Monthly Market Commentary

Global equity markets rebounded strongly in May with strength in four mega-cap technology shares (Microsoft, Nvidia, Apple, Alphabet) driving US outperformance over other regional indices.

Investor sentiment was buoyed by some softer-than-expected US economic updates (cooler CPI print, weaker jobs data), renewing hopes of a Fed rate cut by year end which also sent yields on government bonds lower. For now, investors seem to be favouring the narrative that sees lower interest rates as only good for equity valuations rather one that takes in the idea that risks to the economy (and therefore to corporate earnings) are the reasons why interest rates can fall.

This view will likely hold for as long as investors have confidence that future cash flows will materialise, with some pointing to still solid headline corporate earnings growth as reasons to be optimistic on this front (S&P500 Q1 EPS +5.9%). The issue though is that there are signs a slowing economy is indeed beginning to weigh on corporate earnings. For example, if you strip out the Magnificent 7, earnings per share for the S&P493 in Q1 actually fell 1.80%. This also goes to highlight just how concentrated US equity markets have become, with more than half of the S&P500 gains in May attributable to just four stocks.

US markets dominated performance in May with the NASDAQ and S&P500 up 6.9% and 4.8% respectively. US small caps also delivered strong performance with the S&P600 Small Cap Index up 4.9% to finish broadly flat over a two-month time horizon. European bourses lagged with the French CAC amongst the weakest, up only 0.1%, while Germany's DAX and the UK FTSE up 3.2% and 1.6%, respectively. Asian markets were quieter with Japan's Nikkei225 up only 0.2% and China's Shanghai Composite Index closing down 0.6%.

IT and Communications delivered exceptional performance, up 8.5% and 6.4%, respectively. Utilities also did well, up 6.9%, benefitting from the lower yield dynamic. Most other sectors delivered between 2% to 3% during the month, however it was notable how weak Consumer Discretionary and Energy were with both essentially flat.

The AUD rose 2.8% against the USD, with the Bloomberg Commodity Index also up 1.3% despite a 6% fall in WTI Oil prices. The VIX fell 2.73 points to close at 12.9 - very low vs history. Against the backdrop of a lower rates outlook, yields on US 10yr Government Bonds fell 18bps to finish at 4.50%.

In terms of new positions, the Fund recently gained exposure to gold miner, Newmont Corporation. In addition to the stock's prospective ~8% Free Cash Flow yield at current gold prices, we were also attracted to the group's well-diversified portfolio of long-lived assets in geopolitically attractive regions, which has only been enhanced by its acquisition of fellow gold miner, Newcrest. Given its status as one of the world's lowest cost producers with an all-in-cost base of $1,250, we feel confident that Newmont can continue generating strong cash flows with management indicating a policy of returning all free cash flow to shareholders once the company's asset disposal program is complete.

German-based consumer brands and adhesives manufacturer, Henkel was the Fund's biggest contributor to performance in May. Shares rose strongly after management upgraded FY24 EBIT guidance by 11% (two months after previously being issued) in a Q1 pre-release. Driving the upgrade was both solid operational performance on the margin front and a lower drag from FX/M&A. Given solid momentum, a strong balance sheet, and sales-based multiples which continue to price in margins below what we believe the business can earn on a through-cycle basis, we think risk/reward remains attractive and will continue to hold even after recent share price strength.

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