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The Reshaping of a Political and Economic Orthodoxy

Diagnosis and Implications for Capital Markets

Global bond yields are rising to the point that policymakers are justifiably panicking. But bond yields are the *symptom*, not the cause. This analysis lays out what that means for the next cycle: the choices that built the problem, the choices required to resolve it, and the new economic orthodoxy that will reshape the winners and losers of the next cycle.

PART 1

End of an Orthodoxy

Diagnosis, sequence, cause

PART 2

The Mechanism of Regime Change

Choice, institutions, politics, geopolitics, technology

PART 3

What It Means for Markets

Back up the curve, into liquidity, into being paid for risk

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PART 1

End of an Orthodoxy

Diagnosis, sequence, cause, and the diminishing marginal returns that defined it

Executive Summary

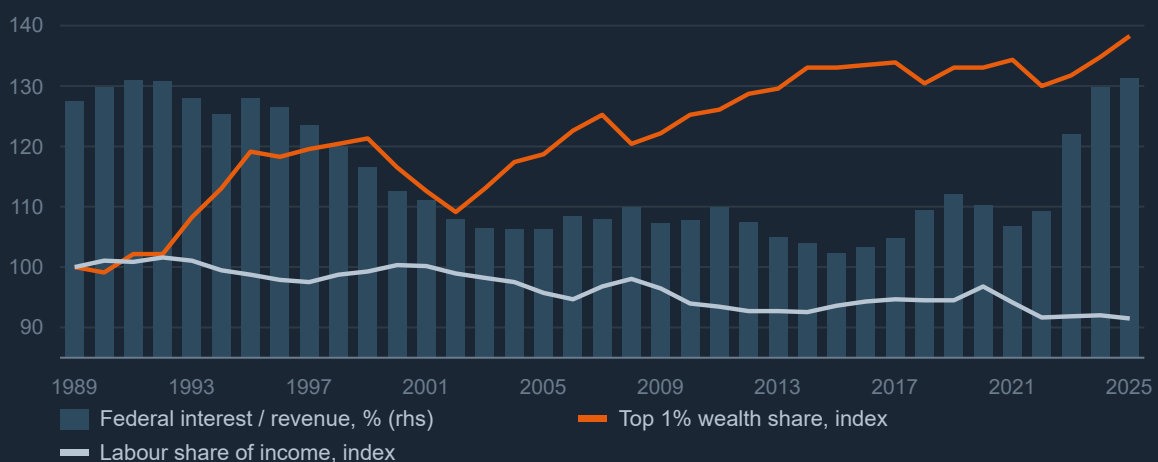
Global bond yields have risen to levels that are increasingly constraining policymakers. Yet higher yields are better understood as a symptom of deeper structural forces than as the root cause of the problem. Three factors have contributed to this backdrop. First, fiscal policy in many advanced economies has become progressively less disciplined over the past two decades. In the United States, **the lapse of statutory PAYGO in the early 2000s marked an important shift**, followed by a succession of tax cuts, crisis interventions, entitlement expansions and pandemic-related spending measures that were only partially offset elsewhere in the fiscal framework. Similar trends have been evident across much of the developed world, leaving governments with structurally higher borrowing requirements.

Second, economic policy has increasingly relied on asset appreciation and financial conditions to support growth, while the returns to capital have significantly outpaced those to labour. Over time, this combination has contributed to rising inequality, weaker productivity growth and a greater dependence on policy support. As a result, economic downturns have often required larger and more sustained interventions than in previous decades.

Third, the post-war international order is becoming more fragmented. Rising geopolitical competition, trade tensions and growing security concerns are encouraging governments to devote greater resources to defence, industrial policy and economic resilience. While these objectives may be strategically justified, they also add to fiscal pressures at a time when public balance sheets are already stretched. Taken together, these forces help explain why bond markets are increasingly questioning the sustainability of existing policy trajectories. The longer these underlying imbalances persist, the more difficult the required fiscal and structural adjustments become, particularly in an environment of heightened political polarisation and electoral uncertainty.

CHART 1 Wealth effect in action – growing interest expense becoming a headwind

Top 1% share of total wealth vs labour share of income, index 1989 = 100; federal net interest as % of revenue (rhs)



Source: Office of Management and Budget, Historical Tables, Budget of the United States Government FY2027; BEA NIPA (FRED), wages & salaries + GDI and corporate profits w/ IVA & CCAAdj + GDI, quarterly, as at 01/09/26.

Some might argue that markets should be more concerned about inflation than they currently appear to be — long-term inflation expectations have stayed elevated but broadly stable. But what we actually see is a stagnant labour market, rising youth and graduate unemployment, real wage growth turning negative again, consumer confidence at recessionary levels, and voters across the developed world increasingly rejecting incumbents. **The bond market and the electorate may be reacting to the same underlying problem: an economic model that no longer delivers sufficiently broad-based growth and is becoming ever more reliant on debt and policy support.**

Recent market concern may reflect a delayed recognition of these pressures rather than an overreaction. Policymakers spent years relying on QE, ZIRP, forward guidance, yield-curve control and targeted balance-sheet operations instead of addressing deeper structural challenges. Even Mario Draghi, one of the era's architects, has argued that such tools buy time but do not resolve underlying weaknesses: his European competitiveness report calls for the structural and supply-side reforms that two decades of monetary experimentation largely postponed. Voters have repeatedly expressed dissatisfaction through Brexit, Trump and now the AfD in Germany, but these movements have generally proved more effective at articulating grievances than delivering durable solutions. Few of the underlying policy choices have meaningfully changed.

The adjustment process is already underway. It is unlikely to proceed in a straight line, and further policy mistakes may be made in pursuit of short-term political goals. Yet politicians who test market confidence often face tight constraints, as illustrated by Liz Truss's experience in 2022. Populist movements may continue to gain ground across the developed world, but financial markets are likely to remain an important check on policy choices. The Federal Reserve is reassessing aspects of its policy framework, regulators are paying closer attention to market concentration, and concerns around fiscal sustainability are moving back to the centre of economic debate. This shift in priorities was probably inevitable; the AI boom may simply have delayed it. **Many investors remain positioned for a continuation of the previous regime, leaving markets exposed to elevated concentration, weaker liquidity and valuations built for a world that may no longer exist.**

Stability breeds instability — the end game

Hyman Minsky argued that calm markets manufacture their own next crisis. When conditions look safe, borrowers, lenders and policymakers take on more risk, add more leverage, and underprice danger. **Each intervention that restores stability can encourage the behaviour that ultimately sows the seeds of the next crisis.**

The developed world is living that pattern now. Four decades of strong market returns are often treated as proof that the system works. US equities have compounded at rates unmatched in modern history. Household net worth sits at a record. Yet those measures reveal little about the economy beneath them: **real wages stalled, home affordability reached its worst level on record, private sector job creation stagnated, and a child's odds of out-earning their parents fell by half.** As growth, productivity and demographics became less supportive, policymakers increasingly relied on financial conditions and rising asset prices to sustain demand. Over time, that approach boosted wealth on paper but left housing, labour markets and social mobility under growing strain.

That is why this now looks as much like a political challenge as an economic one. The distortions created by decades of asset-led growth have become increasingly visible, while the costs of correcting them remain politically contentious. **The IMF estimates that the required adjustment amounts to roughly 4% of GDP**, a surprisingly manageable figure given the scale of the problem. What remains lacking is the political willingness to distribute that burden. Genuine crises eventually force competing interests to compromise.

Cracks emerging

Three separate fault lines are cracking at once: politics, the economy, and markets. Any single one would justify caution. All three together is what we suggest is the endgame.

Fault line	Where it is showing	Why it matters
Political cracks	Near-record low incumbent re-election odds; rules-based global order under active strain; wars and realignment (Ukraine, Iran); populist protest votes across the developed world	Legitimacy of the existing policy regime is being withdrawn simultaneously by voters and by allies, the two constituencies that made the regime work
Economic cracks	5.8–6.3% GDP deficit against ~2% growth; private-sector job creation stalling; ~\$3 of new deficit needed for each \$1 of new GDP	The economy has become structurally debt-dependent: growth requires ever-larger deficits, and each dollar of deficit buys less growth than the last
Market cracks	Buffett Indicator ~235–250% (record range); margin debt/GDP above every modern cycle peak; equity concentration at record levels; speculation via 0DTE, prediction markets, single-stock leveraged ETFs	The market is pricing perfection at the same moment the economy is running out of policy room: the historical set-up for a valuation reset

CHART 2 Trend growth vs debt – debt is future consumption denied

US GDP growth vs debt to GDP



Decline in real GDP growth over time is evident despite the marked pick-up in government debt. Source: FRED as at 30/06/26.

CHART 3 Buffett Indicator – the extreme excess of market valuation over underlying growth

US total equity market capitalisation / US GDP, %



Source: Bloomberg as at 30/06/26.

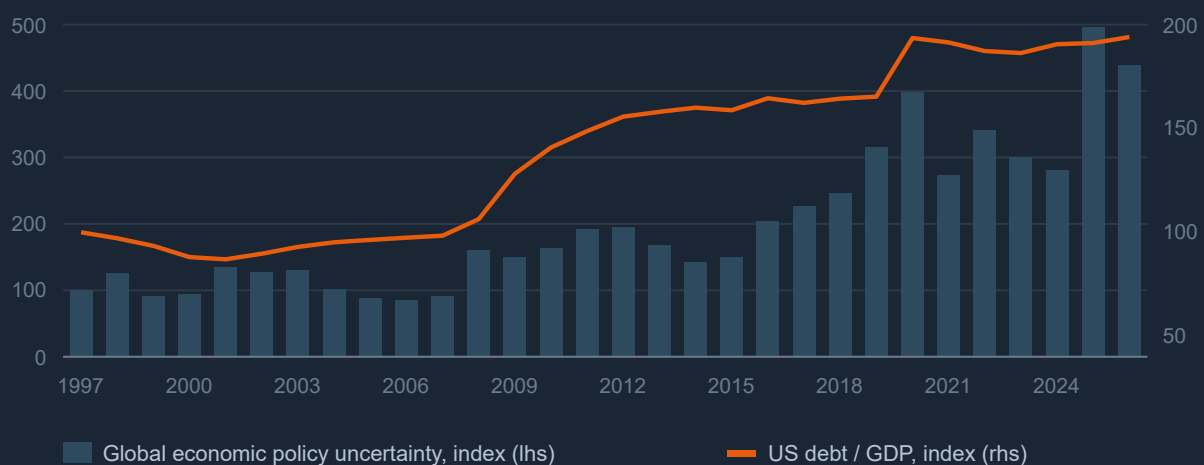
The twilight hour

Every economic orthodoxy eventually dies. An orthodoxy isn't a party programme or a position on the left-right spectrum. It's a shared way of thinking about how the economy works, defended by both parties in office. Democrat Roosevelt introduced the New Deal order; Republicans Eisenhower and Nixon embraced it. Reagan and Thatcher introduced neoliberalism; Clinton and Blair embraced it too, and the "Third Way" consolidated the Reagan settlement across party lines rather than offering any real alternative to it.

That cross-party consensus is what gives an orthodoxy its power, and what makes its collapse so dangerous for the political establishment. When voters decide the settlement is failing them, switching to the other mainstream party changes nothing: it runs the same operating system. What remains is a figure who promises to tear the whole system down, chosen by an electorate that had run out of legitimate mainstream alternatives. Such figures are a symptom of the orthodoxy's collapse, not its cause. Trump is the arch example: he diagnosed the grievance accurately, then delivered the same capital-favouring policies in a different costume. But he and those like him are the old orthodoxy's death knell, clearing the political ground for whatever replaces it.

CHART 4 Growth in policy uncertainty – sharp increase post-2015 as debt and deficits have also risen

Global economic policy uncertainty vs US debt/GDP, both indexed to 100 (1997)



Source: Bloomberg as at 30/06/26.

The four-stage process of the end of an orthodoxy

Each of the four periods below marks one stage in the arc from neoliberalism's founding to its exhaustion. The economics, politics and markets differ in each period, but the direction of travel doesn't: growth bought with progressively more debt, progressively lower returns per unit of that debt, and progressively greater political instability.

Period (Khalidun stages)	Years	Economy	Politics	Markets
I. Neo-Liberal (Founding)	1979–1996	Deregulation and investment boom; globalisation opens world trade; consumer and corporate leverage builds	Institutionalised, ideologically coherent governing parties; high incumbent re-election rates	Strong growth; global trade imbalances emerge
II. Speculative (Consolidation)	1997–2008	Globalisation exports disinflation; the economy financialises; production moves offshore; US shifts to deficit	Increasingly partisan; parties fight each other rather than the cycle	Deregulation boom; financial innovation (CDOs, derivatives); two boom-bust bubbles
III. Bubble (Luxury)	2008–2022	Zombie-business growth under ZIRP; collapse in social mobility; capital-owning top decile and labour shift to gig economy	Grievance and bailout politics; confidence in mainstream parties collapses; populist movements rise	Asset-price hyperinflation across every asset class; passive investing and private markets a one-way bet; rise of crypto
IV. End Game (Disintegration)	2023–	Negative marginal return on borrowed money; housing/healthcare structurally unaffordable	Rules-based order breaks down; near-zero incumbent re-election odds; wars and realignment	Debt-financed revenue routed through opaque SPVs; deficits edge toward monetisation

Original sin: two policy choices, forty years of diminishing returns

Capitalism remains the strongest economic system available, and neoliberalism's core principles are defensible on their own merits. Yet two policy choices, compounded over decades — the systematic privileging of capital over labour and an outsized reliance on the wealth effect — have done more than any others to create the instability of today's two-speed, **"K-shaped" economy**.

Policy choice 1: capital over labour (trickle down economics)

The first choice was the **systematic favouring of capital over labour** through the tax code, merger policy, collective bargaining and financial regulation. No single decision looks catastrophic on its own; several are even defensible. The compound effect shows up in every metric of who owns the economy, runs it, and captures its gains.

Metric	I. Neo-Liberal	II. Speculative	III. Bubble	IV. End Game (now)
Labour share of income	~64–65% (stable)	~62–64%	~58–61%	~52–57%
Corporate profit share of GDP	~6%	~7–8%	~10–12%	~14% (record)
Corporate markup vs marginal cost	~21% (1980)	~30%	~50%	~61% (record)
Industry concentration (HHI)	Falling	Rising through 2000s	Rising in >75% of industries	~+90% avg. rise since 1980
New-business entry rate	~13% (1980)	~10–11%	~8% (2018)	Near record low
Absolute mobility (children out-earning parents)	~79% (1970s cohort)	~62%	~58%	~50% (41% for father/son)

Sources: BLS (labour share); Federal Reserve of Kansas City and Richmond (industry concentration); Akcigit & Ates / NBER (markups and profit share); Census Bureau BDS (entry rate); FRED (real wages).

Policy choice 2: wealth-effect economics

The second choice was **elevating the wealth effect, using higher asset prices to drive spending, investment and confidence, into a primary transmission mechanism of macroeconomic policy.**

Greenspan introduced it as a market backstop; Bernanke and Powell turned it into an explicit objective, justifying QE on the grounds that higher asset prices would lift household net worth and, in turn, real activity. Every row in the table below tells the same story: the cost of sustaining the mechanism has risen sharply, while the growth it delivers has diminished.

Metric	I. Neo-Liberal	II. Speculative	III. Bubble	IV. End Game (now)
Effective real Fed funds rate	~+3–4%	~+1–2%	Negative most of period	Positive, debt-constrained
Total debt / GDP	167% → ~250%	~250% → ~350%	~350% → 405%	~400%+; federal 120%
Marginal productivity of debt	~70¢ per \$1	~40¢ → <10¢	~15–20¢	~10¢ or less
Federal deficit per \$1 of growth	Not primary tool	~\$1.20	\$2.33 → \$1.41	~\$3.00
Margin debt / GDP	~1–1.5%	~2.6–2.8%	3.97% (2021)	~4.0–4.5%

Sources: Federal Reserve H.15 and Z.1; Hoisington Investment Management; FINRA; PGPF/CRFB; CBO February 2026 Outlook.

Two choices framed today's world

Neither choice was catastrophic on its own. Compounded across four decades, their interaction is what broke the system. The wealth-effect channel routes the benefits of easier money to asset owners first. Capital-favouring tax and regulatory policy lets those owners keep more of what they gain. The resulting inequality then demands ever more transfer-payment support, funded by ever more debt, serviceable only through ever more of the same wealth-effect mechanism. That loop is what the four-period framework traces.

CHART 5 How capital won over labour from the 1980s onwards

Labour share vs corporate profit share of gross domestic income, %



Source: BEA NIPA (FRED), computed as wages & salaries ÷ GDI and corporate profits w/ IVA & CCAAdj ÷ GDI, quarterly, as at 01/09/26.

The tailwind that hid the cost of QE

The term "Great Moderation" was coined by Ben Bernanke in a 2004 speech describing the drop in macroeconomic volatility across the developed world from roughly the mid-1980s onward. Bernanke offered three candidate explanations: structural change, better monetary policy, and good luck. Unsurprisingly for a central-bank governor, he argued the second was the main cause, and the following two decades of central-bank practice were built on that assumption.

We think that reading was incorrect. **Structural tailwinds, not skilled central bankers, produced the Great Moderation**, and those tailwinds would have delivered low, stable inflation almost regardless of who was setting policy. Globalisation was exporting disinflation at industrial scale. The Baby Boomer generation was in its peak working years. Real energy prices spent most of the era falling from the 1970s shocks. Climate change was an externality nobody had put on the balance sheet yet. A single-superpower geopolitical order kept supply chains cheap. None of that was central-bank policy, and all of it hid the true cost of increasingly aggressive stimulus. That helps explain why QE appeared to carry few immediate costs: powerful structural tailwinds offset much of the inflationary pressure that conventional models might have predicted. Yet the absence of sustained goods-price inflation did not necessarily mean monetary expansion left no imprint on the economy. **Instead, much of that effect appeared in financial assets and property markets, where valuations rose far faster than underlying economic growth.** In that sense, Friedman's broader insight remains relevant: monetary conditions ultimately influence prices, although not always in the places policymakers expect. History offers precedents for periods in which abundant liquidity coincided with rapid asset-price appreciation and growing financial imbalances. With hindsight, those risks may have received less attention than they warranted during the Great Moderation era.

The tools that sustained the orthodoxy are now constrained

The final reason this orthodoxy is ending is that the two policy tools used to sustain it are increasingly constrained themselves. For forty years, monetary and later fiscal intervention met each downturn at what appeared to be a manageable cost, with deficits absorbed by falling rates and balance-sheet expansion offset by powerful disinflationary forces. That backdrop no longer holds. **Higher debt levels are already narrowing policymakers' room for manoeuvre, even in the absence of a crisis.** Meanwhile, many of the structural tailwinds that made monetary easing appear costless, including globalisation, favourable demographics and abundant supply-side capacity, are weakening or reversing. When the next downturn arrives, policymakers may find themselves able to deliver less support, at greater cost, than in previous cycles. That is not simply a forecast but a reflection of changing constraints. Returning to the old policy mix is, in our view, unlikely, given that the economic and market trade-offs are now materially larger than investors became accustomed to during the Great Moderation.

'This time is *not* different'

Joseph Schumpeter's most enduring point about capitalism, creative destruction is his own term for it, was that failure is not a defect of the system but a necessary feature of how it works. Without failure, without the loss of capital that follows from bad investment and the loss of political capital that follows from bad policy, the system cannot clear its mistakes. What Schumpeter would recognise in the current settlement is a capitalism whose regenerative mechanism has been systematically disabled: three decades of intervention designed to dampen the clearing effects of the business cycle has produced not a more stable system but a more fragile one, populated by zombie firms, hidden defaults in private credit, and asset prices detached from the real economy.

Edward Chancellor's *The Price of Time* (2022) extends the argument across a much longer horizon: roughly a millennium of rulers and central banks suppressing interest rates below what a free market would set, from the medieval usury debates through the classical gold standard to the twentieth century's managed-money experiments. The historical pattern Chancellor identifies is strikingly consistent. **Periods of sustained interest-rate suppression have often coincided with rising asset prices, increasing wealth concentration and the gradual build-up of financial imbalances.** They have also frequently been followed by some combination of market disruption, political realignment and policy regime change. The current cycle exhibits many of the same characteristics. Whether this results in a gradual adjustment or a more disorderly transition remains uncertain, but the pressures acting on the existing policy framework appear increasingly difficult to ignore.

PART 2

The Mechanism of Regime Change

Choice, institutions, politics, geopolitics, and technology

Three roads from here — only one practical solution

Every discussion of how this cycle ends collapses into a choice among three options. Only the first is genuinely open to the US.

Option	What it is	The verdict	Realistic?
1. Fiscal consolidation	A calibrated ~4% of GDP mix of spending cuts and revenue increases, the size the IMF estimates would stabilise the US debt path	Works on both sides of the ledger; the US has the bandwidth; and, depending on the mix chosen, potentially the least painful politically, since the burden can be targeted rather than falling on everyone at once	Yes: the only realistic path
2. Financial repression	Light-touch, incremental measures (QE, Operation Twist-style shifts, SLR changes, TGA drawdowns) nudging demand for Treasuries without a formal cap	This is what has been tried for years, and markets have now priced in that the toolkit is exhausted. Small moves already draw negative reactions; large ones would confirm the distress they are meant to disguise	No: a slower route to Option 3
3. Full YCC / debasement	A formal cap on yields, or the deliberate inflating-away of debt: the assumed fallback if Option 1 is not chosen	Works only under conditions the US does not have. Leaders who preside over serious debasement rarely survive it, and the democracies that experience it rarely emerge with the same political settlement intact	No: politically and economically catastrophic

Option 1: The only realistic path

People describe fiscal consolidation as the hard option. It's actually the least destructive of the three. The IMF puts the required adjustment at roughly 4% of GDP, achievable given the right political will albeit not without costs both socially and economically. It works on both sides of the ledger at once, cutting demand on the fiscal side while rebuilding supply capacity through whichever mix gets chosen. Inflation taxes savers and low-income households indiscriminately and invisibly. Fiscal consolidation can be targeted instead, and targeted beats regressive every time.

Option 2: Buys only time, exhibits diminishing returns

This middle road is familiar. We've followed it since 2008: QE, Operation Twist, SLR adjustments, TGA drawdowns, the light-touch financial-repression toolkit. It bought time and fixed nothing, leaving a debt mountain that strains the system as rates normalise. Japan spent trillions of yen trying to push inflation higher, and now that it has arrived, the debt load is crushing the recovery it was meant to enable.

Option 3: Why inflation is unlikely to solve today's problem

Many argue Option 3 is inevitable, pointing to two historical episodes as proof it was used before and will be again. Those episodes aren't good comparisons. Latin America gives a better test case for the debasement route, and success there is hard to find.

Precedent	The claim it can work	Why the conditions do not match today
US, late 1940s–50s	The Fed capped Treasury yields for a decade without incident	Executed with capital controls, a captive war-mobilised savings base, post-war growth tailwind, and the US ran a trade surplus. Today: twin deficits, no capital controls, no war-time mandate
Japan's YCC (2016–24)	A developed economy can cap yields for years	Works because Japan owns the overwhelming majority of its own debt domestically and ran current-account surpluses. The US depends on foreign capital: the opposite starting position

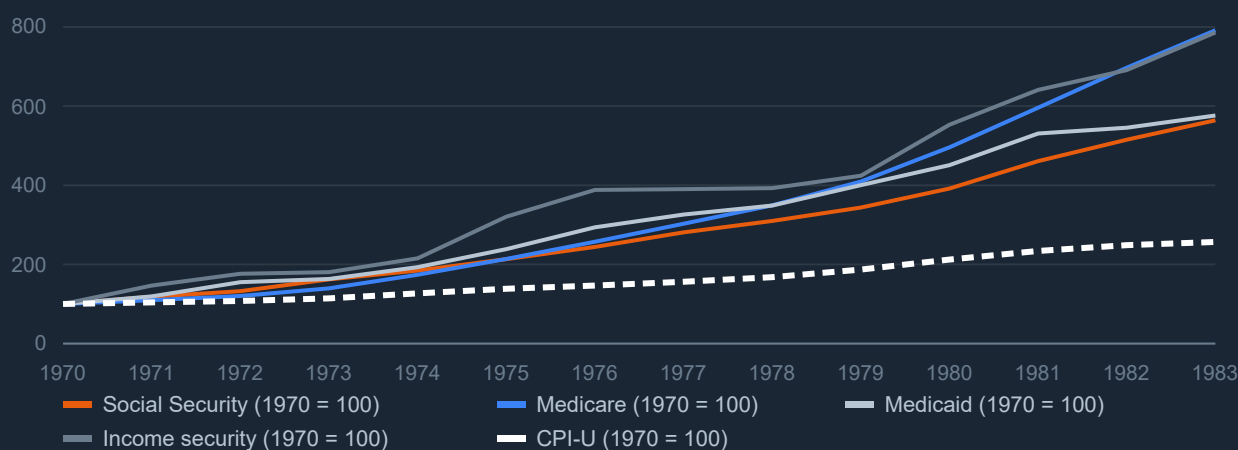
The reason inflation cannot solve the debt problem is not merely that entitlement outlays are indexed to prices. It is also that the value of entitlements are now significantly greater than the debt pile to be inflated away.

Inflation triggers two separate compounding mechanisms at once: it raises the cost of delivering the entitlements that already exist, and it creates the political conditions under which new ones get added.

The 1970s is the best example of this. Between 1970 and 1980, headline CPI roughly doubled. Over the same period, Social Security outlays quadrupled, Medicare outlays multiplied by five, and income-support outlays multiplied by nearly six, all in nominal dollars, on programmes that were supposed to be "indexed" to prices that had grown at half the pace.

CHART 6 Why inflating away the debt won't work (see the 1970s)

Entitlement outlays vs CPI, indexed to 100 (1970–1983)



Source: FRED.

Institutional change: the Warsh Fed

Kevin Warsh's first months as Fed Chair are among the clearest indications that elements of the wealth-effect era are being reassessed from inside the institution that helped build them. You can see the direction of travel in what he's said, in what his first FOMC meeting did, and in who he's brought in to help shape the review.

The core reorientation

"Winning the battle against the Panic of 2008 was a necessary but insufficient condition to win the peace," Warsh argued when he resigned from the Fed in 2011. The tools that stemmed the crisis should have been dismantled long ago instead of institutionalised, in his view, and that belief has increasingly informed his broader critique of the post-crisis policy framework. **Warsh has repeatedly called large-scale asset purchases "reverse Robin Hood," arguing that they disproportionately benefit asset owners while distorting capital allocation and inflating financial-asset prices relative to the real economy.**

What the first FOMC meeting showed

At his first meeting as Chair, on 17 June 2026, Warsh dropped the standard forward-guidance boilerplate and revealed a dot plot with **nine of eighteen FOMC participants pencilling in a rate hike for the year**, materially more hawkish than markets had priced in. Loretta Mester, no natural ally of a hawkish surprise, welcomed the removal of guidance language that had become increasingly difficult to reverse once introduced: the Fed's own "Hotel California problem."

The Fed put isn't gone. It has become more expensive, and risk-asset holders are the ones paying the new premium.

The task forces: who is doing the work

The team Warsh has assembled provides a further indication of the direction of travel. Raghuram Rajan and Mervyn King both built their public reputations warning about financial-system fragility before it was fashionable to do so, and Rajan's 2005 Jackson Hole paper challenging Alan Greenspan's complacency remains one of the clearest examples. **Few of the people he has brought in are known for defending the post-2008 consensus; several built their reputations by questioning it.**

Political change: the Treasury and the return of labour over capital

Where the Fed side is institutional, the Treasury side is going to be political. Bond vigilantes are already imposing arithmetic on fiscal deficits. The deeper adjustment investors need to price is a political rebalancing between capital and labour, driven by an electorate that has become increasingly dissatisfied with the existing settlement.

What the electorate has already told us

Voters are telling us the direction of travel. Brexit and Trump's election both reflected dissatisfaction with a system many voters felt no longer worked for them. Neither ultimately delivered the economic rebalancing many supporters expected, and voter dissatisfaction has persisted. A majority of young Americans now say they don't trust capitalism as an economic system. That's a signal about the political viability of any future settlement that doesn't visibly rebalance capital and labour.

This is increasingly a single-term political era. Few incumbents can survive without a credible plan to rebalance labour and capital. Figures on both the left and right are early signals of the same broader realignment.

The rebalance runs through regulation, as well as taxation

The forty-year shift from labour to capital ran through the regulatory code as much as the tax code, and the reversal will run through the same channels. Higher tax rates alone never explained capital's rising share. The deeper mechanisms were antitrust abandonment (Bork's consumer-welfare standard), the deregulation of finance (the Glass-Steagall repeal), the tax-preferred treatment of buybacks over dividends, and the erosion of labour-market and collective-bargaining protections. Lastly, the Citizens United ruling also directly enabled Super PACs and the ability of corporate interests to raise unlimited funds for political campaigning. Reversing the tilt means unwinding those regulatory choices, not just lifting headline tax rates.

Policy lever	How capital-over-labour was implemented (1979–2024)	How the reversal works (2024–)
Corporate taxation	Top rates cut from 46% (1986) to 21% (2017); global race to the bottom	OECD minimum tax; higher effective rates; closing the loopholes that made headline rates meaningless
Buybacks	Effectively tax-free versus dividends; largest single use of corporate cash flow pre AI	Excise tax rising; restrictions in years of layoffs or in subsidised sectors under active discussion. Treat buybacks in same way as dividends.
Antitrust	Consumer-welfare standard (post-Bork, 1978) allowed HHI to rise in >75% of industries	Return toward a structural standard; enforcement rebuilt; scrutiny of AI infrastructure consolidation
Labour-market regulation	Erosion of collective bargaining; minimum-wage stagnation; gig-economy loopholes	Sectoral bargaining pilots; minimum-wage floors indexed; reclassification rules tightened
Financial regulation	Repeal of Glass–Steagall (1999); Dodd-Frank (2009) enabled shadow-banking to grow outside of prudential oversight	Renewed prudential oversight of shadow banking; bank capital requirements steer risk back onto regulated balance sheets

The counter-argument, that higher corporate taxes hurt investment, that closing loopholes chases capital abroad, that antitrust enforcement chills innovation, does not survive contact with the last four decades of evidence. Corporate profits rose to record shares of GDP while corporate reinvestment as a share of those profits fell. **The tax code often rewarded financial engineering more generously than productive investment.**

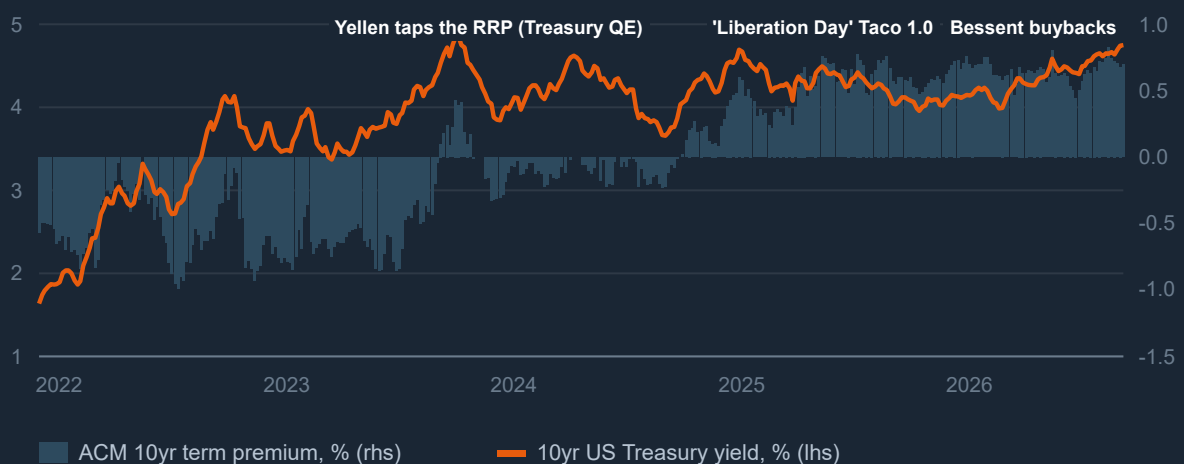
Measures such as the OECD's 15% global minimum tax illustrate the broader direction of travel by reducing the arbitrage that weakened previous headline rates.

Good for the debt-market problem too

The rebalancing isn't just politically necessary. It's fiscally productive too. A larger labour share could reduce reliance on transfer payments, which now account for a significant share of federal spending. Higher wages fund the demand side that fiscal policy has been substituting for. A broader tax base, built from labour income earning a bigger share of a growing pie, raises revenue without the drag on investment that higher marginal rates on already-narrow bases produce. Rising savings rates would help too, funding government needs directly.

CHART 7 Treasury policy put on the US bond market evident since Q4 2023

10-year Treasury yield vs ACM 10-year term premium, 12/2021 – 09/2026



Source: Bloomberg as at 08/09/26.

Geopolitical change: the hammer and anvil

The endgame isn't playing out inside a single national economy. The US and China are pursuing incompatible dominance strategies: China through industrial scale, the US through technology and the dollar's reserve-currency role. Middle powers and the euro area increasingly find themselves caught between them: large enough to have interests of their own, but not large enough to set the contest's terms.

Mark Carney's January 2026 Davos programme for Canada shows what a middle-power response looks like once the assumption of automatic prosperity through alliance membership disappears: a trillion dollars in fast-tracked investment across energy, AI, critical minerals and trade corridors, doubled defence spending, and twelve new trade agreements across four continents in six months. Mario Draghi's report on European competitiveness makes the parallel case: without a step-change in investment, **€800 billion a year**, Europe risks getting crushed between the US hammer and the Chinese anvil.

The world increasingly appears to be organising around three broad centres of economic gravity rather than a single US-centred system: a China-centred Asian sphere, a US-centred sphere, and a looser coalition of European and middle-power economies focused on industrial policy, defence and strategic autonomy. Reserve-currency status remains predominantly US-based, supported by the scale of the eurodollar system, although its relative importance may diminish over time.

The investment case for exposure to the middle-power response, from European industrial policy and Canadian critical minerals to Japanese and Korean defence spending, appears considerably stronger than it did during the era of hyper-globalisation. National-champion models are also re-emerging across strategic sectors including energy, semiconductors, defence and AI infrastructure.

AI: an industrial revolution built on uncertainty

AI is real, and it's already reshaping the economy from a financialised base toward an industrial one. Corporate objectives are genuinely shifting away from profit maximisation through financial engineering and toward investment in physical capacity, the first such shift in a generation. But it's happening at a scale and pace that's hard to reconcile with anything we actually know about the technology's eventual returns. The capex spend needed for this transformation may simply worsen the inequality already disrupting society today, an outcome that may prove less productive than its proponents expect.

What we do not know

Open question	Why it undermines the current investment case
Which model wins?	Closed proprietary stacks (OpenAI, Anthropic) versus open-source stacks (Chinese DeepSeek, Meta LLaMA) offer very different capital-intensity and revenue models: the whole capex thesis is different for each
How much compute is needed?	The demand curve for top-tier models has disappointed. Most enterprise use cases run on smaller, cheaper models; frontier take-up has been well below what the capex build implies
Where does the ROI actually land?	The biggest productivity gains so far are showing up in smaller companies running cheaper models on lower budgets
Marginal cost economics	Every additional query adds real cost (compute, energy, water). Unlike the last cycle's near-zero marginal cost businesses, there is no clear path to the economies of scale that made prior industrial revolutions self-financing
Regulatory response	The same electorate forcing capital-over-labour reversal will not tolerate AI consolidating into two or three trillion-dollar rent extractors. Regulation will constrain the winner-takes-all outcome current valuations discount

The financing problem

The uncertainty in the table above would be manageable if the industry were funding itself out of current profits. It isn't. The capex cycle runs on free cash flow diverted from buybacks, new debt, and a wave of very large IPOs, while the cost base gets deferred through long depreciation schedules and off-balance-sheet leasing arrangements. Hyperscalers are already stretching stated GPU depreciation from 3-4 years toward 6, smoothing reported earnings against a useful-life reality the accounting won't support indefinitely. Data-centre leases and power purchase agreements get structured to keep the liability off the balance sheet. Revenues get pulled forward through vendor-financing and related-party arrangements that resemble the pre-2008 originate-to-distribute credit chain.

None of this is guaranteed to be sustainable. The cost base is being postponed, not eliminated. As depreciation schedules mature, lease obligations become more visible, and vendor-financing arrangements unwind, accounting reality may converge with market expectations more quickly than investors anticipate. The industry is betting that returns arrive before deferred costs become more visible, and that today's rent-accrual model remains viable. **That's a multi-trillion dollar wager that this cycle avoids the investment excesses seen in railroads, canals, electrification and TMT.**

Here's the final paradox: if AI delivers the gains its proponents claim, that success may deepen the wealth concentration and corporate dominance the political system is increasingly questioning. Legal and regulatory challenges to unfettered Big Tech are mounting, most visibly against the social media platforms, and it's difficult to see how AI, a far more consequential technology, remains immune from similar scrutiny. The Standard Oil analogy is worth considering.

PART 3

What It Means for Markets

Back up the curve, into liquidity, into being paid for risk

Seismic shift in policy objectives

For four decades, the primary object of macro policy was the price of risk assets. Alan Greenspan established the framework informally with the "put" markets came to expect after 1987 and 1998. Ben Bernanke made it explicit: when he introduced QE, he stated openly and repeatedly that the goal was raising the price of risk assets, on the theory that higher household net worth would produce spending, investment, and through those channels, real activity. **The wealth effect wasn't a side-effect of policy. It was the policy.** Every major intervention over two decades relied heavily on asset prices as a primary transmission mechanism into the real economy.

That objective is shifting now, and the shift is seismic. Debt levels are increasingly constraining policy choices, the Great Moderation tailwinds that once absorbed the cost of further asset-price support are gone, and policy protection is moving from equity markets to the bond market itself. Policymakers no longer need to manage the level of the S&P 500. They need to manage the yield on the Treasury curve: the government's own funding cost, and the credibility of the debt stock behind it. Warsh's own framing of the old model is already on record. On the Treasury side, Scott Bessent has openly described himself as *"the nation's top bond salesman"* and made lowering the 10-year yield the administration's stated policy priority, a striking reversal from a decade in which the S&P 500 was the barometer that mattered most. His actions, while counterproductive at times, have sought to reinforce that message: an expanded Treasury buyback programme, a shift of issuance toward short-dated bills globally, and continuous verbal intervention aimed at the long end. The bond vigilantes are delivering the same message from the other side of the trade. Politicians will take longer to accept this than central bankers, but the direction of travel is no longer in doubt. The tailwind that made asset-price appreciation the default outcome of every policy cycle is gone. The stability of the bond market is increasingly becoming the central policy objective.

Profit tailwinds becoming headwinds

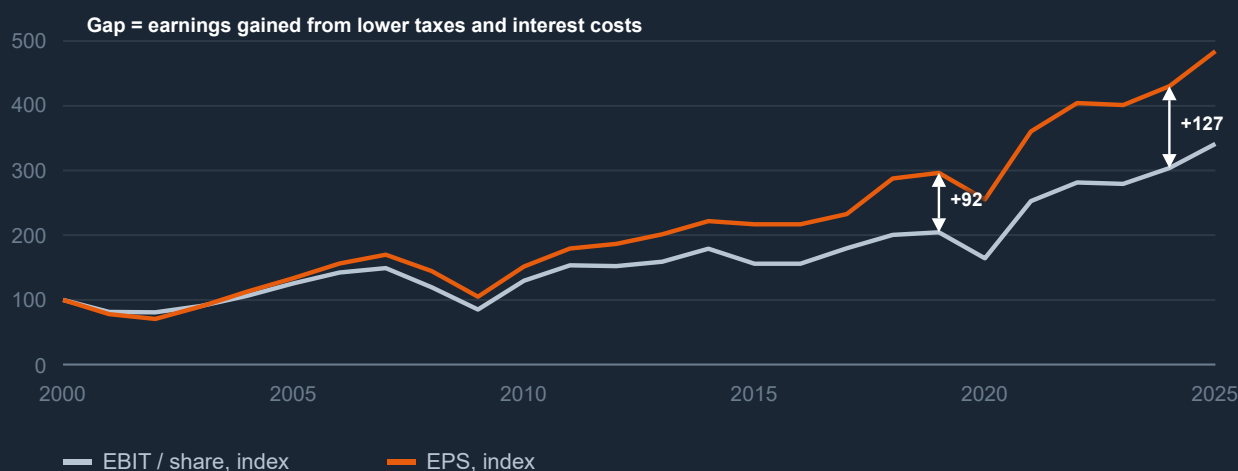
Most of the large drivers of corporate earnings growth over the last forty years were not, in fact, drivers of productivity. They were the compounding effects of a set of one-way structural tailwinds: **falling corporate taxes, falling interest rates, growth in monopolisation, falling labour costs, and the rise of a small cohort of dominant technology platforms whose free cash flow financed a buyback boom.** Each was individually large. Together, they help explain a substantial share of the margin expansion that underpins today's equity valuations. And many of them are now weakening or beginning to reverse.

The critical point is that these tailwinds have not merely stopped blowing. **They are increasingly becoming headwinds.** Corporate tax rates have stopped falling. The low-cost debt cushion built during the 2020–21 refinancing window is beginning to run off. Labour costs are being pushed up by trade fragmentation and by a policy environment increasingly hostile to the offshoring model. And the Big Tech free cash flow that funded the buyback era is being consumed by AI capex on a historical scale, exactly as regulatory scrutiny intensifies.

Earnings driver	1980–2022: tailwind	2023–: now becoming a headwind
Corporate tax rates	US federal top rate cut from 46% (1986) to 21% (2017); global race to the bottom drove effective rates lower still	OECD 15% minimum floor in force; political appetite unambiguously for higher effective rates and closing loopholes
Interest rates	Falling from ~15% to zero across four decades; the 2020–21 refinancing window let corporates term out debt at multi-decade lows	The termed-out cushion runs off through 2026–28; refinancing at multiples of the prior coupon; net interest costs rising even as debt loads stay flat
Labour costs	Globalisation, offshoring and the collapse of unionisation compressed labour's share and delivered access to cheaper alternatives	Trade fragmentation and reshoring reverse the offshoring dividend; labour share reversing; wage floors indexing; sectoral bargaining pilots
Big Tech FCF and buybacks	A cohort of dominant, low-cost, high-margin platforms generated the free cash flow that funded the buyback era, peaking near \$1 trillion annually	AI capex is now consuming that free cash flow rather than returning it; the buyback engine is being crowded out just as regulatory pressure on the same platforms rises
Corporate concentration	Two generations of antitrust permissiveness (post-Bork consumer-welfare standard) let markups rise in more than 75% of industries	Return toward a structural antitrust standard; enforcement rebuilt; monopoly rents will be squeezed as regulators unwind accumulated concentration

CHART 8 Impact of lower tax and interest costs on corporate earnings

S&P 500 EBIT/share vs EPS, indexed to 100 (2000) — the gap is the combined tax + interest effect



Source: Bloomberg (SPX Index EBIT & trailing EPS per share; LUACTRUU Index yield to worst) and FRED/BEA (effective tax rate = $1 - \text{CP} \div \text{A053RC1Q027SBEA}$, both "without IVA/CCAdj" basis). Annual, as at 01/09/26.

The industrial reshaping of capital markets

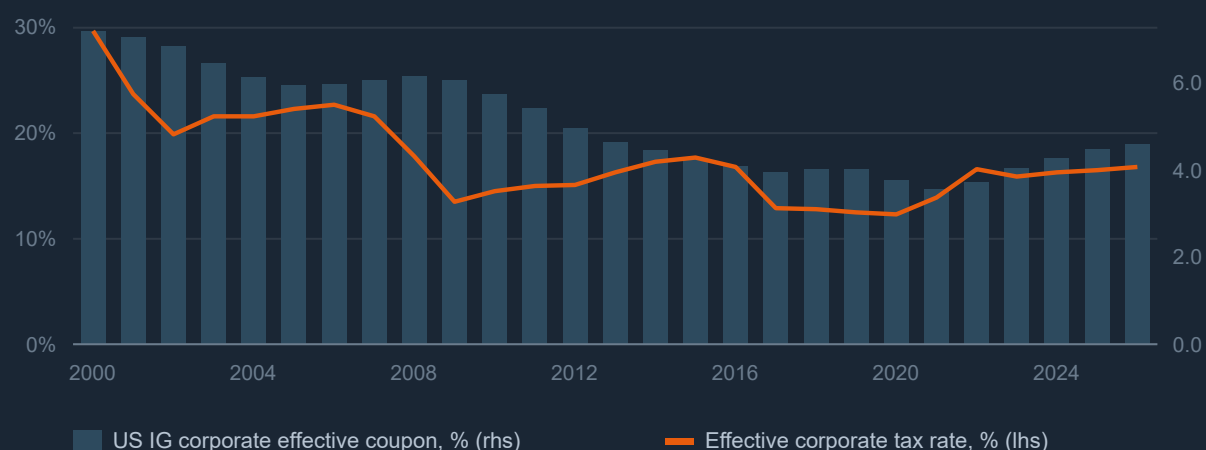
This is more than a shift in headwinds. **Capital markets are being structurally reconfigured as the flows that powered the last decade's financial-engineering-driven returns are dismantled.**

From asset-light to asset-heavy: capital markets rewired

For four decades the US public equity market was dominated by low-capital, low-marginal-cost technology and financial businesses that generated enormous free cash flow, most of which went to buying back their own shares. That machinery is now being dismantled on two fronts at once.

CHART 9 Corporate tax rates and interest rates over time – is the trajectory finally changing?

The two inputs — effective corporate tax rate (lhs) and US IG corporate effective coupon, % (rhs)



Source: Bloomberg and FRED/BEA as at 01/09/26.

The technology sector itself is evolving from an asset-light FCF machine into a capital-hungry industrial one, with a marginal cost per query (energy, water, compute) that a traditional industrial business would recognise, and a depreciation profile an order of magnitude shorter than earlier industrial cycles (GPUs 3-6 years versus fibre optics 25-30, electrical grids 30-40, railroads 40-plus). At the same time, the buyback engine that turned favourable macro tailwinds into equity-market returns, peaking near \$1 trillion annually and accounting for a substantial share of S&P 500 EPS growth over the last decade, is being consumed by AI capex instead.

Corporates are shifting from being net buyers of their own equity to being net issuers of both equity and debt to fund the build-out.

The issuance side of the shift compounds the problem. The US public equity market has been contracting for two decades: listings fell from roughly 8,090 in 1996 to around 3,900 by 2025, largely because businesses went private and stayed private for longer. AI capex programmes are now so large they are increasingly difficult to fund through private markets alone, and a wave of very large IPOs is already in the queue, which means the US listing count is likely to expand for the first time in a generation. But these IPOs are pricing at or near full enterprise valuations. The multiple expansion that made the Amazon 1997 IPO (~\$438m market cap) or the Google 2004 IPO extraordinary public-market opportunities for public investors has already been captured in the private rounds. Public investors will get the maturity phase this time, not the growth phase: fewer dollars flowing from corporates to shareholders, more shares issued into the market, and less of the future value left at the point of listing.

The global capital flows are reversing

For four decades the US ran the developed world's lowest household savings rate and got away with it, because it never needed to fund itself out of its own savings. The yen carry trade, petrodollar recycling, Chinese reserve accumulation and European official-sector buying provided the external pool that funded US deficits and anchored long yields. That model is now visibly running down. Foreign holders own roughly 30-31% of publicly-held US federal debt, down from around 50% at the 2008 peak, and foreign official holders have fallen from 59% of foreign holdings a decade ago to 42% at end-2025. The Treasury market hasn't fractured, because the US private sector, stablecoins and money-market funds have stepped in instead. But the composition has changed, and the long-term direction of that change has been one of declining foreign participation.

Structural feature	The four-decade market that is ending	The market that is replacing it
Dominant business model	Low-capital, low-marginal-cost technology and finance, near-zero marginal cost per unit of output	Capital-heavy AI infrastructure with meaningful marginal costs per query (energy, water, compute) more resembling a traditional industrial sector
Return on capital	High and structurally stable: the FCF machine that funded the buyback era	Materially lower and less certain: heavy capex today, uncertain revenue 'rents' capture
Free cash flow use	Returned to shareholders through buybacks; peaked near \$1 trillion annually, driving EPS growth without earnings growth	Consumed by AI capex on a historical scale; buyback capacity crowded out for as long as the capex cycle runs
Depreciation lifecycle	Long-lived asset bases: fibre optic ~25-30 yrs; electrification grid ~30-40 yrs; railroads 40+ yrs	GPUs in data centres carry a 3–6 year useful life; hyperscalers already stretching depreciation schedules to fit the accounting
Number of listed companies	Contracting for two decades: US listings fell from ~8,090 in 1996 to ~3,900 in 2025 as businesses stayed private	AI capex programmes are so large they cannot be funded privately, so the number of listed names is likely to expand for the first time in a generation

The equity story is where the unspoken risk sits, because it's the flow that hasn't turned yet, and the outperformance behind it is already historic in scale. **US equities have risen from roughly 40% of the MSCI ACWI in 2010 to a record ~62-64% today**, the highest concentration any single national market has reached since the modern index began. Over the five years to end-2024, the MSCI USA returned 108.4% against just 29.9% for the MSCI ACWI ex-US, and US equities outperformed the rest of the world in eight of the last ten calendar years. US mega-caps ended 2024 trading on roughly 32x earnings, more than twice the multiples of both emerging-market and developed ex-US peers. Global institutional portfolios have gradually increased their US weightings in response, and foreign allocations to US risk assets now sit at record levels, sustained by the assumption that the US remains the default destination for global capital seeking growth. 2025 saw the first meaningful challenge to that pattern: Europe, emerging markets and Japan all outpaced the US in local-currency terms. The allocation position hasn't moved to match it yet.

That assumption is precisely what the fragmenting global order and the return of domestic industrial policy are calling into question. Middle powers are increasingly adopting policies designed to encourage greater domestic deployment of capital. The UK's Mansion House Accord, signed May 2025, commits 17 pension providers, roughly 90% of active DC savers and £252 billion, to allocate 10% of default funds to private markets, with half ringfenced for UK assets by 2030. The Draghi report prescribes the same shift at continental scale, and Canada's Carney programme is doing the same on a national-champion basis. None of this points to a mass withdrawal from the US. It points to the same slow, marginal flow reversal already visible in Treasuries, playing out in a market priced for record inflows, record US concentration, and little sign of reversal.

Demographics: the flow reversal nobody is positioned for

For four decades, the demographic tailwind pushed capital into risk assets one way. The Baby Boomer generation moved through its peak accumulation years with monthly contributions into 401(k)s, IRAs and passive default funds, one of the largest sustained bids risk assets have ever received. It flattered index returns, made passive investing look self-reinforcing, and gave the wealth-effect toolkit a demographic engine to work against. **That tailwind is now fading and, in some areas, beginning to reverse.** The Peak 65 Zone began in 2024, and 2025 marked its absolute peak: 4.18 million Americans turned 65 that year, about 11,400 every day, with the surge continuing through 2027.

The Alliance for Lifetime Income's 2024 study found **52.5% of Peak-65 Boomers hold total assets of \$250,000 or less**, a threshold that forces retirees to sell down principal rather than simply spend income. A 1994 GAO-cited study projected the US pension system would turn from net saver to net drawer around 2024, and that projection arrived almost exactly on schedule.

The largest asset managers are already repositioning. Fidelity announced a revised target-date glide path in October 2025, transitioning through Q1 2027, a live re-engineering of the largest US target-date platform timed almost exactly to the demographic peak. BlackRock launched LifePath Paycheck in 2024, embedding lifetime annuities into default DC vehicles. PIMCO's 2025 US Defined Contribution Consulting Study reports two-thirds of institutional consultants expect increased personalisation of glide paths around participant demographics, and its June 2026 paper argues active fixed-income allocation extends asset longevity for the decumulation cohort. None of these firms has publicly named the shift a Peak 65 flow reversal, but every change points the same way: more fixed income, less equity default exposure. That's broadly where the rest of this analysis points as well: back toward bonds, back toward income-generating assets, back up the credit and liquidity curve. **Bonds remain materially under-owned relative both to prescribed glide paths and to the demographic drawdown already underway.** This may be one of the most underappreciated flow reversals now underway, and it doesn't require a market crash to matter. It only needs the demographic clock to keep ticking, at 11,400 sixty-fifth birthdays a day.

What the market's new drivers are starting to look like

The old drivers of returns are ending. New ones are already emerging, and we believe they will shape the most consequential structural pivots of the next cycle.

This tide is now shifting. The Fed is increasingly stepping back from the policies that pushed investors down the credit and liquidity curve. Demographics are turning more conservative. Shadow-banking regulation will be extended. Scott Bessent has explicitly prioritised Treasury funding conditions over asset-price support, while Kevin Warsh is now advancing from inside the Fed the critique he first articulated in 2011. **The direction of the next decade's flows is back up the curve.**

The implication is direct. Investors are paying close to the highest prices in history for risk assets while accepting some of the lowest prospective compensation for the downside they carry: record margin debt relative to GDP, record valuations and record equity concentration, all at once. Portfolios need to be liquid, and investors need to be properly compensated for risk. **The dominant structural shift of the next cycle is the reversal of the last: back into public over private, liquid over illiquid, quality over reach, and paid-for-risk over hope-for-multiple-expansion.**

Back up the credit and liquidity curve

For four decades, monetary policy, particularly QE, encouraged investors down the credit and liquidity curve. That process is now reversing. As the wealth-effect toolkit was progressively deployed, the reach-for-yield behaviour documented by Krishnamurthy and Vissing-Jorgensen during QE2 became one of the defining flows of the era. Successive rounds of QE encouraged investors to move further down the credit and liquidity curve in search of return.

Period	Direction of travel	Where capital was pushed	Symbolic instrument
I. Neo-Liberal	Down the credit curve begins	IG credit and equities; high-quality actively-managed portfolios	60/40
II. Speculative	Further down	Hedge funds; structured credit (CDOs); options; small-cap and commodity exposure	Structured credit
III. Bubble	The QE-forced descent	Private markets; direct lending; passive equity concentration; low-quality credit and covenant-lite loans	Private credit fund
IV. End Game (now)	Reversing → back up the curve	ODTE options and single-stock leverage at the top of the K; forced retreat toward liquidity and quality is beginning at the institutional edge	ODTE options / T-bills

One important nuance: **the problem lies within the shadow-banking system, not the banks.** The regulated banking system is materially better capitalised and supervised than at any point in the last four decades. The risk is concentrated in private credit, illiquid alternatives, and the leverage embedded in derivative and structured-product markets that sit outside the prudential perimeter.

Market liquidity now appears increasingly dependent on stable flows, raising the risk that volatility episodes generate larger price dislocations than in previous cycles. Those risks are amplified by the reduced scope for policy intervention described earlier. At the 2023 Jackson Hole symposium, Barry Eichengreen argued that today's public debt levels leave policymakers with far less room for error and that the historical record of orderly fiscal consolidations remains limited.

Recognition of these constraints may be overdue, but risk assets remain priced for a continuation of the previous regime rather than the adjustment now underway.

Market discipline reintroduced

Post the Great Moderation, bond market signals take on a new level of importance. The bond market is one of the few remaining self-regulating mechanisms in the modern policy toolkit, and rising yields are its principal instrument of correction. When yields rise, they often signal underlying imbalances, including persistent deficits, overly accommodative financial conditions, or asset markets that have become detached from economic fundamentals. The effects of higher yields are broad-based. Rising yields refocus fiscal authorities on prudence by raising the cost of servicing existing debt. They tighten financial conditions through the credit cycle, forcing banks and non-bank lenders alike to reprice their books. They raise the risk-free rate that anchors every discount-rate calculation, which lifts the hurdle rate for corporate capex and puts marginal investment projects below the threshold that justifies capital being deployed.

And they operate directly on the household side: consumer borrowing for autos, credit cards and housing becomes more expensive, marginal borrowers come under increasing stress, and lending standards tighten in response. The whole system is disciplined at once, and the discipline arrives whether policymakers welcome it or not.

The difficulty facing the US at present is that **a K-shaped economy needs two policy rates and can only receive one**. The interest-rate-sensitive half of the economy – small businesses, consumers, marginal borrowers – could genuinely use lower rates today, because it is where the tightening is transmitting most quickly and painfully. The other half – AI capex, hyperscaler build-out, and government spending itself – has so far proved considerably less sensitive to borrowing costs, and it is precisely the half that is currently driving aggregate demand above the level the supply side can absorb. **Because policy operates through a single rate, and the demand-driving half of the economy is the insensitive one, higher rates may be required to restore equilibrium – even though the cost of that adjustment falls disproportionately on the sensitive half that did not create the imbalance**. Rates will plateau at whatever level ultimately re-anchors the whole economy, not at the level that would be comfortable for the bottom of the K. That is an uncomfortable political reality, but it is also the mechanical reality of running a single-instrument monetary system against a two-speed economy.

Regional champions over global winners

For four decades, the biggest winners of the neoliberal order were the businesses best positioned to operate across borders. **That model is now going into reverse. As the global order fragments into three broad blocs (US, Asia, Europe/middle powers) and as governments across the developed world return to explicit industrial policy, the businesses best positioned for the next cycle may increasingly be regional champions in strategic industries, not global operators with distributed supply chains.**

One early illustration comes from the automotive sector: General Motors, materially more US-focused than its European rival, has delivered roughly a 70-percentage-point performance gap over Volkswagen in the last twelve months. Nike, one of the defining global consumer brands of the last four decades, is down more than 30% year-to-date in 2026 in what will be its fourth straight annual decline, amid rising concerns around China exposure and tariff risk. Costco, by contrast, with its US-focused footprint and simpler supply chain, has compounded steadily through the same period. In defence, European national champions like Rheinmetall and Leonardo are among the best-performing large-caps globally since 2022, precisely because governments now prefer domestic producers on strategic-autonomy grounds. **The examples span multiple sectors. It is a general reordering: businesses whose competitive advantage was the ability to operate globally are increasingly being repriced against businesses whose advantage is the ability to serve, and be protected by, a particular political geography.**

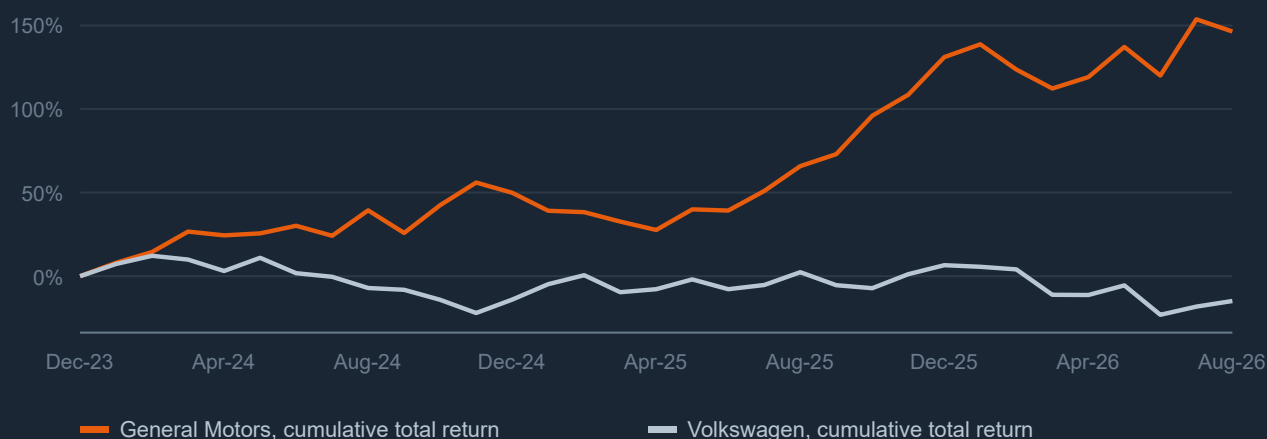
Conclusion: the regime change is already underway

The defining feature of the current moment is not that regime change is coming. It is that the mechanisms that have been used to postpone it for four decades have reached their practical limits. **Debt levels across the developed world sit at levels that constrain any further can-kicking, and the Great Moderation tailwinds that made the last four decades of stimulus look cost-free have flipped into headwinds.** Globalisation, favourable demographics, cheap energy, a stable geopolitical order and free climate optionality all worked to hide the true cost of the policies deployed against every stumble since 2001; each is now working in the opposite direction. A new approach is required, and it is being forced, because the old one can no longer function.

Sector	Regional champion (winner)	Global operator (laggard)	Performance gap
Autos	General Motors (US-focused): +67% total return over 12 months	Volkswagen (global): –3% total return over 12 months	GM +70pts ahead over the last year; ~+124% cumulative over 3 years
Consumer / retail	Costco (US-focused warehouse retailer): steady mid-single-digit annual gains through 2024–26	Nike (global brand, heavy China/EMEA exposure): –30%+ YTD 2026, fourth straight annual decline, 12-year lows	Cumulative gap of well over 50 percentage points since early 2024
Defence	Rheinmetall (Germany), Leonardo (Italy) and other European national champions: multi-hundred-percent gains since 2022	Historically global defence primes constrained by cross-border sourcing risk; regional producers preferred for strategic-autonomy reasons	European regional-champion defence stocks are among the best-performing large-caps globally since Ukraine
Energy / minerals	Domestic and allied-supply producers (US LNG exporters, Canadian critical minerals, Australian rare earths)	Integrated global majors dependent on politically-exposed supply chains	Divergence accelerating as friend-shoring policies steer capital toward domestic and allied producers
Technology (emerging)	National-champion AI infrastructure programmes: US (CHIPS Act), EU (EuroStack), China (domestic stack), Japan (Rapidus)	The four-decade global-supply-chain semiconductor model is being deliberately broken up along political lines	Government support is now the largest single factor in strategic-tech valuation

CHART 10 GM over VW demonstrates the benefits of domestic focus over global supply chains and customer base

Cumulative total return, General Motors vs Volkswagen (Dec-2023 = 0%)



Source: Bloomberg as at 01/09/26.

Because the toolkit is exhausted, the change now underway is not optional. Politics is shifting from a long period of policy consensus toward a more electorally driven and contested settlement. New economic policy (orthodoxy) is shifting from capital-favouring wealth-effect stimulus toward a rebalancing of labour and productive investment. The Fed is retiring its own wealth-effect toolkit under Warsh; the Treasury is being forced to confront its arithmetic by a bond market that has stopped extending unlimited patience. The geopolitical order is fragmenting into three broad blocs. And capital markets are inverting: from buybacks to issuance, from private and illiquid back toward public and liquid, from global multinationals toward regional champions. These are not marginal adjustments. They are a regime change on the scale of the shift from the New Deal order to neoliberalism at the end of the 1970s.

And yet most of the market participants we speak to still expect more of the same: another QE cycle if markets stumble, the continuation of the passive concentration and private-market bid that defined the post-2008 environment. We do not see how any of that is possible on the scale the markets are expecting. Markets may want it; voters certainly do not. The speed and specific path of the transition remain uncertain, but they are bounded and manageable so long as the policy framework for acting on them is built in advance rather than improvised after the fact.

The greater danger is the market structure itself. **Today's capital markets are, on almost every measure, poorly positioned for a regime change of this scale.** Passive concentration is at record levels; margin debt is above every modern peak; illiquidity has been engineered into portfolios through private credit and alternatives; and the Buffett Indicator sits at its highest recorded reading. Each of these features amplifies rather than absorbs shocks.

The regime change is already underway. The market has not yet noticed. The gap between those two facts is the largest single mispricing in institutional portfolios today.

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