# COOPER INVESTORS GLOBAL EQUITIES FUND (HEDGED)

## QUARTERLY COMMENTARY REPORT

AFS LICENCE NUMBER 221794
ABN 26 100 409 890

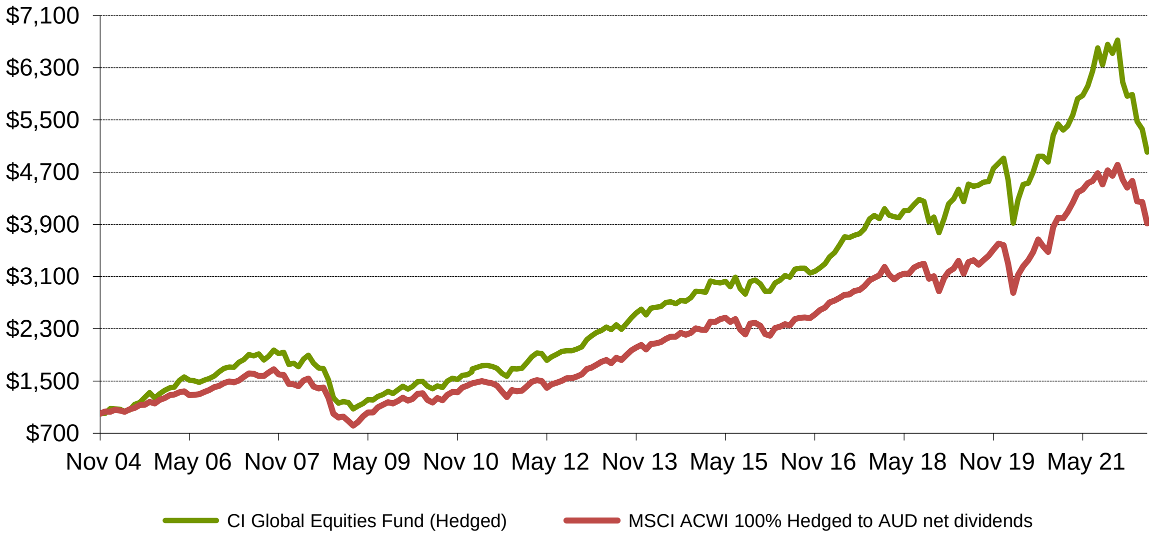
For current performance information please refer to the Monthly Performance Report.

## JUNE 2022

| **Cooper Investors Global Equities Fund (Hedged)** | ****PORTFOLIO** | **#BENCHMARK** | **VALUE ADDED** |
|---|---|---|---|
| *Calendar Year Ending* | | | |
| 6 months to 30 June 2022 | -25.6% | -18.7% | -6.9% |
| 31 December 2021 | 23.6% | 20.2% | 3.4% |
| 31 December 2020 | 12.4% | 11.0% | 1.4% |
| 31 December 2019 | 28.2% | 25.4% | 2.8% |
| 31 December 2018 | -5.4% | -7.9% | 2.5% |
| 31 December 2017 | 23.4% | 20.8% | 2.6% |
| 31 December 2016 | 8.1% | 10.1% | -2.0% |
| 31 December 2015 | 4.1% | 2.7% | 1.4% |
| 31 December 2014 | 10.4% | 11.4% | -1.0% |
| 31 December 2013 | 28.6% | 28.0% | 0.6% |
| 31 December 2012 | 19.2% | 18.5% | 0.7% |
| 31 December 2011 | 6.7% | -3.6% | 10.3% |
| 31 December 2010 | 11.8% | 12.9% | -1.1% |
| 31 December 2009 | 20.1% | 30.2% | -10.1% |
| 31 December 2008 | -39.1% | -40.1% | 1.0% |
| 31 December 2007 | 14.7% | 8.5% | 6.2% |
| 31 December 2006 | 25.0% | 18.4% | 6.6% |
| 31 December 2005 | 34.8% | 19.7% | 15.1% |
| **SINCE INCEPTION*** | **9.6%** | **8.1%** | **1.5%** |
| **SINCE INCEPTION^** | **400.4%** | **291.4%** | **109.0%** |

* Annualised
^ Cumulative (1 December 2004). Initially, the Fund invested predominately in Australian equities. However since May 2006, the Fund has been invested in a broad range of global equities.
** Net of fees and expenses
# MSCI ACWI 100% Hedged to AUD Net Dividends
Past performance is not necessarily a reliable indicator of future performance

**CI Global Equities Fund (Hedged) – Net of Fees**
**$1,000 Invested since Inception**




Source: National Asset Servicing

# COOPER INVESTORS GLOBAL EQUITIES FUND (HEDGED)

## QUARTERLY COMMENTARY REPORT

AFS LICENCE NUMBER 221794
ABN 26 100 409 890

For current performance information please refer to the Monthly Performance Report.

## JUNE 2022

*"Success is not final, failure is not fatal: it is the courage to continue that counts."* **Winston Churchill**

*"The greatest danger in times of turbulence is not the turbulence. It is to act with yesterday's logic."* **Peter Drucker**

## Market and Portfolio Commentary

To say the last 12 months has been a game of two halves is understatement bordering on farcical. For the 6 months to 31 December 2021 the portfolio gained 11.7% versus the Benchmark which rose 6.2%. In the 6 months to 30 June 2022 the portfolio declined 25.6%, versus the Benchmark which fell 18.7%.

Positive contributors to return for the quarter were **Yum China** (relief as Shanghai lockdowns eased), **Arthur J Gallagher** (ongoing strong operating trends for insurance brokers) and **Ferrovial** (traffic beating forecasts in tollroad and airport assets).

The larger detractors to return for the quarter included **Workday** (phasing of some growth pushed into H2)**, Techtronic** (market implying sharp deceleration expected in power tools) and **ICE** (has de-rated around 25% since the Black Knight deal announced in March).
Over the last decade the CI Global team has undertaken extensive global travel hunting for Value Latency and building a unique relationship network and Watchlist of opportunities. We stand behind a track record of careful stewardship of investor capital, outperforming 9 of 11 years from 2011 to 2021 and typically outperforming 70-80% of down months.

In that light the performance of the fund in this year's sell-off has been somewhat disappointing.
We do not get everything right – we may misjudge a management team, misinterpret an industry trend change or be too early or late in a decision.

What happened and what are we doing about it?

1) Portfolio Construction: Positioning into the end of 2021 was in hindsight inappropriate for the rising risks of a sharp inflection in policy rates slamming the breaks on the global economy. Our allocation to Stalwarts had declined throughout 2020 and 2021 - we redeployed into Growth and Cyclicals where weighting had grown due to our positive assessment of ongoing operating trends, outperformance of positions and investment in additional new ideas. In short, we were slow to pivot, noting that around 5% of the underperformance year-to-date occurred in the month of January.

2) Stock Selection: We have been batting below our average where a number of investment propositions didn't play out to our original thesis. We would call out:

    a. Activision Blizzard – our investment preceded news that the company was under investigation for workplace bullying. When it became clear management had misled the market on the extent of the problem we sold, led by our principles of Responsible Investing. We did not benefit from the subsequent M&A premium paid by Microsoft.

    b. Just Eat Takeaway – The business has been hit by fee caps in US cities plus increased marketing spend in key markets in response to free-spending peers funded by cheap capital. The net effect has pushed the earnings and cash flow inflection points in their UK and US businesses further out.

c. Yum China – With the world emerging after two years of COVID, the extreme Shanghai lockdowns caught the company and frankly us a little by surprise. While the proposition for domestic KFC roll-out remains intact Yum China has not behaved like a Stalwart this year.

As per our opening quote by Sir Winston Churchill, "Success is not final, failure is not fatal: it is the courage to continue that counts."

We have taken this opportunity to double down on the CI Way and VoF Process. **Focus** and **clear decision-making** through the lens of bottom up and top down insights and capital allocation to the best Subsets of Value is the secret sauce of success. Indeed, after three excellent global trips this quarter (see Trip News) we remain convinced that our approach and privileged access to a phenomenal global network of the best business owners, operators and capital allocators will continue to yield insight and opportunity to generate outperformance from our Watchlist.

With markets now going through another dislocation this is the time for laser sharp thinking and application of what has worked for more than 20 years at CI.

Without conducting a full macro post-mortem, consider just some of the many superlatives written on market action in 2022.

- US bonds posted their 'worst 1st half performance in over 100 years'.
- It's been 'the worst first half in global equities since 1987' and 'worst start for the S&P since 1970'.
- March saw 'the biggest weekly rally in commodity prices in 50 years'.
- Inflation in the US 'surged to a four-decade high'.
- The average US 30Y mortgage rate has doubled driving 'housing affordability to collapse at the fastest clip on record'.
- And finally, the implosion of the Crypto bubble has been called 'the largest Ponzi scheme in human history'.

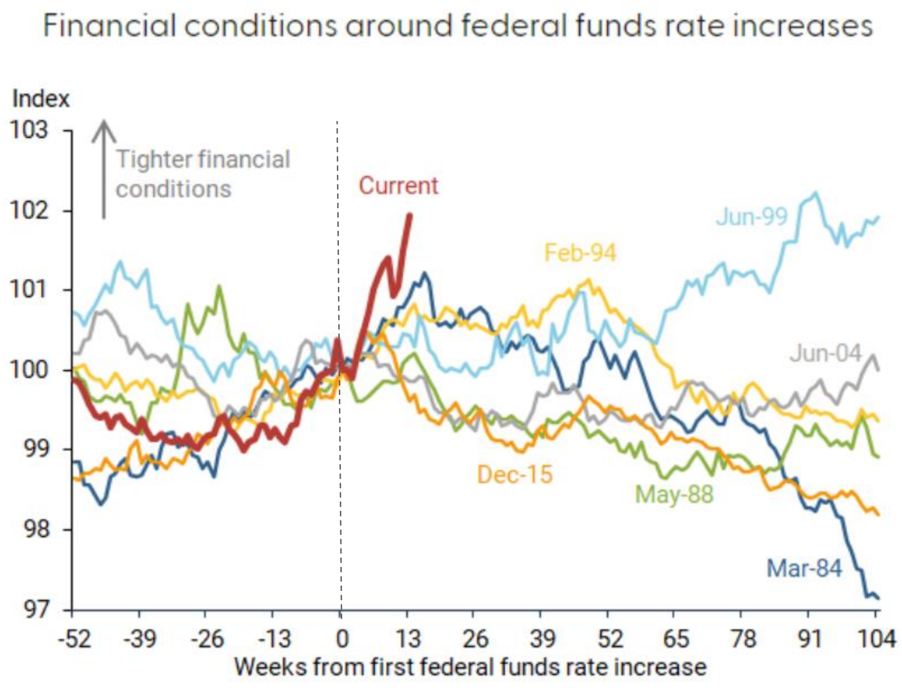
Suffice to say while equities market volatility is an ordinary part of investing, this year so far feels very much *extraordinary*.

If Federal Reserve Chair Jay Powell woke up on the 1st of January and declared that his New Year's Resolution was to cause a recession, you'd have to say he's tracking well.

Several historically reliable bellwethers are flashing recession risk. The Yield Curve (US10Y yield minus 2Y yield) is inverted. The price of copper has rolled over, falling 25% from its March high. And the US consumer (per University of Michigan sentiment survey) appears to have capitulated. Anecdotally too it is clear that consumers in the US, UK and here in Australia are feeling the pinch, squeezed between higher prices for energy, food and (for those not prescient enough to have locked in fixed home loans) higher mortgage repayments. What remains unclear is when 'demand destruction' starts to cause the drop in reported inflation so desired by the Fed. But if the sheer *pace* of tightening in this cycle feels unprecedented, that's because it has been.

For current performance information please refer to the Monthly Performance Report.

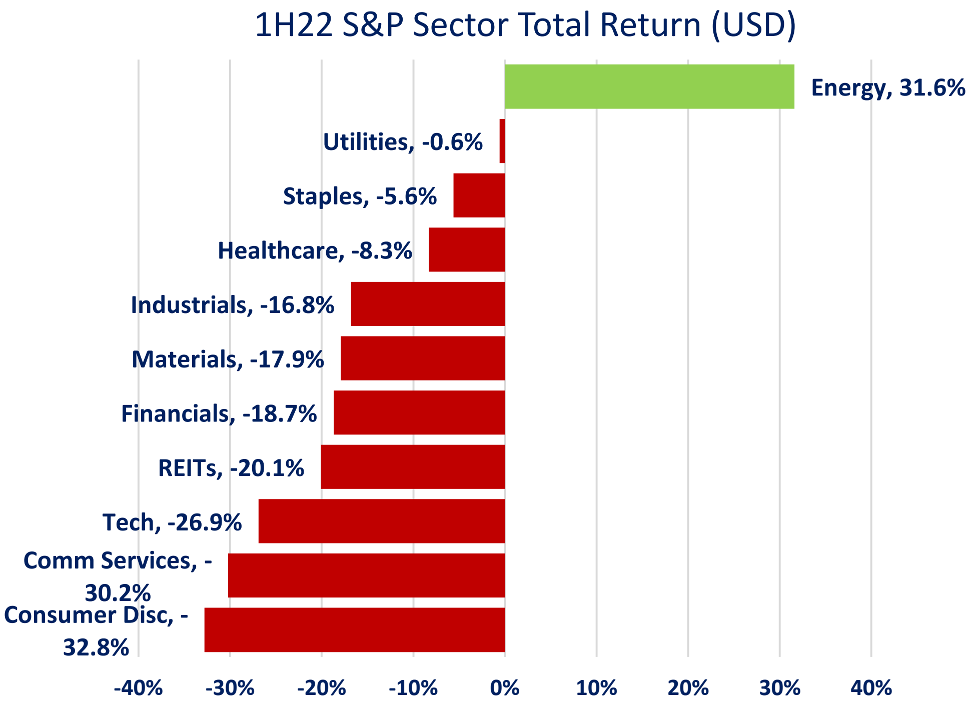
## JUNE 2022



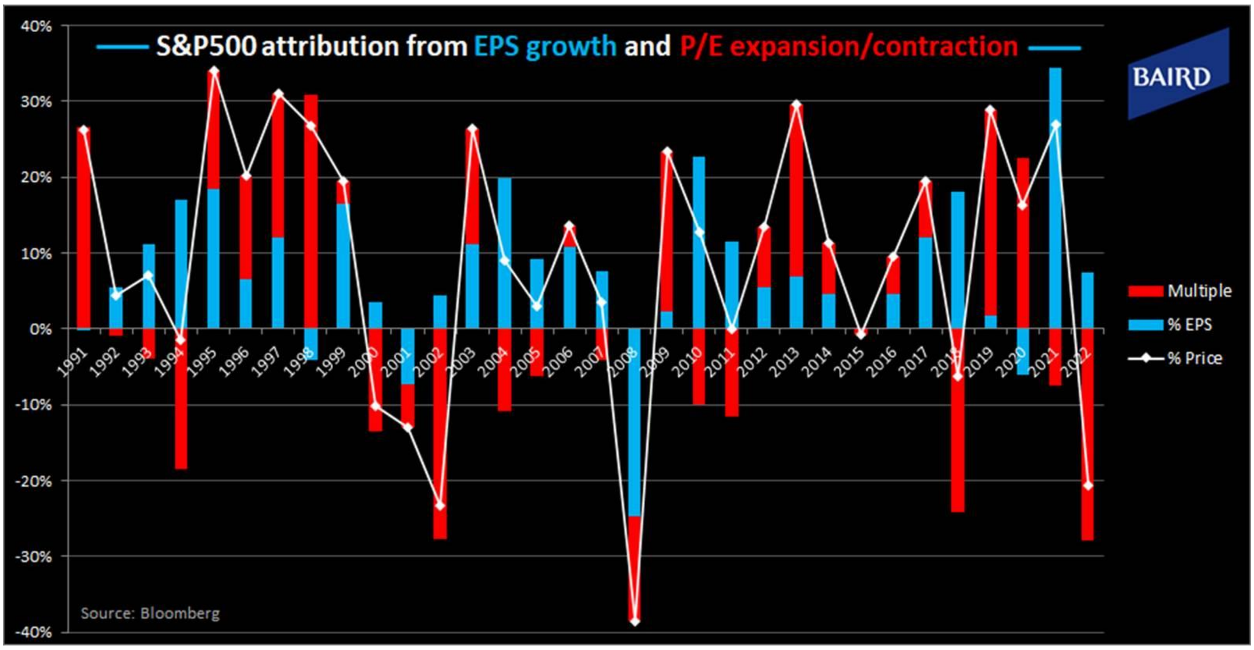

*Source: Federal Reserve Bank of San Francisco, GS US Financial Conditions Index*

The chart above shows a weighted average composite of short-term and long-term rates, the trade-weighted dollar, an index of credit spreads and a proxy for CAPE (the cyclically adjusted PE ratio) for equities. Far from a slow transition or 'soft landing', the vibe is that in 2022 the punch bowl has been ripped away, the music stopped, the lights turned on and merrymakers booted out into a cold and unforgiving night.

The impact on listed equities has been dramatic with almost every sector down. Remarkably the only winner year to date has been Energy, a sector universally shunned during a sustained period of low oil prices and decarbonisation or 'greening' of portfolios.




While many companies are still reporting reasonable earnings growth, the impact from price falls has been a near 30% multiple compression, the largest we have seen in our careers beyond even the dotcom or GFC crashes, as this excellent chart from Baird shows:




*Source: Baird*

# COOPER INVESTORS GLOBAL EQUITIES FUND (HEDGED)

## QUARTERLY COMMENTARY REPORT

AFS LICENCE NUMBER 221794
ABN 26 100 409 890

For current performance information please refer to the Monthly Performance Report.

## JUNE 2022

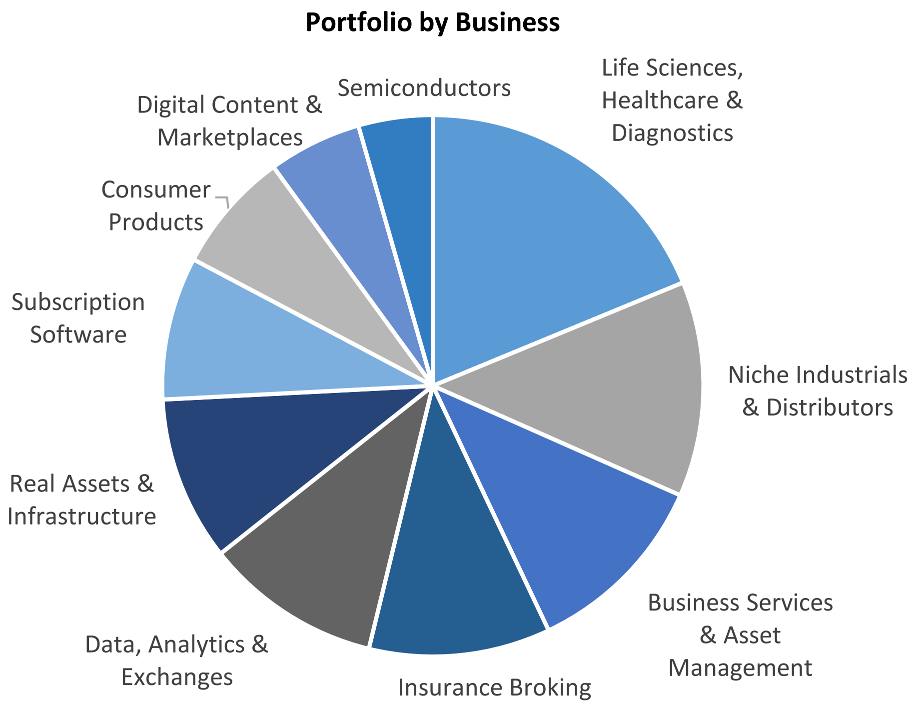
Relief does not appear imminent with more rate hikes by central banks guided for the rest of 2022 and geopolitical dislocations in Eastern Europe and China yet to resolve. In Ukraine the conflict drags on with major implications for global energy and food markets – we spoke to a Norwegian oil and gas business in recent weeks who told us they are piping natural gas down to Germany at incredible prices, many multiples of a barrel of oil equivalent. When we asked, 'What happens when winter comes,' the response was 'You don't want to ask that question'. In China the government is persisting with its 'COVID-Zero' policy, suppressing movement of goods in and out of the region and impairing day-to-day freedoms of the population. Interestingly our investment in Yum China gained 15% over the quarter indicating that perhaps, as in 2009, the first market where sentiment bottoms out may be China.

## The Portfolio

The portfolio is positioned around Subsets of Value.

- **Stalwarts** (33% of the portfolio) – sturdy, strong and generally larger companies with world class privileged market and competitive positions (AON).
- **Growth companies** (25%) – growing companies with identifiable value propositions using traditional value metrics and run by focused, prudent and experienced management (Synopsys).
- **Bond like equities** (4%) – stocks with secure, low-volatile dividends that can be grown and recapture inflationary effects over time (Ferrovial).
- **Low risk turnarounds** (5%) – sound businesses with good management and balance sheets. (Vontier).
- **Asset plays** (7%) – stocks with strong or improving balance sheets trading at discounts to net asset value or replacement value (Sony Corp).
- **Cyclicals** (18%) – stocks showing both upside and downside leverage to the cycle with experienced and contrarian managers who allocate capital prudently (Ferguson).

Regarding sectors, index provider classifications are often inconsistent with diversified businesses, for example we own several categorised as 'Industrials' but with meaningful portions of their business selling healthcare products or even software. We produce the chart below to simplify portfolio exposure via market and business type:

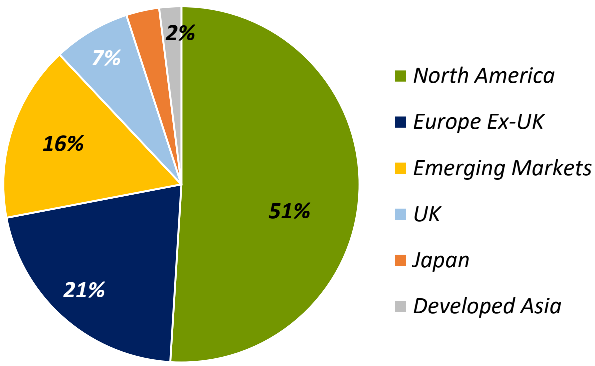


For current performance information please refer to the Monthly Performance Report.

## JUNE 2022

| | |
|---|---|
| **No. of Stocks** | *42* |
| **Region Weights** | *North America 56%* |
| *(by listing)* | *Europe 23%* |
| | *Asia 13%* |
| **Most OW Sectors** | *Industrials, Health Care* |
| **Most UW Sectors** | *IT, Energy* |
| **Cash** | *8%* |

**Geographical Exposure by Source of Revenues#**




*#Derived on a look-through basis using underlying revenue exposure of individual Fund stocks*

| Portfolio Metrics | |
|---|---|
| Price to Earnings [1, 2] | 18.9x |
| Price to Free Cash Flow [1, 2] | 19.3x |
| Return on Equity | 19% |
| Debt to Equity | 33% |
| Net Debt to EBITDA | 0.99x |

*[1]Next twelve months forward*

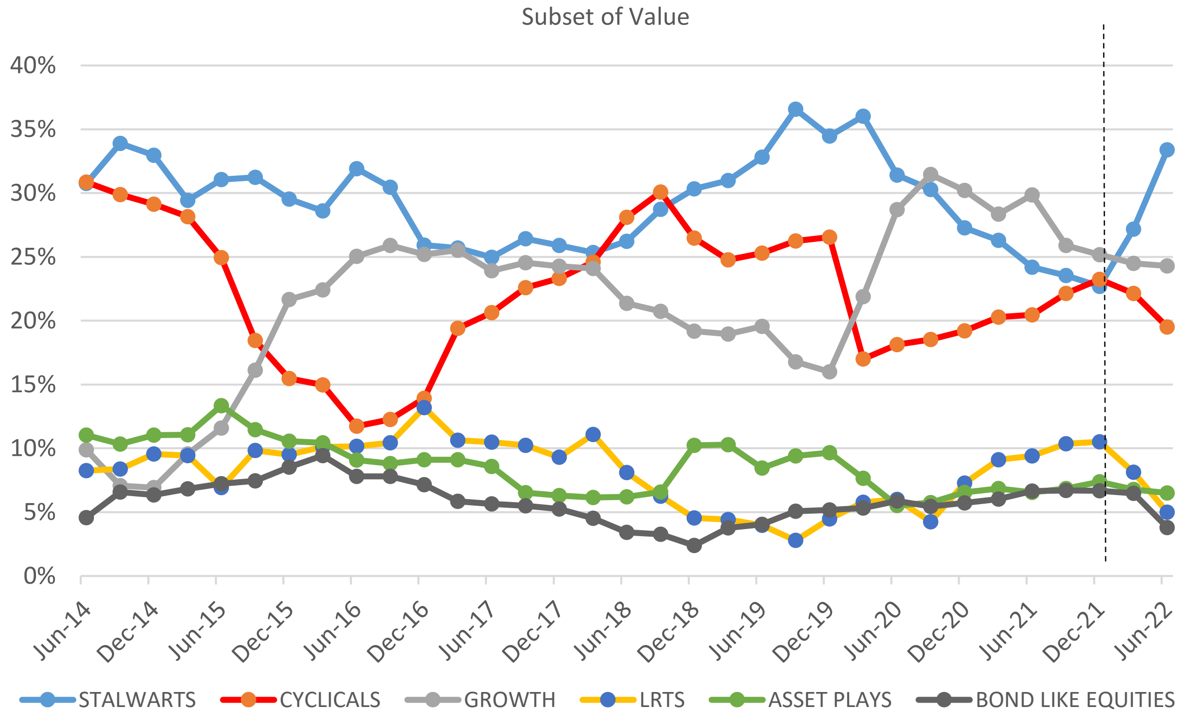
*[2]A number of stocks have large cash balances (e.g. Hoya, Veeva) which has been deducted from the 'P' in calculation of portfolio ratios*

For current performance information please refer to the Monthly Performance Report.

JUNE 2022

## Portfolio Changes

In recent months we are beginning to see fantastic long-term opportunities in some of the very best Stalwart and Growth businesses on our watchlist, where to coin a phrase, some 'babies have been thrown out with the bath water'. We have upweighted Stalwarts in the portfolio. We see significant Value Latency in our existing Stalwarts, many of which have fallen 20% or more year to date and we have been adding to positions. We think it is likely that the role of highly recurring compounding businesses that are cash generative with strong balance sheets will come back to the fore in a world of slowing growth, especially in a relative value sense versus other assets. Volatility begets opportunity and accordingly we have bought four new Watchlist positions in the quarter, three of which are Stalwarts:




One of our new buys is **London Stock Exchange Group ['LSEG']**, a UK listed financial infrastructure business. While retaining the name of a regional stock exchange LSEG has been on a journey of becoming a far more diversified and global data and analytics business. Much of this metamorphosis occurred over the 2009-2018 tenure of former CEO Xavier Rolet with current CEO David Schwimmer making the final strategic step with the 2019 acquisition of Refinitiv from Blackstone.

As the former data business of Thomson Reuters the capture of Refinitiv represents a transformational deal for LSEG in terms of size and scope. Refinitiv owns a number of world class assets including Real Time Data Feeds which power global capital markets across a broad range of asset classes. In addition the deal brings optionality with a controlling stake in US-listed TradeWeb, a leading player in the electronification of fixed income trading.

Refinitiv also comes with a few 'hairs'. As a group of fairly siloed businesses there has been limited integration of a globally disparate sales force, substandard performance management around client service, and pockets of severe technology underinvestment. A prime example is the desktop terminal business Eikon which has been losing share to Bloomberg and Factset for years and requires significant reinvestment. It is these 'hairs' that we felt the market was choosing to ignore after the deal announcement in 2019 when the share price shot off like a rocket. Fast forward to March 2021 and it was a case of reality bites with recently installed CFO Anna Manz having the unenviable task on her first market update call to announce a steeper on-boarding and integration bill than was expected.

This led to a period of sharp underperformance where, back at around £70 the equity has been de-risked with the integration heavy lifting now well underway. At around 19x core earnings (stripping out TradeWeb) with 70% of the P&L now recurring subscription revenues, LSEG represents compelling Risk Adjusted Value Latency. This is a set of world class financial infrastructure franchises that can grow mid-single-digits, are relatively inflation immune and at ~50% EBITDA margins are under-earning their peer group. The rapid de-gearing given a highly cash generative business model presents management with a nice problem of what to do with the excess cash. We would expect a growing stream of buybacks or dividends in future.

A number of stocks were sold during the quarter.

We initially bought design software group **PTC** in 2018 at around $90 with the business midway through transitioning customers onto a subscription model. The share subsequently fell as low as $46 in the COVID sell-down but recovered with solid execution by the management team, rising as high as $153 in mid-2021. We began reducing the position as Value Latency dwindled and exited fully this quarter after a volatile but successful four-year investment.

**SimCorp** and **Cosmos Pharmaceutical** were sold after meetings with management during trips to Denmark and Japan respectively. Both face challenging operating environments though for different reasons. Investment management software business SimCorp has been struggling to win new customers in the key US market where they are competing with Blackrock's Aladdin business – this is a hard problem to solve that will now need to be tackled by a newish management team with a recently appointed CEO and the CFO announcing his retirement.

Japanese drugstore roll-out Cosmos is taking its unique low-cost model from the heartland of Kyushu in the south-east of Japan up into the more densely populated regions of Kansai (Osaka) and Kanto (Tokyo). The roll-out holds much promise, however our recent travels there indicated that a tricky period lies ahead. Japanese retailers of all stripes face the inescapable reality of inflation – something new to much of the population – and this is likely to erode what are already skinny trading margins.

## Stock News

During the quarter **Colfax** concluded its plan to separate into two independent and public companies. As such the portfolio now holds two smaller positions in the newly created entities, **Enovis Corporation** and **ESAB Corporation**. Enovis is a medical device business focusing on orthopaedics while ESAB is a world leading provider of equipment and consumables in the Welding and Cutting industry.

Our investment in Colfax was predicated on this moment whereby focus and energy would be unleashed by separating the businesses and we see compelling Value Latencies in both. A focus during the quarter has been to reach out and build relationships with both new management teams, culminating in a visit to Enovis over in Delaware and a site tour of ESAB's local operation in Preston, Victoria.

## Trip News

The quarter saw an extensive resumption of travel with the team spending many weeks on the road across trips to the US, Europe and Japan.

After two years being locked in Australia this was an exciting period and a wonderful opportunity to reconnect in person with the businesses owned in the portfolio. While we have continued to speak to them regularly over video-conference, there was *universal* agreement that physical meetings are preferred.

The response to meeting requests was highly conducive. Management teams were more receptive than usual to spend time with us and each trip had instances where we were told Cooper Investors were the first investors the company had interacted with face-to-face since the beginning of the pandemic.

In total across all trips we caught up with around half the portfolio within a 6-week period, meeting senior management almost without exception. It was a fantastic period of focused insight gathering and gave us the opportunity to revisit investment propositions, update VoF conclusions and do site tours of factories, facilities and retail stores. We also met with more than 50 Watchlist stocks and peers. Visiting in person provided the opportunity to take the temperature on the ground of each region, as well as meet local industry experts and other investors in a more informal setting than a Zoom screen.

A full summary of meetings would extend this newsletter to 30+ pages so we will offer brief highlights. Travels across Europe took us to London, Copenhagen, Amsterdam and Brussels. The most memorable meeting was with **Eurofins Scientific** CFO Laurent Lebras whom we were grateful to catch up with in Belgium. While the meeting was conducted either side of a Perspex screen (local COVID restrictions remain tighter than elsewhere) Laurent's passion and energy for the business was palpable. We sometimes use the slang of a 'put the notebook away' meeting, and this was one of those. Laurent explained with great clarity the advantage of Eurofin's hub and spoke lab testing model, how it enables small labs to rapidly scale to attractive margins and how density and proximity to customers leads to both a better and faster service outcome for customers and superior returns for Eurofins shareholders. Laurent was formerly Head of APAC at L'Oreal, an organisation renowned for tight focus on operational performance. Founder Gilles Martin's ability to attract senior management of this calibre to what is a smaller organisation (Eurofins had a market cap of ~€3bn when Laurent joined in 2015) is impressive, but reflected down through everyone we have met in the company over our two and half years as owners. Indeed, Eurofins has an inbuilt advantage in hiring high quality scientists – as Laurent explained, scientists tend to be conservative folk and Eurofins' long term mindset, focus on innovation and investing deeply into labs is an attractive career proposition for them. Thus far Eurofins has returned around +45% in AUD terms versus a benchmark return of 4% over the holding period. We are even more excited around the proposition today and have increased our stake in recent weakness.

In the US the trip covered both the East and West Coast (San Fran, New York, Connecticut, Philadelphia, Washington) with some time in the Midwest (Minneapolis, Cincinnati).

There was somewhat of a dichotomy during the trip, with markets swinging up and down on Wall Street but meetings with management suggesting little panic. Businesses have already been through such a difficult two years that levels of stoic resilience are high - corporate balance sheets are relatively strong and revenues and bookings growth still seem solid. The vibe was that top line resilience would be good, though it is worth noting that the tone from companies in the subsequent 8 weeks has deteriorated.
The main area of concern and uncertainly was around profitability. Earnings impact will be most acutely felt across manufacturers due to raw material inflation and more globalised businesses due to the FX headwind of a strong Dollar. Broadly companies told us they have been increasing prices since mid-

last year – those willing to take the margin hit and focus on share gains for the long term have seen the market unforgiving on their share prices.

A key meeting for us was with Matt Teratola, CEO of newly spun-off **Enovis Corporation**. It is telling when a company CEO does the background work on us before a meeting – it shows a care and respect for shareholders. Unsurprising given you can follow the proprietorial behaviour thread back from Enovis to Danaher, with Danaher founder Mitch Rales installed as Chairman after the spin from Colfax. The company today has two operating segments – Prevention and Rehab, and Reconstructive. P&R make and supply a variety of braces, supports and orthotic devices, while Reconstructive sells joint implants for hips, knees and ankles.

Industry growth along with some focus around pricing and assortment should give these businesses mid-to-high single digit growth, with perhaps a point or two higher while pent-up COVID demand gets soaked up. The most exciting latency is margins where Enovis is currently under-earning its peer group. Competitors like Stryker make mid-20's margin with Enovis currently mid-teens - there is a clear pathway for Matt to lead the group to 20% EBITDA margin over the next 2-3 years through efficiency, operating leverage and a more intentional pricing strategy.

In Japan we were among the first overseas visitors in two years - the border remains effectively closed to independent tourists. As business travellers we were allowed in but needed to take a battery of 'pre-Quarantine' measures to get through the COVID red-tape including a sponsored visa, pre-trip PCR test and the downloading of a government app onto our phones that could monitor our health and location. Everything worked smoothly and we found Japan to be, as usual, a blissful place to visit.

Meetings focussed on the areas where we have capital invested – personal care (via Unicharm and Cosmos) and semi-equipment (via Hoya). As mentioned earlier in the newsletter, the takeaways from visiting several drugstore businesses led us to exit our Cosmos position.

The meetings with semi-equipment makers were far more positive, the highlight being the time we spent with **Hoya** CEO Eiichiro Ikeda who was recently appointed in March. The discussion got us excited about the opportunities that may unfold from having a fresh pair of eyes at the helm of an 80-year-old company.

Ikeda-san joined Hoya in 1992 and has worked across various roles in both the Information Technology and Life Care businesses. As COO running the IT segment in 2013 Ikeda was instrumental in restarting investment in the mask blanks and HDD businesses after a long period of the segment being treated as a cash cow by HQ. Today these represent the future of the business and are the major growth drivers in the medium term.

Going forward, it is clear that capital will be allocated based on the potential of individual businesses and so less restricted by the 'cash cow' or 'growth' classifications applied by prior regimes. Whilst the business is hungry for growth, Ikeda expressed that "Hoya's strength is in profitability control", key to Hoya's exceptional financial quality and returns on capital over a long period.

A major driver of growth today is Hoya's EUV mask blanks business, where they are the technology leader and occupy 80% market share. Hoya collaborate closely with key customer TSMC to develop leading edge technology and although competitors are trying to catch up, there is a first mover advantage at each stage of technological advancement. Prohibitive switching costs are incurred if buyers want to change suppliers, given finely tuned designs and delicate processes. Gigantic end customers like Apple and Samsung will continue to drive global innovation around technology and will require suppliers such as Hoya to be closely involved. This incumbent position gives us confidence in Hoya maintaining high market share and margins for a good period.