Investment Commentary

"The basis of successful investing is the thoughtful analysis of the fundamentals "

Philip Fisher

Our World Stars Global Equity strategy has done well this year. We are not surprised - we started the year optimistic and still are.

We invest in global leaders, companies that have great quality and can generate high returns over the long term. Last year investors took a lot of blows, on inflation, interest rates and valuations. Good companies sold off hard, creating an opportunity for us to buy more of them at great prices.

Philip Fisher's book Common Stocks and Uncommon Profits, written in 1957, is the definitive book about long-term fundamental investing in quality companies. It provides an important perspective in uncertain times. To Fisher, successful investing is grounded in fundamental analysis and qualitative factors. He believed in understanding the facts about a company's business and in focusing on companies with unique and sustainable competitive advantages and strong long-term prospects for growth and value creation.

The record shows that we did the work to make sure we understood what was going on in the companies we own and to reinforce our conviction. Our best performers include technology companies like Nvidia, Salesforce and Adobe that are long-term beneficiaries of the growth of the digital economy, artificial intelligence and the internet of things. Our consumer and industrial stocks have not done badly either.

We thought this year would be positive and that is how it has turned out so far. The second half of the year could bring a long-expected slowdown but we think that private and corporate demand will be resilient and interest rates in the US and Europe are close to a peak, which will support economies and markets. There may well be volatility but many good companies are cheap and will do well. That is why we think any pullback will be a buying opportunity like last year.

Charles Gelinet, portfolio manager of our Emerging Market Bonds strategy, has written this month's Investment Insight on the opportunity for Turkish corporate bonds following the elections this year. You can read it by following this link or clicking on the attachment.

World Stars Global Equities

Our World Stars Global Equity strategy had strong performance, closing up 6.5% for month and up 23.1% for the six months year-to-date, both in US dollar terms. You can find our latest factsheet here.

Performance broadened out in June. Across our top ten stocks which all rose by 8% or more, six were in industrials, three in technology and one in healthcare & life sciences. Adobe rose by 17% after releasing good second quarter results with 13% revenue growth in constant currencies and higher operating margins of 45.3%. It raised full year guidance on revenues and EPS. The rapid development and deployment of Firefly, Adobe's generative AI technology, is delivering significant new customer engagement and additional revenues, and should drive higher prices.

4 Carlton Gardens
London SW1Y 5AA
United Kingdom
Tel: +44 20 3478 1800

1 Rockefeller Plaza
New York, 10020
United States of America
Tel: +1 212 219 0200

Gartenstrasse 10
8002 Zurich
Switzerland
Tel: +41 44 552 80 70

2, Sir Augustus, Bartolo Street
Ta' Xbiex XBX1091
Malta
Tel: +356 2034 5006

J. Stern & Co.
www.jsternco.com
info@jsternco.com

Our industrial companies were boosted by a resilient macroeconomic background in the US and elsewhere, and by increasing enthusiasm for the opportunities that AI could unleash. Eaton, the US power management company, rose by 14%. The company is strongly placed to gain from the accelerated investment in data centres, linked to AI, which is one of several structural growth areas across the business. This pattern was reflected in the performance of other key providers in the sector, including connector and sensor producer Amphenol, which closed the month up 13%. Leading water technology provider Xylem rose 12% following the completion of its USD 7.5 billion acquisition of peer Evoqua. The acquisition is expected to deliver significant revenue synergies adding to the integration cost savings already disclosed.

On the downside, enterprise software provider Salesforce fell by 5% but is still up 60% year to date. The company pointed to continued cautious spending by its corporate customers, with large contracts taking longer than normal to close. Salesforce has a strong value proposition that allows enterprises to deepen their engagement with their customer base and our investment thesis remains unchanged.

Multi-Asset Income

The mid-point of this year was reached with a strong performance from our strategy, which was up 3.6% for the month and is now up 8.6% year-to-date, both in USD terms. You can find our latest factsheet here.

Equities were the leading performers with a gain of 7.3% in June (up 22% year-to-date) followed by our fixed income portfolio with a return of 2.7% (up 3.8% year-to-date). The non-correlated funds were down 0.4% (-2.7% year-to-date) impacted by the challenging inflation environment in the UK and the expectation of further interest rate increases by the Bank of England.

In equities, the technology sector's rally of previous months this year was less prominent with greater interest in other sectors. For example, Schlumberger rose by 15% in June as positive economic data raised the prospect of a soft landing for the US economy. Similarly, despite disappointing economic data in China, Estee Lauder rose by 7% boosted by recurring rumours around additional stimulus from the Chinese central and local governments.

Our fixed-income portfolio saw the recovery of some of our energy companies (YPF, Tullow and Seplat) and further strength from our Ukrainian holdings (Kernel and MHP). In the US high-yield sector, Lumen Technologies continued its recovery helped by broader strength in the asset class.

Over the past few weeks, news flow in the US has underlined the resilience of the economy despite a record level of monetary tightening through 2022-23. More broadly, although inflation is moving in the right direction in many countries, central banks remain hawkish, at least for the time being. US Treasury yields have risen across the yield curve and short-term real interest rates are now higher than before the 2008 Financial Crisis. Following this year's stronger-than-expected relative performance of our equity portfolio, we have further reduced our equity exposure from 35% to 30% and are reinvesting the cash in a combination of credit and short-dated US Treasuries. With very short-term US Treasuries now yielding around 5.4%, cash may be 'king' again.

Emerging Market Bonds

Our Emerging Market Bonds strategy was up 1.5% in June and is up 3.6% year-to-date, both in US dollar terms. Risk sentiment improved on stronger economic data, while inflation remained in line with forecasts. Emerging market credit spreads tightened, particularly in the high yield component, which now trades marginally inside the last 20-year average. You can find our factsheet here.

There was positive underlying corporate news too. Tullow Oil (Ghana, energy) announced it would buy back a portion of its outstanding bonds, which was seen as efficient capital allocation and helped address medium-term refinancing risks. Kernel's (Ukraine, agro-commodities) processed volumes of oilseed increased driven by an improvement in capacity utilisation of its plants with stabilising power supplies in Ukraine.

Our companies in Nigeria rallied on signs of a shift to a more normalised and conventional policy framework in the country. New president Bola Tinubu vowed to reset monetary policy, adopt a uniform exchange rate and end the nation's fuel subsidy programme in efforts to boost economic growth and investor confidence. Our company in Argentina also benefited from broader country dynamics. Sergio Massa became the consensus presidential candidate of the ruling coalition party for upcoming elections in October. He is viewed as more pragmatic and market-friendly than other candidates.

The market is increasingly focused on the resilience of economic growth. A slowdown is broadly anticipated but we believe there is likely to be a widening growth differential between emerging and developed markets, which should support the asset class. Corporate credit fundamentals continue to be strong although peak credit quality is likely behind us. Valuations continue to provide protection again recession risk.

Today, our Emerging Market Bond strategy offers a 12.5% p.a. yield to maturity (in US dollar terms) with a relatively short duration of 3.3 years. This comprises a 7.5% p.a. income yield which provides a degree of visibility on future returns, as well as capital appreciation potential given that the average bond price is 84 cents on the dollar.

June 2023