CREDO

Macroeconomic Commentary[1]

Global equity markets finished the second quarter of 2023 in mostly positive territory. The quarter began on a positive note, with most indices posting gains in their local currencies. The MSCI World experienced a positive return of 6.8% (in USD) over the quarter. In the US, the Dow Jones Industrial Average, S&P 500 and Nasdaq all delivered positive returns of 4.0%, 8.7% and 13.1%, respectively. This performance was mainly driven by the strength in Technology stocks and strong corporate earnings results, despite rising inflation. In Europe, the Euro STOXX 50 gained 4.2% over the period. In contrast, however, the FTSE 100 experienced a slight decline and returned -0.4%. This was driven largely by the Bank of England's decisions to raise rates twice in the quarter, and weak economic growth. In fixed income markets, the yields on US and UK 10-year bonds increased by 37 and 90 basis points, respectively. Brent crude oil declined by -3.5% due to concerns over rising global demand and the impact of ongoing supply disruptions. Copper experienced a more significant downturn, dropping by -7.3%.

Fund Commentary

During the second quarter of 2023, the Credo Global Equity Fund (CGEF) increased by 2.6%, underperforming the MSCI World Index by 4.2 % in USD terms[2].

Q2 of 2023 was a difficult quarter for global equity fund managers. Coming out of the mini-banking crisis experienced in the US during March, fund managers remained cautious as to whether there would be any further fallout. At the same time, markets remained heavily focused on key economic data to ascertain the direction of interest rate travel. The main themes continued to focus on inflation, interest rates, recession, and geo-politics. The market had been eagerly awaiting confirmation that inflation was under-control and that central banks could pivot, and start slowing the rate of interest rate hikes, and in fact, start cutting interest rates. To this point, there seems to be a strong belief that the US economy has remained resilient, will likely have a "soft landing", and hence the US market has rewarded US stocks with strong gains during the quarter. The story, however, is a little more tepid across the Atlantic. In the UK, it appears that the Bank of England is still fighting strong inflation data, fears a "hard landing" and hence, continues to rise interest rates rapidly. This again, has been reflected in the performance of the FTSE 100 index.

Probably the biggest theme to emerge out of Q2 of 2023, was the tangible arrival of AI (Artificial Intelligence) through the recognition of ChatGPT. The launch of ChatGPT in January 2023, and subsequent hysteria it caused, led to a significant re-rating of several mega-cap technology companies over the last three months. These companies include, Apple, Microsoft, Meta Platforms, and Nvidia, to name a few. Interestingly, these companies are also the largest cap weighted companies in the world, and as their valuations increase, so does their representation and contribution to the performance of their respective indices. So, what we have seen through the course of the last three and six months, is a very narrow rally of approximately 10 to 15 mega-cap stocks, that have created the illusion of a very strong rally in equity markets. Yet, stripping away the contribution of these stocks to performance returns, indices would look far less sanguine. As Value investors, we tend to steer away from highly rated Growth companies, and as such, although we have some exposure to names like Microsoft, Meta Platforms and Alphabet, our general underweighting of the sector is a large contributor to the CGEF's underperformance.

(1) Source: Bloomberg.
(2) Performance of the Credo Global Equity Fund Class B Retail Shares over the period 31/03/2023 to 30/06/2023.

The main positive contributors to the CGEF included strong performance from higher beta stocks as well as some healthcare names. Meta Platforms, Flutter Entertainment, Frontdoor, HCA Healthcare and Cigna Group were all positive contributors over the period.

The detractors from the portfolio included some consumer facing stocks like Dollar General, which surprised the market with a profit warning, and The Walt Disney Company, as well as some of the more defensive names in the portfolio like Progressive Group, and British American Tabacco.

We added new positions to the portfolio during the quarter, which included Entain plc and JDE Peet's. We sold out of our positions in Canada Goose and Unilever.

Looking Forward

The second quarter of 2023 has been a difficult period for Value orientated investors. Performance returns have been heavily skewed depending on one's exposure to a handful of mega-cap technology/Growth stocks. These narrow market rallies are concerning and are generally unhealthy for markets, which tend not to end well. The euphoria around the introduction and benefit of AI into the world, seems to be a little overdone. Stocks that appear to be best positioned to take advantage of the "new new thing" have all re-rated significantly and look expensive at current levels. We refuse to get sucked into this "FOMO" trade and continue to follow our disciplined approach.

As always, we remain patient and true to our investment philosophy.

Jarrod Cahn, Co-Portfolio Manager