
# Discovery Global Equity Feeder Fund

## Market background

The MSCI All Countries World Index (ACWI) rose during the quarter, finishing near its high over the period. Sentiment was supported by a strong earnings season, with companies mitigating the effects of higher costs resulting from supply chain constraints. Despite inflation at multi-decade highs and expectations of further central bank action in 2022 following the Bank of England's move to raise rates for the first time in three years, the assumption that the absolute level of future rate rises by the Fed will be kept low has been viewed as positive by investors for equities. The discovery of the Omicron variant at the end of November led to a sell-off for global markets and a jump in the VIX volatility index, accompanied by a double-digit percentage decline for energy prices, but investor sentiment recovered as pandemic fears subsided.

Regionally, the US was the best performing major market. Europe also outperformed most major regions, helped by an ECB announcement that it would boost its asset purchase programme in Q2 2022, while ending its pandemic emergency asset programme by March 2022. The eurozone's November manufacturing PMI registered its first headline index rise since June, led by Italy, while production in Germany and France lagged. In contrast, Chinese economic growth slowed, affected by downturns in the property market and consumer confidence, while the Hang Seng Index ended the period in negative territory, capping its worst annual performance for a decade. Geopolitical tensions between Moscow and the West contributed to severe weakness for Russian equities.

With the exception of communication services, all sectors posted a positive return over the quarter. Cyclically sensitive sectors like technology and materials did well, but so did more typically defensive areas of the market such as health care and consumer staples.

## Performance review

For the quarter, the Fund performed broadly in line with the comparison index.

Stock selection in the technology sector was positive. US semiconductor business Broadcom was the largest stock contributor, helped by reporting good results and increasing profit guidance, reflecting a better performance in both its semiconductor and software divisions. Being underweight semiconductor giant Nvidia however, was the leading detractor from relative performance. US software giant Microsoft was particularly strong as it benefitted from good results showing an acceleration in overall revenues, better margins and upside to estimated cashflows from its Azure cloud business. US test and measurement equipment company Keysight Technologies presented good results and indicated a better revenue growth outlook within the core business, while new customer wins are set to support emerging growth areas.

Although copper miner Freeport-McMoRan initially pulled back on slowing economic growth in China, signs that government policy was becoming more supportive enabled the stock to recover strongly, along with metal prices. We believe the long-term demand story for copper remains intact, which combined with limited new supply is likely to be supportive for pricing. Stock selection in healthcare sector was also positive. US health insurer UnitedHealth Group is viewed as a quality compounder with the ability to grow its membership base, which continues to exceed expectations.

US online payments business PayPal reported disappointing results, with the company providing lower revenue guidance for Q4. The company cited the reversal of travel recovery, weaker back-to-school spending and more instore shopping as the reasons for the poor performance. Overall, stock selection in financials was positive, but US giant Citigroup was hurt by the Fed's more hawkish stance, combined with growth and asset quality concerns, especially in their credit card division. Although not owning Tesla proved helpful in December, it was a negative for relative performance over the quarter as a whole.

## Outlook and strategy

Looking ahead to the new year, at first glance it seems investors face a very similar environment to the one at the beginning of 2021: broad COVID restrictions, China-US tensions, supply chain issues, as well as uncertainty over inflation and a broad consensus that monetary policy will see some tightening, and a market that appears utterly unconcerned over these headwinds. However, there will almost certainly be a notable difference, a sharp slowdown in profit growth from the near 50% gain likely to have been generated in 2021 as a result of the global economic rebound. Current forecasts look for a high single digit percentage gain for US profits in 2022 which, though not bad, comes with a lot of uncertainty around the impact of inflationary pressures on corporate margins. The ability to meet market expectations will prove crucial as elevated market valuation multiples means disappointments are likely to be heavily punished.

While the surge in corporate profits last year was led by economically sensitive sectors such as energy, industrials, materials and consumer discretionary, above average gains for the current year will likely prove to be more diverse across the industry spectrum and be more related to company specifics than to any broad macroeconomic improvement. Hence, we think that individual stock selection will prove the key driver for generating index-beating returns. However, we do identify certain key drivers that should provide a tail wind to earnings for companies that offer quality, value and momentum in fields such as climate change, automation, infrastructure spending and technological disruption.

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