Sparinvest

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

The portfolio returned 5.13% in the month, ahead of the 0.97% for MSCI Europe. The portfolio's value bias was the primary driver of outperformance, supported by a lower exposure to Information Technology than the benchmark. The MSCI Europe Value index returned 4.32% in the month, benefitting from the value style as well as its sector exposures. Relative to MSCI Europe Value, the portfolio received a modest boost from a slightly higher exposure to the value factor. This was partly offset by the portfolio's lower exposure to Energy and Financials, funded by a higher allocation to Information Technology.

Energy was the strongest performing sector as it benefitted from the higher oil prices due to the blockade in the Strait of Hormuz. Financials and Communication Services were also relatively strong sectors. Information Technology was the weakest-performing sector, weighed down by semiconductor stocks. After detracting from relative performance for much of the year, the portfolio's lack of exposure to ASML contributed almost 1% to relative returns during the month.

Several portfolio holdings performed particularly well, making stock selection another important driver of outperformance. European steel producer ArcelorMittal contributed positively after reporting strong second-quarter earnings, reflecting an improving European steel market. UK based telecoms group Vodafone's shares also rose in July after French telecom billionaire Xavier Niel agreed to buy a 16% stake at a premium, boosting investor confidence in the company's turnaround.

Strategy

European Value invests in European equities, 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 countries.