Monthly Market Commentary

Global equity markets performed very well in the first quarter with strength broadening throughout the period. Many developed world indices reached fresh all-time highs as a combination of, amongst others, AI enthusiasm and rising hopes of a US soft landing contributed to the positive sentiment.

Japan's Nikkei225 was the standout performer, finishing up 20.6%, and finally eclipsing its previous 1989 record high. Fuelling this strength had been signs that after years of moribund pricing in the general economy, inflation was finally taking hold. Also influential was greater interest from overseas investors following broader recognition of a series of structural reforms spearheaded by the Tokyo Stock Exchange aimed at improving corporate governance across listed Japan Inc.

US large caps delivered an impressive quarter's performance with the S&P500 and NASDAQ up 10.2% and 9.1% respectively. Both indices set new record highs in March, as did the S&P500 Equal Weight Index demonstrating the degree of breadth improving. For now, investors seem happy to focus on decent economic data, dismissing several stronger-than-expected inflation prints which scaled back investors' expectations of Fed easing. US small caps struggled in a relative sense but made up some lost ground in March to close the quarter up 2%.

European bourses were mixed. Germany's DAX led performance (+10.4%) with, amongst other factors, ECB rate cut expectations helping propel the index to new highs. France's CAC40 also did well, up 8.8% also setting new highs. In contrast, the UK FTSE100 meaningfully underperformed, finishing up just 2.8% for the quarter, weighed down by the softer economic backdrop.

China's Shanghai Composite Index also struggled to deliver much in the way of performance. While it finished up 2.2% over the quarter, performance was very volatile on a monthly basis as ongoing debt issues, a sluggish economy, and geopolitical tensions weighed on sentiment towards Chinese equities.

Performance on a sector basis broadly reflected the above themes with Information Technology and Communications both up more than 12% thanks to the AI/Magnificant-7 exposure. Energy, Finance, and Industrials were also up around 9%, indicative of investors' receding concerns over a US recession. This also helps to explain the weakness in defensive sectors. For example, Staples and Utilities were up 2.9% and 0.6%, respectively.

The Fund initiated new positions in Bayer (a German agri/healthcare group), Newmont (a gold miner), and Nestle (a global beverages and foods business) which is this quarter's 'Stock in Focus'. Additionally, the Fund received shares in rewards company Pluxee after it was spun-out from Sodexo.

Japanese carmaker, Subaru was also added to the portfolio during the quarter. As a leader in the fast-growing US SUV category, with ~9% market share, Subaru is one of the best quality automakers. This is evident in its high operating margins, low inventory and lack of incentives needed to drive sales.

hile Subaru is still relatively early on its EV transition journey, something that will ultimately consume substantial resources, it is starting with significant net cash on hand (>¥1trillion vs ~¥2.5 trillion market cap) and partnering up with bigger players to share the burden. With the stock trading on an EV/EBIT of less than 4x, we also think a lot of this risk is reflected in the valuation. Given strong fundamentals and a solid balance sheet, we think Subaru makes for a compelling investment proposition.

The Fund sold a large part of its holding in Japanese telco, KDDI, and wrote calls on its holding in H&R Block (tax advisor), Henry Schein (dental distributor), Secom (security firm) and Wheaton (metals streaming) on a combination of valuation grounds and, in KDDI's case, a change to the investment thesis.

Brazilian brewer, Ambev, was a major detractor to fund performance over the quarter. Its shares sold off following a disappointing FY23 result mainly driven by Argentinian currency devaluation and its impact on revenues and operating income. Forward cost guidance was also somewhat disappointing relative to expectations. However, the stock is now very cheap on a range of metrics with current prices capitalising decade low margins/returns into perpetuity. We think this is overly pessimistic, and at some point, margins and returns should normalise. Furthermore, we think significant downside from here is capped thanks to a solid balance sheet which also affords management time to assess a new capital structure in light of changing tax law in Brazil.

On the flip side, Japanese trust banking group, Sumitomo Mitsui was the biggest contributor to performance with shares fully participating in the Japanese equities' rally. Driving this is the fact that Sumitomo Mitsui remains very well positioned to benefit from higher rates' outlook in Japan. The stock has also enjoyed some earnings upgrades over the quarter on the back of a more favourable operating environment.

Spanish utilities business Redeia, was also a meaningful contributor to performance with shares performing well after announcing larger than expected capex plans in coming years. As a regulated utility, its earnings are largely a function of its regulated asset base (RAB) times a regulated return, something we think has scope to move up in coming years.

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