

International Alpha Q3 investment update

October 2024

Investment manager Tom Walsh and investment specialist Andrew Brown give an update on the International Alpha Strategy covering Q3 2024.

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Andrew Brown (AB): Hello. Welcome to the International Alpha third quarter update. My name is Andy Brown. I'm an investment specialist for the International Alpha Strategy, and I'm joined today by Tom Walsh, co-head of the International Alpha Investment Team and a member of the Portfolio Construction Group.

So, over the next 10 minutes or so, we plan to talk a bit about performance, about some of the ideas that have made their way into the portfolio recently, what the team has been up to, and then we're going to try and end with some optimism for the future. Tom, hi.

Tom Walsh (TW): Hello.

AB: Thanks for joining. Let's start with performance. I guess it's been a slightly more encouraging quarter. Can you talk a bit about that and what this means for the longer-term performance as well?

TW: Yes, as you say, it's been a more encouraging quarter. The strategy at absolute terms rose in high single digits, slightly better than the benchmark. Encouraging early signs. **It's** a very short period obviously, but over 12 months, the strategy is now also ahead of the benchmark and that follows on from 2023 calendar year when obviously we also outperformed the benchmark. So, we're very aware that our longer-term numbers, the three-year and five-year rolling performance is below what we would hope to deliver for clients and below what our clients have a reasonable expectation for us to deliver. We see these as signs of improvement and certainly encouraging that the strategy really is starting to move as we would hope.

AB: Well, that's encouraging. So, it sounds like momentum is tentatively beginning to turn. In terms of the stock-specific contributors, can you talk a bit about that? What did well over the quarter?

TW: Yes, it's striking really how diverse a range of companies appears in the top contributors with all the noise around Japan and China, you might expect that was dominating. But actually, it's a really broad range of companies by industry, geography and type of growth company that are contributing to the performance of the portfolio over the last three months.

The top contributor would be MercadoLibre. It's one we've often spoken about over the years. It's Latin America's leading e-commerce business continues to perform very strongly. So, they had results during the quarter that were much better at both top line and profit than the market was expecting, and the shares performed strongly on the back of that. That's really encouraging. It's been held for over 14 years in the strategy and to see that company continue to go from strength to strength so many years later is really great.

A very different type of company, also one of the biggest contributors was DSV, that's a Danish freight forwarder. The shares reacted very positively to them securing the purchase of one of their competitors, a company called DB Schenker, which they won after a protracted auction process. Clearly, it's a large deal and that brings some risks. But this is the core competence of DSV, it's one of the core parts of our investment case for the company, its ability to consolidate the freight forwarding industry, to improve the businesses it owns and also generally to improve its overall levels of profitability. So really excited and enthusiastic about seeing such a range of different companies contributing.

AB: Yes, that's good to hear. Stock picking coming through and being rewarded. As always, there are stocks that do less well. One that caught my attention, I was a bit surprised actually, was Samsung Electronics, featuring as the largest detractor. It feels strange that, given the excitement around semiconductors, and some of the narrative around artificial intelligence driving growth. Can you talk a bit about that?

TW: Yes, Samsung has had a trying period of late. It is one of the larger holdings in the portfolio precisely because we're enthusiastic about its exposure to the growing semi industry and also continued accelerated investment in artificial intelligence related computing and infrastructure.

The challenge they've had over the last quarter or so has been around a very particular type of high-performance memory that is particularly in demand for new artificial intelligence investment, and they've been having some manufacturing problems with getting that out of the factory gates as they would like to. That's led to them losing some market share in that key high-growth market at the moment, and that's led to them falling behind a little.

That specific issue has been compounded by some cyclical worries around the semi-industry more broadly. It's, as I say, over the long term still one we're very enthusiastic about. But as we've emerged from one of the longest and most protracted down cycles in recent times, that recovery has been a little bit more sluggish than some people were expecting and hoping for, and you've seen that feeding through into some downgrades to expectations in the second half of this year and into the first half of next year. That's affected Samsung. It's also affected some of our other semiconductor-related holdings, such as ASML and Technoprobe.

AB: Thank you, that's very helpful.

And just moving on to new ideas in the portfolio. Some might say we've become a little bit narrow in the idea generation during that period towards the end of Covid. I know the team's been working very hard at trying to broaden the funnel of ideas at the bottom. Can you talk a bit about that and then maybe link it into what we've been doing during the quarter? Because it feels like there's been more activity than our clients are perhaps used to seeing.

TW: Yes, we've always been a diversified growth strategy and we always look to invest across the full range of growth opportunities that are available to us in the international universe. It's very much one of the lessons we've tried to take from the difficult period in 2021-22, to make sure that we continue to do that and make sure that the ideas coming through our research funnel are as diversified as possible and we really are tapping all the opportunities available to us in the market.

And I've been really encouraged to see how that's come through in terms of the research that we're discussing and ultimately in the holdings that we've taken. So, in the last quarter, we took four new holdings, which is quite a high number by the long-term history of the strategy. One of them was Roche, which is the Swiss pharmaceutical giant. I imagine many people have heard of them.

Another was Stella Jones, which I'm guessing fewer people have heard of. That's a Canadian business, specializes in the manufacture of electricity pylons. And it's managed to carve out really quite a strong position in a niche market that's very favourably positioned to growing energy infrastructure spending across North America over the next decade and beyond.

So, both of those fairly steady compounding type businesses. We've also taken new holdings in two much higher growth companies. One was a company called Kaspi, which is a Kazakh super app. It's used by over 70% of Kazakhstan's population. And the other would be Money Forward, which is a Japanese software business. Again, fairly rapidly growing company.

Quite different businesses, obviously, across very different parts of the world. The common factor about them all is they're great growth businesses in our view. And we see potential for them to grow their profits and their share price at an above market rate for the next five years and beyond.

AB: That is an eclectic mix of businesses. Very interesting to hear more about that. Moving on to what the team has been up to more broadly, last year we talked about I think it was 22 different investment trips that the members of the team were involved with. What's been the activity level this year and maybe talk a bit about some of those trips and some of the meetings that have been interesting.

TW: We've been busy as ever getting out on the road and seeing new companies, seeing prospects, seeing existing holdings. So, in the last few weeks we've been out to Germany, to Ireland, to Italy, to Japan and to the Netherlands. And just coming up in the next few weeks, one of the analysts from the desk is off out to China. He is very excited to be spending a couple of weeks out there scouting for new ideas. Slightly disappointed because this trip has been in the pipeline for a few

months, so disappointed to see the market rallying so hard before he gets out there to meet these companies. But really, it will be very interesting to see what he comes back with.

I was lucky enough to spend a couple of days in the Netherlands a couple of months back, and met with IMCD, which is a long-standing holding, but also with ASML, where I was able to spend an afternoon with the new chief executive there and a number of other senior executives. Really doing a deep dive into the business, both the changes in leadership that that company's had over the last year and also the development of next-generation technologies they continue to bring through. So really taking advantage of what is a long-standing and close relationship with that company to get, I guess, a quality interaction much higher than perhaps we might get just via a Zoom call on a standard roadshow.

AB: Well, it sounds like there's been lots going on and lots of engagement with companies, which is great to see. Tom, it's always good to end on a positive note. As we close off this update, I'm keen to hear your thoughts on what makes you optimistic on the portfolio from this current juncture.

TW: I think there's lots of different things. It's encouraging to see that performance is becoming more stock-driven and a more diverse range of companies that are driving performance rather than as a narrow number of themes. So, that's encouraging to see.

I'm encouraged by the range of new ideas that are coming through our research funnel and indeed the number of diverse ideas that are making their way into the portfolio. I'm encouraged by the operational performance of the companies we invest in. And by the balance of the portfolio that I see, you've got this established excellence, many of these long-standing holdings like DSV and MercadoLibre that have been in the portfolio for a long time and continue to deliver outsized returns to the portfolio, but also this emerging potential of new holdings that are coming in enhancing the quality and growth characteristics of the portfolio.

And those characteristics you can see in terms of the financial metrics that come out. Independent estimates suggest that the aggregate or average portfolio sales growth is at an 80% premium to the market over the next three years, EPS growth at 40% premium, free cash flow margins at 70% higher than the market. So, these are profitable businesses, not just growth, but profitable growth. and a vastly superior return on equity as well despite having almost no debt on the balance sheet.

So, strong companies delivering strong growth and, we know these are estimates, you can't anchor off them too closely, but they are highly supportive of our investment hypotheses and if these companies can deliver on our expectations, we're confident that the share prices will follow.

AB: Signs that performance is turning, long-standing holdings continuing to deliver, some exciting new ideas coming through and favourable portfolio characteristics. That sounds like a good point to finish on. So, thank you very much for your time, Tom, and thank you everyone for listening.

International Alpha

Annual past performance to 30 September each year (net%)

	2020	2021	2022	2023	2024
International Alpha Composite	23.7	15.4	-38.3	18.7	31.0
MSCI ACWI ex US Index	3.4	24.4	-24.8	21.0	26.0

Annualised returns to 30 September 2024 (net%)

	1 year	5 years	10 years
International Alpha Composite	31.0	6.5	6.5
MSCI ACWI ex US Index	26.0	8.1	5.7

Source: Revolution, MSCI. US dollars. Returns have been calculated by reducing the gross return by the highest annual management fee for the composite. 1 year figures are not annualised.

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