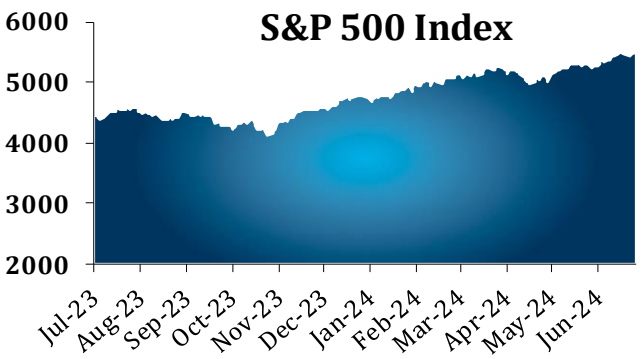
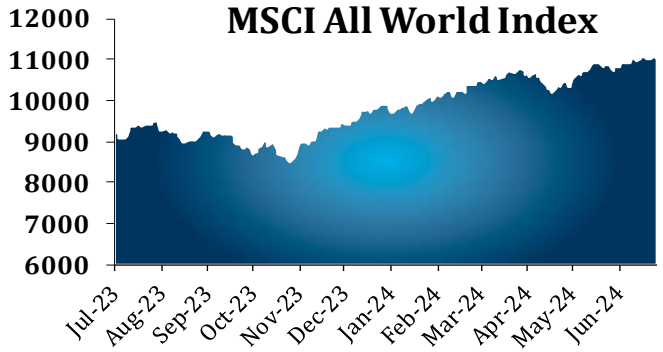
Public

# Stock Market Analysis

## Market Warnings Signals




ANCHOR
Investment Management

The major global stock market indices hit new records in the second quarter, driven by companies linked to artificial intelligence "AI". But the health of the bull market, measured by breadth, continued to deteriorate in the quarter. While a few "technology mega-caps" drove the performance of the major indices, fewer stocks are participating in this year's rally. The MSCI ACWI Equal Weighted Net Total Return Index declined 1.1% this quarter and only returned 0.9% in the first half of the year compared to 2.9% and 11.3% for the "market cap-weighted" MSCI ACWI Net Total Return benchmark. That is the widest underperformance ever in the first six months of the year.

Investors' focus on AI has caused the technology weighting in the S&P 500 Index to rise to levels seen twenty-five years ago during the "dot com bubble". While the official weighting of the tech sector in the index is now 33%, this does not include some of the mega-caps in other sectors that are also driving the "AI rally", including Amazon, Meta Platforms and Alphabet. If you include these companies, the weighting rises to 42%. During the first three years of the century, older investors will painfully recall that the technology weighting fell from 35% to 13% as the dot com bubble burst. No one can predict when the current momentum will end, but we believe it is important to remain disciplined in security selection. The lack of participation by other sectors is likely due to the impact of the tight monetary policy of most global central banks. Higher inflation and interest rates are holding back economic growth, and investors are focused on companies that can overcome these headwinds. We believe this creates opportunities with significant valuation differences occurring in companies outside the spotlight.

Looking forward, we expect the interest rate headwinds to dissipate slowly. The ECB has begun lowering rates, and US short-term interest rates should start declining in the second half of this year. The Federal Reserve has indicated that it will reduce the Fed Funds rate when inflation returns to 2% or are sufficiently confident it is sustainably on that path. The average market projection is just under two 0.25% cuts in the Fed benchmark this year, and falling interest rates are historically positive for the financial markets.

Public

# Stock Market Analysis

Elections and conflicts around the globe create some uncertainty, but with poles indicating that former President Trump is the leader in the US election, investors believe he is a known/market-friendly candidate. The radical China and immigration policies that he has raised during his campaign do raise investor concerns, but it is difficult to separate political posturing from his true policy agenda. Many pundits are hoping to see the divided government continue in the US to keep a lid on any harmful policies. President Biden's poor performance in the recent Trump/Biden debate raised concerns in the bond market that there could be a Republican sweep of the House and Senate, which could lead to higher deficits and interest rates. While this is a risk, it is very difficult to make market calls on political events, as we saw in the initial reaction to President Trump's election eight years ago.

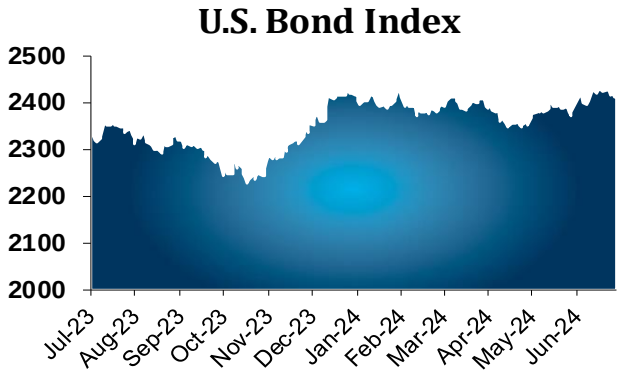
The Anchor Equity Composite declined 1.5% in the second quarter but returned +19.9% over the past 12 months, compared to +3.0% and +19.5% respectively for the MSCI ACWI Total Return benchmark. The equity composite has produced a 12.0% average annualized return over the past 5 years compared to 11.0% for its benchmark. Quality dividend shares lagged the major benchmarks in the second quarter due to the narrow market breadth. The High-Quality Income Composite returned -2.5% in the quarter compared to 0.4% for the SG Global Quality Income benchmark. The portfolio has produced a +5.5% annualized return over the past five years compared to 4.5% for the benchmark. *

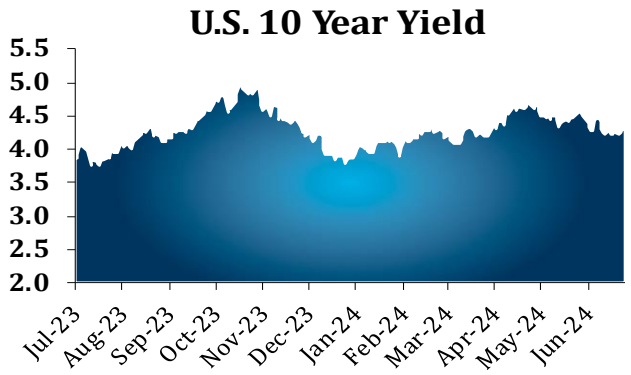
*Performance is based on Anchor equity composite portfolios. Returns include changes in unit value, reinvestment of all distributions, investment management fees, execution, custodial and other charges. Investment results are best judged over the long term. Performance should be evaluated with consideration of the client's specific goals and investment objectives. Past performance is not necessarily indicative of future results. Returns for indices or benchmarks are provided in U.S. dollar terms and solely for informational purposes. These indices or benchmarks are non-managed indices that do not accrue advisory or transactional expenses. Benchmarks are based on the client's selected asset allocation and are calculated in U.S. dollar terms. The Anchor Equity Portfolio benchmark uses the MSCI AC World Total Return Index. The Anchor High Quality Income Portfolio benchmark uses the SG Global Quality Income (USD) Index.

Public

# Fixed Income Analysis

## Rates and the Labor Market




ANCHOR
Investment Management

June was a timely reminder that we are in an election year. The day after the Trump-Biden debate, interest rates rose notably (10Y= +0.11%) as the bond market priced a greater chance of a Trump victory. Trump has been vocal about increasing tariffs on China and cutting taxes. This could lead to continued budget deficits requiring more treasury issuance to fund the shortfall. We saw a more dramatic impact to French government debt yields in June on the back of Presidential elections in France - specifically the potential for Marine Le Pen's far-right National Rally party to gain influence and possible "Frexit." The spread between the French 10-year bond yield and German 10-year yield (a signal of stress) rose from 0.48% to a high of 0.82% (higher than during March 2020!) before ending the month at 0.72% after the first round of elections. In addition to the U.S. and France, there is an election upcoming in the UK.

Treasury rates declined from the end of May. The 2-year treasury yield (4.75%) declined 0.13%, while the 10-year treasury yield (4.39%) fell 0.10%. Treasury rates have mostly retraced the surge in rates we saw in April as the market has reacted to the ebbs and flow of economic data, which has generally suggested a marginal slowing of the economy, weakening labor market, and continued disinflation. A continuation of these trends should lead to at least one rate cut by year-end – the market pricing per fed fund futures is for just under two 0.25% rate cuts in 2024. However, uncertainties remain – the labor market is a good example of this. The unemployment rate has risen to 4.0% from 3.7% at the end of 2023. The number of job openings to the number of unemployed has fallen from 1.4x at year-end 2023 to 1.2x (though steady for the last two readings). The four-week moving average of initial jobless claims and continuing jobless claims have drifted higher, though not materially. These data points suggest a weakening labor market. Additionally, the Bureau of Labor Statistics (BLS) household survey has suggested the same weakening trend (-456,000 in May). Meanwhile, the BLS's closely followed nonfarm payrolls report (which surveys businesses, not households) still suggests a very robust labor market (+272,000 jobs in May). This unusual anomaly where two of the BLS's labor market reports show very different results has been the case since mid-2022. We would expect that the Fed's tight monetary policy should reduce inflation but there will be an economic impact.

# Fixed Income Analysis

In mid-June, the Federal Open Market Committee (FOMC) left the fed funds rate range unchanged (5.25%-5.50%). They also released an updated dot plot – individual member's projection for the fed funds rate path over the next few years. The median dot now shows an expectation for one 0.25% rate cut, one fewer than the last (March) dot plot. Market rate cut expectations have consistently been pushed back on the back of elevated (though declining) inflation and a strong (though weakening) labor market. These factors were also reflected in the updated Summary of Economic Projections (individual members' projections for inflation, growth and the unemployment rate). The year-end median projection for core PCE inflation was revised higher by 0.2% to 2.8%, while the 2025 year-end unemployment rate projection rose 0.1% to 4.2%. We also note that the longer-term dot - representing members' view of the (theoretical) rate at which prices are stable and the economy at full employment - rose from 2.6% to 2.8%. The fed funds rate above this terminal rate is deemed to be a restrictive monetary policy. While there is significant dispersion in the 2026 dots, all but two of the individual projections expect the fed funds rate to be restrictive for the foreseeable future.

Anchor Investment Management Ltd. is Licensed to Conduct Investment Business by the Bermuda Monetary Authority

ANCHOR
Investment Management

## Disclaimer

This material is not intended to be relied upon as a forecast, research or investment advice, and is not a recommendation, offer or solicitation to buy or sell any securities or to adopt any investment strategy. Past performance is no guarantee of future results. The opinions expressed may change as subsequent conditions vary. The information and opinions contained in this material are derived from proprietary and nonproprietary sources deemed by the authors to be reliable, are not necessarily all-inclusive and are not guaranteed as to accuracy. There is no guarantee that any forecasts made will be correct. Reliance upon information in this material is at the sole discretion of the reader. Investment involves risks. Readers should consult their financial advisors prior to any investment decision. Index performance is shown for illustrative purposes only. You cannot invest directly in an index. Sources may include MSCI, Bloomberg, and S&P Global. Information contain within is private and confidential and for the sole use of clients of Anchor Investment Management Ltd. (“AIM”). AIM respects the intellectual property rights of others. If you see a copyright or trademark of yours which is being infringed, you may notify AIM at info@anchor.bm. We will contact you to obtain details of your claim.