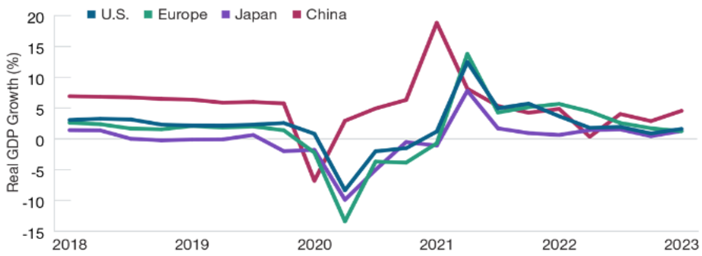
# MONTHLY BULLETIN

## July 2023

### Thought of the Month

For the month of June 2023, the main themes that affected our portfolios and respective strategies are:

1 – Macro environment a serious concern, recession worries remain.




As of March 31, 2023.
Sources: Haver Analytics/U.S. Bureau of Economic Analysis, Statistical Office of the European Communities, Cabinet Office of Japan, Japan Ministry of Internal Affairs and Communications, International Monetary Fund.

The first half of 2023 ended with a month of continuous pressure on capital markets. Growth has slowed in all major economies, but there are no signs of recession yet.

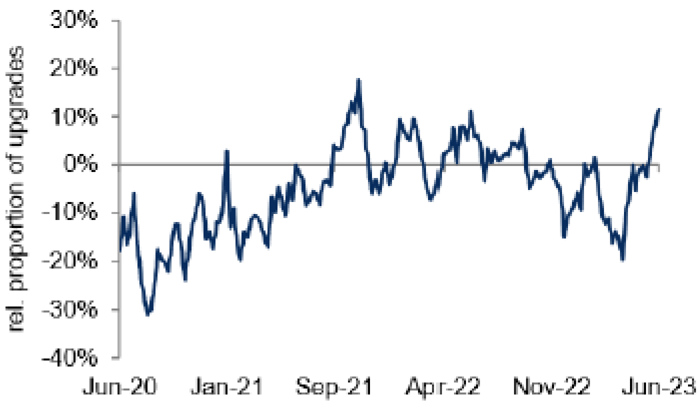
Currently, the main trade-off is between being excessively pessimistic and miss important opportunities, versus acting on the expectation of the delayed impact of 500bps rate hikes effected by the Fed.

Although banking crisis seems contained, tight credit conditions remain. In collboration with the debt ceiling saga, both have a negative effect on investment interest and liquidy.

Core inflation readings keep elevated, with service sector inflation trending up and energy price being a serious risk, for Europe in particular. We should expect the US inflation to hover between 3% and 5% for some time (years) and during this period, the US Treasury will need to issue around $1.4trilliion in debt to cover deferred payements and restore cash reserves.

Our worries gravitate around heavy Treasury issuance, a shrinking money supply, and the lagged impact of credit tightening, as these have enough power to destabilise markets. We live and work in a low "signal-to-noise ratio' in the data, with narratives that do not converge around fundamentals, therefore we remain cautious and keep an active stance on our stock selection process and risk management.

2 – Is the worst priced into Real Estate markets?

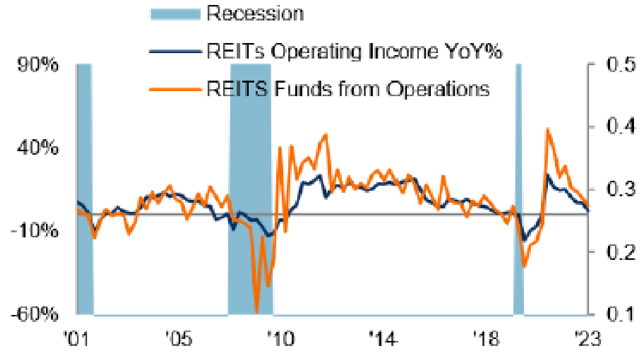



Source: State Street Global Markets, Thomson Data Stream, I/B/E/S

As the Fed continues to work towards the 2% inflation target, we are analysing various factors that tend to put real estate sector on the short list of concerns.

There are incipient signs of market participants becoming more positive on the REITs space (and so are the analyst revisions, in the Chart). Although operating income growth is slowing, the perception is that the bad news have already been accounted for since the sector is valued below the 25th percentile. Some of the REITs are very well prepared to fare the challenging credit environment (the selected ones in US and Canada, and many in Singapore) with the Weighted Average Maturity of Debt relatively long, low leverage risk and interest coverage ratios at reassuring levels.

In US, earnings, sales and cashflow growth have outpaced the same for the broad market, with the MSCI US REIT outperforming the MSCI US index by 12%. At this point in time, we are monitoring the funds from operations as this is a better representation of a company health versus the traditional EPS. From this perspective, the underlying profitability of REITs sector is not encouraging, especially ahead of potential recession (see Chart).




Source: State Street Global Markets, Bloomberg

In conclusion, for the sector at this point in time, we think that majority of the bad news are already priced in, and while earnings and profitability are below expectations, balance sheets are strong and cap rates imply attractive valuations for a selected underlying (this includes office and residential, too).

3 – Equity market rotations.

Money flow has been in a slow flight-to-quality since the market bottomed in October last year, with most of the monies flying into mega-cap technology issues, namely, AMZN, META, GOOG, MSFT, NVDA, TSLA and of course, AAPL which in the last couple of weeks, has become the largest capped company in the world, topping $194.48 per share for a $3.02 trillion market cap on the final trading day of June. June saw an intensified interest in quality stocks from all over the World.

To note that all mentioned tech companies are in the world's top ten largest capped companies with NTT (Nippon Telegraph & Telephone), Saudi Aramco and Berkshire Hathaway making up the other three at the close of June 2023.

Earnings Season for quarter two's results will begin in a couple of weeks and is usually synonymous with downside guidance, no guidance at all or underwhelming overall results. It is the main contributing factor to why quarter three is the most volatile (and sometimes miserable) quarter of the year. Whether or not the tech giants can keep this momentum up along with the Homebuilders, Discretionary and Industrial sectors, is the theme attracting significant attention.

In addition, analysts have warned that large banks' earnings have peaked as net interest income is likely to continue to decline, credit costs are gradually normalizing and increasing, and expenses are pressured by inflation. We see flows normalising and gaining interest in Japan financials, with a surprising tick up in European financials, too.

We are expecting a volatile quarter, not only month of July, and while believing in the inflows into Real Estate sector, we will not chase the European financials related ones.


Source: State Street Global Markets

## From the News Desk to the Investment Team

- 7th June - China share of US Goods Imports falls to lowest since 2006.
- 8th June - US trade deficit widens to 6-month high, expected to dent economic growth.
- 15th June – FOMC, Fed maintain the federal funds rate in a target range of 5 to 5-1/4 percent.
- 16-21st June - Secretary Blinken's visited the People's Republic of China.
- 20th June - China cuts benchmark lending rates as policy easing picks up.
- 21st June - Fed Powell expects more Fed rate hikes, pause temporary.
- 22nd June - BOE hikes rates to 5% in surprise move.
- 25th June - Europe ECB doesn't want stablecoins backed by central bank money.
- 26th June - S&P cuts China GDP forecast as calls for stimulus intensify.
- 27th June - PBoC set onshore Yuan stronger than expected for second day.
- 30st June – Yellen decides to travel to China to reestablish "contact".

Major US indices closed out a strong first half of the year, powered by technology stocks as Apple achieved a historic $3 trillion market capitalization. Notably, the S&P 500, Dow Jones, and Nasdaq Composite indexes all notched gains for the week, month, quarter and first half of the year. For the month of June, the S&P and Nasdaq both added about 6.5%, and the Dow's 4.6% gain was the best showing since November. For the first six months of 2023, the Nasdaq grew a record 31.7% higher for its best first half since 1983, and the S&P soared 15.9% for its best first half since 2019, while the Dow added a more modest 3.8%.

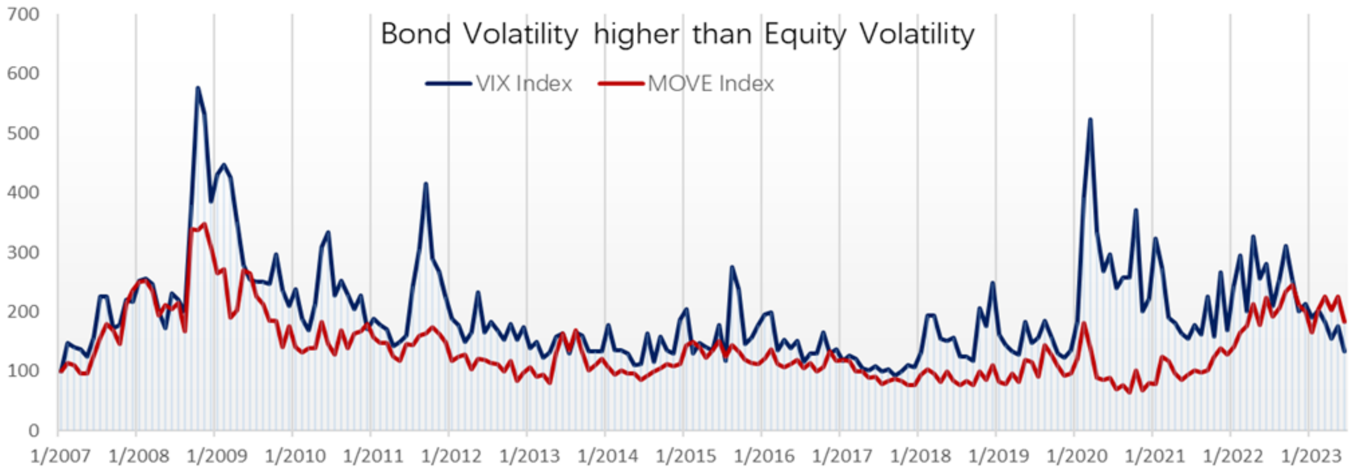
Federal Reserve policymakers have put their interest rate hiking cycle on pause, leaving their target for short-term interest rates at a range of 5.00%–5.25%, but they have more work to do to lower inflation to acceptable level. On the labour market front, the signals were mixed with average hourly earnings growth of 0.3% in May and 4.3% year-on-year being higher than the Fed's comfort level.

In Europe and especially UK, inflation has been stickier than expected, with expectations for both headline and core inflation to fall as more restrictive monetary policy takes hold. The risk is still with the core inflation to stay higher, and this is true for other major regions, as well.

In China, recovery is losing its steam after a strong first quarter driven by the economy's reopening after COVID-19-related lockdowns, many downgrading their forecasts for full-year economic growth in China to 5.5%–6.0%.

Bonds provided stability despite a quarter of significant volatility. The Bloomberg U.S. Aggregate Bond Index finished in the black for the last three and six months. Corporate investment-grade and high-yield credit produced the highest returns in the first quarter, but at the cost at an increased volatility.

The ICE BofA MOVE Index tracks volatility in the (high yield) bond market and returns from levels last seen during the 2008 G.F.C. and above equity volatility (CBOE Volatility Index, or VIX, tracks equity volatility).




Sources: Bloomberg, New Dimensions Capital, as of 30th June 2023.

Looking forward:

- If last month we were supporting the upside surprise, and to a certain extent we were right, we are currently looking to diversify our risk through our equity allocations. Regionally, US is still supported by good macro indicators and earnings expectations, but earnings season picks up again and we see volatility ahead.
- After a sensational half year, technology stocks may look for a pause and indicate profit taking by the first entrants in these trades. We expect flows to prove such adjustments, and precede a move into lagging sectors like Industrials, Consumer Staples together with a fading momentum in global equities.

## Investment Views

Recent data show a slightly less positive trend in economic activity in the United States, the Euro area, and also in China, whose post Covid recovery remains modest. Only the United Kingdom is outperforming expectations. That said, the figures remain broadly consistent with the continued modest growth scenario.

Inflation has continued to come down rapidly, in line with producer prices, but underlying inflation is proving more stubborn against a backdrop of still solid labour markets. Central bank policy tightening now seems to be nearing its end. Risks of fresh turbulence continues to run high ahead of potential interest rate hikes and increased geopolitical pressures. These risks argue for broad diversification, with bonds once again playing a protective role in case equity markets fall. For equity only investment vehicles, diversification into defensive sectors may pay better than compared to the beginning of the year. Signs of investment interest in quality and low volatility sectors are becoming more obvious.

In Asia, S&P indices showed a strong performance, with the Pan Asian BMI advancing 3.4% for the month, and 6.3% for the year. Japan was the largest contributor to the regional benchmark, while sector wise, only Healthcare finished in red.

| Jun-23 | GLOBAL GROWTH | APAC GROWTH | GLOBAL QUALITY | APAC QUALITY | GLOBAL MINVOL | APAC MINVOL | Global IG 1-3Y | Global IG 3-5Y | GLOBAL HY | GLOBAL YIELD |
|---|---|---|---|---|---|---|---|---|---|---|
| | EQUITIES | | | | | | BONDS | | | EQUITIES |
| 1 MONTH | 4.71% | 4.55% | 4.34% | 2.98% | 2.20% | 1.10% | -0.16% | -0.69% | 2.21% | 4.06% |
| 1 QUARTER | 8.94% | 7.85% | 8.39% | 0.91% | 0.75% | 1.61% | 0.30% | -0.57% | 1.68% | 1.24% |
| 1 YEAR | 24.67% | 21.53% | 22.57% | 6.20% | 5.85% | 5.09% | 1.76% | -1.52% | 10.13% | 7.17% |
| 3 YEARS | 35.21% | 29.94% | 41.29% | 5.78% | 17.29% | 3.97% | -0.13% | -8.37% | 3.79% | 30.78% |
| 5 YEARS | 72.27% | 62.32% | 79.78% | 21.47% | 31.73% | -1.07% | 7.03% | -3.62% | 9.63% | 33.77% |
| 10 YEARS | 204.82% | 180.43% | 219.66% | 89.43% | 109.10% | 41.23% | 14.00% | 1.87% | 40.93% | 88.57% |

Source: New Dimensions Capital, Bloomberg.

In terms of factor performance, all equity factors stayed in the positive territory. The weakest was Min Volatility in APAC, while Growth kept strong and doubled returns for the rolling quarter.

In APAC, investors returned to Quality and reversed the negative performance earlier in the quarter, when Growth and Technology names attracted all interest. Quality names (mainly characterised by low debt, stable earnings, higher ROE) made June 2023 a successful month. In Singapore, Daiwa House Logistics Trust or Yangzi Jiang Shipbuilding, names with ROE and cash levels above sector average, have outperformed in June almost 3 times the previous two months together. Similarly, Boston Properties in US, an office REIT with ROE = 10.5%, Debt/Assets = 13.9% and solid cashflow levels ended June at +16% after it drew down half of that in the previous two months.

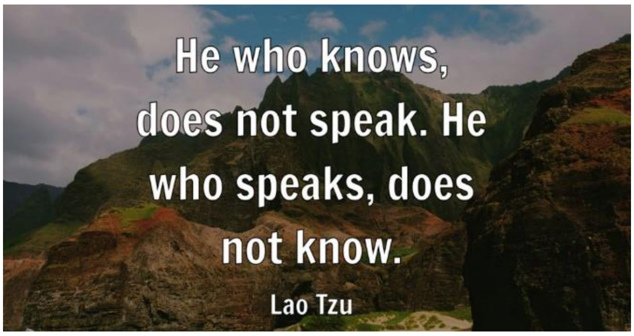
The voices predicting US recession seem to fade into horizon, together with their bewildered drivers. Economic growth and corporate earnings have so far proven sturdier than expected, as the drawdown of excess savings, resilient asset prices, and a strong labour market have supported consumer spending.

We are still cautious on global equities, with a selective interest in sectors that will be driven up as alternatives to the tech sector unwinding. As the 12-months forward P/E for the S&P493 (excluding the surging seven - Apple, Microsoft, Nvidia, Amazon, Meta, Tesla, and Alphabet) is still around 15x, we would rebalance our portfolios targeting lagging sectors like Industrials, Consumer Staples or slowly reviving Real Estate and Banks (but very selectively for these).

NEW DIMENSIONS CAPITAL

## New Dimensions Capital – About Us

We transformed the quote by Lao Tzu and stand by it: " Those who know, do not predict. Those who predict, do not know."




The best we can do in this fickle business of investing is to weigh the evidence thoroughly, evaluate multiple outcomes and set respective priorities, be humble and appreciative, and leave predictions to those whose job is to engage rather than understand.

As we approach the second half of 2023, markets look like pricing a benign path forward based on implied volatilities standing at lowest levels since the pandemic, while S&P500 is up 20% since last October 's low. We think this is not the time for predictions but of serious preparations for a stormy regime ahead – recession, market consolidation, wars, derailing financial system … are all possible outcomes.

All investors face a balancing act. There is a path upwards for equities, but it is narrow and bumpy, while the unknowns in all asset classes can morph swiftly in real risks. A.I. resources have dealt with it to a certain extent and will continue to improve our understanding of unknown risks, but we all know that such risks spread and mutate together with the amount of data that is behind the machines dealing with it.

We work to improve our knowledge first and persistently provide better outcomes through our investments.



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