STRATEGY OUTLOOK

June 2023

Key takeaways-

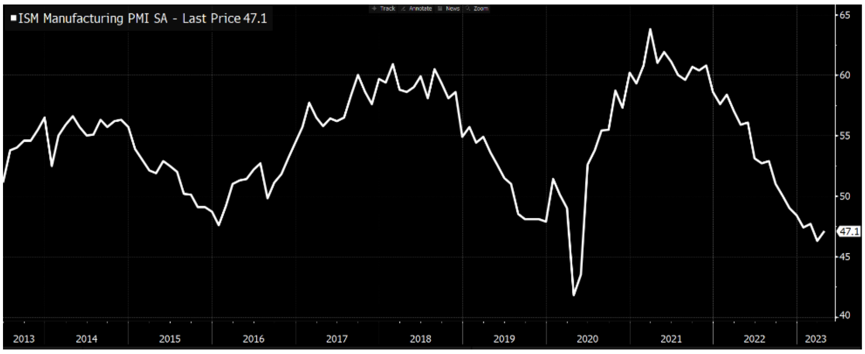
- Nvidia and Cheddar Cheese up 40%
- The calm before or after the storm? resilient markets, nervous investors.

June and summer have finally hit us here in Zurich. Markets too seem to be encountering a mirage against the future **direction of interest rates, inflation, and liquidity**. Are we returning to the old normal of sub trend growth and 2% inflation? The return of liquidity? Stickier inflation etc and, as usual, a lot of news flow across the economic, political, geopolitical, and social spectrums.

As the S&P500 remained unchanged for May the action was all within the index. The new darling of the stock market, NVIDIA, posted a +36.3% move with the wooden spoon going to Advance Auto Parts at -41.9%. NVIDIA is at the **vanguard** of the Artificial Intelligence (AI) revolution. **Undoubtedly it is a revolution, but history is brutal** and shows these darlings seldom stay in the spotlight. The first graph looks at a variety of stocks through their Price/Sales ratios and highlights how 'special' Nvidia currently is.

Just as Nvidia stole the headlines recessionary concerns remain resolute. **Germany has officially entered a recession** over the month with very weak consumption data. Other proxies for global demand remain weak including South Korean exports -15% this year.

The second graph highlights the Institute of Supply Management (ISM) manufacturing survey which languishes at Covid levels. It's the same picture across the ISM service sector too. These are priced into markets today. Indeed, it's been a turbulent few years with the COVID demand shock (2020), the stimulus driven rebound (2021) then reality hitting home in 2022. For what it's worth we remain of the opinion that we have been in a mild 'recession' for quite a while (despite robust labour markets) and markets reflect this. However, we're cautious of the narrative that Nvidia (and gang), via AI, are the **elixir to the productivity issues and hugely deflationary.**



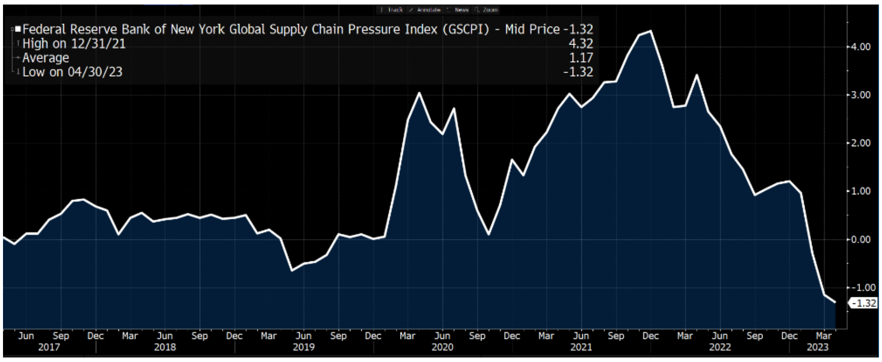
Invention, adoption, and change take time. We read recently that it took 48 years after the invention of the first tin can for the can opener to be invented. For the steering wheel on a car, it was 8 years and for sliced bread it was 30 years after the standard loaf of bread was sold. **AI is advancing at breakneck speed.**

Inflation is falling but there remains a **huge current cost of living crisis**. The faster prices fall the better. Inflation is psychological and will affect consumption, capex spending and savings. The official narrative isn't however clear.

"We now understand better how little we understand about inflation " Jerome Powell

"If inflation is not controlled the Fed will have to do a lot more " Fed Bullard

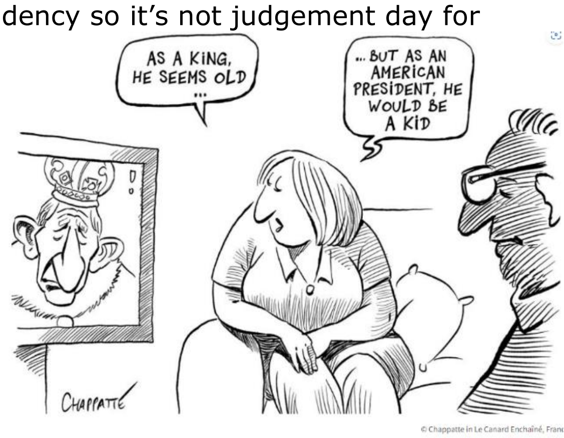
UK food prices as highlighted by Cheddar Cheese (+39%), eggs (+37%), Milk (+33%) and potatoes (+28%) over the last 12 months are examples of the pressure on the consumer. Add in mortgage costs, energy bills etc and the squeeze is real.



However, producer prices are collapsing. Spanish PPI a year ago was running at +40%. For April it was -4.5% yoy. The third chart from the NY Federal Reserve highlights the collapse in the pressure on global supply chains.

So short term we expect inflation to continue to fall. However,…. We remain concerned structurally of the end game. **There is too much debt.** The banking system is beginning to creak at the seams, politicians, due to the political system, only seek re-election and ultimately the money needs to be repaid. Do we see a continued kicking of the can down the road or are we witnessing the start of financial repression. It matters as the issuance of debt is deflationary but money creation (banks being forced to lend) is inflationary.

In other news Florida governor Ron DeSantis has announced his presidential candidacy. Biden tried and failed several times for the Presidency so it's not judgement day for DeSantis's political career but it's important given he needs to defeat Mr Trump.



Checking William Hill, the UK based bookmaker the odds for next year's Presidency are - Biden is 11/8, Trump 9/4, DeSantis 4/1, Robert Kennedy Jr 16/1, Kamala Harris and Nikki Haley both at 28/1. **Place your bets.**

Broadly we remain underweight in equities. The full effect of interest rate hikes is only beginning to develop. Ultimately, we believe stocks are bottoming and are looking for opportunities to get bullish. Over the month we did increase the beta of the portfolio by adjusting exposure in emerging markets and technology. Going forward we have, and are, adding niche investments which fit our strategic themes, and which don't require as much of a binary bet on many of the issues discussed.

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