CIO favors adding quality growth to portfolios, as firms with competitive advantages and exposure to structural growth drivers should continue to deliver robust earnings growth. (UBS)

Looking for opportunities beyond US tech

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US equities on Tuesday shrugged off higher-than-expected job openings revealed by May's Job Openings and Labor Turnover Survey (JOLTS), with the S&P 500 index closing above 5,500 for the first time and claiming a 32nd record high this year. That left the index up 15.5% so far in 2024.

Despite the strong labor market data, investors were encouraged by Federal Reserve Chair Jerome Powell's acknowledgement that the US central bank has made "quite a bit of progress" in reducing inflation.

The rally has continued to be led by tech. The FANG+ index, which tracks the top 10 most traded tech stocks, has climbed 4.0% in the first two days of this week versus a 0.9% increase for the index overall. Year to date, the FANG+ is up 35%.

But while we are positive on the outlook for US megacap tech stocks and the development of AI, we expect the rally to broaden, so investors should not neglect opportunities beyond recent US tech leaders.

Global quality wealth compounders have a track record of delivering solid risk-adjusted shareholder returns. Companies that are able to reinvest their earnings at returns consistently above their weighted-average cost of capital and generate strong free cash flows can be expected to create long-term value for shareholders. To benefit from this, we recommend companies with a competitive edge, pricing power, and high barriers to entry.

The outperformance of quality companies in Europe and Asia are expected to continue. While political uncertainty surrounding the French election has proved a drag on the Eurozone equity market in recent weeks, we believe the region will benefit from a pickup in global industrial activity alongside central bank rate cuts. Highly profitable and innovative companies headquartered in Europe that are global leaders in their respective industries should continue to deliver high and durable earnings growth with lower volatility.

Secular trends including energy transition, blue economy, and water scarcity offer quality growth opportunities. While the US election poses risks, we believe global greentech companies and investments in renewable energy infrastructure should remain well positioned amid the global drive to reduce carbon emissions. The increased political focus on reducing pollution and preserving ocean ecosystems should benefit companies offering wastewater treatment solutions, and those focused on innovations that cut pollution at source. In addition, we estimate the market size of industries looking to address water scarcity to grow further from the current USD 655bn.

We therefore favor adding quality growth to portfolios, as firms with competitive advantages and exposure to structural growth drivers should continue to deliver robust earnings growth.

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