

## War - What is it good for?

**“Supreme excellence consists of breaking the enemy's resistance without fighting.” Sun Tzu, *The Art of War***

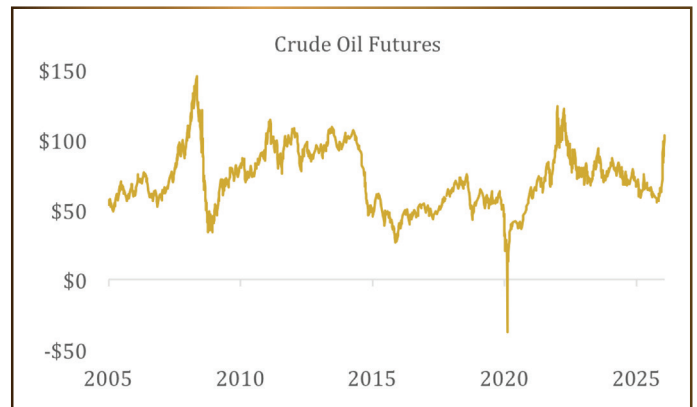
The 2026 Iran war has caused oil prices to surge above US\$100 per barrel due to disruptions in the Strait of Hormuz, increasing global energy costs. This shock acts as a regressive tax, fuelling inflation and harming lower-income households, while increasing transportation and production costs. The resulting economic environment is stagflationary, causing stock market drops and reducing consumer spending. However, the endless consumption of financial literature makes it easy to slip into industry jargon that can be difficult to connect to real world applications. With that in mind, it's important to take a step back and assess what financial risks we could all be exposed to as a direct result of this conflict.

With each war, amongst the myriads of reasons for and against the interventionist approach, nothing is the same afterwards, with oil typically being the first thing to place its flag in the sand and let us know that the world has changed. In the wake of Russia's invasion of Ukraine, oil rallied more than 465% from its post-Covid trough. Admittedly, some of those lows were a ludicrous byproduct of a world coming to a standstill, so a rally was bound to happen in any case. As a result of the ongoing conflict in Iran, the price of oil has already increased some 70%. For those who think that it will only be reflected in energy bills, then you would be wrong as such movements dictate the price of much of our daily lives as it forms a core component in the production of fertiliser, which is a pre-requisite to the food we eat, clothing, transport, plastics (toys, packaging and everything in between), and not to mention all other synthetic materials we use on a daily basis, such as paints, rubber products and even asphalt. As such, whilst the price of oil may respond quickly, a domino effect soon occurs. We all feel the hikes at the petrol pumps but impacts elsewhere can often be harder to spot as some companies will try to absorb it into operating costs, therefore narrowing margins, which makes them less resilient in a scenario of rising wages should the inflation spike become more endemic.

There is no doubt that peace brings immense benefits to humankind, the planet, and the resources we depend on. Yet history shows that, for many reasons, a peaceful resolution is not always possible. When conflict erupts, death tolls rise, land is devastated, and lives and valuable resources are lost. This article is not about whether war is right or wrong; it is about what we need to consider when the inevitable happens.

Investors will no doubt be considering taking some risk off the table. In many cases this will simply be reflected in a move to cash to protect the absolute value of the portfolio. Whilst there is an understandable psychological reason to keep that headline AUM figure from sliding, in real terms that is the surest way to lose money because the impacts of inflation can be sneaky. If the oil supply shocks and surging energy prices become more pervasive, not only will this dampen economic activity, but it will immediately reduce the spending power of your retirement pot.

Moving to gold is also a common thought and longer term it has rewarded investors but not in a linear fashion. Its gone through many periods of doing very little, which means its place in portfolios can be subject to many



discussions, especially through the 2010s when the gold price went nowhere at a time when equity markets had the double tailwind of low interest rates and quantitative easing. However, it's now more than doubled over the last 18 months as investors concerns started setting in and so it's more than earned its place in portfolios again. That said, it's strangely correlated with equity markets at the moment and, whilst we are in no doubt that it will continue to be an important insurance policy for times of stress and a longer term hedge against inflation, there's no single place to put your money that will guarantee protection when trying to reduce exposure to risk.

Many policymakers will maintain expectations for a shorter period of conflict, which will enable them to look through the near-term price spikes and allow them to position interest rates accordingly. Persisting with looser monetary policy may help shore up balance sheets, but being late on rate hikes could risk triggering a repeat of 2022, where interest rates were increased almost too quickly for markets to absorb.

History tells us that shocks are typically short but frequently act as a catalyst to a longer-term permanent change, with most advancements in technology being the result of a war – such as radar, jet engines, and even early computers, which were all designed because of military investment. Even in recent history, we saw a rapid development (and approval) of an mRNA vaccine after decades of development. However, by the time these breakthroughs become evident, it can already be too late to benefit and, similarly, by the time the fog begins to clear, markets may already have recovered much of their near-term losses. As such, the best way of structuring portfolios to take advantage of any relief rally is simply to be positioned ahead of it.

Investing 101: Ensure your portfolio risk profile and asset allocation are consistent with your needs, while avoiding short-term knee jerk reactions that can lead to crystallising big losses. Most importantly, ensure that you take a holistic, long-term view and stay true to your objectives.

**David Bushe**  
CHIEF EXECUTIVE OFFICER

# Investment Tools for a Crisis

Before touching on current events, I think it's worth taking a pause to acknowledge how last year's returns represented a refreshing change of pace, and not just because markets performed so well, as that should go without saying.

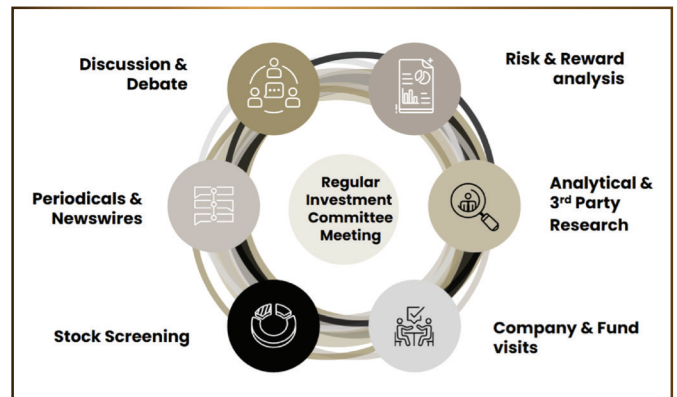
What is refreshing is that, in contrast to what seems to have defined the investing landscape in the wake of the Global Financial Crisis, returns weren't dominated entirely by US outperformance, so diversified portfolios were rewarded for their prudence as virtually every other market outperformed by a significant margin when compared against America's main index.

The US market still climbed 8.3% in sterling terms in 2025, but UK, European, Emerging Market and Japanese equities all delivered more than twice the return over the same period. This was driven by an environment that encouraged an investor rotation away from US equities, such as a notoriously volatile approach to trade policy (mildly put), increasing talks of an "end to US exceptionalism", alongside supportive monetary and fiscal policy in other markets.

This momentum was carried on into the New Year as inflation was heading towards target in most markets and there was a predictable path of rate cuts on the horizon to provide a further tailwind to equities. Yes, there are concerns relating to excessive valuations within the AI theme and broader technology sector, but such risks are a common aspect of committee discussions and can always be diversified away. Markets almost started to seem suspiciously calm before they were shunted into disarray after the United States and Israel launched airstrikes on Iran and the subsequent fallout that came with the effective closure of the Strait of Hormuz. Since then, indices have been jittering back and forth between a flight for the exits and an opportunistic rebound in response to more reassuring headlines.

When things start going awry, I try to remind myself to only stress about what I can control. With that in mind, it's important to remember that we have no control over how the current conflict progresses from here and, whilst the base case for most commentators seems to be for a swift end to the conflict, the timing of any resolution is something to which few people have any sway. What we do know is that the longer the war goes on then the further away economic data will be from what economists were predicting at the beginning of the year. Markets have already started pricing in higher inflation, and the downward trajectory of interest rates has been firmly put on hold. Not only that, but 10-year bond yields (the investment industry's yardstick for risk free returns) are heading higher to reflect an increasing likelihood that central banks could soon embark on a hiking cycle. Beyond that, it's extraordinarily difficult to quantify how things will progress from here and, given how quickly the landscape is evolving, it would be futile to try.

If we don't know what tomorrow holds in store for us, it might prompt someone to ask how we can expect to navigate what comes next. Whilst we are currently in uncharted waters, as no two crises are ever identical, a rich history of financial markets and a good depth of industry experience within FIM's Investment Team, provides us with the tools needed to ensure client capital is positioned to have the appropriate level of resilience in times of stress, whilst also being able to benefit from the upside when markets normalise.



Tools within the Investment Team include our regular committee meetings (quarterly and biweekly), where we share concerns and collaborate on ideas. We all sit within close proximity, so these conversations never really stop, but the regular meetings are an important way of addressing and highlighting any assumptions we have about how portfolios are structured. For example, the investment case for some portfolio holdings may change, or it may be that the underlying strategy is overly exposed to illiquid small cap stocks when the initial rationale was for large international equities. These meetings must also include regular economic discussions to ensure there are no avoidable risks on the horizon. Economists were largely in agreement that, in a post-Covid-19 environment, inflation would be transitory, but 2022 proved to be a very damaging year for portfolio managers who got that call wrong, so it is essential to ensure that, as a team, we are able to factor those risks in. Supporting this is a range of external data and research providers, such as Bloomberg, Alpha Terminal and Capital Economics (amongst others), that provide essential context so that we can cut through the noise of the media news cycle.

As it happens, ahead of this current crisis, we had already been nudging portfolios to account for lingering risks, such as those relating to lofty valuation multiples or the potential for a return of inflationary pressures despite consensus forecast for a continued trend towards target. As such, whilst we naturally revisited our rationale as things started to escalate, we were overall confident that the longer-term themes remained intact.

However, these qualitative discussions are only able to happen within the Investment Team because additional teams within the company provide the essential support needed to keep records in check and data accurate. With that, the Compliance Team, the Client Services Team and the Settlements Team are all integral parts of the overall client experience.

These tools help define how we operate on a day-to-day basis. It's not flashy and it is far removed from some of the more off-the-wall media portrayals of the investment industry, but these processes and functions enable an environment whereby the Investment Team can effectively perform under pressure when times get tough. This is all in keeping with FIM Capital's mission statement to "deliver exemplary investment management and fund administration services to all our clients to mutually deliver, grow and prosper".

**Michael Craine**

DEPUTY CHIEF INVESTMENT OFFICER

# Playing God

Amidst the fog of war, investors' attention has temporarily shifted away from the impact of artificial intelligence and how this evolutionary technology is going to affect the world. A few weeks ago, this was (nearly) all that mattered to markets. It will matter again greatly, and soon. The scope for disruption from AI is beyond huge, even if tangible productivity gains are hard to detect right now.

Today, the main financial beneficiaries of AI are hardware producers such as **Nvidia** and software developers like **Anthropic**. High-powered chips can now generate sufficient computing capacity to enable the current generation of AI software to think for itself. This is a fast-moving place to be. Nvidia's 2-year-old cutting-edge 'Blackwell' processing chip has been superseded by an even faster chip ('Rubin'), designed for agentic AI (where computers reason for themselves). For now, it is investment and spending on this technology, which is driving growth, adding an estimated 0.5 percentage points to US GDP in 2025. This is forecast to last for another 2 years or so, after which time the software should start to pay for itself. That is a sobering thought, especially as analysts routinely underestimate the pace of advancement in AI.

For companies to survive beyond 2030, they will need to fully embrace AI into their business practices. Unnerving as it all sounds, this is no time to be a Luddite. In practice, we seem to be getting better at embracing new technologies. The US Federal Reserve Bank observes that 'adoption lags' have been falling in recent years. Take-up of AI software by American businesses now stands at 55%, just three years since the technology became widely available. According to Capital Economics, this compares with an adoption rate of 20% for the PC and 30% for the internet, at exactly the same stage in their respective development cycles.

Most firms and individuals are currently using AI like a search engine with wings, asking ChatGPT to provide a written answer to a question or to write an essay (this article is not one of them). Regulators have noticed that easy-to-spot scams from 'Nigerian oil prince's' (sic) have been replaced with beautifully scripted communications which appear genuine on nearly all levels. Passport copies can be forged with ease, identities stolen, Zoom/Teams meetings populated by highly convincing avatars. For every upside to the new technology, there is inevitably some criminal downside. But this is a poor reason not to engage.

Why now? The origins of AI go back over 50 years. But it is only recently, in the last decade or so, that technology has been sufficiently developed to build so-called 'large language models' (LLM), capable of understanding and generating human language by processing vast stacks of data. Cynics point to the quality of this data as being the Achilles heel of the new technology. They are right, but not for long. As the LLMs continue to accumulate information, so data reliability will improve as systems cross-check for origin and accuracy. The new technology will threaten businesses and livelihoods in some sectors whilst creating huge opportunities in others. Plumbers and Premiership footballers are probably safe (for now). But estate agents, accountants, lawyers and, yes, investment managers should all be concerned.

Another winner of the AI revolution will be power generators and energy distributors. Most self-respecting property companies these days own a data centre or two, containing banks of computer processing power. These buildings are hi-tech, but they still need old fashioned electricity to power them up and keep their contents chilled. The International Energy Agency (which has been in the news recently for other reasons), notes that electricity consumption from data centres has grown at 12% annually for the last 5 years and accounted for 1.5% of global



consumption in 2024. This figure is expected to at least double by 2030. Oil, gas, wind, solar, tide. We need it all.

But where will it be needed? The hyperscalers, that is, those companies like **Amazon**, **Alphabet** (Google) and **Microsoft**, which can quickly 'scale-up' capacity to meet demand are largely based in the US and China. It is these two countries which will probably see the greatest uplift in economic growth, at least in the early years. But actual adoption of the technology by workers is more surprising. Here, the US is a clear laggard, well outside the global top 20 of country users measured by **KPMG**. China features strongly; but the leading regional users are dominated by computer literate emerging markets, from India to South Africa, Brazil and the mighty Costa Rica.

Whilst, in theory, AI should improve our lives (e.g. through the more efficient development of life-saving drugs), there are worrying downsides. Early indications are that the new technology is shifting employers' attitude towards hiring. Although the figures are skewed by some naïve policy making, unemployment has been rising in the UK and the US. Employers may be curbing headcount as they wait to see exactly how this new technology will evolve. Maybe, like the adoption of email, it will make us more efficient, but at the same time increase our workload. Or maybe, many of us will simply be replaced by a machine. Right now, nobody knows for sure.

What is very clear, is that governments and legislators will need to establish a set of AI rules to guard against malpractice. Anthropic's co-founder and CEO Dario Amodei suggests a digital 'constitution' which determines how a central AI model will behave. Anthropic gives its proprietary AI model ('Claude') a set of high-level 'principles and values' with the goal of educating the software to a level which prevents it from going rogue. Ideally, this rule setting should be carried out supranationally, i.e. by a politically neutral working party, transcending national boundaries or governments.

Today, as politicians seem more intent on firing missiles at each other than co-operating, this seems like a far-flung ideal. But with the Genie out of the bottle, the aspiration is highly important, nonetheless. And there is precedent. The *World Wide Web Consortium (W3C)* sets certain standards for the internet through legal and regulatory frameworks enshrined in code since 1994. For the new AI technology to be equally effective, governments need to step up now (some preliminary legislation already exists in the US) before businesses do it for them, with undesirable conflicts of interest, at both corporate and national level.

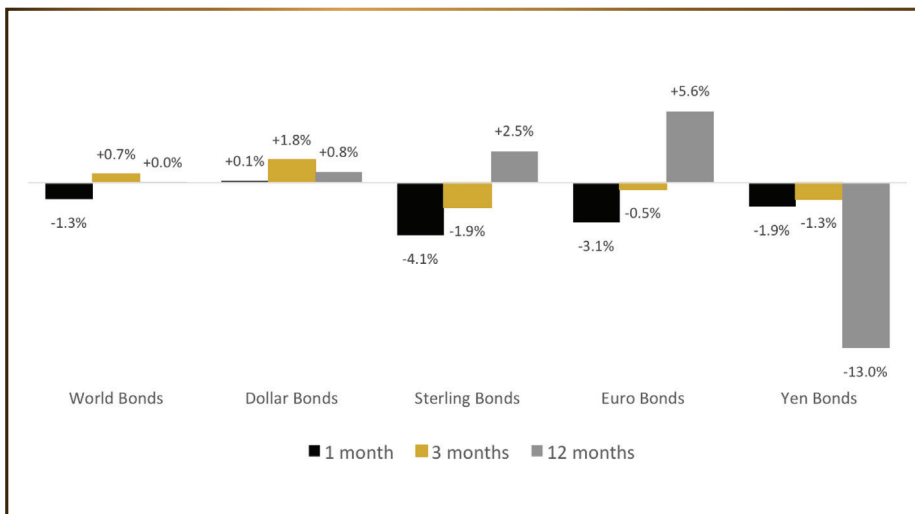
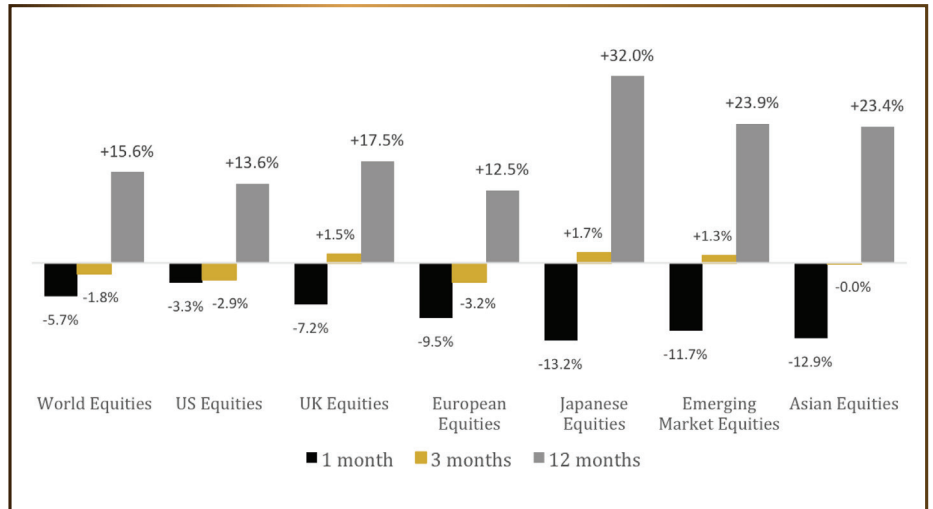
A final thought from Anthropic. In their opinion, artificial intelligence will disrupt 50% of entry level white-collar jobs over the next 5 years whilst new processing power could generate intelligence more capable than every living person in just 1-2 years. Things are about to change and neither businesses nor individuals will have any serious option but to change with it.

Russell Collister



### World Equity Returns (GBP)

Iran conflict caused a clear flight to safety from risk assets which has been reflected in significant declines through March, whilst 12 months returns remain robust after an excellent year for global equity performance.

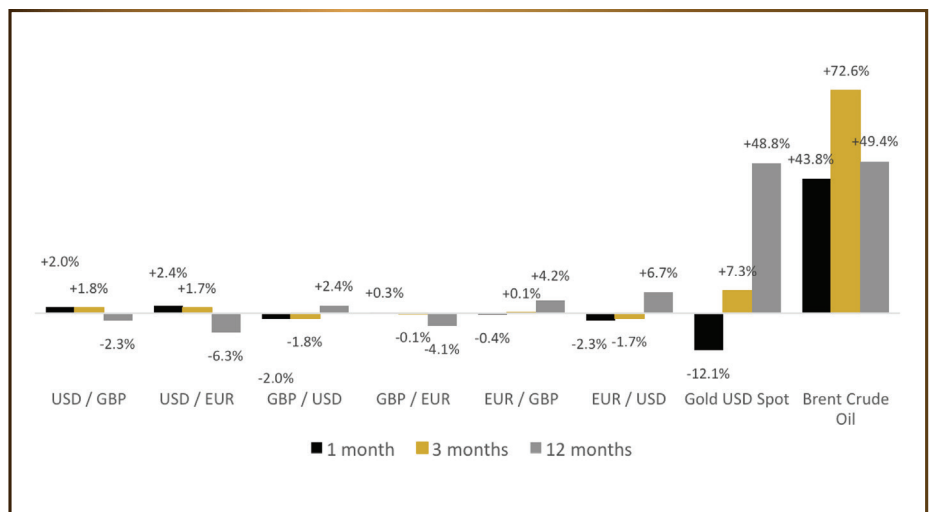


### Bond Market Returns (GBP)

The inflation impact of the conflict is expected to be felt harshly in the UK and European economies as they are more dependant on external sources, which goes some way to explain why bond yields have increased in these markets.

### Currency Movements

Currency movements appear relatively modest compared with last year's changes, although USD gained against GBP and EUR. Gold has sold off significantly since the beginning of the year, but follows an excellent rally in recent years. It's unsurprising to see that oil has been the biggest mover.



**Investment Management Briefing Editor:** Michael Craine, Deputy Chief Investment Officer

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