

The February Outlook

Market Stance

CURRENT MARKET ENVIRONMENT

Equity market rotation continues

Commentary

- There was significant outperformance in January from the more cyclical parts of the equity market: materials, industrials, energy, emerging markets
- Dispersion also across the AI theme: software under extreme pressure, tech hardware holding up
- The dispersion within AI argues against a widespread bubble: unlike 1999/2000 a rising tide is not lifting all boats
- This has been validated in part by the tenor of macro data released in January, suggesting systematic upside surprises to economic growth

Upshot

- The market consensus which emerged towards the end of last year increasingly backed a soft landing narrative, so positive news may be in the price to some extent

GOLD

Strategic relevance in a portfolio context remains

Commentary

- Gold has fulfilled its role as a portfolio diversifier and hedge against increased geopolitical uncertainty
- However, gold's volatility has increased significantly in recent months, and it has been less of a "risk-off" trade
- Nevertheless, gold remains a very small component of private sector portfolios, and there is scope for additional central bank purchases

Upshot

- We think gold will continue to play an important role in multi asset portfolios, as a diversifier and hedge against elevated geopolitical uncertainty

EQUITY VALUATIONS

There has been a change in the structure of equity market pricing

Commentary

- The multiple of the global equity index has remained largely unchanged since the autumn
- However, the premium valuation of U.S. stocks has somewhat moderated
- This primarily reflects the re-rating of many markets outside the US in recent months, for many of whom P/E multiples have moved a bit above normal
- The important theme is PE multiple convergence: ex-US markets are less relatively attractive in valuation terms than they were

Upshot

- Longer term forecasts still suggesting positive real returns from equities, but with much smaller excess returns over fixed income than in the last decade

SARANAC MULTI-ASSET POSITIONING

Market environment

Commentary

- The soft-landing narrative lends itself to higher risk asset exposure, the valuation background points in the other direction
- Given these different pressures, positioning remains risk-aware, but not pessimistic
- Equities remain the largest contributor to risk, but cash weights are also very low, reflecting the significant exposure to alternative assets

Upshot

- Portfolio structure reflects the need to maintain exposure to market risk, but with sufficient diversification to allow for adequate returns to be realised in a more challenging market environment

 The Long Read

Checking in on the U.S. Consumer - Implications for Markets

SNAPSHOT

The outlook for the US consumer is becoming more nuanced as the forces that previously supported spending begin to ease and financial pressures build.

While households have remained resilient for several years, signs of softer demand, weakening sentiment and greater reliance on borrowing point to a gradual shift in behaviour that is now visible across both essential and discretionary categories. These pressures are not confined to the US and mirror broader global trends of slowing real income growth, tighter financial conditions and more cautious household decision making.

Although a sharp downturn is not our central expectation, the transition to a more constrained consumer environment is becoming increasingly evident and carries important implications for market dynamics, sector performance and portfolio positioning.

Anyone wanting to forecast the path of the global economy is usually well advised to start with the U.S. consumer – ultimately private consumption makes up almost 70% of U.S. GDP, which in turn accounts for approximately one quarter of global GDP. When American consumers spend freely, it supports corporate revenues, employment and investment, and it spills over into stronger global demand. When they retrench, the consequences are felt far beyond U.S. borders. Historically, sustained slowdowns in consumption have been a reliable precursor to broader economic weakness and market volatility. The financial health of U.S. households therefore matters a great deal to the economic outlook.

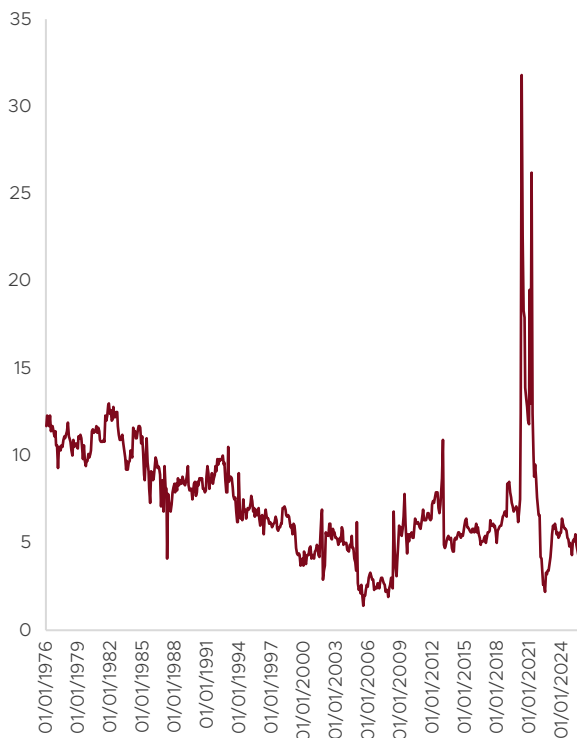
For much of the past few years, consumer spending remained remarkably resilient. Even as interest rates climbed and inflation eroded purchasing power, consumers continued to travel, dine out and buy discretionary goods. Real wage gains and a remarkably tight labour market provided a firm foundation, while excess savings accumulated during the pandemic offered an additional buffer. Many argued that this combination would allow households to weather higher rates indefinitely. Markets embraced this view, with equities holding up well and consumer-sensitive sectors proving more resilient than expected.

As we enter 2026, however, that narrative is increasingly being questioned, with some evidence emerging that suggests the consumer may be losing momentum. Real spending growth is slowing back towards trend, household debt burdens are rising, confidence remains fragile and labour-market conditions seem to be softening. This is particularly evident amongst lower-income households. Real personal consumption growth has slowed noticeably since late 2024 and has flattened in recent months. Consumers are still spending in nominal terms, but much of that growth reflects higher prices rather than increased volumes. This distinction matters, because it reveals a household sector that is increasingly constrained by rising costs.

The Long Read

CHART 1

US Personal Saving as a % of Disposable Income



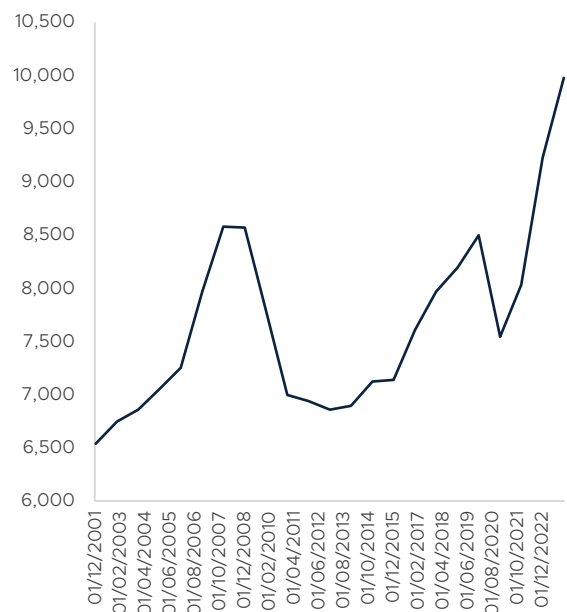
¹Source: Conference Board

Discretionary categories in particular are showing signs of fatigue. Big-ticket purchases, leisure spending and non-essential retail have weakened relative to essential goods. Travel demand, once a powerful post-pandemic tailwind, has begun to normalise. Even in services, which had been the most resilient segment of consumption, growth is moderating. These shifts suggest that households are becoming more selective and more cautious, prioritising necessities as financial pressure starts to build. At the same time, the balance-sheet support that sustained spending earlier in the cycle is fading also. Pandemic-era excess savings have largely been run down, especially among lower- and middle-income households.

With that buffer depleted, lower income consumers specifically are increasingly relying on credit to maintain living standards. Total household debt in the United States has reached record levels, driven primarily by rising credit card balances, auto loans and higher cost personal borrowing. Meanwhile interest payments on variable rate debt have surged, pushing debt-service ratios higher and squeezing disposable incomes.

CHART 2

US Credit Card Debt per US Household



²Source: U.S. Federal Reserve

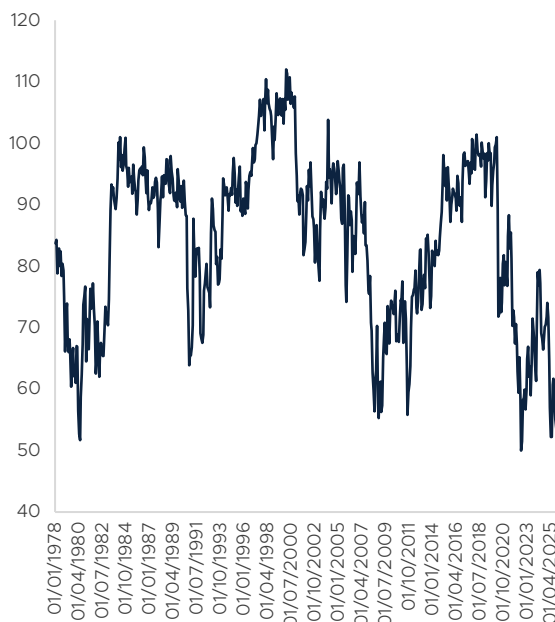
The composition of this debt is particularly concerning. Credit-card borrowing, which carries some of the highest interest rates, has grown rapidly. Delinquency rates, while still moderate by historical standards, are trending higher, especially among younger and lower-income borrowers. Auto loan delinquencies are also on the rise, reflecting both higher interest rates and elevated car prices.

The Long Read

Unsurprisingly, consumer sentiment has become more pessimistic over the last year, with households expressing persistent concerns about inflation, job security and the broader economic outlook. Although confidence has rebounded modestly from its post-pandemic lows, it remains far below levels typically associated with strong consumption growth. The current disconnect between weaker confidence yet still positive spending is unlikely to persist indefinitely. Historically, when sentiment weakens, spending often follows suit.

CHART 3

UoM Consumer Confidence



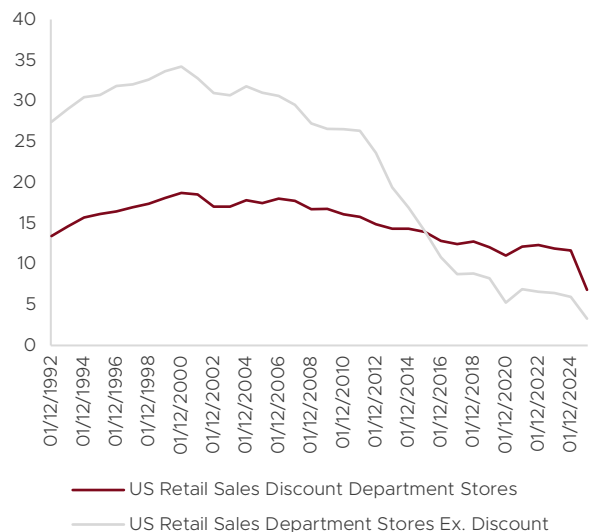
³Source: University of Michigan

Importantly, the more pessimistic mood is predominantly a theme amongst poorer households. This K-shaped pattern, in which higher-income households continue to spend comfortably while lower-income households struggle, has become a more dominant feature of the U.S. economy in recent decades.

Wealthier consumers, supported by asset price gains, strong income growth and residual savings, remain relatively insulated from rising borrowing costs and inflation. Their spending on premium goods, luxury travel and high-end services has held up well. Whether this is enough to support broader consumption is debatable however, given lower-income households account for a significant share of marginal consumption, and their retrenchment poses a meaningful risk to overall spending growth. The retail sector illustrates this dynamic rather well. While headline retail sales have not collapsed, the composition of spending has shifted. Discount retailers and value-oriented brands are gaining market share, while traditional mid-market chains and discretionary categories are under pressure. A wave of store closures across the U.S. reflects not only the ongoing shift toward e-commerce but also genuine weakness in physical retail demand. These closures point to overcapacity in the sector and to a consumer that is becoming increasingly price sensitive.

CHART 4

US Retail Sales



⁴Source: U.S. Census Bureau

 The Long Read

The labour market, long the backbone of consumer resilience, is also showing signs of cooling. Job growth has slowed, hiring intentions have dropped and layoffs have picked up in certain sectors, particularly technology, finance and parts of manufacturing. While unemployment remains low by historical standards, the direction of travel is clearly less favourable than it was a year ago. Wage growth, too, is decelerating, reducing the pace at which real incomes can rise. This matters because labour market conditions are perhaps the dominant drivers of consumer spending intentions. When job security weakens and income growth slows, consumers become more cautious, defer discretionary purchases and build precautionary savings. Even small changes in employment sentiment can have outsized effects on spending, especially when households are already financially stretched. A modest rise in unemployment or a further slowdown in wage growth could therefore tip consumer behaviour more meaningfully.

Beyond the labour market, the rate of inflation is the other determining factor in consumer behaviour. While price pressures have eased from their post-pandemic peaks, inflation remains above the Federal Reserve's 2% target and has proven stickier than policymakers had hoped. With current levels of inflation inconsistent with a rapid return to price stability, the scope for aggressive interest-rate cuts is limited which ultimately prolongs the period during which households must contend with elevated borrowing costs. But exactly how desirable is a swift return to inflation rates at or below 2%? Clearly it depends on whether the disinflationary dynamic is demand or supply side driven. Weakening consumer demand poses a clear downside risk to growth, as even a modest deceleration in spending growth can have a sizable impact on overall economic output via the negative feedback loop of reduced services sector activity, slower growth in corporate earnings and an increase in the unemployment rate.

Although this article focuses primarily on the U.S., an increasingly strained consumer is not purely a U.S.

phenomenon. In the UK and across Europe, households are grappling with the lingering effects of high energy costs, elevated mortgage rates and fiscal tightening, largely via a higher tax burden. Consumer confidence remains weak, and real incomes are only slowly recovering. In Japan and China, weak domestic demand has prompted renewed policy support, while in many emerging economies, tighter global financial conditions and weaker trade growth are constraining household spending also. All this underscores a broader global theme. After years of extraordinary fiscal and monetary support, households in advanced economies are entering a more constrained phase of the cycle. Savings buffers are depleted, borrowing costs are high and real income growth is slowing. While this adjustment is unfolding gradually, its cumulative effects are becoming increasingly visible in the data.

On balance, a more pronounced economic slowdown is not our central scenario, not least because other parts of the global economy continue to hold up. Global manufacturing shows signs of turning a corner, the technology led investment cycle is in full swing, while artificial intelligence may eventually provide a meaningful boost to productivity. In any case, the implications of a deteriorating U.S. consumer for financial markets will be quite nuanced and largely depend on the pace and depth of such contraction. Within equities, consumer staples companies and discount retailers may well benefit from a more price sensitive consumer, while discretionary sectors such as travel, leisure and luxury goods likely fare worse. Banks will have to content with slower loan growth and rising delinquencies while lower interest rates may put more pressure on margins. Bond markets on the other hand likely stand to gain if a weaker consumer accelerates the move toward easier monetary policy. Falling inflation expectations and slower growth would support government bonds and high quality credit, notwithstanding a deterioration in the fiscal outlook.

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