Investment Commentary

THE NEXT TRADE

You are only as good as your last trade is an old adage about short-termism that is a helpful foil for us and our investment approach at times of great uncertainty.

We are at a turning point following the devastating impact of the pandemic on our economies and lives. Governments and central banks have taken significant steps to support economies and livelihoods that have been affected by the measure to close down economies and protect our populations. Vaccines are being implemented and are having a positive impact despite the issues around changing variants and potential side effects.

The longer-term the approach the clearer the perspective. The sad death of Prince Philip, Duke of Edinburgh, is a marker that the second Elizabethan age, a way of describing the post-war period, is gradually drawing to its close. It has been a period of great turmoil and conflict but also one of great hope, innovation and prosperity, not least in the dramatic increases in life expectancy and in the performance of markets over that time. The rivalry between powers, political and social unrest and other adversity we face today is no different than that experienced by previous generations and we have no doubt that we will have to face them in future as well.

The United States is on track to administer 200 million doses by President Biden's 100th day in office. According to the AARP (American Association of Retired Persons), 80% of over 65-year-olds in the US are already vaccinated and at the current pace the US is on a trajectory to achieve 80% vaccination of its population by mid-July, an important threshold for herd immunity. The US has proven its ability to innovate and produce at scale and the discourse is already shifting to what the government will do with the billions of excess vaccine doses that will be produced through this year. Given the issues in Europe and elsewhere it is striking that once again the New World may come to the rescue of the Old.

The companies we are invested in have reported strong results and vigorous demand for their products and services. Our long-term perspective and our fundamental approach is why we are optimistic about the global economy and about the prospects for our investments. We trade very little and for fundamental reasons only, so each trade matters.

For us market volatility and sector rotation are opportunities. Last year we bought 'value' as in 'value/growth', industrial, consumer and healthcare companies that had been impacted by the short-term impact of the pandemic and that had the promises of significant rebounds in their sales and earnings. This year we have bought 'growth' that has been left behind by the sector rotation. Market short-termism has allowed us to buy a position in *Salesforce*, the leading software platform that we had been looking to buy for many years but held off until now because of its valuation, at much cheaper prices than before.

We invest in quality and value for the long term so for us the next trade is always the same as the last: to buy companies with strong and sustainable competitive positions, in good and growing markets, with managements with a record of value creation and balance sheets so strong as to whether any adversity, including the present. As we write, the sector rotation

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appears to have reversed and many of our less cyclical and higher growth companies are performing strongly.

The year to come will continue to be challenging and we have to hope that the vaccine rollout will be effective in reaching people and addressing the issues of variants and side effects as our analysis indicates so that economies can open up throughout the year. We are confident in the quality and value of the companies that we have invested in and will continue to focus on the fundamentals to take advantage of opportunities as they arise.

World Stars Global Equities

Our World Stars strategy continued its positive performance in March, closing the month up 3.0% in US dollar terms.

March saw a continuation of the sharp rotation towards 'value' stocks in the wider equity market, which has been a feature of the first quarter. In the US equity market, for example, 'value' stocks have outperformed 'growth' by c. 20% since early January.

Performance was broad based. Given the rotation it was mostly driven by companies that are more closely linked to a substantial economic recovery such as industrials and consumer, although some of our digital companies performed as well buoyed by strong results and other news.

Leading our World Stars portfolio was *Facebook*, up 14%, which continued to demonstrate the breadth of its operating model, with the announcement that there are now over one million e-Shops registered on its platform with over 250 million active buyers. As the company seeks to develop its presence in e-commerce and monetise its user base, the news was validation of its efforts in the field and its ability to develop incremental revenue streams in the form of commissions from sales generated, as well as growing its advertising base.

Mobile tower owner, *American Tower,* rebounded by 11%. The company has signed an agreement with DISH Corporation in the US allowing DISH to lease space in up to 20,000 of American Tower's sites, as it seeks to expand its 5G wireless infrastructure, securing a further revenue stream for American Tower.

Within the broader industrial space, specialty chemicals provider *Sika* was up 12%, underpinned by expectations it will benefit from increased infrastructure spend going forward, with the Biden administration unveiling its plans for a USD 2 trillion infrastructure and climate investment program. The company is also well set to benefit from its position as a provider of sustainable construction solutions as well as the upcoming recovery in the automotive market. Importantly, it continues to deliver on its cost optimisation plans and having de-levered from the Parex acquisition, it maintains flexibility for further M&A going forward.

Within consumer staples, *Nestlé* also rebounded strongly. The company continues to reposition its business towards the most attractive structural end markets with the sale of its North American water business marking the disposal of the more commoditised part of its water franchise. This follows earlier similar moves, including the sale of the Chinese peanut milk business, Yinlu, with the proceeds being deployed to increase the company's presence in the health & wellness categories, as well as new distribution channels. We believe these strategic moves, coupled with an invigorated R&D pipeline, should help the company to achieve its target of re-accelerating its top line back to mid-single levels.

Performing strongly also within the broader consumer staples industry was *Givaudan*, the leading flavours & fragrances player. The stock had lagged a bit recently after a strong showing in 2020. The company remains a classic compounder, driven by structural trends in the consumer industry, including the shifts to health & wellness, active beauty and natural ingredients. We believe the stock will continue to be driven by the associated growth in underlying earnings.

Within the luxury space, *LVMH*, continued to test new highs as the luxury market remains one of the most resilient within the broader consumer space. Since the end of March it has reported very strong Q1 sales, up 30% on an organic basis, led by the US and Asia ex-Japan.

On the weaker side during the month was gaming software developer *Activision*. The stock benefited last year as consumers stayed at home with video gaming emerging as a key form of at-home entertainment. With vaccination rates picking up and countries starting to progressively re-open the stock has lagged more recently. Looking forward however, we believe that Activision will be able to leverage on its significantly expanded user base as more people got introduced to gaming during Covid-19. This increased user base, coupled with the solid pipeline of new game introductions, positions the name well for the months ahead. Also on the weaker side during March was *Visa*, as the US Department of Justice announced an inquiry into the company's debit card practices. This is not the first time that the payment networks have come under investigation for anti-competitive practices, with concerns arising from the inherent strength of their competitive positioning and the oligopolistic nature of the industry. We would expect any inquiry to be settled in the same way as historic investigations, with moderate financial or business impact on the payment companies.

Multi-Asset Income

Following from the strength of the previous month, the Multi-Asset income strategy had another positive month finishing up 1.2% in US dollar terms (up 1.5% since the start of the year). However, the month of March was marked by higher volatility and whilst equities finished strongly, up 2.7% in US dollar terms (up 3.2% year to date), our fixed income portfolio ended the month on a slightly weaker note, down 0.5% (still up 0.5% since the start of the year). Non-correlated assets also had a strong month with a positive performance of +1.6% (now up 1% for the year).

The equity portfolio benefited from the strong contribution from the more economical sensitive companies, while the digital transformation names were somewhat lagging, supporting the rotation trend witnessed earlier in the year. The further positive news around the Covid-19 vaccine deployment and the substantial fiscal package being prepared by the new US government were significant sources of support to equity markets.

Prospects of a substantial economic surge in the second part of the year resulted in US 10-year bond yields rising rapidly to new highs for the year of around 1.75%. This triggered some weakness in the asset class, with the higher quality most secured part of the market correcting downwards, and subsequently dragging down the high yielding bond segment. The weakness was broad across emerging markets and developed markets. Turkey saw some profit taking following the resignation of the governor of the central bank (see EM bonds commentary).

Looking ahead, the re-opening of the global economy in the second part of the year should bring further positive news on the corporate front and we are very comfortable that our investments both on the equity and the credit sides will reap the benefits as strong companies will strengthen.

We are nonetheless very aware that positive economic developments also mean ultimately higher bond yields. Although this is a positive development signalling the 'back to normal', it also could increase volatility.

Emerging Market Bonds

Yields on the benchmark 10-year treasury note rose another 0.3% over the month of March against an optimistic backdrop in the US, supported by the rapid deployment of vaccines and good economic data. The impact of the rate rise resulted in further pressure on fixed income assets including our emerging markets bonds portfolio, which was down -0.4% for the month, taking year-to-date performance to -0.5%.

At the issuer level, one of the largest contributors to performance was *TV Azteca,* which recovered 7.5% after the weak performance in February. *Tullow Oil*, a position which we added to the portfolio last month also performed well, returning 6.5%. There was also significant demand for the new notes (5.5x oversubscribed) of *Liquid Telecom*, which helped the bonds return 4.3% in March.

The biggest detractors from performance came from our Turkish names, specifically *Sisecam, Koc*, and *Turkcell*. Turkey's president, Erdogan announced another replacement of the central bank governor, two days after the bank hiked interest rates to curb rising inflation and a depreciating lira. This is the third replacement in less than two years, and increased concerns around central bank credibility, potential policy change, and consequences for the Turkish lira and balance of payments. That said, we are comfortable with the underlying credit quality of the Turkish corporates within our portfolio and view the sell-off as another opportunity to add new high-quality Turkish issuers to our portfolio at attractive yields.

While there is likely to be interest rate volatility going forward, we expect further rate increases to be more muted in the short-term and our outlook for emerging market corporate bonds remains positive, with our portfolio still offering an attractive current yield of 6.6% for less than three years duration.

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