

Q4 2023 - International Value Quarterly Update

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I'm Allison Fisch, a co-portfolio manager on our International strategies.

The fourth quarter turned out to be a very good quarter for international markets. What we saw was inflation beginning to slow down in a lot of the world, and so expectations that interest rates could be coming down as well. That, coupled with lower energy prices, led to a rallying of most non-US markets as well as in the US.

Now, the exception to that was within China, where the weakness continues that we've seen for much of the last several years, with fears around the property markets, the macro, and the direction of, of government policy, as well as the economy being in question in the minds of most global investors.

In this backdrop, we saw growth stocks outperform value stocks, largely because of the expectation of those interest rates coming down, and along with it, the idea that discount rates could be coming down as well. With all of this in mind, our portfolios somewhat underperformed the broader index, um, with a lot of puts and takes, largely due to company-specific reasons.

When we look at where were the sources of weakness in the portfolio, you see anything China-related being somewhat weak. So, looking at our portfolios, our positions in Alibaba were detractors during the quarter, part of that again due to sentiment, but also because of company-specific performance reasons as we saw the incremental market share, um, being donated essentially by Alibaba to its competitors.

Also a source of weakness within the portfolio: Julius Baer, the Swiss wealth management firm. This is a great business that we think should be gaining share, given what's happened to Credit Suisse, uh, in the last year. However, in the quarter, they reported a big loss due to the bankruptcy of Signa, an Austrian property conglomerate to whom they had made a rather large amount of loans. Um, the size of this exposure, while not that damaging to the company's long-term earnings potential, is damaging to the sentiment in investors' minds because it calls into question the risk controls at the bank. And we saw pretty significant weakness in the stock price around that announcement.

Another detractor in the portfolio was Nokia in the telecom equipment space. Uh, this one was also a detractor in the third quarter, though this quarter it was due to them losing out on a large 5G contract with AT&T, which is one of its more profitable customers.

The portfolio overall did return positively, and some of the biggest contributors in the quarter, uh, came largely from our European names. So, that includes Rexel, which is a distributor of low-voltage electronic equipment. This company reported strong earnings in the quarter, and also, because of this improving sentiment around European macro, these sort of highly cyclical industrial names like Rexel performed quite well.

Um, also performing strongly in the quarter was Sainsbury's, the UK grocer. They posted good results in the grocery segment, largely offsetting some softness that they're still seeing on the general merchandise side.

In terms of activity in the portfolio, we added a new name: Teleperformance, which is an outsourced customer service provider, so the people that you talk to when you call the customer service line, essentially. Uh, this is a strong business, and they've got a, a very good and growing market share. The fear in the name is around artificial intelligence—that this business could basically be completely disrupted by an AI solution. We believe those fears are overblown. Um, if anything, AI can help to strengthen this business and strengthen the idea of using an outsourced option, so we were happy to add it to the portfolio.

In light of the weakness in China, we also added China Merchants Bank. Across the board, this is one of the leading retail banking franchises in China, with a very strong deposit franchise. Really, it's gotten cheap enough for us because of the negative sentiment around the entire geography.

When we look across our portfolio, we see it positioned largely in cyclical names still, given where we are in the cycle and where the fears are in investors' minds. And the opportunity for value stocks on the international side of the market remains extremely strong, with valuation spreads near all-time historic levels. We're looking forward to 2024.