

A differentiated approach to global stock selection

July 2024



Gautam Samarth

Head of M&G Systematic Investment strategies

To date, 2024 has been another year of surprises in global financial markets, with global equities managing to outperform expectations across many markets. And just as importantly for investors, this year's outperformance provides a valuable diversity across sectors and geographies compared to the dominance of US technology stocks in 2023. There is a large differential between investment returns recorded by the top 100 performers listed on the MSCI All Country World Index: the highest has been 170% and the lowest 43%. At the same time, US-listed companies hold only 22 of the top 100 performance spots. Equally we see strong returns across sectors other than technology, including consumer staples, financial, industrial and even utilities.

With lower-risk global cash investments yielding 5% and equity earnings yields in most major markets (apart from the US) also elevated at levels at or above 5%, global equities make an attractive option for investors in the current conditions given their greater potential to deliver relatively higher returns. Equally, South African investors may want the diversification benefits of global stocks. In today's market, careful stock picking can add attractive value to a local portfolio.

Outperformance with an information edge

In global equity investing, investment managers face a significant challenge: identifying the stocks that will outperform the overall market. The global equity investment universe is vast, with some 10,000 different stocks listed around the world. Trying to choose those companies that can beat the MSCI All Country World Index (ACWI) can be daunting, requiring a significant amount of resources. At M&G Investments we employ a successful artificial intelligence (AI) model, as used in the M&G (Lux) Global Maxima Fund, to help our large team of equity analysts and portfolio managers construct our global equity portfolios – we believe this is the only way to be able to thoroughly cover such a huge number of companies. The [M&G Global Equity Fund](#) and [M&G Global Property Fund](#) are managed using this Global Maxima model, as are the equity portions of the [M&G Global Balanced](#) and [M&G Global Inflation Plus Funds](#). All of these funds are offered in South Africa on several major offshore platforms, in both US dollars or rands.

Our AI model and its database are continually expanding, improving and being refined to account for the latest data and market developments, from company-related performance data to macroeconomic data and collective market data. Containing some 30 years of history, 400 metrics per company and a current total of over 5.0 billion data points, it analyses this data to understand the historic relationships and patterns between the data and share prices, ultimately to determine the probability of a company delivering above-market returns (alpha) going forward. Each company receives an alpha score, and the 100 companies with the highest scores are selected to be reviewed for inclusion in the portfolio. Since not every asset manager is able to command the resources to develop and operate such a model, we believe that this gives M&G an information edge in our global equity investing.

Besides detecting patterns and relationships between data that are indistinguishable to humans, AI offers a speed and scale of analysis far beyond that of the largest teams of research analysts. AI can also be updated continuously, preventing the database from becoming "stale" – the M&G model has 4.0 million new data points coming in daily. It is also able to be tailored and improved to accomplish different tasks, and importantly, it is unemotional, using a strict rules-based process.

Combining technology with human expertise

The M&G approach combines the skills and experience of human fund managers with the benefits of AI, as the M&G team must verify the model's recommendations and correct any unintended risks or mistakes that could be present in the combined portfolio. This could be concentrations in a particular country, sector or investment style, for example. Portfolio managers and analysts delve into the reasons for the recommendation, bringing to the table their detailed understanding of specific companies, sectors, impending corporate action or changing government regulations, as well as ESG concerns – areas to which AI is largely blind – as well as qualitative factors such as poor management, or why a stock may have re-rated. As a result, it is the humans that have the final say in portfolio construction and how it changes over time.

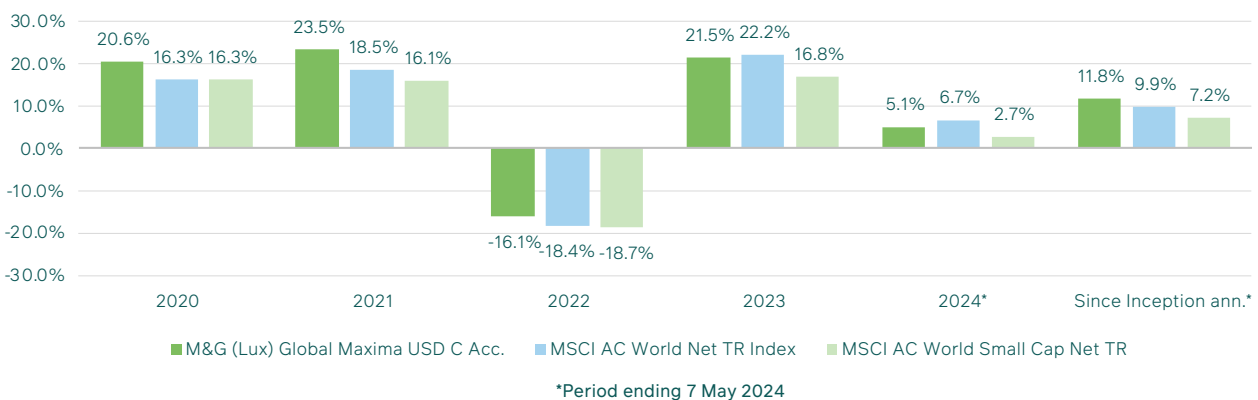
In fact, the strategy is very actively managed as the model is re-run once a week and stock picks and/or position size can change as frequently as this.

A preference for smaller companies

The M&G Global Equity Fund and other portfolios employing the Global Maxima strategy have been underweight to the global mega-cap stocks for some time now, and overweight small- and medium-cap businesses. This is due in large part to our desire to maximise the positive impact of our AI model, as this part of the market is where it is most effective and has the most information advantage. Mega-cap stocks are well known and deeply researched by every equity fund manager worldwide, while smaller companies are less known and there is much more likely to be mispricing. We are therefore willing to accept some of this style risk to get the full benefit of the huge amount of information we have captured to be able to correctly select outperforming companies, and the success of this tradeoff is reflected in the Global Maxima Fund's performance history to date.

A differentiated source of outperformance

Graph 1: M&G (Lux) Global Maxima Fund performance



M&G (Lux) Global Maxima Fund Performance Summary (USD). The fund's benchmark is the MSCI ACWI Net Return Index. The benchmark is a comparator against which the fund's performance can be measured. It is a net return index which includes dividends after the deduction of withholding taxes. The index has been chosen as the fund's benchmark as it best reflects the scope of the fund's investment policy. The benchmark is used solely to measure the fund's performance and does not constrain the fund's portfolio construction. The fund is actively managed. The investment manager has complete freedom in choosing which investments to buy, hold and sell in the fund. The fund's holdings may deviate significantly from the benchmark's constituents.

Source: Bloomberg, 07 May 2024, Morningstar Wider Universe, USD C class shares, income reinvested, price to price. Benchmark returns stated in USD terms.

As Graph 1 shows, since its inception in January 2020, the M&G (Lux) Global Maxima Fund has outperformed its benchmark (the MSCI ACWI Index, net total return) by nearly 2.0% per year, returning 11.8% p.a. versus 9.9% p.a. Notably, this has taken place in extremely different conditions, through the Covid period and the difficult year that was 2022, when the fund lost less than its benchmark.

Although it has not been a good period in which to be underweight the global mega-cap stocks, astute stock picking has been the primary driver of its outperformance over its history. This attests to the power of M&G's AI model and the management team's ability to harness this power and apply it successfully to generate above-market returns for our clients.

Disclaimer.

This document is for information purposes only and is not an offer to or solicitation for investors to invest in any of the capabilities or products offered by MandG Investment Managers (Pty) Ltd [M&G Investment Managers] (Registration no. 2013/051515/07) and MandG Investments (Namibia) (Pty) Ltd (Registration no. 1996/85) [M&G Namibia] or any of their associates, being MandG Investments Unit Trusts South Africa (RF) Ltd (Registration no 1999/005242/06) and MandG Investments Unit Trusts (Namibia) Ltd Registration no. 2007/609. M&G Investment Managers is an authorised discretionary financial services provider by the Financial Sector Conduct Authority of South Africa [FSP45199] in terms of the Financial Advisory and Intermediary Services Act, and has its registered offices at 5th Floor Protea Place, 30 Dreyer Street, Claremont, 7708. M&G Namibia is an approved person in terms of section 4 of Stock Exchanges Control Act and has its registered offices at 6 Feld Street, Windhoek, Namibia. Information given in this document has been obtained from, or based upon sources believed to be from an accurate and timely source but M&G Investment Managers and M&G Namibia make no representations or warranty, express or implied, with respect to the correctness, accuracy or completeness of the information and opinions. This information is not intended to constitute a basis for any specific investment decision. Investors are advised to familiarise themselves with the unique risks pertaining to their investment choices. Investors should seek the advice of a properly qualified financial consultant/adviser before investing. The value of an investment will fluctuate and past performance is not necessarily an indication of future returns.