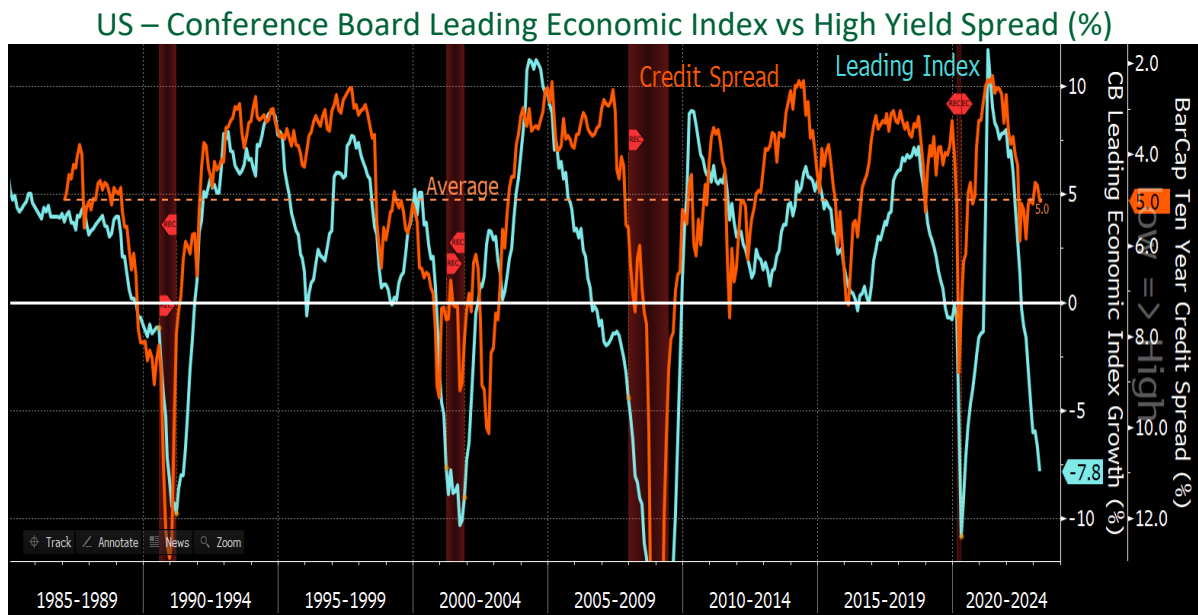


"It is easier to resist at the beginning than at the end."

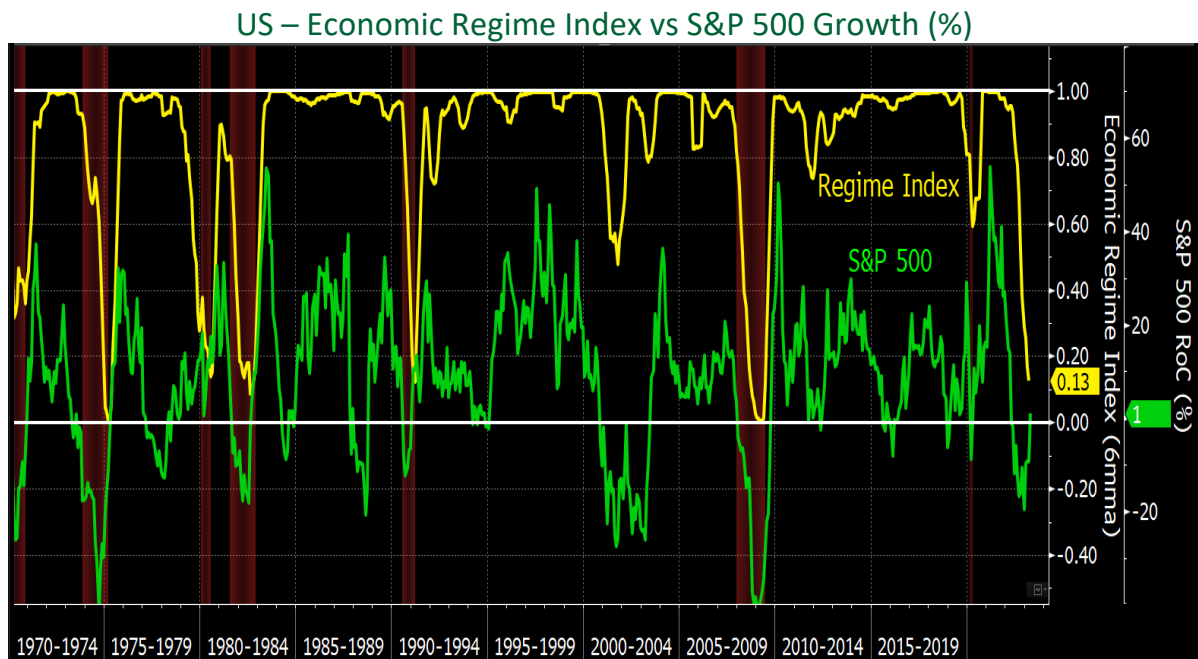
Leonardo da Vinci

1. RECESSION RISK

The most anticipated US recession has not yet materialized.



The Leading Economic Index is currently already at the extreme negative levels it has been at during previous recessions. The High Yield Spread, though, (on an inverse scale) is still at its average level.



The above Economic Regime Index (reflecting changes in capacity utilization, jobless claims, etc.) is also already at a recession level. We can conclude from these charts that we may well face a relatively short recession – as we had with the Pandemic.

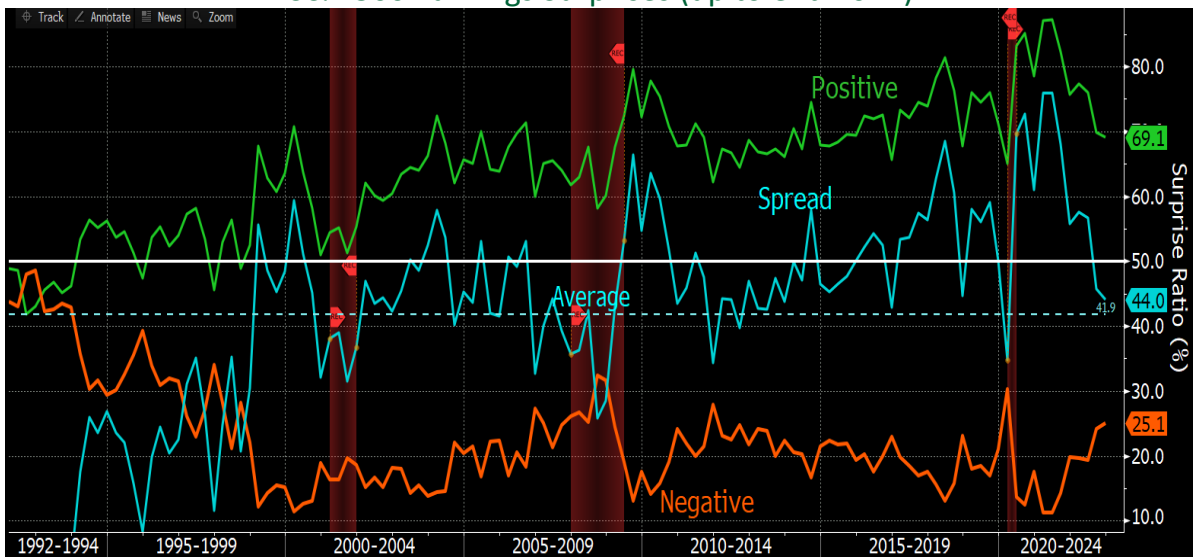
2. REPORTING SEASON

The first quarter 2023 reporting season is in full swing. Just over half of the US's S&P 500 constituents have already reported, and just over forty percent of the European constituent peers. This table summarizes the two regions' results:

	S&P 500 1Q2023 Results (28 Apr 2023)			Bloomberg BE 500 1Q2023 Results (28 Apr 2023)		
	Growth	Surprise Factor	# +ve Surprises	Growth	Surprise Factor	# +ve Surprises
Sales	4.4%	2.1%	66.0%	6.7%	2.5%	69.5%
Earnings per Share	-0.1%	6.6%	79.8%	47.6%	34.5%	65.0%

Results have thus far predominantly been positive and better than expected. The S&P 500 constituents have delivered fair top line growth, with earnings trading water. The latter, especially, came in over 6% better than expected, with 80% of the businesses delivering better than expected. Overall European results have been even better. We would, though, remind our clients that the latter results are more skewed towards Financials, which did particularly well off a low base.

S&P 500 Earnings Surprises (up to end 2022)



The current S&P 500 Earnings Surprise Factor of 80% is at an elevated level compared to historical norms (the green line) - a full 10% up on the level at the end of the previous quarter. Current results have supported many share prices over the past two weeks.

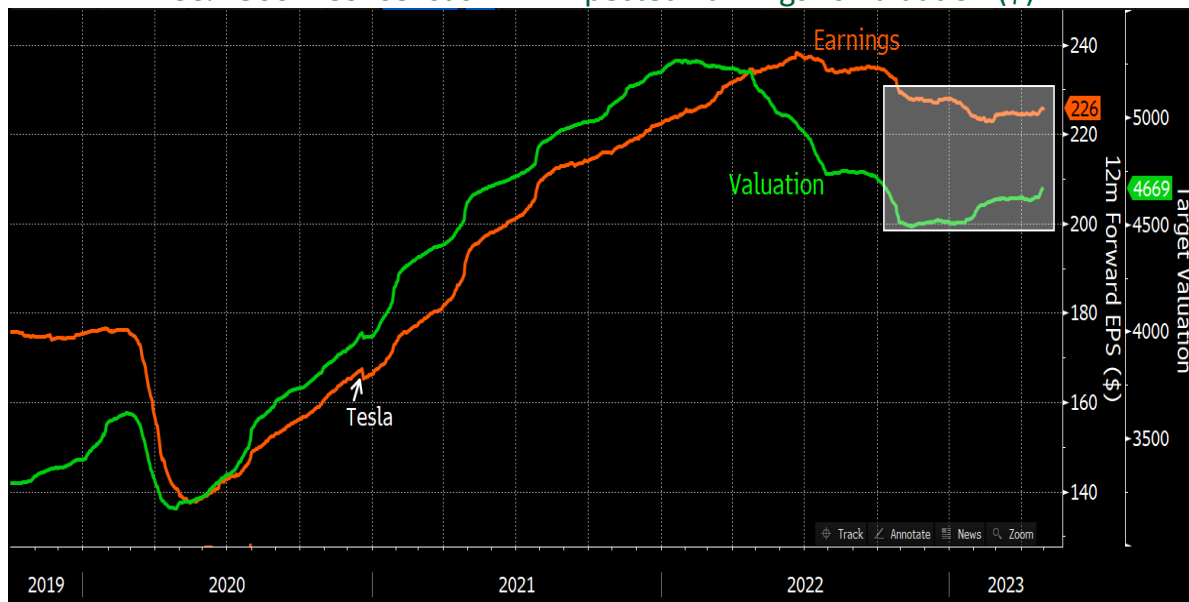
Dollar vs Trading Basket Currencies and Dollar Growth (%)



Currency effects continue to play a role in results. As many of the S&P 500 constituents are global operators, many reported continued earnings dilutions from foreign shores. As the above chart depicts, although the Dollar has been depreciating (the green line), at the end of March it was still 4% stronger than a year ago (yellow line). Many companies referred to constant currency sales in this order higher than Dollar sales. The reverse, of course, can be said of European results. On a constant currency basis, therefore, it seems US companies have continued outpacing European peers.

The Dollar is currently (29 April) at a level of -1.3% against its level a year ago. Chances are that it is now becoming a tailwind for the current quarter's S&P 500 results.

S&P 500 – Consensus 12m Expected Earnings vs Valuation (\$)



The above chart reflects consensus Earnings and Target Valuation levels for the S&P 500 Index. Following a period of deteriorating Earning expectations, it seems to have stabilized, with marginal increases recently. Valuation levels have, for a while, been increasing following the sharp decreases last year with the rising interest rates. The current S&P 500 upside of +12% is close to the average of +13% since the Financial Crisis. We believe the combination of all these is constructive for equity investing.

3. GROWTH TO VALUE ROTATION

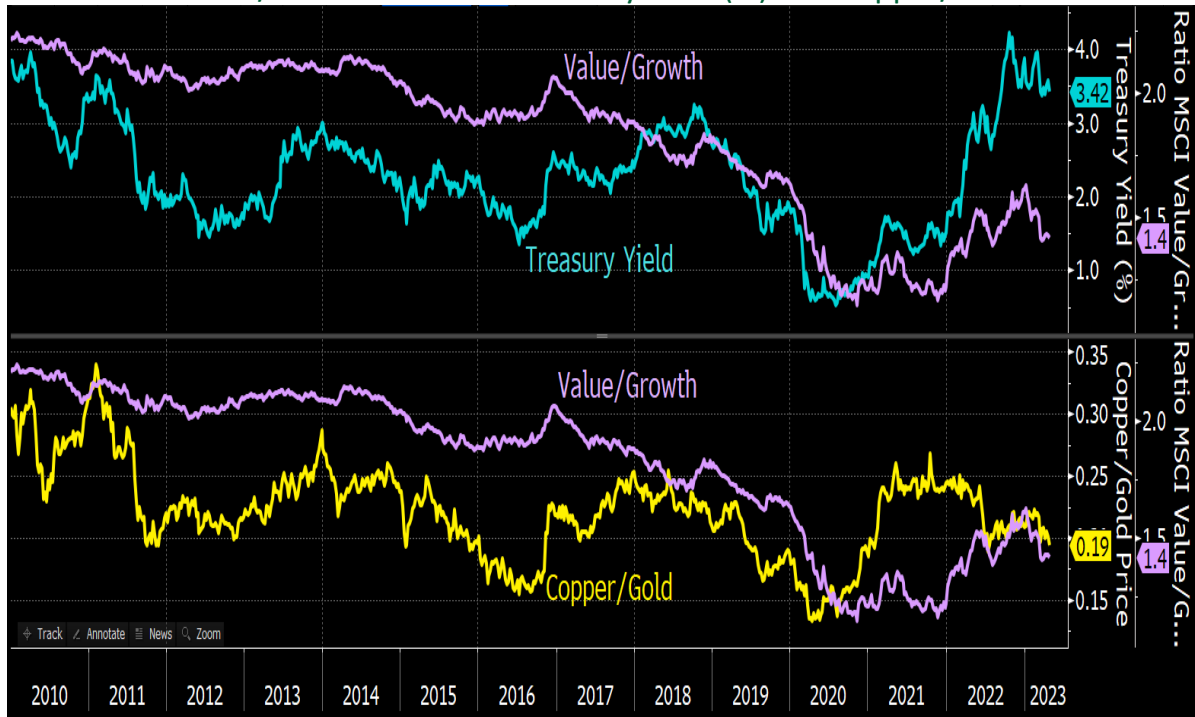
The Value style of investing outperformed Growth by almost a third last year (considering the S&P Value and Growth indices). It has been an exceptional relative performance under the dire capital market circumstances of 2022. This performance stands out against the long-term relative compounded outperformance of Growth of +4% p.a. over and above Value's delivery. Investors must seriously consider when to re-engage with Growth again.

There are indications that stars are in process of aligning for the Growth style of investing to resume its structural outperformance trend. The necessary conditions under which Value can continue to outperform on a sustainable basis seem to have run most of their course. Whilst core US inflation remains somewhat sticky, the Atlanta Fed Sticky Inflation Index seems to be in process of rolling over with Accommodation Rent the main remaining culprit. US headline inflation has been dropping nicely and the Federal Reserve's task of controlling rates through hiking rates seems to be mostly done. US interest rates are in process of settling at lower levels than feared just a few months ago.

We expand on these themes in the following charts:



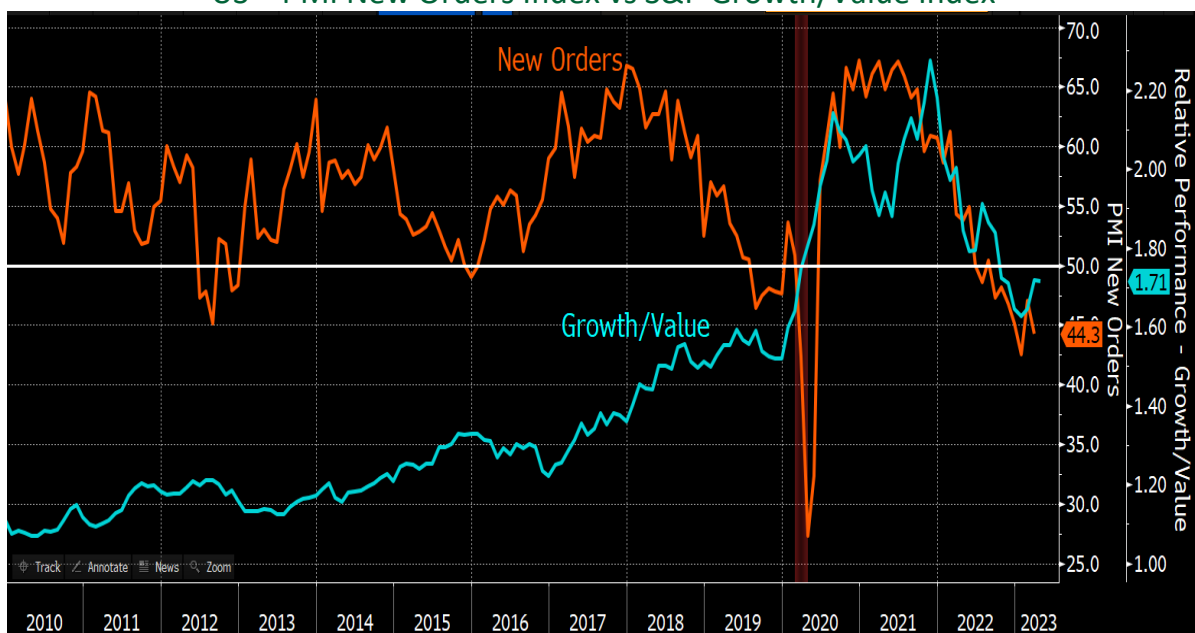
S&P Value / Growth Index vs Treasury Yield (%) and Copper/Gold Ratio



Considering the top section of the above chart, the Treasury Yield has dropped from over 4.2% to 3.4% (the blue line), with the Value/Growth Index (purple line) following suit. On the economic front, the US growth outlook seems moderate at best with little reason for much higher rates. Investors are expected to soon yearn for growth again, and with valuation multiples down by a third since the end of 2021 and now on long-term average levels, they may now be more willing to pay for growth.

This economic (and organic) growth issue is confirmed in the bottom section of the chart – the Copper/Gold ratio (broadly reflecting perceptions of economic growth) has been slipping recently. This also argues rather for Growth at the expense of Value.

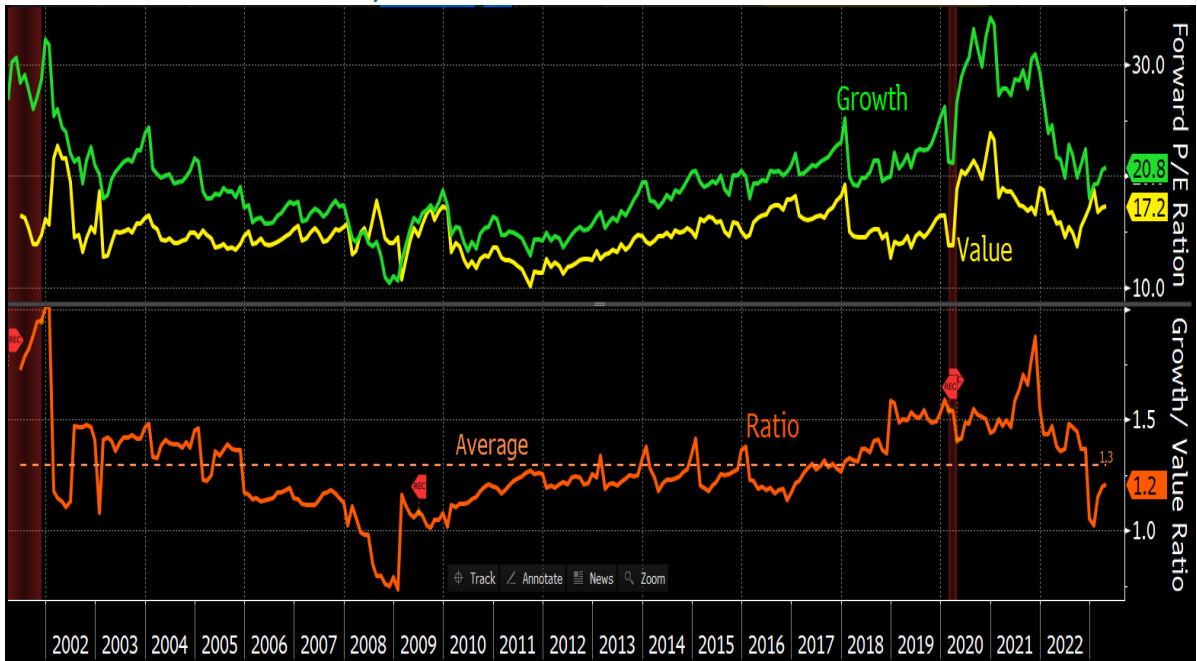
US – PMI New Orders Index vs S&P Growth/Value Index



The Manufacturing New Orders Index in the above chart has dropped sharply from the beginning of 2021 and has now been in contraction territory for almost a year. The Growth/Value Index has come down with it. With supply chain complications following the Pandemic now mostly resolved, we cannot expect the Orders Index to stay in its contraction territory for too long. On this basis, investors may be considering switching opportunities to Growth.



Forward P/E Valuation Ratios – S&P Value vs Growth

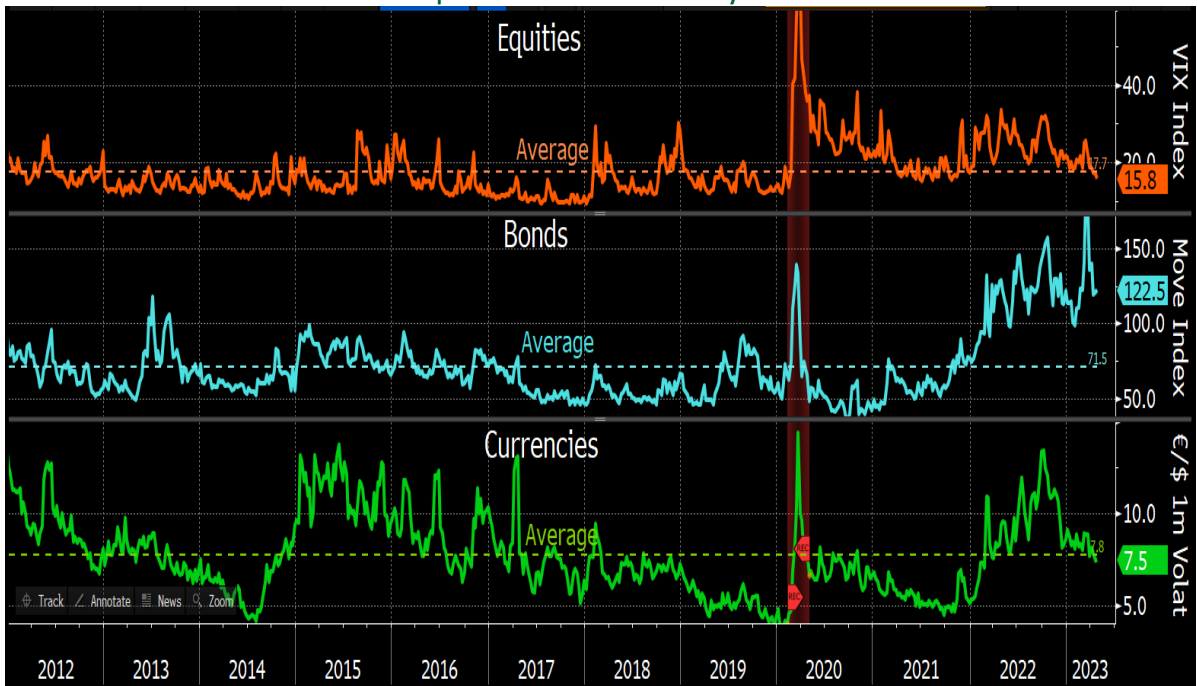


Logically, Growth is usually valued higher than Value. The relative valuation ratio (the orange line in the above chart) is, though, currently below its long-term average. Especially with a tempered economic and earnings growth outlook, this relative valuation level is now more attractive than what it has been since 2017.

There are already signs of Growth's comeback.

4. VOLATILITY

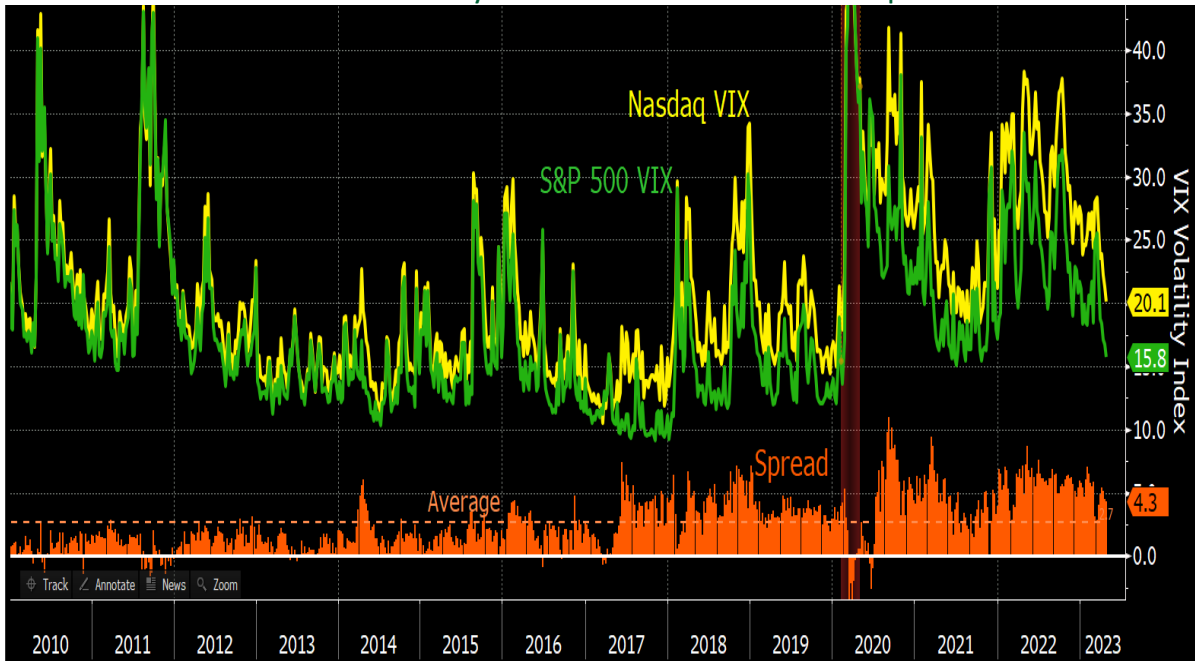
US Capital Market Volatility Indices



As depicted on the preceding chart, Equity and Currency volatilities have dropped materially, with both currently close to long-term average levels. Volatility in the Bond market remains elevated. Equity investors, therefore, may wonder whether Bonds may again unsettle their asset class. With inflation dropping nicely, the Federal Reserve's tightening task about done, a weak economic outlook and High Yield Spreads being stable, we do not currently have material reservations in this context.

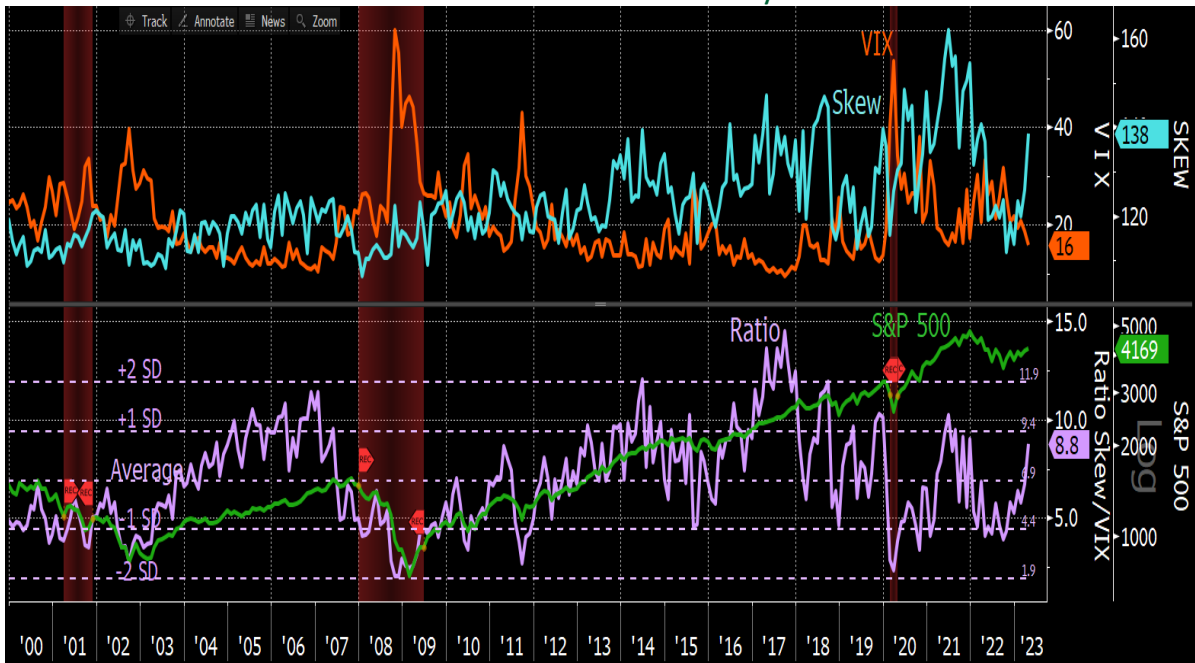


VIX Volatility Indices – S&P 500 vs Nasdaq



The Nasdaq VIX Index (the yellow line in the above chart) has also moderated materially, reflecting the moderation of the volatility in Technology shares. Whilst not back on average yet, its spread (the orange bars) with the S&P 500 VIX Index has also narrowed materially. This indicates investor risk appetite to invest for growth in process of returning.

S&P 500 – VIX vs SKEW Volatility Indices



The SKEW Equity index (a different volatility measure) has increased sharply recently (the blue line in the above chart). Its ratio with the VIX Index (as reflected in the purple line in the bottom section of the chart) indicated a strong Equity Buy signal late last year. Its current trend is supportive of share prices.

5. DOLLAR VALUE

The overly strong Dollar has hampered US company earnings for over five years, as many of them are global operators which has resulted in less valuable offshore earnings. As we touched on in par. 2, it seems this headwind is slowly becoming ‘water under the bridge’.

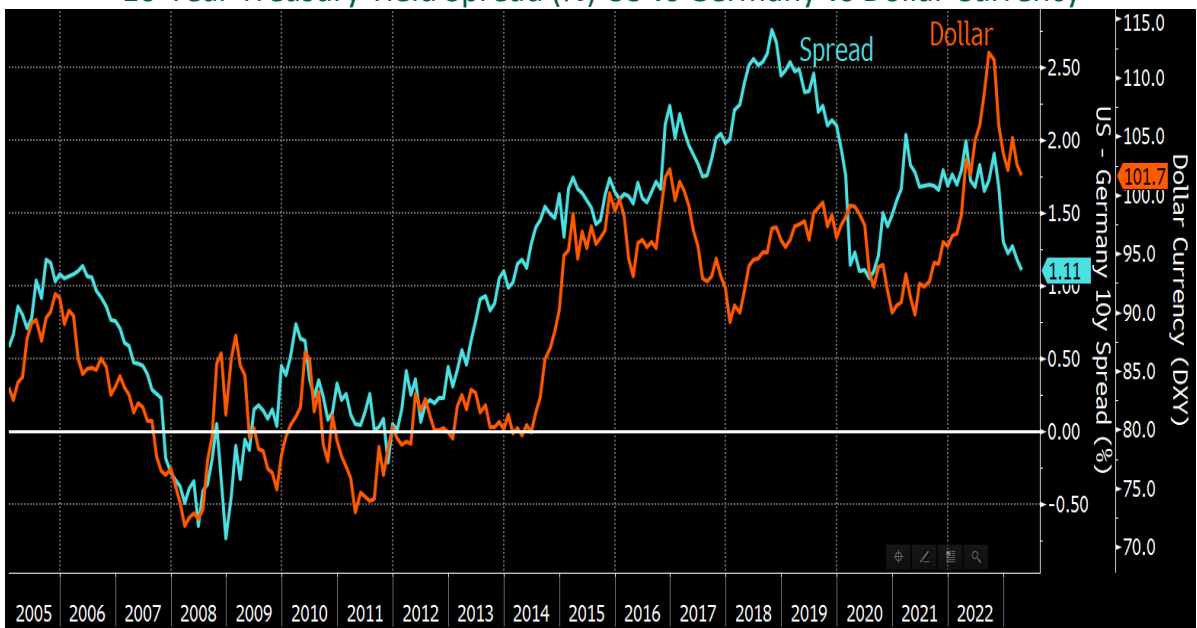


US – Twin Deficit vs Dollar



The US twin deficit is currently continuing its pre-Pandemic growing trend that started in 2015. Its safe haven status attracted huge reserves since the Pandemic, but with a more normalized global economic environment, the twin deficit constraints may resume its effect on the currency again.

10-Year Treasury Yield Spread (%) US vs Germany vs Dollar Currency

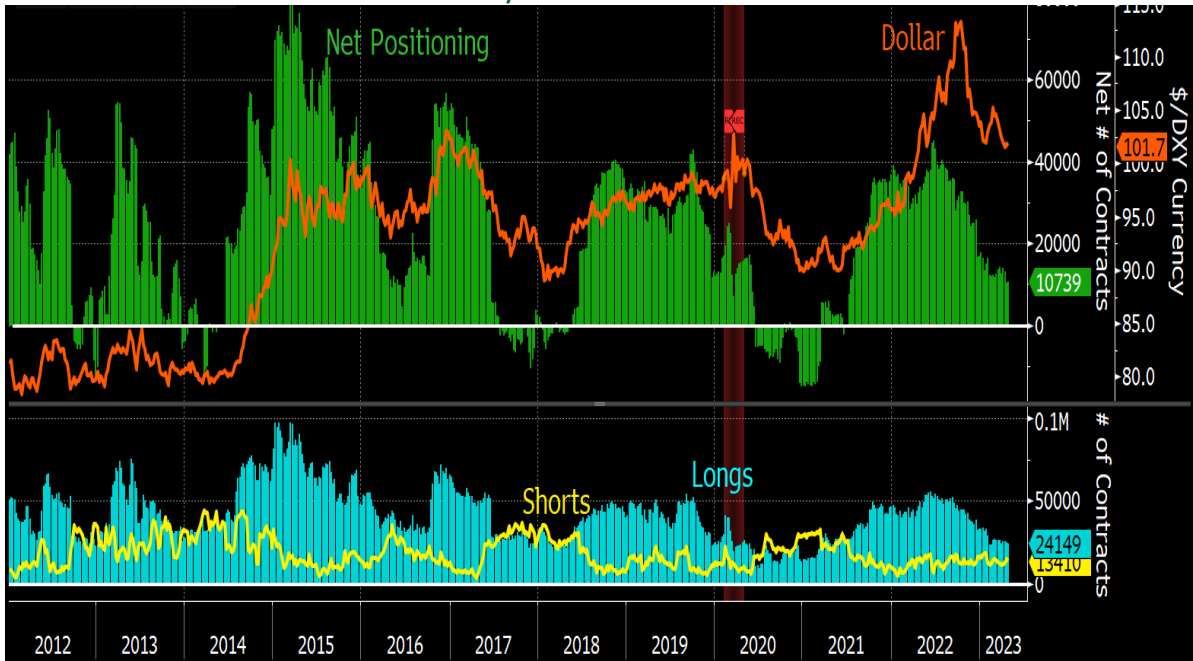


Apart from the haven status, the positive spread between US and European (German in the chart) interest rates has also attracted reserves into the US, and clearly benefitted the Dollar. The spread is currently close to a ten-year low, with the recent drop in the Dollar correlating with the drop in the yield spread. It seems US interest may also have contributed to a weaker Dollar.

We take cognizance of the active market positions taken in the Dollar in the chart following on the next page. Considering the bottom section of the chart, the Dollar short positions have stayed relatively stable over the recent past (the yellow line), while the long positions have dropped materially (the blue bars). The net positioning of the longs against the shorts shows a drop of ~40,000 contracts to ~10,000 contracts currently (the green bars). There is a clear correlation between these net positioning number of contracts and the Dollar, with the former reflecting some risk of further Dollar weakness. Whilst we cannot speculate on the outcome of the Ukraine war and China's economy reopening, these may become further factors in determining the Dollar's value.



Dollar vs Dollar Currency Futures Number of Contracts Issued



6. TECHNICAL PICTURE

Dollar vs 50- & 200-Day Moving Averages



The Dollar is technically in a weak position – it has broken downwards through both its 50- and 200-day moving averages, it triggered a ‘death cross’ (the 50-day crossing the 200-day moving average), both averages are in downward trends and its current value is currently below both moving averages.

Against this, the S&P 500 Index is currently in the opposite, positive position on all these measures.

Gerrit Smit

**Partner - Head of Global Equity Management
Stonehage Fleming Investment Management Limited**

6 St James’s Square
London
SW1Y 4JU

T +44 20 7087 0000
Email gerrit.smit@stonehagefleming.com
www.stonehagefleming.com/gbi



RISK DISCLOSURE

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Stonehage Fleming Investment Management Limited
6 St James's Square
London
SW1Y 4JU

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