

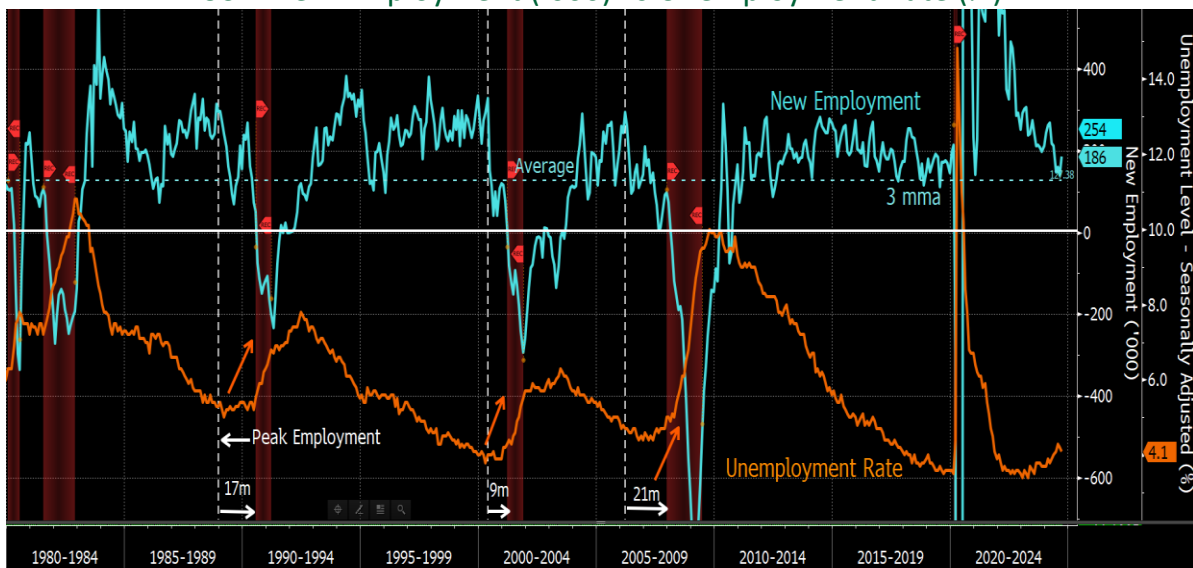
*"Predicting rain doesn't count. Building arks does."*

Warren Buffet

## 1. US EMPLOYMENT

Investors are intensely focused on US employment data to monitor for any potential recession risks.

US – New Employment ('000) vs Unemployment Rate (%)



The September New Employment data was surprisingly strong, and well above the long-term average (the blue lines). Along with that, the Unemployment Rate dropped for a second month in a row by 0.1%. The manufacturing sector employment growth of +0.9% also remained relatively strong (not reflected in the chart). This argues against many views of a structurally softening employment market in the US.

US – Employee Perceptions of Employment Market vs S&P 500

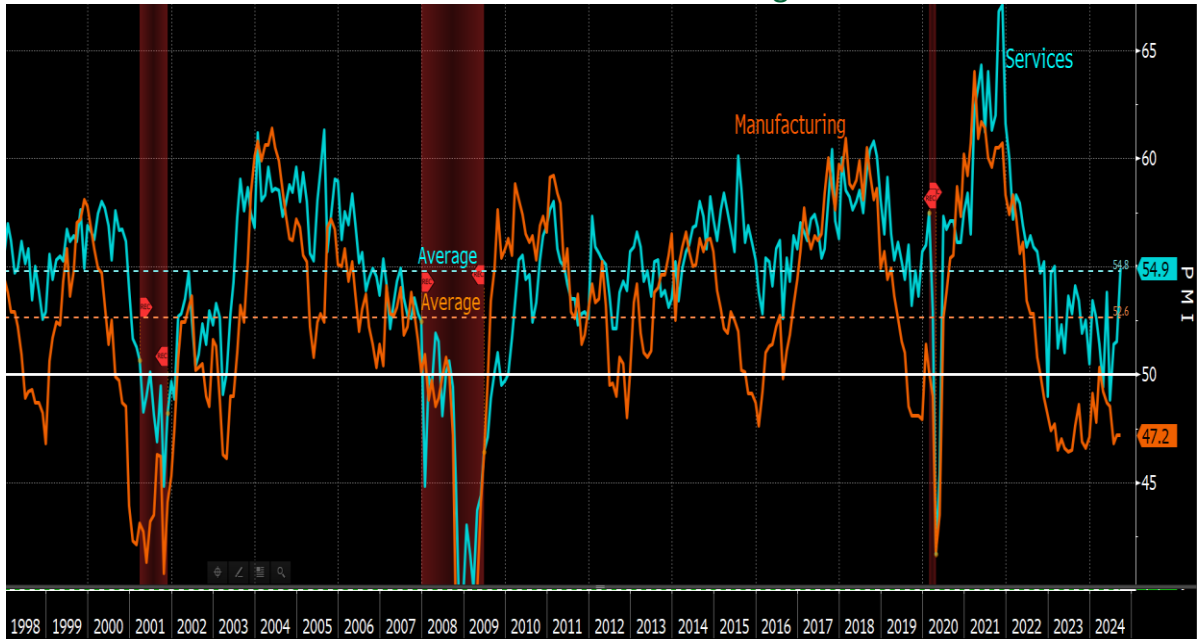


Worker perceptions of the employment market continue to weaken. The percentage of them who believe jobs are readily available continues to drop (the blue line), while percentage of workers with the view that jobs are hard to find keeps rising (the purple line). The spread between the two series (the orange line) keeps dropping. That has historically been a negative economic indicator. On balance, whilst still holding its own, US employment is expected to remain under scrutiny.

## 2. US ECONOMIC ACTIVITY & EARNINGS

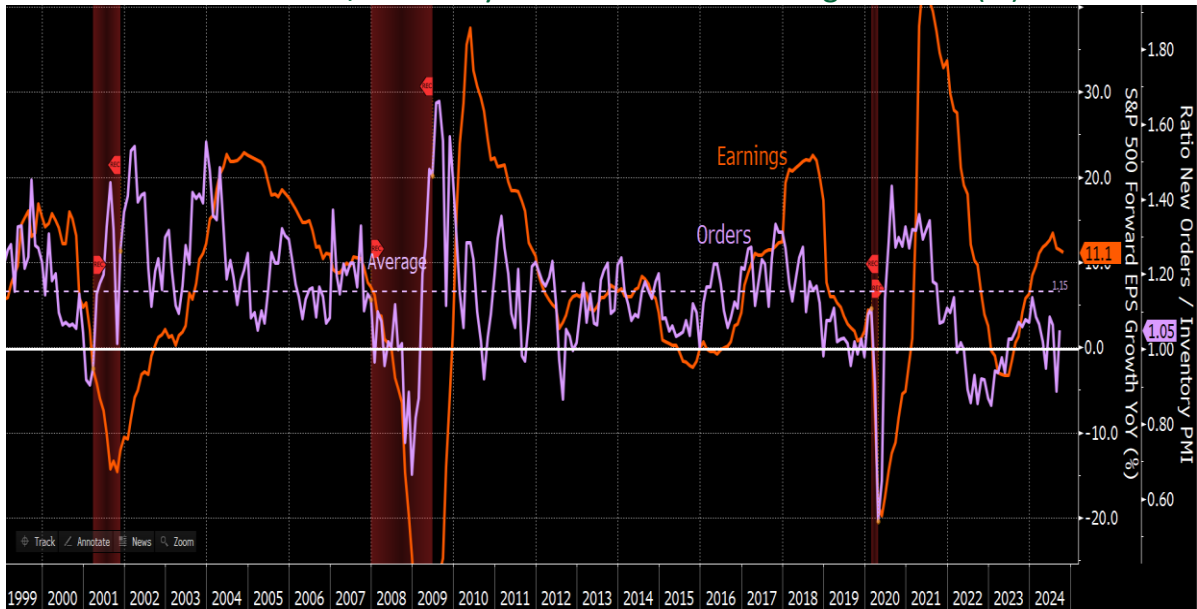
Along with the employment data, we consider current US economic activity.

### US – Services vs Manufacturing PMI



Services PMI data has recently bounced back strongly, and is back to its long-term average. Seeing as it is the biggest contributor to economic activity, this bodes well for the immediate economic outlook. In contrast, recent Manufacturing PMI data has fallen back again, and is close to the current cycle's lows. It seems Manufacturing is the risk factor in this context.

### US – Orders/Inventory PMI vs S&P 500 Earnings Growth (%)



Both Orders and Inventory PMI data are currently contracting (below the 50 neutral PMI level). Their relative ratio (the purple chart) is, though, on balance, currently in favour of Orders. Inventory PMI data has been contracting for all of the past six months, with Orders more stable. With Services PMI data remaining strong and the Dollar somewhat weaker, chances are that Orders can remain stable.

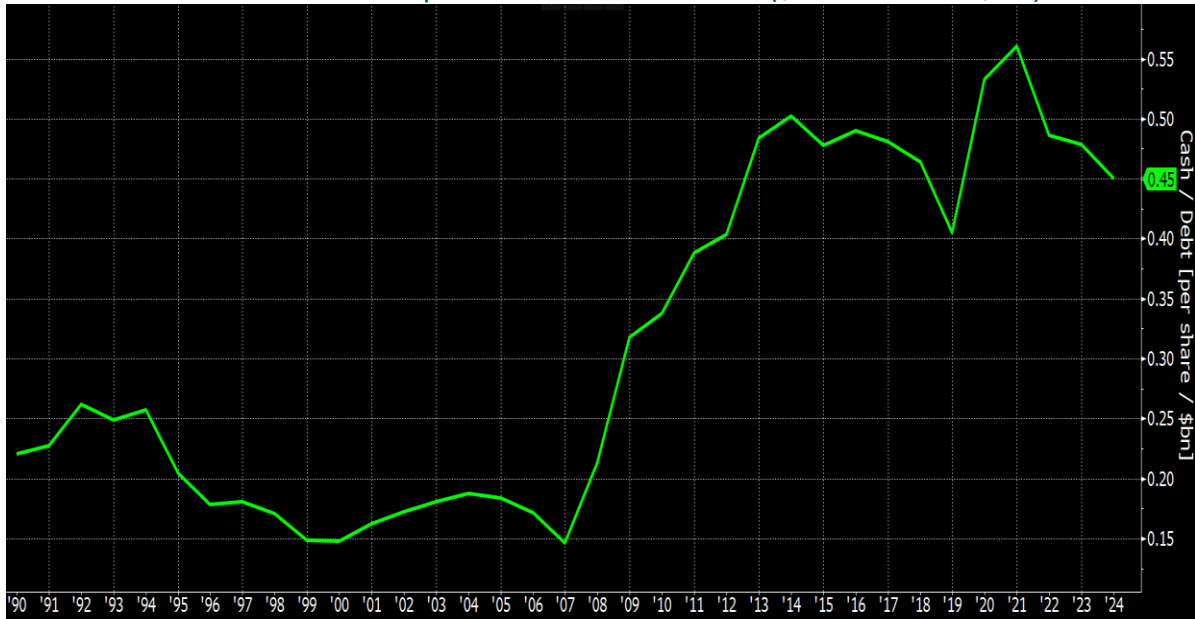
A gap has opened between the Orders/Inventory PMI ratio and expected S&P 500 earnings growth (the latter, at +11%, remains elevated (the orange chart)). It is all finely tuned and, all said, along with the Goldman Sachs Economic Activity Index and Industrial Production remaining stable, we would need some recovery of the Orders/Inventory PMI ratio to keep supporting earnings.



### 3. US CASH

With US interest rates on a structural downward trajectory, it is worth considering general cash levels:

S&P 500 – Total Liquid Funds vs Total Debt (\$ Per Share & \$bn)



Whilst the above chart's ratio is not on a pure like-for-like basis, the trend provides valuable information. On this basis, cash levels are relatively high compared to debt levels. It is currently more than double the ratio of pre-Credit Crisis levels. Along with this, the Net Debt / EBITDA ratio is not far from Pandemic era record low levels, while the Total Debt / EBITDA ratio of 3.7 times is close to record low levels (not reflected in the chart). It seems US corporates are generally in a strong financial position.

US – Bank Deposits & Money Market Funds (\$) and as Ratio of US Market Capitalisation (%)



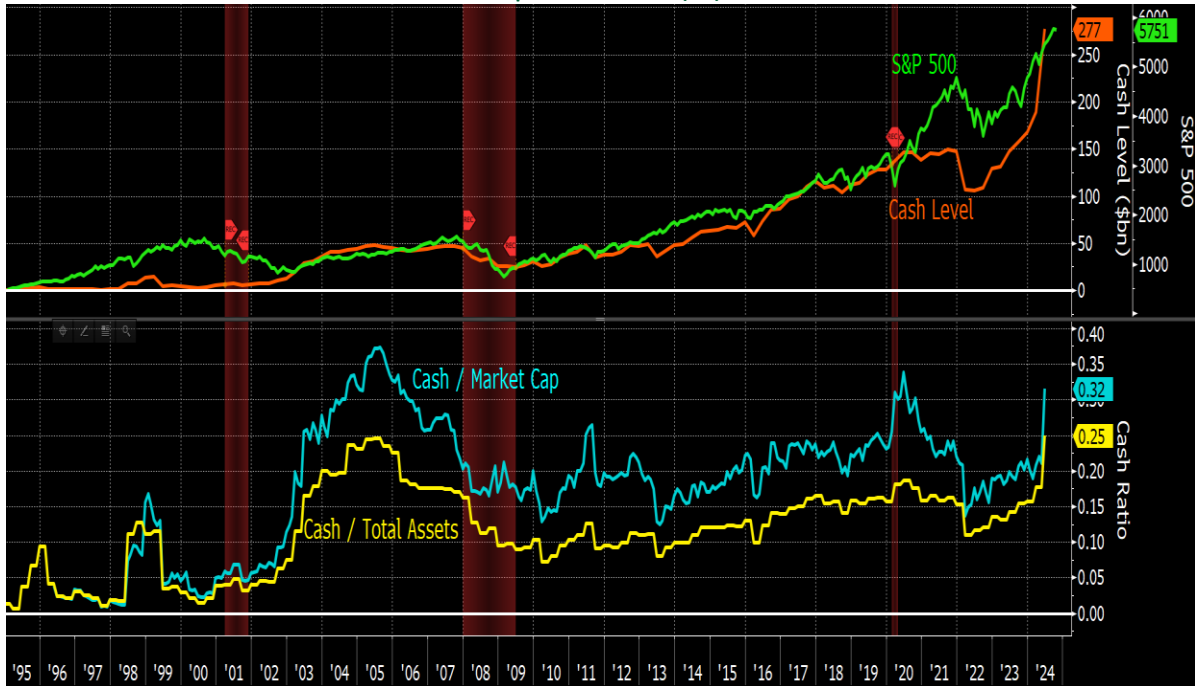
There is currently a record \$22 trillion in US Bank Deposits and Money Market funds (the green chart). This is a fifth above its trend line, but at a record low 38% ratio (the orange chart) of total actively traded market capitalization. Whilst we can expect cash levels to remain relatively high with an uncertain economic outlook, lower interest rates can divert some of that into the stock market over time. Whilst we do not expect that to have a particular impact on share prices, ample resources are available to be utilized should shares become cheaper. This can provide some floor to the stock market.



#### 4. BERKSHIRE HATHAWAY CASH

An update on Berkshire Hathaway's cash levels is appropriate.

Berkshire Hathaway Total Cash Level (\$bn) vs S&P 500, its Total Assets and Market Capitalisation (%)



After selling material volumes of shares in the second quarter, their cash level is at a record \$227 bn level (the orange chart). It is a quarter the level of its Total Assets, and 32% of its Market Capitalisation. In terms of the former (the ratio management would consider), it is at a record level, close to pre-Credit Crisis levels.

Management optimised the 2022 period of Federal Reserve tightening to invest more at lower share prices. On the above ratio bases, the cash level is now more than double at that time. It seems management has taken a cautious stance on the stock market.

Berkshire Hathaway – Share Price (\$, absolute and relative)

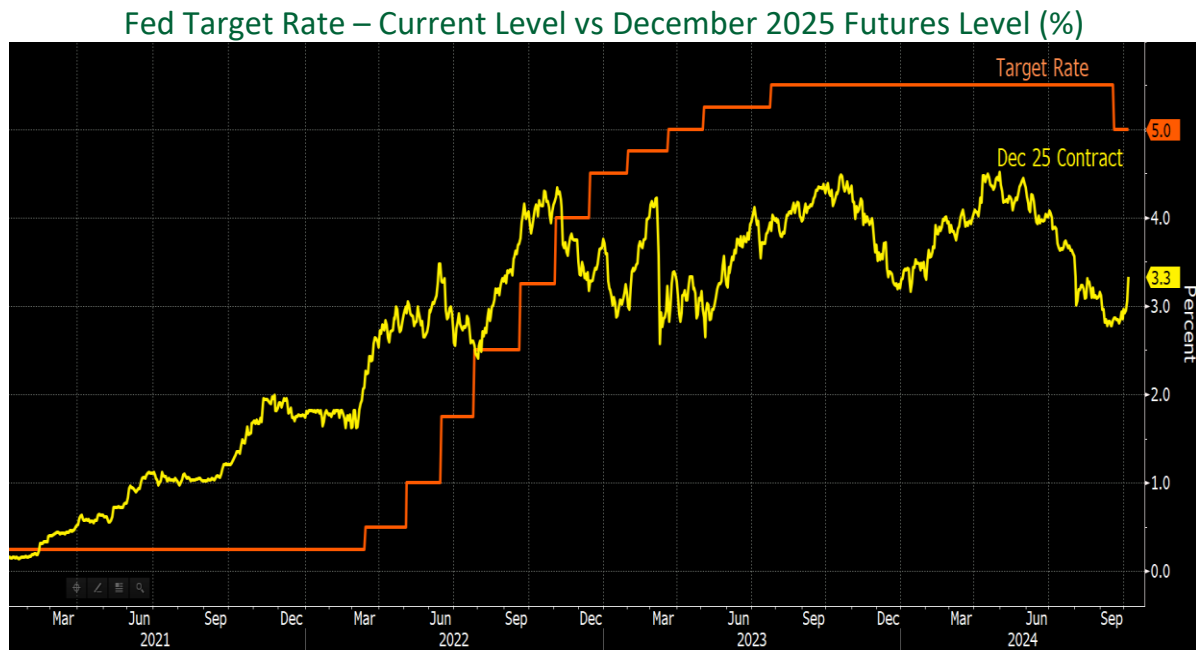


The share price is close to a record level on an absolute basis (the orange chart) and close to its Credit Crisis relative record level (the white chart) when it was in an excellent position to capitalise on the financial market disarray. It seems the share has below market risk currently.



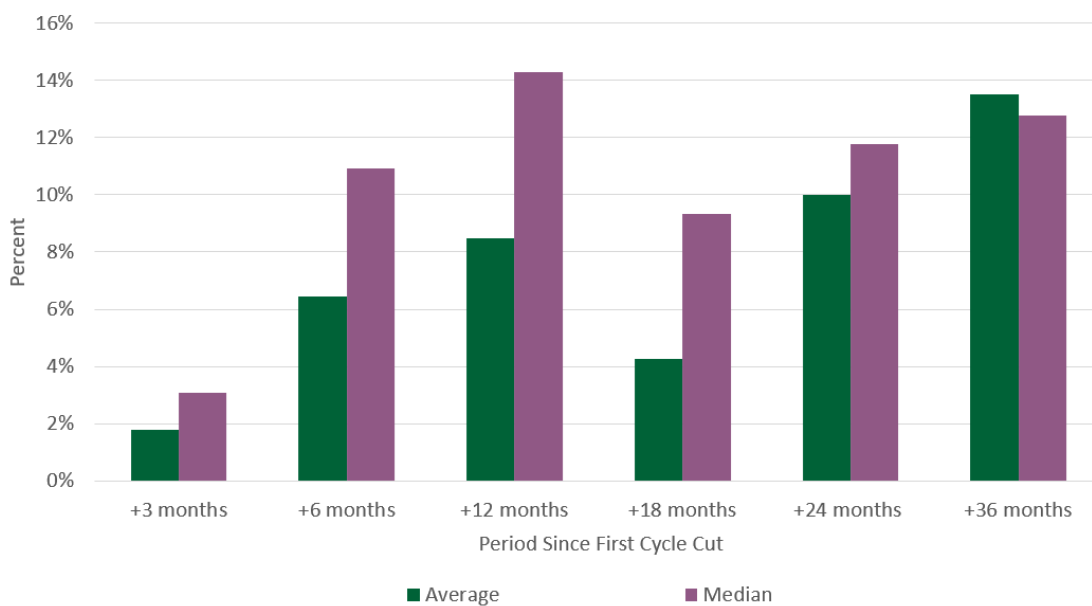
## 5. FED RATE CUTS

After holding its target rate for over a year, the Fed has started a new easing cycle.



Market expectations are currently for total cuts of a further 1.75% by the end of next year. This would mean the target rate would be 3.25% (most probably also in terms of real levels), which would leave the Fed with ample reserves for further loosening. Investors will consider the effect of such a pathway on share prices.

**S&P 500 – Total Return Following the First Fed Cycle Rate Cut (%)**  
Annualised for periods > 1 year. Data since 1980



Past performance should not be used as a guide to future performance.  
Source: Bloomberg, Stonehage Fleming Investment Management. September 2024.

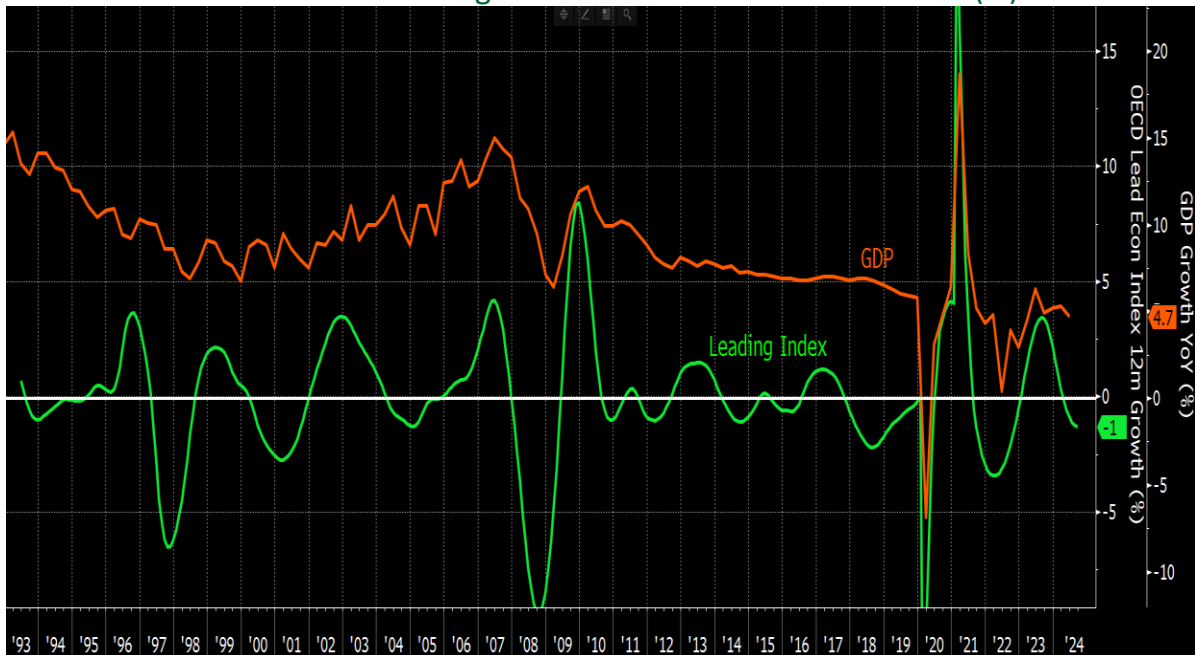
Historically, shares have generally provided attractive returns following the first cycle rate cuts. The data includes the negative experiences with the Technology bubble and the Credit Crisis. Those were exceptional circumstances and investors can, on the basis of this chart alone, look forward to positive experiences from further Fed rate cuts.



## 6. CHINA

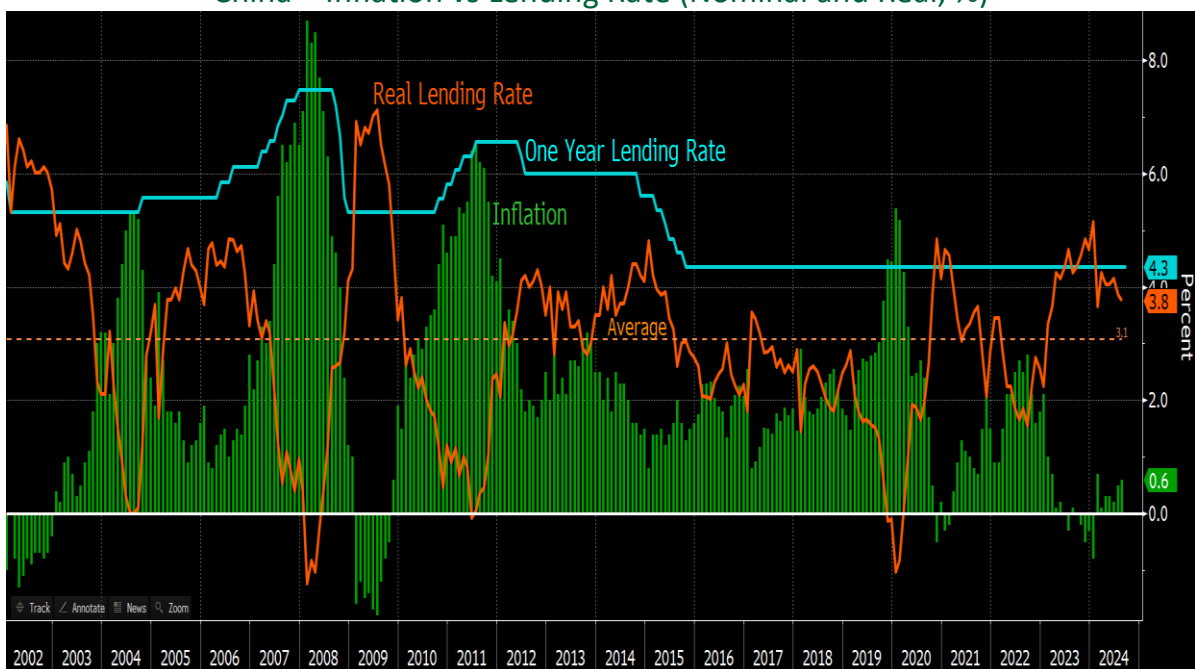
The Chinese government has announced a strong financial package, in essence to support their property market and share prices. They have indicated that further steps may follow to support the economy.

China – OECD Leading Economic Index and GDP Growth (%)



The package has been successful thus far to turn around investor sentiment from extreme negative levels on both the mainland and Hong Kong stock exchanges. It has brought many share valuations back up to more recent average levels. Considering the negative economic outlook in the above chart, investor uncertainty remains, though, that the stimulus is only monetary in nature (with hopes that it later flows into the real economy) and that fiscal support is also necessary to ensure the improvement of their economy.

China – Inflation vs Lending Rate (Nominal and Real, %)

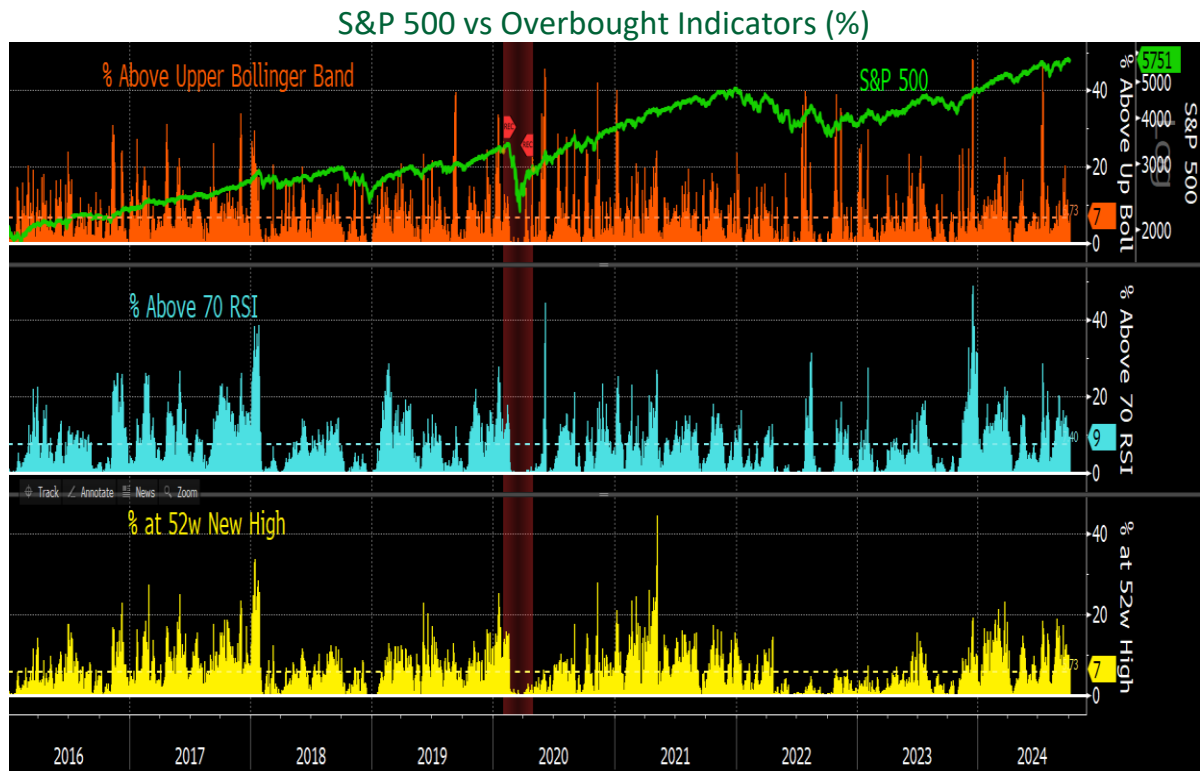


The economy has more deflationary than inflationary risk, currently leaving the real one-year lending rate close to 4%. This is clearly dampening economic growth. To attract more permanent foreign investors (rather than short term traders), they would need a clear indication that rates will be cut further, and that fiscal support is also on its way.



## 7. TECHNICAL PICTURE

With the strong stock market, we consider the Overbought technical picture:



The indicators under consideration are the percentage of S&P 500 constituents above their upper Bollinger band (7%), above their 70 RSI overbought level (9%) and at 52-week new highs (7%). All these percentages are close to their respective individual averages, leaving an impression of a still relatively healthy technical picture.

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