CIBC PRIVATE WEALTH MANAGEMENT

CIBC Private Wealth Blog

International Update: European Due Diligence

Matt Scherer, CFA

October 5, 2018

The MSCI All Country World ex USA stock index was up roughly 0.5% in September, but remains down over 2.5% for the year. The wild ride continued last month as the market declined over 3.0% early on, only to stage a strong recovery in the back half of the month. The same themes continue to pressure international stock markets, with emerging market and trade uncertainties topping the list.

More specifically, emerging market stocks and their related currencies remained under pressure through much of the month as investors focused on both Turkey and Argentina as high-risk countries. So far, it does not appear the currency crisis is spreading beyond these borders—a factor that we are watching closely as investors are nervous the crises will infect larger developed markets. We expect market uncertainty and increased volatility to be the new norm as we negotiate trade tensions and changing central bank policy.

We continue to believe in focusing on company fundamentals during periods of volatility, and to that end, I traveled to London and Paris last month to visit with several companies in CIBC's International Growth portfolio—as well as a number of interesting new prospects. Five days and more than 20 meetings later, a few observations emerged.

Macro Debate: I found it interesting that there was a lack of consensus regarding the direction of the U.K. and European economies. Typically, investors and even management teams have a "herd mentality" wherein one line of thinking regarding the direction of the economy gradually emerges. BREXIT remains the focal point of the debate. Some investors and CEOs feel that BREXIT is a speed bump that will be managed, while others are extremely nervous. On the Continent, I found investors are focused on the path of interest rates, a debate that has growing similarities to discussions currently taking place in the U.S. The European Central Bank (ECB) remains accommodative, but hints of inflation have some investors worried that rates may rise faster than expected.

Technology Stocks: Similar to the U.S., technology stocks are in favor in Europe. The main difference in Europe is the lack of options. The tech sector is much smaller, which has resulted in growth investors becoming more concentrated in fewer options.

EM FX: The emerging market foreign exchange crisis was also top of mind for many of the companies I met with. Again, our bias toward growth means the companies we invest in are typically selling goods into high-growth markets, including emerging markets. Underlying demand trends remain healthy, but the foreign exchange translation has been a headache in many markets like Turkey and even China. Hedging is not an option in many of these markets.

Socially Responsible Investing (SRI): While SRI inquiries continue to build in the U.S., the trend in Europe has clearly taken hold. At the conference I attended, there were specific lectures and meetings on the topic. I continue to believe this trend will accelerate as future generations gain wealth and prioritize this approach to investing.

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As portfolio managers, it is critical that we meet with companies, and especially with management teams on their home turf. We find the conversations are more interesting and complete when meetings take place in a CEO’s office, rather than on a roadshow in our office. In addition to gaining a better understanding about philosophy, trends and fundamentals, these face-to-face meetings are immensely useful in developing the big-picture themes described here.

Matt Scherer is a portfolio manager and equities analyst for CIBC Private Wealth Management with more than 20 years of industry experience.