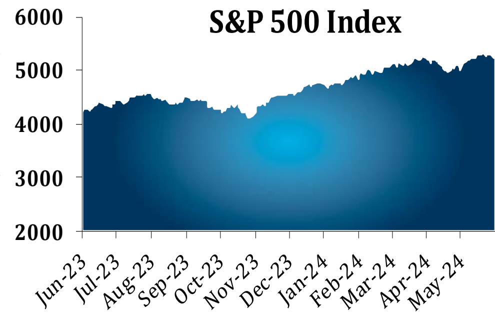
This Month in the Markets

May 2024

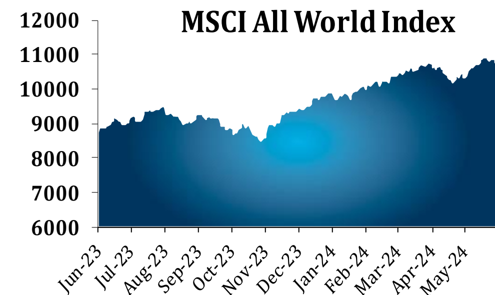
Equity Commentary

No May Showers

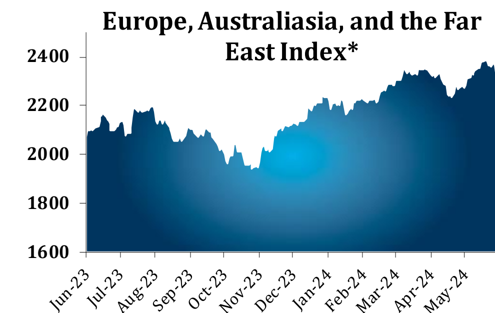
May was a good month for equities as the economic outlook supported risk assets in general. As a result, the MSCI ACWI Index was up 4.1%. The MSCI Emerging Markets Index was the underperformer in the month, with a small gain of 0.6%. U.S. shares led the gains, with the S&P 500 Index rising 5%. Growth outperformed value in terms of investment styles, with the MSCI All Country World Growth Index climbing 5.1% while the MSCI ACWI Value Index was up 3.0%. The MSCI ACWI Information Technology Sector was the biggest gainer, with a rally of 8.1%, driven mainly by semiconductor companies behind a strong Nvidia earnings announcement. Conversely, the MSCI ACWI Energy Sector Index had the slightest advance of 0.3%, primarily due to the oil price retreat. The Bloomberg Commodities Index increased by 1.8% in May, mainly due to the surge in copper prices.



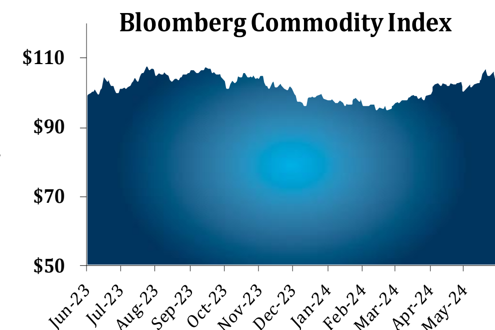
We had one sale and one buy in the quarter. We sold Starbucks Corp. (“SBUX”), as it reported declining traffic within its occasional-customer base, pressuring comparable store sales. The coffee chain’s operating margins have also been hurt by wage pressures and store unionization. We added MercadoLibre Inc. (“MELI”), a one-stop solution for Latin American commerce. The company’s competitive advantage is derived from an ecosystem of mutually reinforcing services, with a core marketplace supported by a payments and lending arm, a best-in-class shipping service, and an increasingly robust advertising platform. We think MELI has compounding potential with 5-year revenue growth and ROIC of >20%. Furthermore, the company trades at a ~6% free cash flow yield and is growing EBITDA by ~25% per year.



Salesforce Inc. experienced the largest underperformance in May, with its stock falling 12.8%. Concerns over slowing IT spending came to the fore as the company reported lower-than-expected fiscal 2025 first-quarter revenue and guided for second-quarter revenue lower than anticipated. In contrast, UBS Group AG, emerged as the top performer, with its stock rising 21.9%. This positive performance resulted from the successful completion of the Credit Suisse takeover and much stronger than expected first quarter financial results.



Our primary strategy is a mix of value and growth investing. Strident adherence to either discipline comes with a series of risks and mistakes. To acknowledge this, we try to avoid making the following often common mistakes made by either religion. Whitney Tilson recently released some lists of common mistakes for both value and growth investors. We have listed these below with our commentary in italics.



*MSCI EAFE Index

Value Investor Mistakes:

1. Investing in low-quality businesses whose stocks were value traps because the businesses' fundamentals continued to decline. *This often shows up in declining same-store sales, or revenue overall.*

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Equity Commentary

2. Failing to buy high-quality businesses whose stocks were fabulous long-term compounders. *Errors of omission can sometimes be the most painful of all. Failing to buy a wonderful company at an o.k. price can haunt an investor for years.*

3. Selling the stocks of great companies way too soon because they had risen and didn't appear as cheap. *Great companies have an uncanny ability to improve over time, compound value, and go from strength to strength. There will be periods when the market realizes this, and valuations will look richer. Pull up a stock chart on a longtime compounder and note the multiples over time. There will always be times when valuation seemed extended, but the company tended to grow into that and more given time.*

4. Failing to understand/appreciate powerful new technologies/trends. *Value investing assumes mean reversion. Unfortunately, this works better for markets overall than individual stocks. Capitalism is about competition, and products and services change over time. Disruption is happening even faster these days. It's important not to try to be contrarian just for contrarian's sake. Sometimes, the trends do have legs and staying power.*

Growth Investor Mistakes:

1. Overestimating future growth, forgetting the powerful force of reversion to the mean – driven by technology changes, new competitors, size acting as an anchor to growth, etc. (Trees don't grow to the sky!) *In this case it is ironically important to determine what is more permanent rather than a fleeting trend. Is this a secular theme, or is this a product cycle?*

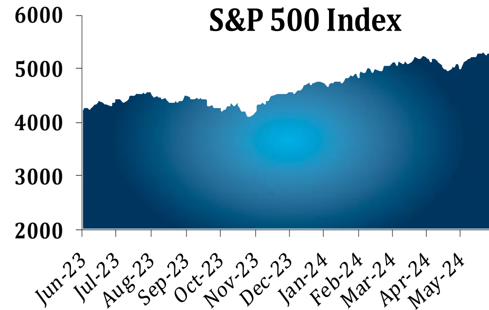
2. Paying too high a price for a stock, so even if the business performs well, the stock doesn't. *Buying Cisco at the peak of the internet bubble would be a great example. Determining what is too high of a price should revolve around some disciplined valuation work. Growth at any cost is crazy.*

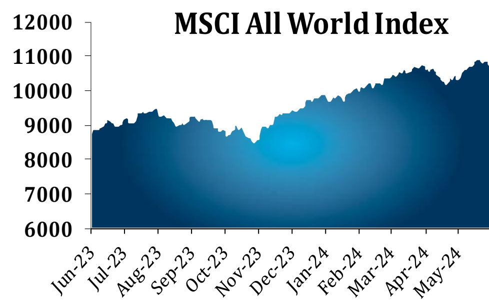
3. Falling in love with great companies and failing to sell when they should. *Avoiding these errors is difficult, especially when some almost contradict each other. For example, when is it alright to fall in love and ignore valuation to some extent but also not sell when you should? What price is too much to pay, and will growth persist? Unfortunately, there is no mathematical formula for the most critical questions*

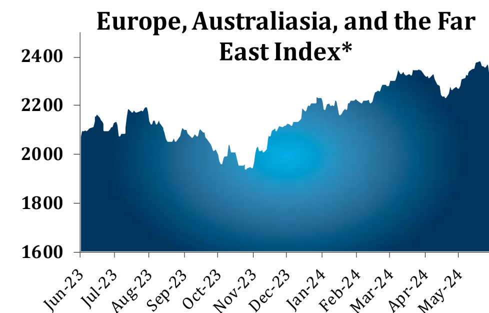
4. Getting sucked into "story stocks." *A narrative without numbers is a dangerous predicament.* Numbers provide the edifice for a solid story. *Similarly, however, blindly looking at numbers without context or understanding the qualitative factors of a business can lead one to buy value traps (see #1 value investor mistake).*

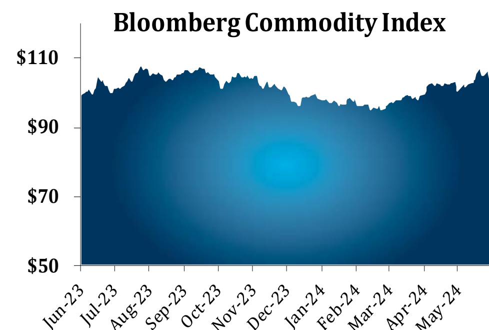
Source: "How I combined the best of value and growth investing," Whitney Tilson's Daily, Whitney Tilson, May 31, 2024.

https://stansberryresearch.com/articles/how-i-combined-the-best-of-value-and-growth-investing









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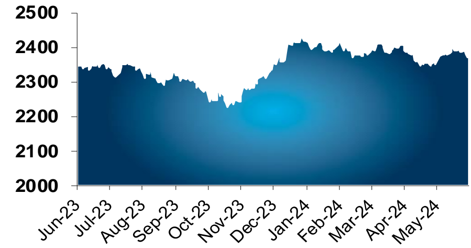
Fixed Income Commentary

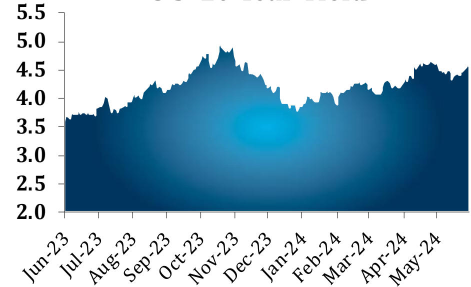
May Musings

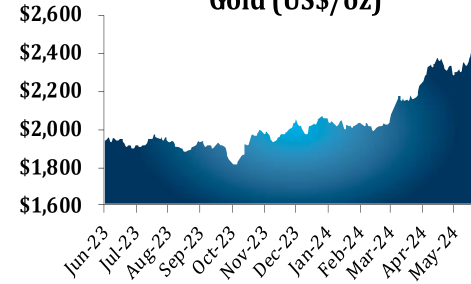
Treasury rates declined in May, retracing part of the increase in April. The 2-year treasury yield declined 0.16% to 4.87%, while the 10-year treasury yield fell 0.17% to 4.50%. The 2-year – 10-year slope ended May inverted by 0.37%. Still inverted but down notably compared to the 1.10% peak in mid-2023. An inverted yield curve is widely considered a leading indicator of a recession. The 2Y-10Y curve has been inverted for a record 705 days (as of the time of writing). This has been an oft-cited data point for those market pundits who contend that a recession is on the cards. As is seemingly always the case, there is more than one way to interpret the data. From the 6-month tenor to the 5-year tenor the curve is inverted by approximately 0.90%. However, from the 5-year tenor to the 10-year tenor the curve is practically flat. This suggests the market is expecting a shallow cutting cycle (starting in late 2024 per fed fund futures), followed by relative inactivity. As opposed to panicked, rapid rate cuts (2007/08, 2020), which suggests the Fed is expected to cut rates gradually as economic data moderates - a "soft landing." This is the Fed's ideal path, to be sure. The difficulty for the Fed and all investors lies in reading the tea leaves for a myriad of considerations, including the lag in monetary policy, ongoing fiscal spending, and leading versus lagging economic data, to name a few. All in an election year when the US appears more divided than ever…and Trump was just indicted!

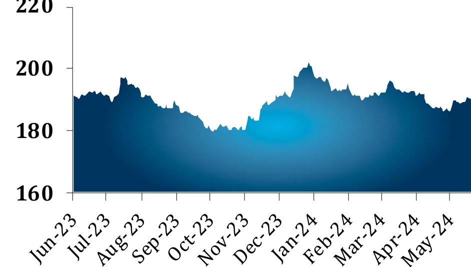
Over the last 18 months, companies have taken advantage of the strong investor demand for corporate credit to tap the market and shore up liquidity (for example, Boeing in April). This is on top of the huge refinancing waves we saw in 2020 and 2021 on the back of historically low treasury rates and very supportive monetary and fiscal policies. As such, credit spreads, though at historically tight levels, have continued to grind tighter. This suggests little fear among credit investors of a looming economic slowdown. Having said this, there has been evidence of some slowing in consumer spending, as highlighted by May retail sales figures that missed consensus targets and lower revisions from the previous month. Also, the Q1 GDP contribution from consumer spending was notably lower QoQ, though this data is admittedly choppy. Perhaps most notably, several retailers, including Target, Walmart, Amazon, and Walgreens, have announced price cuts on thousands of products to woo consumers.

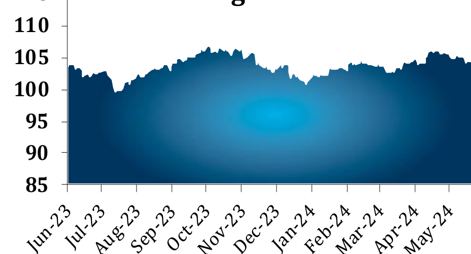
At the time of writing, the market expects just under two 0.25% rate cuts in 2024. Inflation data reported in May supported the continued disinflationary trend. We expect the shelter component to continue to decline going forward, given its long lag, which should continue to push the consumer price index lower, all else equal. With regards to the labor market, the incoming data still suggests modest weakening at the margin. For example, the number of job openings to unemployed workers has fallen to 1.2x, down from a peak of 2x in early 2022. If it were to occur, material weakening of the labor market should give the Fed confidence to cut rates and join the chorus of other developed central bank's easing. The Swiss National Bank and Riksbank (Sweden) have already cut rates this year, while the ECB is nearing a certainty of cutting rates in its June 6th meeting. Additionally, the Bank of Canada is widely expected to cut rates in its June 5th meeting.











*Merrill Lynch Global Broad Market, Ex US Dollar Index

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