- It was notable how mixed regional equity markets were in May, with a considerable gap between winners and losers. The strength in Japanese equities stood out. We cannot help but note that this was constructive for our portfolio given that our bottom-up process led us to have a 17% weighting in Japan at the start of 2023.

- Arguments for Japanese shares tend to be top-down. They revolve around a potential departure from deflation and persistently low economic growth. Another great hope is for improvements from a corporate sector that has for years generated poor returns on equity and offered only weak governance. It is beginning to look as if coordinated efforts by the government, the Bank of Japan, and, particularly over the last year, by the Tokyo Stock Exchange are beginning to pay-off. Unsurprisingly, Warren Buffet's visit to Tokyo drove stories around the opportunities in Japanese shares, but these opportunities have been around for some time.

- NASDAQ's continued strength was also noteworthy, this month driven by a narrow set of mega-cap stocks perceived as benefitting from the AI opportunity. Chief among these was chip maker, NVIDIA, which surged on an eye-watering uplift in its guidance for the top-line. We leave it to the reader to judge if the narrowness in performance is sustainable, merely noting that the equally weighted S&P500 has never had a worse year-to-date versus its higher profile cap weighted comp.

- Elsewhere performance was weak across the board, with most other global indices down more than 3%. Sector performance also showed a substantial gap between the winners and losers. The backdrop remains tough. For example, US corporate profits recorded the steepest drop over three quarters since 2009, and Eurozone loan demand is falling at its fastest pace since 2008.

- Performance in the US was driven by strong gains in the NASDAQ, up 5.8%, with the S&P 500 flat for the month. European bourses all underperformed to varying degrees with the German DAX down 1.6% and the French CAC and UK FTSE both down more than 5%. Asia was more mixed with Japan's Nikkei 225 surging 7% versus China's Shanghai Composite which was down 3.6%.

- On a sector basis, Technology and Telecoms led performance, up 8% and 3.5%, respectively. All other sectors were in negative territory with Energy the biggest laggard, down 10.5%. Materials, Staples, Utilities and Financial Services were also very weak, each falling more than 5%.

- The AUD fell 1.7% against the USD with commodities also weak. The Bloomberg Commodity Index was down 6.1% while the West Texas Intermediate fell by 11% on growing concerns around the health of the global economy and resilient supply driven by Russian production.

H&R BLOCK

- In terms of new positions, the fund gained exposure to US-based tax specialist, H&R Block (HRB). While a weak tax season and some execution issues have contributed to the recent bout of share price weakness, we think the stock is now very cheap, trading on a ~15% FCF yield. With no balance sheet risk, and a ~$960m buyback programme underway (~20% of the market cap), we think HRB has time to address its issues while we are being reasonably compensated in the interim.

- Our holding in Japanese industrial conglomerate, Mitsubishi Electric (ME) was one of the biggest contributors to performance. With ME doing a much better job at realising price rises, earnings' momentum is accelerating across the group (FY24 EBIT guidance of 27% growth). In keeping with Japan Inc's greater focus on shareholder returns, management also announced a ~2% buyback at the last result, its second buyback program in 20 years. While the stock has risen sharply in recent months, asset-based multiples remain undemanding. Hence, given the likelihood of strong momentum continuing and a solid balance sheet to pursue more capital management, we think the risk/reward remains attractive.