



NCM Core Global/Core International
Equity Strategies
 NCM Monthly Commentary for July 2024



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Cumberland Investment Counsel Inc., affiliate of NCM Asset Management Ltd.

Q2 2024 Review

After delivering robust returns during the first quarter, global equity markets continued their upward climb during the second quarter of 2024. Some of the key factors driving the returns included strong corporate earnings, reduced fears about a global economic recession, and enthusiasm over artificial intelligence that powered massive gains in Technology stocks. Given this backdrop, stock market returns during Q2 2024 were positive on a total return basis across major developed market regions as seen in Chart 1 below.

CHART 1

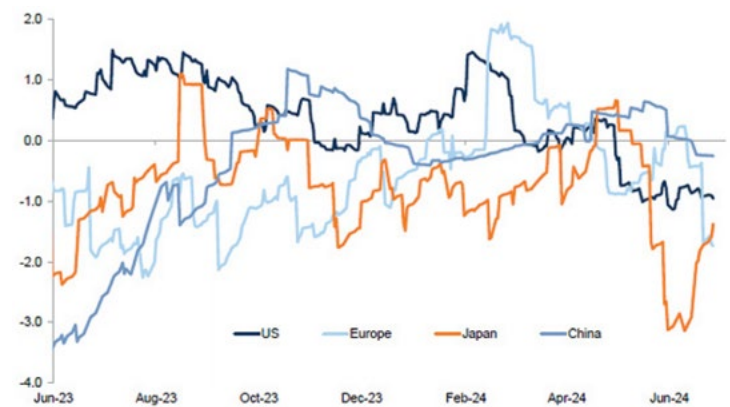
Index	Geog. Region	Currency	Price change	Total return with dividends
MSCI World	Global	US\$	8.4%	9.0%
S&P 500	US	US\$	10.2%	10.6%
Stoxx Europe 600	Europe	Euro	7.0%	7.9%
Tokyo Stock Price Index	Japan	Yen	16.2%	17.3%

While the strength in global equity markets can be attributed to many factors, the increasing likelihood of an economic soft landing and the hype around artificial intelligence are the key driving forces. Any disappointments on those fronts could lead to a period of elevated volatility for equities. In terms of the economy, Macroeconomic Surprise indexes turned negative during the month of June for major economies around the world as seen in Chart 2 on the right.

This phenomenon was particularly pronounced in the US, where the Bloomberg US Economic Surprise Index for the month of June reached its lowest level in over a year as seen in Chart 3 on the right.

CHART 2

Exhibit 5: Macro surprises have turned negative
 Macro surprises (MAP), Europe = 75% Euro Area + 25% UK



Source: Goldman Sachs Global Investment Research

CHART 3



If this trend were to continue for several months, it would be worrisome. From our perspective, the reason the U.S. Surprise Index turned negative is because consensus has been revising their numbers upwards over the last several months as fears of a recession have dissipated. As a result of these upward revisions, the expectations bar has been set higher and now we find ourselves in a situation where

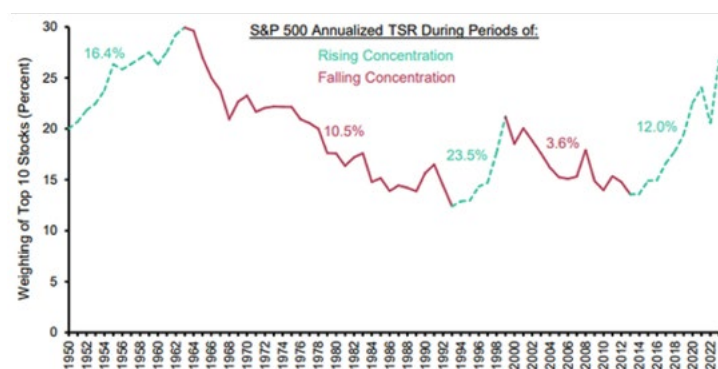
the economic data has come in below this higher bar. It's too early to be concerned because one month does not make a trend, although this is something we will be monitoring. In our view, what's really happening is that the economy is slowing not shrinking. The latest GDPNow figure from the Federal Reserve Bank of Atlanta estimates that real GDP growth in the second quarter of 2024 was 1.7%. This is a decline from their previous estimate of 2.2% given on June 28. While GDPNow is not an official forecast of the Atlanta Fed, it is a running estimate of real GDP growth based on available economic data for the current measured quarter. From our perspective, a slowdown in the economy strengthens the case for interest rate cuts in the U.S. and that's a good thing as it would help stimulate the economy.

In terms of Technology stocks, they have captured the attention of investors given the outsized returns being generated. These stocks have also received attention because of their growing influence in the S&P 500 index in terms of the weight they make up in the index. On a year-to-date basis through June 30, Nvidia alone has contributed 30% of the gain generated by the S&P 500. In addition, Microsoft, Amazon, Alphabet, Meta, and Apple have collectively generated more than 30% of the gain in the S&P 500 during the first half of the year. When you add it all up, 6 companies have generated more than 60% of the upside in the S&P 500 for the first six months of 2024. Said another way, the breadth in the U.S. stock market is narrow. If the outlook for these companies deteriorates, it would place a very large burden on the remaining companies in the index. The largest stocks in the index have not only driven the lion's share of stock market returns, but these Tech behemoths also make up a huge percentage of the S&P 500 index. The concern about market concentration is easy to see when you consider that the top 10 stocks in the S&P 500 (by market capitalization) accounted for 14% of the index a decade ago, 27% at the end of 2023, and 37% of the index as of June 24, 2024. While investors usually think of elevated concentration as a sign of downside risk, the S&P 500 rallied more often than it declined during the 12 months following past episodes of peak concentration. By examining S&P 500 market cap concentrations over the past century, Goldman Sachs Research identified 7 episodes in which the 10 largest stocks exhibited extreme concentration. In most of these periods, stocks continued to rally after reaching peak concentration. The most recent episodes occurred in 2009 and 2020, with both periods coinciding with sharp improvements in the macroeconomic outlook. In 1932, peak concentration marked the bottom of a major economic downturn (not a market top) and the stock market boomed in the aftermath of this downturn.

A separate study on market concentration reinforces the notion that periods of high market concentration are not to be feared. The recently published report was written by Morgan Stanley Investment Management. The results of their study show that since 1950, the S&P 500 has delivered above-average returns in periods when concentration was rising and below-average returns when concentration was falling. This can be seen in Chart 4 below.

CHART 4

Exhibit 9: S&P 500 Annual Returns During Rising and Falling Concentration 1950-2023



Source: FactSet and Counterpoint Global.

Portfolio Review

During the second quarter, we established several new positions in our Global and International portfolios. In our Global strategy, we established new positions in ASML, Broadcom, and Wolters Kluwer. In the International strategy, we initiated new positions in Arch Capital and Tokyo Electron. A brief description of each new holding can be found in the **Appendix**.

Outlook for 2024

In terms of our outlook, we continue to have a cautiously optimistic view. First, the global economy continues to show signs of resilience and concerns about an economic recession have dissipated. Second, inflation has fallen enough to set the stage for interest rate cuts from central banks around the world. This process is already underway with recent interest rate cuts from the Bank of Canada, the European Central Bank, and the Swiss National Bank. Third, corporate earnings have been steady and have surprised to the upside in many markets around the world. For all these reasons, we continue to have a favourable outlook for global equity markets.

We continue to focus on companies with strong fundamentals, competitive advantages, and exposure to secular growth themes. Some of these themes include artificial intelligence, electrification of global infrastructure, decarbonization of the global economy, and healthcare innovation. We own several companies across our portfolios that are well positioned to benefit from these structural trends.

In terms of the risks, we would highlight geopolitics, an above average valuation in the U.S. stock market, and the likelihood of volatility as we approach the U.S. Presidential Election in the fall. In terms of valuations, the U.S. stock market is heavily skewed by the Magnificent Seven and other Technology stocks. We would argue that many of the large Technology stocks deserve to trade at above average valuations given their attractive growth profiles, their robust free cash flow generation, and their pristine balance sheets. On a historical

basis, the lead up to U.S. Presidential Elections has been associated with elevated volatility in the stock market. Therefore, we would not be surprised to see a stock market pullback or a correction in the months ahead. Having said that, the stock market has typically delivered attractive gains in the months following the U.S. Presidential Election. Overall, we believe the risk-reward profile for the stock market is well balanced and we remain cautiously optimistic as the second half of the year gets underway.

APPENDIX A

Company descriptions for new positions added to the Global Strategy

ASML

Spun out of Dutch electronics giant Philips in 1995, ASML has grown to become the dominant player in one of the critical steps in the production of semiconductors – lithography. The process of using light to trace integrated circuits onto silicon wafers, it is lithography that determines how small the features on a chip can be, and how densely manufacturers can pack transistors together. Today, the most advanced form of lithography technology is ‘extreme ultraviolet’ (EUV). EUV light has a wavelength 14 times shorter than deep ultraviolet (DUV) light, the previously most advanced technology used in lithography. To date, only one company in the world has mastered EUV lithography and that company is ASML. This puts the company in a virtual monopoly position for EUV technology. Demand for semiconductor chips looks set to grow with artificial intelligence, the electrification of vehicles, 5G technology, and the Internet of Things. Given its leadership position, we believe that ASML is very well positioned to benefit from these trends in the years ahead.

Broadcom

Broadcom is a global technology leader that designs, develops, and supplies a broad range of semiconductor and infrastructure software solutions. Its semiconductor solutions focus on complex digital, mixed signal, and analog products across a variety of end-markets. The company’s software products help customers plan, develop, automate, manage, and secure applications across various platforms. Historically, Broadcom’s semiconductor business has been a market-leading franchise with high margins and market-level growth, but the emergence of Artificial Intelligence (AI) related demand has spurred stronger growth across its portfolio, specifically in its Networking business unit. Broadcom’s AI-related revenue has grown from less than 5% of its semiconductor business to more than 30% during 2024 driven by the robust growth in its industry-leading Ethernet switch silicon business and its custom silicon solutions.

Wolters Kluwer

With roots dating back to 1836, Wolters Kluwer is a global leader in professional information, software solutions, and services in the following sectors: health, tax & accounting, financial corporate compliance, and legal & regulatory. Over the last 2 decades the company has reorganized its business, going from the leading print publisher of professional information materials to being one of the largest players in the potentially much larger digital information services industry. One of the keys to the success of Wolters Kluwer is the mission critical nature of its offering. The company provides ‘must have’ solutions across several different industries including accounting, medical, and legal. The mission critical nature of its product offering has allowed the company to develop long-term customer relationships and a highly recurring revenue base which accounts for approximately 80% of total sales. The company is also a beneficiary of ongoing improvements in artificial intelligence. The company began deploying AI into its data and information services in 2017 and today it uses AI in about 50% of its digital products.

APPENDIX B

Company descriptions for new positions added to the International Strategy

Arch Capital

Arch Capital Group is a specialty Property & Casualty insurance company that operates in the insurance, reinsurance, and mortgage insurance markets. The company initially focused on casualty lines but in 2001 Arch installed a new management team that expanded its solutions into the global insurance and reinsurance markets. Over time, and primarily through acquisitions, the company also built a significant mortgage insurance business. Arch has consistently generated industry-leading underwriting margins in the re/insurance business and is known for being nimble and opportunistic when it comes to pivoting its business mix. The pricing environment and the competitive trends in various product lines are the key factors that help determine where management should allocate its capital. Arch Capital has a long history of world-

class management execution, proving itself as an exceptional capital allocator across insurance cycles and with a strong underwriting discipline over many years.

Tokyo Electron

Tokyo Electron is a leading semiconductor production equipment (SPE) company and is a top 5 SPE company globally. The company has strong market share in the areas of coater/developer, etching, deposition, and cleaning equipment. Tokyo Electron is especially dominant in both the etching and deposition segments of the semiconductor equipment industry. Deposition equipment applies thin-film coatings to surfaces while etching selectively removes material. The combination of these two segments is critical during the chip fabrication process along with lithography, which produces the mask that exposes areas for materials to be deposited or removed. Tokyo Electron's dominant position as a key equipment vendor creates scale advantages that fuel research and development spending at levels that very few competitors can match. Over the next 5 years, Tokyo Electron is expected to nearly double its spending on Research & Development (R&D) to approximately US\$10 billion. The company is also planning to expand its workforce by 10,000 people. The increased spending on R&D will allow the company to pursue secular growth opportunities in artificial intelligence, electrification, and 5G technology.

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