2024 Outlook: Global Equities

By: Manas Gautam | December 12, 2023

Keep Calm & Carry On

KEY POINTS

1. We remain focused on company-specific fundamentals. While market conditions and macro events change year-to-year, company fundamentals drive share price appreciation over the long-term, which, across portfolio holdings, have largely remained healthy and in-line with our expectations.

2. We believe our companies are poised for growth. Many companies that suffered sharp declines in their share prices last year made the most of this slump by refocusing on the best opportunities and achieving profitability faster. In our view, these businesses have essentially de-risked themselves — and yet these improvements are not reflected in their current share prices.

3. We continue to assess the long-term implications of a higher cost of capital. We believe many companies that did not build sustainable businesses will start to run out of cash, thus reducing competition and benefiting companies that have already established valuable businesses and brands.

What We Are Seeing:

High yields have driven record inflows into money market funds. As investors crowd into money market funds while outflows from equities steepen, it seems the whole world has become content with earning the ~5% yield that Treasurys provide. But as history and human behavior have shown, envy and fear of missing out will inevitably creep back into the minds of market participants, who will start searching elsewhere for higher returns.

We believe our companies are poised for growth. Many of our companies that suffered sharp declines in their share prices last year made the most of this slump by refocusing on the best opportunities and achieving profitability faster. These companies are now starting to witness the fruits of their hard labor, are poised for growth, and more focused on execution than ever. In our view, these businesses have essentially de-risked themselves — and yet these improvements are not reflected in their current share prices.

Opportunistic buying of debt has been a common theme. Several of our companies bought back their debt for cents on the dollar given the selloff of their bonds. This is a transfer of wealth to equity holders and not only deleverages our companies but is akin to share repurchases at attractive prices (which we also love!).

Share price volatility, especially in the small and mid-cap space has been excessive. Several companies witnessed a 20-30% drawdown on the back of a single quarter's earnings release. As business owners, we believe true intrinsic value does not change that much quarter to quarter. However, guidance-obsessed market participants seem to be selling first and asking questions later.

Concerns over mega-cap mania. Given just a few companies are driving the majority of index returns year-to-date (the Magnificent 7), we worry about a new Nifty-Fifty era where market participants continue buying "safe," high quality stocks at any price. Market-cap-weighted indexes are great, until they aren't — especially when a handful of companies surge to new heights and increase concentration risks. Furthermore, index flows, driving performance, driving flows make prospective returns weaker. This reflexive dynamic weakens the system, yet this weakness does not seem apparent to investors at the moment.

What We Are Doing:

We maintain our belief that equities will be the best-performing asset class over the long-term. Equities provide ownership in the creativity, ingenuity, and productivity of hundreds of thousands of talented workers. While money can be inflated, talent cannot.

We remain highly invested alongside clients. We continue to allocate a significant portion of our deferred compensation into the portfolios we manage.

Recent market volatility has created buying opportunities. Higher interest rates and an increased cost of living continue to put pressure on the consumer. As a result, we have observed significant drawdowns in some consumer-oriented businesses and have taken advantage of the volatility to invest in some of these companies at compelling prices. We believe these companies provide a strong consumer value proposition and are resilient businesses whose value is not reflected in their current prices.

We remain focused on company-specific fundamentals. While market conditions and macro events change year to year, company fundamentals drive share price appreciation over the long-term, which, across portfolio holdings, have largely remained healthy and in-line with our expectations.

We continue to be objective and holistic in understanding the opportunities and challenges that each of our companies face. Questions we ask ourselves range from how big can the business become in the next 3-5 years, to what are its scale advantages and unit economics, what are management's motivations, and can the business provide a strong consumer value proposition while generating cash flow.

We continue build trusted relationships with management teams. We aim to provide constructive, strategic, and tactical advice as they navigate the current macroeconomic backdrop.

What We Are Watching:

Public versus private markets. Asset classes that don't have daily marks did not experience the pain or drawdown that public markets witnessed in 2022. However, higher interest rates should impact all asset classes and we believe, in some cases, the high valuations of private assets do not reflect fair value of what these companies would actually trade for.

Long-term implications of high borrowing costs. The lack of successful public IPOs and general shortage of deal volume again this year leads us to believe public markets — the largest pool of capital — are closed. Given the high cost of borrowing, we believe many companies that did not build sustainable businesses will start to run out of cash thus reducing competition and benefiting companies that have already established valuable businesses and brands.

Green shoots of a new business cycle are emerging. We are starting to see green shoots of a new business cycle, which we believe will push our companies into offense mode versus playing defense. We hope to get our fair share of success and create long-term value for our clients when our companies begin to reap the benefits of the wind on their back.

***Risk Considerations**: There is no assurance that a strategy will achieve its investment objective. Portfolios are subject to market risk, which is the possibility that the market values of securities owned by the portfolio will decline. Market values can change daily due to economic and other events (e.g. natural disasters, health crises, terrorism, conflicts and social unrest) that affect markets, countries, companies or governments. It is difficult to predict the timing, duration, and potential adverse effects (e.g. portfolio liquidity) of events. Accordingly, you can lose money investing in this strategy. Please be aware that this strategy may be subject to certain additional risks. In general, equity securities' values also fluctuate in response to activities specific to a company. Investments in foreign markets entail special risks such as currency, political, economic, and market risks. The risks of investing in emerging market countries are greater than the risks generally associated with investments in foreign developed countries. Illiquid securities may be more difficult to sell and value than publicly traded securities (liquidity risk). Investments in small- and medium- capitalization companies tend to be more volatile and less liquid than those of larger, more established, companies. Derivative instruments may disproportionately increase losses and have a significant impact on performance. They also may be subject to counterparty, liquidity, valuation, correlation and market risks. Privately placed and restricted securities may be subject to resale restrictions as well as a lack of publicly available information, which will increase their illiquidity and could adversely affect the ability to value and sell them (liquidity risk).*

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Marketing Communication