ANCHOR CAPITAL
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Shares in the Anchor Capital High Street Global Equity portfolio: 2015 performance

Global stock markets had a turbulent 2015 with major international bourses ending the year with a whimper rather than a bang. While oil prices were already on the decline at the end of 2014, the bottom fell out in 2015 as a global supply glut resulted in the price of crude plummeting to as low as $37/bbl. Although strong data releases from the US indicated that its economy was well on the mend, Europe continued to struggle despite the European Central Bank (ECB) launching a EUR1.1trn stimulus package which it recently extended to September 2017 or beyond. China's slowdown continued, sparking off significant global market volatility and an emerging market (EM) sell-off. Besides oil, other major commodity prices (platinum, gold, iron ore etc.) plummeted as growth in the world's second-biggest economy and largest commodity consumer, continued to slow. A rampant US dollar saw EM currencies remain vulnerable throughout last year and in December, following months of conjecture, the US Federal Reserve (Fed) finally raised rates for the first time in almost a decade.

Other events, such as the financial crisis in Greece, also weighed on global market sentiment with geopolitical concerns taking centre stage as the year came to a close. In November coordinated attacks across Paris by ISIL militants rattled markets, while Turkey shooting down a Russian warplane near Syria's border and the harrowing (and continuing) Syrian refugee crisis added to concerns.

Nevertheless, despite all the doom and gloom (especially around China), the Shanghai Composite Index still managed to close the year 9.4% YoY higher, while the NASDAQ Composite Index advanced 5.7% YoY, the CAC rose 8.5%, Germany's DAX was up 9.5% and Japan's Nikkei Index finished the year c. 9% higher. However, the Hong Kong Hang Seng Index ended December 7.2% down YoY, while the Australian market shed over 2.0% in 2015 as lower commodity prices impacted many shares on that country's main board. Elsewhere, the S&P 500 Index and the Dow Jones Industrial recorded a 0.7% and 2.2% YoY loss, respectively, while the UK FTSE 100 Index dropped 4.9% (again on the back of having a heavy commodity share weighting). Overall, the big winners globally (in terms of shares) in the S&P500 Index, FTSE 100 etc. were technology counters, with Netflix being the best performing share YoY as it rocketed 134.4%, while Amazon rose 117.8%.

In what follows we look at the YoY performance of those shares in the **Anchor Capital High Street Equity Global portfolio** as at the end of December 2015. We note that these are the shares in our portfolio as at the end of last year and with shares added at different times during the course of the past year the movement in these shares' prices do not necessarily reflect the share-price movement in our portfolio (for those shares). We also highlight that non-US shares in the portfolio have been rebased to dollar so as to show an apples-to-apples comparison. ***Please see the chart showing the performances of these shares on page 4 of this note.***

We start with the winners and among the top-performing shares in our portfolio, **Pandora A/S** posted impressive share price gains last year taking the title of best-performing share as it soared 54.8% YoY. Currency tailwinds, high margins, the continued increase of its store network and the expansion of its strategic alliance with Disney into Asia Pacific all contributed to its stellar performance. We believe the Pandora brand still has very real traction globally and FY16 should represent another year of very strong earnings momentum for the Group.

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Global Ideas is a newsletter published three times a week (Monday, Wednesday and Friday) and available only to clients of Investor Campus and Anchor Capital. The key objective of this newsletter is to provide ideas for investment in the global investment universe.

We scan the globe looking for good opportunities. We provide our model portfolios, as well as news and views on our watchlist, which is continually reviewed and updated.

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In second position, the **Starbucks** share price increased by 46.3% YoY. The company reported record FY15 results which saw earnings increase from $2.1bn in FY14 to $2.8bn in FY15 – up 33% YoY. Added to that, since Starbucks started paying a dividend in 2009, the company has increased its quarterly payout each year with the board of directors already having approved a 20% YoY FY16 dividend increase. Last year the chain launched several key initiatives including a mobile feature that enables mobile orders and payment across the US. CEO, Howard Schultz said in October that China might one day be a larger market for Starbucks than the US with the company planning to open c. 700 stores in the Americas in the next year and c. 900 in Asia. With this momentous (untapped) opportunity for Starbucks in China expect to see robust growth for the business going forward.

Alphabet, formerly known as **Google**, rounded out the top-3 YoY performers as its share price soared 44.6% on the back of several strategic moves including the appointment of former Morgan Stanley CFO Ruth Porat, who is known for her fiscal discipline. Since Google rearranged its corporate structure in September, its new parent company (Alphabet) has also started reshuffling several projects and breaking out its various divisions into stand-alone entities. Google's search business continued to thrive last year, particularly on mobile devices, while the company started getting more revenue from YouTube. In 2015 it also brought its virtual reality (VR) device into the mainstream (in a deal with *The New York Times* it distributed more than 1mn VR viewers to subscribers), released two smartphones and Sidewalk Labs — a start-up “to fix cities”.

Royal Caribbean Cruises Ltd, **NASDAQ Inc.** and **AutoZone** recorded double-digit share price gains, rising by 22.8%, 21.3% and 19.8% YoY, respectively. **Royal Caribbean Cruises Ltd** had a very good year with the company taking full advantage of international growth opportunities including sending cruise ships to countries with growing middle classes, such as China. At the same time the détente between the US and Cuba also counted in its favour. In addition, Royal Caribbean’s share price rise was driven by strong earnings growth and the company’s stated intention of increasing its return on capital to double digits and to double its 2014 EPS by 2017 under its so-called, Double-Double Programme, which was announced in 2014. According to *Travel Weekly* the strong US dollar has also helped to facilitate a double-digit jump in international travel (from the US) – more good news for the company.

Although **AutoZone**, which owns 5,000 stores in North America and Brazil, saw its share price come under pressure in December, it still ended 2015 higher. The company has had c. 37 consecutive quarters of double-digit EPS growth and in its latest quarter (1Q16), AutoZone recorded net income growth of 8.3% YoY while same-store sales rose by 3.5% YoY.

Admiral Group (+18.7%) continued to grow faster than many of its competitors over the past year. The company, which operates in the extremely competitive UK motor insurance space, had a great 2015 with 1H15 customer numbers increasing 6% YoY to 4.19mn. Late last year it also emerged that UK car insurance premiums were on the increase, having risen by 8.1% YoY in 3Q15. In addition the company is highly cash generative and has an attractive dividend yield of c. 5.9% (it pays a special dividend every year while its “normal" dividend is set at c. 45% of post-tax profits).

November saw **UBS Group AG** (+14.1% YoY) report robust 3Q15 results which showed that its net income nearly tripled to CHF2.07bn ($2.1bn) from CHF762mn in the same period of 2015. This as the bank took a tax credit and set aside fewer provisions for legal probes, helping its investment banking unit swing to a profit. However, UBS pushing back its goal of 15% adjusted return on tangible equity from 2016 to 2018 (on the back of tough macro conditions and new Swiss capital rules) weighed on the share price and saw the stock coming under pressure despite the good results.

The online travel business has been booming over the past few years and online travel company, **Priceline Group** (+11.8% YoY) has benefited (with one or two bumps in the road as the company tends to give softer guidance and then reports above-expectation results). In 2015 Priceline expanded through some very savvy acquisitions including the purchase of Booking.com (which made it a big player in Europe), the acquisition of Asian hotel reservation site Agoda together with its investment in China's Ctrip and its acquisition of PriceMatch. On the negative side, at its latest results presentation, the company (which makes most of its money from international operations) bemoaned how currency headwinds are weighing on its results saying that exchange rates for the euro and British pound were “significantly reducing” its growth rates when they were translated back into US dollars.

While entertainment giant, **The Walt Disney Company** (Disney; +11.6% YoY) had a strong year overall it wasn’t without its hiccups. After its first two 2015 quarterly reports buoyed the share price, comments made by CEO Bob Iger that its 3Q results saw ESPN subscriber defections resulted in the share price plunging over 20% in August. Cable networks, led by ESPN, account for c. 44% of Disney’s operating income and concerns around subscriber loss are likely to linger. However, we believe it’s overdone as ESPN still has multi-year (exclusive) NBA and NFL broadcast deals as well as rights to broadcast college football playoffs giving it a relatively wide moat until Disney’s other segments start picking up the slack.

With Disney boasting an impressive array of major (and very profitable) movie franchises which flow into most of its operating segments and with its unprecedented global reach we have high hopes for the company’s performance in 2016. *Star Wars: The Force Awakens* is already obliterating box-office records and ancillary sales related to the franchise are likely to rocket. *Nomura’s* Anthony DiClemente said in mid-December that he’s “optimistic the company is well positioned” to see as much as $3.6bn in revenue and $2.2bn in operating income from the *Star Wars* franchise. He sees box office sales potentially reaching $818mn in North America and $2.2bn abroad (we note that this weekend the movie reached $812mn in North America alone and opened to record box office of $53mn in China—the country’s highest-ever opening weekend).

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Sales of its HIV (Atripla, Truvada, Stribild etc.) and hepatitis C (HCV) drugs (Sovaldi and Harvoni) have blasted **Gilead Sciences**' (+7.4% YoY) share price higher this past year with Group net income soaring to $8.73/share in 9M15, up from $5.18/share in 9M14. According to the *World Health Organisation* (*WHO*) there are c. 180mn people globally with HCV - making it a disease with a huge patient pool for Gilead's treatments. The company's HIV medications are currently used on c. 85% of patients in the US. The duration of treatment for its HCV patients has been reduced from 24 weeks to 12 and the company is attempting to further reduce this duration to eight weeks. It has said that it expects to continue to grow in the US HCV market with only c.10% of 4mn US HCV patients having thus far been treated by Gilead. The company is also awaiting approval for its next-generation HCV cocktail this year, which could further solidify its leadership in this treatment area.

JPMorgan Chase advanced 5.5% YoY in 2015 with the company enjoying a strong balance sheet and high capital levels. Added to that, it has a relatively high dividend yield in the current low-rate environment. The bank's assets have grown to more than $2.5trn which many commentators have attributed to the leadership of its Chairman and CEO Jamie Dimon, who has led JPMorgan Chase through enormous challenges since the GFC. Research firm Keefe, Bruyette & Woods, said in August that JPMorgan's has maintained one of the strongest balance sheets in the industry.

Blue-chip consumer goods Group, **Unilever Plc** (+5.3% YoY), which makes more than 50% of its revenues in EMs such as China, India and Brazil, last year saw an improved performance in these territories after a lacklustre 2014 (and this was despite the continued slowdown in China). At its latest results presentation the company indicated that it expects underlying FY15 sales growth to come in towards the upper end of its 2%-4% (previously disclosed) target range. Importantly, the company has a portfolio of immediately recognisable products which carry unrivalled pricing power for the Group despite the economic headwinds it might face.

PNC Financial Services (+4.5% YoY) reported a solid set of 3Q15 results in October with the company indicating that it was its tenth consecutive quarter of $1bn or more in net income, which it said reflected consistency "… without the benefit of higher interest rates..". While regulatory headwinds are a concern, with a net margin of c. 25% the Group has been able to achieve higher profitability in its latest quarter than its competitors. Overall, the company seems well positioned to grow on the back of a diverse revenue mix, solid capital levels and prudent cost management.

Nestle SA (+2.1% YoY) faced immense pressure this past year which saw sales of its Maggi noodles halted in India following a food contamination scare and a one-off charge as the company set aside more money to cover rebates on prescription skin-health products in the US. Added to that, the Group was hamstrung by the high value of the Swiss franc, which reduced the level of its overseas sales. In contrast to Unilever the company also continued to see a slowdown in its EM sales (which account for c. 43% of total sales).

Finally, among the winners (albeit marginal) **Yum! Brands** managed to eke out a YoY share price gain of 0.3% in 2015. Its dismal performance was mainly due to the slowdown in China which contributes c. 56% to Group revenue. After years of unsuccessful efforts to get its China business back on track (and making headlines in that country for all the wrong reasons – chicken hygiene issues, food and avian flu scares etc.) the company announced late last year that it intends to split off its China business in a move that has been welcomed by the market. Following the spin-off c. 95% of Yum! Brands' KFC, Taco Bell and Pizza Hut locations in China will be franchised, which is expected to boost royalty fees for the company and is also likely to lower the volatility of Yum's earnings. Recently Yum said that the two companies would provide value by delivering EPS growth of 15% p.a. from both vs past EPS growth of 10%.

Of the 25 shares in the *Anchor Capital High Street Global Equity portfolio*, 9 shares recorded YoY declines with **American Express** (AmEx;-25.2%) emerging as the worst performing share in portfolio. The company's troubles began in February last year when retailer Costco announced it would end its contract with AmEx as its main credit-card provider in March 2016. On top of that, the company was also impacted by the strong dollar, stiff competition, increased spending on growth initiatives and regulatory issues. The US Department of Justice (DoJ) challenged AmEx's agreements with merchants, which prohibited these merchants from steering customers to less expensive forms of payment. AmEx is appealing the decision, however, if it loses the appeal, its payments market share could be damaged even further while the Group's transaction fees could also be impacted. In contrast to AmEx's poor performance, its peers MasterCard and Visa's share prices were up 12% and 16% YoY, respectively.

With a 21.8% YoY decline, **Alibaba** was the (surprise) second-worst performer among the shares in the Anchor portfolio. Slowing growth in China and question marks around Alibaba's own ability to sustain a strong growth rate weighed heavily on a company that listed in September 2014 with much fanfare in one of the biggest IPOs in history. We note though that Alibaba has managed to recoup some of its share-price losses having rebounded c. 25% from its October 2015 lows as Alibaba's numerous acquisitions and investments across different industries seem to have been given the thumbs up by investors.

In third spot, **FedEx Corp** recorded a 14.2% drop in its share price last year. In two of its four quarterly results, the company failed to meet analyst expectations and in July 2015, it also warned shareholders of a tough 2016 to come. Its woes didn't stop there and in September the company downgraded its FY16 guidance, which FedEx attributed to "weaker less-than-truckload industry demand, unexpectedly large self-insurance reserves, and increased operating costs for FedEx Ground." On the positive side, FedEx announced stronger-than-expected 2Q16 results in December with EPS coming in at $2.58/share, against $2.51 expected, on revenue of $12.5bn vs $11.9bn in 2Q15.

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Global alternative asset manager, **The Blackstone Group** saw its share price decline by 11.9% YoY from a high base while **Lloyds Banking Group (-8.9% YoY)**, which was bailed out by UK taxpayers following the GFC, has over the past few months seen its share price trade below the government's break-even price. In general, most of the UK's biggest banks have seen their shares retreat over the last two months of 2015 as concerns over the state of the global economy weighed on sentiment. However, in the case of Lloyds, there has also been a steady flow of scandals (including over mis-selling and rate-rigging) at the bank with investors justifiably concerned that they may not have seen the last of the bank's transgressions. Yet another concern is the impact on the share price of the forthcoming retail sale of Lloyds and the offloading of the remainder of the government's stake in the bank. The UK government has set June 2016 as the target for having it 100% in private hands - the offloading of its remaining 9.2% stake in the bank will likely also weigh on the share price.

Last year saw **The Cheesecake Factory's** (-8.3% YoY) share price underperform as the restaurant chain was impacted by challenging economic conditions including higher food costs and a turbulent sit-down (restaurant) category. Other expenses also impacted the company including a rise in the minimum wage in the US. The company said on its 3Q15 earnings call that the wage bump represented "… about $12mn in incremental labour cost next year, which equates to about $0.17 in EPS."

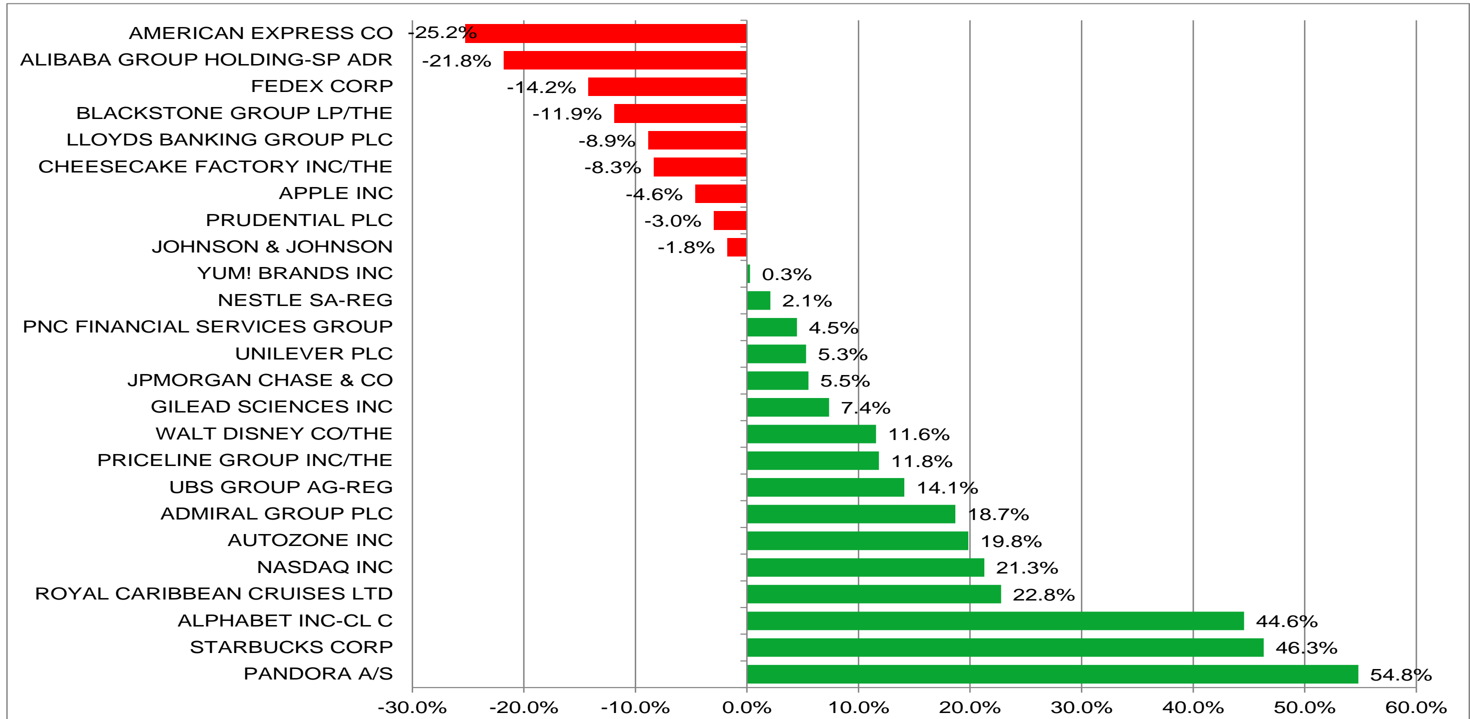
While its share price may be down 4.6% YoY, 2015 was a busy year for **Apple**, with the company releasing the Apple Watch, the iPhone 6s and 6s Plus, the iPad Pro, a new Apple TV and reports surfaced around a foray into the car segment. The company also reported record iPhone 6 and 6 Plus sales and China became its fastest-growing market. However, several analysts have expressed doubts over the tech giant's ability to keep up its impressive iPhone sales record and initial reports in December of cutbacks by iPhone chip producers weighed heavily on the price. Commentators also see the Apple Watch as an underwhelming product which isn't expected to contribute significantly to revenue or earnings for quite some time. While some of these concerns are valid, we note that the last quarter of 2015 saw the release of the so-called s phones (with minor updates every 2 years). Historically, the s-releases tend to lag sales compared with their counterparts. We believe it's a *fait accompli* that the iPhone 7 and 7 Plus cycle launch later this year will once again see iPhone sales grow significantly.

In November, **Prudential Plc's** (-3.0% YoY) 3Q15 results showed that China's growing middle class helped increase profits for the UK insurer with 3Q Asia sales rising by 20% YoY on the back of a strong performance from Hong Kong. However, the company's robust results were somewhat overshadowed by large withdrawals (c. GBP4bn) at its UK fund management arm, M&G, resulting in pressure on Prudential's share price.

Finally, with a drop of 1.8% YoY, **Johnson & Johnson (J&J)** rounds out the 9 worst-performing portfolio shares of 2015. The company experienced a tough year of declining revenue as it was hammered by plunging sales of its hepatitis C medicine (3Q pharmaceutical sales declined 7.4% YoY) and unfavourable currency exchange rates (it recorded a 15.8% negative effect from currency translation in international markets in its third quarter). Weak International growth also didn't help matters. However, looking ahead, late last year J&J announced audacious plans to file for the approval of over 10 new products by 2019 – J&J expects each of these products to bring in sales of $1bn or more p.a.!

Marco de Matos

<u>Anchor Capital High Street Equity Global portfolio shares' 2015 performance, YoY % change (rebased to $):</u>



Source: Bloomberg, Anchor Capital

The business of money: Global asset management and stockbroking

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