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# GLOBAL EQUITY MARKETS: A TALE OF TWO HALVES

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Global equity markets finished the year down 9% percent and our portfolios suffered an 8% percent decline. If we look at the global equity markets, it was really a tale of two halves. January was very strong with markets up 5.5%, but what we found is as the year progressed, certain concerns crept into the market, including emerging market concerns in areas like Turkey and Brazil, which have a sovereign debt crisis. And also the Chinese market started to suffer as investors questioned the ability of the world's second largest economy to keep growing at the sort of pace it did over the last 10 years.

As fundamental equity investors, we used the initial strength during the course of the year, especially in the US market, which initially held up much better than the rest of the world, to keep reducing our US exposure in the portfolio. This was purely based on fundamentals. So names like Moody's Corporation and Mastercard towards the fourth quarter of last year were disposed of in total, after very significant gains over the last five years.

What we started to find is that the emerging markets started to come down significantly, in the case of China 25%, Turkey was done up to 50% at one point, although we have no exposure in that country. We have made some changes in the portfolio where emerging markets, based on revenue generated for our portfolio in those relevant areas of the world, is now as high as 30%, which is the highest it's been for the last five years. We find as global equity investors that when the news flow is quite bad, often that presents us with opportunities to increase in areas of the market which might seem out of favour in the short term, but where the long-term – a three to five year time horizon – kicks in for us and might turn out as a good outcome for our investors if we make these acquisitions today.

Some of the other new names that came into the portfolio include businesses like facebook, rather controversial in the short term. We believe that as that industry gets more regulated over time, businesses like Alphabet or Google and facebook would actually be in a stronger position to navigate some of the data privacy concerns that are making headlines at the moment, at a time when these stocks are actually trading at very favourable valuation levels.

We've also initiated a position in Sage Software. They released results last week, which we continue to believe will set the path for future returns, because they showed 7.6% organic growth rates. We believe they will be successful in the long-term transitioning of their business to a subscription-based software model, just as Microsoft did over the last five to six years.

When we look at some of the concerns we have in the world, clearly Chinese debt levels have exploded over the last 10 years. There've been a lot of corporate bonds issued which will put strain on those businesses that are over geared. But the way we invest in our high quality portfolio is to stay away from businesses with high gearing. So obviously we're not going to invest in areas like European banks and Chinese banks. Instead, we want to make sure that we invest in very solid growth dynamics through areas like digital advertising and software cloud-subscription based models. And that's why names like facebook and Sage have forced their way into the portfolio.

We also believe that when we look at the last five years where we've generated close to 7% compound returns in dollar terms, which far exceeded the average global equity investment at 2.4% compound growth, that might well continue for us in terms of our absolute return targets for the portfolio. It's always dangerous to put a target out there, but given that our portfolio companies typically grow their earnings by 7% to 10% in the long term and our valuation levels are now at price earnings levels of 17 – which is much more favourable than a year ago – we think that over the long term, these are the sort of returns that our investors can expect going forward and we look forward to the challenges that this new year holds for us.