

Global Core Equity Fund

1992 Second Quarter Report

Description

The Global Core Equity Fund invests worldwide in common stocks and convertible securities with the objective of preserving and increasing investors' capital in US dollar terms. Harding, Loevner, McNally & Co. manages the Fund's investment portfolio. Capital Trust Company administers and oversees the Fund, and maintains custody of its investments. Units of the Global Core Equity Fund can be purchased or redeemed monthly at net asset value.

Portfolio Overview

At June 30, 1992, the portfolio:

- held investments in 39 large companies, including 18 US companies;
- was broadly diversified in terms of geographic distribution (as illustrated);
- consisted of 97% common stocks, the balance in cash and options; and
- had an annual yield of 2.6%.

The Past Quarter

The Fund performed exceptionally well in both absolute and relative terms, rising in value by 7.2%, before fees. Returns were enhanced by stronger European currencies.

The FT Index of world stocks rose by 1.4% in dollars. The US market itself accounts for a large component of this index. This quarter the S&P 500 rose 1.8%, compared to the FT ex. US Index which rose by 1.3% in dollars.

HLM's approach has been to build a globally diversified portfolio of high quality companies. Returns to holders of the Fund have, as a result, not only been high in absolute terms, but have also been much more stable than market indices.

Diversification and stock selection have proved their worth to holders of the Fund.

Transactions

In the US, HLM has largely stuck to the winning lineup of high quality growth companies. It believes that prices of cyclical stocks discount a recovery whose durability is in doubt. The capital spending cycle is one which *does* appear to offer attractive investment opportunities world-wide. Three investments were made in this sector during the quarter. **Dover Corporation** is a diversified manufacturer of industrial products. It is well managed, has good returns on equity and normally commands a premium valuation. It does not at the moment, as the share price has suffered from cyclical earnings concerns. HLM is confident that management is of the quality required to generate earnings growth.

In Europe, **Brown Boveri** is the worldwide leader in power generation, power transmission and related industrial products. The power generation business has an attractive secular outlook. Recent orders have been good and the share price does not discount recovery.

Makita is a Japanese manufacturer of power tools. It dominates the professional and semi-professional market in Japan itself, and will benefit from the forthcoming renewal of Japan's housing stock that HLM sees as an important and inexorable long-term trend. It is increasingly successful in taking market share from established producers in the West, notably Black & Decker. Makita is a good example of a Japanese company whose share price has suffered in the bear market despite greater financial strength and better products than its global competitors.

HLM's continual search for attractive companies in which to invest has again led to new investments in Asia. In addition to Makita, two new positions were established during the quarter:

In Hong Kong, a holding in **South China Morning Post** was added to the portfolio. The old fashioned name of this company belies its state-of-the-art publishing technology, the foundation of its domination of the English language newspaper business in Hong Kong. The company has no debt, pays out all its earnings to shareholders, yields 7.0% in, effectively, US dollars and should grow at a minimum in line with the rapidly growing economy.

The final Asian addition to the portfolio was of the **Siam Fund**. This closed-end fund is managed by Indo Suez Asia and has a portfolio of blue-chip Thai equities. It trades at a discount to its assets (like most closed-end funds), but is unusual in that from January 1993, investors will be able to redeem their holdings at full net asset value. Even in the absence of a rising market in Thailand (which HLM expects), the Siam Fund will provide an attractive return as the discount inevitably closes.

Companies

The only sector whose share price performance stood out in the quarter was the oil-related sector. **Baker Hughes**, **Royal Dutch** and **Schlumberger** all performed well, rising by 21%, 15% and 13% respectively. Other good performances were seen from an eclectic list of companies. Large, steady growth companies such as **L'Oréal**, **Sandoz** and **Unilever** all rose by significant amounts. L'Oréal's underlying business continues to be sound, but the 17% rise in the share price was chiefly the result of the narrowing of the discount between the ordinary shares and the non-voting "C.I.s" held in the portfolio. Sandoz likewise has demonstrated its quality as a steady growth company, but the proximate reasons for the 20% rise in the stock price were Swiss deregulation and improved financial disclosure. Among other changes to Swiss company law, companies will be able to buy back shares. Sandoz is likely to be among the first to take advantage of this new freedom.

Two Hong Kong stocks were good performers. **Hong Kong Gas** rose by 12% in response to the good local market and its well received bonus share and warrant issue to shareholders. Operating results were largely ignored in the excitement but confirmed that this well-managed company is capable of 20% annual growth in the next few years without damage to its balance sheet. The Fund's new holding in **South China Morning Post** provided instant gratification, rising by 17% after purchase.

Performance from the US holdings was mixed. **Corning** rose by 11% and now seems to have put the financial damage from the breast implant controversy behind it. **Bandag** rose by the same amount in response to good earnings in a difficult environment.

Among the losers, the biggest was **Apple Computer**, which fell by nearly 18%. All computer manufacturers were treated harshly in a quarter when leading companies in the IBM-compatible market cut prices and issued warnings about profitability. Apple is still misunderstood by a market more in tune to the commodity-type producers such as Compaq or Dell. Unlike these companies' products, Apple's Macintosh computer is not a commodity product. It is differentiated by its unique and attractive operating system, and therefore has greater control over its prices and margins than have other industry participants.

Perhaps the most remarkable performance in the quarter was from **Bangkok Bank**. Despite a sharp fall in the market in response to the political turmoil, the share price rose by 10%, testimony to the company's strength and underlying value as a fast growing regional financial institution.

Investment Performance

	Year to date	Total Returns %			
		1991	1990	Since Inception (12/89)	
				Cumulative	Compound
Global Core Equity Fund	5.8	28.5	6.4	49.8	16.9
Comparative Benchmarks:					
FT World Index	-7.4	19.7	-17.1	-5.1	-2.0
S & P 500	-0.8	30.4	-3.1	28.4	10.2
Global Fund Index (Lipper)	-0.5	18.7	n/a	n/a	n/a

Note: In response to repeated requests from investors for performance information of greater comparability, performance of Global Core Equity Fund is now being reported before management and trustee fees. These fees amount to approximately 1.5% per annum.