Monthly Market Commentary

A broad-based decline in global equities left investors with few places to hide this quarter. A surge in oil prices and bond yields were the two most noteworthy developments. Some would argue that a market pullback is only natural after a strong first half of the year. We are of the view that recent weakness is a continuation of a turbulent period for equity markets that started last year and that is more reflective of underlying economic realities.

The reality that interest rates might have to stay higher for longer drove bond yields to fresh, multi-decade highs and weighed heavily on investor sentiment. Supply concerns pushed oil prices significantly higher and further exacerbated the upside risk to inflation. At the same time, the AI hype that propelled tech stocks earlier in the year fizzled out somewhat and led to the tech sector underperforming the broader market. Risk indicators like the VIX rose, reminding investors that coming out of the woods unscathed is not a given amidst the most aggressive monetary tightening cycle in recent history.

Almost all major equity indices suffered losses in the third quarter. The broad-based S&P 500 and the tech-heavy NASDAQ fell by -3.6% and -4.1%, respectively. Asian markets were also weak with the NIKKEI down -4% and Hong Kong's Hang Seng down -5.9%. In Europe, the Euro Stoxx 50 dropped by -5.1% with both the French CAC and the German DAX in the red. UK's FTSE 100 was the only notable index that bucked the trend and finished up 1%.

Energy was the only sector that delivered meaningful positive returns of +10.4% on the back of resurgent oil prices. Utilities were at the other extreme, suffering a -9.9% drop with a surge in bond yields the main culprit. Tech is also worth noting, down –6.2%, and underperforming the broader market for the first time this year as excitement around AI subsided. All other sectors were down low to mid-single digits in a broad-based market weakness.

Oil prices saw their strongest quarter since June of last year, increasing significantly by 28.5% and closing above the $90 mark. Constrained supply rather than a surge in demand is to blame with other commodity prices increasing only modestly (Bloomberg commodity index up just 3.3%). US treasury yields surged, with the 10-year increasing by a whopping 73 bps and closing the quarter at 4.57%, the highest since 2007. The VIX jumped by 4 points from June lows not seen since pre-COVID to 17.5 points. The USD gained against nearly all major currencies.

Two American firms contributed most to the Fund's performance this quarter. On top was H&R Block, a tax preparation company with operations in the US, Canada and Australia. It delivered a better-than-expected margin and stronger buybacks that have propelled the shares materially higher. A close second was CF Industries, an agricultural fertiliser manufacturer. Strong results and the gas price differential between Europe and the US stabilising, supported the shares.

The largest detractor to performance this quarter was Swiss pharmaceutical giant Roche (see stock in focus). Despite recent weakness we see significant value and took advantage of the weakness to add to the position. Brazilian brewer Ambev was another detractor. Weakness in the Brazilian Real and a P/E derating on the back of worsening sentiment on Argentina, one of their key export markets, were some of the main drivers.

The fund initiated a new position in KDDI, the second biggest Japanese telecom. Low levels of debt provide balance sheet optionality while carrying a low valuation relative to earnings potential and growth. The fund exited two positions on valuation grounds after reaching our price targets - CNQ, a Canadian energy company, and Loews, an American insurance conglomerate.

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