

# Wasatch International Select Strategy

DECEMBER 31, 2019

## New Zealand and Japan Drove Strategy's Strong Return

### OVERVIEW

The Wasatch International Select strategy had a double-digit gain in the fourth quarter and outperformed the benchmark MSCI EAFE Index, which finished the same period up 8.17%. For the 12 months ended December 31, 2019, the strategy outperformed the 22.01% rise in the benchmark.

During the fourth quarter of 2019, global markets broadly rose as investors responded favorably to macro developments, including an agreement on a "phase one" deal expected to resolve portions of the U.S.-China trade dispute.

In early December, Japan's upper legislative house approved a U.S.-Japan trade deal introduced in September and passed by the lower legislative house in November. The deal, expected to go into effect in January 2020, will see more than \$7 billion in tariffs on U.S. goods reduced or removed in exchange for lower tariffs on Japanese industrial goods imported by the U.S. Japan, our heaviest-weighted country, added the most to the strategy's return during the quarter and our group of holdings outperformed the benchmark's position in Japan.

Following news of faster-than-expected growth in New Zealand during the latter-half of 2019, stocks in the country rallied. Although the strategy has just two holdings in New Zealand, it is overweight versus the benchmark in the country, which makes up 0.25% of the Index. Our holdings in New Zealand contributed significantly to the strategy's return and outperformance of the benchmark for the period.

### PORTFOLIO MANAGERS



**Ken Applegate, CFA, CMT**  
Lead Portfolio Manager

3 / 5  
YEAR ON STRATEGY / YEARS AT WASATCH



**Linda Lasater, CFA**  
Lead Portfolio Manager

3 / 13  
YEAR ON STRATEGY / YEARS AT WASATCH

Decisive election results had a positive effect on the United Kingdom's market. While many analysts still worry about the potential outcome of Brexit, the election nonetheless provided a measure of clarity that has been rare in recent years, and investors seemingly felt optimistic about the prospect of market-friendly policies in the U.K. Equity-market returns in the U.K. were also aided by the British pound's recovery. Despite the drag of an underweight position, the strategy's U.K. holdings outperformed their benchmark counterparts.

China was the only country that subtracted from the strategy's return for the period. Our lone holding in China, which we mention below, was the largest detractor from the strategy's performance.

On a sector basis, our group of holdings in the health-care and information-technology (IT) sectors produced strong gains for the quarter, adding significantly to the strategy's return and driving its outperformance of the benchmark. In these sectors, the strategy benefited from stock selection and being substantially overweight versus the benchmark. Of the sectors in which the strategy was invested, the materials sector was the only one that subtracted from the strategy's return, albeit less than one-quarter of a percentage point. Our lone holding in the sector, which we mention below, was one of the largest detractors from strategy performance.

## DETAILS OF THE QUARTER

Both of the strategy's top contributors for the period came from New Zealand. The share prices of both companies rose over 35%.

The first, **Fisher & Paykel Healthcare Corp. Ltd.**, designs and manufactures medical devices, including heated humidification systems, patient warming devices, and neonatal care products such as infant resuscitators. Our research has shown that the company is well-run and it has been

operating consistently with our expectations. We anticipate continued growth and are watching the adoption of the company's new product, F&P Vitera™, a full-face mask for use with continuous positive airway pressure (CPAP) devices.

The second, **Xero Ltd.**, provides cloud-based accounting software for small- and medium-size enterprises. Xero was the first-to-market with a true cloud solution and is widely considered best-in-class. The company also has a unique acquisition model that has benefited its efforts to obtain referrals. We believe Xero is a long-duration growth story.

One of the companies that led the strategy's positive performance in the U.K. was **Halma plc**. Halma operates over 40 companies focused on safety, health and the environment. The company has four business segments. The process safety and infrastructure safety segments focus on creating products that protect people and assets, such as monitoring devices for flammable and hazardous gases as well as fire and smoke detectors. Halma's medical segment focuses on making devices for ophthalmology and advanced blood pressure monitoring. And the company's environmental and analysis segment focuses on products to monitor and test water, typically for municipalities. We believe Halma is a high-quality company with a solid management team.

As mentioned above, the strategy's largest individual detractor was from China. **Vitasoy International Holdings Ltd.** is based in Hong Kong and offers soy milk, tofu, rice milk, tea, juices and related food-and-beverage products in over 40 countries. Increased competition in China and weaker-than-expected earnings caused Vitasoy's stock price to decline during the period. However, we continue to like the company and do not believe there are any fundamental issues that would crimp Vitasoy's long-term growth potential.

Japanese materials company **Pigeon Corp.** was the second-largest detractor from strategy performance for the quarter. Pigeon is a leading provider of baby bottles, lotions and related products in Japan. The company has struggled due to weaker-than-expected sales. While we still think Pigeon has a compelling growth story, we continue to monitor developments as management responds to what has been a more-challenging period.

The third-largest detractor from strategy performance was Denmark's **Chr. Hansen Holding A/S**, which subtracted less than one-quarter of a percentage point from the strategy's return. Chr. Hansen is a bioscience company that develops and produces natural ingredients such as cultures, enzymes, probiotics and natural colors used in the food, nutritional, pharmaceutical and agricultural industries. The company has experienced softer demand for some of its products, including natural food colorings, particularly from emerging markets. Chr. Hansen's annual report released in October showed that organic growth had declined 2% from the same period in 2018, which weighed on the company's share price. We continue to like the company, believing that Chr. Hansen remains an innovator and leader in the food cultures and enzymes market.

## OUTLOOK

For the International Select strategy, we believe we have invested in a set of outstanding companies that have the potential to produce the long-term growth we expect. We are continuing our intensive research efforts so that we might fill the strategy with companies that we believe are well-positioned to contribute to its performance over the long term.

Most international markets posted solid returns in the fourth quarter to close out a strong year. In the U.S., the S&P 500® Index rose 31.49% for the 12

months ended December 31, 2019, its best return since 2013. Meanwhile, the U.K. showed early signs of casting off the shadow of uncertainty created by Brexit that has loomed for nearly four years.

We are heartened by the positive shift in the U.K. and feel the strategy is well-positioned to benefit from a market that has punched above its weight, even prior to investors' optimistic response to the recent U.K. elections. Early on, as Brexit became a looming market factor, Wasatch adjusted the firm's U.K. holdings to prioritize those with significant revenues from international sources, rather than focus on companies with revenues tied primarily to the U.K. Thus, we believe we provided our funds with a measure of insulation against the unpredictability that has accompanied years-long Brexit negotiations and has weighed especially heavily on domestic demand.

To this end, we are excited about the U.K. companies the strategy holds and believe they are structured such that they should grow, even if the recent uncertain environment were to persist. Our excitement is heightened by the prospect that the current trend could hold and the cloud over consumer and business spending in the U.K. could continue to dissipate.

Although the final quarter of 2019 held much in the way of good news for investors, we are cognizant of the fickle nature of such short periods. Despite the impressive end to the year, and the encouraging developments that helped facilitate such positive results, trade tensions and broad deglobalization efforts continue to weigh on global growth.

As for us at Wasatch Global Investors, we continue to pursue our investment discipline. Three of our team members just returned from attending a pan-European conference in the U.K. Moreover, our team has requested meetings with an additional 60 companies for another U.K. research



trip planned for the end of January 2020. We believe our due diligence, especially conducting boots-on-the-ground research, is a strategic advantage that allows us to find outstanding long-term growth companies for the strategy.

Thank you for the opportunity to manage your assets.

Sincerely,

Ken Applegate and Linda Lasater

*The MSCI EAFE Index is an unmanaged index and includes reinvestment of all dividends of issuers located in 21 developed-market countries, excluding the U.S. and Canada. This index is a free float-adjusted market capitalization index designed to measure the performance of mid-cap and large-cap securities.*

*You cannot invest in this or any index.*

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*Brexit is an abbreviation for "British exit," which refers to the June 23, 2016 referendum whereby British citizens voted to exit the European Union. The referendum roiled global markets, including currencies, causing the British pound to fall to its lowest level in decades.*

*The "cloud" is the internet. Cloud-computing is a model for delivering information-technology services in which resources are retrieved from the internet through web-based tools and applications, rather than from a direct connection to a server.*

*The S&P 500 Index includes 500 of the United States' largest stocks from a broad variety of industries. The Index is unmanaged and is a commonly used measure of common stock total return performance.*

*This commentary is intended to provide you with information about factors affecting the performance of the Wasatch International Select strategy during the period. References to individual companies should not be construed as recommendations to buy or sell shares in those companies. Wasatch analysts closely monitor the companies held in the International Select strategy. If a company's underlying fundamentals or valuation measures change, Wasatch will reevaluate its position and may sell part or all of its holdings.*

*Past performance is not indicative of future results.*