Q1 2024 - Global Value Quarterly Update

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Hello, my name is Ben Silver. I'm a co-portfolio manager on our Global strategies, and I'm going to take the next few minutes to take you through what happened in the first quarter calendar of 2024.

Markets were strong globally, with developed markets doing particularly well. They were led by the US, which was really driven by moderating inflation, as well as an expectation that the Federal Reserve will start to cut rates. A similar sentiment was observed in the UK and Europe, along with a milder winter, which led to lower energy prices. The Japanese market was also quite strong due to expectations of stronger earnings coming from a weaker yen, as well as more inflation.

Growth was actually quite strong in the quarter, although the "Magnificent 7" turned into the "Fab 4." They did lead and were the main factor in our underperformance versus the broader market. Financials and Industrials were the strongest sectors, really driven by, on the financial side, benign credit costs, as well as strong earnings and expectations of rate cuts.

The strongest performer in the quarter was money center bank Citigroup. Along with those factors I just mentioned, they also announced an expectation of lower expenses, between $500 million and $700 million for calendar 2024, as part of their larger expense reduction expectation of over $2 billion over the next few years.

Also contributing was Daimler Truck. Their Mercedes-Benz division, which is their European division, showed very strong margins. They've done a nice job since separating from their parent company in terms of managing costs and focusing on their business, and it showed in their performance for the quarter.

Lastly, electronic assembler Hon Hai was also quite strong. They are showing share gains in the iPhone business based on their expansion in India, and their server business showed really explosive growth of somewhere close to 40%, driven by AI. They expect some share gains from Nvidia’s new GP platform.

Communication services and consumer staples were the weakest sectors. Charter Communications, a US cable company, was the largest detractor in the quarter. It was driven by continued losses in subscriptions to fixed wireless, as well as uncertainty around their ACP program, which was a subsidy for some of their customers, and an announced increase in capex. Most of these things are in the range of outcomes that we expected when we first made the investment, so we're still confident in the position, and we've added to it during the quarter.

Also weak was Randstad, the staffing company, really due to organic declines in the US and Germany. This is a continuation of the weakness in the market. They continue to operate the business very well from a cash flow standpoint, as well as expenses, and continue to be a leader in the industry. Brazilian brewer Ambev was also weak as they dealt with the devaluation of the Argentine peso, as well as a weaker currency in general and a change in tax rules in Brazil. There are some moderating factors that can go along with this, and there are some offsets. They've done very well in terms of protecting volume and share in the industry, and we're still confident in the investment.

We initiated a couple of new positions in the quarter. The first one is Tyson Foods, the largest meat processor in the US. They're in four different businesses: beef, hog, chicken, and prepared foods. The first three businesses all generated no earnings, and they've had almost the worst fiscal year in their history because of this. It's a unique set of events that happened here. The start of inflation in cattle feed led cattle ranchers to slaughter a lot of meat, so there wasn't enough volume, which really hurt the processors. They mistakenly thought this would lead to increased chicken consumption, so they added capacity in chicken, which never happened. They also added capacity in hogs and pork because of the African swine flu that decimated the Chinese herd, but that capacity came back very quickly, leaving the whole industry with massive excess capacity.

We also added CVS, which operates in three main businesses. They're the largest retail pharmacy in the US, have the largest PBM in Caremark, and have a significant HMO in Aetna. All three businesses are going through challenges. The reason they put these businesses together is to focus on reducing costs in the healthcare system through scale and working together in these three different parts of the industry. Just taking them one by one: the retail pharmacy has been under pressure for years from the payers, which are the PBMs. The result of this is Rite Aid, one of their competitors, has recently gone bankrupt. We think the overall pressure on drugs and generics should moderate, as there's not much left to squeeze out of the system, and it's not really good for the whole system to have a lack of choice in that area.

The PBMs are always under political pressure, but that business model has changed dramatically too. It used to focus on making money off generics in the system, but it's really moved to specialty pharma, where 1% of the population is driving 50% of the spend. So, their value add is really controlling costs in that area, and we think they'll continue to do that.

On the HMO side, increased utilization, especially in the Medicare Advantage part of the business, has really hurt. We do think that part of the business will go back to profitability, the historical profitability they've exhibited with controlling the plan as well as other expenses. We like the stock a lot. It's very cheap, and we've added it to the portfolio.

We also added to our Chinese exposure. As we've spoken about before, while developed markets rallied, and even emerging markets ex-China did well, China continues to suffer under the threats of a real estate bubble, as well as intervention by the government and political threats. The market is very cheap, and we're adding selectively to global. In doing that, we added to KI and Galaxy during the quarter, as well as Magna Auto Parts, which is more of a developed market company. We funded this through trims of Webtech and Acore, as well as Michelin, all on strength. We sold out of Volkswagen, and as I said last quarter, the range of outcomes has really widened with that company. When they purchased the Chinese EV maker, it really called into question the value of all the money they've spent on their R&D efforts in this area, as well as moving away from their divestiture plan.

So, that's a wrap for the quarter. Thank you for spending these last few minutes with me, and I'll see you next quarter. Bye-bye.

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