Looking into 2024
Risk and Markets

EUROPE
ASSET
MANAGEMENT

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Risk and the Issues for Consideration

- Model and Generic portfolios suffered in 10 out of 12 months in 2023 with the active investment industry largely trailing most global equity indexes.
- Almost the entire economics community predicted a recession in 2023 which never materialised.
- As such, high quality corporate and sovereign bonds failed to really excite in 2023 with performance found in just High Yield and Money market instruments.
- These two sectors are found at both extremes of the bond universe which speaks to the level of bar bell diversification one had to adopt in 2023 to outperform in bonds.
- Global equities were up 4% prior to November's rally with almost all of that gain coming from just 7 American stocks out of a total 1,500 companies listed within MSCI World.
- Despite the late rally in 2023, there were huge elements of the global market flat or negative in performance terms for 2023.
- Properly diversified solutions are simply not constructed to outperform a market where 70% of the gains are coming from limited constituents.
- Performance of the same 500 American stocks (S&P500) through 3 different lenses in the first 10 months of the year.

    1. S&P500 up **9.23%**
    2. S&P500 (MAG 7 only) up **78.42%**
    3. S&P 500 Ex MAG 7 (aka S&P493) down **-1.03%**

See for Yourself

Is 2024 Different to 2023?

- To put into context – 2024 has begun with the Mag 7’s starting market cap being bigger than the market cap of Japan, France, China and the UK combined.
- These 7 stocks make up 29% of the S&P500’s size meaning passive clients are subconsciously allocating a vast amount of capital into a very small pool of winners – a disaster witing to happen.
- Likewise, the S&P500 makes up 70% of the global equity market meaning 7 stocks now account for 20% of the global equity market.

The Regulatory Conundrum: Up before the Beak!

- Consider that most investment solutions are globally these days and most have a 50-80% weighting to equities, it's conceivable that 15%+ of most models are allocated to just 7 stocks just to keep pace if you have a passive portfolio.
- Remaining agnostic about the viability of these 7 stocks, for 2024 to replay 2023 we need these companies to not only remain exceptional but to keep getting more exceptional to maintain their dominance. Risk!

Risk ON

2023 November and December = Good News

- November and December's aggregated performance represented one of the sharpest market recoveries since 2008-9.
- Primarily, the speed of this rally backs up the assertion of deep levels of pessimism existing in markets over the first 10 months of the year. The Mag 7's parabolic performance had somewhat masked this in an index level.
- On a headline level, the performance of these two final months put almost all clients back into profit for 2023.
- The rally came just in time for end of year reviews to turn away from another year of pejorative conversations about lackluster performance to one of slightly more positivity around clients and markets finally starting to make their way back from the natural losses of 2022.
- Notably, this rally brought the most relief to those in the more defensively minded portfolios which had a torrid 2022 and badly needed some positive performance.
- Both Bond and equity markets took part in the rally with notable strength coming from Emerging market debt (up 11%), AAA Corporates (up 9%) and Gilts (up 9%).
- Nirvana – Both Bonds and Equities Rising – A reverse of 2022…not!
- The year-end rally was the perfect example of the risks in selling a portfolio and moving to cash, which many clients were opting for, contra to the message coming from the advisory community about staying the course and remaining invested.

Risk in the Macro, Risk in Politics

Slightly more Upbeat = Positivity for 2024?

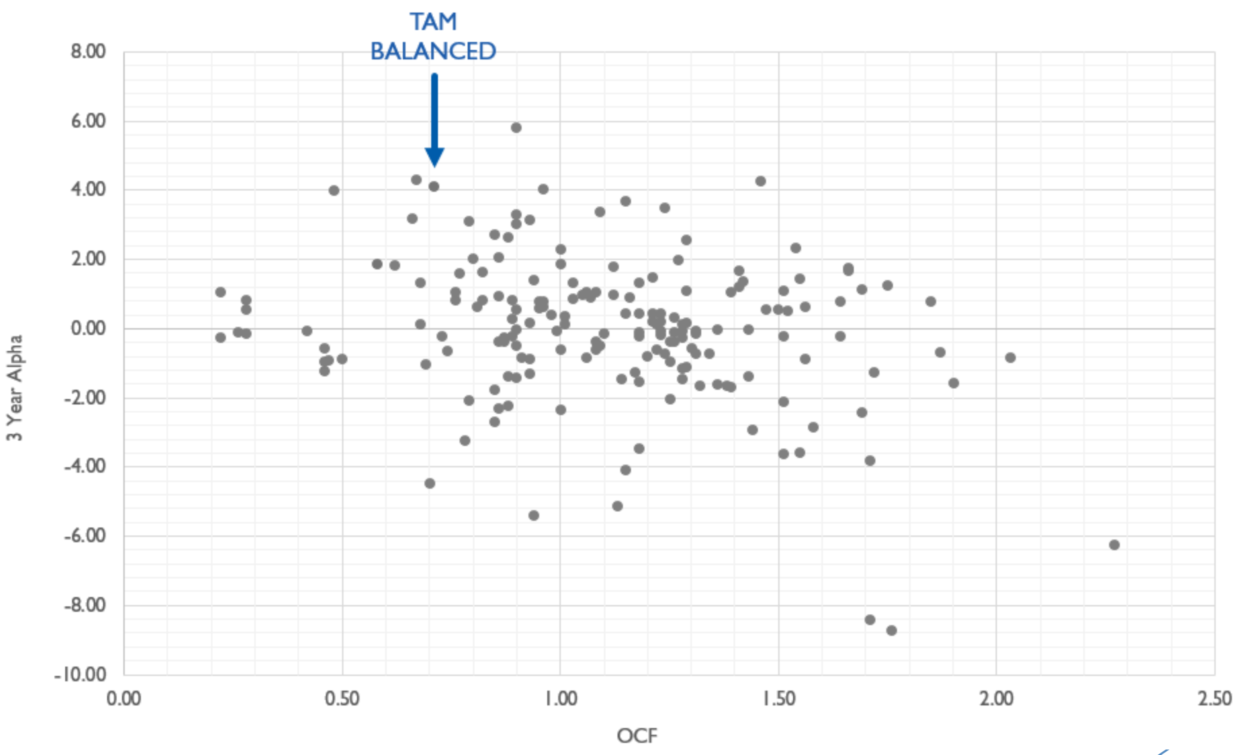
- From a macro perspective, we see 2024 moving into a market regime where inflation's floor will be 2% rather than its ceiling. Likewise, interest rates are going to revert to a more normalised, pre 2008 level where 3% is the floor as opposed to the ceiling.
- We expect 2024 to house more volatility in the short term as the market gets to grips with these new paradigms.. Active management will be critical here to avoid short term overvaluations and identify valuation pockets primed to benefit from continued positivity.
- We see 2-3 cuts as more appropriate in both 2024 and more in 2025 with that equating to 0.75-1% of reduction to the central bank rate and not starting till later in the year .
- This scenario also sees equity positivity remaining in place but **tilted towards value stocks over Mag 7** and with additional equity volatility taking its cue from global CPI trajectory which should come down but with turbulence. Real yields are going to become an area of interest for client portfolios as are income via dividends.
- Holistically, this spells a positive environment for the 50/50 portfolio which can take advantage of a rallying equity market under a soft-landing scenario but also deliver capital preservation from high quality bonds should a recession ensue.
- Politically, 2024 will see the largest number of the global population voting for a new leader in history.
- Across the Atlantic, Trump has an uncomfortably high chance of taking the White House again. Whilst he remains a wildcard, he is now a known unknown and portfolios should be better prepared for his brand of presidency.
- Trump's 2016 tax cuts are up for renewal or scrap in 2025 so expect to see these reversed if Biden wins but maintained if Trump takes a second term. This fact remains underpriced by the market so expect to see some positive correlation between Trumps polling and the S&P 500.

Bull Markets Climb Walls of Worry

Risk and Value

3 Year Alpha vs. OCF

Is there a reasonable relationship between price and value?



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