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# Stay Calm – Stay Invested

The current equity market volatility during the summer of 2024 has attracted plenty of attention and expert conjecture. We don't claim to have any better interpretation of the daily gyrations other than to observe that if the equity markets are a weighing machine over the longer term and a voting machine in the shorter term, market participants have been active at the poll stations.

*"Avoiding the worst days is appealing – however, catching the good days in the stock market is crucial, and they often tend to follow close behind the worst days."*

Our firm has been managing client monies for over three decades with a long-term stock-picking approach supported by structural trends and themes. Over that time, we have witnessed plenty of market turbulence and several market downturns, which can last days, weeks, months, and sometimes beyond. It is relevant to remember that market downturns and corrections are a very normal part of being invested.

## Time in the market versus market timing

While the concept of "time in the market vs market timing" is of limited comfort in the eye of the volatility storm, our firm belief is that it is critical for a long-term investor to stay invested. Otherwise, you risk missing out on the few days in the market when the rises come – sometimes out of the blue. Avoiding the worst days is, of course, appealing – however, catching the good days in the stock market is crucial, and they often tend to follow close

***Bo Knudsen***
***CEO and Portfolio Manager***
*C WorldWide Asset Management*

behind the worst days. For example, five of the best days in the US stock market (S&P 500) in the last 50 years were in the autumn of 2008, when there was great uncertainty due to the Lehman Brothers' bankruptcy. Managing a strategy that attempts to be "nimble" and predict when corrections will happen is not where we strive to add value. We do not believe that this is a repeatable path to investment success.

That being said, the current stock market environment also opens up good opportunities. Still, our responsibility remains the same, and that is to continuously review portfolio exposures and analysing whether we have the right stocks and the right long-term weightings. We have a strong bench of candidates that can come into play when relevant. We invest in quality companies and business models with a strong pedigree and sustainable growth track records.

What has served us well during times like these is to step back from the daily headline noise, reflect, and ask ourselves the following; is this a market adjustment or a seismic change, indicating a market regime change and shift in leadership?

## What caused this?

Oftentimes, when market volatility rises sharply, it can be explained by a single factor. On this occasion, though, several contributory factors have conspired to the current situation.

It has been well documented that we have witnessed an extreme market concentration driving returns. This has been concentrated in AI-related companies but also in other parts of the global market, such as weight loss drugs and Japanese value stocks.

While interest rates have been high and financial conditions tight in most of the developed world, Japan held on to its ultra-loose monetary policy. This led to a rapidly depreciating currency, which encouraged a large leverage trade whereby investors borrowed at zero in a depreciating Japanese Yen and invested in the narrow stock market leadership discussed above.

*"What has served us well during times like these is to step back from the daily headline noise, reflect, and ask ourselves some key questions."*

We think that three things happened to unhinge this. Firstly, investors began to question the near-term payoff from the large AI investments, resulting in some profit-taking in technology stocks. Secondly, the Bank of Japan increased interest rates, causing the Yen to appreciate and forcing investors to deleverage. Thirdly, a weaker-than-expected US jobs report led to concerns that a recession was imminent if not current and the Federal Reserve would need to cut interest rates more aggressively than anticipated. This weakened the US Dollar and further strengthened the Japanese Yen, exacerbating the carry trade unwind.

## Is this a market adjustment or a shift in leadership?

It is unlikely that we will see more interest rate rises – rather the opposite. A lower interest rate environment will benefit many of the quality growth stocks in our portfolios – companies with solid earnings expectations in future years. For example, as described in our insight "Compounding Earnings through Sustainable Growth" certain consumer staples companies have been challenged by the high interest rate environment, and those companies will, all else being equal, face a brighter future with lower interest rates.

In our portfolios, we remain exposed to the "Productive and Digital Society", a theme that we have been invested in for many years and believe will continue. In terms of AI developments, they will be more evolutionary rather than revolutionary from here. We have yet to see the vast amounts of money that companies worldwide are investing in AI translate into new growth areas and "killer apps" that are innovative enough to trigger new significant investments. There is nothing to suggest that AI does not have the potential to create technological breakthroughs that we can barely imagine. However, as we described in our insight "Showcasing AI Portfolio Exposure", the specific achievements and timing are hard to predict.

But we are convinced that AI will change and improve the world in many ways, and in our portfolios, we are exposed to just that. Especially in AI infrastructure and semiconductor equipment for chip production, which we find particularly compelling.

We have invested in the AI theme without trying to find the next GitHub or the next "killer app". We have effectively worked with picks and shovels, and we have been assured that all the companies in our portfolios that are investing in picks and shovels will continue their investments.

Two other themes that will continue with undiminished vigour are the energy transition and supply chain repatriation, which will drive the need for advanced manufacturing. Even with the uncertainty surrounding the outcome of the US presidential election, these are unavoidable themes, and our strategies are well positioned towards them.

## The long game – stay invested

We maintain a slightly distanced relationship to the current situation. We do not participate in the daily battle of views in the stock market. We leave that to the speculators. For us, the long game isn't debatable. Where we choose to place our focus dictates how we invest. This means we are sticking to the long term.

Our investment mindset is anchored by an unwavering belief in thinking rationally and strategically about the future and investing accordingly. Simple, perhaps, but in our view, both effective and repeatable.

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## Disclaimers



C WORLDWIDE ASSET MANAGEMENT FONDSMAEGLERSELSKAB A/S

Dampfaergevej 26 · DK-2100 Copenhagen

Tel: +45 35 46 35 00 · Fax: +45 35 46 36 00 · VAT 78 42 05 10 · cworldwide.com

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