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REVIEW

MARCH 2025

No Wait

Message in a Bottle

Who Needs Politicians?

Pressure Drop

Rothschild & Co

MARCH 2025

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Editor's Letter

It was Sam Goldwyn, the legendary Hollywood producer, who observed, "If people don't want to come to your movie, you can't stop them."

Goldwyn understood human appetites and weaknesses and the market in which he operated. Not simply a fatalist, he appreciated there are trends too powerful to resist, moments when it is impossible to push against the tide.

Several contributors pick at such threads. George Karamanos examines the remorseless rise of passive funds and ETFs, Charles Bendit illuminates the fatal flaw in the fixed income-based model of Silicon Valley Bank, and Chris Pitcher evaluates distillers' attempts to offset the long duration properties of their product through innovative packaging and smaller bottle sizes. In similar 'structural' vein, Harry Bartlett cites the opportunities for Buy Now Pay Later stocks and Harry Dow contemplates the effects of demographics on construction companies.

Such trends are embedded, ineluctable. They torch the arguments of bull or bear at the point where ideals collide with reality. Thus, we have seen many politicians contorting themselves to adjust to the new occupant of the White House. As Mike Tyson memorably put it, "Everyone has a plan until they are punched in the face."

When tides are so powerful, politicians cannot stand in their way. If proof was needed it is offered by Spain, which, as Gonzalo López points out, is comfortably Europe's best performing economy despite being 'ruled' by a coalition so wide there is effectively no government. Politics and economics: in our supremely connected world the former has lost control of the latter.

No Wait

The Benefits of Mounjaro

Simon Baker
Biopharmaceuticals Research

No therapeutic area in my career, outside the small issue of the coronavirus pandemic, has captured the market's imagination like obesity. As pharma analysts, we have spent a considerable portion of our time talking and writing about it. We have opined on clinical trials, intellectual property, manufacturing and pricing. About the only thing I have not done is take the drugs. Until now.

My first attempt at weight loss preceded the 2020 pandemic. Confinement at home and the need to fit into a wedding suit conspired to make it very successful. I ended the year over 25kg lighter, entering territory unvisited since Tony Blair's first government. Most of the weight stayed off, but the chart did bounce from 90kg to 99kg. My ascetic lifestyle and punishing fitness regime were not delivering fully, so it was time to practice what I preached and try a pharmaceutical intervention.

In the UK, the provision of obesity drugs on the NHS is almost non-existent, with stringent requirements far in excess of the approved indications. As a result, the online private market has filled the gap, initially with Boots but now augmented by many others. As both Novo Nordisk's Wegovy and Eli Lilly's Mounjaro (in the UK, the obesity indication is not called Zepbound) are prescription products, an online consultation is required.

Straightforward questions were completed (weight, height, pre-existing conditions), followed by an ingenious identity check. My driving licence was scanned and I was asked to upload a photo of myself to confirm my BMI measurement was genuine, to ensure I was not seeking an inappropriate prescription for purely cosmetic reasons. The process took less than 48 hours, over a weekend, albeit it is being tightened by the introduction of video consultations.

Which drug to choose? In our discussions of Wegovy and Mounjaro/Zepbound, we have always noted the average weight loss is the mean of a wide spread of outcomes, from around zero to -50% in the case of Mounjaro. Therefore, concluding one (Mounjaro) is definitively better than the other is slightly misleading, but it is true that, on balance, the performance is skewed towards Lilly's product. Overriding efficacy, however, was the question of supply. While both are now readily available in the UK, I was faced with Mounjaro or a wait, so opted for the former. Nevertheless, the higher headline figure of 22% weight loss compared to 18% for Wegovy certainly had an impact. Based on an entirely unscientific sample, I know of nobody on Wegovy for weight loss, while recent reports suggest a 70% share for Mounjaro in this market.

Online checkout completed (with a 40% offer code, taking the first dose down to around £100 plus delivery), I was told the drug would arrive within a few days. Two days later, a shoebox-sized package arrived, containing a Mounjaro pen in a small box sandwiched between icepacks wrapped in a wool blanket. Not quite Apple levels of slick packaging, but impressive. The instructions for administering the weekly dose are exhaustive, but my nurse wife helpfully trimmed the process down to the essentials: take the top off the pen, screw on the disposable needle, dial up the dose to one (the pen has been repurposed from an insulin device), inject and press. The needle is so fine as to be undetectable, so the process is painless. And so the journey begins.

The following day, I sensed its presence through a very mild nausea. Clinical trial categorisation of side-effects rises from Grade 1 (mild) to Grade 5 (death). Grade 1 nausea is defined as a loss of appetite without alteration in eating habits and fewer than two vomiting episodes within 24 hours. Grade 1 vastly overstates my experience, which I would describe as Grade 0.5. I never felt sick, but did feel 'not quite normal', with alleviation coming from tea or water.

I expected the nausea to follow eating, where my newfound reticence had not yet translated into smaller portions. Surprisingly, I most often experienced nausea on an empty stomach rather than after a meal. Starving oneself into shape is not the way these drugs work. Rather, they modulate appetite and satiety, making one feel fuller for longer. That took a little adjustment. I was surprised how quickly the sense of fullness manifested, within the first week of treatment. Although I am not traditionally a grazer, the few nibbles I did take during the day declined swiftly and noticeably.

All the trimmings

After one week, I saw the first impact on weight, a couple of pounds. Over the course of the first month, four doses of the starting 2.5mg strength, that doubled. Compared to the timeline of weight loss seen in the clinical trials, it was a little slower, but progress nonetheless. This period coincided with a family trip to Center Parcs, hardly an ideal environment in which to lose weight.

With each monthly reorder of the drug, the dose increases 2.5mg, so I am now on 12.5mg, the penultimate step to the maximum 15mg. The price also increases, from £149.99 to £199.99, a little cheeky given the manufacturers' prices are flat across the dose range. For the first few increases, I was not aware of any increase in nausea, experiencing low-level effects on the second day after injection. For the 12.5mg dose, there was a distinct increase in symptoms, albeit still far from the official definition of 'mild nausea'. Titration up to the maximum dose was part of the clinical trial protocols for all initial obesity studies, but we hear reports from US physicians that the proportion of Zepbound (Mounjaro) patients on 15mg dosing is small.

I am undecided whether to increase the dose and know of people who stopped at 10mg in part owing to tolerability but also because the weight loss was sufficient. This patient-driven dosing approach was adopted by Novo Nordisk in the recent REDEFINE-1 trial of its next-generation obesity treatment CagriSema. When offered the chance to lower doses for reasons of efficacy or tolerability, patients in the study did just that, resulting in a lower average weight loss that severely impacted Novo's share price last December. Clinical trials should represent the real world, but there are limits.

One question that has been asked with increasing frequency by friends, colleagues, clients and consumer analysts is the impact of these drugs on alcohol consumption. In the US, over 25 years of consumption growth has been erased in the last three, with many pointing the finger at the GLP-1 agonists.

Survey work by Cornell University has reported lower alcohol purchasing by households on these drugs, by around 3.5%. Prospective clinical trial data is still awaited, but early retrospective studies suggest an effect, potentially caused by a combination of feelings of satiety and changes to dopamine levels in the brain. Some people have asked me, in concerned tones, if I have stopped drinking. The answer is no. Beer consumption appears entirely unaffected, but I have noticed a glass of wine lasts longer. That has meant fewer bottles of wine in the monthly shopping basket and raises an interesting point. The monthly drug price should be seen as a gross price. The net cost, after smaller grocery bills, will be lower, in my case close to zero.

After five months, I have lost 9kg, leaving less than 2kg to go. The journey has been a good one, although I am not sure how it ends when I reach my goal. Low dose? No dose? The drug is easy to obtain and administer. Despite it being a weekly injection, I still manage to forget to take it on Wednesdays, but a day's drift is unimportant. A weekend start would probably be more sensible, but while some are clamouring for a daily oral obesity therapy, that wouldn't fly with me. Mounjaro works for me at a reasonable rate albeit slower than the average clinical trial experience. The positive impact on my cardiovascular, renal and hepatic health will not be known for years, nor will the potential Alzheimer's risk reduction, but these are early days. The tolerability has been fine, although it would be nice to have no nausea whatsoever. That aside, I have no issues, certainly nothing approaching an 'adverse event'.

Would I recommend Mounjaro/Zepbound or Wegovy for weight loss? I would, in both cases. As TV adverts say, 'individual experiences may differ' but mine have been positive. Nausea management, if you have it, is the key. So the question is less about weight loss than how will you feel about doing it?

Morality Tale

SVB: A Very Modern Bank Run

Charles Bendit
Capital Markets Research

Silicon Valley Bank (SVB) was almost uniquely vulnerable to the series of events that culminated in its collapse on 10 March 2023. Solvent on paper just 48 hours earlier, the episode highlights the lightning pace at which modern bank runs can occur, enabled by seamless communication and mobile and internet banking. But, as with the long line of bank crises before it, the causes of SVB's collapse were entirely rooted in human nature – failure to manage or mitigate risk, and the instinct of depositors to perpetuate panic and to find safety in the face of uncertainty.

Founded in 1983, SVB carved out a niche in serving growth-stage companies in the technology sector over the subsequent four decades. Its deposits more than tripled over 2020-21, increasing by more than $100bn during the COVID-era boom in venture funding, IPOs, secondary offerings and special purpose acquisition companies, as tech startups parked their newly raised funds at the bank. By the end of 2021, SVB had $189bn in deposits, of which more than 90% were uninsured (in that they exceeded the Federal Deposit Insurance Corporation (FDIC)'s $250,000 coverage limit), well above the industry average of nearer to 50%.

Unable to deploy this fresh liquidity into lending products as its clients were flush with VC funding and anyway tended to have more modest borrowing appetites compared with traditional businesses, SVB instead allocated a disproportionate share of its total assets to fixed-income securities, primarily long-duration US treasuries and agency mortgage-backed securities (MBS). By the end of 2021, securities made up c55% of its $120bn in total assets, far higher than most banks. In so doing, SVB was also locking in low returns for years to come, and in effect taking a bet on long-term rates staying low.

SVB had increased its duration risk meaningfully, with the estimated duration of its MBS portfolio (roughly six years) making it highly sensitive to rising rates.

Beginning in March 2022, in response to soaring inflation, the Fed increased rates at the fastest pace in forty years, increasing the federal funds rate from 0.25% to 4.5% by the end of 2022 and ultimately to 5.5% by July 2023. The increase in rates and rate expectations impacted SVB in two ways: (i) as tech fundraising dried up, its highly concentrated depositor base continued to burn through cash to sustain operations, resulting in a c$25bn deposit outflow in H2 2022; and (ii) it put the bank's securities portfolio under water, as the value of its fixed-income securities, particularly long-dated, moved inversely to higher rates.

By the end of 2022, unrealised losses on SVB's available-for-sale (AFS) and held-to-maturity (HTM) securities portfolios had increased to more than $17bn from c$1bn a year earlier, including c$15bn losses in the HTM portfolio, not far off SVB's c$16bn in tangible equity. Since HTM securities are not carried at fair value (meaning their declining value was not reflected on the GAAP balance sheet), SVB's financials appeared solid, when the bank was, by other non-banking measures, effectively insolvent in Q4 2022. Further, regulatory exclusions – allowing mid-sized banks to omit unrealised losses on their AFS securities portfolios from their regulatory capital calculations – made SVB look robust on these measures also.

On 8 March 2023, in an effort to shore up liquidity and instil confidence prior to an impending credit rating downgrade from Moody's, SVB management pre-emptively announced the sale of $21bn in low-yielding AFS securities, crystallising a $1.8bn loss. To compensate, it announced a $2.25bn capital raise, comprising a $1.25bn in common stock offering, a $500m private placement from General Atlantic, and a $500m preferred stock issuance. But, contrary to management's intentions, the move spooked the market, triggering a 60% intra-day share price plunge, as investors interpreted the efforts as a sign of further trouble.

Fearing SVB's imminent collapse, a number of prominent venture capitalists, including Peter Thiel (of the Founders Fund) and David Sachs (Trump's AI and crypto czar), advised their investee companies to withdraw uninsured funds immediately.

On 9 March, SVB lost $42bn in deposits, roughly one-quarter of its total. This was more than four times the $10bn in deposits lost by Wachovia in eight days and more than two times the $19bn lost by Washington Mutual in sixteen days around a decade and a half earlier in

Funeral parlour

the lead up to the 2008-09 Global Financial Crisis.

SVB management expected another $100bn to be withdrawn the next day, on 10 March, which would amount to more than four-fifths of its remaining deposit base. This would outdo all previous bank runs in scale and scope. Unable to meet the withdrawals requests, SVB ran out of liquidity and its stock plunged a further 60% in pre-market trading.

On 10 March, SVB failed to secure additional liquidity or find a buyer, and the FDIC shut the bank down and placed it into receivership, crystalising the biggest US bank failure since 2008.

This put c$151m in uninsured deposits at risk, sparking panic in the system. To prevent wider contagion, the Fed and FDIC took emergency action on 12 March. The FDIC moved to guarantee all US deposits, effectively expanding deposit insurance to 100%. Next, the Fed created the Bank Term Funding Program (BTFP), allowing banks to access funding by pledging as collateral their securities at par value, as opposed to market value, eliminating the liquidity risk that SVB had suffered.

This was not timely enough to evade Signature Bank's collapse, given depositors feared similar risks to SVB as it had a largely uninsured deposit base that was highly concentrated to the crypto sector.

Neither could it contain the panic that led to the collapse of First Republic, a regional bank that catered to high-net-worth individuals, and so housed a large percentage of uninsured deposits, and managed an underwater portfolio of long-duration, low-interest mortgages. The $30bn deposit injection from eleven large banks on 16 March provided only temporary relief – First Republic was seized by the FDIC and subsumed into JPMorgan Chase just six weeks later, on 1 May. SVB's assets were acquired by First Citizens Bank by the end of March.

SVB's collapse is a lesson in failed risk management, specifically a failure to hedge interest rate risk and an overreliance on a single industry for the client base. But it also exposed fault lines in banking regulations around AFS and HTM accounting rules that allowed the bank to avoid recognising large unrealised losses on its balance sheet, and raised questions around FDIC insurance limits, which had been increased in response to previous banking crises.

Further, the bank's collapse highlighted the speed at which modern bank runs can occur. Concerns, valid or otherwise, can be communicated at pace across social media and deposits withdrawn swiftly via mobile and internet banking.

Proposed regulatory changes in SVB's aftermath specifically address how mid-sized banks account for AFS unrealised losses, removing the opt-out for these banks when calculating their regulatory capital. But HTM securities continue to be held at carrying value in both GAAP accounts and regulatory ratios. For this reason, in the event that rates, particularly at the long end, go higher, it is possible many such HTM securities portfolios across US bank balance sheets will again be sufficiently underwater to undermine confidence.

That the yield on the ten-year US treasury has increased markedly since the Fed's first rate cut in September 2024 is potentially an ominous sign. As of Q3 2024, HTM unrealised losses across the US banking industry amounted to $225.4bn, an improvement on the $390.1bn peak recorded in Q3 2023. However, since then long rates have moved higher, suggesting this position will worsen materially by Q4 2024, particularly if marked to market.

Most banks are not like SVB in having a disproportionate share of their assets invested in securities; but cracks may appear elsewhere, for example in commercial real estate portfolios where distress is often tied to higher rates. For now, the market remains sanguine about these risks and the sector continues to enjoy the benefits of higher rates on net interest margins.

Message in a Bottle

Evolution of Spirits Packaging

Chris Pitcher
Beverages Research

There is no 'use by' date on a bottle of whisky. This simple observation is perhaps one of the most profound considerations when understanding the mechanics and valuation of the distillers. Unlike beer or milk, unopened, spirits do not perish and can theoretically be stored indefinitely. If kept upright, with a well-fitted cork to prevent evaporation, whiskies, vodkas and gins can be consumed over months, if not years, even after opening. Consequently, bottles accumulate through all layers of the supply chain, from the distillery to wholesalers and retailers, right through to people's homes. An audit of even the most well-curated drinks cabinet will probably yield a dusty bottle or two of obscure liquor, often gifted or purchased in a moment of holiday euphoria. This propensity for inventory to build up amplifies cyclicality, reduces visibility and lies at the heart of the current problems faced by the industry.

On its website, Ballantine's Scotch recommends finishing an opened bottle within six months to two years, depending on how much is left, as the more air in the bottle means faster oxidation. An entire industry has emerged to help the moderate wine drinker enjoy an opened bottle over more than one sitting. From the basic wine stopper to inventions such as 'Vacu Vin' and 'Coravin', all are battling a natural process. Spirits by their nature preserve better and are therefore not a naturally fast-moving consumer good. Clearly, Ballantine's owner, Pernod Ricard, would prefer a drinker did not savour the product over two years but purchased more frequently, within the considerations of responsible drinking. But the ultimate pace of rotation is determined by how many servings there are in a bottle.

This may seem a simple calculation but in essence a serving is a subjective measure. In *Raw Spirit*, Iain Banks took a break from sci-fi and applied himself to the science of tasting whisky, journeying around Scotland in search of the perfect dram. In parallel, he was intrigued by whether there was an accepted definition of what 'dram' entails. The best explanation he was offered was from a distillery worker he encountered called Willy, who declared a dram is "a measure of whisky that is pleasing to guest and host". In practice, beyond the gauge of the exciseman's hydrometer, there is no standard.

Governments have varying views on the matter. The US health authorities define a standard alcoholic drink as any beverage containing 14g of alcohol. Given ethanol is less dense than water, this is equivalent to 1.5 fluid ounces of 80 proof spirit. The conversion of transatlantic weights and measures is an arcane subject, but in metric terms this is 44ml of spirit at 40% alcohol by volume (ABV). However, there are no federal regulations on the size of a serving in a bar, with an American pour at the discretion of the bartender, or rather the proprietor if they have a keen eye on their bottom line.

Definitions differ on the other side of the pond. UK health authorities talk in terms of 'units', with one unit being 8g of alcohol or a 25ml shot of 40% ABV spirit. Out in the trade, under the Weights and Measures Act, a publican may choose to serve customers in either multiples of 25 or 35ml but not both in the same establishment. To complicate the issue further, the world's largest distiller, Diageo, defines a standard serving of spirits as 33ml in its esoteric volume metric which adjusts all alcohol types to 'equivalent units'.

The frequency of purchase is also determined by the size of the container. The most common in the US is the 750ml glass bottle, also a known as a 'fifth' of a gallon, which can therefore contain between fifteen and thirty shots depending on a drinker's preferred dram. Erring on the side of generosity, if we assume the 50ml serving, or a 'double' in UK parlance, and a moderate level of consumption of a couple of whiskies a week, the bottle should last about two months. As such, the spirits brand owners have fewer shopping interactions with their drinkers than some consumer categories, where usage and, sometimes, purchases can be daily or weekly. This impairs the visibility suppliers have on shifts in consumption patterns.

However, changes are afoot which could improve matters. Prior to 2020, under regulations set by the Alcohol and Tobacco Tax and Trade Bureau (TTB), US distillers could only choose from a shopping list of seven bottle sizes, ranging from a 50ml 'miniature', synonymous with the inflight drinks trolley, through 100, 200, 375 and 750ml to the more substantial one-litre and 1.75l 'handle', so designed to ease the pouring. In 2020, after extensive consultation, the TTB added 720 and 900ml and 1.8l

The problem

alternatives. Effective 10 January this year, a further fifteen standards were introduced, extending the range to 3.75l and plugging many gaps.

The wine industry enjoys a more elongated, potentially exponential, ladder of bottles to choose from, so long as they are filled in even litres above three. The largest on record is the Melchizedek, or Midas, which contains 30l. When full, this behemoth weighs in at 80kg. Given the higher alcohol context, such a vessel would contain between 600 and 1,200 shots of spirits, depending on the size of the pour, and therefore it is not wholly surprising the TTB resisted calls to remove the cap on the upper limit for spirits bottles.

The additional flexibility is helpful. But distillers already had options to offer their wares in smaller packages to unblock some of the inventory bottlenecks, yet the 'fifth' remains the default setting. However, the change in US bottle regulations coincides with executive changes at the world's largest distiller. Debra Crew, Diageo's CEO, took over in 2023, after a career spanning several consumer goods companies, including four years at PepsiCo. Complementing Crew's experience from the blue system, Nik Jhangiani, a veteran of the red system, joined as CFO in September last year from Coca-Cola Europacific Partners.

The introduction of soft drinks experience in the boardroom is already having an influence on strategy. The Coca-Cola System was an early adopter of a strategy dubbed 'price pack architecture' in which a wide range of pack sizes are presented at varying price points across multiple channels to maximise profitability per consumer. On the stage at a major consumer conference in the US last month, Jhangiani openly admitted Diageo had a lot of work to do around its price pack architecture where its capabilities remain underdeveloped against many other consumer categories.

Barely a Coca-Cola conference call goes by without multiple references to the importance of price pack architecture to its revenue management strategy, especially since there was a sea change in focus from volume- to value-led growth under CEO James Quincey. A brief survey of Diageo's transcripts reveals the concept is not new to the company but had only received infrequent mentions historically. Crew's predecessor in running Diageo North America, Deirdre Mahlan, explored the notion briefly in an investor call in 2018. Prior to that, the concept gained passing mention in a productivity presentation in 2015 and a tangential reference at a capital markets event in 2011. The company was clearly aware of the idea but including a bullet point in a slide presentation is a far cry from embedding the concept in working practice and systems.

The strategy has proven effective. In his previous role at Coca-Cola Europacific Partners, Jhangiani helped to turn a persistently loss-making bottling network in Germany into profit. Part of the improvement was a thorough review of the mix of portfolio by pack, price and channel to identify where the business was losing money and then being prepared to walk away from low-profit volume.

A word we expect to hear more on Diageo conference calls, and potentially across the spirits industry, is 'transactions'. While there has been a lot of press speculation concerning the company's plans for its beer business and stake in Moët Hennessy, we are not referring to M&A transactions. Instead, this relates to the number of units purchased by a consumer as distinct from volume or litres. Over the past four years, Coca-Cola has become more focused on growing transactions ahead of volume, in other words tilting the portfolio to smaller pack sizes. This means more individual single-serves than multi-buys. For a distiller, this is the equivalent of migrating from the 'fifth', which is effectively a multi-buy, towards smaller bottles.

The benefits of this transition are legion. The first is improved visibility. As discussed, distilled spirits are a slow-moving consumer good where purchase frequency is calibrated in months, not days or weeks like soft drinks. By way of example, a loyal Johnnie Walker Black drinker, who enjoys a couple of drinks a week, would purchase on average six standard 750ml bottles a year. Were this drinker to move to a 200ml bottle, they would transact 23 times, not six. For the record, we do not expect such as dramatic change in purchasing habits, but it is illustrative of how visibility could be materially improved with only modest changes.

Secondly, it allows the distillers to target different occasions and price points to improve the reach of their core brands. Again, this is not new. For over a decade, Diageo has been using smaller sizes of its more standard Scotches, such as White Horse, to target the price points where beer sells in Latin America and Africa. More recently, the focus has been on broadening the reach of the prestige brands, notably Don Julio 1942, which retails for around $190 per standard bottle. This is a substantial financial commitment if a drinker has not yet tried the liquid. To lower the total out of pocket cost there is a 375ml bottle at $90, but the real opportunity to recruit drinkers is with the 50ml 'mini' at a less eye-watering $20. Still in the iconic tapered bottle, Don Julio teamed up with Jimmy Kimmel and Guillermo Rodriguez to showcase the 'mini' 1942 at last year's Oscars. It was a huge success. Within six months the format became the primary sales driver for the brand, leading to a 62% surge in demand in North America.

This also has important implications for mix. While only $20, the implied price per litre of the 'mini' is $400, more than one and half times the standard bottle. The drinker pays for the experience, but it is a much more efficient means to try a product and avoids stock piling at home if they want to experience multiple brands and styles. For the distiller, it is a great way to recruit new consumers to their prestige brand, bringing the top shelf more into reach.

Pack sizes also provide another mechanism for price increases or reductions without having to move the shelf price of a specific brand. Prior to 2020, the step changes between each permitted bottle size were too material to allow the distillers this flexibility, while other consumer goods categories were able to offer less for the same price through 'shrinkflation'. Now distillers could achieve a 4% net price increase by moving a brand from the standard into a 720ml bottle.

Lastly, for UK, European and Japanese distillers, the new bottle sizes will be toasted with a glass or two of Scotch, Cognac or Shochu. While many of the sizes may seem somewhat random at first read, they move America into line with international standards. For over three decades 700ml had been the standard in Europe. For Shochu, it is 720ml, which harks back to the old shō system, where one shō was 1.8l, with a half shō more practical for storage and serving without a handle. The US adopted the 750ml bottle as standard when the country moved to the metric system under the Carter Administration in 1980. At the time, this was in line with the UK which had moved from a standard 26 2/3 imperial fluid ounce bottle before it later aligned with Europe in the 1990s. This standardisation could mean improved manufacturing efficiency across the industry, as the TTB motivation was in "eliminating unnecessary regulatory requirements, reducing barriers to competition and providing consumers broader purchasing options". Ironically, these changes came into effect shortly before the recent US tariffs look likely to spark a trade war.

Despite these fundamental developments, we do not expect purchasing habits to change overnight. But if Don Julio can elevate the 'mini' from the inflight drinks-trolley to the Hollywood afterparty, we expect consumer habits may follow suit. Supply chains and reporting systems will need to recalibrate but a gradual migration will have lasting benefits for the distilling industry and hopefully free up some space in the nation's drinks cabinets.

Passive Aggressive

The Relentless Rise of Index Funds

George Karamanos
Strategy

In 2024, the S&P rose 22% with earnings upgrades of 10.5%; the SXXP rose 13.8% with upgrades of 1.22%. Each enjoyed multiple expansions above 10%. The question is: does this reflect the revaluation of a vibrant economy or retail savings' allocations to listed equities?

The mantra has always been that share price movements reflect the fundamentals of a company. This may no longer be the case.

In the past, active institutional investors dominated trading flows, focusing on corporate strategy and valuation. Increasingly though, trading flows are perceived to be dominated by company-agnostic passive funds. Their stock allocation reflects the weightings of the indices or themes they are set to follow, hence a feedback loop is created behind size and performance. Stocks that outperform increase in size, attracting more passive fund flows, which extends the outperformance. Fundamentals and valuation are irrelevant.

According to FactSet, the S&P and SXXP ownership split between active and passive funds shows active investors own almost twice as much equity as passive funds in the US, and four-to-five times the amount in Europe. However, in terms of 2024 net flows, active funds dominated European stocks, and are highly relevant in the S&P.

In the US, nine out of the 21 largest stocks are dominated by passive flows: Microsoft, Apple, Broadcom, Visa, Mastercard, Walmart, Costco and, marginally, Netflix and Amazon. In ten of the 21, active investors were selling and passive funds buying.

In Europe, thirteen of the top 21 stocks saw active manager selling and passive fund buying, though only four stocks were dominated by passive flows. Europe, it seems, is more reflective of fundamentals.

Yet there is no pattern on either exchange. Instead, we need to review each stock individually to determine whether the share price reflects fundamentals or not. Therefore, we would argue almost half the largest stocks on the SPX do not reflect fundamentals as things stand.

This means the proportion of stocks owned by fundamental and valuation-agnostic investors will continue to rise, rendering price and value discovery increasingly challenging. Perhaps private markets will become the value benchmark. The private equity market is estimated to be $1.7trn in 2024, with venture capital adding $284bn. Considering the investor base of this asset class, and the often-comparable size of the companies in this space, they would appear to be more fundamentally valued.

This means the stock market cannot be relied upon to be the barometer of the economy. Rather, it is becoming a barometer of retail sentiment, considering the asset allocation preferences of younger investors has shifted from listed equities to private equity, direct investments and crypto or digital assets. Meanwhile, 24% of ETF-owning households are under 35 years old, have completed four years of college and are married or living with a partner. The majority of ETF-owning households make more than $50,000 pa and more than half own ETFs directly.

According to the 2024 Asset Management Industry factbook, $68.9trn of assets worldwide were invested in regulated open-ended funds (mutual funds, ETFs, institutional funds). Of this, $33.9trn was registered in the US, one-third invested in US corporate equity, $21.5trn in Europe and $0.7trn in Asia-Pacific.

The January release from the Asset Management Industry shows active mutual funds AuM at $15.6trn, with indexed mutual funds and ETFs at $16.2trn. Domestic US equity AuM were $7.3trn, index funds accounting for $11.5trn, while world equity AuM in active mutual funds totalled $2.4trn, $2.09trn indexed. In terms of fund flows in December, active managers saw $67bn of outflows while index funds saw $116bn of inflows. Domestic equity funds saw $49bn of net outflows for active managers versus $94bn of inflows by index funds.

Several companies are trying to move their listing to the US, in part to benefit from this trend. By doing so, however, they become captive to the whim of the retail market, the ultimate owner of passive funds, positively and negatively, regardless of fundamentals.

Historically, the market value of a listed company reflected its corporate fundamentals. No longer. Value is increasingly propelled by retail asset allocation decisions that reflect the savings capacity of households and their thematic preferences, social pressures and aspirations, rather than the specific positioning and prospects of the company.

Nothing Else Will Do

In Defence of the Tank

Joe Orchard
Aerospace & Defence Research

Detractors of the main battle tank (MBT) argue that 'this time is different'. The latest iteration of cheap anti-tank warfare – first-person view (FPV) drones – has tipped the balance of power decisively in favour of the countermeasure *du jour*.

Drones costing a few hundred bucks have supposedly created lasting economic and operational asymmetry on the battlefield. Multi-million-dollar tanks have been exposed in the wars in Ukraine and Nagorno-Karabakh, their efficacy has been thwarted. We hear similar arguments applied to other military domains – manned fighter jets versus unmanned aerial vehicles, for example. The cost of big-ticket items rises remorselessly, while the cost of countermeasures moves in the opposite direction. This debate frames much of the discussion in the US around defence spending. Elon Musk, cost-cutter-in-chief, has tweeted that tanks resemble a 'deathtrap' while fighter jets are 'obsolete'.

Armed forces face the challenge of equipping themselves for how their next war will be fought. This raises questions around spending priorities, made more acute when people ask where the money will come from in the first place. We have already seen evidence of a shift in spending priorities among NATO's European members. The organisation's lesser-known spending target states that 20% of defence expenditure should go towards major new equipment. NATO Europe has risen from 19% on equipment a decade ago to 34% in 2024. This corresponds to more than a threefold increase in absolute terms. Markets have reacted accordingly. The MSCI Europe Aerospace & Defense Index has returned 27% pa on average over the last three years versus 2% for its benchmark.

In Europe, a broader consensus has emerged looking to increase defence spending in the face of geopolitical instability and Trumpian pressure. The new NATO Secretary General, Mark Rutte, has pointed to a revised spending target 'considerably more than 3%' of GDP (currently 2%), which is likely to be enacted at NATO's June summit. But few European countries are in rude financial health. There is little room for manoeuvre. This accentuates the importance of procuring not just equipment, but the right kind of equipment.

Which brings us to tanks. If they've been fatally compromised by the onset of drone warfare, then substantial outlays on MBTs would represent a strategic and financial misstep. A recent McKinsey study concluded that European armoured vehicle stocks declined 77% from 1992 to 2022.

This trend, however, is being reversed. Several governments have placed orders for additional or upgraded MBTs – sometimes both. Austria is the latest country announcing plans to bolster its fleet. It is reportedly seeking to acquire 58 German-made Leopard 2 tanks. The price tag? €1.7bn, which equates to a smidge under €30m per tank (before you add support and maintenance costs). They don't come cheap.

MBT losses in Ukraine are not insignificant. The website Oryx records equipment losses in the war where photo or videographic evidence is available. It estimates 3,756 Russian tanks and 1,072 Ukrainian tanks have been destroyed. Ukraine's armed forces claim they have destroyed 10,000 Russian tanks. Substantial military losses tend to point to a failure in strategy rather than reveal a fatal flaw in a particular piece of equipment. Videos of successful FPV drones often identify tanks that are operating with little or no infantry support. Tanks, like all military equipment, are most effective when used as part of a combined arms package.

Last year, a NATO official suggested FPV drones had overtaken precision-guided missiles or anti-tank mines as the main destroyer of Russian tanks in Ukraine. Hit rates on the battlefield are disputed. The co-producers of the Javelin anti-tank missile, US defence contractors Lockheed Martin and RTX, promote a 94% 'engagement success rate'.

Viewing it the wrong way

Crunching the numbers on Ukraine's missile stocks versus the number of tanks destroyed suggests a far lower rate in reality – a recent Forbes article placed this between 7% and 20% for Ukraine's anti-tank missiles.

FPV drones also aren't particularly accurate. Military experts suggest it often takes between two and ten drones to destroy a tank. Their rudimentary manufacturing process inevitably means some detonate too early or not at all, while tank modifications reduce the drone hit rate further.

Nevertheless, drones retain two distinct advantages over guided missiles: range and cost. Ukrainian drones can operate from up to 10km away versus a maximum range of 2.5km for the Javelin. This means that – unlike a Javelin operator – a drone pilot does not need to have sight of his target before launching. And the differences in cost are stark. A diminishing hit rate is less of a concern when an FPV drone costs $400 compared with over $200,000 for each Javelin missile.

Yet military strategists have pencilled in the tank's obituary before. The Yom Kippur War in 1973 saw 1,000 Israeli tanks succumb to the Soviet-developed Sagger guided missile. The relatively cheap missiles rendered expensive tanks wholly ineffective. The same argument is made today.

But the evolution of warfare constitutes a series of actions and reactions. Since 1973, tanks have developed more sophisticated active protection systems – countermeasures that disrupt or eliminate an incoming threat – and enhanced defensive measures such as explosive reactive armour designed to scatter an inbound projectile. Any flaws in these systems stem from their design to counter pre-drone threats, but this does not mean they cannot be adapted or improved.

Some improvements seem more basic than others. Russian and Ukrainian tank operators have installed metal grills around the turret to trigger a drone's explosive charge early and minimise the chance of a tank's hull being penetrated. In Russia's case, however, these grills have reportedly reduced manoeuvrability and visibility. Electronic warfare has also been deployed to a much greater extent in an attempt to jam the frequency of incoming drones.

In October last year, Israeli firm Rafael announced that it had upgraded its renowned Trophy active protection system to close the vulnerability gap against drones. The company has not revealed exactly how the upgraded system works but Trophy uses sensors and radar to incorporate both electronic warfare and active interceptors to destroy incoming projectiles. Israel uses Trophy on its Merkava tanks. It also features on the US Abrams tanks and has been integrated on the UK's soon-to-be-delivered Challenger 3s. Last year, Germany unveiled its first Leopard 2 with Trophy installed. Rafael places the system's effectiveness rate at 90%.

Tank armour, meanwhile, is usually strongest at the front and sides of the vehicle to protect against the likely trajectory of incoming missiles and will need to be upgraded to withstand top-down attacks. Tanks will probably become heavier as a result and require improved mobility (the ability to transmit an engine's power). This opens opportunities for a specialist military transmission manufacturer like RENK, a German firm that presented the world's first hybrid transmission system for MBTs last year with an output up to 1,500 kW (versus a maximum of 1,300 kW for the transmission RENK builds to power the Leopard 2).

Ultimately, equipment capability, rather than vulnerability, will best define how countries rearm during the current spending cycle. A fundamental aspect of warfare is the need to capture and hold physical space. The most effective way to accomplish this on land is through the astute use of tanks (alongside other armoured vehicles) because they offer unrivalled capability – cross-country, heavily armoured, long-range firepower that can penetrate defences and provide cover for advancing forces. Future tanks will continue to offer this, and no doubt be better protected and more mobile. As an Australian general observed at a 2019 conference, "A tank is like a dinner jacket: you don't need them very often, but when you do, nothing else will do".

Weather Report

Differences Between Coffee and Cocoa

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Cocoa and coffee, two of the world's most widely consumed stimulants, have faced unprecedented supply crises in recent years, with extreme weather causing crop shortages and prices to surge to all-time highs. However, differences in value distribution, pricing power and market structure have led to varying degrees of margin pressure for chocolate and coffee manufacturers.

There are many similarities between the two commodities. Both require specific temperatures, rainfall and soil conditions, limiting their cultivation to the equatorial coffee and cocoa belt and rendering them inherently sensitive to climate change. Coffee prices soared after extreme weather events including droughts in Vietnam and erratic rainfall in Brazil, and cocoa prices spiked owing to severe droughts and excessive rain in West Africa. Cocoa's supply issues were compounded by ageing trees and pervasive crop diseases that led to acute supply shocks that tripled prices over two years. Meanwhile, coffee faced prolonged supply challenges, with Robusta prices tripling between 2020 and 2024.

The supply of both coffee and cocoa is highly concentrated. Vietnam and Brazil account for more than half of global coffee bean exports, while Côte d'Ivoire and Ghana supplied nearly 60% of global cocoa beans before the 2023-24 crop year shortage. Supply constraints in these critical producing countries, coupled with reduced market liquidity and record levels of speculation, have amplified price volatility.

A structural issue in cocoa is chronic underinvestment by farmers on account of low farmgate prices. In Côte d'Ivoire and Ghana, government-set prices protect smallholder farmers from price volatility but prevent them from benefiting when global prices surge. This limits their ability to invest in new trees, fertilisers, pesticides and irrigation, which constrains yields. Unlike cocoa, coffee faces less regulation, with no fixed farmgate prices, as it holds less economic and political significance in West Africa, and its major producing regions South America and Southeast Asia operate in liberalised markets.

As the climate warms in the coming decades, the challenges for coffee and cocoa cultivation will intensify. However, Arabica coffee, which comprised c67% of green coffee exports in 2024/25 and c63% in previous years, is particularly vulnerable to climate warming, owing to its narrow temperature tolerance (18-22°C) and need for high elevation. Rising temperatures are therefore rapidly shrinking suitable growing areas. Cocoa, although also climate-sensitive, tolerates warmer climates (18-32°C) and lower elevations. A 2019 study found that half of Mesoamerica's vulnerable coffee plantations could transition to cocoa. In Colombia, some coffee farmers have already switched, taking advantage of existing infrastructure and benefiting from the commodity's greater heat tolerance and historically stable prices. The 2024 cocoa price surge has further incentivised production in liberalised Latin American markets.

Cocoa's interchangeability helps mitigate supply risks over the long term. While West Africa remains dominant, diversification into Southeast Asia and Latin America reduces dependence on a single region. Consumer-grade cocoa (Forastero beans), which accounts for 90-95% of global production, blends seamlessly into mass-market chocolate, allowing manufacturers to shift sourcing without altering taste or reformulating recipes. Even fine-flavour cocoa remains flexible, as chocolate's heavy processing masks the subtle differences in beans. Coffee lacks this adaptability. Although Robusta is more heat-tolerant, it cannot fully replicate Arabica's distinct flavours in the specialty market. Consumer aversion to Robusta's bitterness limits blending, making coffee premiums more dependent on bean quality and scarcity. This rigidity prevents farmers from easily switching to Robusta for climate resilience without sacrificing premium pricing.

Long-term uncertainty surrounding coffee and cocoa supply and pricing remains high, as climate change and more frequent extreme weather events could drive increased price volatility. However, chocolate manufacturers are relatively less impacted thanks to greater pricing power, even amid similar commodity price inflation.

The cocoa-chocolate supply chain is long and asymmetric, with cocoa farmers receiving only 7% of a chocolate bar's retail

price. Transforming cocoa beans into chocolate involves complex processing – fermentation, roasting, grinding, conching and moulding – that is dominated by a handful of multinational firms. The top three cocoa processors, Barry Callebaut, Cargill and Olam, control over half of global cocoa grinding; six major chocolate manufacturers Mars, Mondelēz, Ferrero, Hershey, Nestlé and Lindt & Sprüngli hold a combined c60% retail share. This concentration in later stages of the value chain grants large players considerable bargaining power over millions of small farmers, leading to a gradual decoupling of chocolate prices from cocoa costs.

In contrast, the coffee supply chain is simpler and more fragmented. Farmers sell to mills or cooperatives, with green beans exported to roasters. Specialty coffee chains are even shorter, often involving direct trade between farmers and roasters, bypassing traditional intermediaries. While large roasters like Nestlé and JDE Peet's and retailers like Starbucks exist, thousands of small roasters and cafes dilute pricing power. The third-wave coffee movement emphasises traceability and quality, fostering artisanal brands. Low capital barriers and cultural resistance to homogenisation sustain this fragmentation, keeping coffee prices closely tied to green bean costs. For JDE Peet's, the world's second-largest coffee player, green beans make up over one-half of its cost of goods sold, resulting in thinner margins and greater exposure to price volatility.

While innovations like single-serve coffee pods and capsules and ready-to-drink products allow coffee roasters to premiumise and partially decouple from bean costs, the impact of this remains limited. The bulk of the market, particularly roast and ground coffee, is commoditised. Specialty coffee's premiumisation is inherently constrained, as its value is directly tied to beans. On the other hand, chocolate's versatility in shape, form and flavour enables an expansive array of products, which drive both consumption growth and a broad pricing spectrum and further reinforces its pricing power.

Coffee, coffee, everywhere

At the end-market level, chocolate benefits from strong emotional resonance and brand loyalty, providing greater protection against price sensitivity. As a treat associated with indulgence, nostalgia, festival celebrations and gifting occasions, demand for chocolate remains resilient even amid rising prices. In comparison, coffee faces more elastic demand, as daily drinkers quickly notice price hikes and can switch brands or opt for alternatives like tea or energy drinks. This distinction – chocolate as an indulgence versus coffee as a daily necessity – enables chocolate makers to pass on commodity inflation more effectively, while coffee brands are pressured to compete on price.

Both industries face slowing consumption in mature European and US markets, but their growth trajectories in emerging economies differ. For coffee, growth is led by local brands. China's Luckin Coffee has overtaken Starbucks with localised offerings. In other rapidly growing markets like Vietnam, the Philippines and Indonesia, domestic players dominate the coffee market by integrating local supply chains and catering to regional coffee cultures, limiting the presence of multinationals.

In contrast, chocolate remains dominated by global giants, thanks to their strong branding, economies of scale in distribution and manufacturing, and efficient international raw material sourcing, making it difficult for local rivals to complete. Premium chocolate, in particular, is viewed as a luxury gift for celebrations, reinforcing multinational dominance through marketing and aspirational branding.

In conclusion, while both cocoa and coffee face substantial challenges from climate change and supply chain disruption, their distinct market structures, pricing power and consumer dynamics shape their differing resilience. Chocolate's more consolidated industry and appeal as an indulgence provide a buffer against price volatility, whereas coffee's fragmented market and status as a daily necessity make it more vulnerable. As climate risks intensify, these differences will sharpen and shape their future trajectories.

Demography is Destiny

Population and Construction Materials

Harry Dow
Construction & Building Materials Research

The world's population is expected to peak by 2084 at 10.3 billion, up from 8.2 billion today. But over one in four people already lives in a country whose population is in decline, and another one in ten should see their population top out over the next 25 years.

The demographic shift is most pronounced in developed countries. The European Union's base-case forecast is for the population in the bloc to peak by 2026 before entering gradual decline.

This is compounded by a changing age composition. By 2050, the proportion of Europeans over the age of 65 will increase to around 30%, from 20% today, as a result of the continent's current sluggish birth rate.

Over recent years, natural population declines, where deaths exceed births, have been offset increasingly by higher levels of international migration into Europe. Economists argue this is necessary, at least if people expect living standards to rise further. However, political winds in Europe suggest the appetite for this is diminishing.

The results of recent European elections all point to a more hardline approach, even across mainstream parties. If we are entering a future with lower levels of migration, population declines are likely to accelerate ahead of the EU's base case.

This presents a challenge for the construction materials sector. Population and GDP growth are critical determinants of demand. More people consume more materials and higher levels of GDP generally brings increased penetration per capita too. Interest rates and policy waxes and wanes, but demographics are king when predicting long-term materials consumption.

It is striking that in Germany, Europe's largest market, deaths outpace births by over 300,000 people per year. A natural imbalance has been the case for some time but has accelerated post-COVID. Since the mid-2010s, immigration rose to levels that pushed the population back into growth and, in turn, housing completions rose to meet this new demand, reaching nearly 300,000 per year.

But we do not see the levels of migration experienced in recent years, particularly those in both 2015-17 and 2022-23 caused by migration crises, as indicative of future trends. Monthly net migration is trending much lower to levels only just offsetting the natural population decline.

With the overthrow of the Assad regime in Syria, and the potential end to war in Ukraine, the possible return of refugees to their homeland could add further downward pressure.

The result leaves us forecasting household formation, the pace at which housing need is added to each year, to almost halve compared to pre-COVID levels. This results in demand for housing recovering to a structurally lower level than previously.

Germany is not alone. Austria, Italy and Spain all also have natural population declines – albeit some, like Spain, have built backlogs of need from historical under build.

Stimulus of the size announced by the new German government can also offer a meaningful reprieve from these demographic pressures in the medium term. However, in the long run, without substantial, indefinite immigration into these countries, the demand engine of population growth is likely to fade. As a result, the materials sector will increasingly have to look elsewhere for growth.

Firstly, although volume growth of heavyside materials in developed regions such as Europe should continue to slow, prices for materials, like cement, are likely to more than compensate, advanced by themes such as the net-zero carbon transition.

A December 2024 report from the World Cement Association argued that in the most aggressive carbon-reduction scenario, global demand for grey cement clinker by 2050 could decline by as much as 50%.

While we agree some volume erosion is probable, this headline figure is unhelpful. Excluding China, declines are forecast closer to 30%, and if we assume the cement majors also capture demand in lower clinker cements, this falls further to a more modest 10% decline in volume by 2050, with demand still rising globally through to 2035.

More importantly, this fall in volume should be more than offset by increases in price. We explored cement's net-zero transition, among other sector transformational themes, in 'Metamorphoses' (July 2024), where we expected prices in Europe to rise over 40% as carbon costs ramp.

This should be accepted downstream. As prices rise across the industry, customers are generally willing to pay a premium for low-carbon cements, not least

European demographics

because cement constitutes a small proportion of overall building costs. In addition, carbon allowances create a ratchet effect, with prices rising but becoming sticky to the downside.

The cement majors, Heidelberg Materials and Holcim, with their carbon capture investments should take first-mover advantage. Heidelberg opens the world's first net-zero cement plant at the end of May 2025 at Brevik in Norway, and the great majority of carbon-neutral capacity coming online through to 2030 is from the majors.

As the EU phases out free carbon allowances starting 2026, and the carbon price rises, the cost of producing full-carbon cement will rise substantially – crucially far higher than that of producing net-zero cement.

Combined with a lower clinker content, we expect clinker capacity in Europe to rationalise as smaller players lack the capital (both monetary and knowledge) to decarbonise, improving utilisation, margins and returns across the industry.

In addition, the penetration of recycled materials, such as recycled aggregates, still offers an avenue for volume expansion in Europe, which partly offsets virgin material demand growth attrition. Holcim and Heidelberg have recognised this trend and have been aggressively expanding into this area organically and through acquisitions.

Beyond the heavyside, the lightside industry is less exposed to demographic pressures, given the benefit of increasing technology penetration. Sika is a clear example, as the use of construction chemicals increases.

In developed markets, this takes the guise of rising repair and maintenance needs of buildings and infrastructure. Globally, over 35% of bridges and 25% of roads, highways and energy infrastructure is near or past its natural lifespan. In the US, over 35% of bridges need replacement or refurbishment.

In addition, the changing age composition of developed markets can provide opportunities. As the share of seniors increases, resulting in a further lack of working age, specialised labour, products that are easy-to apply or use advanced automation should take share.

Outside Europe, consumption per capita of cement in emerging markets (excluding China), at just under 300kg by 2024, has yet to reach levels seen in developed countries. Even this level is much lower than historical peaks of now developed nations, at over 500kg.

Combined with increasing GDP per capita, we expect consumption to ride the cement 'bell curve' and continue to rise as housing and infrastructure demand grow, providing still sustainable growth in emerging markets.

In addition, the standards to which these new projects are built are also advancing. Even in developing countries, building basements can now require advanced waterproofing, with infrastructure demanding improved durability and longevity, which in turn offers further growth opportunities for the lightside industry.

While demographics are shifting, particularly in the developed world, there remain positive levers for nominal growth. However, in the future these levers will likely be increasingly more focused on price and new product penetration gains.

Credit Where it's Due

Buy Now, Pay Later

Harry Bartlett
Banks
Research

Ten years ago, if you'd mentioned buy now, pay later (BNPL), most people would have stared at you in bemusement. Now, it's a common part of the payments' vernacular, and a staple at online checkouts.

What is BNPL, why has it become so popular, and is it just a fad?

While it may seem a relatively new phenomenon, in its simplest form, the product has been around almost a hundred years. During the Great Depression, many people could not afford to pay for goods in full at the point of sale, so merchants introduced 'layaway' programmes whereby customers paid in interest-free instalments, only taking possession of the item when the balance was fully paid.

These programmes remained popular in the US until the 1980s, when the flexibility offered by increasingly popular credit cards meant most layaway programmes were discontinued owing to declining demand.

They made a comeback after the Global Financial Crisis, as many consumers struggled to access traditional forms of credit. But it wasn't until the early 2010s that BNPL arrived in the form we know today. Building on the rising popularity of e-commerce and advancements in technology, a new wave of payment companies integrated seamlessly into merchants' online checkout pages, offering a new form of credit where customers could pay for goods in simple, interest-free instalments, yet, unlike layaway schemes, the goods would be received upfront. Merchants would benefit from higher average order values and order conversion while, in return for taking the credit risk, BNPL lenders would charge merchants a fee.

Initially concentrated to a few geographies, BNPL was an immediate success. In Sweden, it became the most popular online payment method by 2019, accounting for one in four purchases. In Australia, BNPL e-commerce penetration hit 8% by 2019, within five years of Afterpay being founded.

But it wasn't until 2020 that BNPL usage exploded. Fuelled by the pandemic-induced shift from in-store purchases to online, e-commerce accelerated, and BNPL with it. Global volumes rose from $61bn in 2019 to $159bn by 2021. The US, which had been a relatively slow adopter, saw usage increase fourfold over this period, as global players aggressively expanded into the world's largest market. Valuations of BNPL companies soared, culminating with Block's purchase of Afterpay for $29bn in 2022. The future looked bright.

Yet valuations plummeted just a year later, as many investors began to question the long-term viability of the model. BNPL lenders failed to demonstrate profitability, and some smaller players fell into administration.

Central to this thesis were two concerns. Firstly, as BNPL loans are primarily interest-free, in a higher rate environment lenders would be unable to offset rising funding costs by passing them on to customers. In addition, there was an underlying belief that BNPL was a product for inferior credit quality consumers who cannot obtain credit cards, and therefore, in a more challenging macroeconomic environment, credit losses would multiply.

Both arguments have merit, but viewing BNPL purely through this lens is an oversimplification. On funding, sure, there is not the natural variable-rate offset that credit cards have in a higher rate environment. But this ignores the higher relative take rate BNPL enjoys, providing an additional buffer against fluctuations in transaction costs.

On credit, certainly, losses tend to be higher for BNPL lenders relative to credit card issuers. Yet this is not an apples-to-apples comparison.

For whatever you think about the credit quality of its users, it's hard to argue BNPL is not a superior product from the perspective of consumer indebtedness. At heart, this stems from how lenders make their money. For credit cards, almost all issuers generate the majority of their revenue from interest and late payment fees. Large initial credit limits and nominal minimum payment requirements are designed to encourage overspending and the accumulation of revolving debt. After all, the less of their outstanding balance customers pay off each month, the greater the interest and late payment fees issuers earn.

For BNPL, however, revenue is mostly derived from merchant fees. In most cases, the consumer pays nothing. With no interest charged, the incentive for lenders to develop practices resulting in higher consumer debt is removed. Unlike credit cards, customers are given clear terms and repayment plans for each transaction, and repayments are automatically taken from customers' accounts to prevent delinquencies.

P(&)L?

Moreover, if a customer fails to make a payment, their credit is frozen until repayments resume.

Highlighting the superiority of BNPL as a credit product, the Consumer Financial Protection Bureau's January 2025 study of the BNPL market found that in the same cohort of 55,000 users of both BNPL and credit cards, BNPL default rates were 2.1%, compared with 10.1% for credit cards. In other words, all else equal, BNPL results in lower defaults and a better outcome for consumers.

So, although across the broader population BNPL credit losses tend to be higher than credit cards, owing to BNPL's popularity among younger generations and the less affluent, the credit argument deserves a more nuanced discussion. Despite persistent inflation and a higher-for-longer rate environment we have not seen the spike in defaults many were expecting, and large BNPL players are achieving gross profit margins around 50%, putting them on a par with many of the best fintech businesses globally. Cost bases have been rationalised and BNPL lenders are reaching the scale where GAAP profitability has become a near-term probability rather than a long-term pipe dream.

With BNPL lenders waylaying investors' fears around the long-term viability of the business model, share prices have surged. Affirm has risen c100% from its August 2023 nadir, while Sezzle and Zip are 300% and 50% higher respectively than a year ago. And it's not just investors taking note. Large incumbent firms such as PayPal have entered the market, while credit card issuers and networks have launched their own instalment products to compete with their fintech rivals.

So, what does the future hold for BNPL? With competition growing, scale and efficiency will be critical in determining who wins. Size is important in any industry, but particularly in payments owing to the thin take rates and largely commoditised product. We have seen this play out already, with BNPL volumes increasingly concentrated among a few large players while smaller lenders have struggled to survive. These larger lenders have a head start, but whether they retain their supremacy will depend upon their ability to continue to build their brands, leverage their technological capabilities and monetise their existing customer bases.

Pulling back to take a panoramic view, while the rampant growth seen during the pandemic is unlikely to be repeated, BNPL is well placed to continue to ride on the coattails of rising e-commerce adoption. Global BNPL expenditure reached $316bn in 2023, an incredible success story from a standing start only a decade ago, but it is still only 5% of e-commerce payment. Whether it can take a larger share of online spending will depend on its ability to win customers beyond those primarily seeking a cheaper form of credit, particularly in the US credit card market where the rewards culture is so prevalent.

The most material opportunity, however, lies in the point-of-sale market, which accounts for around 85% of total commerce. Whether BNPL providers can gain traction in this largely untapped market is unknown. Either way, one thing's for sure: BNPL is here to stay.

Less About Displacing Bloomberg

The Landscape of Data and Desktops

Russell Quelch
Capital Markets Research

The three leading providers of desktop terminals and data to financial institutions, LSEG, FactSet and Bloomberg, are often pitted against each other. Hence, any mention of competitive displacements has investors fretting about shifts in market share.

Yet the suggestion growth is reliant on share gains appears naïve. Rather, we see an evolving landscape in which all three prosper by leaning into their respective strengths and embracing interoperability and generative AI (GenAI) in data and workflow solutions. By tackling longstanding inefficiencies in daily processes and data usage within financial services firms, providers can deepen and widen the total addressable market (TAM) and reshape the pricing model, leading to revenue growth upside.

Despite a strong cyclical backdrop for equity markets, debt issuance and trading volumes, most Data & Analytics stocks underperformed the market last year. This reflected structural pressures arising from customer consolidation, smaller data budgets, rising technology costs and anaemic industry headcount growth in financial services.

Passive investing remains a structural pressure for active asset management. While assets under management (AuM) in registered US mutual funds and ETFs are an all-time high, passive products have been the primary contributor. Active mutual fund AuM are below 2021 levels. Passive AuM now account for 51% of registered mutual funds and ETF AuM, from 44% in 2021.

Technological innovation is also impacting. As financial services firms replace manual processes with technology, this challenges Data & Analytics providers that sell products on a per-head basis.

In this context, GenAI is mission critical. The providers that deliver innovative GenAI solutions to help customers extract alpha and improve operating efficiencies can turn technology innovations into a huge positive.

In capital markets, real-time insights from GenAI offer tangible benefits in trading, risk management and compliance, while in investment banking they can provide unique alpha in research and financial modelling. GenAI can also help firms improve customer service and interaction. In corporate and small and medium business banking, lending and risk management are obvious areas for efficiency gains as GenAI can glean real-time insights from a large pool of structured and unstructured data.

In addition, Data & Analytics providers have other levers to pull.

Pricing has historically been an important pillar of growth. While, for obvious reasons, some providers do not disclose their annual price increases, Bloomberg announces a blanket price increase for its terminals every two years.

Bloomberg's recently announced price increase of 6.5% for 2025 and 2026 is below 2023 and 2024's 9.6% and broadly in line with US inflation on a 24-month lag. Competition limits price increases above inflation and we anticipate similar front book price increases from LSEG and FactSet in 2025.

Beyond 2025, we expect a move towards usage-based pricing. At present, most recurring products are monetised through flat-rate subscriptions. However, as providers shift towards enterprise sales and solutions that leverage GenAI, we expect subscription plus usage-based pricing increasingly to be implemented – a point endorsed by LSEG and FactSet management at their most recent investor days.

This could be a game changer, as inflation and competition will no longer limit pricing. Usage-based pricing also offers scalability, flexibility and increased retention, all of which afford margin protection.

In 'Quality Time' (May 2022), we estimated the addressable market for core data, workflow and investment solutions for financial services at $35bn. LSEG and FactSet have since corroborated our estimates.

In terms of market share, Data & Analytics providers have historically inclined towards the opaque. Today they are more direct. On the investor call last August, Michel-Alain Proch, LSEG's CFO, observed, "We are increasingly displacing other providers as Workspace becomes more powerful". At its investor day in November, Goran Skoko, FactSet's CRO, said, "We have multiple examples of displacing our main competitor [on the buy side]".

While FactSet and LSEG have high revenue retention (c95% at FactSet), a portion of the back book will churn

Data driven

annually, offering opportunities for competitive displacement. Both providers claim successes. Yet competing over 5% of the back book should not be a focus for providers or investors.

LSEG and FactSet are both investing in unifying their data models to enable the delivery of multiple datasets from a single data layer. A unified data platform helps scale providers to deliver content to customers more efficiently and cost effectively, and to cross-sell more datasets through a single application programming interface (API). We expect this to aid scale providers in accelerating enterprise-wide data contracts, leading to greater displacement of independents in markets where specialist providers have historically dominated (e.g. private markets, reference data, ESG).

Once a unified data model is established, it is easier to overlay GenAI on multiple datasets in tandem, creating a custom service linking historically siloed structured and unstructured data. This is particularly valuable where real-time data insights are critical. Leveraging a unified data platform with GenAI can generate unique alpha and increase reaction times with recommended next-best actions based on the insights.

Customer technology budgets offer opportunities for LSEG and FactSet as they are generally expanding, in contrast to data budgets which are often under pressure.

Increasing platform interoperability is essential. As providers add to their capabilities in data and workflow applications through the development of solutions, partnerships and acquisitions, and increase interoperability within customer workflows, this fuels enterprise sales discussions with CTOs. Hence, LSEG and FactSet are less reliant on peer displacements and can focus on displacing point solution providers with enterprise software in areas such as CRM systems, consensus forecasting and modelling, third-party expert network and messaging and trade execution platforms.

Expanding the TAM is essential. New client adjacencies and geographies have traditionally been the primary source of TAM expansion. While LSEG and FactSet continue to explore opportunities in areas such as corporate investor relations, PE/VC companies and emerging markets, the advent of GenAI and a focus on enterprise data agreements allow them to explore white space revenue opportunities. One such is Data-as-a-Service (DaaS), which enables providers to 'jump the wall' from being a cost to becoming a trusted source of internal operating efficiencies.

Within large financial organisations, Gen AI and large language models have been catalysts for the growing realisation that these innovations provide efficiencies in data sourcing, quality management and lineage. To leverage the benefits, firms must ensure their foundational data layer is appropriately structured.

At its CMD in December 2023, LSEG noted its financial services customers are spending £50bn in house on Data & Analytics versus £35bn on external workflow, data and feeds, and analytics solutions. Data management is a component of this in-house spending and LSEG's CEO, David Schwimmer, recently hinted this is a focus: "We have expertise, scale, and provide enormous amounts of data to our customers. Then they have to spend their own capital and human resources managing and interacting with their own data, etc. And typically, they are not operating at scale and don't have that expertise as a core competency. So, we see that as an opportunity."

LSEG and FactSet are well-positioned to access this white space. While some well-known providers including Oracle and Databricks have established solutions in the market, we suspect large financial organisations historically focused spending in this area on internal projects. According to TABB Forum, 45% of Wall Street banks plan to

'significantly increase' investment in data management technology over the next three to five years. We expect much of this to be externally focused.

Building and managing this data infrastructure can help firms to lower costs, increase innovation, reduce risk and react quicker using a more complete, shared pool of data and analysis.

By providing DaaS to help customers establish and maintain a virtual data layer and common API feeds, we expect LSEG and FactSet to increase penetration of their data and workflow solutions over time.

LSEG's growth strategy is based on enterprise data access and workflow solution contracts with large financial institutions. As customers streamline data sharing and workflow management, LSEG should benefit given its position as the number one global provider of real-time data and a top three global provider of pricing and reference data. It also has scale advantages, which affords multiple touchpoints for cross- and up-selling.

LSEG also has a co-development partnership with Microsoft. By enhancing Workspace with Microsoft Teams, Excel and PowerPoint, and overlaying this with GenAI copilots and chatbots, LSEG will help financial organisations to reduce complexity and link users across divisions and asset classes with chat, productivity tools and unique data insights. LSEG derives its revenue primarily from the sell side. We see a sizable opportunity as it leans into this client base.

Moreover, The Open Directory, alongside Workspace 365, will enable LSEG to expand into adjacent markets, leveraging brand and distribution opportunities from Microsoft.

LSEG's revenue is evenly split between the Americas and EMEA. This renders it underweight the US relative to global financial services GDP. However, by leveraging brand and distribution opportunities with Tradeweb, Microsoft and other partners (e.g. Dun & Bradstreet), LSEG can grow in US financial services, a more attractive market than low-growth EMEA.

FactSet's data and technology ecosystem remains a competitive advantage, and it has built a leading buy-side franchise. Using a similar playbook, it is growing in areas such as wealth management, investment banking, corporate investor relations, private equity and venture capital. These account for c30% of annual subscription value.

Its revenue mix is ideal. The Americas supply 65% of revenue, Asia is the fastest growing geography and EMEA is its smallest playground.

Yet despite this favourable tilt, FactSet appears more sensitive to headcount growth in financial services than LSEG. LSEG's annual subscription value (ASV) growth does not correlate with the deterioration in industry headcount growth over the past three years, whereas FactSet's seems related.

Also apparent at FactSet's November investor day was an accelerated focus on new technology to increase clients' usage of FactSet data and reliance on its workstation for decision making. Based on our view of how these technologies will reshape the Data & Analytics landscape, we believe the strategy is apposite.

FactSet's newly announced suite of GenAI offerings, designed to power the workflows of portfolio managers, wealth advisors and investment bankers, appears to offer tangible operating benefits. Product demos at the investor day were differentiated and targeted specific inefficiencies in user workflows.

While we agree with both LSEG's and FactSet's strategies and have confidence in their capacity to grow in tandem, the timing of investments and expected payout period are critical for investors. LSEG appears further through its investment cycle and at the point of earnings acceleration, while FactSet's investment journey has a way to run.

Having enjoyed a 440bp improvement in its adjusted EBITDA margin over the past three years, FactSet is guiding to no medium-term expansion and a decline in 2025. In contrast, LSEG has only seen a 30bp improvement in its adjusted EBITDA margin over the period as it increased investment to improve its data and platform offering. We forecast 100bp of margin improvement in 2025, as LSEG starts to reap the benefits of its investment.

LSEG's investment appears to be improving enterprise sales to its largest customers. In 2024, management highlighted enterprise sales to tier 1 banks including HSBC, Barclays and Standard Chartered. While FactSet's enterprise ASV has increased from 25% in 2014 to 49% in 2024 and management refers to an 'enhanced enterprise sales approach', the unit of revenue per client and per user has remained broadly unchanged since 2018.

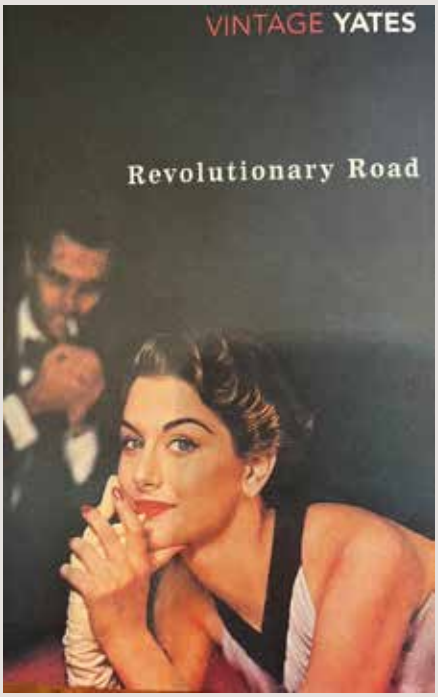
In conclusion, as GenAI solutions become mainstream, users must focus on their technology and data infrastructure. Combining once-siloed data and applications to increase interoperability and create unique alpha presents financial institutions with new opportunities to establish a competitive advantage.

For Data & Analytics providers that were once constrained in their ability to grow owing to competition and underlying structural challenges facing their addressable market, new technologies will reshape the value proposition, expand the TAM and restyle the pricing model. This will lead to fresh revenue opportunities.

Investment is required. Those providers who invest successfully ahead of these changes will enjoy accelerating earnings growth as customers adopt new technologies to improve profitability. Others will be constrained in the near term by the 'cost to get there'.

For investors, while the Data & Analytics sector will increase in its structural growth attraction, timing the run is essential to maximising returns.

Revolutionary Road (1961)



Richard Yates chose the title for his classic tale of conformity and imaginative failure "to suggest that the revolutionary road of 1776 had come to something very much like a dead end in the 1950s". The novel portrays a marriage in slow-motion collapse, its death throes picked over in sculptural detail and cold-eyed prose. Revolutionary Road is the suburban cul-de-sac where the American Dream came to die.

On the surface, Frank and April Wheeler appear to have everything. A comfortable suburban house, a well-paid job, two attractively blond children, friendly neighbours. But they have conflicting ambitions, which prove to be the fault-line in their marriage.

Frank works for Knox Business Machines in Manhattan, a clock-watching job he despises and ameliorates with long liquid lunches and a secretarial affair. Having corpsed as an actress in a local am-dram production of *The Petrified Forest* in the opening scene of the novel, April is a reluctant mother, a woman dreaming of liberation. In her mind this entails a move to Paris, the romanticised city of exiled Americans from John Singer Sargent to James Baldwin which Frank falsely claims to know, where she will work, allowing her husband to find himself and be creative. "You'll be reading and studying and taking long walks and thinking. You'll have time."

Only Frank doesn't want 'time'. Despite his self-characterisation as 'a Jean-Paul Sartre sort of man', he is in thrall to the comfort-blanket of the Knox pay cheque, much as he had been when April's first pregnancy prevented them from emigrating to the Left Bank. Frank exemplified, Yates commented, "a kind of blind, desperate clinging to safety and security at any price". For all his literary conceit and stylised disdain for the bourgeois life of the commuter, the only art Frank practices is deception.

Yates, who had a dramatist's ear for speech, brilliantly conveys Frank's self-deception through the distance between his inner monologue and spoken words. After the disastrous play he joins April in the dressing room. 'What he planned to do was to bend down and kiss her and say, "Listen: you were wonderful".' In the event, he says, with misguided and misfiring irony, "Well, I guess it wasn't exactly a triumph or anything, was it?"

Frank is a self-regarding, big-talking, moral coward. When chosen by Knox to write a series of best practice presentations for staff on topics such as 'Speaking of Inventory Control', he feigns contempt for the task. On his commute home he imagines the conversation he will have with April: "A thing like this just proves what a bunch of idiots they are," he will say, to which – in his imagination – she will admiringly respond, "I think it proves you're the kind of person who can excel at anything when you want to, or when you have to." On arrival, she proves entirely uninterested.

This is because the gap between the couple and their separate ambitions is expanding remorselessly. As the arguments increase and the ever-unfrank Frank finds excuses not to follow 'their' dream, April, eyes firmly on the horizon, succumbs to despair. Yet Frank is still unable to leap, instead imagining a conversation with her therapist in which the latter concludes, "I think your own evaluation of the difficulty is essentially correct, Mr Wheeler."

Revolutionary Road, which became a film in 2008 directed by Sam Mendes and starring Leonardo di Caprio and Kate Winslet, is a brutal, bitter – and bitterly funny – dissection of a splintering marriage which serves as a metaphor for a fading dream. It was Yates' first and finest work, his only novel in which comedy and despair maintain a perfect balance before desolation and hopelessness gained the upper hand.

A chain smoker and card-carrying alcoholic who never wrote while drunk, Yates was the realist laureate of the 'hopeless emptiness' of the 'age of anxiety'. He subsisted in cheap rooms and low-rent apartments in New York, Iowa, California, Massachusetts, Connecticut and Alabama.

Wherever he lived, his surroundings were the same: a Remington, scattering of books, cigarettes, coffee, beer and bourbon. Somewhere to sleep.

It was no way to live, but the only way he could write.

A Fair Share

Sustaining Plant Rental

Neil Tyler
Business Services Research

It occurred to me during a recent trip to North America that becoming a Business Services analyst has caused me to develop a new perspective on the world around me. I now keep an eye out for trucks distributing laundered uniforms or tackling pest problems in case a chance encounter with an employee provides insight into the business of these largely inconspicuous corporate giants. As I pass construction sites on my travels, and yearn for the promised infrastructure upgrade, I build a mental inventory of the amount and type of rented equipment being used to rebuild America. Yet although the volume and variety is, frankly, mind-boggling, and the judgement undoubtedly crude, this empirical research suggests the equipment rental industry and its three leading participants have plenty of room to grow.

Business models offering access to rather than ownership of assets have always existed but have become ubiquitous in recent years. Alongside the more obvious flagbearers in transport, holiday accommodation, office space or media, businesses which maximise asset utilisation have been growing rapidly and ever more seem to be appearing. Toolshare.co.uk allows me to monetise my own equipment fleet accumulated over two decades of (ongoing) house renovation. Libraryofthings.co.uk offers the opportunity to rent a vast array of useful items ranging from pressure washer to popcorn maker. Clearly, while asset ownership increases the need to maximise the asset's use, any model which derives a repeatable stream of revenue from an asset rather than a one-off sale should have plenty of attraction.

The current economic uncertainty is prompting investors to question the resilience of the rental business model. Despite the apparently compelling prospects for rental, share prices of the leading companies have fared poorly in the equity market rodeo accompanying President Trump's first weeks in office. As I write, the S&P500 has conceded all its post-election gains and equipment share prices have fallen between 15% and 30% this year. There is little doubt Trump's unorthodox approach to trade and international relations is impacting the short-term US economic trajectory, not least thanks to the potentially inflationary consequences of his policies. The inflation and high interest rates of the past two years have already tempered developers' appetite for investing in new building projects. But at the same time the prospect of a sustained higher cost of capital seems only to enhance the relative attractiveness of renting over ownership.

Advances in technology have been instrumental in the proliferation of the sharing economy, often by making access to the product as frictionless as possible. Although the nature of the assets means equipment rental will always require plenty of human involvement (think delivery and maintenance of a 50-tonne digger), technology has nevertheless lubricated many of the historic sticking points, particularly at the more sophisticated rental operators. Apps and ordering platforms that skilfully guide the user to the most appropriate equipment; telematics allowing rental branches to monitor the operating hours and performance of the equipment and undertake preventative maintenance or swap an asset to avoid downtime; and even simple GPS tracking that can avoid a driver having to scour a vast construction site to collect the correct piece of equipment. Since many of these insights are available to the rental customer, contractors can hone their operating costs by keeping tabs on how efficiently their rental budget is deployed.

Technological progress and equipment innovation offer a motivation to rent. Rather than buying now and risking obsolescence, why not rent the latest and most efficient model, leaving open the option to upgrade as technology progresses. The thought process is analogous to that of a friend who postponed replacing his recently sold car with an electric vehicle in anticipation of ranges improving – only to find his interim solution combining Uber and Zipcar provided greater flexibility at lower cost. Indeed, the rapid progress in battery electric and solar power is translating into rental demand in these categories. Picture a temporary solar farm that fits on the back of a truck, unfolds to the size of a football pitch and delivers enough power to support an entire building site. If that site is remote (and sunny) this solution or something similar solves the

problem of having to transport fuel constantly to run generators, but can also provide power to the completed building if grid connection is delayed or prohibitively expensive.

When I have dabbled in my 'digger spotting' hobby back in the UK, the pastime has been slightly underwhelming. Not only do my anecdotes back up more empirical research that the UK rental market is both more fragmented and less complex than in the US, but the machinery itself is, in general, much less impressive. Like so many aspects of life in the US, construction operates at a different scale. The machinery reflects that scale. Moreover, the average project size in the US non-residential construction market is growing. Projects with a total value over $400m accounted for more than 20% of the total value of projects breaking ground over the past twelve months from 15% five years ago. As construction projects grow in size and capture world-scale facilities in new industries, the wider range of equipment and ability for a customer to keep track of their rented inventory places even greater reliance on technology to manage this complexity.

Currently, around 55% of construction equipment sold in the US ends up in the hands of rental companies, the remainder being bought by builders and contractors for their own use. The penetration of rental has grown steadily from less than 40% twenty years ago, but this is prompting some to question the scope for continued progress. Against this concern we see a world in which the cost of capital (and thus asset ownership) has risen sharply. We also see projects which are larger and more complex and equipment which is ever more role-specific. These two influences combine to make it less likely contractors will want to invest in their own equipment in case the next contract fails to materialise or requires different assets.

A capital idea

Within the 55% average rental penetration, the range varies widely. Some types of equipment are almost exclusively rented. At the lowest end of the penetration range, however, sit the long and growing list of items bracketed under the 'specialty rental' umbrella. These tend to be used by customers to support operations rather than to undertake them. It follows therefore that those customers should be even less inclined to own, store and maintain that equipment, provided they can be confident it will be available when and where they need it. And since the specialty customer is less likely to be familiar with the equipment, providing installation and ongoing support adds extra revenue to the initial rental sale.

Proponents of the sharing economy will be aware of the environmental benefits of businesses making more efficient use of underutilised assets. Better utilisation means fewer of these assets will need to be produced, and the embedded CO_2 within each could be spread across its workload. The European Rental Association's Life Cycle Assessment tool estimates that one of Ashtead's rented mini-diggers replaces the need for ten owned assets. By extension, using the company's fleet of 11,000 mini diggers to replace owned assets would save the equivalent annual CO_2 emissions of taking 77,000 passenger cars off the road. Multiply these savings across the different types of equipment and across the remaining 85% of the rental industry, and the potential environmental benefits of relying on rented assets can be huge.

Logically, these lower emissions can then accrue at least partly to the building constructed. Although still a tiny minority, examples exist of building owners and developers pushing for the use of rented equipment during construction as a means of lowering its carbon footprint and thus that of their organisation. Priorities such as these seem likely to grow in importance in boardrooms, irrespective of the environmental agnosticism of the current US administration.

So next time you're stuck in traffic through the endless M4 motorway upgrade or, more optimistically, making your way into a music festival this summer, why not try making a mental note of the volume and variety of equipment on show, and find out who it belongs to?

Pressure Drop

The US Gulf of Mexico in Focus

Sebastian Erskine
Oil & Gas Research

Amid the flurry of executive orders that followed Donald Trump's return to the White House in January, one in particular captured the interest of netizens and pundits alike. This was executive order 14,172 ('Restoring Names That Honour American Greatness') to rename the Gulf of Mexico as the 'Gulf of America', reflecting the 'pivotal' role it played in the national security and economic prosperity of the US. Overnight, this body of water, bounded by the US, Mexico and Cuba, transformed into a political football, pitting compliant corporates, including BP and Chevron, against journalists and foreign leaders. While Mexico's President Claudia Sheinbaum joked about renaming North America 'Mexicana Americana', Associated Press reporters have been barred from White House press briefings over the agency's refusal to accept the change in name.

Nomenclature aside, however, this body of water is a source of genuine excitement for the oil and gas industry. This is an impressive feat given both the US Gulf of Mexico's status as a mature basin and the extent of frontier development in today's buoyant offshore market, spanning Suriname, Namibia, East Africa (Mozambique and Tanzania) and, most recently, Colombia, following Petrobras' Sirius discovery. The industry's renewed focus on the region is because, thanks to innovation, reservoirs in the frontier Paleogene (or Wilcox) play, spanning the central and western regions of the US Gulf, are, after many years of dormancy, finally being unlocked for commercial development. Investors need to cast their minds back to the late 2000s and early 2010s when the Paleogene play was last *en vogue*.

BP proved an important early player, announcing the discoveries of Kaskida (275 mboe) in May 2006 in a water depth of c1.8km, Tiber (238 mboe) in August 2009 in a water depth of c.1.3km, and Gila (75 mboe) in December 2013 in a water depth of c1.5km. However, from a developer's perspective, there are unique challenges presented by the Paleogene play. These include the depths of reservoirs, ultra-high pressures (more than 15,000 psi) and temperatures (above 350°F). In order to extract hydrocarbons from a deepwater well with shut-in pressures greater than 15,000 psi, you need subsea production systems (SPS) capable of withstanding these conditions across the entire development (i.e. drilling, installation, production etc) value chain.

As a testament to these complexities, BP announced the formation of an alliance with Chevron and ConocoPhillips in January 2015. Under the agreement, BP opted to sell around half its equity interests in Gila and Tiber to Chevron, while the trio agreed to joint ownership in the Gibson exploration blocks, east of Gila. The aim of this was to pool the technical strengths and balance sheets of the three companies in order to reach final investment decisions (FIDs) on Gila, Gibson, Guadalupe and Tiber, which together were known as Tigris. Chevron was viewed as an obvious partner, in light of its success in jointly bringing the Jack (268 mboe) and St. Malo (454 mboe) fields in the Paleogene to production in December 2014, following discovery in 2004 and 2003 respectively and sanctioning in October 2010. Chevron had also made a discovery at Guadalupe (149 mboe) in December 2014 in a water depth of c1.2km.

However, early momentum behind the Paleogene was scuppered by the US shale boom and the severe 2014-16 oil price crisis, in which Brent lost c70% of its value. E&Ps opted to cut costs and to review their exploration & appraisal (E&A) activities. Indeed, the consortium BP announced in 2015 changed, with ConocoPhillips withdrawing as part of a wider deepwater exit, and Petrobras and Venari Resources dropping their smaller stakes. Moreover, in September 2018, Chevron announced it would not be pursuing the Tigris project, opting instead to focus on its Anchor discovery (441 mboe) in the Paleogene. With this, it decided to exit its operated share of the Tiber and Guadalupe discoveries. While BP opted to press on with Tigris, Chevron's exit represented something of a nadir in the US Gulf of Mexico's Paleogene story.

The arrival of commercially viable 20k psi SPS technology has precipitated a step-change in activity, supported by a broader recovery in

the offshore cycle since the depths of the pandemic in 2020. The first deepwater project to deploy 20k psi technology was Chevron's Anchor, which was discovered in December 2014 in a water depth of c1.6km. The technology deployed was the product of a joint industry programme started in June 2015 between Chevron and the OneSubsea business, which was formed in 2012 by Cameron International and Schlumberger (SLB). OneSubsea has since been fully consolidated into SLB, which owns a 70% equity stake, with listed European oilfield services (OFS) groups Aker Solutions and Subsea 7 holding 20% and 10% respectively. Anchor reached FID in December 2019 following a detailed and prolonged front-end engineering and design stage and commenced production in August 2024 via a semi-submersible floating production unit (FPU), with a design capacity of c75 kbpd of oil and 28 mcf/d of gas. This was an industry first and, with the 15k psi SPS threshold finally crossed, has set the stage for further important developments in previously inaccessible reservoirs. Wood Mackenzie estimates new high-pressure, high-temperature technology could unlock in excess of 2 mboe of resources in the US Gulf.

As such, Anchor has been followed by a slew of recent Paleogene discovery FIDs. In December 2023, Shell reached FID on its Sparta discovery (240 mboe) and, in order to optimise costs, chose a FPU design at 90 kbpd that closely replicated its earlier 100 kbpd Vito and Whale projects. Shell is the largest operator in the US Gulf and, in addition to replication, is pursuing innovation through its remote start-up of offshore facilities. Vito and Whale both commenced production from a control room in Louisiana, and Sparta is expected to do the same in 2028. BP reached FID on Kaskida in July 2024, creating a sixth production hub for the operator in the region alongside Argos, Atlantis, Mad Dog, Na Kika, and Thunder Horse. BP opted for a floating production platform with a design capacity of 80 kbpd, and the group is targeting first oil in 2029. Outside the majors, Beacon Offshore, which was formed by Blackstone Energy Partners in 2016, reached FID on its Shenandoah development (378 mboe) in August 2021. The field will be produced using a 120 kbpd semi-submersible FPU, with first oil targeted for the second quarter of this year.

Up and away

As an oil services analyst, the commercialisation of the Paleogene is music to my ears. Following a developer taking FID on a project, engineering, procurement, construction and installation (EPCI) contracts will be awarded, usually immediately. An obvious beneficiary of activity in the Paleogene is US-listed OFS group TechnipFMC, who, in 2024, secured $500-1,000m in integrated EPCI awards for both Sparta and Kaskida, where standardised (through the group's Subsea 2.0 configure-to-order offering) 20k psi subsea trees will be deployed. CEO Doug Pferdehirt has, on recent earnings calls, been keen to stress it represents a critical growth engine for the business and the wider industry, alongside more high-profile frontier basins. Paleogene projects mooted for development in the coming years include BP's Tiber, Guadalupe and Kaskida's West Bump, Shell's Leopard (153 mboe), and LLOG Exploration's Blacktip (120 mboe).

The broader point here is that in light of the fading role of shale in the global liquids supply mix and the need to offset decline rates, innovation in deepwater hydrocarbon development can unlock new reservoirs in well-understood, mature basins. The Paleogene is perhaps the most prominent example.

Who Needs Politicians?

How Spain Conquered Europe

Gonzalo López
Banks & FinTech Research

For years, Spain has been recognised for its dominance in sports. It is known for its European and World Cup champions in football, tennis legends like Rafael Nadal, and golf icons such as Seve Ballesteros and, more recently, Jon Rahm. But few predicted Spain would also emerge as one of the fastest-growing economies in Europe. Its transformation is hugely impressive considering the severe economic struggles it faced in the aftermath of the Global Financial Crisis in 2008 and European sovereign debt crisis. As a banking analyst, I have been particularly struck by its turnaround, and this essay examines the origins of Spain's resurgence and its long-term sustainability.

The country's performance in 2024 defied expectations. Its economy grew 3.2%, double the forecast at the beginning of the year. This followed a solid 2.7% expansion in 2023 and materially outpaced the 0.8% growth recorded across the eurozone. Even more surprising is the contrast with the other major European economies. While Spain surged ahead, Germany contracted 0.2%, France managed a 1.1% increase, Italy grew a paltry 0.5% and the UK expanded 0.9%. Spain alone accounted for 40% of the eurozone's growth in 2024, cementing its position as the fastest-growing major economy in the region.

This remarkable performance followed years of economic difficulty. Spain and its banking sector were severely affected by the 2008 financial crisis, owing to its overexposure to risky assets, the collapse of the housing bubble, and its undercapitalised financial system. The economy then suffered another devastating blow in 2020, when the COVID-19 pandemic led to an 11% contraction in GDP. The near-total shutdown of its vital tourism sector, which accounts for almost 13% of the economy, exacerbated the downturn.

A major factor behind Spain's resurgence has been its ability to utilise strengths beyond its traditional reliance on tourism and the real estate construction tied to it. While the country received a record 94 million visitors in 2024 – competing closely with France, which welcomed 100 million – it has also made big strides in sectors such as Financial Services and Technology, which might have seemed unthinkable not long ago. This diversification allowed Spain to withstand external shocks that might have otherwise destabilised its economy.

The Services sector has been a critical engine of Spain's growth. Unlike traditional industrial economies, Spain's is more reliant on services than manufacturing. This structural difference has rendered it less susceptible to the slowdown that is affecting the eurozone's manufacturing sector. With a strong tourism industry and thriving services sector, Spain has been able to sustain economic growth, while other countries have been grappling with declining industrial output.

Furthermore, Spain's relatively lower energy costs compared with other major eurozone economies afford it a major economic advantage. This is the result of the country's focus on renewable energy and its reduced dependence on Russian gas, which helped to shield it from the energy price volatility many European nations have experienced. Spain has the second-largest renewable energy infrastructure in the EU.

Spain, indeed the Iberian Peninsula, benefits from a common energy market that prioritises renewables, diversifying its energy sources and reducing reliance on imported fossil fuels. As a result, Spanish businesses and households enjoy more predictable and affordable energy expenses.

Despite the positive trends, one of Spain's long-standing economic challenges is its intractable unemployment rate, which remains the highest in the EU and is almost double the bloc's average. This has cast a long shadow over the country's economic progress for some years. However, there are signs of improvement, as in the final quarter of 2024, it fell to 10.6%, marking the lowest level since 2008.

Another factor contributing to Spain's economic success and the improvement in employment is its demographic advantage, which is fuelled by strong immigration. In 2022, Spain recorded its highest net immigration in over a decade, with c750,000 people arriving. Since then, migration flows have remained robust, particularly from Latin American countries such as Colombia, Peru and Venezuela. This inflow of workers has been a major contributor to Spain's superior economic performance, especially compared with countries such as Germany and France, which are grappling with demographic challenges and shrinking labour forces. It is noteworthy that 30% of the new jobs created in the eurozone in 2024 were in Spain, a country

representing 10% of the zone's GDP and c13% of the population.

The Spanish economy benefits from several advantages in the context of immigration. Cultural and linguistic ties with Latin American countries facilitate the integration of migrants, allowing them to assimilate more quickly into Spanish society and the workforce. Additionally, recent waves of immigration have included individuals with higher education levels, such as professionals in medicine, engineering and skilled trades – fields that are in high demand. Spain's relatively open immigration policies have substantially increased its working-age population, which has grown 4% since 2019 – nearly double the rate of other major European economies.

Additionally, the country stands to benefit from cyclical productivity gains as its economy continues to expand. Productivity improvements, propelled by advancements in technology, labour efficiency and infrastructure investment, will accelerate economic growth.

Clearly, then, Spain's economic outlook appears strong. In addition to its historical strength in hospitality and tourism, it is supported by steady immigration, lower energy costs, productivity gains and resilient consumer demand, which combined create a favourable environment for sustained growth. Additionally, lower interest rates from the European Central Bank will probably affect Spain more rapidly than other countries, given the country's greater exposure to variable-rate loans, particularly in the mortgage sector. As a result, reduced debt burdens, increased disposable income and stronger purchasing power should boost both private consumption and investment.

The fall-out from the new Trump administration in the US is another important factor. His stance on immigration could encourage Latin Americans to migrate to Spain rather than to head northwards, providing a further boost to the country's demographic and economic opportunities.

The positive momentum on Spain's economic front stands in bleak contrast to the ongoing turmoil in its politics. Corruption investigations involving the Spanish prime minister are intensifying, reaching boiling point at a crucial moment for his already-fragile government. With the ruling coalition relying on a wide array of parties, including Catalan and Basque nationalists, to stay in power, the government's stability and longevity is in question.

In light of Spain's deeply polarised politics, it has become increasingly difficult for Pedro Sánchez's minority government to push through legislation or secure approval for a budget for the remaining three years of his prime ministership. Ironically, however, the political stasis may be contributing to Spain's economic resilience as, without constant changes and disruptions caused by new policies, the economy has been able to proceed without interruption and to focus on its many structural strengths.

As long as these advantages endure, the need for political intervention diminishes, allowing Spain to thrive despite – and because of – its ongoing political challenges. The interplay of political inertia and economic momentum characterises Spain's unusual position, one where the absence of legislative activity has not hindered its economic progress.

Animal spirits

Chronicle of a Death Foretold

Fall and Rise of the Bookseller

Archie Cotterell
Editor

A couple of weeks ago I was on a packed train heading west. Out of curiosity, I walked its length to see how many passengers were reading books. The answer was six, though several more might have been reading on phones or iPads, it wasn't possible to tell if the content was long form. Conversely, the number watching films, playing games, texting friends, reading the news, shopping online, scrolling social media or sleeping was, broadly, the rest. The death of the book and, by extension, the bookseller, has long been predicted.

It is not hard to fathom why. Since the arrival of Amazon with its deep discounts and Kindle, book retailers have been on the back foot. This has been compounded by the hours consumers spend online and the attention deficit that ensues, the introduction of Netflix and streaming platforms, the end of the Net Book Agreement, which protected pricing, publishers going out of business, and the collapse of the high street and attendant footfall. When Borders closed its doors in September 2011, and with Waterstones in a doom loop of declining sales and shuttered shops, the writing, as they say in the book trade, was on the wall.

Fast-forward to 2024 and Waterstones, the UK's biggest bookseller which includes Hatchards, Foyles, Blackwell's and Hodges Figgis in Dublin, has announced revenues up 17% to £528m and profits rising £20m to £32.8m. There is talk of an IPO. Elliott Investment Management, the fund that bought a majority stake in 2018, added Barnes & Noble, the largest bookseller in the US, to its portfolio the following year. Waterstones opened twelve new stores in the UK in 2024, including in such apparently unpromising locations as Newport (Gwent) and Grimsby, while Barnes & Noble opened 57 in the US. Both plan similar levels this year.

It is not just Waterstones. In the urban village in which I live there is a Waterstones, Heron Books, an independent currently expanding into larger premises, Oxfam Books and a large second-hand bookshop, lights ablaze each evening with poetry readings, book talks and local interest events.

How has it happened? As the high street withers under the twin assault of online shopping and the egregious imbalance of bricks n' mortar business rates, how have booksellers, those in the eye of Amazon's original hurricane, prospered? And this in a market in which – judging by my train survey – few people still read?

The answer, in two words, is James Daunt. In 1990, having chucked in his job at JP Morgan, the 26-year-old opened his eponymous bookshop in Marylebone High Street. Daunt Books offered a distinct retail experience, long on customer enjoyment and service, short on process. The space became legendary, with its Edwardian gallery and ecclesiastical calm, a temple of books.

By the time Daunt was headhunted in 2011 by Alexander Mamut, the Russian oligarch who had recently bought Waterstones, he had expanded his empire to six shops in affluent suburbs such as Hampstead and Holland Park. And bookselling was in freefall.

At Waterstones, Daunt made one seismic change. He decentralised buying, allowing the individual stores' booksellers to decide which and how many titles they stocked. Not only did this empower and encourage local management, it ensured each shop was unique, and catering for its local market. "I hate homogeneity," he said, "the idea is that each time you are creating a bookshop for the community." This was the chain recast as independent.

A corollary of Daunt's decision was he severed relationships with publishers. There were no more HQ-led in-store promotions, which had raised £27m pa, no three-for-two offers. The benefits flowed. By focusing obsessively on the interests and buying habits of customers of specific locales, there were fewer returns to publishers, improved stock management metrics, each store felt individual, process was eliminated, the consumer experience enhanced.

Critically, this decision ensured every Waterstones' employee was a booklover. This was intrinsic to Daunt's vision. "I require my bookshops to be run by booksellers. If you are not interested in books, and you don't read or you don't care then work somewhere else." There were also external benefits

he identified and leveraged. Whereas most retailers appeal to a specific demographic, bookshops' potential market includes pretty much everyone. Then there are the ancillaries, a cup of coffee, Harry Potter puzzle, or Christmas card. They are also less exposed to inflation. Even post the demise of the Net Book Agreement, publishers set the price for the product – a product which has remained extremely good value. When James Daunt founded his eponymous store in 1990, a paperback was £6; it is now £8.99. There are not many products which offer six hours or more's pleasure for not much more than the price of a pint in central London.

Further structural benefits include the fact books are aspirational – most parents would like their children to read – and they don't have a sell-by date. In the case of some, the reverse. John Williams' *Stoner* was published in 1965 and sold barely two thousand copies. In the mid-2000s it was reissued and championed by celebrated novelists including Ian McEwan and Julian Barnes and sold over six hundred thousand. Other books, for example Patricia Highsmith's *The Talented Mr Ripley* (novel 1955, film 1999, Netflix series 2024) have been brought to new audiences through the big and small screen, rekindling interest in an author's work and footfall across bookshops.

One unpredictable benefit was COVID. Sales rose 77% across 2020-22. The sheer length of downtime encouraged many adults to read again, while an artfully placed, carefully curated bookcase became a must-have on Zoom.

Then there were incrementals, innovations which individually altered little but in sum helped to change the weather. There was the introduction of in-store cafés, reading areas, card displays, book launches and author events. Daunt understood that as the high street declined there was a benefit to being the most appealing experience on it.

A thirst for reading

That is why you can find profitable Waterstones in Grimsby and Middlesborough, towns that have lost their M&S and Next but where the bookseller continues "to curate a sensible array of books".

With the industry facing a near-death experience it began to pull together. Publishers plugged audiobooks, spin-off toys and calendars and puzzles, graphic novels, collectible editions. Literary festivals exploded. BookTok was embraced, the mid-list concertinaed. Shorter books for shorter attention spans were published. Event launches such as Prince Harry's *Spare* were seized upon. Genre fiction was pushed, book clubs encouraged, podcasts adapted, influencers promoted.

James Daunt's success, and vision for what a bookshop is and could be, led Elliott to install him as CEO of Barnes & Noble (while remaining CEO of Waterstones) after it bought the US chain in 2019. But although his Midas touch appears to have crossed the pond, the industry continues to face enormous challenges.

The most obvious is from AI. No one knows where it will go or how the creative industries will survive novels, films, paintings being devoured, or rewritten, rescripted or reimagined 'in the style of' or 'with extra…' For artists and publishers, the risk is existential, for retailers scarcely less so.

The second risk, evidenced by my train journey nano-sample, is a diminution in enthusiasm for books. The National Literacy Trust's recent survey makes unhappy reading. In the UK, two-thirds of eight-to-eighteen-year-olds 'do not enjoy reading' and do not 'read for pleasure'. Whether this results from or supports the defunding of libraries is moot. It is clear however that screens in all their forms, in their easy gift, must shoulder a considerable part of the blame.

But booksellers and publishers have one incredibly powerful weapon in their armoury: their product. If your product is a story, whether fiction or non-fiction (it is hard to know which is more freighted), there will always be demand. Because human beings are programmed to love stories. We need to find out how they end. Stories give shape to the unknown or uncertain. It is why we read to our children at night.

Build Your Dreams

The Chinese Auto Industry

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The China-based organisations within the Western-listed automotive original equipment manufacturers (OEMs) began to become problematic three-to-five years ago. Volumes in the country have fallen, and the starting point for industrial profits was higher than the group average. Light vehicle factory capacity in the West is also too high relative to current demand – retail volumes in Europe and North America are three million units below 2019 levels in aggregate – so the export channel eventually steals from Peter to pay Paul. This essay explores the automobile industry in China and explains why its fortunes changed.

In 1985, China's population had breached one billion and about five thousand light vehicles were produced locally. This was but a rounding error in the then global total of about 45 million units pa. Four decades on, China claims responsibility for one in three of the light vehicles produced each year. Its annual output of thirty million units roughly equates to the sum of the next five most productive countries (the US, Japan, India, Germany and South Korea). Moreover, sources indicate plant capacity in China totals 45 million units, equivalent to half the number of light vehicles sold worldwide in 2024.

The historical opportunity presented by China was clear: light vehicle sales (LVS) had stagnated in developed markets (US, Western Europe, Japan), vehicle ownership per capita in China was relatively low (one car per thousand people, versus c700 and c300 in the US and Germany respectively), and China's focus had shifted from political to economic issues following the death of Chairman Mao.

The two determinants of demand for light vehicles in any country are: (1) vehicle price relative to household disposable income; and (2) credit availability. China's LVS growth derived mostly from the former.

In 1979, the Joint Venture (JV) Law of the People's Republic of China Using Chinese and Foreign Investment was enacted. This offered, for the first time, a framework for foreign companies and investors seeking to do business in the country. American Motors, now buried within Stellantis, was the first Western OEM to establish a Chinese JV. It formed the Beijing Jeep Corporation in 1983 with Beijing Automotive Works. Shortly afterwards, Volkswagen laid its foundations in Shanghai.

In 1994, the Automotive sector was designated a 'Pillar Industry' of modern China, one of a handful intended to improve the national economy. It is easy to see why: light vehicles have thousands of subcomponents, and profitable local production requires coordinated expertise in metallurgy, petrochemicals, electronics and textiles, among others. The related government policy contained a demanding schedule for the sector's development. By 2000, annual light vehicle production should be circa three million units and only two or three large scale OEMs should exist. Enter Dongfeng, First Automobile Works (FAW), and Shanghai Automotive Industrial Corporation (SAIC). By 2010, China should be self-sufficient in product development, be internationally competitive, and manufacture at least six million units annually.

To abet, the policy codified a requirement for foreign automakers to establish JVs with domestic partners in order to undertake business in the country, restricted their ownership to no more than 50% and prescribed a local content rate. The rationale was obvious: it enabled the transfer of critical knowledge from West to East. International JVs became the backbone of the Chinese automotive industry, which explains the shape of the industry today even if they are no longer a requirement. The Stanford Centre on China's Economy and Institutions argues most wisdom accumulated upstream from the OEMs, because the JVs held domestic suppliers to a higher standard than their local counterparts.

China's entrance into the World Trade Organisation accelerated the development of its automotive industry. Annual light vehicle production and retail volumes grew on average 15% from 1994 to 2002, and 116% over the next three years to five million units.

In 2004, a new automotive industrial policy was released. It encouraged the development of so-called 'new energy' vehicles – hybrid and all-electric propulsion – which served as the basis for today's industry. At this point, the only all-electric vehicles were niche experiments by brands like General Motors or Toyota and were discontinued after a few years.

The one in the middle, please

Western OEMs were rewarded through most of China's ascendancy. Chinese consumers preferred their premium brands and relatively higher quality. Vehicle sales earnt above-average profitability because production costs, particularly labour, were lower and designs were bought-in – other parts of the organisation had already paid for the R&D. This is the setup of Renault's Dacia today, albeit based in Eastern Europe.

However, in recent years, foreign automakers were caught flat-footed by China's abrupt shift to electromobility, a switch catalysed by additional policy in 2017. The New Energy Vehicle mandate set annual targets for the electrified portion of manufacturers volumes and was complemented by other programmes dealing with charging infrastructure.

Ford no longer reports its financial results by region, but we estimate the cumulative operating loss in China over the past few years is in the order of billions of dollars. At a summit in 2024, CEO Jim Farley, commenting on this, admitted, "We (Ford) have never seen competition like this before".

Over fifteen years, China grew to be as important as Europe to Porsche (the manufacturing entity) with retail volumes comprising about one-third of the group. The country's relative and absolute contribution has since halved, roughly. Porsche announced last year its distribution network in China would be downsized meaningfully, which tells its own story.

General Motors and SAIC are restructuring their JV to address market challenges, which has decimated income. The Detroit automaker anticipates related cash and non-cash costs to total $5bn, or about 10% of consolidated revenues, and involves shuttering plants.

Meanwhile, the volumes of China's BYD have skyrocketed. In 2017 it sold about four hundred thousand vehicles; in 2024 that figure exceeded four million, mostly with 'new energy' propulsion systems. The increase in the value of its equity has been similarly dramatic (up 600%).

After decades of generous government subsidies, tax breaks, procurement contracts and other policy incentives, a slew of homegrown automotive brands with high degrees of vertical integration have emerged. The product from Western OEMs no longer has superior quality, particularly in lower-cost segments, so in a markedly softer economy consumers have rightly questioned their comparatively higher sticker prices.

Software is the new king of differentiation, and the Chinese equip their cars with some of the world's most advanced digital cockpit features. This creates human capital challenges for traditional manufacturers. Indeed, at the 2024 Redburn Atlantic CEO Conference Rivian Founder and CEO Dr Robert Scaringe shared that the way the 'old' OEMs interact with their suppliers often means they are disconnected from the creation of technologies. As automotive analysts, we now monitor technology giants like Xiaomi and Huawei which entered the game last year and have been successful.

Volkswagen identified its product problem in 2023 and purchased a minority stake in XPeng, a Guangzhou-based all-electric start-up automaker. The idea is to build upon XPeng's in-house software and hardware, to which the investment granted access, for the next generation of its product in China. The country has represented 35-40% of Volkswagen's unconsolidated retail volumes since 2015, so exiting the market is not an attractive option.

GlobalData forecasts European brands (including JVs and associates) will not recover market share lost to Chinese brands by the end of this decade, and that Nissan, Honda and Toyota may incur further losses. In 2023, Elon Musk opined that the top ten automakers of the future would be Tesla, followed by nine Chinese ones. It is hard to argue against them.

Risk and Reward

Understanding Litigation Financing

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We have all heard the phrase, "cases stuck in the courts", but for many well-funded defendants, litigation fatigue is more than just a delay, it is a deliberate strategy. By filing motions, postponing court hearings and launching counterclaims, defendants extend legal proceedings in the hope the plaintiff will exhaust their financial resources and either abandon the case or settle for a lower amount.

Traditionally, legal expenses were the exclusive burden of plaintiffs, but increasingly investors across the globe are looking to fund litigation claims. 'Litigation financing' is an arrangement whereby a third party, usually a private investor or financial firm, agrees to cover the legal costs associated with a claim in exchange for a share of the proceeds if the claim is successful. This 'market', which is analogous to 'ambulance chasing' solicitors taking on personal injury cases in return for a share of the proceeds, has gained traction as both plaintiffs and investors recognise the potential benefits in a landscape that increasingly prioritises access to justice and financial returns.

In recent years, litigation finance has evolved from a niche sector to a major force, one reshaping how legal battles are fought and financed. Litigation funders, who provide capital upfront, are estimated to have over $15.2bn in assets under management globally.

For investors, litigation finance presents an intriguing opportunity. As an alternative asset class, it allows them to diversify portfolios and access potentially high returns tied to complex, often multi-million-dollar legal cases. Unlike traditional investments, which may be subject to market fluctuations and largely correlate to economic conditions, litigation finance offers an entirely uncorrelated opportunity. It delivers a binary outcome: high-risk, but potentially hugely rewarding.

One of the engines of growth in litigation finance is the rise of 'nuclear' verdicts, the extremely large jury awards that have become increasingly common in court cases and typically involving claims above $10m. However, in some instances they can escalate into the hundreds of millions, particularly where they relate to personal injury, product liability or commercial disputes.

The impact of litigation financing has wide-reaching implications, not only for the plaintiffs and their legal teams, but also investors and industries increasingly exposed to legal risk.

For corporations, the rise of nuclear verdicts has required them to reassess their approach to risk management and litigation. These large jury awards have the potential to destabilise companies financially, influence industry practices and shape broader legal trends.

For insurers, litigation finance is both a challenge and an opportunity. Positively, it may alleviate some of the pressure on insurance companies by ensuring claimants or defendants have the resources to pursue or defend high-stakes cases, which might have otherwise fallen under the insurer's policy. Less constructively, it can increase losses, adding a layer of complexity to pricing. The increasing frequency and size of nuclear verdicts, particularly in high-risk industries like trucking, healthcare and manufacturing, are making it more difficult for insurers to price risk accurately.

As the frequency and value of legal claims continue to increase, insurers are faced with the challenge of recalibrating their pricing models to reflect the changing landscape. In response, many are raising the price of premiums, tightening coverage terms or, in some cases, simply withdrawing cover in high-exposure markets.

Technology, as always, will play a major role. Legal tech companies are developing sophisticated algorithms to predict case outcomes based on historical case data, court rulings and precedent. These new data analytics tools and platforms will help investors assess the merits of legal claims, improving the overall due diligence in deciding which cases are worth investing in and, ultimately, improving the overall risk/return profile.

Some institutions are increasing their exposure to this asset class, recognising the diversification potential it can offer to investment portfolios given its minimal correlation with financial markets. If the market continues to mature, it is likely institutional investors will bring additional liquidity and sophistication to the sector, further legitimising it as a conventional investment vehicle. With more institutional capital entering the space, we are almost certain to see further innovation in the way legal

Also investors

cases are financed. For example, new funding structures, such as the securitisation of litigation claims, could provide even more liquidity for investors, allowing them to pool funds across a wider variety of cases and legal sectors.

Litigation finance has the power to alter the legal landscape dramatically. Opinions over the ethics of investor involvement are likely to differ. Some will view it as a way of widening access to justice. For individuals who cannot afford to pursue their legal rights, third-party funding provides an avenue to seek compensation without bearing the financial burden of litigation. Similarly, businesses that might otherwise settle out of court owing to the prohibitive costs of a legal defence can pursue litigation knowing they have financial backing.

Conversely, others will argue that expanding access to finance could have negative consequences for the wider ecosystem. While they note third-party financing will enable some underfunded companies to face legal challenges head on in the reasonable pursuit of justice, it will inevitably lead to an increase in the frequency of costly lawsuits. The growing number of funded claims places additional pressure on industries, insurers and the courts, which could result in more cautious management strategies and potentially stifle innovation in those sectors already exposed to heightened legal risks. In addition, the attraction to a company of operating within the letter, but not the spirit, of the law will be greatly enhanced and the power of regulators, often with limited funds, forced to litigate against third party-funded defendants commensurately reduced.

This in turn leads to a broader systemic risk that companies everywhere are exposed to greater competition, higher legal costs and evolving insurance practices. Adjustment to the new playing field may not always be straightforward.

Litigation finance is no longer a niche sector. It is becoming increasingly familiar in the broader financial ecosystem as nuclear verdicts and the risks they pose to industries and insurers – and hence the opportunities they raise for investors in an alternative asset class – become more pronounced.

As the litigation funding sector continues to expand, so it is encountering growing scrutiny and regulatory challenges. A notable development occurred recently when the UK Supreme Court ruled that certain litigation funding agreements were not enforceable, a judgement which has sent shockwaves through the industry. This ruling has raised concerns over the validity of existing agreements and may prompt a re-evaluation of the legal framework surrounding third-party funding, potentially leading to increased regulation and adjustments in how these agreements are structured in the future. Legal and regulatory hurdles such as these highlight the evolutionary nature of the sector and its need to adapt to a changing landscape.

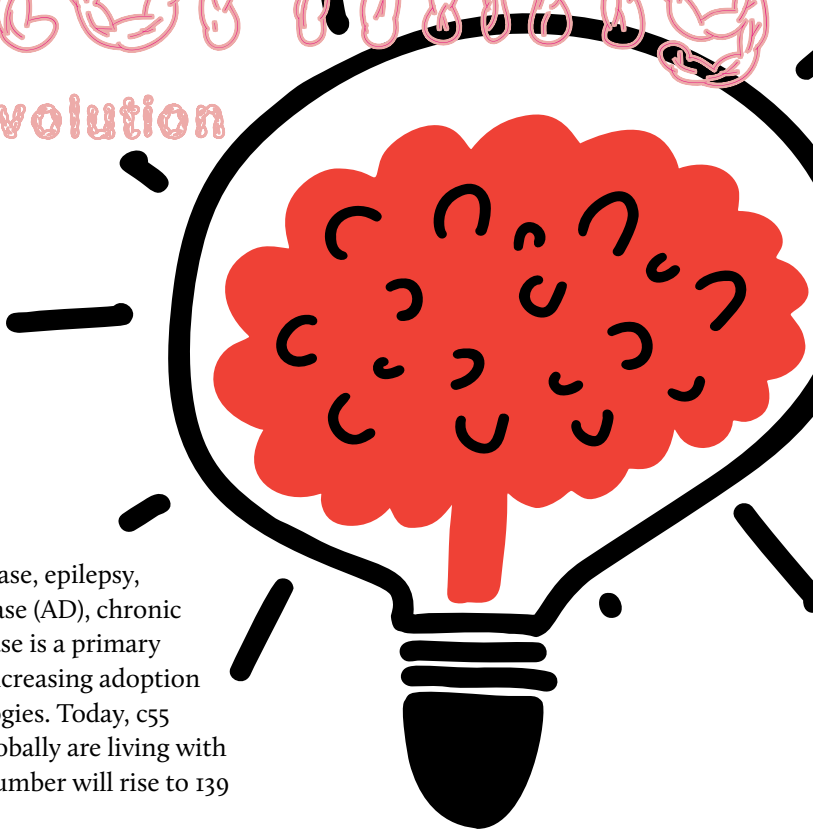
For investors and insurers alike, it is essential to stay vigilant regarding the risks involved. The use of litigation finance across all industries will evolve. Those insurers that reassess their risk management strategies, coverage and pricing will be able to differentiate themselves, while those investors who navigate the complexities will cross a frontier in the world of alternative investments.

And those plaintiffs fortunate enough to find an investor to sponsor their case will stride into the courtroom with the prospect of asymmetric risk and none of the fears of their predecessors.

Brainstorming

A Neurotechnology Revolution

Levon Dermanoukian
MedTech
Research



Neurotechnology is on the brink of transformation. From neuromodulation to brain-computer interfaces (BCIs) and enhanced neuroimaging, innovation offers hope for restored functionality, improved mental health, cognitive enhancement and more. As a result, the global neurotechnology market should grow faster than the wider MedTech sector. Its performance is being propelled by advances in technology, an increasing prevalence of neurological disorders (one in three people is affected by a neurological condition, an increase of 18% since 1990) and wider application through consumer wearables.

In 2024, early-stage financing enjoyed a neurology boom, with the value of early seed deals almost doubling YoY to $88m. Focus has largely been skewed towards neurostimulation, which accounted for 20% of the largest investments. Among the major venture capital investments in MedTech, BCIs have ranked highest. Neurology has led the pack at $1.2bn, the funds representing c30% of total Medtech investment over 2024. This goes hand in hand with the wider Biopharma industry, with the top late-stage (Series C) valuations (post-money) reaching 2.5x (on average) pre-money valuations.

The reason for neurotechnology's importance is straightforward. By 2050, nearly two billion people will be over 65, dramatically increasing the burden of neurodegenerative diseases. Hence, neurological disorders are already increasing (Parkinson's Disease, epilepsy, Alzheimer's Disease (AD), chronic pain). This increase is a primary catalyst for the increasing adoption of neurotechnologies. Today, c55 million people globally are living with dementia; that number will rise to 139 million by 2050.

Additionally, the increasing focus on minimally invasive procedures has encouraged greater adoption of neuromodulation therapies for treating chronic pain and movement disorders.

Similarly, the integration of AI across therapeutic tools is improving precision and adaptability, enhancing treatment efficacy via personalised approaches. AI is also used in imaging technologies to analyse neurological conditions more efficiently, reducing noise and diagnosis time.

As demand for innovative solutions continues to rise, the sector will expand further. This expansion can broadly be divided into three primary categories.

The first is neuromodulation devices. These modulate neural activity through electrical impulses including both implantable and non-invasive neurostimulation technologies. They comprise spinal cord stimulation (SCS) for chronic pain management, deep brain stimulation (DBS) for movement disorders and psychiatric conditions, vagus nerve stimulation (VNS) for epilepsy and depression, transcutaneous electrical nerve stimulation (TENS) or peripheral nerve stimulation (PNS) for pain management and non-invasive brain stimulation (e.g. transcranial magnetic stimulation (TMS) devices). The latter are expanding therapeutic applications in neurorehabilitation, pain management and mental health treatments.

According to Boston Scientific, the neuromodulation market (comprising SCS and DBS) was worth $3.6bn in 2023 and is expected to grow at a 6-7% 2024-26E CAGR. The primary indication targeting 'pain' (mainly SCS) should grow mid-single digits from an expansion into further indications. DBS will be accretive to Boston's growth, but the SCS market has recently been under pressure, in part reflecting an increased preference for non-invasive tools.

Next there is Neuroprosthetics and BCIs. Neuroprosthetic tools include devices that replace or enhance the function of a damaged nervous system, such as cochlear and retinal implants, and are beginning to emerge as a viable source of

The market

intervention for brain injuries. Among these, cochlear implants, which have been available since the 1950s, are widely adopted by hearing-impaired patients globally. Demand for advanced neuroprosthetics should keep growing as research into bionic limbs and brain-controlled exoskeletons continues to evolve. Similarly, recent studies have highlighted that neuroprosthetic tools enabling bidirectional interactions with the nervous system could be extended to cognitive disorders (e.g. AD).

We argue this feedback approach offers a powerful rationale for personalised care. There is an invasive component rendering it challenging to adopt but which could expand the scope of treatments. However, we cannot assert such developments will leap across into the invasive neuromodulation space given its differing applications. While neurostimulation focuses on regulating neuronal signals, neuroprosthetics aims to restore cognitive functions.

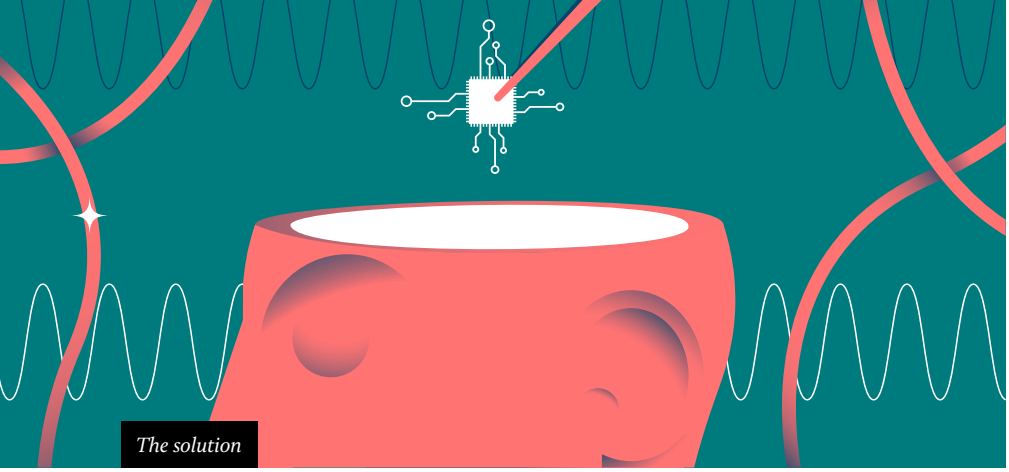
BCIs, on the other hand, are systems that allow direct communication between the brain and external devices. They enable individuals to control devices such as computers through their thoughts. The technology interprets brain signals, translating them into commands that can operate various applications, from prosthetic limbs to computer cursors. Precision Neuroscience, which recently raised $93m in funding, rounding its valuation to c$500m, is creating an interface with the promise of being reversible (i.e. the implant can be removed more easily, leaving almost no sequel), causing no damage to the brain. Its capital raise is a clear example of excitement from the street. BCIs are also gaining traction beyond medical applications, with potential use cases in education, workplace efficiency and even human augmentation, which will make them increasingly adopted.

Finally, we have Neurodiagnostics, which comprises technologies such as electroencephalography (EEG), magnetoencephalography (MEG) or advanced imaging modalities like magnetic resonance imaging (MRI), used for diagnosing and monitoring neurological activities and conditions. Imaging technologies accounted for 78% of total neurodiagnostic market revenue in 2022, with non-invasive techniques offering a differentiated advantage. The expanding use of AI-enhanced diagnostic tools is expected to propel this segment further, although this is not a new proposition.

Given, then, that this is an exciting space, the million-dollar questions are: who are the leading players and what is their competitive dynamic?

In neuromodulation, the trio dominating SCS for chronic pain management and DBS for movement disorders are Medtronic, Abbott Laboratories and Boston Scientific, who shared 99.6% of the market in 2023.

In Neuroprosthetics, Cochlear has established itself as a leader in implantable hearing solutions, with its cochlear implants materially improving auditory function in patients with hearing impairments. Meanwhile, Synchron is advancing BCIs through less-invasive procedures, enabling individuals with paralysis to control devices through thought. Neuralink, today valued at c$8bn, also focuses on BCIs and is revolutionary, owing to



The solution

its bi-directional brain-computer communication. This not only allows thought-controlled device interaction but also potential sensory feedback, paving the way for advanced neuroprosthetics, cognitive enhancement and medical breakthroughs in paralysis and neurological disorders.

In Imaging, mid-single-digit near-term growth is led by GE Healthcare, Siemens Healthineers and Philips. Given the outperformance of multimodal imaging (enhancing spatio-temporal resolutions) with molecular imaging (MI) through Positron Emission Tomography (PET) in neurodiagnostic performances, we view GE Healthcare and its radioagent Vizamyl as best placed to lead the pack. That the radiodiagnostic opportunity in AD is opening up a $1.5bn total addressable market (TAM) by the end of the decade in the US alone, according to Lantheus, only adds to the attraction.

Despite this immense potential there lies the ever-complex landscape of potential insurance reimbursement barriers. Reimbursement plays a crucial role in the adoption and accessibility of all medical devices, and neurotechnologies are no exception. Traditionally, neurostimulation tools have not received proper reimbursement coverage; will it remain that way?

In the US, while the Food and Drug Administration evaluates technologies in the context of benefits and risks to patients, payers are focused on the economics. In general, the less regulated the device (Category 1 being the loosest regulation, rising to Category III) the easier reimbursement becomes as categorisation is in proportion to the risk level to patients. Currently, Category III technologies are eligible for Medicare reimbursement, but this is contingent on questions of safety and effectiveness. Payments are highly restrictive (i.e. routine costs only are allowed) or are capped at the amount payable for using a specifically approved device. Thankfully, facilities may sometimes receive payment from private payers. However, since Medicare's coverage and reimbursement policies influence private payers' coverage, its adoption is crucial for market penetration. It is worth noting the application process can take months, if not years.

A recent study highlighted that neuromodulation reimbursement rates declined from $553.6 in 2010 to $436.3 in 2023, reflecting a 21.2% decrease across all current procedural terminology codes, a clear negative for the sector. Overall, both invasive and non-invasive tools are receiving payment cuts, ranging from cost-control strategies capping reimbursements to less advanced and less costly neuromodulation devices.

Since the US accounts for a large proportion of the neuromodulation TAM, we see this reimbursement setback as detrimental. However, continued innovation in adaptive neurostimulation, which enhances precision and efficacy through personalised treatment, could sustain long-term adoption by shifting demand towards superior products.

Moreover, in the face of such challenges, alternative pathways to traditional reimbursement are beginning to emerge. Incentive-based reimbursement is one such pathway. New Technology Add-on Payment (NTAP), for example, is used by the Centers for Medicare and Medicaid Services (CMS). It provides additional payments to hospitals for utilising certain new medical expertise, thus enabling them to take a chance on novel technologies.

In Europe, reimbursement has been challenging, varying by country but shifting positively in recent years. In July 2023, the National Authority for Health in France released new guidelines for add-on reimbursements of various medical devices, including neuromodulation systems such as the PROCLAIM 5 spinal cord stimulation system and the INFINITY deep brain stimulation systems by Abbott. Clearly both leapt the bar of the benefit derived.

Similarly, we have witnessed positive signals in MI. These have not only been through positive long-term trends and additional transitional pass-through payment for new radio-agents (additional reimbursement to promote innovative drugs), but also through CMS's proposal to unbundle imaging procedure and radiopharmaceutical agents. Similarly, AI-enabled enhancements in neuroimaging are demonstrating positive pricing. This confirms the appetite for innovation, which should drive future growth.

Beyond medical applications, neurotechnology is expanding into the consumer market, focusing on wellness enhancement. Companies such as Muse, with its neurofeedback headband for optimising sleep and cognitive performances, or Samphire Neuroscience offering a wearable device for premenstrual syndrome and period pain relief, exemplify this trend.

The synergy between consumer-driven innovations and medical advancements is expected to ignite strong momentum over the coming years. It is one reason we remain highly optimistic about a sector where the promising near- and long-term growth potential creates an attractive investment opportunity.

Retailing Wellness

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The US wellness economy was estimated to be worth c$2trn in 2024, representing one-third of the global total. Its annual growth between 2019 and 2023 was over 8%, a healthy lick for a discretionary goods category.

Some 82% of US consumers say wellness is a daily priority and 58% said they are prioritising it more than hitherto. Millennials and Gen Z spend more than older demographics. This suggests growth will persist given lifestyle habits are typically established in younger years. As Millennials are entering their peak earning and spending phase, the market should accelerate.

Consumer brands are positioning themselves to benefit. But what exactly is 'wellness'? Does it differ between individuals? Who decides? And when and how, and how much, does one consume of that product or experience?

Wellness is in the eye of the beholder. It is a fragmented space and definitions are multifarious. There are so many fads. All it takes is one celebrity or influencer to post a comment or upload a photo and a product or trend explodes in popularity. The 'next big thing' is always around the corner.

The wellness market has been gaining traction over a considerable period. Consumers are self-evidently keen to improve their lives in ways traditional healthcare is unable to meet. These include Nutrition, including weight management, and Sleep, which ranks as the second most important wellness factor for consumers, yet it is the realm in which they have the most unmet needs. Further underserved subcategories are Women's Health and Healthy Ageing. Women's Health traditionally comprised basic menstrual care and intimate health products. However, interest in menopause care, pregnancy and fertility is increasing, the average spend rising. Healthy Ageing is also topical given developed country demographics and the emphasis on preventative healthcare. But there are also numerous niche opportunities. Wellness is not 'one size fits all'. The depth and breadth of the market is expanding exponentially. To be successful in a competitive space, retailers and brands must focus on four trends.

Firstly, science-based and clinically recommended matters. Historically, 'wellness' leant towards 'clean' and 'natural'. We argue there is a reversion towards 'authority' – proven ingredients and efficacy-driven choices. This plays into the hands of established retailers.

Next is convenience. Ease of access and simplicity are critical. Fitness club memberships boomed pre-pandemic, but we note a shift towards more personalised ways to participate shaped around the day. It is essential to avoid the doctor's clinic, given cost and lack of access, but consumers wish to be familiar with health basics such as vitamin and mineral deficiencies, cholesterol levels and screening metrics.

Thirdly, there is tracking and monitoring, and the need to balance these with privacy. Given the personal nature of health, an individual's data is an essential constituent of any solution. Wearables will remain central, raising issues over privacy and consumer trust. Again, this plays to big brand retailers in whom customers have invested faith and have the apps on their phones.

Finally, inevitably, there is AI. This will become central, given the diagnostic and customisation capabilities it offers. Technologically innovative retailers will prosper. When authoritative brands take leadership, the market opportunity feels credible.

Retailers such as Walmart and Ulta Beauty will probably lead, given their scale, reach, trust and authority. They are investing in the space. Amongst its recent initiatives, Walmart has launched same-day pharmacy delivery, free health screenings, a private-label food brand focused on 'plant-based' and 'made without'. The bigger battle is to deliver more in-depth healthcare solutions to underserved markets, something it is uniquely positioned to do given its geographic and demographic coverage. The latest iteration, building out Walmart health centres, ended last May – the complexities of the US healthcare system proving insurmountable even for Walmart, at least for the moment. It is not walking away, simply returning to the drawing board.

Ulta Beauty is conducting extensive market research to seek science-based solutions. It has set up a dedicated team and Wellness is one of the four pillars of its strategy.

Given Ulta's editorial role in beauty and personal care, it is well placed to succeed.

Research Matters

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Second Sunrise

America's 'exorbitant privilege' has depended on its sponsorship of the global rules-based geopolitical and economic system. US dollars funded the symbiotic rise of China. Now, China is experiencing a 'second sunrise' away from the pull of the US economy. Meanwhile, other ageing major saver economies are tilting towards spending. While China's growth model facilitated lower US Treasury yields and increased US borrowing, the opposite is now true. The dollar's reserve currency status will be eroded.

Enterprise Software

Call My Agent

Almost a trillion dollars has been invested in AI infrastructure and investors are looking for a return. Step forward agentic automation in enterprises, where almost $4trn pa is spent globally on humans undertaking tasks AI agents can perform. The proliferation of agents will trigger a powerful enterprise automation wave, accelerating the conversion of labour to software. We estimate the agentic automation opportunity will add $500bn pa, or c25%, to enterprise software revenue by 2035.

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Letter from America

Leadership Under Fire

Rajat Chaudhury
Global Financials Specialist

The most important idea I have learned throughout my time in the military is that it is not about you. From this stems everything I know and believe about effective leadership.

It started on day one. As we stepped off the bus at Basic Training at Fort Sill, Oklahoma, the drill sergeants made us align our green duffle bags 'perfectly' with each other's. Some of the bags were slightly off the line, but mine were fine, so I stayed put. Yet all of us, even those who had executed the task perfectly, had to drop down with the rest of the platoon to do pushups because someone else had failed to perform. Thinking about it now, did I really have to do pushups because whoever was next to me had screwed up? Nope, that was not the lesson those drill sergeants were trying to instill: it was because we as a platoon didn't help each other and work as a team.

This lesson has stuck with me all the way from being a Private to a Second Lieutenant, and I try to apply it in every endeavor. The concept is a hard one to digest, especially on Wall Street where it often feels it is each man for himself. This 'it isn't about you' concept is the backbone of every leadership philosophy the military teaches, one that can and should be carried over into the corporate world. Indeed, many of these lessons are found within some of the greatest leaders I have met.

I use 'leader' not 'manager' deliberately. I have seen plenty of phenomenal managers but few great leaders. You may ask, what is the difference? In short, managers tend to focus on the mission whereas leaders, by focusing on their subordinates and peers, accomplish the mission and set others up for future success, not least by setting a profound example.

Reflecting the fact it is never about you, I will turn to two of many examples of men who have done far greater things than I, to explain what I believe leadership is about. These are some of the greatest heroes, Medal of Honor recipients, who embodied selfless service, leadership by example, courage, dignity, respect, honor, integrity and audacity. I hope I can display such qualities if I am ever in similar situations, whether in combat or in the corporate world.

Firstly, Lt. (SEAL) Michael Murphy. Mike Murphy was awarded the Medal of Honor for his bravery during 'Operation Red Wings' on 28 June 2005. If you have seen the movie *Lone Survivor*, you will know his story. Murphy and his team were deep behind enemy lines in the Hindu Kush region of Afghanistan conducting a recon mission. Unfortunately, the four-man SEAL team was compromised and a firefight broke out between it and more than fifty anti-coalition militia. The enemy force far outnumbered the SEALS and held a terrain advantage leading to the team aggressively bounding down the mountain's steep edges. On such austere terrain, radio signals were weak and the team was unable to contact headquarters to request support. Lt. Murphy spied an opening and unhesitatingly, with complete disregard for his own life, maneuvered into the gap. Lacking cover, he was immediately fired upon, but nevertheless contacted the Quick Reaction Force (QRF) and calmly provided his unit's location, enemy details, and so on – all while he was under fire.

Extreme empathy and a sense of duty is the lesson here. Lt. Murphy disregarded his own safety and placed his teammates first. Obviously, at Redburn Atlantic we aren't being shot at day to day (though clients have been known to be 'disappointed' with the odd stock call), but empathy is key. Try to put yourself in your peers' and subordinates' shoes, knowing everything you do as a leader effects them the most.

I was at a drill the other day and we had just welcomed a new battalion commander. He mentioned there is a poster on his wall with a picture of a solider in full battle kit going through the dirt, and a quote saying, "Anything and everything you plan and decide, this man is going to have to execute". Sometimes as leaders it is easy to be carried away by a strategy you consider phenomenal, but it's essential to remember it is your troops who are going to have to work day and night to deliver.

This brings us neatly back to Lt. Murphy. He knew what was needed in order for his soldiers to live and realised he as a leader was simply there for his team. The decision to make that call on the edge of that open cliff was intentional and decisive for these reasons. Sometimes as leaders we may be called upon to take the brunt of the force so our subordinates can succeed. It can be a hard concept to grasp among the life-changing bonuses for management on Wall Street.

Secondly, there is Staff Sergeant (SSG) Ty Carter, who was stationed on Combat Outpost (COP) Keating

Primus inter pares

in Afghanistan, which was situated at the bottom of a constricted, bowl-shaped valley. This terrain put his platoon at constant risk.

One day, the unit's worst fears were realised. Enemy forces surrounded all four sides of the COP and initiated contact with rifles, and DShK heavy machine guns. SSG Carter and his team were also battling combatants who had breached their base, so there was absolute chaos. As the battle continued, every position around the base started to run low on ammunition and other supplies. Without regard to his own safety, Specialist (at the time) Carter proved himself time and again. He resupplied ammunition to fighting positions, provided first aid to a battle buddy, killed enemy troops and risked his own life to save a fellow soldier who was injured and pinned down by overwhelming enemy fire. He did all this while under heavy small arms and indirect fire that lasted more than six hours.

The lesson here is one of extreme courage and loyalty. Many people know what the right thing is to do but say, 'Not my problem'. Well, as leaders, the standard rises immensely. It is your job to stand up and deliver for those around you. If you are unwilling or unable to do this, then, let's be honest, you're not a leader.

Carter went above and beyond, risking his life numerous times so his soldiers had a chance to survive the torrential downpour of bullets and RPGs. Although his armored vehicle was the only safe spot during the firefight, he voluntarily went into the open to assist his soldiers. Having the boldness to do the right thing is certainly difficult, but sometimes as a leader you must 'place yourself in the open' and be willing to suffer for what is right.

At 461 Fifth Avenue this is (hopefully) unlikely to be in the form of taking a bullet for your co-worker, but it will be in the form of assessing the feasibility of leadership plans, allocating roles, listening to personal issues that may impact performance and so on.

It is your job as a leader to implement those plans and go into battle for your 'soldiers' and to give them the best you can, because it is no less than they deserve.

The Rental Rollercoaster

The Twists and Turns of Tenancy

Tejasvi Muvvala
Graduate Research Analyst

As I bid farewell to the rat exterminator for the seventh time, I find myself reflecting on the challenging, and commendable, nature of his work. Each week, the elderly gentleman arrives at our house with the hope he has successfully captured a rat in the trap hidden under my shower. I personally couldn't think of much worse than seeing, or smelling, a dead rat. Despite his frequent reassurance that the rats (along with the mice) can't infiltrate our house, I can't help but wonder: is living in London really worth it? And are we getting our money's worth?

Living under two hours away from my parents and their constant assurance I can return home if needed, I've found myself contemplating why so many young people are drawn to London. For me, the city has always been synonymous with family days out or shopping trips. But somewhere along the way, it became assumed, and the dream among my friends that we would all move to the city together. Now, though the option to return home remains, I wonder what keeps me locked into renting.

It's not just my experience either. I've noticed all around me – at the gym, in restaurants, at the pub – everyone seems to be of a similar age. Well, perhaps they're older than I am, but I hardly ever see children, and rarely encounter elderly people. I may be more aware of those within my demographic, but a quick Google search confirms this observation isn't entirely imagined. In inner London, 23.5% of the population falls within the 25-34 age range, compared with only 12.7% in the rest of England.

As the barriers to entering the property market grow almost insurmountable, it's no surprise many young people are forced to rent for longer. According to estate agents Hamptons, young people comprise 66% of all renters in the UK. Moreover, the number of renters under 45 surged by nearly 150,000 last year to 3.4 million – the fastest increase in a decade.

This rise in renting coincided with the government's decision to wind down 'Help to Buy' in March 2023. As a result, 33% of renters claim they don't foresee homeownership in their future, up from 20% in 2022. While there are rational reasons to rent, such as the freedom to explore different areas or a desire to prioritise other investments over homeownership, the primary factor is financial: 80% of renters say affordability is the main reason for not buying a home. This is unsurprising given the typical deposit for a first-time buyer in London has reached £125,000.

The alternative to buying is little better. Rents have increased dramatically, with younger tenants shouldering the burden of an additional £3.5bn in costs, pushing prices to record highs. Between November 2023 and 2024, rents surged 11.6%, the fastest pace since records began in 2006, according to the Office for National Statistics. In 2024, the average London tenant sent 44.6% of their net pay to their landlord. And in the twelve months to January 2025, the average UK rent increase of 8.7% exceeded inflation (3%) and wage growth (5.9%).

Rising rent and house prices can be traced to a shortage of available properties. Despite the Labour Party's pledge to build 1.5 million homes by 2029, the UK construction sector is on track to deliver the fewest new houses in a decade, hampered by planning regulations and high mortgage rates. Industry experts have warned that without material support for first-time buyers or increased funding for affordable housing, the government is unlikely to meet its targets. But to emphasise the mess that is the property market, there are more than 38,000 'vacant dwellings' in London and over 700,000 in England, with around 37% empty long term. This begs the question, why are these properties not being taken advantage of first?

The financial challenge of renting is just the tip of the iceberg though, as securing a property has become more competitive than ever. Having personally navigated the frustrations of platforms like SpareRoom, I can attest to the difficulty in even receiving a response from landlords, despite paying for a premium account to contact them within a week of their listings. A recent SpareRoom survey revealed that nearly half of renters must decide on a room during the viewing itself.

Those who may have it even worse than young renters, however, are lodgers with live-in landlords. There are increasing examples of live-in landlords suggesting lodgers spend as little time as possible at home, despite the extortionate rents being demanded. One example, which went viral on social media recently, receiving over 85,000 likes, was for a room with a single bed, wardrobe, desk and chair priced at £1,350/month. The ad suggested, "This

Casting a shadow

space would ideally suit someone working long-ish hours in the city during the week and leaving the city for weekends. I am also teaching the violin here in the evenings from 4-8.30pm Monday to Thursday. Whilst this takes place on a different floor to the bedroom I am offering, it would be audible, so this room would suit someone who is not home until post-8.30pm." The ad further made clear that whoever took the room would be prohibited from using the living room, having any guests and making noise after 11pm.

Exploitative landlords are demanding high prices and offering as little as possible. Lodgers will not even be protected under the new Renters' Rights Bill, which aims to reform the private rental sector and end 'no fault' evictions.

But is London the root of the problem? Rental prices outside the capital decreased QoQ in late 2024 for the first time since before the pandemic. Although rents beyond London were 4.7% higher than at the end of 2023, the growth rate marked its slowest pace since 2021.

However, Londoners moving out of London has fallen to the lowest rate since 2013. The city's vibrancy and opportunities are undeniably enticing. Unlike the US, which boasts a number of dynamic second-tier cities, the UK lacks comparable alternatives to London. For instance, moving from London to Bristol would – despite the savings on housing – result in a 23% reduction in net income. In contrast, moving from New York to Denver would only decrease net income 2%. Moreover, London remains the hub for most of the UK's highest-paying jobs, solidifying its position as the place to be despite prohibitive costs. Employment in high-paying occupations has grown 95% nationally since 1993, but for London, this growth has been 240%. Preference for living in the city has surged again after the pandemic, as businesses enforce returning to the office, with Deloitte even linking bonuses to office attendance.

But maybe there is a chink of light. London's rental prices in January have risen 2.4% YoY, the smallest increase since 2021. Additionally, prospective tenant inquiries have dropped 16%, according to Rightmove, as some renters buy homes, benefiting from a lowering of mortgage rates. Living in London, despite overcrowded tubes, pricey coffee and steep rents, still offers the sense of freedom, excitement and convenience so many desire. There is also a domino effect – as more young people move to London it's inevitable their friends and peers will want to be there too, only heightening its pull.

The challenges of living in London are undeniable but the bustle, charm and opportunities far outweigh the obstacles. As I let the exterminator out, cook a recipe with friends and argue about our party guestlist, I can't help but feel content and grateful.

Arthur Blessit

27/10/1940 – 14/01/2025

Arthur Blessit was a perfect example of nominative determinism. Having accepted Christ at a revivalist prayer meeting when he was seven, he was ordained aged twenty while studying at the Golden Gate Baptist Theological Seminary in Mississippi. A Charismatic Evangelist Protestant, he spent several years as an itinerant preacher before winding up in Los Angeles as the counterculture reached its high.

Blessit opened a coffee shop, His Place, amid the pornography and flophouses on the Sunset Strip. There he ministered to the downtrodden, to drunks and dopeheads and the dispossessed, saying, "You don't have to drop pills to get loaded, just drop a little Matthew, Mark, Luke and John." "Christ," he maintained, "is the ultimate trip".

One night, he claimed the voice of the Lord told him to go out into the world. He took the twelve-by-six foot cross off the wall of His Place and, having added a wheel to its base, started wandering around Hollywood, engaging willing or able passers-by in theological debate.

Catching the hiking bug (and applying a strictly literal reading to Luke 9.23 – 'If anyone would come after me, let him deny himself and take up his cross daily and follow me'), Blessit set out on Christmas Day 1969 to walk from LA to Washington DC carrying his cross. It took six months, causing him to observe, "If I'd known I was going to carry it I would not have made it so big."

In New York, he re-established His Place near Times Square among the hustlers and hookers, which he advertised with a peephole and the words 'Totally Naked'. When the porn-oriented peeped, they were greeted not by a scantily clad lady but a sign pronouncing, 'Man Stands Naked Before His God'.

In 1971, he expanded his horizons beyond the US and set out on foot with his cross to spread the word around the world. Over the next thirty seven years he covered 324 countries, 25 islands and 40,235 miles, entering the Guinness Book of Records for the 'world's longest unbroken walk'. Having had his cross stolen in Assisi, he made a lighter one (45lb to the original's 110lb), noting the wheel wore out every 2,000 miles, while his boots needed resoling after 500.

Along the way he took in war zones, disaster areas and some of the most lawless places on earth. Man-made dangers accompanied him through Sudan, Somalia, Soviet Russia, Afghanistan, Northern Ireland during 'the Troubles', Nicaragua, where he was almost executed at the roadside by firing squad, Iran, Iraq, North Korea and Morocco, where the locals stoned him. Natural hazards impeded him in Kenya (baboons), Tanzania (elephants) and Zimbabwe (crocodiles), while in the jungles of Central America he had to cope with "diseases, parasites, leeches, rabies, fungus, mosquitoes and ticks".

Yet it was in the US he encountered the most hostility. A man in a Texan outpost threatened to nail him to his cross if he didn't get out of town; another pulled up in a Chevvy and took a pot shot but somehow missed; and the police were forever "coming up with their lights on and sirens blaring asking me where my permit was".

While in the Third World people generally treated him as "a holy man", in the US they assumed he was "from the Ku Klux Klan, or an anti-abortion protester, or right-wing nut".

Through it all he kept on walking, preaching, engaging with whoever he met. Those included John Paul II, Bob Dylan, George W. Bush, Colonel Gaddafi, Yasser Arafat and Menachem Begin, all of whom entertained him. But his focus was on ordinary people. "My church and congregation are out there on the road. That's where my home is."

Arthur Blessit announced his death on his website, proclaiming, "I have completed my walk and mission on Earth. These feet that have walked so far on roads of dirt and tar will now be walking on the streets of gold".

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