

**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.

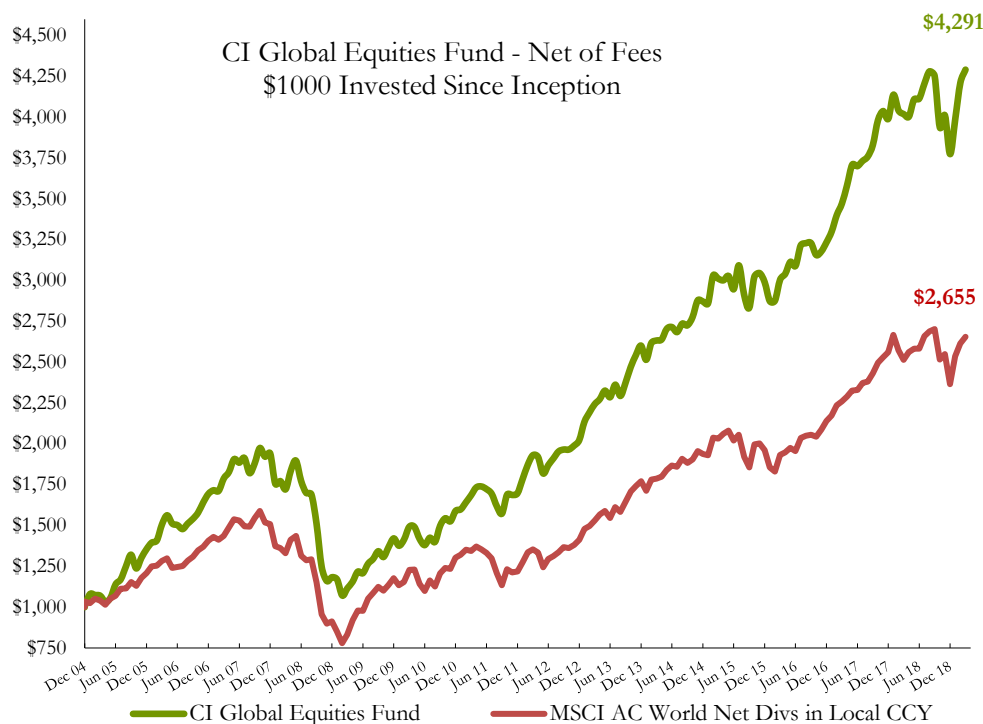
**MARCH 2019**

*“Do you know the only thing that gives me pleasure? It’s to see my dividends coming in.” **John D. Rockefeller***

*“Mediocrity is never worth the trip.” **Sergio Marchionne***

	<b>**PORTFOLIO</b>	<b>#BENCHMARK</b>	<b>VALUE ADDED</b>
ROLLING 3 MONTHS	13.70%	12.28%	1.42%
ROLLING 1 YEAR	6.77%	5.61%	1.16%
ROLLING 3 YEAR	12.62%	11.19%	1.43%
ROLLING 5 YEAR	10.27%	8.24%	2.03%
ROLLING 7 YEAR	12.09%	10.10%	1.99%
ROLLING 10 YEAR	14.42%	12.30%	2.12%
SINCE INCEPTION*	10.70%	7.05%	3.65%
SINCE INCEPTION^	329.07%	165.52%	163.55%

\*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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**MARCH 2019**

## Market and Portfolio Performance

The first quarter of 2019 has once again proven the perils of trying to time the market. Global equities have rebounded quickly from the Q4 2018 correction with the S&P500 recording its strongest Q1 in around 20 years. At March end the index is only a couple of percent from its all-time high back in October yet fund flow data suggests a lot of money that fled the market in late 2018 has yet to return.

The market decline saw valuations in the beginning of the year become attractive once again (as it turns out, all too briefly) and we tried to make the most of the fall buying four new positions in high quality Watchlist stocks: Shimadzu, Amphenol, Ferroviol and Japan Exchange.

Broadly the portfolio had a good quarter with a strong reporting season. Of 40 stocks, 26 rose more than 15% in the period with only 3 positions delivering a negative absolute return. Many reported solid margin expansion, increased dividends, de-leveraged balance sheets and share gains in key end markets.

Consider Techtronic, a leading manufacturer of power tools for professional contractors. Despite concerns of the slowing US construction cycle and peers blaming everything from mortgage affordability and trade tariffs to the weather, Techtronic reported another exceptional year of double digit growth in its key Milwaukee brand driven by innovation and new product development. Dividends were increased by 26% and the balance sheet is now net cash. It's a good example of how highly focused management behaviour leads to peer leading financial outcomes for shareholders - the stock has rebounded 60% from its Q4 low.

We are confident of our portfolio holdings generating continued positive cash flow and earnings growth into 2019, while a notable feature of the quarter was several businesses (discussed in Stock News) announcing important acquisitions. Elevated M&A activity continues to be a theme across our Watchlist.

For the quarter the portfolio returned 13.70% versus the benchmark which returned 12.28%. The AUD was flattish for the quarter versus the US Dollar, fell about 2% versus GBP and JPY but gained 3% on the EUR.

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

1. **Constellation** – Announced strong results and a special dividend
2. **Danaher** – Shares rose on the back of the announced GE biopharma deal (See Stock News)
3. **Roper** – Delivered strong results and another software acquisition

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

1. **CME Group** – After a strong 2018 the stock sold off its high with moderating trading volumes
2. **Intercontinental Exchange** – Similar dynamics to CME
3. **Aleatica** – An index rebalancing impacted the stock which has a relatively small free float

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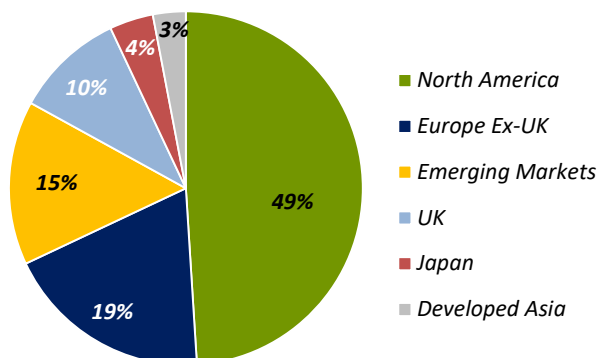
## MARCH 2019

### The Portfolio

The portfolio is diversified by country and sector:

<b>No. of Stocks</b>	40
<b>Region Weights</b>	US 51%
<i>(by listing)</i>	Europe 23%
	Asia inc. Japan 10%
<b>Most OW Sectors</b>	Industrials, Financials
<b>Most UW Sectors</b>	Energy, Consumer Disc.
<b>Cash</b>	5%

**Geographical Exposure by Source of Revenues<sup>#</sup>**



<sup>#</sup>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** (35%) – growing companies with identifiable value propositions using traditional value metrics and run by focused, prudent and experienced management (Costco).
- **Stalwarts** (38% of the portfolio) – sturdy, strong and generally larger companies with world class privileged market and competitive positions (AON).
- **Low risk turnarounds** (3%) – sound businesses with good management and balance sheets. (Pentair).
- **Asset plays** (4%) – stocks with strong or improving balance sheets trading at discounts to net sset value or replacement value (Liberty SiriusXM).
- **Cyclicals** (10%) – stocks showing both upside and downside leverage to the cycle with experienced and contrarian managers who allocate capital prudently. (Ametek)
- **Bond like equities** (4%) – stocks with secure, low-volatile dividends that can be grown and recapture inflationary effects over time (Getlink SE).

### Buys

The Fund invested in two new Japanese positions during the quarter, **Shimadzu Corporation** and **Japan Exchange Group** [“JPX”].

We have been following **Shimadzu** for around 3 years and moved to initiate a position following the heavy sell-off in 4Q18 where the price stock declined by over 40%.

Shimadzu is based in Kyoto, a region we have long admired due to its ability to produce high quality companies. Kyoto companies are commonly focused on one or two high technology niches, contrasting them to the often distracted typical Japanese corporate. Founded by Genzo Shimadzu in 1875 the business initially made scientific instruments to support the nascent industrialisation of Japan during the Meiji Restoration. This focus on technology has been unwavering since then with one of their research team receiving the Nobel Prize in Chemistry in 2002. Today Shimadzu’s core business is in Analytical and Measurement Instruments, an industry we have been following and investing in for many years. We like the strong positioning of key players (including Shimadzu), their end market exposure to favourable tailwinds (including healthcare, environmental and food industries) and the high quality razor-blade business model producing recurring revenues.

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**JPX** is another company that has been on our Watchlist for a number of years and following our meeting with management in December 2018 our conviction in the company's ability to grow and diversify their revenues away from the cash equities business was increased. We initiated a position in January.

The JPX was formed following the merger of Tokyo Stock Exchange (equities focused) and Osaka Securities Exchange (derivatives focused) in 2013. Following a successful integration of the two exchanges today JPX is the world's 3rd biggest (and Asia's largest) equities exchange and the 16th largest derivatives exchange. Unlike other equities exchanges JPX is experiencing a growth in the number of listings through a vibrant IPO market and limited M&A. We're excited by the medium term opportunities to diversify the revenue streams through the growing information business and further growth of the derivatives business which will increase in scale following the upcoming takeover of Tokyo Commodity Exchange. Given the supportive role JPX is playing implementing the corporate governance reform in Japan we believe the regulatory environment should continue to be benign.

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In January the portfolio bought a position in **Amphenol**. Amphenol is a Watchlist stock we have been admiring and following for years and we pounced on an attractive entry point. The share price fall in Q4 2018 was only the 3rd time since the GFC that the stock had fallen more than 20%. By the end of the quarter the price is already nearly back at all-time highs.

Amphenol is one of the world's leading manufacturers of connectors and the company is unique in having a diversified revenue base with no industry representing more than 20% of sales. This means we expect Amphenol to continue to weather macro storms and grow at a rate above GDP given the electrification of many industries.

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The Fund also bought a position in **Ferrovial** during the quarter.

Spanish-listed Ferrovial represents a corporate simplification story with family backing and a net cash balance sheet at the holding company level. The long term reason to hold is the attractive and growing dividend streams from a portfolio of developed world infrastructure assets. These consist of the world's best toll road concession (ETR-407, a busy expressway going through suburban Toronto), a growing portfolio of 'managed lanes' in the US (dynamically tolled lanes that sit alongside an existing freeway) and a controlling stake in Heathrow Airport in the UK.

In an environment where listed infrastructure is trading at very expensive valuations Ferrovial trades at a significant discount due to a convoluted group structure whereby the bulk of P&L revenue comes from a low margin contracting business ('Services'). Wisely in our view the controlling Del Pino family have decided to exit the Services business meaning the future investment proposition for Ferrovial minorities becomes essentially all about the infrastructure risk and return profile. We expect this will lead to the discount to intrinsic value closing, in addition to a possible special distribution from the proceeds of the Services sale, along with further greenfield toll-road opportunities arising in the US.

## **Sells**

The Fund exited **Aalberts Industries** early in the quarter. The hypothesis of Aalberts becoming an industrial capital allocator champion ('CAC') in the vein of a Halma or Ametek is still valid, however culturally this is not an easy transition and progress will be slower than initially hoped. While management are doing

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a good job to this end a number of nearer term concerns around the balance sheet, earnings quality and operating trends in the European end markets drove our decision to redeploy the capital elsewhere.

We sold our small position in **MKS Instruments** at a loss to fund the Amphenol acquisition.

We also rotated the small position in **Prosegur** into Ferrovial where we see a better risk-adjusted value latency proposition.

## Stock News

This quarter **Danaher** announced its largest ever acquisition with the US\$21bn purchase of GE's biopharma business. The Fund is approaching 9 years as owners of Danaher Corporation. We are accustomed to the Danaher acquisition playbook and the company is one of the rare corporations that consistently creates shareholder value from its M&A investments. In fact a sizeable portion of the Fund is dedicated to this concept.

Over the last decade Danaher has morphed from an industrial focused business into one of the world's leading Diagnostics and Life Sciences companies. The GE deal fits perfectly into what we would expect from the company. The stock is up 4.5x over our holding period thus far adjusting for spin-offs. This return has been delivered through the business transition and today we see a higher growth, more recurring and predictable business with further margin expansion opportunities looking forward.

Another meaningful deal this quarter was **Brookfield's** announced US\$4.8bn acquisition of Oaktree Capital. The size of the acquisition is ~11% of Brookfield's market cap so it is not a 'bet the house' deal though it is headline-grabbing given the Oaktree founder and co-Chairman is famed investor Howard Marks. Oaktree listed in 2012 and, like many of its alternative investor peers has been a disappointing listed investment with the shares barely up 20% on its IPO price (including takeover premium).

The deal is structured in a way that Oaktree management retains their 38% stake in the business and the earliest they can completely exit is by 2029. This deal catapults Brookfield into the top tier of alternative asset managers. Our attraction to Brookfield is its big balance sheet of US\$25bn invested in high quality areas of property, infrastructure, renewables and private equity.

In February **Saputo** acquired leading UK dairy processor Dairy Crest Group for C\$1.7bn. Like Danaher, Saputo has an excellent acquisition track record and their continued consolidation of the dairy industry is a core feature of our investment proposition. The challenging environment for the industry is surfacing high quality M&A opportunities such as this and we are very supportive of Saputo using its scale, balance sheet and expertise to deploy capital in this counter-cyclical manner.

Saputo has typically targeted undermanaged or underfunded players, however with Dairy Crest they are buying a high quality and well run operation. The deal gives Saputo a platform in Europe which they can complement with additional acquisitions over time. Saputo have a truly global presence with scale operations in the US, Canada, Argentina, Australia and now the UK.

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**MARCH 2019**

## Trip News

In typical fashion we spent a number of weeks during the quarter in the US. A key standout trend was the intent by corporates to invest in technology and the urgency to do so. We have in a short space of time witnessed some big acquisitions and mergers in the name of scale – BB&T with Suntrust, Fiserv with First Data and Fidelity National with Worldpay are very recent examples of large announced transactions. Given the tone of the conversations we are having with many companies we would not be surprised if this acquisition trend continued.

We also spent time in Northern Europe where the focus was on Nordic capital goods and insurance markets. We have exposure to both through Sampo in Finland and Sandvik in Sweden while we follow a number of high quality Nordic industrials and capital allocators on our Watchlist. The conclusions were positive in both cases, particularly on the management transition currently taking place at Sampo whereby CEO Kari Stadigh is retiring to pass on the reins to Torbjorn Magnusson. Over the course of multiple meetings with Sampo's management team we have developed high levels of conviction that Torbjorn will do an excellent job both in running capital allocation at the Sampo level and in his new roles as Chairman of If (Sampo's wholly owned P&C insurance company) and Nordea (Sampo's largest listed stake).

Sampo currently trades on a 7% dividend yield (its highest yield since the GFC) and in April will pay a full year dividend of €2.85 implying an ex-div price of ~€38. We would expect management to increase the dividend to €3 per share for April 2020, implying a forward yield of almost 8%.

Bear in mind the current yield on 10 Year Euro-bonds is *zero* (in fact less than zero at the time of writing).

This is highly compelling for us given the sustainable and attractive characteristics of the Nordic insurance market and our view that the pass-through dividend from Nordea is sustainable due to an improving cost structure and more favourable capital position post the re-domicile from Sweden to Finland. Valuations for Nordic banks are currently suppressed due to ongoing headlines around the Estonian money laundering story but this should have minimal impact on Sampo which can sell any of its positions at any time.

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This quarter saw us undertake an 'immersion experience' in Japan, something we have found beneficial in previous years in the US and Europe. Living and working on the ground for five weeks provided a tremendous opportunity to deepen and broaden our networks in Japan which hopefully will yield a richer level of insights into our investments going forward.

There continues to be significant discussion amongst investors as to the success of the ongoing corporate governance reform which was first implemented in 2014. Whilst we see many positive signals from these initiatives as we meet companies, we believe a far greater force of reform will be the continuing challenges posed by the labour market. Unlike governments and their policies the pressures from the labour market are inexorable.

Japan's working age population peaked at 70% of the population in 1996, declining to 60% today and forecast to reach around 50% by 2045. Most of the companies we meet will describe this as their core challenge. For example, the convenience store association is attempting to lobby the government to restrict the 24 hour openings of their stores as they are struggling to staff them. When we spoke to Oriental Land Company (Tokyo Disney) they described concerns around attracting staff as the key reason for their decision to move a larger number of their part time and casual workers onto full time contracts.

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## MARCH 2019

Offsetting these challenges are the significant labour related “latencies” we observe across Japan, these include: 1) low female labour force participation 2) low labour productivity and 3) uneconomic business operations. We speak to many companies that continue to produce unprofitable product lines as these provide employment. Whilst there are deeply entrenched cultural and attitudinal reasons for this the economic justifications (valid post the bursting of the Bubble Economy in the early ‘90’s) no longer apply.

As these pressures increase, including labour cost pressures, we expect to continue to see firms focus on their productivity and thus increase their profitability. In addition, this is providing strong tailwinds for firms selling productivity systems and services to corporate customers.

A memorable experience was travelling to Kagawa Prefecture in southern Japan to attend the AGM of one of our holdings Unicharm (apparently we were the first and only *gaijin* – foreigner - to have ever attended the event).

Unicharm is a Family-Linked Company run by the second generation Takahisa Takahara who along with his family maintain around a 30% interest. Today selling baby diapers across Asia is their largest segment, representing around 45% of group sales. In 1981 they were predominantly selling female sanitary products and were considering entering the baby diaper business, but at the management meeting to discuss this initiative every executive with the exception of the one presenting the idea was against it. Despite this Keiichiro Takahara (Founder and President at the time) gave the go ahead, saying “If an idea is supported by many people it is old and obsolete.”

We observe this entrepreneurial culture being alive and well within Unicharm today as they continue to take risks, innovate and enter new markets with a relentless focus on short term execution. This contrasts with our experience meeting ASICS in Kobe who also had an extraordinary founder in Kihachiro Onitsuka. Today however their ownership base has fragmented and ASICS has developed into a typical Japanese corporate. This has resulted in the business losing focus and entrepreneurial zeal and despite positive industry tailwinds and they now struggle to grow the top-line whilst earning sub-economic returns.

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