

Market Commentary**Global Market Overview for Q3 2024**

During Q3 2024, global equity markets saw steady performance driven by regional economic conditions and central bank policies. Inflation stabilized, and with it, several central banks, notably the U.S. Federal Reserve, began rate cuts, encouraging a more favorable environment for equities.

That does not mean the quarter was without drama. Signs of the impending Federal Funds rate cuts triggered an unwinding of the carry trade in Japan. Over a few weeks the Yen appreciated over 12%, and the Nikkei saw considerable gyrations, at one point falling 12% in one day only to rebound by 11% the next.¹

The run-on effects of the Fed rate cut did not end there. The eventual 50 basis point cut in September provided the People's Bank of China (PBOC) room to enact monetary stimulus of their own, providing a late quarter catalyst for Chinese equity performance.

Market Performance¹

- Europe slightly outperformed gaining 6.9%, despite ongoing economic challenges and lower growth prospects compared to other regions. Defensive sectors and select cyclical industries like industrials saw gains due to improved market sentiment and sector rotation
- Japanese equities, as reflected by the TOPIX, posted an equivalent 6.9% gain in Q3 following the early-quarter volatility. This was influenced by Japan's unique position as one of the few markets with rising interest rates to counter persistent inflation.
- The MSCI China index surged by 23.6% for the quarter, marking its strongest performance since the Global Financial Crisis. This rally was fueled by China's late-September stimulus package, which provided targeted support for the real estate sector and broader economy. The stimulus uplifted Chinese assets and provided a significant boost to emerging markets overall.
- MSCI EM recorded a 7.8% gain, with Asia seeing strong support from the China-led rally. The impacts were more varied across other emerging regions; for instance, Latin American markets like Brazil posted moderate returns, with gains constrained by local inflationary and currency pressures.
- The US Dollar reacted to the ongoing drumbeat of Fed Rate cuts by fall by just over 5% as measured by the DXY index of the dollar versus a basket of foreign currencies.

Regional Analysis¹**Europe**

Economically, Europe continues to lag global growth trends, with the region struggling with a prolonged slow growth phase over the past several years. However, recent indicators are signaling potential. European consumer confidence has shown a marked recovery, with a "three-standard-deviation improvement," a potential harbinger of stronger consumption. In combination with other leading indicators, Europe could be entering a "recovery" phase, where returns to equity markets are typically strong.

Japan

Japan experienced elevated volatility early in the quarter, partly due to the U.S. Federal Reserve's rate cuts, which triggered a significant unwinding of the yen carry trade. Japanese markets reacted with great volatility, with the TOPIX index falling over 12% in one day before rallying 10% the next day. The Bank of Japan maintained a hawkish stance amid high inflation pressures, and the new administration shows no sign of changing that path. This makes Japan one of the few developed markets actually increasing rates. Domestic investors, particularly individuals, have been net buyers following the market correction, indicating potential for steady domestic support throughout the rest of the year.

China

In an exceptional move, China introduced substantial monetary easing in late September to address weaknesses in its real estate market and broader economic challenges. The PBOC implemented a series of unexpected rate cuts, including a 50 basis-point reduction in reserve requirements and additional mortgage relief for households. While these measures have bolstered Chinese markets—resulting in a dramatic rise in MSCI China—their broader impact may be limited. While the Chinese equity rally was strong, commodity exposure and external demand in emerging markets remain subdued. Nonetheless, further fiscal stimulus is expected, with policy focused on domestic stability rather than significant external trade adjustments.

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3Q 2024 Shelton International Select Equity Fund Commentary

Summary

For the fourth quarter, all eyes are on the US election and whether the Federal Reserve continues to lower rates. While a thorough perspective of the potential effects of the different election scenarios is beyond the role of this missive, continued easing by the Federal Reserve would extend the weakness of the US dollar and provide incentive for investors to include international markets in their equity allocations.

The Middle East and Ukraine continue to be sources of geopolitical turmoil. The Russia-Ukraine war has evolved into a stalemate, and escalation between Iran and Israel is an outcome that neither side sees in their interest. While it is difficult to predict these conflicts will resolve themselves, so far markets have viewed them with complacency, reflected in the moderating price of oil.

Fund Review

For the third quarter, the Shelton Capital International Select Fund returned 7.91%, underperforming the MSCI AC World ex-US index return of 8.06% by 0.15%. Though the fund was overweight Japan for the quarter, it weathered the early August global selloff and the unwind of the Japanese Carry Trade better than the benchmark. Overall, the fund outperformed its benchmark through almost the entirety of the quarter, until the final several days of September, when the Chinese markets surged on the back of Mainland government stimulus.

The fund benefitted from overweights in Hong Kong and China as well as underweights in Taiwan and the UK. Sector wise, an underweight in semiconductors (in hand with the Taiwan underweight) and Energy stocks were beneficial, offset by our position in industrials and consumer discretionary stocks, which hurt the fund.

Our overweight position in Canon Inc contributed to the fund's performance with the stock gaining over 8% for the quarter. Canon reported quarterly earnings in late July, beating analysts' estimates for EPS and Revenue by over 39% and 10% respectively.² This coincided with analysts raising their price targets over the quarter from an average price of JPY 5414 on 6/30 to an average price of JPY 5009 on 9/30 per Bloomberg.

Shares of Novo Nordisk traded down over 21% during the quarter as the company faced mounting competition in the weight loss space from companies like Roche Holdings and Eli Lilly, in addition to some safety concerns that arose during trials of their next generation weight loss drug. Over the quarter, we positioned ourselves underweight based on underwhelming earnings estimates and fundamentals.²

Our position in Associate British Foods detracted from performance by 0.30%, caused by stock specific events outside of our model's predictive capability. The stock had a three-day losing streak in which it lost over 10% after it lowered guidance for its retail and sugar lines of business. Management cited lower foot traffic due to weather, impacting their retail LOB in the UK and Ireland, as well as a sharp reduction in European sugar pricing due to an increased supply in the market. Though the company's FY25 guidance for the retail LOB was to remain in line with 2024 levels, it also expects the negative impacts from sugar pricing to continue into 2025 before recovering in FY26.²

Demant A/S suffered from a 14% intraday decline in mid-July with the release of its preliminary Q2 results and revised guidance. The company revised down organic growth by about 50% as well as revised down its EBIT by about 8% citing a loss of market share managed care. The company ended down more than 13% for the quarter and detracted 0.29% from the fund's performance.²

¹ Bloomberg

² Axioma

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The MSCI ACWI ex USA is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed (excluding the United States) and emerging markets. Developed market countries include: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Hong Kong, Ireland, Israel, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom. Emerging market countries include: Brazil, Chile, China, Colombia, the Czech Republic, Egypt, Greece, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Peru, Philippines, Poland, Qatar, Russia, South Africa, Taiwan, Thailand, Turkey, and the United Arab Emirates. Net total return indexes reinvest dividends after the deduction of withholding taxes, using (for international indexes) a tax rate applicable to non-resident institutional investors who do not benefit from double taxation treaties. It is not possible to invest directly in an index.

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