Market Commentary Blog

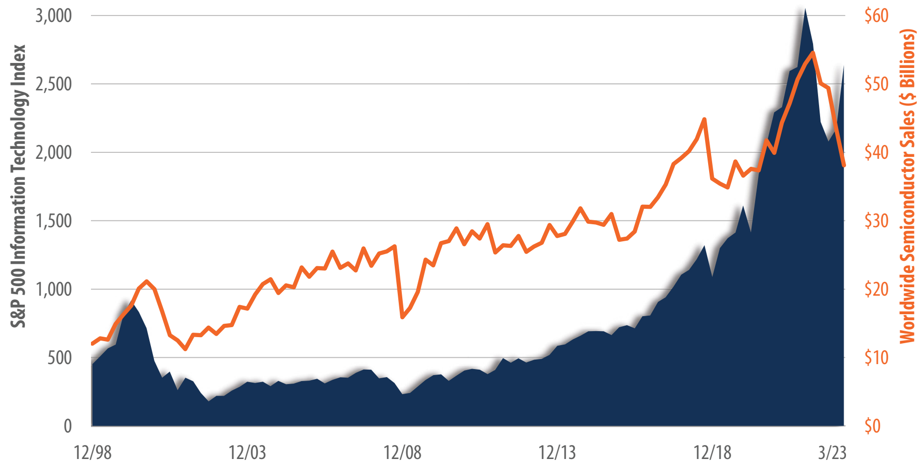
Cash Flow *and Carey*

Robert Carey, CFA
Chief Market Strategist

4/20/23

Technology Stocks And Semiconductors

Worldwide Semiconductor Sales vs. S&P 500 Information Technology Index (Price-Only)



Source: Bloomberg. Quarterly Data Points from 12/31/1998 through 3/31/2023. **Past performance is no guarantee of future results.**

View from the Observation Deck

Tracking the direction of worldwide semiconductor sales can provide investors with additional insight into the potential demand for tech-oriented products and the overall climate for technology stocks, in our opinion. Semiconductors play an integral role in most tech-oriented products, particularly in today's mobile device product lines, such as smartphones, tablets, and wearables. We see that integral role playing out in artificial intelligence, robotics, industrial control systems, and the expansive network that the data we consume flows through each day.

The recent divergent trend between global sales of semiconductors and the performance of the S&P 500 Information Technology Index appears to be an anomaly.

As observed over the totality of today's chart, which goes back to 12/31/1998, the two metrics typically exhibit an increased correlation. While a myriad of factors could explain the inversion noted, two of them stand out, in our opinion. The first is the spike in semiconductor demand during the COVID-19 pandemic, and the second is the revaluation of technology companies as interest rates rocketed off their lows in 2022.

Semiconductors experienced record sales in 2021 and 2022.

Amidst unprecedented demand, the Semiconductor Industry Association (SIA) reported that worldwide semiconductor sales surged by a whopping 26.2% to settle at a record $555.9 billion in 2021. In 2022, sales grew a further 3.3%, to set another record at $574 billion. In 2023, driven by weakened consumer demand and rising inflation, the SIA reported that global semiconductor sales decreased 20.7% year-over-year to $39.7 billion in February 2023, according to its own release. It was the sixth consecutive month of declining semiconductor sales. The World Semiconductor Trade Statistics (WSTS) organization estimates annual global sales to decline by 4.1% in 2023.

Technology stocks are a top-performing sector on a total return basis year-to-date.

In a previous post (Click here to read "The Only Constant Is Change"), we noted that an easing in the chips shortage and lower interest rates across much of the yield curve had likely boosted the valuations of technology stocks, propelling the S&P 500 Information Technology Index to the top of the list in terms of total return through Q1'23. In our view, these factors remain in play today, and could be one of the reasons why, despite a slowdown in semiconductor sales, the performance of technology stocks has shown resilience.

Takeaway

With a total return of 20.99% year-to-date through 4/18/23, the S&P 500 Information Technology Index is the second-best performing sector in the S&P 500 index thus far, trailing only the S&P 500 Consumer Discretionary Index which posted a total return of 21.94% over the same period. Should sales of semiconductors slow as forecast, the decline would come on the heels of back-to-back record-setting sales years. Furthermore, as cyclical sectors are typically more sensitive to interest rates, we think that increases to the federal funds target rate by the Federal Reserve ("Fed") could have an outsized impact on the valuations of technology companies going forward. Conversely, current valuations would receive support if the Fed were to cut rates at some point this year.