

UNCERTAINTY IS THE ONLY CERTAINTY

Markets whipsawed by AI anxiety

Equity markets experienced repeated sharp falls and intermittent recoveries over the course of the month, driven by volatility in some of the companies that have benefitted the most from AI-related investment. The MSCI World index ended the month with a decline of 0.12%, however the US market was notably weak with the MSCI US index declining by 0.71%. Japanese markets were weak in local currency terms, however after central bank intervention to strengthen the Yen, the market was more neutral in Euro terms. European markets were the standout in the month, with the MSCI Europe index rising by 0.97%. The UK was the strongest of the major European markets, with strength from energy producers and a rise in M&A activity lifting stocks.

The focus for market declines was the semiconductor stocks that had delivered extremely strong performance over the past year, with limited capacity leading to very high prices for some semiconductors most needed for developing the data centres to support the expansion of AI. Growing concerns that the stock prices of these semiconductor companies had risen too far, combined with concerns that the current level of investment spending by the AI hyperscalers that are building the data centres was not sustainable, led to sharp falls in semiconductor stock prices.

Adding to the uncertainty in the month, the peace deal between the US and Iran collapsed, leading to further military action by both sides and a renewed blockade in the Strait of Hormuz, resulting in a spike in the price of oil.

Finally, seizing the uncertainty zeitgeist, Kevin Warsh marked his first Federal Open Market Committee meeting as chair of the Federal Reserve, with an extremely opaque press conference that led to inflation concerns in the US, with the consequence that rates on longer term treasuries rose to their highest level since 2007, before the financial crisis.

Value style shows strength despite volatility

The portfolio returned 1.79% in the month, ahead of the 0.12% for MSCI World. The fund style was a major contributor to the outperformance, with the value style performing well in the month. Small-cap's struggled in the month, and the fund's modest small-cap tilt was a headwind to performance. The MSCI World Value index returned 2.94% in the month. Relative to MSCI World Value, the portfolio's style was relatively neutral, as a higher exposure to the value factor was offset by the small-cap tilt and also a slightly higher cyclicality than the more defensive value index. A large amount of the underperformance is attributable to a single stock, Microsoft, that the fund does not own. A recent entry into the Value index, it had a weight of over 6% in the index in the month, and consequently its 23.8% return during the month was a significant headwind to the portfolio's relative performance.

Energy was the strongest market sector in the month, benefitting from the higher oil prices due to the blockade in the Strait of Hormuz. Financials and Consumer Staples were also a relatively strong sectors in the month. Information Technology, dragged down by semiconductor stocks, was the weakest sector in the market. Utilities and Industrials were also weak during the month.

A number of fund holdings had strong performance during the month. US insurers Travelers and MetLife were both strong contributors to performance during the month, with Travelers posting strong earnings and MetLife benefiting from a more stable interest rate environment. European steel company ArcelorMittal was also a positive contributor to performance as the company reported a strong second quarter earnings figure, with the company profiting from an improved European steel market environment. Japanese bank, Mitsubishi UFJ also contributed positively to performance as the company also benefitted from strong annual earnings, with the company reporting stronger than expected loan growth and rising fee income.

Strategy

Ethical Global Value invests in global equities from developed markets, cf. the fund's prospectus. Stocks are selected using the value strategy, meaning that through careful fundamental analysis, the team strives to identify companies that trade at healthy discounts relative to intrinsic value. A risk-aware approach to the portfolio construction ensures a well-diversified portfolio and broad exposure across sectors and regions. The fund applies exclusions as detailed in Methodology Document for Sustainable Investing.

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