STONEHAGE FLEMING

GLOBAL EQUITY PERSPECTIVES 9 SEPTEMBER 2024

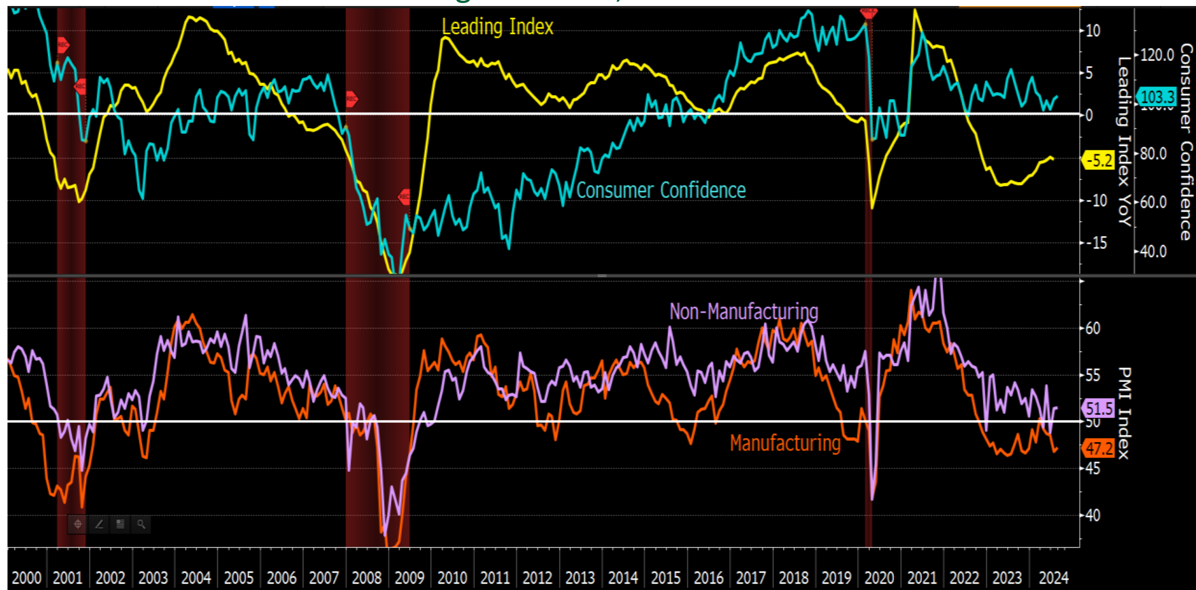
"Knowing what you don't know is more useful than being brilliant."

Charlie Munger

1. US INDICATORS

We combine several important US economic indicators in the following charts:

US – Conference Board Leading Economic, Consumer Confidence and PMI Indices



The Consumer Confidence Index (the blue line, one of the most important indicators) remains stable and above its average, while the Leading Economic Index (the yellow line) remains in negative territory, recovering from a low base. The Manufacturing PMI Index remains in negative territory (the orange line), whilst the Services PMI Index (the purple line) is marginally in positive territory.

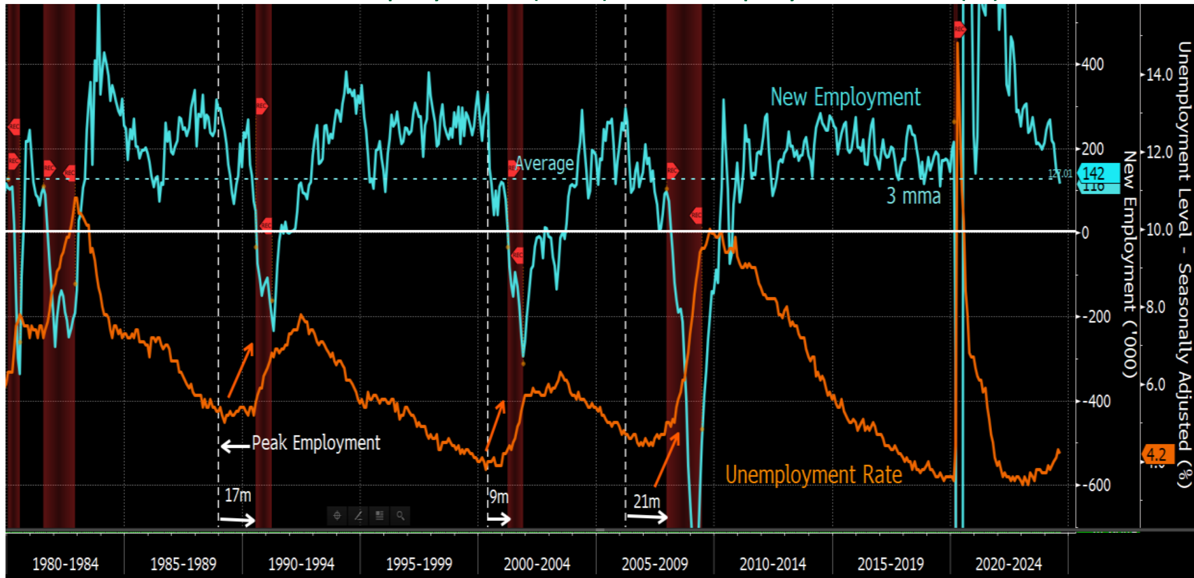
US – Johnson Redbook Same Store $ Sales Growth (%) vs S&P 500

Overall consumption is currently growing at +5%, with the above Same Store Sales Index (the orange line) growing at almost the same level, indicating a still relatively healthy retail market. The US economy currently remains in constructive territory, but clearly is very dependent on their consumer market staying its course.

2. US EMPLOYMENT

The market currently is focused intensely on employment data to assess the risk of an imminent recession.

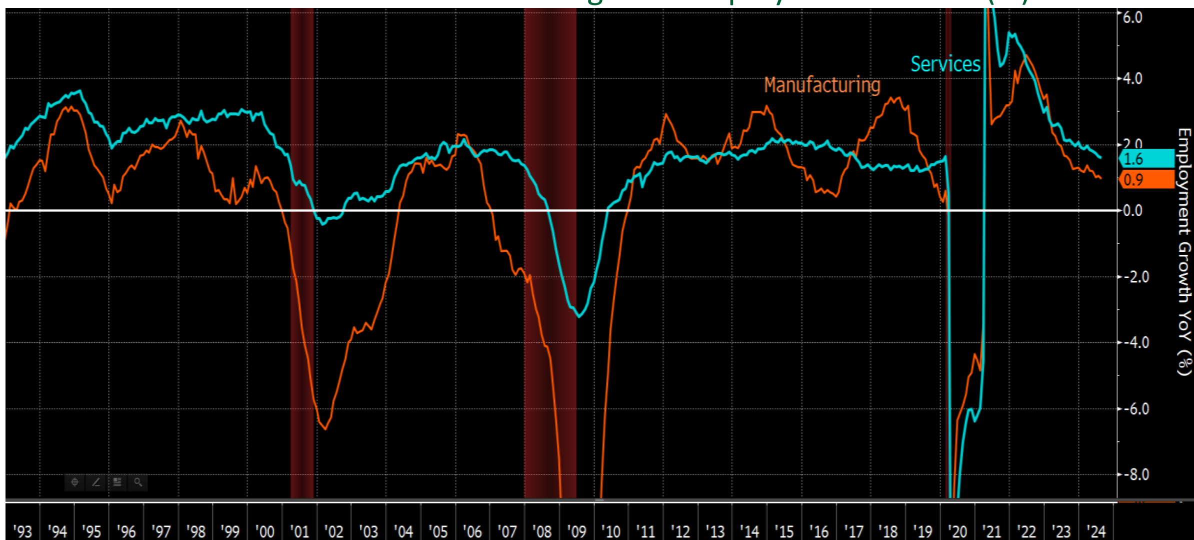
US – New Employment ('000) vs Unemployment Rate (%)



Current new employment numbers are dropping, but they are still close to the long-term average. The Unemployment Rate's trend is upwards. This combination has brought the Federal Reserve (Fed) to the conclusion that they can start cutting their target rate.

The Jobless Claims chart mirrors the above Unemployment Rate chart, with an upwards trend, but still at a relatively low level. Along with this, the New Employment / Total Labour Force Ratio is dropping from record levels, but at 5.2% is still well above historic levels of 4.6% and 3.2% at its peaks before the previous two recessions. The New Job Openings / Unemployed Ratio of 1.1 is slightly above historic levels preceding recessions. It is also a topical point that high immigration is distorting some of the employment data.

US – Services & Manufacturing New Employment Growth (%)



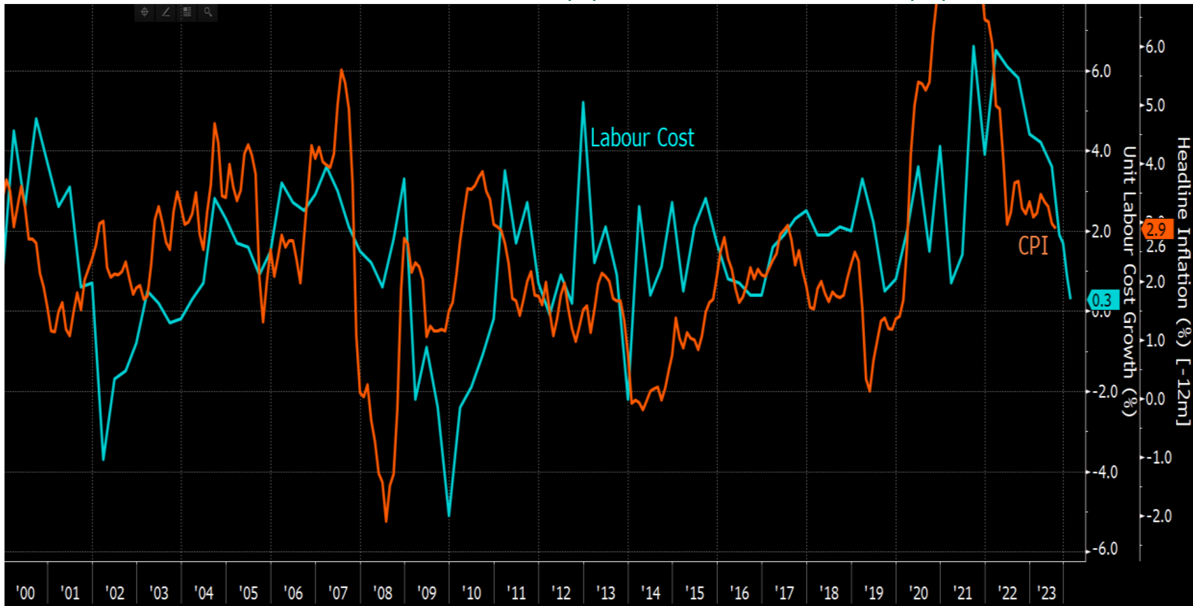
New Employment growth of +1.6% in the Services sector is at a healthy level compared to its historic norm. The more economically sensitive New Employment growth of +0.9% in Manufacturing is at a healthier level than the negative levels before previous recessions.

In conclusion, we take cognisance of a weakening US employment backdrop off its exceptionally strong recent past, but believe it remains relatively healthy. This is supported by the consumer's strong balance sheet.

3. US INFLATION & YIELD CURVE

Whilst there are still some reservations in some quarters whether US inflation is under control, we believe it is, as depicted by the following chart:

US – Unit Labour Cost ($) vs Headline Inflation (%)



Unit Labour Cost (the blue line) leads Inflation (the orange line) by around twelve months (the latter chart is pushed back for that period). Seeing the current low level of Labour cost growth (+0.3%), and the fact that Inflation excluding the Cost of Rent is already at 1.8%, we believe the Fed can relax on this front and start cutting their target rate as soon as at this month's meeting. Such a move is expected to support the bond market. Some of these perceptions are reflecting in parts of the bond market, with general comments that the Yield Curve has reverted into positive territory, raising the risk of an imminent recession.

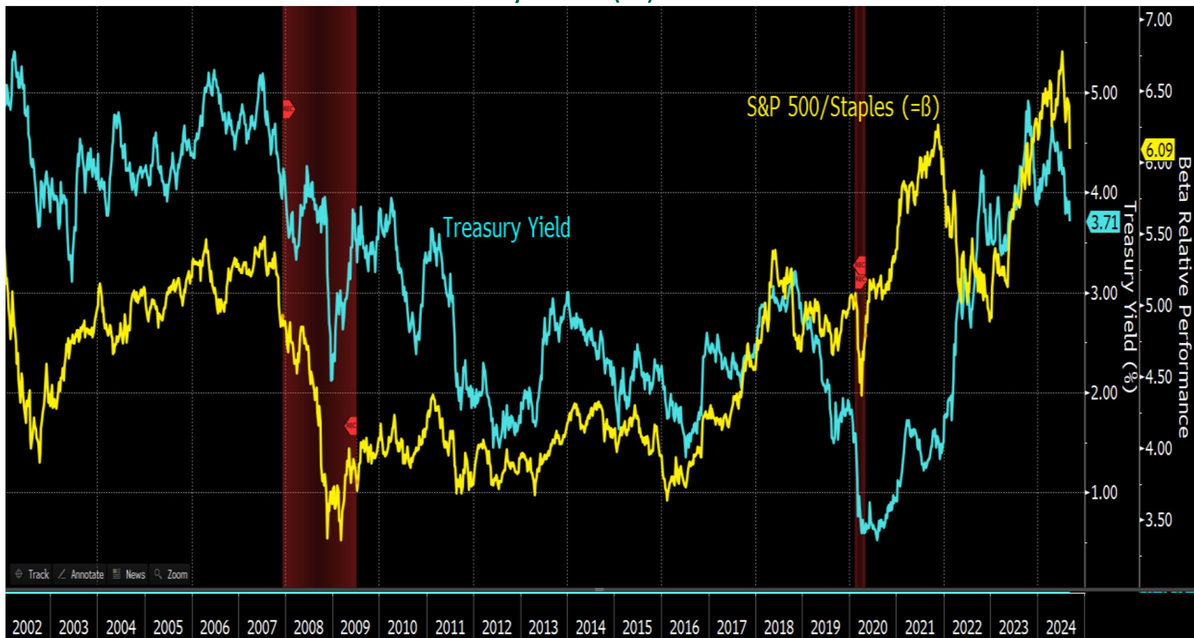
US – Yield Curve (%) and S&P 500

It is only the 10yr/2yr Yield Curve (the blue line) that has reverted (and just marginally so at +.06%). The alternative 10yr/3m Curve (the red line) is inverting further (currently at -1.4%). Historically, both reverted before previous recessions. Along with this, the High Yield Spread reflects a more favourable economic outlook. Whilst we are prepared for a softer US economy, and with a Fed rate cut imminent, we would be cautious to conclude this early that the Yield Curve is signaling an imminent US recession.

4. MARKET ROTATION

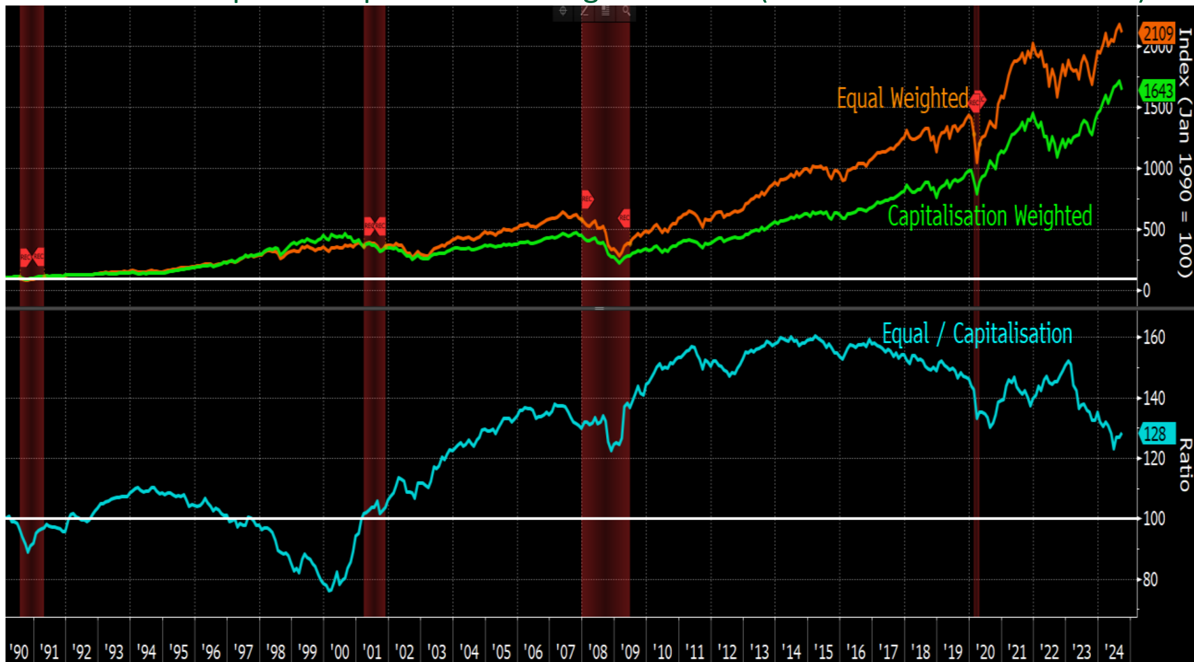
With a structural change in the bond market on its way, equity investors have new considerations in terms of potential sector rotations.

US – Treasury Yield (%) vs 'Beta' Index



We use the S&P 500 Index / Staples Index Ratio as a proxy for Beta stocks. There is a clear correlation between this Beta Index (the yellow chart) and Interest Rates (the blue chart). Logically, we have a similar correlation between Transport and Utilities. With a view of lower interest rates, lower Beta stocks may continue to find interest, while longer duration stocks (e.g. Technology) will have to deliver well on the earnings front to outperform.

S&P 500 – Equal vs Capitalisation Weighted Index (Indexed to Jan 1990 = 100)

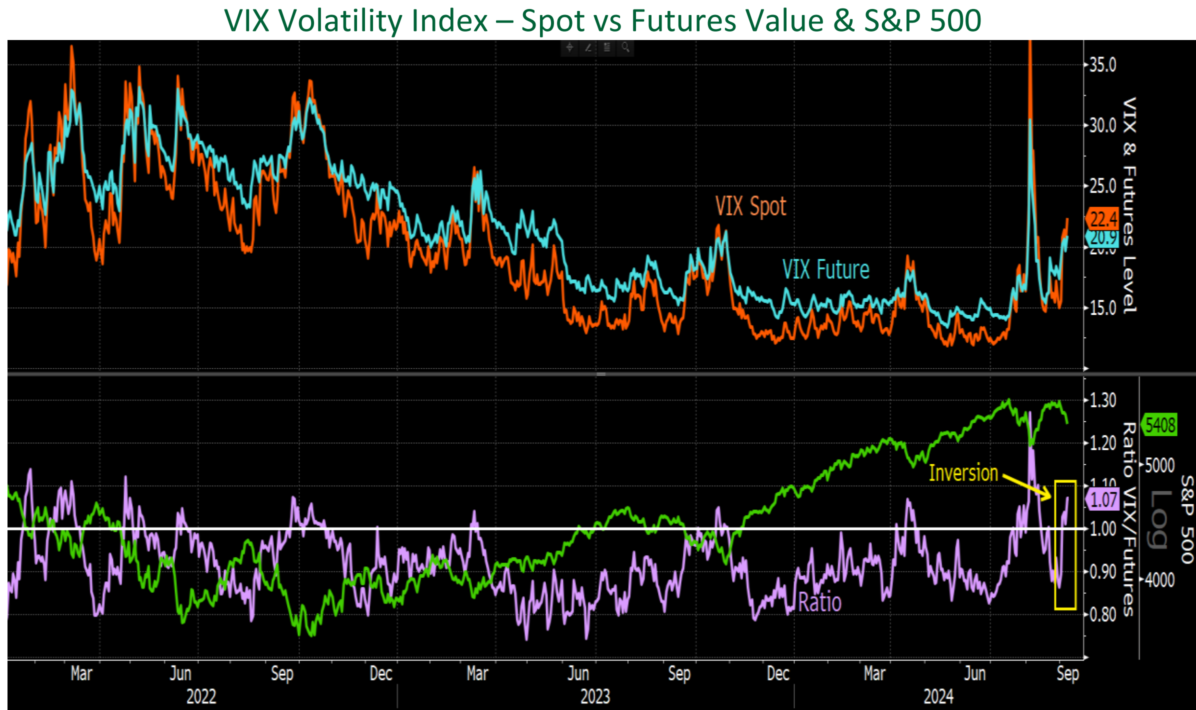


While the equal weighted S&P 500 Index (the orange line) outperformed the capitalization weighted S&P 500 Index (the green line) over the long-term, it has structurally underperformed over the past ten years (the blue line) with Technology doing particularly well. This trend reversed over the past two months. Investors in the large capitalisation stocks will have to ensure their companies' earnings outlook and valuations will provide support for this trend to continue.

5. MARKET VOLATILITY

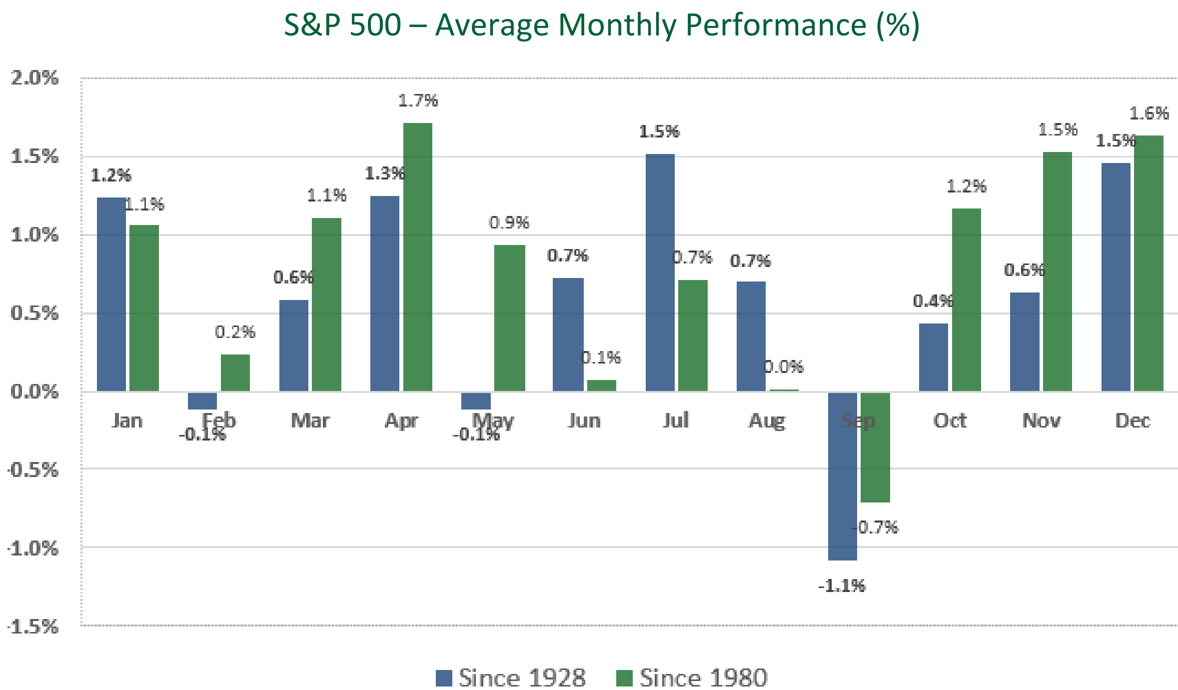
Markets have been particularly volatile since early in August.

VIX Volatility Index – Spot vs Futures Value & S&P 500



Logically, the VIX Spot Index (the orange line) is usually lower than the VIX Futures Index (the blue line). The purple line reflects the ratio of the Spot/Futures Index. It inverts usually with high volatility, as is currently the case. Such inversions have historically happened towards the end of the volatile periods and have previously indicated buying opportunities.

S&P 500 – Average Monthly Performance (%)



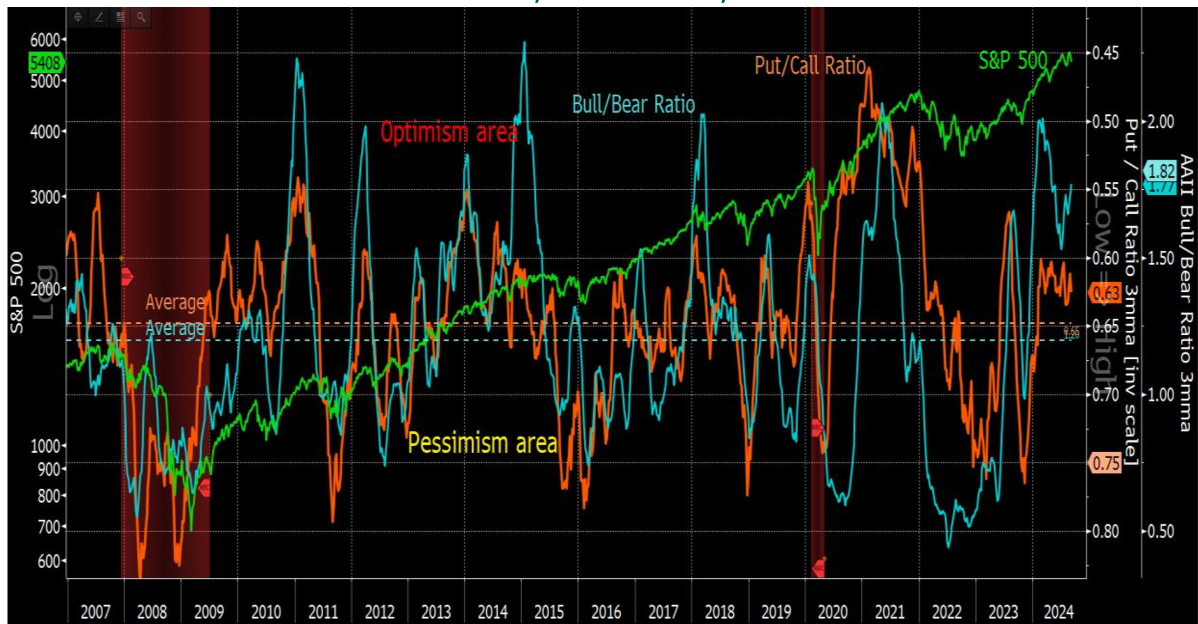
We have considered the average index performance for each month over the ultra-long and the longer-term in the above chart. It has quite similar outcomes for both periods, with September being by far the most negative month. Tying this in with the preceding comment above, astute investors may find good buying opportunities in the coming weeks.

6. TECHNICAL PICTURE

S&P 500 Technical Picture

Whilst the S&P 500 has recently tactically dropped through its 50-day moving average, it otherwise technically appears healthy. Its breadth and overbought/oversold indicators (not in the chart) also do not reflect any alarms, while it remains in a structural bull market. The latter is also true in the context of its relationship with Gold.

S&P 500 vs Put/Call and Bull/Bear Ratio



Both the Put/Call (the orange line) and Bull/Bear (the blue line) Ratios reflect optimism on both the Institutional and, especially, the Retail markets. This leaves little room for disappointing results, as we have seen during the recent reporting season.

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