

# Thornburg International Equity ESG Strategy

Portfolio Manager Commentary  
31 March 2022



## Market Review

- The 1st quarter was a losing one for international markets, with the MSCI ACWI ex USA Index down 5.33% and the MSCI EAFE Index down 5.91%. Emerging Markets lost 6.97% led by China, which was down 14.19% (MSCI Emerging Markets and MSCI China Indices).
- It was a quarter with a lot of macro crosswinds that impacted market performance and caused large dispersions in country and sector performance. The biggest macro drivers in the quarter were the war in Ukraine, the beginning of Fed tightening, and the continued rise in U.S. interest rates, with the 10-year Treasury yield rising 83 basis points and the 2-year yield rising 160 basis points - both ended the quarter at 2.34%. The yield curve is now flat from 2's to 10's, with an inverted yield curve traditionally seen as an indicator of a slowing economy.
- Given the impact of the war and the rise in interest rates Energy, Materials, and Financials outperformed in the 1st quarter while MSCI ACWI ex USA Value outperformed Growth by 11.0%. Among major markets the Eurozone and China underperformed while the UK, Canada, Brazil, Australia and most oil producers (excluding Russia) outperformed. The U.S. (S&P 500) lost 4.6% and Russia was removed from MSCI Indices during the quarter.

ESG underperformed in a quarter where value stocks outperformed but still offers an attractive risk/return profile, particularly in international markets.

## Portfolio Manager

**Lei Wang, CFA**

Portfolio Manager

Supported by the entire Thornburg investment team

## Average Annual Returns (% , as of 31 Mar 2022)

In US\$ terms. Returns may increase or decrease as a result of currency fluctuations.

	QTD	YTD	1-YR	3-YR	5-YR (30 SEP 2015)	ITD
<b>International Equity ESG Composite (Net)</b>	-7.70	-7.70	2.35	17.11	12.43	12.33
<b>International Equity ESG Composite (Gross)</b>	-7.47	-7.47	3.35	18.24	13.35	13.25
<b>MSCI ACWI ex US NTR Index</b>	-5.33	-5.33	-1.33	7.57	6.80	7.67
<b>MSCI EAFE NTR Index</b>	-5.91	-5.91	1.16	7.78	6.72	7.18

## Annual Return Performance Summary (%)

	2016	2017	2018	2019	2020	2021
<b>International Equity ESG Composite (NET)</b>	7.67	23.46	-13.21	24.79	26.90	21.05
<b>International Equity ESG Composite (GROSS)</b>	8.71	23.89	-12.64	25.92	28.11	22.22
<b>MSCI ACWI ex US NTR</b>	4.50	27.19	-14.20	21.51	10.65	7.87
<b>MSCI EAFE NTR</b>	1.00	25.03	-13.79	22.01	7.82	11.26

ITD - Inception to Date. Periods less than one year are not annualized.

Performance data for the International Equity ESG Strategy is from the International Equity ESG Composite, inception date of 1 October 2015. The International Equity ESG Composite includes discretionary accounts invested in the International Equity ESG Strategy. Returns are calculated using a time-weighted and asset-weighted calculation including reinvestment of dividends and income. Periods less than one year are not annualized. Individual account performance will vary. The performance data quoted represents past performance; it does not guarantee future results. Gross of fee returns are net of transaction costs. Net of fee returns are net of transaction costs and investment advisory fees. Thornburg Investment Management Inc.'s fee schedule is detailed in Part 2A of its ADV brochure. Performance results of the firm's clients will be reduced by the firm's management fees. For example, an account with a compounded annual total return of 10% would have increased by 159% over ten years. Assuming an annual management fee of 0.75%, this increase would be 142%.

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- The MSCI ACWI ex USA ESG Leaders Index, made up of companies within the MSCI ACWI ex USA Index with high ESG performance relative to their peers, lost 6.88% in the 1st quarter, about 145 basis points behind the broader MSCI ACWI ex USA Index. The ESG Leaders Index is underweight Value versus the broad index, with a higher P/E and Price to Book, which hurt in a quarter where Value outperformed.

### First Quarter 2022 Performance Highlights

- In the 1st quarter Thornburg International Equity ESG Strategy lost 7.70% (net of fees), 236 basis points behind the MSCI ACWI ex USA Index.
- As noted above macro factors drove a wide dispersion in performance between countries and sectors in the 1st quarter, not unlike the pandemic in the 1st quarter of 2020, and in many cases that dispersion negatively impacted the strategy's relative performance. For the strategy the two biggest drivers of underperformance were country allocation and bottom-up stock selection.
- The strategy was underweight the UK, Canada and Brazil and zero weight Australia and Saudi Arabia/UAE/Qatar/Kuwait, all of which outperformed, and overweight the Eurozone and China, both of which underperformed. A zero weight in Russia was a major positive.
- On a sector basis the strategy was zero weight Energy and underweight Financials, which outperformed, and overweight Industrials, which underperformed. An underweight in Consumer Discretionary and an average 10% in Cash were positives.
- Most of the strategy's underperformance in stock selection occurred in the strategy's Basic Value basket, to which we had an average 43% allocation during the quarter. Many of our Basic Value stocks are higher quality (more consistent earnings or profitability, lower leverage, usually higher valuations) and they underperformed during a quarter where Value outperformed by 11%. Both Emerging Franchise and Consistent Earners did relatively well in a quarter where Growth underperformed.
- ESG Leader stocks in general also underperformed the broader market during the quarter, as represented by the 145 basis point underperformance of the MSCI ACWI ex USA ESG Leaders Index versus the broader MSCI ACWI ex USA Index.

### Current Positioning and Outlook

During the quarter we trimmed Basic Value by about 8%, adding to Consistent Earners, Emerging Franchise, and Cash. Basic Value ended the quarter at 39%, Consistent Earner 35%, Emerging Franchise 15% and Cash 10%. While we view China as relatively cheap after a 39% decline since its peak in February of last year, we are cautious there for the moment given the potential economic and political impacts of an ongoing COVID outbreak, the conflict in Ukraine, and an

### Top Performers (1Q22)

Name	Contrib. (%)	Avg. Weight (%)
NVIDIA Corp.	0.46	1.16
MercadoLibre, Inc.	0.42	0.79
Mitsubishi UFJ Financial Group, Inc.	0.41	2.03
Orange S.A.	0.27	1.12
Norsk Hydro ASA	0.24	1.00

### Top Detractors (1Q22)

Name	Contrib. (%)	Avg. Weight (%)
Meituan	-0.89	2.05
NIO, Inc.	-0.51	0.75
Tencent Holdings Ltd.	-0.51	2.81
ING Groep N.V.	-0.50	2.21
E.ON SE	-0.44	2.54

### Ten Largest Holdings

(as of 28 Feb 2022)

Holding	Weight (%)
E.ON SE	2.9%
Roche Holding AG	2.8%
Seven & i Holdings Co. Ltd.	2.6%
Tencent Holdings Ltd.	2.6%
Tesco plc	2.4%
Sony Group Corp.	2.4%
Hitachi Ltd.	2.3%
Meituan	2.3%
Recruit Holdings Co. Ltd.	2.3%
Enel SpA	2.3%

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ongoing dispute with the U.S. over the listing of Chinese companies there and have cut our exposure by 11% to 9.4%, a 1.7% overweight versus the index.

As we said last quarter, we continue to favor slightly more “boring” companies with pricing power, more consistent earnings and profitability, or discounted stocks with attractive valuations and rerating potential. A number of those names were good relative performers for the strategy in the 1st quarter. While we thought international equities began the year cheap to the U.S. given nearly 15 years of U.S. outperformance, relative valuations only got cheaper in the 1st quarter given the conflict in Ukraine, with the relationship between 12-month forward Price/Earnings ratios on the S&P 500 and the MSCI ACWI ex USA now 2.2 standard deviations cheap to its 15-year average. ESG Leader stocks—companies with superior performance on material ESG factors relative to their peers—may continue to face headwinds as long as Value outperforms but should offer better risk/reward profiles in the longer term due mostly to their positive ESG attributes.

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### Important Information

*The performance data quoted represents past performance; it does not guarantee future results.*

Unless otherwise noted, the source of all data, charts, tables and graphs is Thornburg Investment Management, Inc., as of 31 March 2022.

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Portfolio holdings and characteristics shown herein are from a representative account managed within the investment composite. The representative account is selected based on account characteristics that Thornburg believes accurately represent the investment strategy as a whole. Should these characteristics change materially, Thornburg may select a different representative account. Holdings may change daily and may vary among accounts, which may contribute to different investment results.

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Investments in the Strategy carry risks, including possible loss of principal. Carefully consider the Strategy's investment objectives, risks, and expenses before investing. There is no guarantee that the portfolio will meet its investment objectives.

The Fund/Strategy's adherence to its ESG ratings process may affect the Fund/Strategy's exposure to certain companies, sectors, regions, and countries and may affect the Fund/Strategy's performance depending on whether such investments are in or out of favor. This process may result in the Fund/Strategy foregoing opportunities to buy certain securities when it might otherwise be advantageous to do so, or selling securities for ESG reasons when it might be otherwise disadvantageous for it to do so. Additionally, the process may result in incorrectly evaluating a company's commitment to positive ESG practices and may result in investment in companies with practices that are not consistent with the Fund/Strategy's aspirations.

The MSCI ACWI ex USA ESG Leaders Index consists of large- and mid-cap companies across 22 developed markets and 26 emerging markets countries. The Index is designed for investors seeking a broad, diversified sustainability benchmark with relatively low tracking error to the underlying equity market.

The MSCI ACWI ex USA Growth Net Total Return USD Index is a market capitalization weighted index that includes growth companies in developed and emerging markets throughout the world, excluding the United States.

The MSCI All Country (AC) World ex U.S. Value Index is a market capitalization weighted index representative of the market structure of 46 developed and emerging market countries in North and South America, Europe, Africa, the Middle East, and the Pacific Rim, excluding securities of United States' issuers. The index is constructed using an approach that provides a precise definition of style using eight historical and forward-looking fundamental data points for every security. The index returns reflect the reinvestment of dividends and other earnings, are net of withholding taxes, and do not include any trading costs, management fees or other expenses.

The MSCI ACWI ex USA Net Total Return USD Index is a market capitalization weighted index representative of the market structure of 46 developed and emerging market countries in North and South America, Europe, Africa, the Middle East, and the Pacific Rim, excluding securities of United States' issuers. The index is calculated with net dividends reinvested in U.S. dollars.

The MSCI EAFE (Europe, Australasia, Far East) Net Total Return USD Index is an unmanaged index. It is a generally accepted benchmark for major overseas markets. Index weightings represent the relative capitalizations of the major overseas developed markets on a U.S. dollar adjusted basis. The index is calculated with net dividends reinvested in U.S. dollars.

The S&P 500 Total Return Index is an unmanaged broad measure of the U.S. stock market.

Portfolio construction will have significant differences from that of a benchmark index in terms of security holdings, industry weightings, asset allocations and number of positions held, all of which may contribute to performance, characteristics and volatility differences. Investors may not make direct investments into any index.

**Basic Value:** Companies generally operating in mature industries and which generally exhibit more economic sensitivity and/or higher volatility in earnings and cash flow.

**Consistent Earners:** Companies which generally exhibit predictable growth, profitability, cash flow and/or dividends.

**Emerging Franchises:** Companies with the potential to grow at an above average rate because of a product or service that is establishing a new market and/or taking share from existing participants.

**Basis Point (bp)** – A unit equal to 1/100th of 1%. 1% = 100 basis points (bps).

**Yield Curve** - A line that plots the interest rates, at a set point in time, of bonds having equal credit quality, but differing maturity dates.

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