*Please note that the commentary is for the retail class of the fund.*

Despite more clouds gathering on the horizon of global growth prospects during the third quarter of 2018, global equity market participants preferred to focus on continued strong profit growth numbers out of especially the US to register very strong returns over the period. The MSCI All Country World Index returned 4.3% over the quarter, almost matching the year-to-date number of 3.8%. At the same time, investors have had to adjust their interest rate expectations for the US upwards, as was discussed in a few of our earlier quarterly reports. This was in response to a US economy continuing to surprise on the upside in terms of growth and the sustainability thereof.

Going forward we will continue to monitor escalations in the trade war dialogue primarily between the US and China. Up to now the market has chosen when it becomes concerned about developments, and hence one should exercise judgement when headline-grabbing pronouncements are being made. As we argued in the prior quarter, we think the bigger issue that investors need to focus on is the process of interest rate normalisation playing out in the US. Ten-year yields in the US have moved from 2.9% at the end of June 2018 to 3.1% at the end of September 2018 and have subsequently moved to over 3.2%. Investors should be reminded that in Europe the process of interest rate normalisation has barely started, hence we continue to advise exercising caution when calibrating expectations for equity market returns over the next few years.

Another notable development over the last three months has been the increased cost of capital in emerging market equities. This subset underperformed their developed market complex by 6% over the quarter, on top of an underperformance of almost 10% in the prior three month-period. This has meant that over most periods emerging markets have now underperformed developed markets, with the US equity market continuing to be the stand-out performer over the last decade. Emerging market currencies shared in this adjustment, with the Russian ruble, South African rand and Indian rupee all depreciating by around 12% during 2018. The Turkish lira is down almost 37%, but we view this as mostly self-inflicted as the political regime continued to alienate foreign investors with illogical and, at times, contradictory actions. Developed economies' currencies generally depreciated only slightly against the US dollar over the quarter (around 2%).

Healthcare was the best performing sector this past quarter, with information technology again registering a strong performance. Laggards were energy (after a very strong second quarter), utilities and real estate. Since the start of the year consumer staples (in line with higher long bond rates), financials (slightly more perplexing given the higher interest rate expectations), materials (concerns over emerging market growth prospects) and telecommunications (also higher interest rates) have been laggards, with information technology by far the best performer and healthcare a clear second.

The fund performed marginally worse than the benchmark over the quarter, resulting in a poor last twelve months, and an average last two years. Over three years we are marginally ahead of the benchmark and since inception we are still behind. Fundamental stock picking again disappointed, notably JD.com, L Brands, Aspen and Intu. The tobacco sector also continued to sell off, hurting the fund's performance. Notable winners over the quarter included Blackstone (a long-term winner with more upside in our opinion), Spirit (subsequent to quarter-end we have exited this position), Advance Auto Parts (a strong positive contributor over the last twelve months) and Charter Communications (after a poor start to the year).

We often reflect on positions in the fund that detracted from performance, which should highlight the learning process with which we approach investments. In this commentary, we thought it appropriate to discuss Advance Auto Parts in more detail. Advance is the second largest retailer in the auto parts sector in the US and sells both to the do-it-yourself customer as well as the professional mechanical workshop. We initially invested in this stock in August 2017 after we met the new management team at a conference in the US. This team was brought in to fix a business that was cobbled together through acquisitions, and which had failed to deliver on the promised cost savings and the integration benefits. At the time their operating margin was about half that of the industry leader, and the new team had concrete plans to partially close the gap. At the same time, unusual weather had also adversely impacted industry sales, and there was lots of speculation about Amazon making a stronger push into the category. We thought the weather issue was temporary and believed that the category was less attractive to an online retailer than generally believed. While the management team has yet to deliver on their promise to increase margins, a more normal winter has seen industry volumes pick up again. The Amazon threat has also subsided, with the result that the stock has been our biggest contributor to alpha over the last year. Given that the margin improvement still needs to be delivered (arguing for a degree of implementation risk), we have reduced our position to less than half of what it was at its peak. We continue to see some value in the stock and are watching the execution of the turnaround fund closely.

Portfolio managers
Louis Stassen and Neil Padoa
as at 30 September 2018