Monthly Market Commentary

February saw mixed global equity market performance across regions. Nailing down drivers is trickier than usual but forecasts of higher and later peak interest rates certainly weighed on sentiment and drove relative weakness for US equities.

The case for US rates topping out at higher levels was bolstered by a flurry of strong economic data such as greater than expected CPI and core PCE prints for January, and stronger than expected job growth. Additionally, the highest consumer sentiment reading in more than a year, led some Fed officials to publicly advocate for a resumption of large rate rises.

While we do not have a view on where rates will ultimately settle, we are conscious of the fact that this debate is being had against the backdrop of high equity market valuations.

Risks to the US economy are evident in the inverted yield curve, deteriorating leading economic indicators and early signs of a squeeze on corporate credit. The most notable example of this was the latest Fed Senior Loan Officer Survey where the percentage of US banks reporting tighter lending standards jumped above 40% in Q4. This is consistent with levels seen just before each of the last four recessions.

Given the challenging outlook for equities, the Fund continues to play its role in a diversified portfolio with low volatility and a differentiated return profile. The Talaria Global Equity Strategy delivered 1.61% during the month, taking the one year total return to 9.19%.

US markets were lower in February with the S&P500 and NASDAQ down 2.6% and 1.1%, respectively. European bourses did a lot better with performance led by the French CAC up 2.6%, followed by the German DAX up 1.6%, and the UK's FTSE up 1.3%. Asian markets also did better than US peers with the China's Shanghai Composite Index up 0.7% and Japan's Nikkei225 up 0.4%.

Following a very strong January across the board, all sectors finished lower in February. Technology and Industrials fared better than most, down only 0.1% and 0.9%, respectively. Financial Services, Consumer Discretionary and Staples all fell less than 2.5%, while Energy, Materials, Utilities, Healthcare and Telecommunications all fell more than 4.0%.

The Australian Dollar fell 4.6% against the USD, partly reflecting the weakness in commodities as the Bloomberg Commodity Index fell 4.8% and WTI was down -2.3%. VIX rose 1.3 points to close at 20.7 while yields on 10yr US Govt Bonds rose 41bps to 3.92%.

Japan Inc was the biggest contributor to the fund's performance in February with all our Japanese holdings up for the month. Mitsubishi Electric (ME) rose ~8% as a better-than-expected Q3 update showed the group is doing a good job raising prices and realising solid margin upside. This was particularly the case in the Home Appliances segment where ME is one of the world's biggest manufacturers of air-conditioners. ME's Industrial Automation margins also continue to improve off cyclical lows. As the crown jewel asset, there is plenty more upside to Industrial Automation margins should ME manage to turn the ship towards its >10% target versus the current ca. 6%. While the stock has had a good run, we think there is still good money to be made given reasonable upside to profitability, a still undemanding valuation (ca. 1x Enterprise Value/Invested Capital), and an exceptionally strong balance sheet.

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The Fund recently took exposure to US holding company Loews. This business's primary asset is a ca. 90% interest in commercial insurer CNA Financial (ca. 70% of group book value), alongside smaller investments in Energy, Infrastructure and Hotels. We were attracted to Loews given improving fundamentals at CNA where rising rates are a big tailwind to profits, a net cash balance sheet, a cheap headline valuation (ca. 18% discount to book value) and good capital management (a buyback equivalent to ca. 7% of shares per year).

LOEWS CORPORATION