Market Commentary on the Q3'2023 Results Season:

Approaching Another Transition Year in 2024?

Having gone through a period of **shifting inflation and employment data** in recent weeks, a **rollercoaster ride in yields**,[i] Central Bank officials indicating that **high interest rates will stay for longer** but also **renewed geopolitical tension** due to the Israel-Hamas war as well as **growing fiscal deficits**,[ii] the first two weeks of the Q3'2023 reporting season have clearly signalled that "CEOs have become less confident about a 2024 recovery" (Jane Fraser, CEO of Citigroup) and that "2024 remains a transition year" (Peter Wennink, CEO of ASML).[iii] Interestingly, those companies publishing a profit warning over the last few days were most outspoken about the **weaker macro-economic environment having a direct impact on net sales** (Nokia), with **customers remaining cautious to invest** and "current conditions to prevail into 2024" (Börje Ekholm, CEO of Ericsson).[iv] The ongoing debate on **affordability for customers under high interest rates and elevated prices** goes beyond residential housing and commercial real estate and is currently very much on the mind of CEOs when thinking about their strategic plans in 2024.[v]

Against this market backdrop, there were a number of **new developments of particular interest from an investor's perspective** during the Q3'2023 reporting season: 1) with **inventories having largely normalised** after the post-Covid supply chain crisis, there was not only a substantial reduction in lead times but also **"weakness in short-cycle business"** (Björn Rosengren, CEO of ABB);[vi] 2) lower (and in some cases the sharp drop of) order intakes and the soft topline continue to hit straight down the P&L,[vii] resulting in an **extensive debate about how much further can cost cutting really continue** without impacting the business (Pekka Lundmark, CEO of Nokia);[viii] and 3) the divergence of trade and **different speed of economic growth between major economic blocs (US, China and Europe)** continues to impact not only investor sentiment, but also corporate investment decisions including the shifting and reshoring of supply chains.[ix]

With the latter in mind, we start with a discussion on industrial policy and the **new interventionism, illustrated not only by various state-led infrastructure, chip and green acts** by the US administration and the EU, but also China's increasing economic protectionism.[x] In this context, we highlight latest developments in **intellectual property (IP) theft and technology transfers, while using the construction & building materials industry** as a case study for potentially diverging economic fortunes. With capital allocation policies being widely debated by investors and analysts before the start of 2024, we look at the **current discussion on share buy-backs** before focusing on some new governance-related topics of investor interest, notably the **conflicted independence of auditors** and **corporate corruption & fraud**. With the **telecoms & infrastructure industry** widely claiming to provide the lifeblood for digital connectivity, data traffic and networks, we investigate why investors are still not getting overly excited.[xi] Finally, as **Millennials & Generation Z are becoming an increasingly important and influential constituency** as customers, employees, investors and young CEOs,[xii] we have a look at the current debate and draw some early conclusions from a capital markets perspective.

NEW INTERVENTIONISM

Following up on the institutional debate of the New World Order in our previous Q2'2023 market commentary, it is astonishing to what extent growing geopolitical rivalries, national security concerns and a heightened corporate risk perception have led to a widely accepted rise of big government and state interventionism.[xiii] From a corporate perspective, the growing shift towards economic nationalism and technological decoupling not only has cost implications but also raises market competition issues as governments usually support industries in decline through trade measures and company-specific subsidies.[xiv] In turn, professional fund managers may have to restructure their portfolios and rethink strategic asset allocation policies while some seasoned investors perceive the global economic paradigm shift towards "de-risking" in a more sanguine way, given 1) the potential of huge capex programmes for creating new demand and employment; 2) intense competition for new technologies boosting productivity; and 3) higher costs of alternative supply chains being offset by the additional capacity they bring.[xv]

There is one other argument in favour of protectionism as there are very high stakes of success in newly emerging industries such as artificial intelligence, advanced semiconductors, quantum computing and renewables.[xvi] With "national security risks" being increasingly cited as a primary concern about adversary regimes being able to develop sophisticated weapons and spy agencies breaking cryptographic codes to protect data, issues of cyber security, IP theft and technology transfer have now clearly advanced in corporate risk management priorities. On the downside, not only is this new security-led industrial policy a moral hazard and massive capital misallocation, but there is also a surge in zombie firms, which undermine business dynamics and productivity growth.[xvii]

IP THEFT AND TECHNOLOGY TRANSFER

While we had looked at cyber security issues in our previous Q2'2023 market commentary, the growing threat of IP theft and technology transfer is another critical theme, which has not been widely covered so far while being discussed with investors behind closed doors at best. Whereas the US Chips Act may have brought this grey area to greater investor attention, as the affected Western companies talked more openly about their security concerns, frequent attacks and higher costs,[xviii] this is certainly a much more widespread phenomenon, involving a murky network of spy agencies, hackers and specialised firms world-wide.[xix]

As more engineers and even former senior executives have fled with trade secrets to China in recent months, causing massive financial damages and technological setbacks,[xx] Western authorities have adopted a more concerted effort to protect its companies and prevent technology leakage to China and elsewhere.[xxi] In South Korea, the National Intelligence Service confirmed leaks of "national core technologies" to have steadily increased from three cases in 2017 to 10 in 2021 and three for the first quarter of 2023 alone, with the latter occurring at large companies in the semiconductor, display and car maker.[xxii] More recently, the heads of security services in the US, UK, Canada, Australia and New Zealand have tried to raise awareness of Silicon Valley about risks posed by China in high-tech sectors ranging from quantum computing and artificial intelligence to synthetic biology, outlining that – while all nations spy – "the Chinese government is engaged in the most sustained, scaled and sophisticated theft of intellectual property and expertise in human history".[xxiii]

CASE STUDY: CONSTRUCTION & BUILDING MATERIALS

With interest rates rising housing has been one of the focus points of investor interest when trying to figure out what sector to avoid – despite significant infrastructure projects at both sides of the Atlantic and governments promising more housing – both affordable and more general.[xxiv] For some industry observers, the sector has been in a "perfect storm" as interest rates and energy prices climbed sharply, supply chain disruptions pushed up the cost of building materials and an acute shortage of skilled labour stretched construction schedules.[xxv] In the United States, where idiosyncratic city zoning politics was often aggravated by the influx of migrants, housing has become a major contributing factor of continuing high inflation, with the shelter index portion of the CPI being up by 7.2 per cent year-on-year and accounting for more than 70 per cent of the total increase in all items except food and fuel.[xxvi]

Continuing high inflation remains one of the sticking points for the construction industry,[xxvii] driving companies' pricing strategy despite input costs decelerating,[xxviii] and implying "six to nine months to establish a new equilibrium after price increases", according to the CEO of Cemex, Fernando Gonzalez (Q2'2023 analyst call on 27 July 2023). In addition, labour shortages at both sides of the Atlantic remain a serious issue, with the US construction industry being reportedly short of 546,000 workers – compared with 391,000 construction job openings in 2022 – with hourly wages at $36 in January 2023 exceeding the private industry average of $33 and typical starting salaries for college graduates.[xxix] This brings the new industrial policy of the US administration, notably infrastructure and clean energy projects as well as semiconductor homeshoring,[xxx] to the brink of colliding with the realities of the US labour market,[xxxi] with the majority of construction firms struggling to find workers, facing regulatory restrictions, prevailing wage and apprenticeship requirements as well as immigration reform.

In Europe, higher market prices also imply higher CO2 emission costs, as in the words of the CEO of Holcim, Jan Jenisch, "decarbonisation is the new reality in Europe" and companies have to "translate decarbonisation into buildings solutions" (Holcim Q3'2023 Trading Update, 27 October 2023). This might indicate another diverging development between North America and Europe despite all the efforts of the EU Green Deal to catch up with the US Infrastructure Act.[xxxii]

CONTROVERSY OVER SHARE BUY-BACKS

With higher rates for longer and companies having to review their capital allocation priorities, discussions on share buy-backs have been significantly toned down by senior management during the current Q3'2023 reporting season. When being pressed by analysts during Q&A, corporate executives pointed more frequently to the need to reduce net debt and/or to continue with the existing dividend payout policy.[xxxiii] The main controversy over share buy-backs remains whether they are a good use of corporate money by giving money back to the investors who ultimately own the company, as opposed to investing the money into future growth and/or offer more benefits to its employees.[xxxiv] The critics of share buy-backs argue that this business strategy manipulates numbers and rewards executives whose remuneration is tied to earnings per share or share price performance targets.

Interestingly, a recent study highlighted a “larger pattern in the buy-back market, characterised by high costs and inefficiencies” due to companies using brokers in the process.[xxxv] The pace of share buy-backs started to slow down in the US significantly in Q2’2023 due to higher interest rates, lower oil prices and technology companies investing more into artificial intelligence.[xxxvi]

More recently, there has been increased regulatory scrutiny in the US with respect to share buy-backs, with the SEC adopting a final rule requiring companies to disclose share repurchases on a quarterly basis.[xxxvii] There is also a proposal to quadruple the 1% tax on share buy-backs in the US, that was initially introduced as part of the Inflation Reduction Act in late 2022.[xxxviii] There is a similar trend in Europe, with Dutch lawmakers backing the introduction of a share buy-back tax in September 2023, although it is still not clear when this tax would come into effect.[xxxix]

AUDITORS UNDER SCRUTINY

As annual company accounts remain a vital source of information for institutional investors, the role of auditors, notably the oligopolistic position of the Big Four accounting firms, and inherent conflicts of interest in their business model has come under increasing scrutiny.[xl] It is not only the scope of professional failure, best illustrated by the acceptance of fabricated letters and unchecked payments while auditing the collapsed German payment firm, Wirecard,[xli] which sadly has not been an isolated case,[xlii] but also the culture of overlooking rule-breaking in the pursuit of revenue growth, with too much power being concentrated in the hands of chief executives and loyalty being rewarded above challenging more senior partners.[xliii] From a corporate client perspective, the simultaneous overlap of auditing financial and non-financial accounts as well as providing additional tax and advisory services has been increasingly challenged by governance-focused professional investors.

While the recent PwC tax scandal in Australia led to a renewed investigation of conflicts of interest when providing lucrative consulting work to audit clients,[xliv] regulatory reform of the audit industry remains an unfinished business,[xlv] not only often leaving professional fund managers in the dark about the promised “fair & proper view” of annual accounts, but also adding complexity by missing out on climate-related risks and costs.[xlvi] In the wake of these latest revelations, the traditional partnership model has been increasingly questioned, with EY trying to spin off its consulting business and float it on the stock market,[xlvii] and BDO USA switching to a professional services corporation in summer 2023, keeping an open option to take private equity money for acquisitions. For the latter, its partners are becoming shareholders and employees instead, being “offered tax and other advantages” and, more importantly, removing the “dysfunctionality of decision making” when consulting partners on all major strategic moves.[xlviii]

CORPORATE CORRUPTION & FRAUD

Another governance-led topic of growing investor concern, which has not been widely covered so far, is that of corporate corruption & fraud, despite companies frequently claiming in their relevant governance section of ESG presentations that there has been “no case of corruption” and pointing to more hours of compliance training in the risk management section of annual reports.[xlix] While it is difficult to trace how pervasive corporate corruption still remains and to what extent responsibility goes all the way to the upper echelons of corporate power,[l] the potential scope of reputational damage and massive fines by international courts are some of the huge risks professional fund managers have to consider nowadays before making an investment.[li]

In this context, an interesting debate has evolved to what extent global bribery settlements by anti-graft agencies in developed countries should be shared with developing nations, profiting from the harm done by their companies through fines imposed in secretly negotiated plea bargains.[lii] At the same time, developing countries have started to fight back through their own investigations, as the recent criminal complaint by the Indian Central Bureau of Investigation against Rolls-Royce and BAE Systems shows (dating back to 2003-2012).[liii] More worryingly, the recent claim by a senior executive of Maersk that shipping supply chains are infiltrated by international drug gangs at an “extreme” degree not only has implications for higher security costs including increased checks of employees, but also raises concerns about employees’ safety and the use of legitimate infrastructure for drug trafficking.[liv]

CASE STUDY: TELECOMS & INFRASTRUCTURE

We had originally shown greater interest in the telecoms & infrastructure sector after the EU commissioner, Thierry Breton, himself the CEO of France Telecom, now Orange, until 2005, warned in February 2023 that the industry’s business model will have to undergo through a “radical shift” and that obstacles to cross-border consolidation are “holding back our collective potential compared to other continents”.[lv] Not much has changed since then, with the merger of Orange and MasMovil in Spain proposed in July 2022 still being objected by the EU Commission on competition grounds,[lvi] which is now widely seen as the test case for future M&A activity in Europe’s telecoms industry.[lvii] In the meantime, investors in the sector have become increasingly frustrated not only about the slow roll-out of 5G networks in Europe and the US but also limited monetisation of digital connectivity, data traffic and networks by telecoms operators.[lviii]

As to future monetisation, the two dozen operators in Europe and the US we had followed over the last few months offered a number of interesting ideas, notably with a strong focus on IT security, outsourcing, vertical solutions and Cloud offerings for corporates,[lix] as well as private networks in the US with greater capacity, security and latency for large enterprises.[lx] In this context, a group of 20 European telecoms operators started lobbying the EU Commission to force US large technology companies to pay a “fair and proportionate contribution” towards the costs of network infrastructure and to support the roll-out of 5G and upgrade to full-fibre networks.[lxi] At the same time, there is also a wide recognition that there is not only much higher utilisation of the fibre network required, but also that “Europe remains too fragmented” and the “Cloud sovereignty environment” drives demand for more data centres (Christian Illek, CFO of Deutsche Telekom).[lxii]

Artificial Intelligence (AI) has now also become a key topic of discussion in the telecoms industry - even if most companies (except Telenor and BT Group) still refrain from providing details of their AI projects. The CEO of Telenor, Sigve Brekke, emphasised the "use case" for four areas in particular: a) distribution, b) customer care; c) network maintenance; and d) infrastructure energy (Q2'2023 analyst call on 20 July 2023). In turn, BT Group highlighted new possibilities offered by AI in the areas of network planning, predicting & maintaining traffic and "self-healing networks" (FY2023 analyst call on 18 May 2023). Job cuts were also discussed very openly by BT Group's senior management, with the plan to reduce the current 140,000 employees to 90,000 by 2030 (instead adding 5,000 new jobs for digitisation, IT and AI).[lxiii]

MILLENNIALS AND GENERATION Z

As companies have increasingly started to focus not only on consumer preferences, but also on employee motivation of millennials and generation Z, recent disruptions from the Covid pandemic, economic recession, climate change, the war in Ukraine, new digital developments including AI and higher labour mobility through the Great Resignation in the US have raised awareness about the scope of uncertainty in the modern world as well as the fact that younger generations can provide a different (and often very useful) perspective. While still being at Covid lockdowns, the phenomenal wave of retail trading in meme stocks, often seen by young people as an alternative to computer games, have also brought to attention their short-term trading behaviour, with an expectation of instantaneous reward under high risk and being influenced predominantly through social media followings.[lxiv]

These latest development have resulted in an explosion of generation-specific surveys that highlight not only long-term expectations, but also the potential financial opportunities (and attractiveness) of millennials and GenZ, ranging from the global creator economy as pitched by Goldman Sachs and Citigroup,[lxv] to implications of the Apple ecosystem for changing social circles given that GenZ is the most online of any age group,[lxvi] and even political preferences on housing, social care and immigration.[lxvii] From a capital markets perspective, naturally the greatest interest so far has been on flexible work preferences of millennials and GenZ after Covid lockdowns, often accompanied by a lack of office training and face-to-face conversations with more senior colleagues, [lxviii] with some of the Big Four companies complaining that their new hires lack communication skills,[lxix] to US law firms finding through their GenZ surveys that this generation "highly values social justice and altruism" with implications for their work practices,[lxx] as well as in-depth research on education and wealth accumulation between baby boomers and millennials. As to the latter, millennials entered the labour market with more degrees under their belt, but their home ownership lies well below that of baby boomers at the same age.[lxxi] For any employer – but also government pitching for future votes – this gap is something to watch!

Peter and Irina Kirkow
30 October 2023

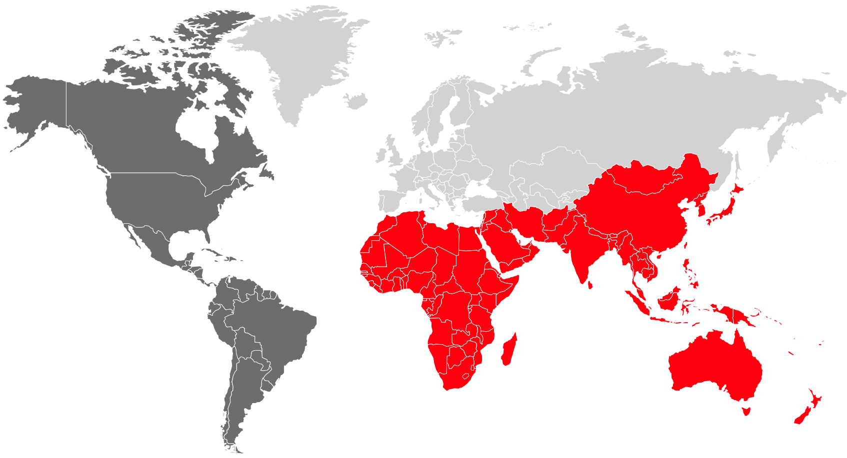
APPENDIX

ABB Q3'2023 results presentation

Growth in the Americas and AMEA; Europe demand muted

Q3 2023 regional, country orders

The Americas	**+13%**
USA Steep growth in PA due to multi-year contract; Strong growth in EL; Strong decline in MO and RA	+13%
Canada	+41%
Mexico	-4%
Europe	**-13%**
Germany Strong growth in PA; decline in EL; steep decline MO due to large rail order in prior year and RA	-33%
Italy	-5%
Netherlands	+86%
AMEA	**+4%**
China Strong growth in MO; PA and EL stable; steep decline RA	-3%
India	+10%
UAE	+13%



Slide 5 All data presented on a YoY comparable basis; all growth comments refer to comparable growth trends. Performance highlighted for largest 3 countries in $ mn terms in each region.
EL = Electrification. MO = Motion. PA = Process Automation. RA = Robotics & Discrete Automation.

Business update

Mixed trends, volume rebound not yet visible, easier comps in Q4

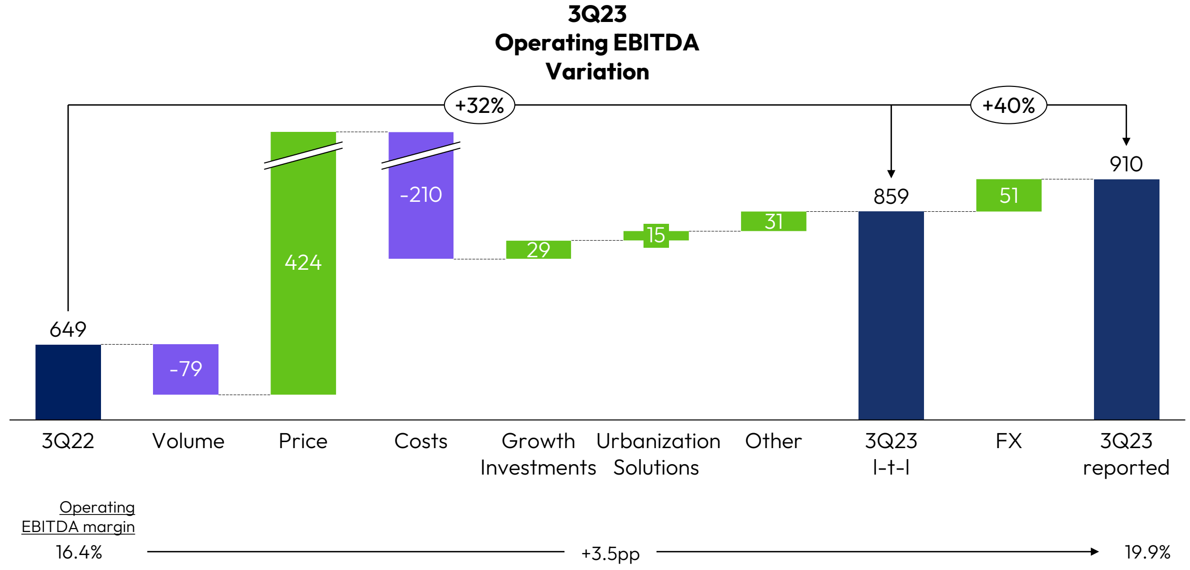
		Q3 2023	Q4 2023
Paints EMEA	Demand continuing to stabilize, Europe flat	Flat	Flat
Paints LATAM	Soft market conditions	-MSD%	
Paints China	Continuation of H1 trend	+HSD%	Growing
Paints South Asia	Mixed market conditions dictating performance	+LSD%	
Powder Coatings	Demand improvement earlier than expected	+MSD%	
Marine & Protective	Continued strength, especially in Asia	+HSD%	
Automotive & Specialty	Weakness in VR Europe partly offset by Auto and VR NAM	-LSD%	
Industrial Coatings	Strength in Coil, Wood still under pressure	-HSD%	-LSD%
AkzoNobel	**Q4 up on easier comps**	Flat	+LSD%

Organic volumes y-o-y

Investor update | Q3 2023 LSD = low single-digit, MSD = mid single-digit, HSD = high single-digit, DD = double-digit 4 AkzoNobel

Pricing, decelerating inflation, and growth investments drive EBITDA increase

CEMEX

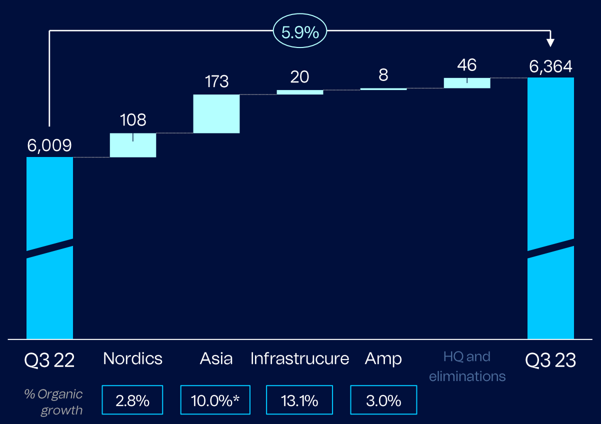


Millions of U.S. dollars

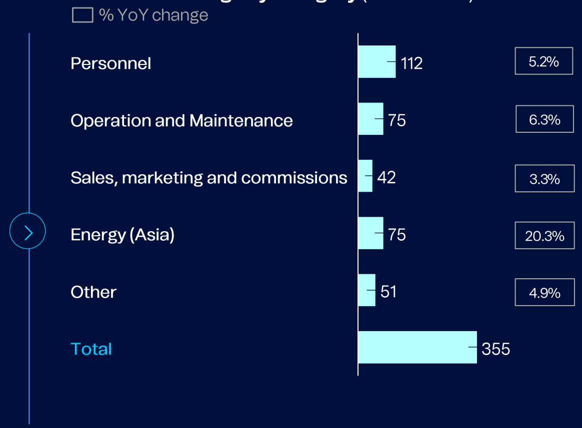
7

Opex increase of 5.9% driven by salary inflation, energy costs, and network expansion in Asia

Organic YoY OPEX (NOK million)



OPEX YoY-change by category (NOK million)



Q3 2023

* 9.4% excluding SIM-tax reversal in Pakistan in Q3 22

13

ENDNOTES

[i] It goes beyond the scope of this market analysis to investigate the extreme daily yield fluctuations in September and October and their technical implications for the bond market, impacting investor sentiment as a significant portion of pension funds and insurance companies were holding substantial quantities of bonds at large mark-to-market losses. For a thorough contextual analysis including repercussions from erratic economic forecasts and conflicting monetary policy, see: Mohamed El-Erian, *"US bond market is losing its strategic footing"*, Financial Times, 17 October 2023 and for an interesting discussion of the yield level compared to bond supply, see: Tomasz Wieladek, *"A big problem looming for bond markets"*, Financial Times, 23 October 2023.

[ii] Given the renewed geopolitical tension after the Hamas' attack of Israel on 7 October, it was perhaps surprising how fast markets had recovered and started focusing on interest rate developments again. When looking at such events over a long period of time, this was not necessarily unusual and follows similar market recoveries like 9/11, see: Ruchir Sharma, *"Why markets are relatively calm in the geopolitical storm"*, Financial Times, 23 October 2023. For two extensive discussions on shifting economic outcomes on the back of "higher rates for longer", see: Katie Martin and Nicholas Megaw, *"'A soft landing is still a landing': stock pullback clouds market optimism"*, Financial Times, 5 August 2023 and Mohamed El-Erian, *"The US may no longer avoid a recession"*, Financial Times, 5 October 2023.

[iii] While US banks argued that in the current rate environment it will still take time to "understand the cost of capital" (James Gorman, CEO of Morgan Stanley, at the Q3'2023 analyst call on 18 October 2023) and that "some sectors in the economy still have to absorb higher rates" (David Solomon, CEO of Goldman Sachs, at the Q3'2023 analyst call on 17 October 2023), senior executives from industrial companies started looking beyond 2024, pointing to secular trends and customer orders indicating "accelerated growth into 2025" (Peter Wennink, CEO of ASML, at the Q3'2023 analyst call on 18 October 2023), given that significant investments are required for Cloud Computing and Artificial Intelligence (Pekka Lundmark, CEO of Nokia, at the Q3'2023 analyst call on 19 October 2023).

[iv] Changes in consumer sentiment due to higher interest rates and a more difficult macro-economic environment were widely discussed during the Q3'2023 reporting season. The CEO of Tesla, Elon Musk, pointed out that "people hesitate to buy a new car in tough economic times" and that Tesla's management wants "first to understand where the global economy is going before we invest full speed in Mexico" (Tesla Q3'2023 analyst call on 18 October 2023). When the CEO of Nestle, Mark Schneider, was asked about signs of changing consumer behaviour at the Q3'2023 sales update on 19 October 2023, he replied that this applies "rather to long-term durables", although his outgoing CFO, Francois-Xavier Roger, conceded that the "sequential moderation of pricing will continue", with prices for diary food products having been down by 25% year-to-date. In this context, when asked about the impact of the current conflict in the Middle East on consumer sentiment, the CEO of Signify, Eric Rondolat, indicated that this could become "potentially significant" if it spreads beyond the Gaza region (Signify Q2'2023 analyst call on 27 October 2023).

[v] While we had extensively covered the "consumer affordability" theme when discussing car manufacturers and their attempt to produce EVs at or below EUR 25,000 in our previous Q2'2023 market commentary, this discussion has now been reignited following the latest rate decisions and statements by the US Federal Reserve and other Central Banks, see among others: Colby Smith and Harriet Clarfelt, *"Jay Powell warns inflation 'too high' in Jackson Hole speech"*, Financial Times, 25 August 2023 and Richard Barwell, *"Central banks still need to justify the case for 'higher for longer' rates"*, Financial Times, 12 October 2023. It was certainly interesting to hear the empathy that one of the richest persons on earth was trying to show to all those people "who live from one pay cheque to the next" and conceding that we have entered a "bad credit situation" in real estate, credit cards, etc. (Elon Musk, CEO of Tesla, at the Q3'2023 analyst call on 18 October 2023).

[vi] While each industry might have its specific issues and economic cycles, it is interesting to follow the semiconductor industry at this particular moment, as they reported "early signs of an inflection" and observed the sector "passing through the trough" (Peter Wennink, CEO of ASML, at the Q3'2023 analyst call on 18 October 2023) given, among others, "early signs of demand recovery for PCs and smart phones" (C.C.Wei, CEO of TSMC, at the Q3'2023 analyst call on 19 October 2023). Similarly, Intel reported "signs of normalisation after a depressed 2023" (Pat Gelsinger, CEO of Intel, at the Q3'2023 analyst call on 26 October 2023). This is against the backdrop of "customers' ongoing inventory adjustment" (TSMC), "some moderation in order" (ASML) and "lower capacity utilisation" (VAT Group Q3'2023 trading update, 12 October 2023), leading to ongoing pressure on free cash flow, the need to be "prudent on capital returns" and "some slowdown in hiring people" (Roger Dassen, CFO of ASML, at the Q3'2023 analyst call on 18 October 2023).

[vii] In the case of Nokia, sales in North America have reportedly dropped by 40% the second quarter in a row, which led not only to another profit warning, but also the announcement of EUR 400mn in cost savings in 2024 and headcount

reduction of up to 14,000 FTEs by 2026. The latter is a new and more pronounced theme for the Q3'2023 reporting period, not only by its magnitude, but also by the impact on the business going forward. For an example of workforce reduction by smaller companies with a regional concentration of labour, see the Austrian lighting company Zumtobel: https://z.lighting/de/group/news-insights/ir/auftragslage-erfordert-neuausrichtung-von-tridonic-komponentenwerk-dornbirn/. Other companies like VAT Group reported the extension of short-time work in Switzerland, see: https://ir.vatvalve.com/en/news/detail/vat-media-release-on-extension-of-short-time-work--2023-09-20, and, in the telecoms industry, a "voluntary departure plan" for Orange Enterprise, which is currently being reviewed by the French labour administration (Orange Q3'2023 results call on 24 October 2023).

[viii] While senior management repeatedly stressed that "our job is to control what we can control" (James Gorman, CEO of Morgan Stanley, at the Q3'2023 analyst call on 18 October 2023), the discussion has moved on as "you cannot run a business when only cutting costs" (Pekka Lundmark, CEO of Nokia, at the Q3'2023 analyst call on 19 October 2023), outlining the seriousness of Nokia's situation by announcing "decisive action strategically, operationally and in costs". When asked by analysts during the Q3'2023 Q&A whether this would also imply "any strategic alternatives for the business", the CEO of Nokia replied that they will look into options for further "portfolio optimisation". When presenting its update on "industrial transformation" with the release of Q3'2023 results, the CEO of AkzoNobel, Gregoire Poux-Guillaume, was adamant to portray the new measures as an "industrial efficiency programme", not just a cost-cutting exercise as frequently asked by analysts at the Q&A (AkzoNobel Q3'2023 analyst call on 25 October 2023). In trying to differentiate this "structural reset" from merely mitigating inflation through cost savings, management claimed that value will be unlocked through automation, de-bottlenecking, footprint/network rationalisation, improvement of supply chain efficiency and a higher utilisation rate in the segment Deco Europe.

[ix] For an interesting discussion of the transatlantic gap between the US and Europe widening, based on higher pandemic stimulus in the US, lower energy prices, the booming technology sector across the Atlantic as well as higher investment and better demographics in the US, see: Valentina Romei and Colby Smith, "*How is the US economy managing to power ahead of Europe?"*, Financial Times, 19 October 2023. In the Appendix, we provide a slide from the ABB Q3'2023 results presentation showing significant differences in regional growth.

[x] The politically enforced economic protectionism in China ranges from raids of Western professional firms (Kathrine Hill et.al.,*"Beijing's 'men in black' step up scrutiny of foreign corporate sleuths"*, Financial Times, 2 May 2023), to ordering public officials not to use iPhones (Patrick McGee, "*Apple stock hit by China worries ahead if iPhone 15 launch"*, Financial Times, 8 September 2023) and imposing restrictions on metals exports like gallium and germanium critical for semiconductor production (Edward White et.al., *"China's curb on metal exports reverberates across chip sector"*, Financial Times, 4 July 2023), to provide a few examples.

[xi] The CEO of AT&T, John Stankey, even claimed "wireless technology (to be) the next strategic frontier", although during the Q&A he extensively elaborated on the bipartisan Infrastructure Act and its implications for underserved areas and affordable service levels, with State applications of the infrastructure bill varying and private capital being expected not to come in before 2025 (AT&T Q3'2023 analyst call on 19 October 2023).

[xii] For an interesting personal profile of the 28-years' old CEO of DIY-chain Leroy Merlin France, Agathe Monpays, a company employing about 30,000 people and with annual sales of EUR 1bn, see: Peggy Hollinger, *"Younger CEOs may be an answer to business uncertainty"*, Financial Times, 1 June 2023. Apparently, the average age of CEOs has been falling from 56 to 53, according to headhunter Korn Ferry, while Board seats going to directors under the age of 50 has increased by 50% since 2022, according to executive recruiter Heidrick & Struggles.

[xiii] For some relevant examples of reshoring and new manufacturing in some of the US rust belt areas, see: Derek Brower, James Politi and Amanda Chu, *"The new era of big government: Biden rewrites the rules of economic policy"*, Financial Times, 12 July 2023.

[xiv] Martin Wolf, *"The new interventionism could pose a threat to global trade"*, Financial Times, 15 February 2023. When following the construction & building materials industry over the last few months, it was stunning to what extent large state-sponsored infrastructure projects had been discussed during analyst Q&A in detail, notably by US companies, with the Infrastructure Investment & Jobs Act, the Inflation Reduction Act and the US Chips Act being most frequently mentioned. However, the relevant application at US State level is still an open question, with Texas and North Carolina being highlighted in terms of transport infrastructure investments (Martin Marietta Q2'2023 analyst call on 27 July 2023). Other operators discussed "heavy manufacturing projects" (Vulcan Materials Q2'2023 analyst call on 3 August 2023), pointing to a "golden era of construction in the US" (Albert Manifold, CEO of CRH plc, at the NYSE primary listing of CRH on 25 September 2023) and "new onshoring manufacturing capacity" in the South East of the US, which was one of the major reasons cited for Summit Materials' takeover of Argos USA in early

September 2023 (Summit Materials/Argos USA analyst call on 7 September 2023).

[xv] Daniel Blake, *"Moving towards a multipolar world need not be a bad thing"*, Financial Times, 31 July 2023.

[xvi] For the new ban of some US investment into Chinese quantum computing, advanced chips and artificial intelligence to stop China's military from accessing US technology and capital, see: Demetri Sevastopulo, *"White House unveils ban on US investment in Chinese tech sectors"*, Financial Times, 10 August 2023. When being asked about the new US export control measures implemented in early October, ASML repeatedly pointed to the need of mature notes in China for such megatrends as electrification and green energy while conceding about the most tangible impact being on "regional shipments" in Asia (ASML Q3'2023 analyst call on 18 October 2023). TSMC pointed to higher costs from supply chains due to the "lower level of overseas semiconductor ecosystems", partly reflecting on the company's recent experience with a lack of qualified labour in Arizona (TSMC Q3'2023 analyst call on 19 October 2023).

[xvii] For some relevant statistics on these zombie firms in the US and the decline in total factor productivity growth since 2008, see: Ruchir Sharma, "*The unstoppable rise of government rescues"*, Financial Times, 27 March 2023.

[xviii] For one of the first Western companies openly addressing the danger of US sanctions increasing the risk of IP theft, see the interview with the CEO of ASML, Peter Wennink, in: Anna Gross and Tim Bradshaw, *"ASML chief warns of IP theft risks amid chip sanctions"*, Financial Times, 8 March 2023. In this article, Peter Wennink mentioned that they had to increase spending on cyber security and protecting its IP by a "significant double digit" percentage every year while fending off thousands of security incidents annually. For ASML pointing to one earlier IP theft incident, see: Anna Gross, *"ASML reveals intellectual property theft by China employee"*, Financial Times, 15 February 2023.

[xix] For the Russian-speaking hacker group Clop's sophisticated methods to target flaws in companies' software supply chain, see: Mehul Srivastava, *"Hacker gang Clop deploys extortion tactics against global companies"*, Financial Times, 15 July 2023 and a more extensive investigation of the involvement and financing of hackers by the Russian security services, see: Misha Glenny, *"The untold history of today's Russian-speaking hackers"*, Financial Times, 5 August 2023. Similarly, India was reported to acquire new spyware after the Pegasus software of Israeli NSO Group to target dissidents and critics had been blacklisted by the US government, while seeking to spend up to $120mn through new spyware contracts, see: Mehul Srivastava and Kaye Wiggins, *"India hunts for spyware that rivals controversial Pegasus system"*, Financial Times, 31 March 2023.

[xx] For an ex-Samsung executive having reportedly been arrested for stealing cutting-edge semiconductor technology from its employer to build a copycat plant in China, causing damages of $230mn for Samsung, see: Christian Davies and Song Ju-a, *"Ex-Samsung executive alleged to have stolen tech to recreate chip plant in China"*, Financial Times, 12 June 2023.

[xxi] For the South Korean government's new measures after the ex-Samsung executive's IP theft, see: Christian Davies, Song Jung-a and Eleanor Olcott, *"The South Korean 'master' of chips accused of sharing secrets with China"*, Financial Times, 26 June 2023. In February 2023, the US Department of Justice and Department of Commerce set up a joint task force with the aim of protecting US technology from hostile government actors. Its first criminal charges were brought against a Chinese citizen and former software engineer at Apple, who was accused of stealing trade secrets for autonomous systems used in self-driving cars, see: Stefanie Palma and Miles Johnson, *"US accuses ex-Apple engineer of stealing trade secrets and fleeing to China"*, Financial Times, 17 May 2023.

[xxii] Christian Davies and Song Jung-a, *"South Korea gets tough on tech leaks to China"*, Financial Times, 17 May 2023.

[xxiii] Demetri Sevastopulo, *"Five Eyes spy chiefs warn Silicon Valley over Chinese threat"*, Financial Times, 18 October 2023.

[xxiv] Germany's new government had promised to build 400,000 new homes every year but managed to build only 295,300 dwellings in 2022, leaving the country short of 700,000 homes by summer 2023, see: Guy Chazan, *"'Catastrophic' outlook for German construction adds to Olaf Scholz's woes"*, Financial Times, 17 July 2023.

[xxv] Looking into 2024, most construction and building materials companies we had followed over the last few weeks indicated "flat volumes in the US and Europe, perhaps some moderate growth" (Fernando Gonzalez, CEO of Cemex, at the Q3'2023 analyst call on 26 October 2023) but notably "softer volumes in Europe in 2024", following a volumes decline of 5-6% in 2023 (Jan Jenisch, CEO of Holcim, at the Q3'2023 Trading Update on 27 October 2023). In turn, the CEO of Vulcan Materials, Thomas Hill, maintained that "growth in demand will continue in 2024 despite inflation" and that "large projects are going to move the needle in 2024", which in his view are "speeding up" (Vulcan Materials Q3'2023 analyst call on 26 October 2023).

[xxvi] Rana Foroohar, *"Housing remains America's biggest supply chain problem"*, Financial Times, 16 October 2023. However, while the CEO of Summit Materials, Anne Noonan, claimed that "this country is woefully underbuilt in residential" (Summit Materials/Argos USA analyst call, 7 September 2023), others expect an "inflection in housing

construction in the fourth quarter of 2023" (Howard Nye, CEO of Martin Marietta, at the Q2'2023 analyst call on 27 July 2023). The CEO of Vulcan Materials, Thomas Hill, observed a "recent growth in single-family housing" but the issue of affordability due to high mortgage rates remains (Vulcan Materials Q3'2023 analyst call on 26 October 2023). Similarly, the CEO of Holcim, Jan Jenisch, maintained that an 8% 30 years' mortgage rate in the US has a huge impact on American residential housing (Holcim Q3'2023 Trading Update, 27 October 2023).

[xxvii] The CEO of Holcim, Jan Jenisch, described the current situation being "still (in a) high inflationary environment for a lot of costs" (Holcim Q3'2023 Trading Update on 27 October 2023). In turn, the CEO of Cemex, Fernando Gonzalez, outlined 2023 input cost inflation trading down from 18-23% at the start of the year to currently 10-11%, whereas pricing was up by 18-20% year-to-date (Cemex Q3'2023 analyst call on 26 October 2023).

[xxviii] In the US market, the strong pricing environment is also driven by capacity limitations due to permit restrictions and demand outpacing supply, particularly for heavy materials (cement, concrete & aggregates) given the amount of huge infrastructure projects and non-residential construction in manufacturing (battery and semiconductor factories). Against the backdrop of supply issues in California and Nevada, Eagle Materials even acquired a cement import terminal at Stockton, California for $55mn as well as announced a new price increase for cement as of 1 January 2024, in the range of $10-15 per tonne, following net sales prices for cement being up by 15% at Q2'FY24 (Michael Haack, CEO of Eagle Materials, at the Q2'FY24 analyst call on 26 October 2023).

[xxix] Amanda Chu, *"Labour shortage endangers Biden's big plans for US building boom"*, Financial Times, 20 February 2023. Similarly, construction project cancellations in Germany reached 20.7% in August 2023 (compared with 18.9% in July) and the lack of new orders was reported by 44.2% of German construction companies in August (40.3% in July and 13.8% a year ago), see: Martin Arnold, *"German builders warn of crisis as they scrap record number of projects"*, Financial Times, 12 September 2023.

[xxx] The problem of "insufficiently qualified labour" in Arizona was cited as one of the main issues – next to labour costs overseas being "little higher than we expected" – for the completion of the new TSMC fab to be delayed by one year to 2025 (Mark Liu, Chairman of TSMC, at the Q2'2023 analyst call on 20 July 2023).

[xxxi] The only US company which disputed labour shortages holding up big infrastructure and manufacturing projects was Vulcan Materials, with its CEO, Thomas Hill, pointing to an "accelerating growth in public activity" and reporting state budgets in Texas being up by 20% year-on-year, Florida by 21%, Alabama by 23% and California by 5% but 50% over the last three years, with local authorities making every effort to speed up investments into construction of highways, railways and other infrastructure (Vulcan Materials Q3'2023 analyst call on 26 October 2023). Interestingly, the CEO of Holcim, Jan Jenisch, also pointed to "huge nearshoring in Mexico", notably the manufacturing of white goods for the US market (Holcim Q3'2023 Trading Update on 27 October 2023), while the CEO of Cemex, Fernando Gonzalez, linked the higher infrastructure spending in Mexico to the forthcoming elections in 2024 (Cemex Q3'2023 analyst call on 26 October 2023).

[xxxii] Holcim itself has increased the share of North America in net sales to 40%, indicating its preference not only for faster permits and less bureaucracy but also higher margins and significant state subsidies. At the same time, Holcim reportedly received six out of 10 EU grants for carbon capture, usage and storage over the last 14 months and it has advanced to 17% usage of recycled construction materials (Jan Jenisch, CEO of Holcim, at the Q3'2023 Trading Update on 27 October 2023). Similarly, Heidelberg Materials aims for the "best decarbonised product" but conceded that it will need to convince its customers first (Dominik von Achten, CEO of Heidelberg Materials, at the H1'2023 analyst call on 27 July 2023). In turn, in the words of the CEO of Hochtief, Marcelino Fernandez Verdes, "construction markets are now embracing sustainability" and he has the vision to "offer carbon-free cement at scale" (Hochtief H1'2023 analyst call on 25 July 2023).

[xxxiii] The CFO of Cemex, Maher Al-Haffar, claimed that they had achieved an IRR of up to 40% from investing in recent organic growth projects, which compares with a cost of equity of 15% and a cost of debt of 7% (Cemex Q3'2023 analyst call on 26 October 2023). On share buy-backs not being a substitute for thoughtful investment in growth, see also: Brooke Masters, *"Share buy-backs need less hate and more scrutiny"*, Financial Times, 17 May 2023.

[xxxiv] Michela Tindera and Brooke Masters, *"The controversy around share buy-backs"*, Financial Times Podcast, 16 August 2023. For companies entering into oblique contracts with brokers that can cost more than buying back shares in the open market, see also: Brooke Masters, *"If companies are going to buy back shares, they should pay a fair price"*, Financial Times, 22 July 2023.

[xxxv] Michael Seigne and Joerg Osterrieder, *The Great Deception: A Comprehensive Study of Execution Strategies in Corporate Share Buy-Backs,* Candor Partners Limited, United Kingdom, 2023. The decline in US share buy-backs in Q2'2023 has been estimated to amount to 20% year-on-year, see: Nicholas Megaw, *"Companies ease off on share*

buy-backs as rising interest rates push up costs", Financial Times, 17 September 2023.
[xxxvi] Stefania Palma and Patrick Temple-West, "US private funds face more disclosures under new SEC rule", Financial Times, 3 May 2023.
[xxxvii] James Politi, *"Joe Biden to revive plan for billionaire tax in State of the Union address"*, Financial Times, 7 February 2023.

[xxxix] *"Dutch lawmakers back tax on share buybacks to cover higher minimum wage"*, Reuters, 25 September 2023. When senior management of KPN was asked about the newly proposed Dutch tax on share buy-backs, the CFO, Chris Figee, responded that – in case this will be adopted – "we will shift away from share buy-backs to dividends" (KPN Q3'2023 analyst call on 25 October 2023).
[xl] Please note that one of the authors of this market commentary has been a director at KPMG Advisory between July 2013 and February 2017, setting up his own independent advisory firm after the EU Directive to address conflicts of interest at auditing firms in January 2017 and the EU Statutory Audit Reform on issues of cost, concentration and competition: https://www.europarl.europa.eu/RegData/etudes/STUD/2019/631057/IPOL_STU(2019)631057_EN.pdf. In this analysis, we rely solely on publicly available information and reflect predominantly on the growing risk and repercussions of conflicted audits from a professional fund manager's perspective.
[xli] Mercedes Ruehl and Olaf Storbeck, *"Wirecard's auditor EY was too gullible, Singapore suspect claims"*, Financial Times, 2 August 2023.
[xlii] Stephen Foley, *"Three failed US banks had one thing in common: KPMG"*, Financial Times, 3 May 2023.
[xliii] A good example of this is the recent scandal at PwC Australia, involving the misuse of government tax secrets for providing information advantage to their own clients, see: Stephen Foley, *"PwC Australia's culture attacked in tax leak scandal report"*, Financial Times, 27 September 2023.
[xliv] Stephen Foley and Michael O'Dwyer, "*PwC to curtail consulting work for US audit clients to reduce conflict of interest"*, Financial Times, 11 September 2023.
[xlv] For issues of the German audit reform after the Wirecard collapse, see: Olaf Storbeck, *"The paradoxical lessons from EY's punishment over Wirecard"*, Financial Times, 4 May 2023.
[xlvi] Camilla Hodgson, *"Accounting firms accused of missing climate risks in company audits"*, Financial Times, 18 July 2023.
[xlvii] The attempted break-up of EY ultimately failed, leading to a highly contested race for the new global chief executive's position after the resignation of Carmine de Sibio in the wake of the collapse of his break-up plan, see: Stephen Foley, *"EY sets up six-way race to lead firm after break-up failure"*, Financial Times, 29 September 2023.
[xlviii] Stephen Foley and Michael O'Dwyer, *"Accounting firms question the partnership model"*, Financial Times, 30 June 2023.
[xlix] For a representative example of the Austrian investor protection association, IVA, enquiring specifically about the prevention of corruption ahead of the 2023 AGM season and a fairly vague reference to its Business Ethics Code by the oil & gas company OMV, see: https://www.iva.or.at/downloads/schwerpunktfragen/2023/hv-fragen_omv.pdf. Activist investors often take a leading role in discovering conflicts of interest and raising their voice against corrupt cases and fraud, see the claims made by Petrus Advisers in terms of related-party lending to the management of Austrian bank BAWAG in June 2023: https://petrusadvisers.com/media/20230630_-_bawag_-_letter_to_eba_vf_-_eng.pdf.
[l] For an extensive discussion of fraud and corruption at the top of the Altice empire, see: Robert Smith et.al., "*Altice fraud arrest throw spotlight on Patrick Drahi's elusive right-hand man"*, Financial Times, 31 July 2023.
[li] A good example of the kind of risk professional fund managers might face is the German copper producer Aurubis, reporting in late August that it had identified "discrepancies in stockpiles and shipments of metal tied to the recycling business in Hamburg", while pointing to "criminal activity" and damages "in the low three-digit-million-euro-range", see: Harry Dempsey, *"Europe's largest copper producer says it has been victim of huge theft"*, Financial Times, 1 September 2023. The shortfall was eventually disclosed to amount to EUR 185mn, with Germany's State Office of Criminal Investigation still investigating, but – by the time of writing - the share price has mostly recovered since its downfall in early September 2023: https://www.aurubis.com/en/media/press-releases/press-releases-2023/aurubis-ag-extraordinary-inventory-completed-and-new-forecast-for-2022-23-fiscal-year. In the wake of the Swiss government-engineered takeover of Credit Suisse by UBS and the ongoing reputational damage of Switzerland as a financial marketplace, it is perhaps no surprise that the finance minister, Karin Keller-Sutter, unveiled sweeping measures to close down on money laundering in late August 2023, see: Sam Jones, *"Switzerland unveils money*

laundering clampdown", Financial Times, 31 August 2023.

[lii] For an example of Indonesia refusing to share information gathered in an investigation into Bombardier after the country has been left out of an earlier Airbus settlement in the UK, see: Peggy Hollinger, *"The fight against global corporate graft needs to aim higher"*, Financial Times, 1 March 2023. For first efforts in setting up a new global corruption court, which focuses more on autocratic leaders in developing nations, but which Western companies can't avoid when operating in those countries, see: Peter Hain, *"The time for instituting a new global corruption court is now"*, Financial Times, 16 August 2023.

[liii] Benjamin Parkin, Rachel Millard and Sylvia Pfeiffer, *"India files criminal complaint against Rolls-Royce and BAE"*, Financial Times, 30 May 2023.

[liv] Ian Johnston and Laura Dubois, *"Drug gangs infiltrating shipping supply chains, warns Maersk executive"*, Financial Times, 18 October 2023.

[lv] Anna Gross, *"'No taboos' over mergers in EU telecoms shake-up, says Breton"*, Financial Times, 28 February 2023. The CEO of Deutsche Telekom, Tim Höttges, made the case for more consolidation by pointing to 67 mobile operators in Europe, with 35 being with less than 500,000 customers (Deutsche Telekom Q2'2023 analyst call on 10 August 2023). When asked about M&A opportunities for his company in Europe, the CEO of Telefonica, Jose Maria Alvarez-Pallete, outlined "in-market consolidation in Spain and the UK" (Telefonica Q2'2023 analyst call on 27 July 2023).

[lvi] https://ec.europa.eu/commission/presscorner/detail/en/ip_23_3421

[lvii] When asked about an update on the proposed merger with MasMovil in Spain in late July, the CEO of Orange, Christel Heydemann, just pointed to the need to gain more market share before Orange would be able to invest (Orange H1'2023 analyst call on 26 July 2023). The latest attempt to test the current regulatory mood in Europe has come from Vodafone's plan to merge its UK business with its smaller rival Three, see: Nic Fildes, *"Telecoms face mounting pressure to consolidate"*, Financial Times, 8 August 2023.

[lviii] In the wake of their most recent profit warnings, it is interesting to note that network infrastructure and service providers such as Ericsson and Nokia have become more vocal about "5G investments in Europe (having) been very slow" and that "operators need catalysts to monetise more revenues" (Börje Ekholm, CEO of Ericsson, at the Q3'2023 analyst call on 17 October 2023). Equally, the CEO of Nokia, Pekka Lundmark, pointed to the fact that "operators are hesitant to invest in the 5G roll-out and are slow to monetise on that" (Nokia Q3'2023 analyst call on 19 October 2023). Similarly in the US, where the CEO of AT&T, John Stankey, complained that "metropolitan areas have not an optimal structure in fiber and broadband yet" (AT&T Q3'2023 analyst call on 19 October 2023) while the CEO of Verizon, Hans Vestberg, outlined that "fibre remains a coveted, high-quality service" but fretted, at the same time, about a "muted upgrade activity, which is something we need to watch in future" (Verizon Q3'2023 analyst call on 24 October 2023).

[lix] Daniel Hajj Aboumrad, CEO of America Movil, at the Q3'2023 analyst call on 18 October 2023.

[lx] Hans Vestberg, CEO of Verizon, at the Q3'2023 analyst call on 24 October 2023. This was a topic Hans Vestberg had already mentioned at the previous quarterly results call, when he pointed out that private wireless is replacing WLAN as there are increasingly security issues for enterprises (Verizon Q2'2023 analyst call on 25 July 2023).

[lxi] Yasemin Craggs Mersinoglu and Javier Espinoza, *"European telecom groups ask Brussels to make Big Tech pay for more networks"*, Financial Times, 2 October 2023.

[lxii] Deutsche Telekom Q2'2023 analyst call on 10 August 2023. Among the infrastructure and network services providers, the CEO of Ericsson, Börje Ekholm, emphasised that "best effort connectivity" is no longer acceptable and that "5G has become a critical tool" (Ericsson Q3'2023 analyst call on 17 October 2023). As data traffic continues to grow, networks need to be modernised, outlining specific opportunities to monetise 5G networks in enterprise digitalisation and horizontal platforms. The latter theme was reiterated by the CEO of Nokia, Pekka Lundmark, who elaborated on the need for networks to "become more programmable" and that, in this respect, "real use cases need to be built" (Nokia Q3'2023 analyst call on 19 October 2023).

[lxiii] The CEO of BT Group, Philip Jansen, outlined his ambition to "transform into future AI capabilities" at the FY2023 analyst call on 18 May 2023.

[lxiv] The much easier access to online brokers nowadays but also the digital impact on investment behaviour and the sourcing of information by GenZ was highlighted in a pioneering survey by Monika Kovarova-Simecek et.al., *GenZ und der Kapitalmarkt. Investitions-und Informationsverhalten der Generation Z im Vergleich zu anderen Generationen in Österreich*, Fachhochschule St.Pölten, 15 May 2023.

[lxv] Leo Lewis, *"Gen-X bankers warn Gen-Z content creators: don't give up the day job"*, Financial Times, 24 April 2023.

[lxvi] Patrick McGee, *"How Apple captured GenZ in the US – and changed their social circles"*, Financial Times, 21

February 2023.
[lxvii] John Burn-Murdoch, *"Boomers and millennials have each other's backs"*, Financial Times, 6 October 2023.
[lxviii] Andrew Edgecliffe-Johnson, *"You can't pin workforce problems all on GenZ"*, Financial Times, 22 May 2023.
[lxix] Isabel Berwick, *"Stop moaning about GenZ grads – they might teach us something"*, Financial Times, 7 May 2023.
[lxx] Joe Miller, *"Big Law falls out of fashion with idealistic GenZ"*, Financial Times, 10 May 2023.
[lxxi] For a representative survey, where the home ownership rate of millennials was 23% below that of baby boomers at the same age in the UK and 10% lower in the US, see: John Burn-Murdoch, *"Millennials are not as badly off as they think – but success is bittersweet"*, Financial Times, 6 April 2023.