COOPER INVESTORS
GLOBAL EQUITIES FUND (HEDGED)
QUARTERLY COMMENTARY REPORT

Cooper Investors Pty Limited AFS Licence Number 221794 ABN 26 100 409 890

For current performance information please refer to the Monthly Performance Report.

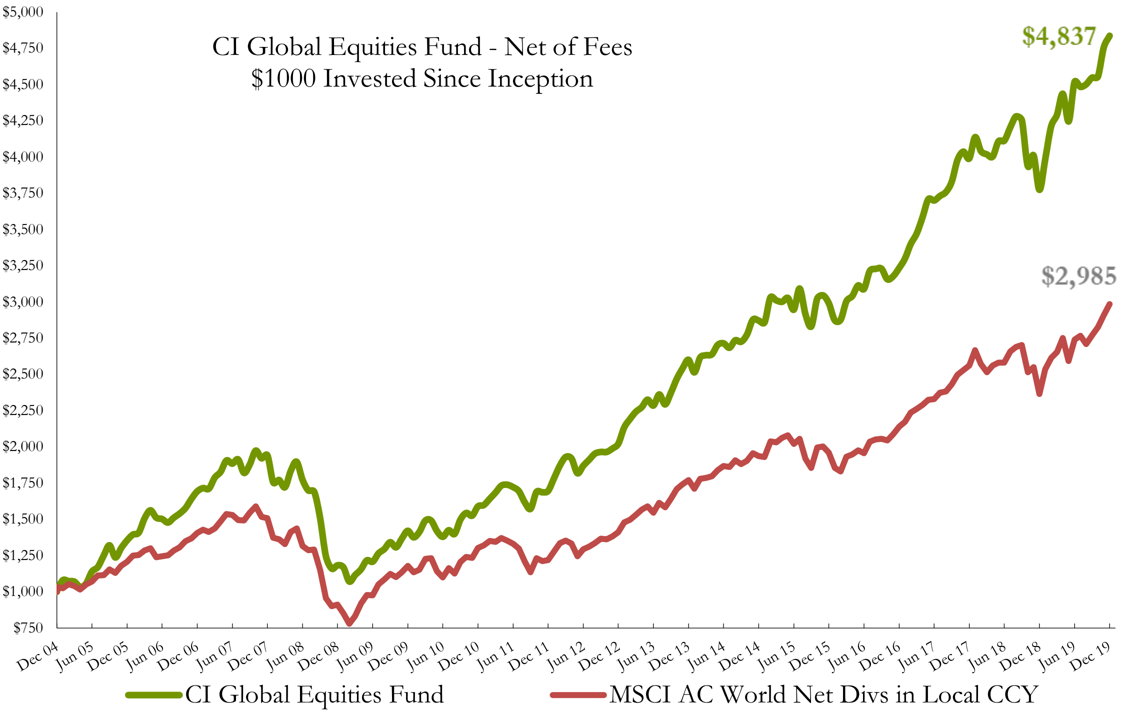
DECEMBER 2019

*"Human capital will go where it's welcome and stay where it's well treated." **Walter Wriston***

*"You cannot describe passion, you can only live it." **Enzo Ferrari***

	**PORTFOLIO	#BENCHMARK	VALUE ADDED
ROLLING 3 MONTHS	6.34%	7.73%	-1.39%
ROLLING 1 YEAR	28.17%	26.24%	1.93%
ROLLING 3 YEAR	14.38%	11.76%	2.62%
ROLLING 5 YEAR	10.99%	9.04%	1.95%
ROLLING 7 YEAR	13.27%	11.29%	1.98%
ROLLING 10 YEAR	13.03%	9.74%	3.29%
SINCE INCEPTION*	11.02%	7.52%	3.50%
SINCE INCEPTION^	383.66%	198.54%	185.12%

*Annualised
^Cumulative (1 December 2004). Initially, the Fund invested predominately in Australian equities. However since May 2006, the Fund has been invested in a broad range of global equities.
**Net of fees and expenses
MSCI AC World Net Divs in Local Currency



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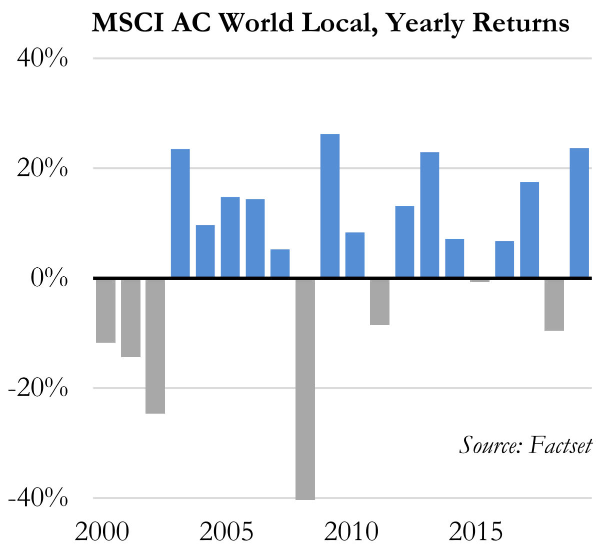
Market and Portfolio Performance

Markets surged into year end with the MSCI AC World (in local currencies) adding +7.73% for the quarter. The index has closed out 2019 with an annual gain of +26.24%. Not only an impressive turnaround after the 20% slump that occurred at the end of 2018, but also the strongest year of the decade.



And what a decade it has been for the index – only two notably negative years and a total shareholder return including dividends of +153%, equivalent to an annualised CAGR of almost 10% per annum.

Back to this year and once again the US and particularly the technology sector has led the rally – the S&P 500 and the NASDAQ gained +29% and +35% respectively.

Up against a very strong bull market the portfolio has performed well in 2019. In the context of an underweight to the US and zero ownership of 'FAANG' stocks we would have been happy to keep up in a year when the market does almost +25% led by the NASDAQ. In fact the portfolio has managed to outperform by several percentage points. This was driven by a few factors.

First, ongoing execution by management of companies that are large core positions. Stocks like **Danaher**, **S&P Global, Halma** and **Aon** are top 10 portfolio weights that we've owned for 4, 6 and 10 years plus. They continue to deliver on their potential with strong market positions, focused and engaged management teams and numerous opportunities to create and realise value latency. Each rose +45-60% this year.

Secondly a number of newer positions delivered strong performance immediately. **Fiserv, Ferrovial** and **Shimadzu** are all 2019 purchases that have risen ~40% or more from their inception price. Our patient approach of buying watchlist stocks that have fallen out-of-favour means we rarely generate material outperformance in the first year of ownership – but of course it can happen.

Thirdly we have been fortunate to see no real 'blow-ups' in 2019. Although there were the usual suspects of large one-day moves from the quarterly earnings cycle, most recovered subsequently. Only one stock, **PTC,** delivered a negative absolute return for the year and that was a mid-single digit decline.

We believe consistent and enduring performance is more meaningful than outperforming in any one year so as we move into the next decade it is worth briefly reviewing the long term numbers. On an absolute basis the portfolio has returned +13.03% pa over a decade and on a relative basis is compounding capital each year at 3.29% better than the benchmark. The portfolio has now been in operation for 15 years and since inception has returned +11.02% absolute and +3.50% relative per annum.

Meanwhile for the quarter the portfolio returned 6.34% versus the benchmark which returned 7.73%. The AUD had a strong bounce, gaining around 4% versus both the US Dollar and Japanese Yen, and 1% to the Euro. AUD fell 2% versus Sterling which surged after the election result.

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The biggest contributors to performance in terms of total shareholder return included:

1. **Shimadzu** – Strong sales for instruments in Japan and Europe offset weakness in China
2. **St. James Place** – Domestic financials rallied over the period of the UK Election
3. **Techtronic** – Continues to outperform peers in both sales and innovation levels

The biggest detractors to performance in terms of total shareholder return included:

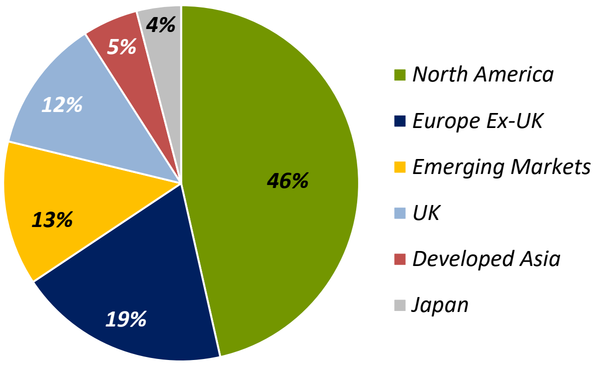
1. **CME** – Softer on lower levels of volatility in markets
2. **Constellation** – Lagged the market on no news (up 45% year to date)
3. **Baxter** – Fell after disclosing an accounting error, subsequently investigated and rectified

The Portfolio

The portfolio is diversified by country and sector:

No. of Stocks	*41*
Region Weights	*US 52%*
(by listing)	*Europe 23%*
	Asia inc. Japan 10%
Most OW Sectors	*Industrials, Financials*
Most UW Sectors	*Energy, Consumer Disc.*
Cash	*4%*

Geographical Exposure by Source of Revenues#



#Derived on a look-through basis using underlying revenue exposure of individual Fund stocks

The portfolio is also positioned around Subsets of Value:

- **Growth companies** (37%) – growing companies with identifiable value propositions using traditional value metrics and run by focused, prudent and experienced management (Costco).
- **Stalwarts** (41% of the portfolio) – sturdy, strong and generally larger companies with world class privileged market and competitive positions (AON).
- **Low risk turnarounds** (2%) – sound businesses with good management and balance sheets. (Envista).
- **Asset plays** (5%) – stocks with strong or improving balance sheets trading at discounts to net asset value or replacement value (Liberty SiriusXM).
- **Cyclicals** (7%) – stocks showing both upside and downside leverage to the cycle with experienced and contrarian managers who allocate capital prudently. (Ametek)
- **Bond like equities** (5%) – stocks with secure, low-volatile dividends that can be grown and recapture inflationary effects over time (Getlink SE).

Buys

The portfolio initiated a position in US-listed **Yum China** during the quarter.

Yum China ["YUMC"] is the largest restaurant group in China operating almost 9,000 restaurants (of which only 9% are franchised) including over 6,000 KFC's and over 2,000 Pizza Huts. YUMC was fully spun off from YUM! Brands in November 2016 and pays a 3% royalty fee on system revenues to its former US parent, in return enjoying exclusive rights to use those brand names in China.

Whilst on the surface YUMC appears to be "just another Master Franchise" our research process highlighted that over YUMC's 32-year history they developed an owner-operator culture distinct from YUM! Brands and distinctly Chinese. This has allowed YUMC to create a highly localised customer proposition benefitting from a strong local appetite for chicken and become the clear market leader. Released from the shackles of a distant decision-maker we observe that YUMC have succeeded in developing an agile and entrepreneurial philosophy that has resulted in richer and deeper IP than YUM! Brands. This is particularly evident in areas like Menu Innovation and Digital (over 95% of KFC transactions are completed digitally) where they are arguably now the global leaders.

KFC is the key value driver for YUMC, representing ~70% of units, ~90% of profits and given KFCs highly attractive new unit economics, 90% of new units. When most people in Australia think of KFC they typically picture a big bucket of fried chicken. Yet KFC in China has a far broader menu that caters to local tastes, such as serving Congee during the breakfast daypart and localising taste profiles to suit regional palates, such as spicier recipes for the Sichuan province. In addition, KFC regularly create new dishes to stoke consumer demand or adjust to price changes. A recent example of innovation and flexibility was switching to duck wraps and mushroom burgers to offset soaring chicken prices which were indirectly affected by African Swine Flu. YUMC have navigated this significant supply chain event with negligible margin erosion.

YUMC is an underappreciated Chinese Stalwart given a stable, simple and cash generative business model run by a highly driven owner-operator culture. Management have several exciting value latencies to execute including new KFC roll outs, improvement of Pizza Hut margins and development of new formats. In addition to growth opportunities a net cash balance sheet and strong cash flow profile means YUMC can provide attractive and growing distributions (currently ~3% combined dividend and buyback).

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In the prior quarter we mentioned the buying of a UK Watchlist stock - this is **Diploma PLC**, a Growth stock we have been following for years. The investment proposition is very much a story of Pattern Recognition.

Firstly Diploma is a 'Capital Allocator Champion' with many of those same cultural attributes and a similarly outstanding track record of capital discipline as other portfolio holdings that sit in this cluster.

Secondly it operates in areas in which we have deep knowledge and a history of successful investment such as surgical devices, diagnostics and connectors. These are niches with secular growth, fragmented supplier bases, high degrees of consumables (recurring revenue) and high cost of failure (requiring skilled procurement) all of which tend toward strong economics for successful players in the value chain.

Diploma is a specialty distributor rather than a manufacturer - its business model targets sub-niches with higher complexity where value-added services are required; surgical kits for endoscopy procedures or optimised wiring assemblies for an F1 car. This has enabled financial performance at significantly higher margins than a typical distributor while returns on invested capital and long term shareholder outcomes have been exceptional. Like many UK stocks over the 'election quarter' the share price has risen sharply in the final months of 2019 to close the year near £20 versus our first buy price of £15.64, however we still see a long runway for Diploma to sustain its trajectory of doubling in size every 4-5 years.

A key part of the model is acquisitions and Diploma typically add a mid-single-digit level of inorganic sales yearly with a history of counter-cyclical buying, operating on the basis that prices are better when sellers are fearful. As a smaller stock (Mcap of US$3bn) Diploma is at a similar stage in its lifecycle to where Halma was 5-6 years ago and is wisely building management bench-strength to ensure scale for ongoing growth.

Sells

We divested the small position in **Japan Exchange Group**. When we initiated the investment we identified a number of attractive value latencies including the development of their Data and Derivatives business. Whilst these latencies remain our recent interactions with the company have led us to revise down our view on the intentionality and expected pace of management's execution of these. In the meantime more attractive opportunities presented themselves.

Stock News

December saw a slew of positive news from **Ferrovial.**

Firstly the sale of Broadspectrum to Ventia (a provider of infrastructure services in Australia and NZ) marked the first significant piece of business in the strategy to exit Services. The divestment process has proven more difficult than hoped - initially it appeared a large private equity buyer would purchase the lot but the outcome now looks more piecemeal with smaller local players taking out specific chunks. Though the process now drags out longer our discussions with management indicated confidence that it should lead to a better result. The price achieved for Broadspectrum backs this up – proceeds of €330mn is ~20% higher than analysts had expected.

Secondly the refinancing of Ferrovial's major Managed Lane ["ML"] asset in Texas, the North Tarrant Expressway was announced wherein the weighted average cost of debt was lowered by almost 200bps, from 5.45% to 3.47%. While the reduction is partially explained by lower interest rates since the initial financing, we see the size of the delta speaking more to the maturing nature of the risk profile of MLs as an asset class. The company's other Texan ML 'LBJ' can be refinanced next year and a similar outcome should benefit a stronger ramp up of distributions from the MLs over the next 5 years.

Finally the result in the UK General Election was welcome at Heathrow Airport where a long-planned expansion and third runway has been a political stoush. The Conservative manifesto confirmed Government support for the expansion which should lead to a considerable increase in the current regulated asset base of ~£17bn. The masterplan looks for capacity growth to 130mn passengers by 2035, an increase of over 50% from this year's 80-85mn. Heathrow announced a £500mn dividend for 2019, 25% higher than had been previously expected. Ferrovial's share of this plus consideration for Broadspectrum adds a further half a billion Euros into their existing cash pile of €1.2bn with numerous opportunities for deployment.

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As mentioned in the prior quarterly, **Danaher** [“DHR”] spun out its dental assets into a new listed company, **Envista Holdings** [“ENV”] via an IPO. In the third quarter DHR listed 20% of ENV and retained an 80% holding. The portfolio participated in the IPO and has held a position in ENV as well as retaining its long term holding in DHR.

This quarter DHR sold its remaining 80% stake in ENV via a share split. This means DHR shareholders had the option to exchange DHR shares for ENV shares at a discount, on a pro rata basis (DHR market cap of $100bn compared to ENV at $4bn). The portfolio tendered DHR shares for ENV shares but the offer was sizeably oversubscribed and the outcome was an immaterial exchange of shares.

However it does set a new chapter in the lives of both DHR and ENV. ENV is now a 100% free float listed entity and the sell out by DHR removes any parent sell-down overhang. So too DHR will start 2020 with a clean slate having completely sold out of ENV and further focusing on life sciences and diagnostics as well as the upcoming completion of the GE biopharma deal.

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In November **PTC** provided updated long term financial targets to the market. This was an important step for the company following twelve months of underwhelming execution which ultimately led to management pushing out previous targets by 12 months.

New CFO Kristian Talvitie also changed the metrics which PTC will use to guide and measure its performance with a clear focus now on Annualised Recurring Revenue (ARR) and Free Cash Flow. This makes a lot more sense for PTC which following a transition period is now almost entirely a subscription-based software company.

PTC’s base case is for US$2.3bn in ARR (a key metric for software subscription companies) and US$850m in Free Cash Flow for FY24. The ARR projection requires mid-teens growth which we believe is achievable given PTC’s portfolio mix. First, their well-established Computer Aided Design software used by the manufacturing industry should grow at a high single digit rate. This is combined with market leading software for applications in the secular growth areas of ‘Industrial Internet of Things’ and ‘Augmented Reality’ which are growing in the 30-40% range. Our extensive work meeting with industry participants indicates to us that PTC’s products are very high quality which supports this growth outlook.

PTC also provided downside and upside ranges for FY24 Free Cash Flow which, depending on macro outcomes, could range from US$700m to US$900m. With a market capitalisation of $8.7bn, PTC trades at ~10x their long range target. PTC’s design software and broader subscription software peers most often trade at 25-30x FCF. The point here is that if PTC execute we see material value latency in the shares.

Trip News

2019 finished with another busy quarter of travel with the team visiting the US, UK, Spain, Switzerland, China and Japan.

We were in Shanghai on “Singles Day” (so chosen on 11/11 as the number "1" resembles a lone individual) which was popularised by Alibaba and has become China’s largest shopping event. This year Alibaba alone sold over US$30bn of goods on the day. Whilst this makes for great headlines we are still developing our thinking on what the increasing importance of sales events in China means for the economics of retail platforms or consumer brands.

During the day as we discussed industries and companies with former executives we noticed they would frequently check their phones to get an update on the metrics of their own ventures' selling (typically on one of the e-com platforms). It is a country that feels like every citizen is in some way an entrepreneur. This reminds us of Frenchman Duc de la Rochefoucauld-Liancourt's description of late 18th century America: *"He marvelled that every inhabitant seemed to cherish the project of making an ample and rapid fortune… few of them are contented with what they have."*

Our research efforts on **Yum China** led us to explore the trends in China's thriving food delivery industry. The blend of high urban density and low cost labour have created ideal conditions for food delivery services that has created a compelling customer proposition when combined with rapid technological change and the learning curve of the platforms This has led to widespread adoption particularly amongst millennials who order 2-3 meals per day delivered to their office or homes.

This is no longer a niche area with penetration rates around 11% of sales for the entire catering industry and as high as 20% for players like Yum China. It continues to grow significantly faster than overall food sales so penetration will increase with long term predictions that it could reach 20-40% of industry sales.

Participants will need to adapt their models to be able to profitably operate in that environment – one of the challenges facing the industry is the employment standards of delivery drivers. They typically charge the platforms RMB7 per trip (around AUD1.45) for items delivered on time. But the stresses and safety risks of trying to meet the challenging schedules appears to be resulting in poor working conditions and there may be a need to increase their compensation which will increase unit costs.

Arriving into Tokyo from Shanghai provides an interesting juxtaposition between two of Asia's most important cities and indeed the two economies. From bustling Shanghai to the more measured pace of central Tokyo. Notwithstanding Japan's slower pace we continue to see signs of positive change afoot in Japan. The week after our visit Shinzo Abe become the longest serving Prime Minister in Japan's history and his stability has been a crucial factor in driving Japan's reform agenda. The results of this reform are evidenced by several 'Japan Inc.' companies taking further governance steps this year, most recently Hitachi divesting Hitachi Chemical in December. Such a move towards increased simplification and focus of a former *zaibatsu* would have been unthinkable in the pre-Abe era.

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In the US we spent time on the West Coast visiting several portfolio holdings and Watchlist stocks. We met with a number of businesses as we scour the market for stock specific opportunities, meeting with companies from several different sectors including medtech, entertainment, shopping malls, industrials and technology. The software and technology industry is one we see as a maturing space in the sense that we are finding more companies aligned to our values and way of thinking.

Software and technology is not the only growth industry out there but it is a large and growing space. Historically we have mainly invested in this space via two areas; software companies that are dominant in their niche area (e.g. **Fiserv**) or incumbents that have evolved with the times (e.g. **IQVIA** or **Amadeus**).

What is exciting for us today is more businesses in these areas are beginning to fit our VoF criteria. In the past our observation was that many software businesses that were growing rapidly had suboptimal earnings or financial quality – excessive stock options or lack of capital deployment prowess deterred us from many stocks. However, with the growth and development of the technology industry and the companies in it we are starting to see more management teams and boards value the same dynamics as we do.