Discovery

# Discovery Global Income Share Portfolio

## September 2023

The strategy follows a fundamental, bottom-up approach to investing in high quality companies where there is a gap between what we believe is the intrinsic value of a company and its share price. The strategy is concentrated, highly active, has a low turnover and a long-term investment horizon. The strategy aims to generate a higher yield than its benchmark, MSCI World (Net Total Return), with lower volatility and some capital appreciation over a complete economic cycle.

Proprietary, bottom-up research is the key driver of our investment process, and we seek to generate the vast majority of our alpha from our rigorous stock selection. We believe that a focus on quality is of utmost importance while managing a strategy with a long-term investment horizon. We seek to invest in high quality companies with industry leading market shares, strong free cash flows, robust balance sheets, excellent managements, and sustainable competitive advantages. As active managers, we seek companies where there is a gap between what we believe is the intrinsic value of a company and its share price. We also look beyond the next twelve months, conduct analysis using appropriate valuation metrics for each sector and look for underappreciated assets within a company. Due to our emphasis on quality, we expect the strategy to be resilient in down markets.

The strategy is managed by Goldman Sachs Asset Management's Global Equity team, comprising eight Global Sector Leads, and led by the Head of International Developed Markets. We employ a team-based approach to investing and every stock that is selected for the portfolio is thoroughly discussed and debated among all the team members before being included. Our Global Sector Leads host regular sector calls with their Fundamental Equity counterparts based in local markets, allowing them to take a global view across their sector. We believe that this team-based structure is efficient for stock selection and ensures that the Lead Portfolio Manager, who has the final buy/sell authority, stays informed at all times.

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# Market Review

The MSCI World Index returned -4.3% (total returns in USD) in September, bringing YTD returns to +11.1%. Global equities fell during the month amidst renewed stress in the Chinese real estate sector, expectations of higher for longer rates globally and contractionary economic concerns, particularly in Europe. All regions ended the period in negative return territory. Energy was the only sector in the index to register positive returns as Brent Crude oil surged +7.7% in the month, while Information Technology and Real Estate were the top laggards.

Increased global bond yields put added pressure on risk assets. The Bank of Japan endorsed higher bond yields earlier in the quarter resulting in a 11 bps increase in Japan's 10yr Government Bond yield in September. This suggested a potential end to negative interest rates in Japan by year-end. Increasing inbound tourism initially boosted small and mid-cap Japanese stocks but concerns arose in September surrounding political tension with China, which may impact tourism. In China, lower economic growth and real estate market concerns continued to plague the region despite new stimulus policies. Encouragingly however, PMI came in at 50.2 in September, thus returning to expansionary territory.

US markets saw a sharp pullback in September, erasing gains from earlier in the quarter. The Fed left its target rate unchanged at 5.25-5.50%. However, its higher-for-longer narrative appeared to gain further recognition from investors after the Fed's September dot plot showed median expectations at 50 basis points (bps) in rate cuts for 2024, down from 100 bps in June. In addition, policymakers' forecasts shifted to favor one more rate hikes in 2023. Manufacturing PMI was above expectations at 49 but economic slowdown concerns lingered given the Fed's hawkish commentary.

The European Central bank raised rates to a record high in September but suggested that this may have been its last rate hike given that Eurozone inflation fell to a two-year low of 4.3%. After falling to a 33-month low in August, PMI slightly rebounded to 47.1 in September, though remaining in contractionary territory. UK markets showed signs of improving consumer confidence with slight recovery in the Consumer Discretionary and Leisure sectors. The Bank of England ended its run of fourteen consecutive rate hikes in September.

# Performance Overview

- On a yield basis, the portfolio's current yield (gross of tax) of 3.55% in the trailing 1-year period is higher relative to the index yield of 2.06%.
- The Goldman Sachs Asset Management's Global Equity Income Strategy returned -2.72% in September, outperforming the MSCI World Index by 159 bps (gross of fees, USD).
- At the sector level, Energy and Financials were the only contributors to absolute performance, while our positioning in Information Technology and Consumer Staples were the largest detractors.
- As of September month end, the strategy had $1,157mm in assets under management.

| Periods Ending 30-Sep-2023 | Global Equity Income Strategy (%) | MSCI World (%) | Excess Return (bps) |
|---|---|---|---|
| September 2023 | -2.72 | -4.31 | **+159** |
| YTD 2023 | 6.32 | 11.10 | -479 |
| Trailing 1 year | 20.91 | 21.95 | -105 |
| Trailing 2 years | 1.61 | -1.00 | **+261** |
| Trailing 3 years | 9.36 | 8.08 | **+128** |
| Since Inception | 9.87 | 10.97 | -110 |

*Source: Goldman Sachs Asset Management. Inception Date: January 01, 2019. The returns are gross and do not reflect the deduction of investment advisory fees, which will reduce returns. Our investment advisory fees are described in Part 2 of our Form ADV. See additional disclosures.* ***Past performance does not guarantee future results, which may vary****. The holdings and/or allocations shown may not represent all of the portfolio's investments. Future investments may or may not be profitable.*

# Performance Commentary

Some of the top contributors and detractors for the month include:

- **HSBC Holdings (Contributor) –** HSBC Holdings, a British multinational universal bank and financial services holding company, was the greatest contributor to absolute performance during the month. The stock rebounded after being a key detractor in August when it released interim results in which management noted that customer lending decreased by $9 billion YOY, citing client deleveraging and weaker demand as interest rates rose. However, the company reported a 5.8% revenue beat in Q2 2023 and higher for longer rates are expected to continue to have a positive effect on banks' top lines. Over the month, HSBC's plan to sell its Canada unit to RBC was approved by Canada's Competition Bureau. There were also reports of HSBC planning to acquire Citi's China retail wealth unit, though yet to be confirmed by either entity. Moving forward, we continue to have conviction in our investment thesis centered around growth in HSBC's Asia engine, its cost cutting measures focused on tech-integrated productivity improvements, and its capital return with targets of 50% dividend payout and $2 billion of share buyback announced in Q1 2023.

- **BP (Contributor) –** BP, a British multinational oil and gas company, was also a contributor to absolute returns. BP surged during the month in line with the broader sector as Brent Crude oil rose +7.7% in September. BP is pivoting from an international oil company to an integrated energy company, which has been, and we believe will continue to be, positive for its longer-term growth prospects. BP has an attractive and sustainable yield, and we like its commitment to return a majority of its surplus cash flow to shareholders. In an effort to achieve its net zero target by 2050, BP has increased investments in resilient hydrocarbons, continued to grow their convenience and mobility businesses, and scaled up their investments in low carbon energy. We look favorably upon BP's strengthened balance sheet, large size / scale, diversification, and proactive strategy in the energy transition theme.

- **American Tower Corporation (Detractor) –** American Tower Corporation, a US-based operator of telecommunications infrastructure, was the greatest detractor from absolute performance during the month. Earlier in the quarter, management noted a slowdown in carrier activity and services revenue. The stock may have also suffered from a dispute with Telkom Kenya, an integrated telecommunications provider in Kenya, which led to service disruptions in the region. Despite the afore mentioned headwinds, the company guided towards 5% organic tenant billings growth for 2023, strong data center business demand with high single digit growth in Q2, and announced a 3.2% increase in its quarterly dividend towards the end of the month. Further, over the period, MTN Nigeria announced that American Tower would be taking over power operations in Nigeria beginning in 2025. We continue to like the company given its strong fundamentals and ability to generate strong cash flows, which can be utilized to fund future capital expenditures around 5G technologies. We believe the company is also expected to benefit from its exposure to international emerging markets with low current mobile data penetration along with growth in mobile data traffic in developed countries.

- **Home Depot (Detractor) –** Home Depot, an American home improvement retailer, was another significant detractor. Although the company reported earnings above consensus expectations earlier in the quarter, YOY results were down amid decelerating growth. EBITDA decreased 6% YOY as management indicated decreased sales in discretionary categories, further fuelling macroeconomic concerns on weakening consumer spending. Home Depot has also faced the headwind of a slowdown in housing turnover, though somewhat mitigated by consumers continuing to invest in their current homes. The stock's performance over the month may have also been impacted by an insider sale of shares at the end of August. Nonetheless, despite the challenging macro backdrop, we remain constructive on Home Depot as it has demonstrated resilience in its top and bottom lines.

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| Period | Gross Return | Net Return | Differential |
|---|---|---|---|
| 1 year | 6.17% | 5.54% | 0.63% |
| 2 years | 12.72 | 11.38 | 1.34 |
| 10 years | 81.94 | 71.39 | 10.55 |

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