Discovery

Discovery Global Value Equity Feeder Fund

Market background

Global equities gained in Q1, but it was a volatile three months. Declining energy prices and China's re-opening got stock markets off to a positive start in January. However, sentiment faltered as strong US and European economic data sparked concerns that further interest-rate raises may be needed to control inflation. In March, there were fears over the stability of the financial system after Silicon Valley Bank collapsed and Credit Suisse had to be rescued.

By industry, there were notable gains for some of the more cyclical parts of the stock market, with automobiles and components performing very strongly over the three months, while technology-related companies also tended to outperform. Banks were among the weakest performers in Q1, given concerns over the health of the financial sector, with energy stocks also lagging broad benchmarks as the oil price declined on a deteriorating oil-demand outlook. Globally, value stocks generally started the year well, but underperformed after the bank-sector turmoil in early March.

Performance review

The Fund delivered a positive absolute return and outperformed the benchmark in Q1. The primary contributors to relative returns during the quarter included some of our autoparts suppliers such as Vitesco, Continental and BorgWarner, as the sector finally began to price in a recovery from last year's supply-chain disruption and other economic headwinds. Other contributors included some of the travel-related holdings in the portfolio, such as airlines easyJet and Jet2, and aircraft engine maker Rolls-Royce, which did well as the post-COVID recovery in demand for travel and related services continued.
Other outperformers included Cars.com, a digital marketplace for new and used car sales; Meta, which has recovered strongly from last year's lows; and HeidelbergCement, a cement producer whose shares have recovered after trading down to what we regarded as extraordinarily cheap levels last year. Energy services business John Wood Group also contributed, its share price gaining after the company received multiple takeover proposals from private equity group Apollo during the quarter.

The main detractors from relative returns included Turkish airport operator TAV, whose shares sold off along with the rest of the Turkish market following the earthquake in the region. Energy services provider NOV also detracted, on the back of the lower oil price; as did Bank of America, whose share-price performance reflected the general sell-off in financial stocks. Other detractors included British American Tobacco, whose share price was impacted by some concerns over market-share losses in the US. Finally, relative performance was somewhat negatively impacted by the strong performance of technology stocks last quarter, with companies that we do not hold such as Apple, NVIDIA, Microsoft, Tesla and Amazon all appreciating significantly.

Outlook and strategy

It feels like we are frequently repeating the same messages in these quarterly updates, but these are messages that are very much worth repeating. And they are that Value stocks are still very cheap relative to growth stocks and relative to history. At the same time, market correlations have fallen, both between stocks and between factors (value, growth, quality and momentum), which, as Bernstein highlighted recently, should be a good environment for stock pickers. Our portfolios, meanwhile, remain very cheap with above-average levels of upside potential, in our view.

In summary, then, even after the solid benchmark-relative performance of our value portfolios so far in 2023, we continue to see significant upside potential against the backdrop of a market that appears attractive for stock-pickers generally, and especially for value investors.

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