GLOBAL LONG-TERM UNCONSTRAINED

Monthly Market Update

MARTIN CURRIE
A Franklin Templeton Company

MARCH 2023 **For professional and wholesale Investors only**

An ever more disruptive decade asserts itself

Innovation is on the increase, despite the risks, providing opportunities

Contents

Zehrid Osmani

Head of Global Long Term Unconstrained

Senior Portfolio Manager

Key risks

Geopolitics dominate, but a resolution of the Russia-Ukraine conflict, whilst seeming unlikely at this stage, could be an important driver for a further rally in European equities.

There are plenty of geopolitical risks to take into account in 2023. The ongoing Russia-Ukraine conflict remains an important focal point, with the risk of both escalation and broadening of the conflict to the NATO bloc. Related to that, the ongoing energy supply risk for Europe will be important to consider, with the European Union needing to continue to make progress towards eliminating its dependence on Russian gas supplies, which it has already managed to progress significantly in record times. Ultimately, we believe that Russia's importance on the international scene will have been permanently diminished. In our view, a resolution to this conflict, whilst highly uncertain and unfortunately unlikely at this stage, could be an important driver of a risk-on rally in European equities.

The recent incidents with the Chinese 'spy balloons' has highlighted not only China-US tensions but also China versus the rest of the world. This continues to spill over into technological conflicts, with the current US administration taking significant regulatory steps to cut off China from accessing leading edge semiconductor technology. This will clearly have implications for corporates exposed to these regulatory changes. China in the meantime continues to state its wish to, in its own words, re-unify the Chinese territory peacefully – a very explicit ambition on the Taiwanese territory. This is most likely to be by far the most sizeable geopolitical risk for financial markets, although timing of any worrisome development on that front is difficult to predict.

Tension between allies, is also a possibility. The Inflation Reduction Act in the US could potentially have negative implications for EU competitiveness as well, which could lead to further nationalistic tensions between blocs. This has been developing over recent months.

Against an uncertain backdrop, we highlight our 10 key risks for investors to consider in 2023, updated from our outlook published in December 2022.

Our 10 key risks

Monetary policies risk – over-tightening in interest rates creates a higher potential risk of policy mistakes for markets and economies.

Fiscal policies risk – lack of follow-through in stated infrastructure spending programs could put more downside risk to economic momentum.

Persistence in inflation – given the difficulty of predicting frictional inflation, risk of stronger and longer lasting inflation could fuel a need for more tightening in monetary policies.

Pandemic relapse risk – localised lockdowns could create further disruptions in supply chains and bottlenecks, which could create shortages and further fuel the frictional inflation.

Corporate margin pressure – more persistent and more elevated inflation could lead to more corporate margins pressure for companies lacking pricing power.

Market volatility and Style leadership volatility – shifting expectations in monetary policies could lead to ongoing volatility in markets, and in style leadership between Growth and Value styles.

Lower long-term growth – growing indebtedness is likely to lead to ongoing low long-term growth in our view, with more scarcity in growth opportunities.

Higher taxation – given higher indebtedness, there is a high likelihood of higher tax rates, both for households and for corporates.

Geopolitical risks flare ups – Russia-Ukraine conflict has tragically materialised in 2022 and will be an ongoing risk, in terms of conflict escalation, with the risk of broadening. Other geopolitical hotspots to watch out for are China-Taiwan, North Korea, Iran-Israel, and China-RoW. Some of these geopolitical risks will be military, others will materialise into technological conflicts, such as China-US.

Climate disasters risk – climate change related disasters are likely to continue to take their toll on various regions, with risk of negative impact on societies, but also on corporates in terms of risk to productive capacities and to assets in general.

Innovation on the increase – as an ever more disruptive decade continues to assert itself in 2023 and beyond

With the ongoing focus on investing for a transitioning world towards net-zero, innovation rates are likely to continue to increase, and with it, disruption risk to traditional businesses is likely to continue to rise.

For long term investors, this opens up good areas of opportunities in some of the recipients of investments to achieved net-zero, but it also highlights the need to be vigilant in terms of disruption risk on established business models, and to ensure disruption risk is assessed in a detailed and structured analytical approach.

Equally important is the ability for companies to remain innovative, to both fend off competitive pressures, and to stay ahead of the disruptive trends that could challenge their market positioning.

It is important to highlight here, in a market where short-term growth will be scarce (particularly Europe), long-term structural growth will be in demand. There are good opportunities across our three mega-trends of **Demographic Changes**, **Future of Technology** and **Resource Scarcity**. The eight medium-term thematic opportunities that we have identified previously still carry an important source of structural growth in our view. These eight medium-term thematic opportunities are:

- Green & Alternative Energy
- Electric Transportation
- 5G Telephony Upgrades
- Robotics & Automation
- Greener Infrastructure
- Healthcare Infrastructure
- Cloud Computing & Cyber Security
- Metaverse & Quantum Computing

There are sizeable infrastructure and capital expenditure drivers across these eight areas, which bring some interesting opportunities to capture areas of structural growth through companies exposed to these themes and their ecosystems.

Overall, we continue to focus on companies with:

- **Resilient earnings growth profiles –** given the ongoing risks of earnings downgrades
- **Structural growth themes exposure –** given the lower growth environment
- **Strong pricing power –** given the ongoing elevated inflationary pressures weighing on corporate margins
- **Solid balance sheets –** to withstand the potential risk of economic hard landing

Europe better than expected – Q4 global results season wrap

Europe's results season was better than expected, and to a lesser degree in the US, while emerging markets were mixed, and Japan weak.

All regions posted positive sales growth, but only Europe reported positive growth in earnings (see below). On aggregate company sales beat expectations across all regions, with the exception of emerging markets. Despite this margin pressures are continuing to come through, impacting companies across a wide range of sectors, in every region.

Earnings downgrades continuing to come through

While we are seeing earnings downgrades coming through across companies, the blow has been softened at a broader index level by strong growth globally from Energy and Utilities. These companies continued be helped by high energy prices.

Consensus estimates remain higher than many strategists have in their top-down estimates, but consensus is coming down closer to our own estimates.

Earnings growth 2023 year on year	Consensus	Martin Currie estimates
MSCI World	+1	-1%
MSCI US	+1%	0%
MSCI Europe	+1%	-5%
MSCI Asia	+2%	+5%

Source: Martin Currie and FactSet as 6 March 2023.

Margin pressures continuing to come through

Growth (%)

Europe

Sales	Earnings
+5.9	+9.3

Still helped by currency tailwinds European companies didn't experience any significant sales misses during the quarter. As we predicted, margin pressure is coming through with some notable misses (on expectations) in Consumer Staples, Industrials and Autos. Financials benefited from the supportive interest rate environment.

US

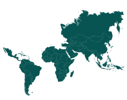
Sales	Earnings
+5.6	-2.6

There were no noticeable sales misses from the US. While earnings surprises were a mix of very strong (Consumer Discretionary) and very weak (Telecoms), with no specific pattern of note. The Technology sector continued to miss on the top line, but has been surprising positively on earnings (85% of companies posted positive surprise), as a result of a shift in focus towards profitability, and cost base management.

Japan

Sales	Earnings
+16.9	-16.5

Given the strong season on sales in Japan, there were no noticeable misses on that front. The earnings negative surprise however does highlight the margin pressures that many companies across a wide range of sectors (notably Telecoms, Industrials and Real Estate), are experiencing in Japan.



Emerging Markets

Sales	Earnings
+4.1	-3.6

No noticeable miss on sales during the period, whilst misses on earnings were across a wide array of sectors, implying margin pressure in this region also.

Source: Martin Currie and FactSet as 6 March 2023.

Important information

This information is issued and approved by Martin Currie Investment Management Limited ('MCIM'), authorised and regulated by the Financial Conduct Authority. It does not constitute investment advice. Market and currency movements may cause the capital value of shares, and the income from them, to fall as well as rise and you may get back less than you invested. The information contained in this document has been compiled with considerable care to ensure its accuracy. However, no representation or warranty, express or implied, is made to its accuracy or completeness. Martin Currie has procured any research or analysis contained in this document for its own use. It is provided to you only incidentally and any opinions expressed are subject to change without notice. This document may not be distributed to third parties. It is confidential and intended only for the recipient. The recipient may not photocopy, transmit or otherwise share this document, or any part of it, with any other person without the express written permission of Martin Currie Investment Management Limited.

This document is intended only for a wholesale, institutional or otherwise professional audience. Martin Currie Investment Management Limited does not intend for this document to be issued to any other audience and it should not be made available to any person who does not meet this criteria. Martin Currie accepts no responsibility for dissemination of this document to a person who does not fit this criteria. The document does not form the basis of, nor should it be relied upon in connection with, any subsequent contract or agreement. It does not constitute, and may not be used for the purpose of, an offer or invitation to subscribe for or otherwise acquire shares in any of the products mentioned.

Past performance is not a guide to future returns. The distribution of specific products is restricted in certain jurisdictions, investors should be aware of these restrictions before requesting further specific information.

The views expressed are opinions of the portfolio managers as of the date of this document and are subject to change based on market and other conditions and may differ from other portfolio managers or of the firm as a whole. These opinions are not intended to be a forecast of future events, research, a guarantee of future results or investment advice.

For wholesale investors in Australia:

Any distribution of this material in Australia is by Martin Currie Australia ('MCA'). Martin Currie Australia is a division of Franklin Templeton Australia Limited (FTAL), (ABN 76 004 835 849). Franklin Templeton Australia Limited is a wholly owned subsidiary of Franklin Resources, Inc., and holds an Australian Financial Services Licence (AFSL No. 240827) issued pursuant to the Corporations Act 2001.

For institutional investors in the USA:

The information contained within this presentation is for Institutional Investors only who meet the definition of Accredited Investor as defined in Rule 501 of the United States Securities Act of 1933, as amended ('The 1933 Act') and the definition of Qualified Purchasers as defined in section 2 (a) (51) (A) of the United States Investment Company Act of 1940, as amended ('the 1940 Act'). It is not for intended for use by members of the general public.

MARTIN CURRIE
A Franklin Templeton Company

Martin Currie Investment Management Limited, registered in Scotland (no SC066107)
Martin Currie Inc, incorporated in New York and having a UK branch registered in Scotland (no SF000300),
2nd Floor, 5 Morrison Street, Edinburgh EH3 8BH

Tel: (44) 131 229 5252 Fax: (44) 131 222 2532 **www.martincurrie.com**