Alpha Beta
PARTNERS

INVESTMENT UPDATE

JUNE 2024

FOR PROFESSIONAL INVESTORS ONLY

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May proved a more positive month than April for risk assets. Notably, industrial commodities surged ahead with mainstream equities performing nicely too despite higher valuations and geopolitics offering no reason to feel particularly optimistic. As ever, we offer a deeper dive for clients in the update that follows.

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The economic backdrop in America remains robust with growth being recorded consistently stronger than all other larger countries. The Federal Reserve kept interest rates on hold, in line with expectation and Consumer Prices Inflation printed a little lower than many had expected at 3.4%. The resulting backdrop proved positive for risk assets, despite Treasury yields remaining stubbornly above the important 4% level by month end. Liquidity made a return during May with Mrs Yellen at the US Treasury continuing to issue Treasury Bills.

Quantitative Tightening will be scaled back to $25bn per month with the ongoing prospects for liquidity positive for the balance of 2024. American growth-oriented stocks performed well, and technology names led by Nvidia saw a return to positive momentum. Such is the rapid-fire growth of Nvidia that the firm is now larger than the entire German stock market; its growth in 2024 alone is worth more than the market capitalisation of Amazon.

With liquidity and government spending powering much of US growth and fuelling the tight labour market its hardly surprising GDP remains robust, and inflation appears to have plateaued slightly higher than the Federal Reserve 2% target.

Whilst positivity remains the dominant market force, there are risks to be considered. Where debt expands to levels where markets become uncomfortable then we tend to see government bond yields rising to compensate for higher risk to capital repayment – effectively a hike in interest rates. This has knock-on consequences to collateral, such as real estate and other asset classes used for liability matching. This is where banks can face difficulties, as we saw with Silicon Valley Bank last year. The UK witnessed something similar under the short-lived Mrs Truss government where pension schemes were impacted, and UK Gilt yields became very volatile for a short period until the Bank of England stepped in.

The chart below shows up-to-date United States GDP break down.

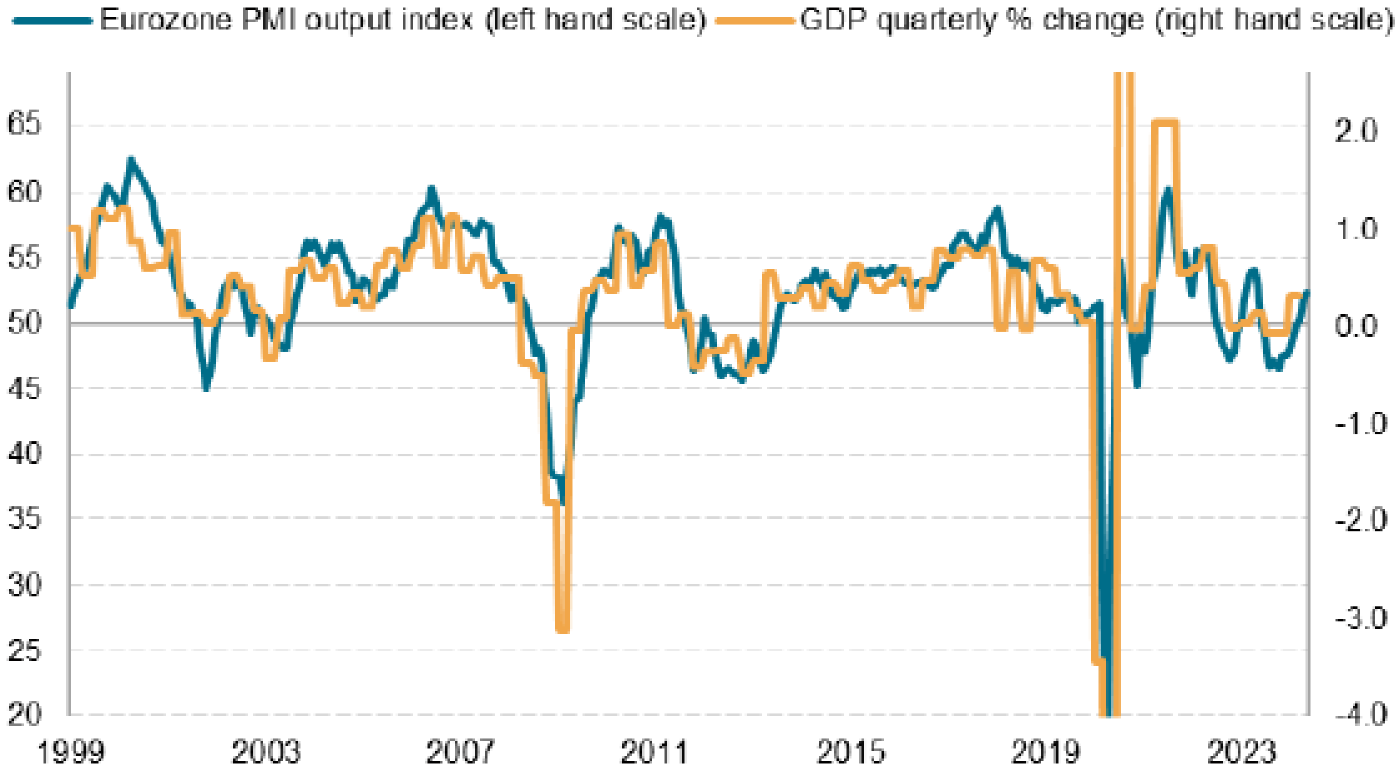
GDP components					
	% of GDP	1Q24	4Q23	3Q23	2Q23
• Consumer spending	68.9%	2.0%	3.3%	3.1%	0.8%
• Government spending	17.1%	1.3%	4.6%	5.8%	3.3%
Federal: 6.6%		-0.7%	2.4%	7.1%	1.1%
State/local: 10.6%		2.6%	6.0%	5.0%	4.7%
• Net exports of goods and services*	-4.3%	-0.9	0.0	0.0	0.58
Exports: 11.1%		1.2%	5.1%	5.4%	-9.3%
Imports: -15.4%		7.7%	2.2%	4.2%	-7.6%
• Fixed investment	17.9%	6.0%	3.5%	2.6%	5.2%
Nonresidential: 14.7%		3.3%	3.7%	1.4%	7.4%
Residential: 3.4%		15.4%	2.8%	6.7%	-2.2%
• Change in private inventories*	--	-0.5	1.3	0.0	-2.2
	Real GDP	**1.3%**	**3.4%**	**4.9%**	**2.1%**

Source: Charles Schwab, Bloomberg, Bureau of Economic Analysis, as of 1Q2024. Components based on real GDP annualized q/q % change. *Represents contribution to percent change in real GDP. Numbers may not add up to 100% due to rounding.

Against the headwind of more US tariffs and rebounding shipping costs, the uptick in Chinese economic activity does appear to have settled back despite the relentless push to resume an export campaign for battery electric vehicles and other green infrastructure to western economies. The People's Bank of China remains likely to add stimulus and to allow the Yuan's value against other currencies to drift lower. We note the PBOC shifted interest rates to their lower boundary, facilitating such a move.

In Europe we were pleased to note a healthy rebound in economic activity from the shallow recession impacting Germany in particular. The uptick in GDP growth and the Eurozone Purchasing Managers Index (shown in the chart below) makes pleasant reading and supports our ongoing support at portfolio level. Despite a surprising rise in German inflation, from 2.2% to 2.4% we still anticipate Mrs Lagarde, Head of the European Central Bank, announcing a cut in interest rates in the near term, and likely ahead of the Federal Reserve.

Eurozone PMI vs. GDP



Data compiled May 23, 2024 including flash PMI data for May and GDP data to Q1 2024.
PMI (Purchasing Managers' Index) based on 50 = no change on prior month, covers goods and services.
Sources: S&P Global PMI with HCOB, Eurostat via S&P Global Market Intelligence.
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At home in the UK, we saw equities performing well, albeit overdue and from a low valuation base. The Bank of England kept rates on hold but hinted at a cut later this year and in line with our forecast made here in recent months. Whilst not obvious, UK inflation has fallen back to 2.3%; lower than America and Eurozone economies. Gilt yields pushed higher coincidental with an announcement of the General Election on 4th July and apparent likelihood of a Labour government. The benchmark 10-year Gilt now offers a 4.3% yield.

Meanwhile in Japan, economic renaissance continues supported by a very much weaker Yen and revised Bank of Japan policies around government bond yields. We note the central bank has intervened twice to prevent the Yen from falling further. We do expect some tighter monetary policy to assist before too long. We also note an uptick in Japanese inflation to 2.6% and wage settlements negotiated at higher levels than has been the case for some time.

Commodities, notably industrial metals, have seen strong performance during May with copper and silver prices rising higher. All other key commodity values including gold, lithium and uranium have re rated as the global reflation continues and demand grows, oil being the only notable laggard of significance so far.

Geopolitics cannot be modelled by investment managers but clearly have the power to move markets. Wars in Ukraine and Gaza remain ongoing. Military activity between Taiwan and China have escalated in recent months. The election in the United States moves closer with implications for markets should the outcome be unexpected. Mr Trump appears to be in the ascendency with his New York "hush money" trial verdict potentially boosting the Republican's electoral appeal to his constituency, who believe his treatment is akin to that of Mr Imran Khan in Pakistan.

At portfolio level we executed the changes discussed here last month. Namely, we took profits in Japan and Europe but remain invested and with a positive outlook. We shortened duration in the fixed income allocation to protect against a move to higher yields impacting longer duration stock. Timing of this move has already proved beneficial. We cut back our emerging markets and China allocation to more modest levels, preferring to bolster US holdings which continue to benefit from clearer and more positive visibility and growth. Overall, we are good shape year-to-date with performance and risk aligned and valuations moving steadily higher in a controlled manner.

As ever, we thank you for continued support and look forward to updating you next month.

Written by the Alpha Beta Partners Investment Team.

All sources Bloomberg unless otherwise stated.

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