BROMPTON
ASSET MANAGEMENT

Quarterly review

for the three months to 31 December 2023

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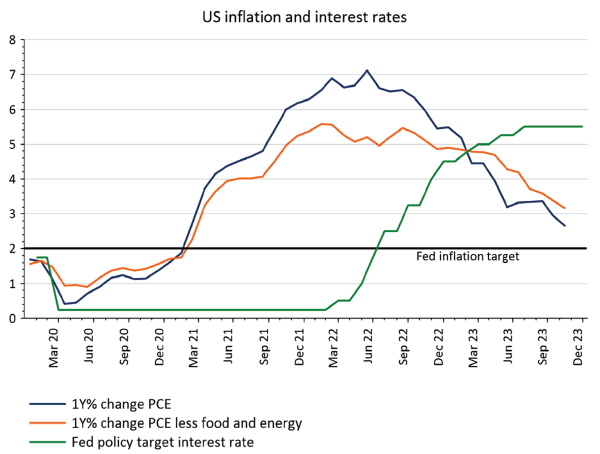
Chief investment officer

Global equities rose 6.42% in sterling over the final quarter of 2023, taking their rise to 15.88% for the year. Markets finished the year in buoyant mood as investors became increasingly confident that interest rates had reached their peak for this monetary tightening cycle. Some leading indicators imply an economic slowdown is coming in 2024. A soft, as opposed to a hard, landing may, however, lie ahead.

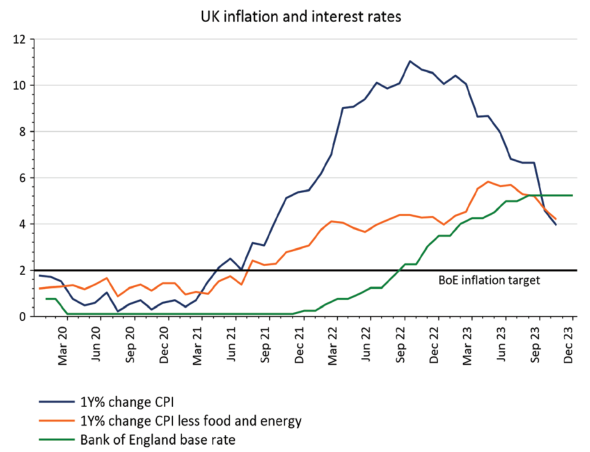
The Federal Reserve's preferred inflation measure, the personal consumption expenditures (PCE) price index, fell to 2.6% in November, just 0.6 percentage points above the Fed's 2% target, as the chart below shows. Rising food and housing costs added to inflation but energy costs were disinflationary, with the oil price down 22.21% in sterling over the quarter in response to weakening economic activity levels, more than reversing earlier rises to leave the price down 9.22% over the year. Minutes of the Fed's December rate-setting meeting included surveys showing that investors expected an interest rate cut as early as June.



Source: LSEG Datastream

The chart opposite reveals a similarly encouraging picture for UK inflation. Headline consumer price inflation (CPI) was 3.9% in November, the lowest figure since November 2021. Core CPI, however, which excludes energy, food, alcohol and tobacco, stood at 5.2% but was still down from 5.6% in October.

Eurozone headline inflation had fallen to 2.4% in November. Equities in Europe excluding the UK rose 7.62% in sterling over the quarter, outperforming US equities, up 6.94%. UK equities gained only 3.21% but smaller companies, typically more sensitive to the domestic economy, gained 8.54%.



Source: LSEG Datastream

US equity market leadership was narrowly focussed on technology stocks, which rose 11.22% in sterling to finish the year up 55.76%. Valuations in the technology sector and other growth sectors tend to rise in response to signs that interest rates are likely to fall because investors discount their future cash flows less aggressively. The converse was the case in 2022, when technology shares fell 26.29% in sterling as a value style of investing proved more successful than growth investing as interest rates rose. Some technology companies responded to the difficult conditions of 2022 by cuttings costs and freezing recruitment. This is likely to have boosted profits in 2023. Technology stocks also benefited from secular change as investors recognised the potential of artificial intelligence. Nvidia, which supplies semiconductors to artificial intelligence companies, rose 222.14% in sterling over the year. In February, Jensen Huang, Nvidia's chief executive, announced the arrival of the "iPhone moment" for artificial intelligence.

Global bonds returned 8.10% in dollars over the quarter but the dollar's 4.26% fall against the pound reduced the gain to 3.50% in sterling. UK government bonds outperformed, returning 8.54% as inflation proved less "sticky" than many commentators had feared. Investment-grade corporate bonds and high-yield bonds rose 8.18% and 6.81% respectively.

Dollar weakness is typically associated with capital flows into emerging market assets and emerging market debt returned 9.26% for dollar investors although only 4.61% in sterling. Dollar weakness did not, however, benefit equity indices in Asia excluding Japan and emerging markets, which underperformed

Quarterly review (continued)

for the three months to 31 December 2023

over the quarter, rising only 1.95% and 3.34% respectively in sterling. Chinese stocks, which comprise the largest share of both indices, fell 8.29% in sterling over the quarter, taking losses over 2023 to 16.05%.

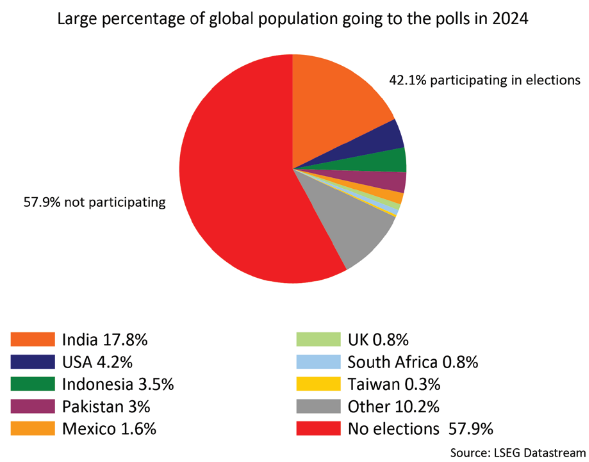
The end of zero-Covid-19 restrictions in December 2022 provided a short-lived economic growth fillip but investors' fears regarding China's over-indebted property sector were confirmed when Country Garden, once the country's largest home builder, joined its rival, Evergrande, in defaulting on its debt. Chinese stocks may remain out of favour in 2024 for two reasons: US bi-partisan support for sanctions against Chinese companies to protect US technological leadership in key sectors and Beijing's regulatory intervention in private companies in pursuit of so-called "common prosperity".

By contrast, Indian stocks rose 7.21% in sterling over the quarter. Investors may have favoured Indian stocks at the expense of Chinese stocks because India's economy is growing faster than China's and because the pro-business policies of Narendra Modi, the prime minister, have improved the ease of doing business in the country. The International Monetary Fund (IMF) reckons India's economy will grow at 6.3% in 2023 and in 2024 whereas it thinks China's growth figures for this year and next will be 5% and 4.2% respectively.

There are grounds to be positive about the prospects for equities and bonds in 2024 because easier monetary policy should prove a tailwind for both major asset classes. Economies have proved resilient so far in the face of rising interest rates despite well-established leading indicators suggesting the onset of recession. These include inverted yield curves as 10-year government bond yields fell below two-year yields, and tighter lending conditions at commercial banks.

US stocks may perform well because the economic environment may favour growth sectors such as technology and growing investor recognition of the commercial possibilities of artificial intelligence. The current year may also prove to be more favourable for emerging market equities overall although it may pay to be cautious about Chinese stocks. Some developing countries have lower levels of public sector indebtedness than industrialised countries and better economic growth prospects. The IMF reckons developing countries will show 4% economic growth this year against just 1.4% for developed countries.

Political risks may, however, move markets more this year than in 2023 because a large percentage of the world's population will be going to the polls in general elections, as shown in the chart below. Countries holding general elections in 2024 include the US, India, Taiwan, Indonesia, Pakistan, South Africa and Mexico and probably, the UK. Gold and gold equities may provide diversification and prove defensive should equity and bond markets fall.



Important information

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