EFFICIENT GROUP

ECONOMIC COMMENTARY

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YOUR MONTHLY ECONOMIC UPDATE

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The good times are here to stay - or are they?

"We believe in what people make possible." This is the slogan of one of the fastest-growing companies in the world, Microsoft. Currently, Microsoft seems to be achieving feats beyond what is possible. Growth within the world's largest economy, the United States, has recently slowed down. Gross domestic product figures show that the number of goods and services created in the last quarter registered the weakest pace of expansion since the second quarter of 2022. At a business level, the majority of corporate America is feeling the pinch of higher interest rates and slowing growth. The impact of higher interest rates is usually only felt 12 months after the original hiking decision was made. It is, therefore, apparent that the worst effects could still lie ahead. For the time being, however, tech stocks, such as Microsoft and Alphabet, seem to be bucking the trend. Since the start of 2023, their respective share prices are already up 28% and 23%. But, on an even broader scale, the top performers all seem to be tech-related stocks.

There are a few reasons why tech is performing strongly in 2023. One of these is investors hopping back into some of 2022's worst-performing stocks, smelling a bargain. Investors also seem to like certain unique qualities in tech, such as resilient demand and growth, which stand in stark contrast to an environment filled with concerns about failing banks and inflation-strapped consumers. There are also company-specific reasons. For example, Microsoft has achieved a new 52-week high because of the current optimism around its artificial intelligence (AI) services, following its investment in OpenAI in 2022. This investment is already beginning to have an impact on market share and performance, and there is a lot more scope as Microsoft starts to merge its cloud (Azure) and AI (OpenAI) services. This combined service already has 2 500 customers, including Shell and Mercedes-Benz, with more customers being added at breakneck speed.

Investors' attention has, therefore, been diverted away from the economically sensitive areas of big tech. For example, the weaker economic backdrop has resulted in consumers buying fewer personal computers (PCs) globally. This has not only affected Microsoft's PC sales but also other areas of its business, i.e. the demand for its software. Other companies, such as Intel, have felt the effects of a softening in PC demand more acutely as many of those PCs are powered by Intel chips. Other segments of the market are also struggling. Google, for example, reported a second consecutive drop in advertising revenue, while Facebook informed its employees to expect a slower pace of hiring following the company's latest round of layoffs amid uncertainty in advertising spending going forward.

Tech's stellar performance over the last several months represents a unique problem for the market: Overdependence on big tech gains has done little to provide assurance about the health of the wider economy, which leaves investors especially vulnerable if tech should stumble again. Signs of this could not be reflected more clearly than by the ongoing layoffs at big tech, which serve to boost near-term figures but is also likely to signal a weakening in the intermediate-term outlook.

While investors have been rewarded for their contrary positioning in big tech, despite a weakening global economic backdrop, they will certainly have to exercise caution going forward as we continue to move into a stock pickers environment.

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