4 July 2023

Dear Equity Client

GLOBAL EQUITIES – 2nd Quarter 2023

Equity investors enjoyed another strong quarter. The MSCI World Index (including Emerging Markets and dividends) grew by +6.2% (inUS$ terms, +3.1% in UK£ terms)*. This brings the first half performance to a pleasing +13.9% (in US$ terms, +8.4% in UK£ terms)*. Another +8.0% (in US$ terms, +2.3% in UK£ terms)* is still required to recover all the bear market losses.

This positive stock market recovery is largely due to the continued decline in US inflation, which has more than halved from 9.1% at its peak level a year ago to 4.0% in May*. Whilst core US inflation remains stickier, the general perception is that US inflation has decidedly turned from a headwind last year to a tailwind this year. The historical pattern of peak inflation being followed by peak interest rates, very importantly, is holding true thus far. This overall outcome has been much more positive than generally feared not that long ago.

This relative comfort has been countered to some extent by fears of an upcoming US recession - by far the most anticipated one. Highly regarded leading indicators have provided recession warning signals for over a year already. Consensus independent economist surveys* indicate a high probability of a recession and world trade has stagnated. Despite this, though, business profits keep surprising to the upside.

Capital market indicators do not yet reflect a material recession. Strong employment continues to support the US consumer, already with, on average, a relatively healthy balance sheet. A healthy US housing market and positive Builders' Confidence Index support overall consumer confidence. Corporate balance sheets are generally also strong. Manufacturing orders/inventory balances have stabilised, indicating stability in the manufacturing sector. The US administration continues to spend around 20% of GDP. Further to this, their Bipartisan Infrastructure, Inflation Reduction and CHIPS & Science Acts indirectly boost government spending by another fifth, increasing overall spending to almost a quarter of GDP*. Energy costs have flatlined, and pandemic-inflicted supply backlogs have mostly cleared.

All-in-all, we believe any upcoming, or even imminent, US recession may be a relatively shallow and short one. Seeing that it is, unlike other recessions, already preceded by a bear equity market and lower valuations, and the stock market discounting machine looking beyond the immediate, we refrain from being overly cautious.

Historic stock market trends accompanying individually (as we have currently) a new 52-week Nasdaq high, a double-digit first half performance*, and furthermore a third year in a US election cycle bode well for the second half of this year. Better than expected company results continue to support investor sentiment. Given that Artificial Intelligence-related stocks largely drove the market thus far this year, we see opportunities for many other quality stocks to still perform this year.

We appreciate all your support.

With best wishes.

Gerrit Smit
Partner – Head of Global Equity Management

** Source : Bloomberg, July 2023*

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