

*"Greatness of spirit is accompanied by simplicity and sincerity."*

*Aristotle*

## 1. US INVESTOR CONFIDENCE

US investor confidence seems to be well on the mend off its recent low base:

State Street Investor Confidence Index vs S&P 500



The above confidence index reflects perceptions of the general state of the economy as it relates to business. It recently has been in the doldrums, but is in process of recovering. This reflects similar constructive trends for the institutional Put/Call ratio and the Individual Investor Sentiment Index.

US – Net Non-Commercial S&P Futures Positions vs S&P 500

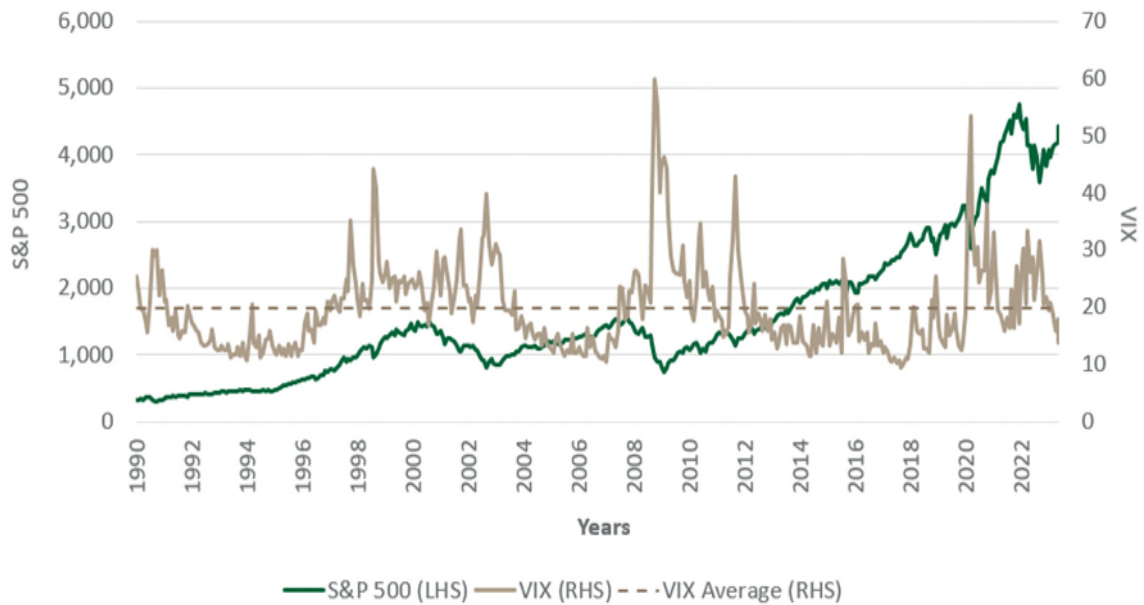


Contrary to the above, the net non-commercial S&P 500 futures positions have recently been in deep negative territory - even worse than during the Pandemic. This situation is currently in a steep recovery process, but still in negative territory. Should this situation continue to normalise, it can further support investor sentiment.

## 2. MARKET VOLATILITY

Equity market volatility has calmed substantially:

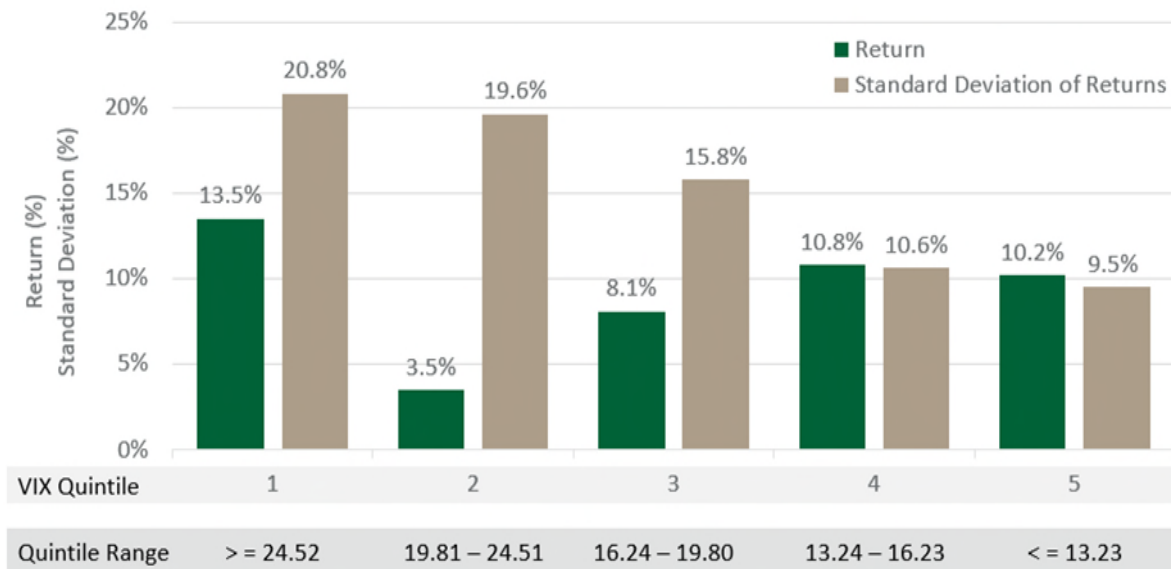
S&P 500 vs VIX Volatility Index



Volatility is currently well below average and currently fluctuates between its fourth and fifth quintiles:

S&P 500 Return vs VIX Quintile Bucket

Since 1990



High volatility (in the first and second VIX quintile buckets) historically was associated with both the best (first quintile) and the worst (second quintile) returns. This is clearly the riskier environment for investing.

Low volatility (in the fourth and fifth quintile buckets) historically was associated with double-digit returns, second best only to the highest return (and highest volatility) bucket. The current investment environment therefore seems the most favorable in this return/volatility context.



### 3. US VALUATIONS

The AI-inspired revaluation of the S&P 500 over recent months has brought equity valuations into the spotlight:

#### US – Next Twelve Month P/E Valuations: S&P 500, Technology, Dow Jones and S&P 500 ex Technology



Technology has re-rated close to record levels, with the S&P 500 and Dow Jones index P/E's still well below their respective record levels. The S&P 500 ex Technology is at a low 16.7 multiple, even lower than the Dow Jones's multiple. This reflects good relative value in the non-technology pool of S&P 500 constituents. On a relative (to S&P 500) basis (the bottom section of the above chart), Technology currently trades well above its 2021 peak levels.

#### S&P 500 – 12m Forward P/E Valuation vs Market Breadth



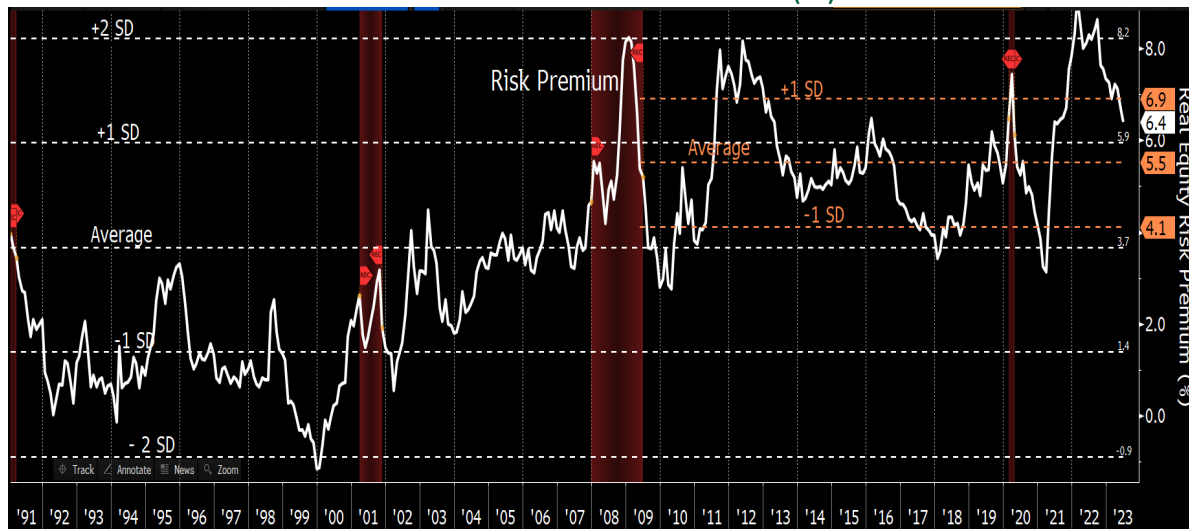
Separate to the above, we take cognisance of the continuing rerating process where the P/E multiple has recently crossed its upper band (the red block in the upper section of the above chart). This rerating process is tested against the market breadth (% of S&P 500 members above their respective 50-day moving averages). The rising lows of this breadth (see the orange supporting line) supports the view that the rerating process can continue.



Absolute S&P 500 P/E multiples are currently marginally above average, whilst the absolute risk premium is on its long term average. The latter, in particular, concerns some investors who are of the opinion that the premium should be at a higher level reflecting a lower interest rate regime than before the Financial Crisis.

Whilst the preceding view may have some merit, we believe there is also merit in considering the real risk premium:

S&P 500 – Real Risk Premium (%)



Resulting from still relatively high inflation levels, the Real Equity Risk Premium is currently well above its long term average, and also above its post Financial Crisis average. It can absorb a further drop in Inflation (of say 1%+), and still be at attractive levels.

Barring some individual stock valuations, we conclude from the above that stock market valuations should not currently deter investors from taking responsible equity exposures.

#### 4. INTEREST RATES

US – Inflation vs Treasury Yield (%)

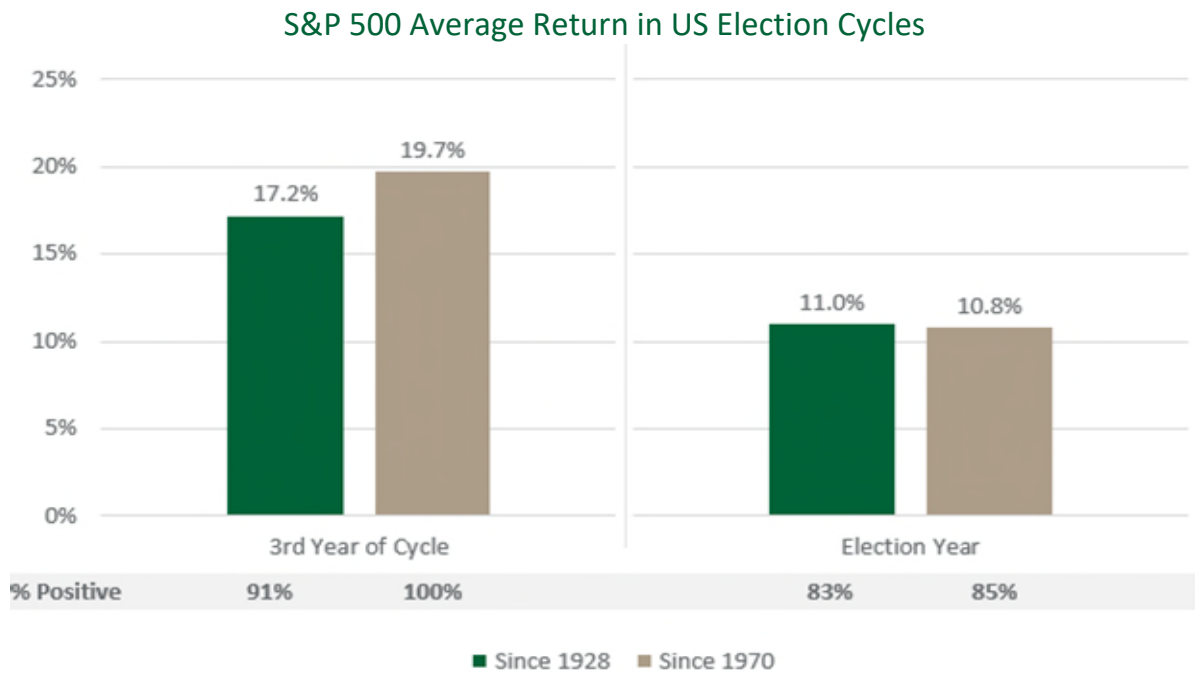


Interest rates have been consolidating at a lower level than what many have previously thought. Persistent views of higher rates are challenged by the above chart depicting that peak inflation levels (see the arrow indicators) are followed by lower interest rates. Real rates are still in minor negative territory (the green bars), but low real rates have been the norm for long and we believe there is less likelihood of much higher interest rates.



## 5. US ELECTION

With the next US election barely a year and a half away, it is worth reminding ourselves of stock market performance in this context:

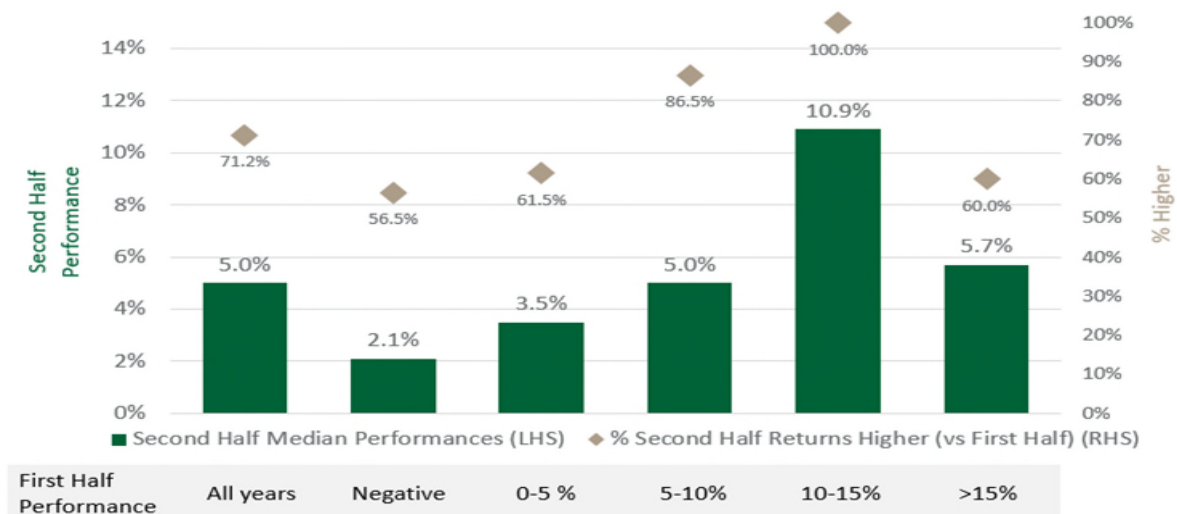


The third year in election cycles have historically rendered strong returns. Over the past fifty years the S&P 500 Index returned on average +19.7%, and furthermore, all of those third years delivered positive returns. Results during the election years have still been in double-digits, but only with an 85% probability of a positive return.

## 6. SECOND HALF OF YEAR PERFORMANCE

The S&P 500 delivered a double-digit performance (+11.3%) over the first half of this year. The chart below considers the historic level of second half performances:

**S&P 500 - Second Half of Year Performance Following Certain First Half Performance (%) 1950 - Current**

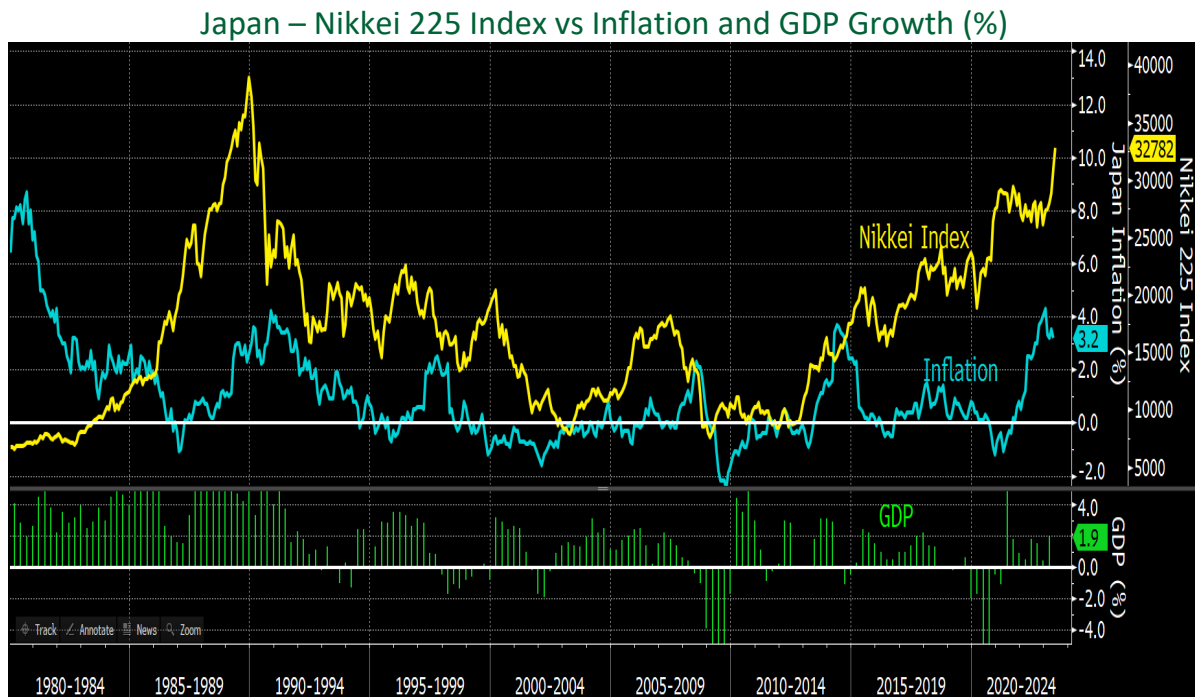


A 10-15% first half performance bucket delivered on average a +10.9% performance over the following six months. This is the best second half performance level for any of the performance level buckets over the first half of the year. Furthermore, all of those second half years delivered positive returns.

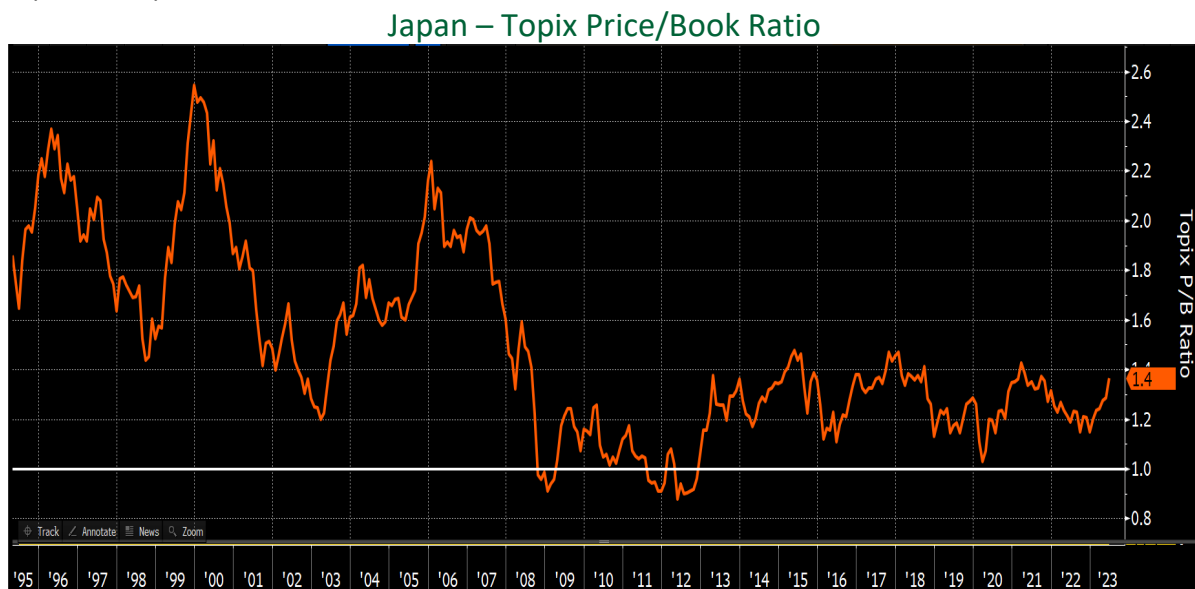


## 7. INVESTING IN JAPAN

The Japanese market is up a strong +16% in Dollar terms over the first half of the year.



The Japanese stock market has a solid tailwind that is expected to structurally benefit investors for a longer spell than over the recent past. Abenomics has been successful in raising inflation (the blue line in the above chart) from depressed levels to 'sweet-spot' levels. Along with its loose monetary policy, this has further stimulated its stagnant economy. The resultant weaker currency also benefits Japanese exports.



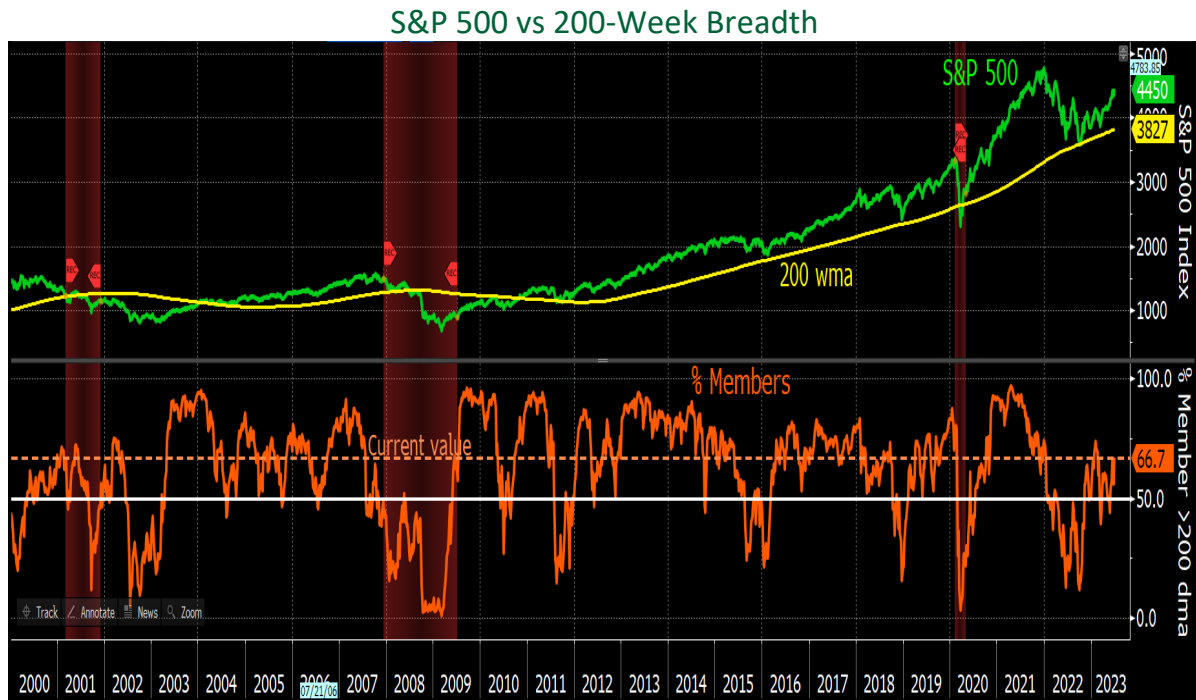
An important – and quite unique – benefit of currently being a shareholder in a Japanese company is the very active program the Tokyo Stock Exchange (TSE) has to improve corporate governance. The TSE announced plans to further firm up on their previous reforms, with hard deadlines for non-conforming companies. They specifically target their low Price/Book valuation metric. These are designed to improve capital allocation and return on equity, which, if successful, can orientate business management towards more effective balance sheets and better cash flow, in the interest of shareholders. We expect more dividends and an extended phase of strong share buybacks, amongst others. Moreover, many Japanese companies are benefitting from the reopening of the Chinese economy, and some investors, including us, prefer taking this indirect approach to investing in China. This in itself supports the Japanese stock market.



## 8. TECHNICAL PICTURE

The S&P 500 technical picture is healthy at June end – it is above its Fibonacci golden ratio, it already had its technical golden cross (in January), the current reading is above both its 50- and 200-day moving averages, both moving averages themselves are trending upwards and it is at a new 52-week record level.

Another important test to form opinion that the market is not overheated is to consider its breadth:



The breadth of exactly two-thirds (the orange reading on the bottom section of the chart), considered against historic levels, does not yet seem overheated (there are numerous readings above the horizontal dotted line). On this technical basis we do not see immediate risk to the current healthy market.

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