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Global Investment Letter

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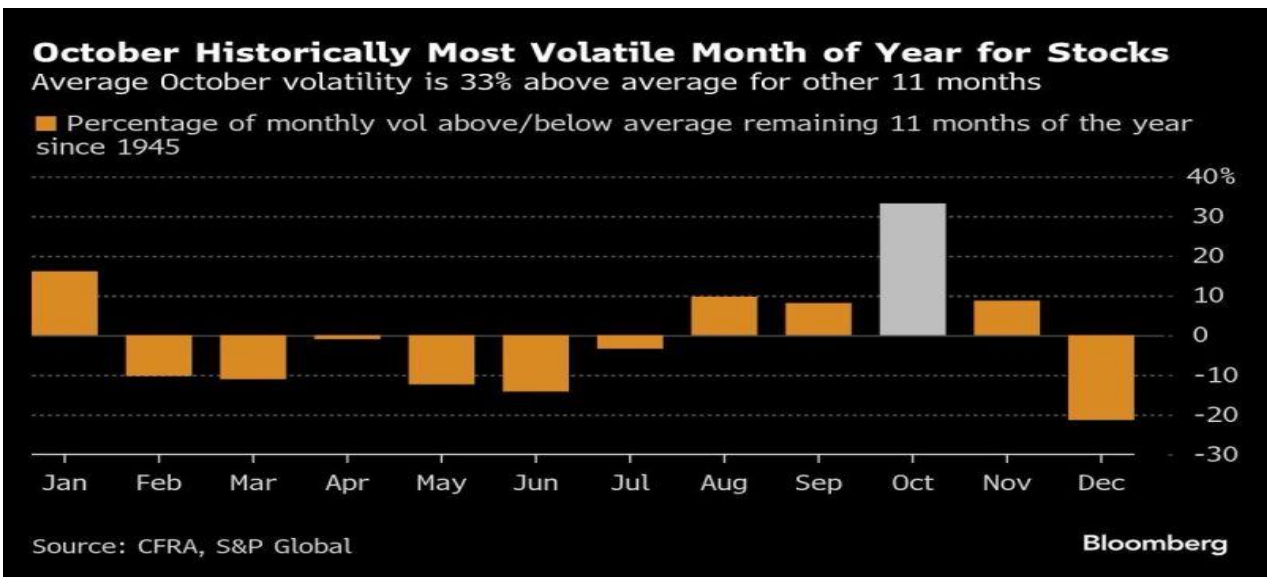
Echoes of the 1970s: Inflation, Politics, and the Next Market Reckoning

Among the host of economic and geopolitical factors clamouring for the attention of investors, the shutdown of the U.S. Government over the failure to pass budget measures in Congress has been the most conspicuous in recent days. This is not the first shutdown, so it is not terra incognita to the financial world, and previous occasions have not produced dramatic effects. We do not believe the shutdown is likely to exert a significant effect on markets unless it becomes protracted, lasting 10 days or more.

That is not to say that our previously expressed reservations about the investment landscape have grown any less concerning. Market valuation levels are demonstrably extended, as is investor optimism/complacency, both of which are established harbingers of market volatility.

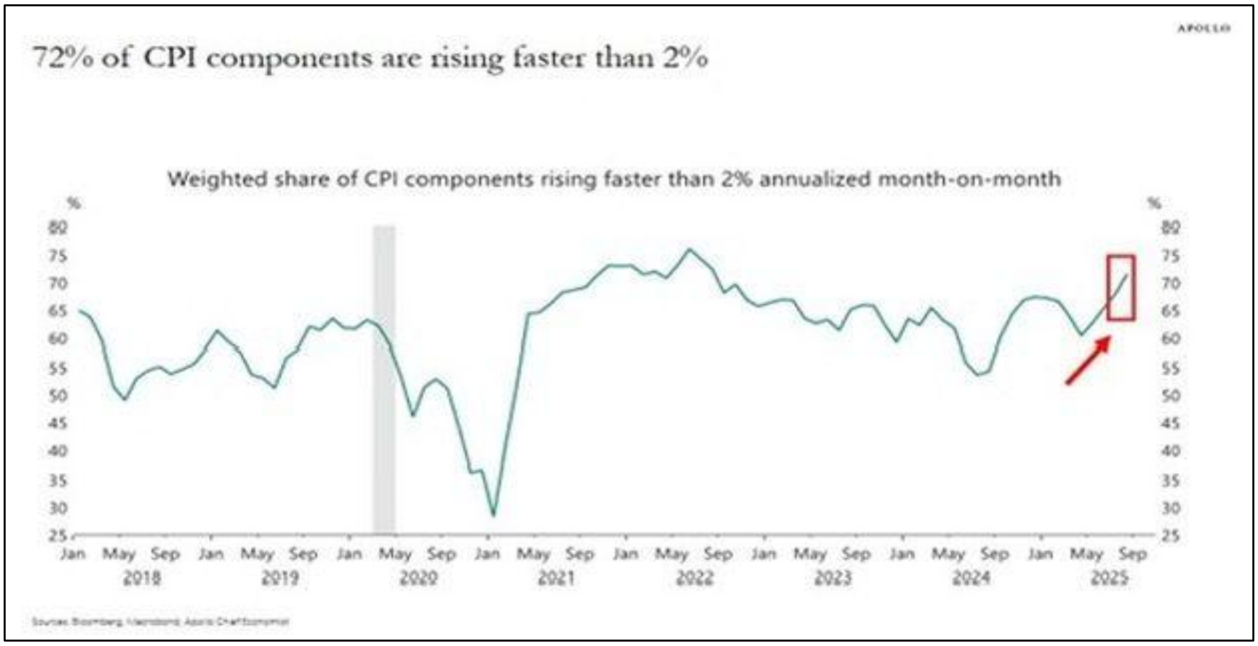
Decades of experience as a money manager shaped our reservations about the equity markets in September, and especially October. The following chart confirms that our 'money manager's intuition' was not misplaced.



Looking forward, the likelihood of a bout of significant market volatility in the coming month has been enhanced by the lack of a meaningful pullback or period of consolidation by the S&P 500 since the spring. There is no shortage of potential catalysts for volatility either in October or later, though the negative seasonality associated with October tilts the probability in favour of sooner. In times such as these, the use and adherence to protective sell prices is especially important.

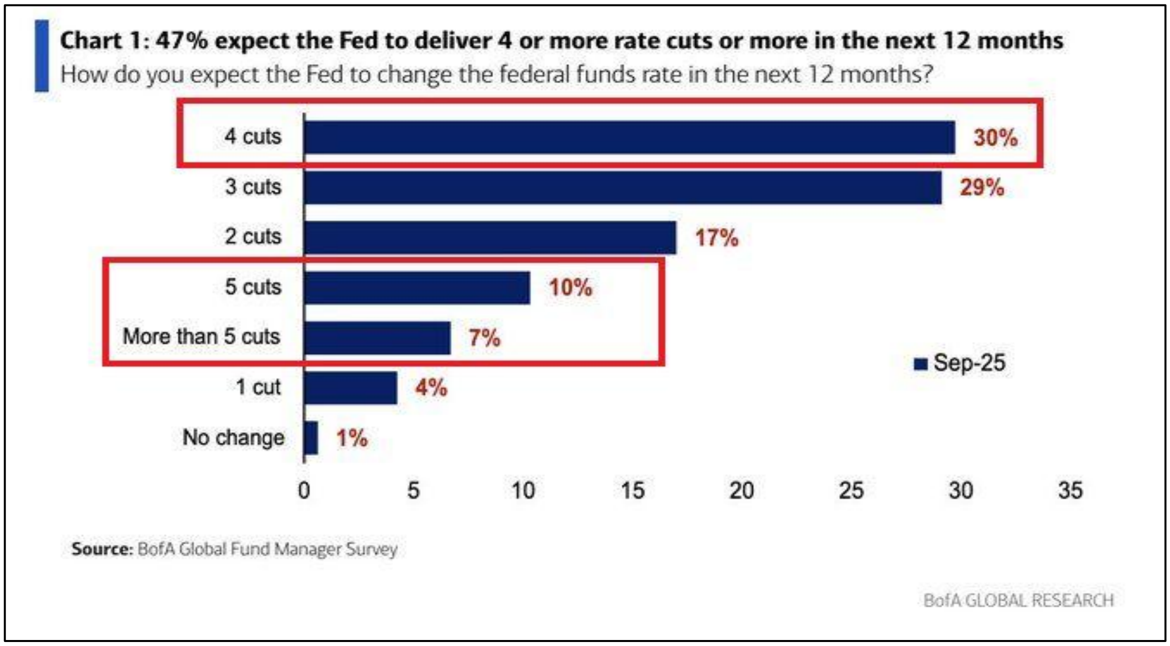
Whether the next bout of serious market volatility arrives sooner or later, evidence continues to build that we are entering a stagflationary environment similar to the 1970s. That evolution will be accompanied by a good deal of volatility, as it was in the 1970s.

The inflationary component of stagflation has remained persistent and is affecting the economy on a broader scale, as the following chart illustrates.



Fully 72% of the components of the U.S. Consumer Price (CPI) Index are rising faster than the 2% target set by the Federal Reserve and other central banks as an acceptable rate of inflation. Such widespread inflationary pressures increase the probability that CPI inflation will continue to build, aided by the full effect of tariffs on prices in the coming months.

The stag (stagnating) aspect of stagnation has been given more credence by the September interest rate cut by the Federal Reserve, which also hinted that last month's cut could be the first of a series. There have been a growing number of economic reports suggesting that the U.S. economy is slowing, with the decline of job growth receiving more than its share of attention. Expectations of a slowing U.S. economy, and with it more interest rate cuts, have grown significantly among institutional investors, as the chart on the following page depicts



Over half of the respondents to the Bank of America survey expect 3 or more Fed rate cuts in the next 12 months, with almost a third expecting 4 declines! That is a remarkable level of easing for an economy with stock markets at all-time highs and inflation tracking well above the 2% Fed target. This pace of rate decline suggests either an economy in recession or a central bank that has caved to political pressure and is acting at the direction of President Trump.

Either comes with serious consequences. Cutting interest rates aggressively to cushion a slowing economy will serve to create the stagflationary economic environment we expect. Cutting rates for political purposes will not only create stagflation but also compromise the integrity and influence of the Federal Reserve around the world.

We are mindful of the mistakes of Fed Chairman Burns in the 1970s, when his move to cut interest rates prematurely caused inflation to build to such an extent that it required the draconian measures of Paul Volcker and circa 20% interest rates to finally extinguish the raging fires of inflation. We hope that similar mistakes will not be repeated and that the current expectations of very aggressive rate cuts will not be met unless inflation recedes from its current elevated level.

The problems faced by the Federal Reserve and other major central banks are why we believe substantial market volatility cannot be avoided. A decision by central banks to prevent inflation from running out of control will force them to keep interest rates higher during a period of economic slowing, thereby amplifying the effects of a recession. In this case, inflation may be brought under control, but at the price of economic hardship and a bear market in stocks.

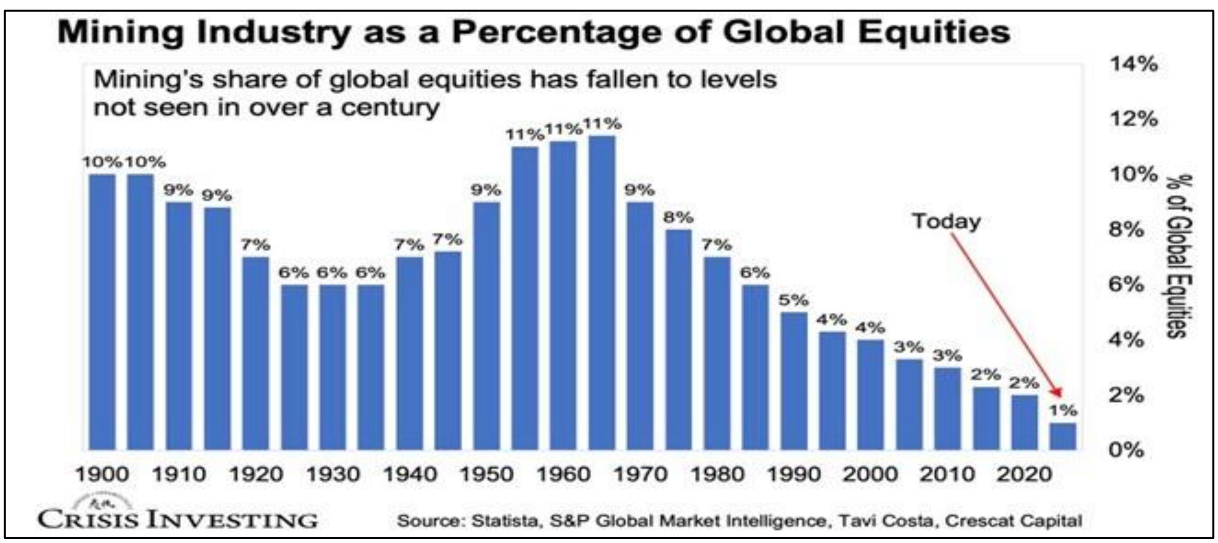
A decision to address the slowing of economic growth with aggressive interest rate declines, while ignoring the effects on inflation, will create the type of environment seen in the 1970s (which was the most severe bear market in stocks since the 1930s, when inflation is considered). In this scenario, actions such as those taken by Volcker will eventually be needed to reset the economic landscape.

We see no way to avoid serious economic and market turbulence ahead.

CURRENT INVESTMENT ENVIRONMENT

As sobering as the comments above may be, we are far more excited about the prospects of the opportunities that will be presented by the volatility we believe will characterise the investment landscape in the years ahead. Certainly, there will be considerable risks, but we believe our use of protective sell prices and the occasional short sale, if warranted, will minimise potential risks and provide profit opportunities.

Volatility will produce opportunities by shaking investor complacency and replacing it with fear, which will serve to drive markets to extremes and create attractive risk/reward entry points. If we are correct in our thesis that we are entering a period of stagflation similar to that of the 1970s, the process will create opportunities that will not be restricted to equity and fixed income markets but include commodities. The significant profits we have realised with precious metals may be an early indication of developing trends in commodities. It has been an unloved sector for some time, as the following chart illustrates.



Mining company shares as a percentage of global equities have fallen from 4% at the turn of the century to 1%, a decline of 75%! While the decline is not surprising given the relentless growth in influence of technology shares on global markets, the extent suggests investor capitulation and eventual opportunity.

We hasten to add that we are not advocating the purchase of mining shares at this point, but it is a sector that we are monitoring and will introduce for the consideration of subscribers if warranted.

As difficult an investing environment as the 1970s was for the majority of investors, it proved very profitable for alert, serious investors. As challenging as our current times are, we remain optimistic that the pragmatic approach we practice in these pages will continue to produce strong results.

EQUITIES COMMENT

S&P 500 (WEEKLY)

The S&P 500 closed the month at 6,688. Our full position, established in June at 6,190, now shows a gain of 8.1%. In response to the September gains, we have raised our protective sell price from 6295 to 6540.

The S&P 500 chart appears to be the picture of bullishness….but there are warning signs. Aside from the negative history of equities in October, the stretched market valuation and rampant investor complacency are cause for concern.

The market's steep rise since the spring makes the S&P vulnerable to a sharp pullback/correction. As well, the price volatility during the rise has contracted significantly, which suggests that a period of above-average volatility can be expected (given the strong mean-reverting tendency of volatility). The extended nature of the market and other factors mentioned suggest that the anticipated volatility will be to the downside.

We are happy to participate in this strong rally by the S&P 500 as long as it lasts, but we are mindful of its high-risk nature and take comfort in the presence of our protective sell price. Our concern that an October pullback by the S&P 500 may become substantial will prompt us to establish a full short position in the S&P 500 should our sell price be triggered. In the event a short position is established, we will set an initial buy price about 2.5% above our short sale price.

HEALTH CARE TRADE

HEALTH CARE SPDR ETF (XLV) (WEEKLY)

The Health Care Select Sector SPDR (XLV) closed September at 139.17, breaking above our trigger level of 139. This move activated our plan to initiate a half position, which was purchased at 139.15. Our initial protective sell price was set at 135.95. The breakout confirms the bullish pattern suggested by the double bottom established earlier in the summer.

Sector leadership remains concentrated in a handful of mega-cap names, with Eli Lilly again central to the narrative as new GLP-1 trial data extended the diabetes and obesity drug theme. Positive flows into health care ETFs reflect renewed investor interest, particularly as valuations across the group are attractive compared to historical norms.

The defensive nature of the sector has also returned to focus. With macro uncertainty still elevated and equity indices vulnerable to volatility, health care's combination of stability and secular growth appeal is increasingly attractive. Capital inflows through September suggest that long-term investors are positioning in advance of potential market turbulence.

With technicals strengthening and fundamental tailwinds intact, we are comfortable with our position and prepared to adjust our protective sell price higher should upward momentum continue.

FTSE 100 (DAILY)

The FTSE 100, represented here by the HUKX.L ETF, closed September at 9,349, extending its uptrend with a 1.4% gain for the month. Our half position, initiated in July at 8,925, now shows a return of 4.7%. With price action continuing to result in incremental new highs, we are comfortable maintaining the trade while keeping discipline through a protective sell stop, which remains at 8,975, to ensure the position does not slip into loss should market conditions reverse.

The Bank of England's (BOE) early-August rate cut provided the initial catalyst for the breakout, though the BOE voted to hold rates steady at its September meeting while agreeing to reduce the pace of its Quantitative Tightening program. September brought further confirmation of an economy showing tentative signs of improvement. PMI data and a rebound in consumer indicators suggested a firmer footing than seen earlier. Sterling weakness has also been supportive, enhancing the competitiveness of the FTSE's export-heavy constituents.

That said, risks remain. The August inflation reading of 3.8% has complicated the policy outlook for the BOE. While further easing remains possible, particularly if the pound strengthens and growth momentum falters, policymakers remain constrained by the danger of reigniting price pressures. For now, the BOE appears committed to a gradual path that balances growth support with inflation vigilance.

While our half position reflects caution toward this market, the market's resilience justifies continued participation.

DAX INDEX (WEEKLY)

The DAX closed September at 23,881, down slightly from August and extending the sideways-to-lower trend that has prevailed since early summer. Our position, established in May at 23,550, shows only a modest gain of 1.4%. Given the lack of progress, we continue to maintain our protective sell price at 23,300 to guard against the possibility that the current consolidation pattern breaks to the downside.

The index remains technically constructive, holding above its 40-week moving average, but the failure to generate upside momentum reflects both domestic and external headwinds. The sharp rally earlier in the year was led by the defence sector and SAP, yet both spent September consolidating or correcting from prior advances. In addition, trading volume has contracted further, suggesting that investor conviction is limited as the market awaits a clearer catalyst. Historically, such compression tends to precede a decisive move, though the ultimate direction remains uncertain.

Structural change in the DAX is also noteworthy. As the Goldman Sachs data illustrates in the chart on the following page, the auto sector's weight in the index has fallen to record lows, while technology now represents a larger share of the market. This evolution reduces reliance on Germany's traditional export engines but also increases exposure to the fortunes of global tech.

Exhibit 7: New economy sectors such as Tech now account for a larger share of the German market
Sector weight as a share of German market (%)

Source: Datastream, Goldman Sachs Global Investment Research

Policy support from Berlin's fiscal stimulus remains a positive backdrop, though it has yet to offset persistent economic weakness and the drag from trade frictions. A firmer euro adds to the challenge for Germany's exporters, leaving the broader economy vulnerable to a less trade-competitive currency.

We remain invested, but cautious. The DAX's inability to build on earlier gains underscores the fragile equilibrium in European equities. A triggering of our protective sell price would prompt us to exit, while a sustained push higher would likely signal the next phase of the rally.

CAC 40 (WEEKLY)

The CAC 40 closed September at 7,896, continuing the sideways consolidation that has characterised trading since the spring. The index remains rangebound between 7,600 and 8,200, with the 10-week moving average (7,801) and 40-week moving average (7,772) converging to underline the lack of clear directional momentum. This extended period of congestion follows the strong advance of 2023, which carried the French benchmark to successive record highs before stalling out.

Domestic conditions in France remain mixed. On the positive side, corporate earnings in several key sectors have exceeded expectations. Valuations, while not cheap, compare favourably to U.S. peers, helping to sustain foreign investor interest.

Offsetting these positives are persistent concerns over sluggish eurozone growth, geopolitical uncertainty, and vulnerability to global trade frictions, all of which keep investors cautious about committing aggressively. As in other European markets, energy price volatility and fiscal strains remain a latent headwind.

At present, the CAC 40 appears to be building a base, and a sustained breakout above 8,200 would signal renewed momentum and prompt us to purchase a full position. Until then, we are content to watch developments unfold from the sidelines.

NIKKEI INDEX (WEEKLY)

The Nikkei closed September at 44,933, consolidating just below its recent high that followed the August breakout above the 2024 peak. Our full position purchased in August at 42,570 has accrued a satisfactory return of 5.6%. We have raised our protective sell price in response to the Nikkei's appreciation from 41,400 to 42,900 to guarantee, at worst, a small gain on the position.

The drivers of strength remained broadly intact through the month. The yen's ongoing weakness provided continued support for exporters, while the lighter-than-expected U.S. tariffs on Japanese goods in August helped reduce trade concerns. Structural demand from Japanese households via the expanded NISA framework and steady foreign inflows reinforced market resilience.

Although global uncertainty persists, the Nikkei's strong relative performance underscores Japan's improving equity story. If these supportive factors remain in place, the market appears well-positioned to sustain higher levels.

SENSEX (WEEKLY)

The Sensex closed September at 80,268, continuing the sideways pattern that has dominated trading for much of the year. The index remains rangebound between 78,000 and 83,000, with both the 10- and 40-week moving averages converging, underscoring the market's lack of directional conviction. This consolidation follows the strong multi-year advance that carried the Sensex to repeated record highs in 2023 and early 2024.

Positive domestic factors remain in play. Inflation readings have moderated, corporate earnings reports have generally been supportive, and robust domestic capital inflows continue to provide a foundation of demand for Indian equities. These elements reflect the structural strength of India's economy, which remains among the fastest-growing major economies in the world.

Countering these positives, foreign investors withdrew an estimated \$3–\$4 billion in September, partly in response to the imposition of punitive U.S. tariffs on Indian goods. This underscores India's vulnerability to shifting global trade dynamics, even as local investors remain committed.

Our long-term outlook for Indian equities remains bullish, and the Sensex has been a consistent source of profitable opportunities for our subscribers. At present, however, we prefer to wait for confirmation in the form of a breakout to new highs before re-establishing exposure. Until then, we are content to observe from the sidelines.

EMERGING MARKETS ETF (EEM) (WEEKLY)

Our position in the EEM ETF, purchased in April at $43.27, continued to advance in September, closing the month at $53.40 for a gain of 23.5%. The ETF has now broken decisively above major technical resistance at circa $51. We have raised our protective sell price from $47.45 to $50.75. A decline back through $51 would be technically bearish and suggest a high probability of a change of trend. Our new selling price is designed to guard against a trend change while retaining most of our 23.5% accrued profits in the position.

As noted previously, the performance of EEM is heavily influenced by Chinese and Indian equities, particularly mega-cap Chinese tech companies, Taiwan Semiconductor, and large Indian financial institutions. These components continued to provide leadership in September, though volatility in Chinese macro data remains a source of investor caution.

The dollar’s weakness has been a tailwind, supporting foreign capital inflows into emerging markets. In addition, relative valuations remain attractive compared to developed markets, and investors are positioning for further upside as long as the consensus expectation for a softer dollar holds.

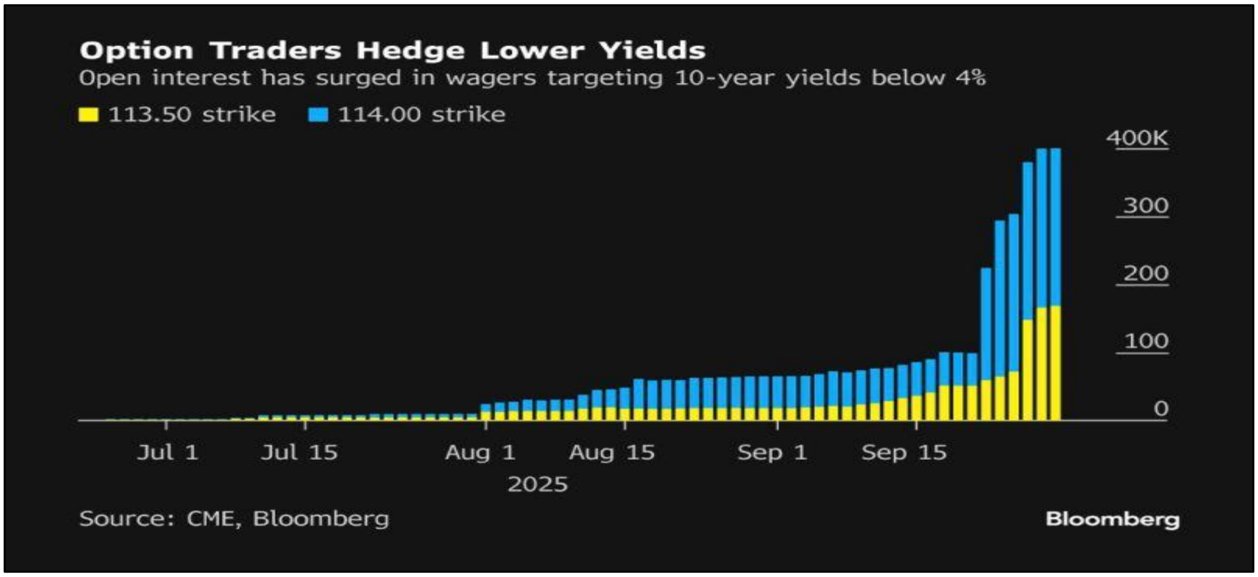
Nonetheless, risks remain considerable. Shifts in U.S. policy, renewed geopolitical tensions, or domestic instability in key emerging economies could quickly alter sentiment. For now, we remain content to participate in the bullish trend while maintaining discipline through our protective stop.

FIXED INCOME COMMENT

10-YEAR US TREASURY NOTE (WEEKLY)

The 10-year Treasury note ended September at 112.52, continuing its modest recovery from last year's lows. The price remains above its 40-week moving average (110.87) and has now edged through the 10-week average (112.45), suggesting a bullish tone and a slow but steady improvement in technical momentum. After a prolonged bear market that pushed yields to multi-year highs, the note has entered a consolidation phase that reflects shifting expectations for monetary policy and growth.

The Federal Reserve's September rate cut and the market's expectations of a series of further rate reductions have been important factors behind the falling 10-year Treasury yields. While the pace of easing has thus far been measured, it has altered the balance of risks in that markets are now more concerned about negative economic surprises than inflation re-accelerating. This is consistent with the surge in options activity betting on yields moving below 4 per cent, which has driven hedging demand across the curve (chart on the following page).



Markets have an uncanny ability to signal change well before it becomes obvious in the data. In recent weeks, a surge in options activity has drawn attention to the bond market, where traders have placed large wagers on U.S. 10-year yields falling below 4 per cent. Open interest at the 113.50 and 114.00 strike levels has risen sharply since August, highlighting a clear investor preference for hedging against lower yields.

History shows that such concentrated positioning often reflects both fear and conviction. In 2019, traders aggressively positioned themselves for falling yields as growth concerns mounted, anticipating the Fed's eventual pivot. More dramatically, during the 2008 crisis, similar hedging activity preceded one of the sharpest declines in yields on record as investors sought safety. In each case, the options market served as an early warning system for a broader shift in sentiment.

The implications for today's investors are significant. This build-up of hedging suggests that the market is preparing for weaker economic data, more aggressive policy easing by the Federal Reserve, or a flight to quality sparked by geopolitical or financial stress. The fact that positioning has accelerated since early September indicates that conviction is building, not fading.

Our view has been to expect higher yields in response to building inflationary pressures associated with a stagflationary economic environment. We continue to anticipate stagflation in the years ahead. However, the combination of building evidence of a recession and the potential for a pullback/correction in equity markets that would drive demand for Treasuries prompts us to expect further downward pressure on yields (higher Treasury prices) in the near-term.

CURRENCY COMMENT

US DOLLAR INDEX (DXY) (WEEKLY)

After a sharp decline earlier in the year, the U.S. Dollar Index (DXY) declined modestly in September and appears to be stabilising in the high 90s. The posting of a bullish weekly reversal bar in September increases the probability of a near-term rally.

The Federal Reserve's interest rate cuts have narrowed the positive rate differential that supported the dollar during the tightening cycle of 2022–23, which put downward pressure on the dollar. The relative strength of the U.S. economy has served to cushion the downside.

The initiation of a global trade war by the Trump Administration should have resulted in a stronger dollar, as its principal trading partners devalued their currencies to offset some of the effects of the tariffs. That the dollar has, instead, weakened is noteworthy and suggests that a reassessment of the role of the dollar may be underway. This prospect is supported by the strength of the euro and gold in 2025.

The lack of a compelling alternative to the dollar as the world's reserve currency has likely prevented the decline of the dollar from being more dramatic. The relative strength of the euro and gold in 2025 may be early signs of a change of perception in the role of the dollar as the reserve currency by the global community.

The secular trend remains bearish, though a near-term rally would not be surprising.

CAD/USD (WEEKLY)

The Canadian dollar continued its recent decline versus its U.S. counterpart following a mid-year reversal that challenged major technical resistance at circa .74.

The weakness displayed by the Canadian currency has been anticipated. The Canadian economy will be relatively more affected than that of the U.S. by the trade war, with a weaker dollar being in Canada's interest from a trade perspective. While the Bank of Canada (BOC) has broadly matched the actions of the Federal Reserve on interest rate changes, we expect the BOC to become more aggressive with rate cuts on evidence of significant weakness in the Canadian economy. We believe the BOC will seek to devalue the currency, though that has proven difficult given the weakness demonstrated by the U.S. dollar itself in 2025.

We expect to see continued weakness from the Canadian dollar, weakness that could see it decline to test the 2025 price low in the event of a significant recession in the Canadian economy.

EUR/USD (WEEKLY)

The euro ended September trading at $1.175 versus the dollar, little changed from the prior month. September trading featured strength by the euro in the first half of the month, followed by a subsequent retreat. The euro continues to trade in a consolidation pattern that is growing progressively narrower, indicating that a breakout may be near at hand. The presence of a bearish daily reversal bar in September suggests that a potential breakout out of the trading channel is more likely lower, which would be consistent with our expectation of near-term strength in the dollar.

Interest rate differentials will play a key role going forward. The European Central Bank (ECB) appears to be intent on proceeding in a measured way with interest rate cuts, being mindful of inflationary pressures remaining stubbornly elevated. Markets have interpreted the September rate cut by the Federal Reserve (Fed) as the first of an aggressive series, though inflation considerations may curtail the ultimate number of Fed rate cuts. A more favourable interest rate differential for the euro would put upward pressure on the currency, which is not seen as desirable for the ECB because of the negative trade implications.

The longer-term value of the euro versus the dollar will be determined by the actions of the respective central banks and the perception of the dollar as a safe-haven for capital. Major technical resistance exists at circa 1.23, while 1.12 represents an important support level. A decline in the euro below 1.12 would be decidedly bearish and suggest a change of trend.

A short-term pullback by the euro would not be surprising.

POUND/USD (WEEKLY)

The British pound fell slightly versus the U.S. dollar in September, ending the month in the middle of the trading range it has occupied for the past several months.

The pound's performance has been shaped by shifting expectations for Bank of England (BOE) policy. Inflation has moderated but remains above target, leaving the BOE cautious about aggressive easing even as the Federal Reserve indicates it may be entertaining a series of interest rate cuts. This relatively more moderate policy stance has lent support to sterling, though slowing U.K. growth and lingering fiscal concerns limit upside momentum.

September also brought renewed sensitivity to energy prices and trade developments. The U.K.'s exposure to imported energy costs leaves sterling vulnerable to volatility in oil and gas markets. Meanwhile, ongoing uncertainty over post-Brexit trade relations and weak consumer demand continue to weigh on investor sentiment toward the U.K. economy.

From a technical perspective, the pound continues to trade bullishly above its 40-week moving average. Worth noting is the bearish weekly reversal bar posted in September, which raises the probability that the resolution of the current sideways trading channel will be a weaker pound.

The pound, as with most other currencies, owes more of its 2025 price strength to a weaker dollar than to its own specific merits. We remain both short and long-term bears on the prospects for the pound.

YEN/USD (WEEKLY)

The yen ended September little changed over the previous month, with the currency testing the 150 level before strengthening to end the month. Central bank policy remains the dominant influence on the value of the yen.

The Bank of Japan (BOJ) has begun cautiously moving away from its ultra-loose monetary stance, signalling a willingness to normalise policy after decades of near-zero rates. However, progress has been gradual, and Japanese yields remain far below those in the U.S. The Federal Reserve's September rate cut has narrowed the interest-rate gap slightly, but the dollar continues to enjoy a significant yield advantage. This divergence explains why the yen, despite being undervalued on many measures, has struggled to mount a durable recovery.

In September, volatility was heightened by speculation over potential BOJ intervention should the yen weaken materially beyond 150. Authorities remain sensitive to rapid depreciation, but their ability to counter structural yield differentials is limited.

Looking ahead, the yen's prospects depend largely on the Fed's easing trajectory. A more aggressive U.S. rate-cutting cycle would serve to put downward pressure on the yen.

From a technical perspective, the yen chart features a potential bullish flag formation that suggests higher prices ahead. A much stronger yen would not be seen as desirable by the BOJ, given its negative impact on trade competitiveness and could prompt a return to a looser monetary policy.

OIL COMMENT

CRUDE OIL (WTI) (WEEKLY)

WTI crude prices weakened in September, closing the month at $62.55 after retreating nearly 5% in the final week. The decline marked a failure to sustain gains above the 40-week moving average (currently near $66.65) and leaves WTI testing support in the low-$60s. From a broader perspective, oil has been in a steady downtrend since mid-2022, with each rally capped at progressively lower levels, a reflection of persistent supply pressure and inconsistent demand.

On the supply side, OPEC+'s moves to ease voluntary production cuts were a key factor weighing on sentiment. The prospect of additional barrels hitting the market comes at a time when U.S. shale output remains robust, providing a steady counterweight to attempts at cartel discipline. Russia's curbs on refined product exports briefly underpinned prices but were insufficient to alter the broader trend.

Demand signals offered little relief. While the U.S. economy has remained resilient, consumption data in Asia pointed to softer industrial activity, with OECD inventory reports confirming the divergence. Crude stocks showed draws, but gasoline and distillate inventories built, suggesting weaker end-use demand.

Looking ahead, the balance of risks for WTI tilts modestly to the downside. Unless OPEC+ restores discipline or a geopolitical disruption curtails supply, the market appears vulnerable to further tests of support at around $60. The EIA (the U.S. Energy Information Administration) projects WTI to average in the mid-$60s into year-end, but without a clear recovery in demand, rallies are likely to be capped by steady growth in U.S. supply.

Volatility is expected to persist, with geopolitical risks cushioning the downside but limited potential for a sustained rally.

ENERGY SELECT SPDR FUND (XLE)

The Energy Select Sector SPDR (XLE) ended September at $89.34, easing from recent highs but holding above both its 10 and 40-week moving averages. This resilience is in contrast with the weakness in WTI, highlighting the role played by the general strength of the stock market in supporting energy shares despite weakness in the underlying commodity.

The sector has effectively consolidated since early 2023, with a broad trading range providing a base for a major breakout to new price highs with an increase in oil prices. As always, we are prepared to purchase a full position in XLE on a breakout to a new high, placing our initial protective sell price about 2.5% below the previous price high. The protracted consolidation period of XLE suggests that when a breakout eventually occurs, the upside could be considerable.

DEFENCE SECTOR COMMENT

US AEROSPACE & DEFENCE ETF (ITA) (WEEKLY)

The ITA ETF, our proxy for participation in the U.S. defence sector, broke out of its recent consolidation pattern to finish higher for the month at $ 209.26. The return on our latest position in ITA, purchased in May at $161.10, is now 29.9%. At this juncture, we are raising our protective sell price from $190 to $195.

The fundamental prospects for the defence sector remain strong. In September, the House and Senate moved forward with their versions of the FY-26 defence bill, preserving an ~$893 billion topline and introducing reforms designed to speed procurement. This is a constructive backdrop for U.S. defence contractors. Noteworthy is the Pentagon's call for industry to double, or even quadruple, production of key missile systems, which underscores the priority being placed on replenishing depleted inventories. These initiatives directly benefit companies such as Lockheed Martin, RTX, and General Dynamics.

Contract flow during September was significant. Lockheed Martin secured an $11 billion U.S. Navy award for up to 99 CH-53K heavy-lift helicopters, while additional funding was provided to sustain the production tempo of the F-35 program. RTX won a $1.7 billion contract for its next-generation radar systems, highlighting the enduring demand for layered air defence among NATO members.

The political dimension also continues to merit close attention. The Trump Administration appears intent on linking the purchase of U.S. weapon systems to more favourable trade terms. While this strategy risks encouraging NATO allies to look more seriously at European alternatives, the breadth and quality of U.S. offerings should ensure continued strong export demand.

We remain bullish on ITA. The combination of rising procurement budgets, urgent missile demand, and the structural need to modernise weapons platforms argues for further growth in revenues and earnings across the sector. As positive as we are on the defence sector, we take comfort in the presence of our protective sell price.

EUROPEAN AEROSPACE & DEFENCE ETF (EUAD) (WEEKLY)

From last month's issue, *"The relatively low daily trading volume was especially apparent in August, which may indicate a lack of negative investor sentiment (which increases the odds of a breakout to new highs if bullish sentiment again asserts itself)."*

The EUAD ETF, our proxy for the European defence industry, did indeed break out of its consolidation pattern and advance strongly in September. EUAD benefited from renewed urgency within NATO following drone incursions into Polish and Romanian airspace, which provided the catalyst for the breakout. The ETF rallied over 7% in the days surrounding these events, illustrating the degree to which geopolitical shocks are now feeding directly into equity performance across the sector.

The long-term backdrop for European defence spending remains highly positive. Rising uncertainty over the durability of American security guarantees has accelerated procurement decisions by NATO members, particularly in air defence and munitions. Unlike the U.S., where procurement processes are already well-established, Europe faces the task of rapidly scaling up industrial capacity, a challenge that provides a significant opportunity for the companies comprising EUAD.

EUAD continues to exhibit strongly bullish characteristics from both a fundamental and technical perspective. It remains an attractive vehicle for participation in the European defence sector for those who are comfortable with its less-than-ideal liquidity characteristics.

We do not hold a position in EUAD, as it doesn't meet our liquidity requirements. But if we did, we would set our protective sell price at $43.75 to guard against a failed breakout.

ROLLS ROYCE HOLDINGS PLC (RYCEY) (WEEKLY)

Rolls-Royce shares built further on their impressive recovery in September, supported by both improving fundamentals in its civil aerospace business and stronger investor recognition of the company's defence operations. The stock has been a prime beneficiary of the renewed investor appetite for European defence equities, which have outperformed their U.S. counterparts in recent months.

Our full position in RYCEY, purchased in May at $10.90, increased its accrued return to 48.6 % at the close of September trading. In response to the price appreciation of September, we have raised our protective sell price from $13.75 to $15.25.

The company has upgraded its guidance for 2025, reflecting improvements in profitability and cash flow, while its defence and power systems divisions are benefitting from sustained budget growth across NATO. There are valuation concerns, with some analysis suggesting the shares trade at a premium to intrinsic worth. However, given the multi-year tailwinds now at play in both commercial and defence markets, Rolls-Royce remains well positioned.

LEONARDO S.p.A. (FINMY) (WEEKLY)

The low volatility price consolidation pattern displayed by Leonardo, and shared by other European defence contractors, resolved itself with a sharp upward move in September, aided by the provocative testing of NATO airspace by Russia. We purchased a full position in Leonardo in late September at $31.75. We have set our initial protective sell price at $29.90.

The company has benefitted from rising European procurement, particularly in helicopters, avionics, and surveillance systems, while also signalling its intention to expand into cybersecurity and dual-use technologies, an important strategic pivot as warfare increasingly extends into digital domains.

Leonardo stands to be a major beneficiary of the push for European "strategic autonomy," as governments seek to reduce reliance on American suppliers. This theme is likely to support revenue growth for many years. Execution risks remain, particularly in managing expansion into new business lines, but the momentum of defence spending in Europe outweighs these concerns in the near term.

RHEINMETALL AG (RNMBY)(WEEKLY)

Our decision to exclude monthly coverage of Rheinmetall from monthly coverage expressed in the last issue proved to be very short-lived. The German defence giant soared to new price highs in September, aided in no small measure by the testing of NATO airspace by Russia. These provocative actions served to remind even the most complacent of the importance of prioritising the defence capabilities of European democracies.

The price breakout by RNMBY prompted us to purchase a full position again, this time at $442.25, with our initial protective sell price established at $429. Rheinmetall finished the month trading at $465.74, which produced a gain of 5.3% on our position. We raised our protective sell price on month-end from $429 to $443.25 to preclude the risk of loss on the position should the September breakout fail.

We don’t expect our current position in RNMBY to replicate the 139% gain in a few months achieved by the position held earlier this year, but believe that attractive gains are certainly achievable.

We must be mindful, however, that RNMBY and other European defence stocks have come a long way in a short time and are susceptible to pullbacks and consolidation periods, in addition to the vagaries of a tenuous global investment environment. The role of protective sell prices in preserving accrued profits and preventing significant losses has never been more important than in our current investment environment.

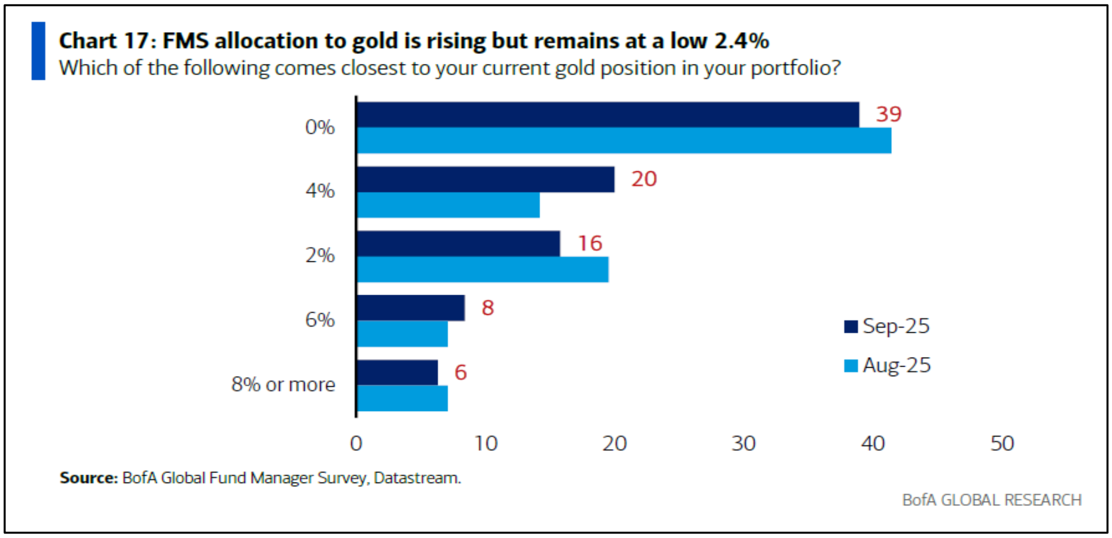
GOLD & SILVER COMMENTARY

GOLD (WEEKLY)

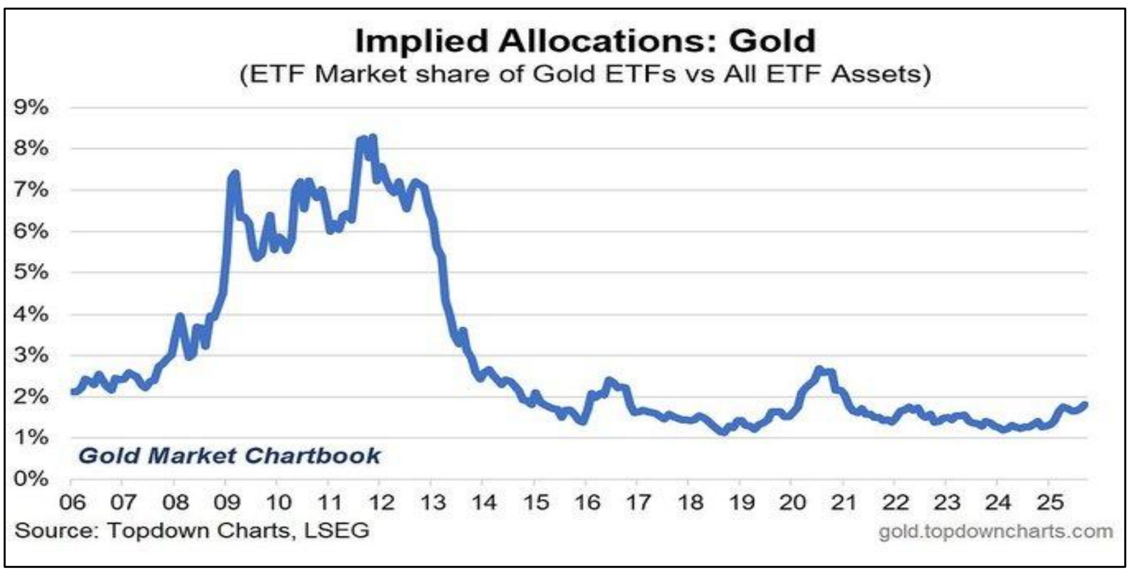
As we noted in the last issue**, "***We stand ready to purchase a new full position in gold on a breakout to a new 2025 price high. The next leg up in this market could be significant*."

The breakout to a new price high did occur early in the month, and we duly purchased a full position at $3512. We set our initial protective sell price at $3430, which is 2% below the previous high of $3500. In response to the sharp price rise in September, we adjusted our protective sell price upward to $3610, which sits just below the low of the mid-month consolidation pattern (which we view as technical support). The return on our latest position in gold at month-end is 9.7%. Our multiple positions in gold over the past year have produced handsome profits indeed.

Our previous experience and market history suggest that long-term peaks in the gold price require broad-based interest from investors, especially retail investors. The following two charts provide heartening reasons for gold bulls on that front.



The chart above illustrates the results of a survey of fund managers, which reveals that the average allocation to gold in portfolios remains a meagre 2.4%. Fully 39% of fund managers have no position in gold at all. The level of participation in gold and gold equities can be expected to rise with the gold price, providing capital flows to propel the gold market higher.



While the first chart reflected the activities of institutional investors, the chart above, which tracks ETF trends, is a more reliable depiction of activity by retail investors. Our contention that gold should be viewed as a barometer of investor anxiety rather than a hedge against inflation is supported by the behaviour of retail investors. Interest in gold ETFs quadrupled during and in the years following the 2008

Financial Crisis, then fell dramatically when enormous monetary stimulus restored a sense of calm to markets. Retail interest in gold ETFs rose again in response to the COVID pandemic before being cut short through the historic application of coordinated monetary and fiscal stimulus from central banks and governments around the world.

Not surprisingly, interest has been rising again of late with the increase in the price of gold. However, retail participation remains near historically low levels, leaving considerable scope for capital flows from the retail sector to drive gold prices higher in the final stages of the current bull market.

In summary, the potential upside for gold remains considerable. Not only is the gold chart bullish from a technical perspective, but the factors driving the investor anxiety that is pushing prices higher, economic and geopolitical uncertainty, remain in place. Finally, the low allocations to gold by both institutional and retail investors provide the potential fuel for a final 'blow-off' phase of the rally in gold prices.

However, we must also recognise that the price of gold has come a long way in a short period of time and may be prone to reversals, which is why we rely on protective sell prices. We much prefer taking large chunks of profit out of the rally, as we have done in the past, and to sit out price pullbacks and consolidation periods until the rally resumes. Therefore, we may enter and exit the gold market again before the current bull market ends.

For the time being, we are content to maintain our current long position in gold until market price action suggests otherwise.

VANECK GOLD MINERS ETF (GDX)(WEEKLY)

From last month's issue: *"A breakout by gold could propel GDX much higher. Therefore, we will purchase a full position in GDX if we establish a position in gold itself."*

Our purchase of a full position in gold in September prompted us to also establish a full position in GDX at $64.25. Our initial protective sell price was set at $62.75, which was about 2.5% below our purchase price. The subsequent strength demonstrated by GDX has prompted us to increase our protective sell level to $71.50, which is just below the low of the most recent price pullback (which we consider a level of technical support). The accrued profit on our initial position in GDX is 18.9 %.

We are at the stage of the bull move in gold where gold equities (and therefore, GDX) may well outperform the underlying metal as both institutional and retail investors seek a home for capital. The inherent leverage of equities to rising gold prices makes them particularly attractive to investors in the latter stages of market advances, when investor sentiment becomes the most bullish.

Our investment strategy with GDX will mirror that of gold; we will seek to participate in the bulk of price advances while sitting on the sidelines during pullbacks and consolidation periods.

SILVER (WEEKLY)

Our position in silver, purchased in June at $35.25, continued to exhibit notable strength in September. Silver closed the month trading at $46.63, which represents a 32.3% profit on our current position. The strength of the latest advance has more than made up for the small losses incurred in our previous purchases of failed breakouts.

The silver market had long been a source of frustration, but the tone of the recent price action suggests that the current rally may still have significant upside potential. In response to the price strength of September, we are raising our protective sell price from $37.50 to $43.75.

ABOUT THE EDITOR

The Editor and Publisher of the Global Investment Letter is Jonathan Baird CFA. Prior to founding the Global Investment Letter, Jonathan spent more than 25 years as an award-winning money manager in Canada, most recently winning a Lipper Award in 2010 for managing the #1 Global Equity Fund in Canada. Jonathan managed several #1 ranked funds over the course of his career as a money manager, investing in all major industries, asset classes and markets. Along with his interest in the world of investment, Jonathan has been a lifelong student of history and uses the lessons of history to help interpret and provide context to current events. Jonathan no longer invests money for others, managing only his own account. The Global Investment Letter represents his personal thoughts and opinions.

Jonathan well understands the difficulty of the investment process and the essential role that quality information and opinion play in successful investing. Each monthly issue will contain comments on major markets, economics, geopolitics as well as investment ideas. There may also be a discussion of investment philosophy or practices and reviews of books deemed of potential interest to readers.