Market Commentary
November 17th, 2023

English Version

Insigneo Weekly Dispatch

A Look Back at the Ideas Presented at Insigneo's Regional Conference Equity Markets Panel

A bias to quality, a focus on relative valuation discrepancies, and a long-term investment perspective were some of the ideas echoed by the members of the panel.

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This week we visited our colleagues from the Southern Cone, during our Insigneo Regional Conference held in beautiful Colonia, Uruguay. Our conference included various panels across multiple disciplines, including private equity, fixed income, and public equity investments. I had the pleasure of moderating the public equity panel and thought I would share some of the market views and investment ideas presented by our panelists, which included portfolio management teams from Morgan Stanley, Natixis, Neuberger Berman, Ninety-One, and Virtus.

We are all aware that uncertainty surrounding interest rates and the possibility of recession are creating a lot of noise in the equity markets. As such, it should come as no surprise that portfolio positioning going into 2024 was a topic of conversation. The main takeaways can be summarized by three general ideas: quality bias, valuation, and long-term horizons. The vast majority of the managers on the panel, including ourselves, have a strong preference for companies that exhibit quality characteristics. Traits such as high cash flow generation, low leverage, strong operating margins, and meaningfully competitive advantages, or "moats", were the topic of conversation. Companies with these traits are more likely to endure an earnings recession or

other uncertainties currently plaguing the markets. Enhancing this positioning was a tilt towards long-term horizons. This idea was enforced by the selection of companies with long-term earnings growth themes, trading at historically low valuation multiples. The premise of avoiding stocks with extended relative valuations was also consistently echoed throughout the panel.

This idea evolved into another topic of conversation which involved a discussion of risks currently being faced by the market, mainly the question “What risks keep you up at night?” Responses to this question revolved around the idea of high market expectations reflected in premium valuations, as companies that fail to meet the lofty expectations implied by their valuation multiples could be heavily penalized by the market. A strategy proposed to mitigate this risk involved purchasing companies with quality traits and low valuations. This strategy appeared to be implemented in different ways depending on the manager’s particular investment mandate; however, all participants shared this common view.

Interestingly, the need for active equity management, rather than attaining exposure to the public equity sector through passive indexing products, was echoed throughout the panel participants. It would be logical to think that a mutual fund manager with an active equity mandate would endorse this idea, as it would promote the need to purchase equity mutual funds. However, if we dig deeper, this idea does make sense given the current market environment. An investor purchasing passive equity strategies such as the SPDR S&P 500 ETF (SPY) would purchase the S&P 500 Index with its current sector weights. This strategy, however, would expose an investor to historically high allocations to the Technology, Communications, and Consumer Discretionary sectors, sectors that contains stocks with P/E valuations trading at the high end of their respective historical ranges. On the other hand, attaining exposure to the markets through an active equity manager does provide investors with the possibility of achieving the appropriate exposure through companies that might present attractive investment opportunities at more compelling valuations.

In addition to providing high-level views of the markets, participants in the panel also provided investment ideas through which to express these views. A number of panelists recommended exposures to different industries such as medical equipment, pharmaceuticals, supermarkets, as well as energy transition themes. However, individual equity recommendations were also provided. Traditional companies like Microsoft Corp. (MSFT) and Johnson and Johnson (JNJ) were mentioned due to their quality-oriented traits. However, construction material provider CRH PLC (CRH), medical equipment manufacturer Danaher Corp. (DHR), and semiconductor manufacturer ASML Holding NV (ASML) also made the list, as these all represent high quality franchises trading at relatively discounted valuations. A final, longer term idea encompassing exposure to the high-quality small cap space was also espoused, as these equities currently trade at significant, multi-year discounts to their large cap counterparts and should benefit from an eventual recovery of the business cycle.

Much like companies such as Walt Disney (DIS) and Verizon Communications (VZ) that we believe represent quality franchises trading at discounted valuations, the panel focused on the same premises of quality and valuation that we currently find attractive. We all believe that these types of companies have a higher probability of soundly navigating through uncertain equity market environments. Given the number of question marks currently surrounding the economy and markets, we believe that sometimes prudence can be the better part of valor.

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