

Santander GO Global Equity ESG

6 / 2024

Fund commentary

Market developments:

Global equity markets have been hitting new all-time highs (+3.3% in EUR, +2.0% in USD), mainly due to many of the index heavyweights staying out of the macro crosshairs. Across regions, the European election anxiety was offset by a benign inflation print across the Atlantic, giving some reassurance for the rate cut camp. Meanwhile the Japanese market continues to blossom as well. The seismic shift in monetary policy and governance activism has attracted a large crowd of foreign investors, getting recommitted to the land of the rising sun in a way we haven't seen for many years. Globally, it's fair to say, though, that the overwhelming majority of stocks has not yet received an invitation to that same party. Hence, as the existing market concentration gets prolonged, there seems an elevated amount of anxiety is creeping in underneath the surface. There are plenty of banana skins that can put markets off balance, so we need to stay eagle-eyed in case current momentum starts to waiver.

Largest holdings:

Our top active position is Alphabet, as we believe that with its leading positions in Search, Cloud and the investments into its AI platform, Alphabet has a long runway for growth with attractive returns. To us, Alphabet looks undervalued and is currently not treated as an AI winner, which we think is unjustified. Hitachi, an attractively valued Japanese industrial conglomerate, is our second largest active position, and is a key player in the energy transition given its broad suite of infrastructural and electrical equipment products. AstraZeneca completes our top-3 active positions and is a UK pharma company that enjoys one of the strongest product pipelines in pharmaceuticals, while at the same time having low risk to patent expiries.

Performance:

In June, the portfolio had both a strong absolute and relative performance versus the benchmark. Sector-wise, our positioning in Industrials, Energy and Consumer Discretionary helped performance most, while we did not experience any particular detractor from any sector during the month. In terms of stock selection, by far most positive contribution came from IT infrastructure play Broadcom, which posted very strong earnings and raised guidance for the full year.

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The demand for custom ASICs, networking solutions as well as more software renewals for the acquired VMware business helped boost results. Also, the stabilization in non-AI related end-markets such as telecom, broadband and storage, was well-received by the market. Japanese Hitachi also continued its ascent given its favorable exposure to strong themes such as electrification and grid modernization. Hitachi also sold its 40% stake in the HVAC JV it has with Johnson Controls, proceeds of which that will likely be returned to shareholders. Within healthcare, Eli Lilly was once again our best performing holding, as its drug against Alzheimer's disease 'donanemab' got a positive nod from the FDA advisory committee. Eli Lilly also showed positive data around its treatment for obstructive sleep apnea (OSA), solidifying its position around many obesity related illnesses.

On the flipside, we saw performance detraction from Australian miner Fortescue, hurt by lower iron ore prices as the Chinese property market remains in the doldrums. Ample ore inventories and weak steel margins is pressuring overall steel output. Even at these lower iron ore price levels, though, Fortescue is still generating lots of cash, so any risk to its generous shareholder return policy, we feel, is greatly overblown. Credit card operator Visa also struggled somewhat during the month as a US federal judge has rejected a settlement between the likes of Visa and merchants, potentially resulting in less favorable terms for the card operators as they need to renegotiate with the merchants.

Portfolio changes:

In June, we switched out of farm equipment maker Deere & Co. as we feel the company is doing what it can to manage a prolonged Ag downcycle, but any stabilization let alone earnings recovery remains delayed. This urged us to move into better alternatives such as Union Pacific, a US railroad operator. As the freight downcycle is nearing its end, we think Union Pacific is one of the better names to benefit from a potential upturn, helped by its improving service metrics and strong operating leverage. Another name we added during the month has been Deutsche Telekom, enjoying a very high FCF yield against a very stable industry backdrop. Even though domestic spend levels remain elevated as the company rolls out fiber-to-the-home, the investments of the T-Mobile USA merger with Sprint are largely done, opening the door for attractive shareholder returns. Furthermore, to safeguard valuation discipline, we have taken profits in several more expensive names (e.g., Microsoft, Costco) and added to higher FCF yielding holdings (e.g., Cheniere Energy, Mercedes-Benz).

Management expectations:

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As we head into the summer lull of lower liquidity and fewer corporate events, the search is on for data points that will keep markets in check. On the macro front, we need to keep a close watch on electoral sentiment swings, escalating tensions in the middle east and the unknown trajectory of the Ukraine war. Also, as the higher-for-longer rate picture finds its way in the real economy, the hope for a V-shaped recovery is fading too. This again plays into the hands of the same behemoths dominating market behavior for well over a year now, likely confirming their status quo as safe havens for the time being. Valuations might look full, but fund flows in these same cohorts show little signs of fatigue, certainly as a rotation into cheaper, underperforming value stocks still looks risky. In terms of portfolio construction, it again comes down to balancing the momentum winners with more attractively valued names with sound fundamentals.

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