RATHBONES

THIS RALLY IS BROADENING…

REVIEW OF THE WEEK
2 APRIL 2024

A RESILIENT ECONOMY IS GIVING INVESTORS INCREASED CONFIDENCE TO MOVE BEYOND THE MAGNIFICENT SEVEN AND INTO CORNERS OF THE MARKET THAT HAVE LAGGED. THIS BROADENING TREND IS VERY ENCOURAGING.

Stocks are closing out a record-strewn quarter. In the US, the benchmark S&P 500 is up 10% this year, marking its biggest first-quarter gain since 2019. The S&P 500 hit its first record high in two years in late January and it hasn't looked back since. It's now set more than a dozen new highs without any sizeable pullbacks so far this year as corporate earnings hold up, enthusiasm around artificial intelligence keeps building, the US economy motors ahead and the US Federal Reserve (Fed) reinforces its willingness to cut interest rates this year.

Wall Street's rally is nothing new: March marked the S&P 500's fifth positive month in a row and it's gained more than 25% over that period. What's much more encouraging are the signs that the rally driven by the Magnificent Seven mega-sized US technology firms is broadening out to include sectors beyond tech, smaller and medium-sized stocks and several global indices. (Indeed, Japan's TOPIX index notched up stronger gains than any of its global counterparts in the first quarter, while Europe's region-wide Stoxx 600 also roared ahead.)

Is the Magnificent Seven's wild ride finally over?
For most of 2023, an unusually small number of stocks drove the gains of the entire US index and most underperformed. But more and more companies are participating in this year's rising markets. The performance of the Seven (Apple, Microsoft, Alphabet, Amazon, Nvidia, Meta and Tesla) has been much closer to that of other large firms, as well as the returns of smaller and medium-sized US companies.

Moreover, the Seven finally seem to have stopped charging as a pack. Three have turned from leaders to laggards and that trio includes Tesla whose near 30% decline this year wins it the dubious accolade of the worst-performing company included on the S&P 500. The remaining four have all beaten the index, but by hugely differing amounts.

What does this tell us?
First, it suggests that investors may be starting to recognise that the Seven aren't really a particularly homogenous grouping. As we explained in the **January edition of our Investment Insights magazine**, they share a common thread – dominance in tech which many investors believed would ensure they'd prove the biggest winners from advances in AI. But each of the Seven's businesses has unique and differing drivers. What does AI chipmaker Nvidia really have in common with a luxury consumer electronics company like Apple? And how similar is the latter to electric vehicle manufacturer Tesla?

Secondly, could the disbanding of the Seven show that investors are getting more confident that businesses outside tech in general, and AI in particular, can thrive and make decent gains? That's something we consider in our next Investment Insights where we take a look at some unsung heroes – a range of European stocks spanning sectors as diverse as pharmaceuticals, food, beauty and luxury goods that have all quietly been doing very well.

The search for hidden stars
While rising stock prices have been broadening out, substantial profit growth is still relatively rare and industry analysts have revised down their forecasts for 2024 for all but the highest quality and sector-leading companies: finding these remains a core focus for us.

As we explain in **our latest Investment Update** , we believe that the outlook for the global economy and corporate profits has brightened significantly over the last few months. But risks haven't vanished entirely.

We have much more confidence than we did a few months ago that good returns can be achieved in the medium-term, but there may be another bump or two in the road ahead this year.

We're particularly optimistic about a range of investments beyond the largest US companies. The very largest stocks in indices at any point usually underperform over five years or more (making a strong case against passive investing, which allocates more to the giants than anyone else). Smaller stocks and those listed in Europe seem more attractively valued. Expectations for profit growth and valuations are significantly lower than among US large cap stocks, so the bar for success is set much lower.

Industry analysts already anticipate that US large caps will grow their profits by 10% or more this year and next,

even though these companies' profits fell last year (outside the Magnificent Seven). The scope for positive surprises therefore seems limited compared to other markets, where expectations for profits are more moderate. Yes, the US usually trades at a premium to the rest of the world. But that premium is currently a lot bigger than usual.

If you'd like join our investment experts at our next Investment Insights webinar on Tuesday, 16 April, to hear more about the outlook for the global economy and markets, you can register at this link.

If you have any questions or comments, or if there's anything you would like to see covered here, please get in touch by emailing **review@rathbones.com**. We'd love to hear from you.

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