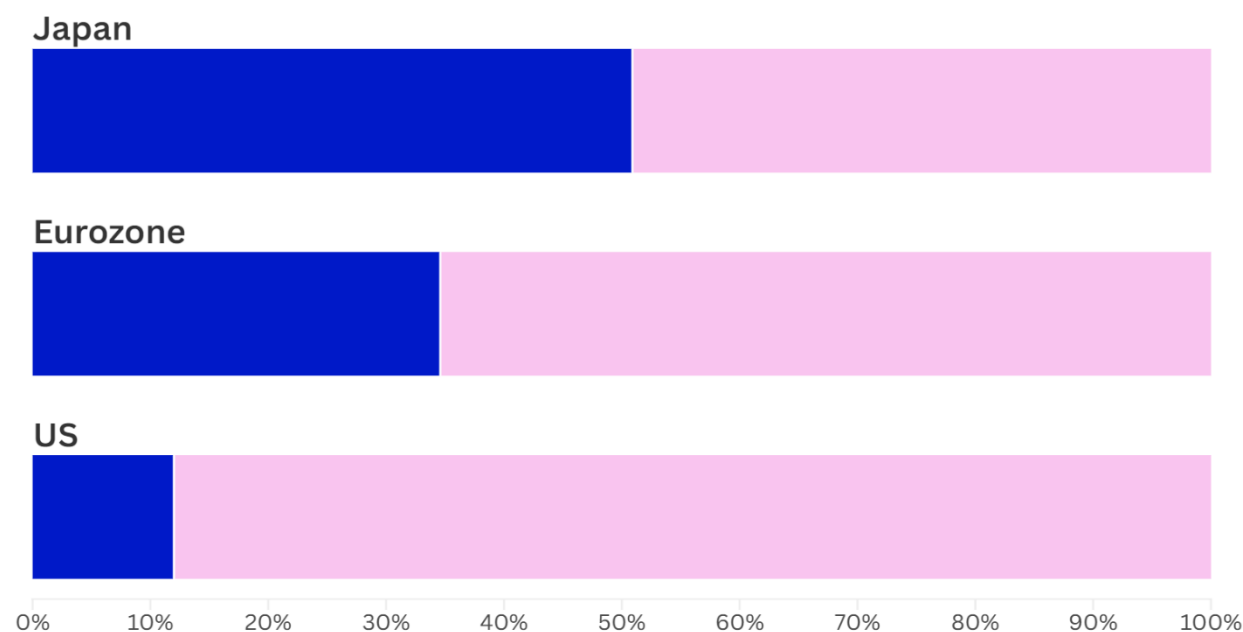
German policymakers are still scarred by the hyperinflation of the 1920s Weimar Republic, an experience that seems to have lodged in the country's DNA. Even so, 37% of German households' financial wealth is held in bank deposits, which seems crackers if inflation is a worry.

The biggest hoarders of cash are the Japanese, with 51% of their financial wealth sitting in bank deposits. That's what can happen after a stock market bubble for the ages, with the flagship Nikkei 225 Index peaking in 1990 before falling 82% to its 2009 trough.

## Mattress money

Cash and deposits as a percentage of total household assets

■ Cash and deposits ■ Other financial assets



Source: Rathbones, FT, as at the end of 2024

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It didn't regain the previous peak until 2024. But had Japanese investors bought that trough in 2009, they would now be sitting on a return of 870%, during a period of virtually no inflation.

US households, by contrast, hold just 11% of their financial wealth on deposit. That still amounts to a hefty \$20.6tn, but is a relatively small share of household net worth, at an estimated \$183tn. Those bank deposits are only slightly below the total liabilities of \$21.6tn, including mortgages and consumer credit. Yet households own \$65tn of equities, more than the \$49tn held in owner-occupied real estate. The US has been a wealth-generating machine.

The US investors' mantra for the last few decades has been 'buy the dip', with policymakers supporting financial markets at almost every turn. Market shocks often forced their hands, but the cavalry kept coming. This helped create a virtuous circle between the rising wealth and households' willingness to consume. The more this circle builds, the greater the risk that a fall in equity markets will depress consumption more than it may have in the past.

Which might be why every man and his dog is constantly on the lookout for anything that could signal a market peak. The trouble is that this fear of market failure has been evident for years, and during one of the more powerful equity

bull markets. It feels like worrying about the hangover before you've even had a drink.

I keep coming back to the observation that, despite the scary headlines and the constant market bubble talk, this still feels nothing like 1999/2000. As I noted recently, this cycle has been supported by strong earnings growth, not just rerating – investors paying a higher multiple for the same profits.

### **They can't both be right!**

The biggest battle today, I think, is between the AI bulls and bears. One of the privileges of sitting in my seat is that I get access to some really interesting meetings. Last week, I was able to hear both sides of the argument expressed with equal conviction.

The bear was a blogger/ journalist/ podcaster by the name of Ed Zitron. His assertion, in a nutshell, is that we are in a massive AI-related capex bubble that will collapse once it becomes clear that OpenAI (ChatGPT) and Anthropic (Claude) will never be able to make an economic profit. This is important because he estimates that these two companies alone purchase between 70% and 85% of all available computing resources. He cited plenty of risks that are already widely debated: big technology companies funding customers who then buy their products (known as circular financing); the

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threat from cheaper open-source AI models; and the shock users may feel as providers switch from generous subscription-style pricing to charging by usage. It's all plausible.

A day later, I met technology fund managers at a very high-profile company. They'd not just drunk the AI Kool-Aid; they'd seemingly fallen into the vat of it when they were babies. They describe the AI capex race as existential, forecasting a cumulative industry capex of \$9.6 trillion by 2030, versus what they believe to be a current consensus forecast of around \$5tn. They see AI's total market rising from \$2tn today to \$11tn in 2030. Some of that will come from robotics and local device 'edge' demand – where AI tasks are processed on or near the device itself rather than in a data centre. They predict that companies will cut headcount to fund more token use, as competitive pressure leaves them little choice. Based in San Francisco, they think they have the best view. A sceptic might say they're too close to be able to see the bigger picture.

If they're right, the performance of the beneficiaries of the current capex boom is at least sustainable and probably just a prelude to further big gains. But if Mr Zitron is right, this whole edifice collapses. It still feels far too early to bet the farm on either outcome.

### Regional highlights

**UK.** Recent UK economic data had been more resilient than expected. Hence, Citigroup's UK Economic Surprise Index sits at +41. However, the latest batch looked a bit weaker. Mortgage approvals in May totalled just 56.2k, down from 66k in April and below the forecast 63k. Rising bond yields and the fear of higher interest rates following the outbreak of hostilities in the Middle East are weighing on demand. Other disappointments included the Lloyds Business Barometer, which fell from 47 to 44 (versus an estimated 48), and the S&P Global Manufacturing Purchasing Managers Index (PMI) – 52.5 in June versus 53.1 in May and 53.1 expected. The S&P Global services PMI slipped to 48.8 in June from 49.3 in May. Respondents indicated that rising energy prices had weighed on consumer spending, while investment intentions were muted as businesses remained cautious amid ongoing geopolitical uncertainty. The final GDP reading for the first quarter was revised lower from 1.1% year-on-year to 0.9%. This at least means a lower probability of a base rate increase from the Bank of England.

**US.** Nonfarm payrolls rose 57k in June, well below the consensus forecast of 115k. Job growth for April and May was revised lower. This left the three-month average at 111k, a solid number given the contraction in the labour force since the start of the

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year. The 'breakeven' rate to stop unemployment from rising used to be around 150k. Now it's estimated at somewhere between zero and 50k. The labour market is in a state of flux due to curtailed immigration and the uncertain effects of AI adoption. Job openings have rebounded, but fewer workers are willing to quit their current jobs, usually a sign of uncertainty. As in the UK, this takes some pressure off the Federal Reserve, with market-based expectations suggesting much less conviction about higher interest rates.

**Europe.** The economy seems to be stabilising after the Iran-related shock. Even so, underlying momentum remains modest, although marginally stronger than expected at the peak of the war. Eurozone inflation eased from 3.2% in May to 2.8% in June. The main driver was softer energy inflation, with this component easing to around 9% from 11% following the US-Iran ceasefire. Food inflation also declined on the back of a monthly drop in unprocessed food. As with other central banks, expectations for higher interest rates from the European Central Bank have been tempered, with just one more increase now expected – and conviction in that is weakening.

**China.** The June composite PMI fell 0.4 points to 53.6. For Q2 as a whole, the index

averaged 53.6, up from 52.8 in Q1, pointing to the private economy growing at a faster clip during the quarter. The June decline was probably a payback effect following the Golden Week holiday in early May. A marginally softer domestic demand environment was reflected in the overall new orders index falling 0.2 points to 53.1, while new export orders jumped 1.4 points to 52.9. External demand for Chinese services rebounded for a third consecutive month after plunging during the war in March, offsetting some of the drag from still soft domestic demand. But even if activity remains sluggish, policymakers are likely to stick to only modest policy adjustments in H2 at the July Politburo meeting, rather than unveil a bazooka stimulus.

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