

“Quality is never an accident – it is always the result of intelligent effort.”

John Ruskin

1. US CONSUMPTION

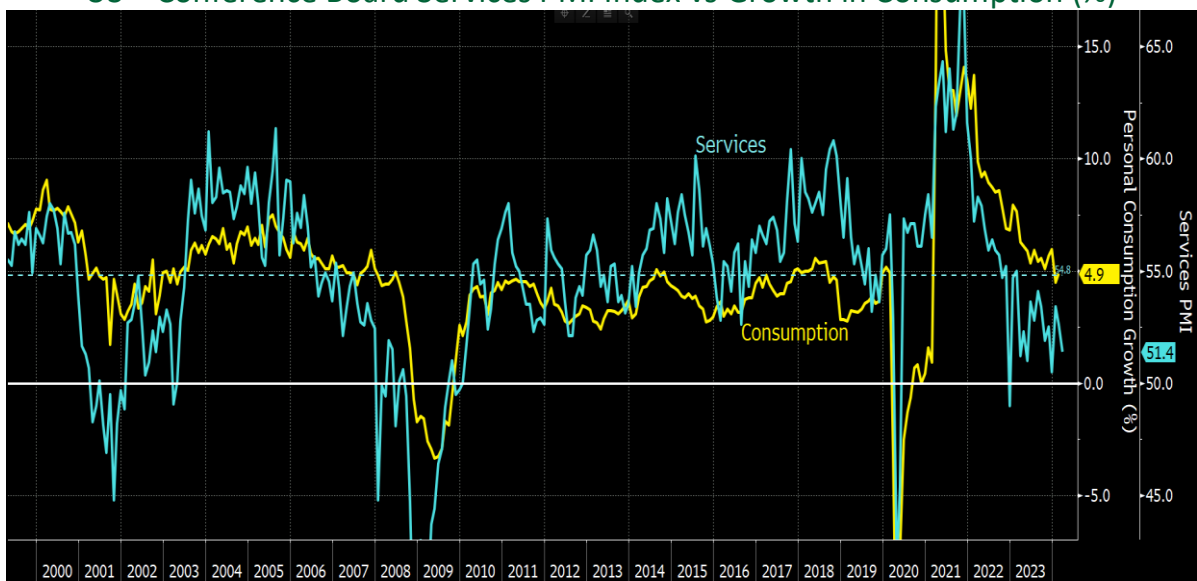
With consumption such a dominant contributor to the US economy, we follow it closely to assess the economic outlook.

US – Conference Board and University of Michigan Consumer Confidence Indices



The Conference Board Consumer Confidence Index remains well above average. The University of Michigan Consumer Confidence Index is rising well off its low base, not far from its average. It therefore seems that investors can continue relying on the US consumer.

US – Conference Board Services PMI Index vs Growth in Consumption (%)

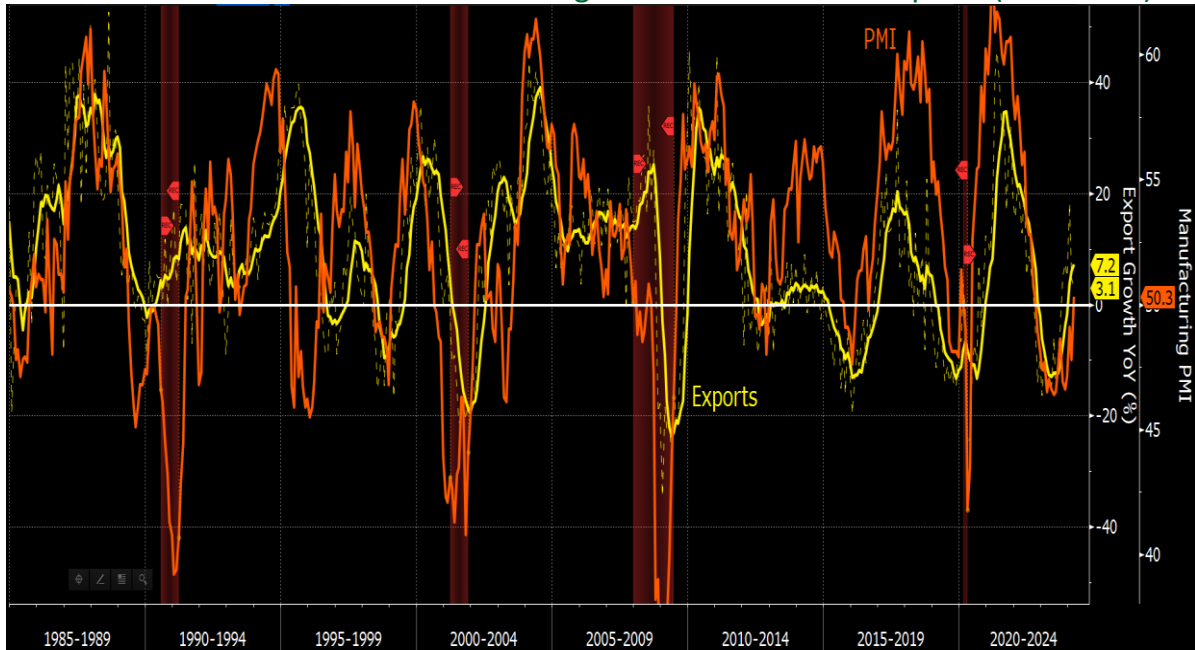


Whilst the Services PMI Index is dropping, it currently remains in constructive territory. Growth in Consumption correlates closely with the Services PMI Index and is dropping off its elevated Pandemic level, but at +4.9% remains at pre-Pandemic peak levels. We conclude that Consumption remains supportive of the US economy.

2. US MANUFACTURING

Whilst Industrial Production is a relatively small portion (less than a third) of the US economy, it remains an important swing factor.

US – Conference Board Manufacturing PMI vs South Korea Exports (% Growth)



The Manufacturing PMI Index (the orange line in the above chart) has recovered well and is currently in constructive territory (>50 reading), indicating positive growth. This index has historically correlated well with South Korean exports (because of the nature of their exports, the yellow line), which is currently also experiencing a positive growth trend, supporting the US Manufacturing Index.

Logically this constructive manufacturing picture supports the outlook for US Industrial Production. It has flatlined since the beginning of 2023, with odds growing for it to turn a positive corner.

US – Citi Economic Surprise Index vs S&P 500



As can be expected from our observations above, the US Economic Surprise Index in the above chart has turned upwards early this year. It is currently well above its average. We conclude that chances remain higher for a soft rather than a hard landing of the US economy. This view is also reflected in US interest rates, which are currently drifting higher.



3. HIGH YIELD MARKET

The High Yield Market is a good barometer of overall capital market stability and confidence.

US High Yield, US Junk Bonds and Emerging Market Bond Price Indices



Prices of US High Yield, US Junk bonds and Emerging Market bonds have been increasing materially since the last quarter of 2023. They are back at levels preceding the Federal Reserve tightening program. This is a welcome confirmation of increasing risk appetite in the capital markets.

US – High Yield Spread (with 10-year Treasuries) vs S&P 500



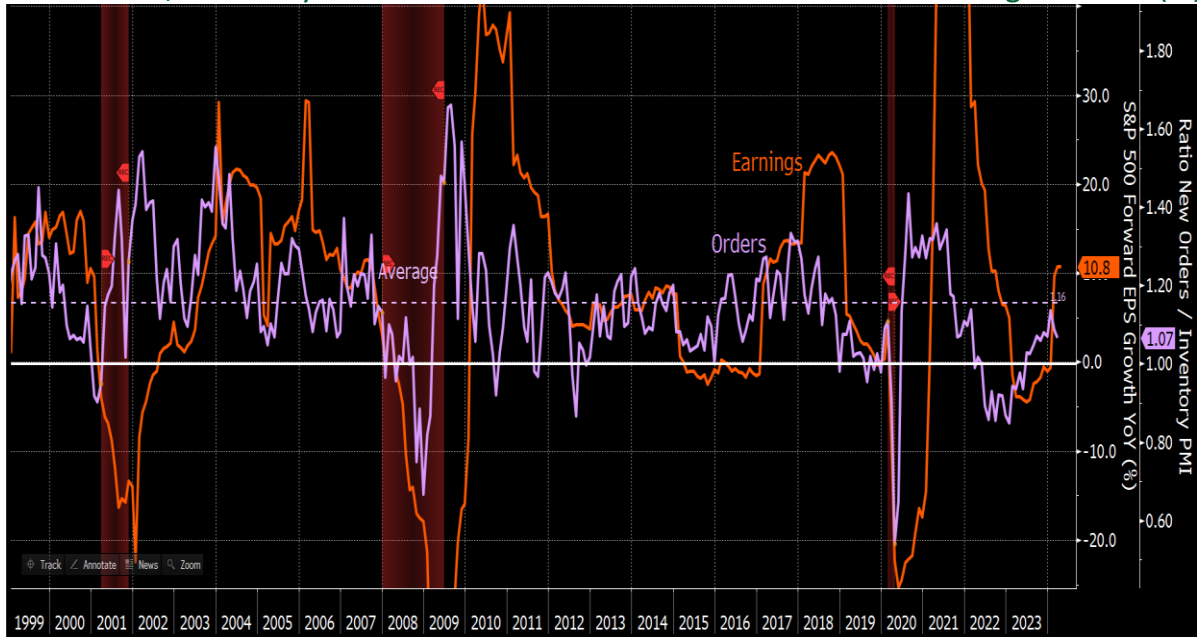
The High Yield Spread is another good barometer of risk appetite. It has dropped (improved) since the middle of 2022 and is currently on its average of just over 4%. This is an indication that capital markets have largely normalised since the Pandemic and the Fed tightening disruptions. This supports our view that fundamental issues can be considered on their merits without the disruptions of an unstable capital market.



4. EARNINGS

Seeing that we are currently in a normalised capital market, the role that earnings play in share performance becomes even more important.

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



Considering the Orders / Inventory PMI Ratio in the above chart (the purple line) it seems that many US based businesses have been overly conservative and that inventories have been depleted. With a better-than-expected economy and orders increasing, these new orders can support earnings growth. Logically, this ratio has a close correlation with expected earnings growth, as depicted in the chart (the orange line). It is striking that S&P 500 earnings expectations are currently increasing quite sharply. South Korea export data reflects a similar picture.

MSCI World Index vs Index of Number of Constituents with Earnings Upgrades



The green line in the above chart reflects the number of MSCI World Index constituents experiencing earnings upgrades. It correlates closely with the price index (the orange line). The Upgrade Index is currently close to its average, and we can expect global economic fundamentals to soon have an effect. Considering our earlier comments in this note, we believe the likelihood that this effect will be positive is growing.

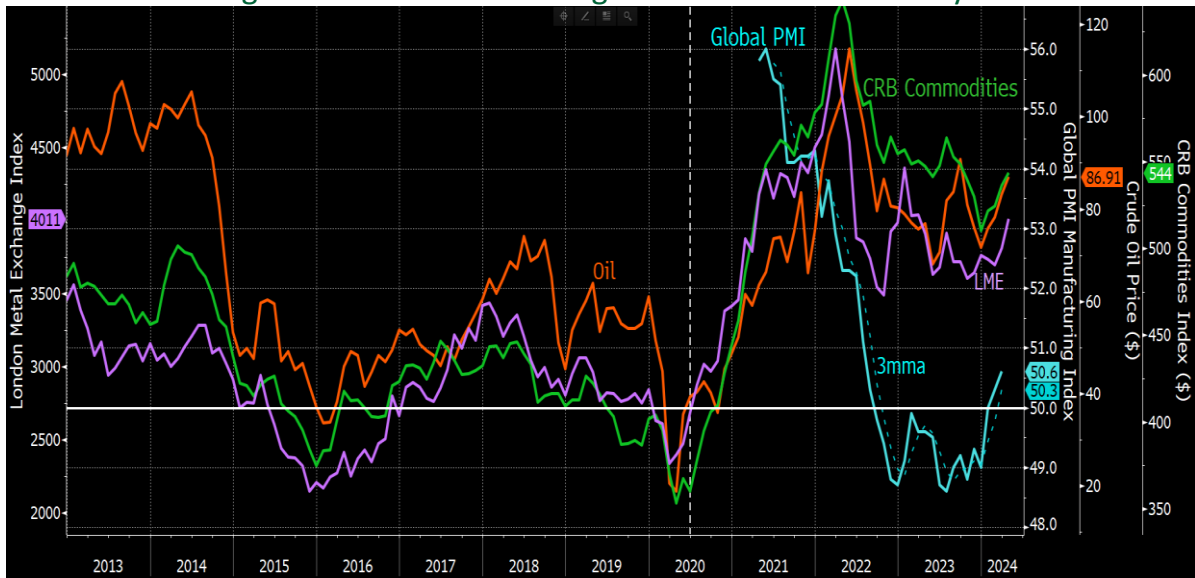
It is striking that earnings perceptions are constructive while many investors fear an imminent US recession. We remain in the soft-landing camp on this front.



5. COMMODITIES

Whilst it is not our investment domain, it is important to note that the commodity market is turning for the better:

JP Morgan Global Manufacturing PMI Index vs Commodity Prices



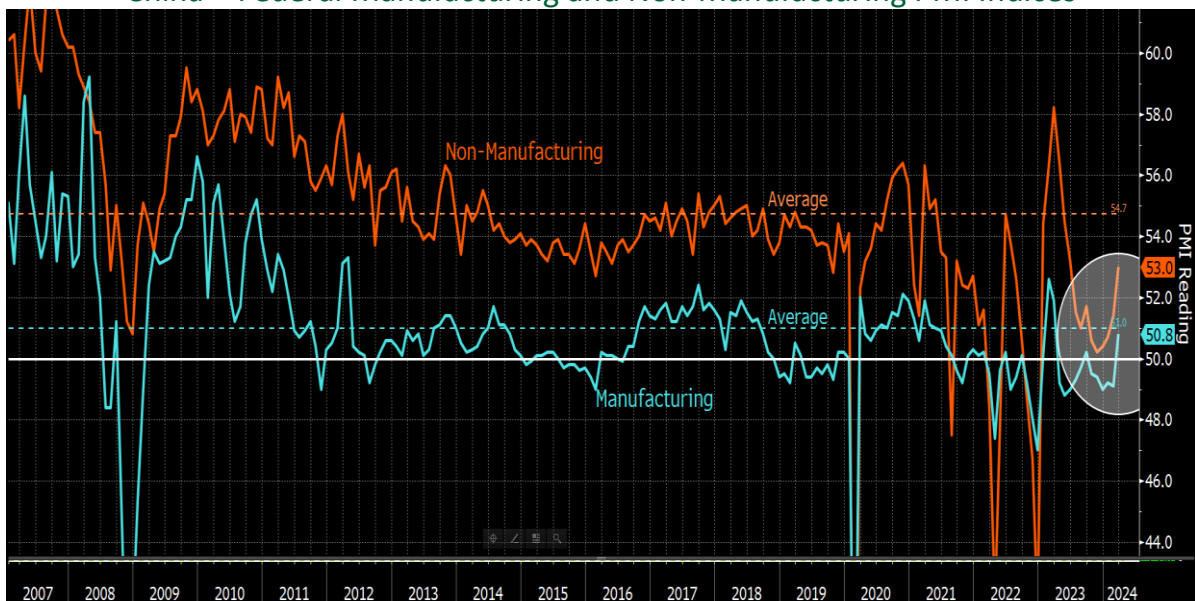
The Global PMI Index has earlier this year moved into constructive territory (a reading above 50, the blue line). Major Commodity Indices (CRB Commodities, London Metal Exchange Index) along with Oil (all in the chart) are all rising currently. Importantly for us, we can expect such a cyclical recovery to tactically attract funds away from the types of businesses with stable growth.

Whilst this reflects an improving global economy, we are uncertain about the longevity of such a cyclical upswing and remain focused on other opportunities we may be offered.

6. CHINA

The preceding constructive comments are also starting to reflect in China:

China – Federal Manufacturing and Non-Manufacturing PMI Indices



Both their Manufacturing and Non-Manufacturing PMI Indices have recently turned upwards and are currently in constructive territory.



China – Number of Domestic and International Travelers (m)

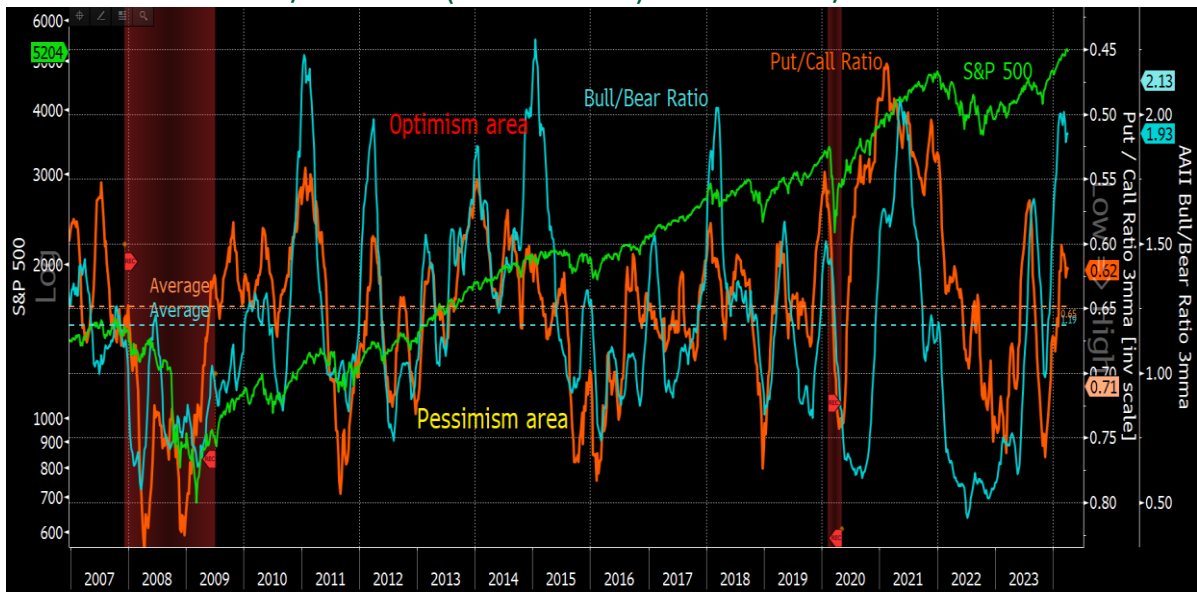


The number of domestic travelers is at a seasonal record level (orange line). Strikingly, the number of international travels is recovering sharply after three years of absence, and is up over 40% since November (green line). We expect this to be positive for luxury and cosmetics businesses.

7. TECHNICAL PICTURE

The technical picture reflects the improving capital market landscape:

US – S&P 500 Put/Call Ratio (inverse scale) and AAI Bull/Bear Ratio vs S&P 500



The individuals retail market is currently super optimistic (the Bull/Bear ratio in the blue line). More importantly, the institutional market (the Put/Call Ratio in the orange line) is also positive, but somewhat more reserved. They have a good correlation with the S&P 500. We perceive the technical picture to be positive, and not yet in the so-called danger zone.

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

Unless otherwise stated, the charts and data used in this document are sourced from Bloomberg, January 2024.

This communication has been prepared for information only and is not intended for onward distribution. It is neither an offer to sell, nor a solicitation to buy, any investments or services. This communication does not constitute a personal recommendation and does not take into account the individual financial circumstances, needs or objectives of the recipients.

Opinions expressed here are as of the date of publication and subject to change without notice. Stonehage Fleming Investment Management shall not be responsible for any trading decisions, damages, or other losses resulting from, or related to, the information, data, analyses or opinions contained herein or their use, which do not constitute investment advice, are provided as of the date written, are provided solely for informational purposes and therefore are not an offer to buy or sell a security.

Any information which could be construed as investment research has not been prepared in accordance with legal requirements designed to promote the independence of investment research. Further it is not subject to any prohibition on dealing ahead of the dissemination of investment research

All investments risk the loss of capital.

The value of investments may go down as well as up and, you may not receive back the full value of your initial investment.

Past performance should not be used as a guide to future performance.

Changes in the rates of exchange between currencies may cause the value of investments to go up or down in the reporting currency.

Issued by Stonehage Fleming Investment Management Limited. Authorised and regulated in the UK by the Financial Conduct Authority (FRN No.: 194382) and registered with the Financial Sector Conduct Authority (South Africa) as a Financial Services Provider ("FSP") under the Financial Advisory and Intermediary Services Act, No 37 of 2002 (FSP No: 46194).

