Week in review

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In this week's update, Kevin Quinn discusses:

- The rise in concentration risk as a small number of stocks continue to drive the market
- US purchasing manager indices show business expansion
- Election polls in France and the US
- Inflation data from Japan, Australia and Canada
- How the US dollar rose while Yen continued to tumble
- NVIDIA's tumble as artificial intelligence (AI) stocks fell
- German business confidence dropped

Latest update from markets (to 27.06.24)

	1 week	YTD
Global shares	+0.1%	15.0%
US shares	+0.2%	19.6%
European shares	-1.2%	9.8%
European government bonds	-0.3%	-1,7%
Global commodities	-1.4%	6.1%
Magnificent 7*	+2.8%	43.6%

Source: Bloomberg, 28.06.24. All returns expressed in euros.

*Apple, Alphabet, Amazon, Meta, Microsoft, NVIDIA, and Tesla.

The long and short

Investing requires a long-term focus but shorter term events can take most of our attention. In this series of updates, we place current events into a longer term perspective.

The long…

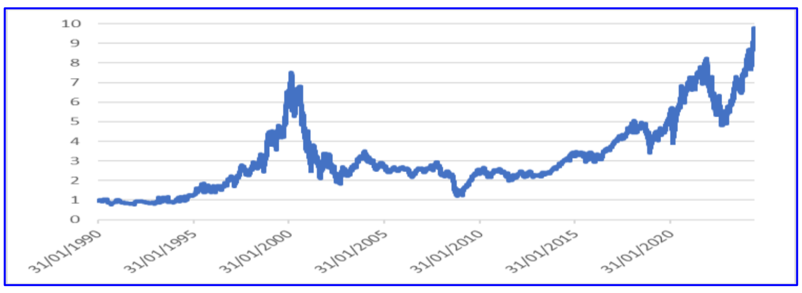
Concentration risk rising

Behind the headlines of the continued strength in equity markets lies one very prominent story - the Magnificent 7*. As was the case in 2023, the Magnificent 7 has continued to be a dominant theme this year.
- This handful of large-cap technology stocks have delivered growth of 44%[1] so far in H1 2024.
- They now make up approximately 20% of the global stock market and close to 30% of the US stock market.[2]

Is a bubble approaching?

These companies are at the centre of the AI phenomenon. While the demand for all things AI continues and companies can scarcely keep up with the demand, there are signs that gains made are now reaching 'bubble' proportions. For example, the price to sales ratio[3], for the US S&P technology sector has now reached levels in excess of those reached during the technology bubble of 2000 (see Figure 1).

Figure 1: S&P Technology sector price-sales ratio since 1990 to June 2024



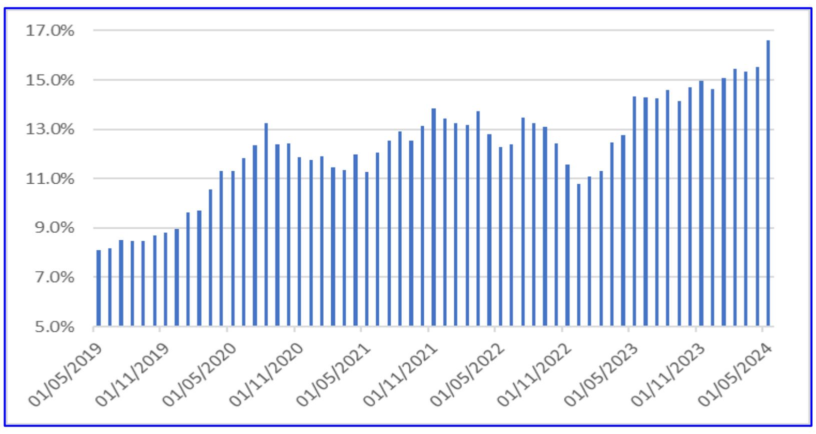
Source: Bloomberg 25.06.24.

The strong performance of these large US tech firms continued into June, though it did falter. This was driven mainly by the AI leader, NVIDIA, seeing a fall of 16% at one point in its share price during the month[1]. It has partially recovered since then.

Before calling the end of the boom in all things AI it's worth bearing in mind that a drop of this kind has happened on many occasions over the last 12 months. What may be different this time is that company valuation levels are now quite stretched (these are expensive stocks!) and it is hard to see too much more headroom for gains in the near-term. What's more likely is share price moves of the kind witnessed for NVIDIA.

Key learning

Figure 2: % of global markets made up of top 5 companies



Source: BOI Investment Markets/Bloomberg 26.06.24

The key learning from this is that "concentration risk" is rising. Five years ago, May 2019, approximately 8 cents of every euro invested in global stock markets would have been invested in the top five companies. By May 2024, that has grown to 16 cents of every euro. The top five companies in the world today have effectively doubled their presence in global stock markets (see Figure 2). It may be time for new leaders to emerge as dominance like this tends not to persist indefinitely.

1. Source: BOI Investment Markets/Bloomberg, calculated from 31.12.23 to 28.06.24
2. Source: BOI Investment Markets/Bloomberg 26.06.24
3. Price-sales ratio compares the share price to sales per share

The short…

Market news

US Purchasing Manager Index (PMI) – PMIs are a measure of economic activity. The US composite PMI rose to 54.6 for June, another expansionary reading and its highest since April 2022.

French election polls – Marie Le Pen's Far Right Rallé National party continues to makes gains, with support rising to approx.34% earlier this week. President Macron's Renaissance Party and its allies trail in third place at approx.21%. The fear about this outcome is being reflected in French government bonds, with investors demanding a higher premium to hold.

US election – President Biden took a tiny lead, of just 0.1%, over former President Trump in a poll of polls calculated on 24.06.24. The first presidential debate took place on 27.06.24 and the general view is that President Biden performed poorly which may result in former President Trump resuming a lead in the polls.

Inflation data – Japanese inflation expectations, as measured by the 10-year breakeven rate, reached levels not seen in 20 years (approx.1.6% per annum). Australia showed inflation rising by 4% year-on-year (y/y), while Canada's inflation rose to 2.9% y/y. Both were higher than expected, giving further evidence about how sticky inflation is proving.

The US dollar rose to its highest level since November 2023 this week, with market speculation shifting to a view that the US Federal Reserve could leave interest rates higher for longer than other major central banks, giving investors an incentive to move cash towards higher earning US bonds. Notably, the yen has fallen in value against the dollar to levels not seen since 1986, and is now down 12% this year alone.

NVIDIA's share price drop - the stock fell by 16% at one point during the week. The fall was a reminder to investors of just how highly valued the company had become, as some investors cashed in on gains. The AI sector, in general, had a negative week. Another example later in the week was Micron Technology, a semi-conductor company that develops memory and storage solutions. Its shares fell by, at one point, 11% on 26.06.24 as its earnings forecast fell short of market expectations. A reminder to investors of the risks now apparent in AI (see the Long) .

US labour market - has shown signs of recent weakening as the job-openings to unemployed ratio has now returned to pre-pandemic levels for the first time. A further deterioration would cause unemployment to rise

German business confidence - a recent survey showed a decline in business sentiment in June having improved for the prior three months. While sentiment in the services sector was positive, manufacturing has again declined.

Source: Bloomberg 26.06.24-28.06.24, BCA research 27.06.24

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Table 1: 5 year historic performances

	2019	2020	2021	2022	2023
Global equities	29.0%	6.7%	27.5%	-13.0%	18.1%
US equities (S&P 500)	33.9%	8.7%	38.2%	-13.0%	22.2%
European equities (Stoxx 600)	28.0%	-1.4%	25.8%	-9.9%	16.6%
Emerging market equities	21.8%	9.1%	4.9%	-14.9%	6.6%
Global bonds	5.4%	4.9%	-2.6%	-15.1%	4.5%
US government bonds	11.4%	8.3%	-2.0%	-12.5%	5.8%
European government bonds	6.9%	4.3%	-3.7%	-18.4%	7.2%
Emerging market debt	14.5%	-3.4%	6.4%	-9.8%	5.4%
Broad commodities	7.9%	-13.1%	37.0%	20.7%	-10.9%
US corporate bonds	11.2%	7.8%	-1.9%	-17.1%	5.8%
European corporate bonds	6.3%	2.4%	-1.2%	-14.0%	8.4%
French government bond aggregate	5.4%	4.5%	-4.1%	-19.0%	6.5%
German government bond aggregat	3.0%	3.0%	-2.7%	-17.8%	5.6%
NVIDIA	80.5%	104.2%	142.1%	-47.1%	228.2%
Magnificent 7	57.7%	102.2%	62.7%	-41.9%	100.4%
Micron Technologies	72.9%	28.4%	33.4%	-42.5%	66.4%

Source: Bloomberg 27.06.24. All returns expressed in euros.

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