



# Bailard International Equity Strategy

Quarterly Recap

## Executive Summary as of December 31, 2022<sup>1,2</sup>

*By the end of 2022, stock and bond investors alike were ready to put a dismal calendar year in the rear-view mirror. Thankfully, the fourth quarter showed markets advancing once again—setting a more hopeful tone going into the New Year. This was especially true for investors in international equities, as the magnitude of Q4 outperformance (a nearly 10% advantage for MSCI EAFE vs. the S&P 500) gave the asset class its first calendar year “win” relative to U.S. indices since 2017. Foreign currencies regained some of their strength against the dollar, thanks to easing U.S. inflation and less hawkish expectations for the Fed. European markets led on the upside, and with the energy outlook improving considerably the regional positioning was increased from underweight to near neutral. The recession question looms large in 2023, but even though the U.S. economy may hold up better than some in Europe and elsewhere, we believe that deeply discounted valuations and an attractive sector mix make a case for international equities’ continued outperformance.*

## Market Commentary<sup>1,2</sup>

2022 came to a close showing the worst annual results for global equities since 2008, as surging inflation forced some of the most rapid interest rate increases from major central banks seen in the past thirty years. At least the final quarter brought relief to investors. Inflation readings—most notably in the U.S.—cooled towards end of year, and stocks rebounded out of the nasty downtrend established over the first nine months.

Foreign currencies also recovered in Q4 as expectations for a gentler Fed rate path eased a portion of the dollar’s prior extreme strength. This helped international equity markets as a group handily outpace U.S. indices. Developed and emerging Europe were the quarter’s regional leaders, and value outperformed growth as it did for the year overall. Fourth quarter returns were 17.34% for MSCI EAFE, 14.28% for

MSCI All-Country World ex-USA, and 9.70% for MSCI Emerging Markets (all indices in USD terms, net dividends).

## Composite Commentary<sup>2,3</sup>

The Bailard EAFE Plus Composite’s Q4 16.23% net of fee return lagged the developed market benchmark return of 17.34% for the MSCI EAFE Index, but handily outpaced the 14.28% return for the MSCI ACWI ex-US Index. Beaten-down Europe enjoyed the most dramatic rebound over the quarter, helped by a relatively mild winter and governmental support which have made the energy cost squeeze on businesses and households less severe than had been feared. Japan underperformed as inflation touched a 30-year high, prompting the government to loosen its policy of yield curve control and allow higher sovereign bond yields. Emerging market returns were pushed

<sup>1</sup> Unless otherwise indicated, developed and emerging market returns and comments are based on the respective MSCI EAFE or Emerging Markets indices (U.S. dollar terms on a total return basis, reinvesting dividends after the deduction of withholding taxes). <sup>2</sup> Regional, country and sector returns and comments cited in the composite commentary section are based on their respective MSCI regional and country indices (U.S. dollar terms on a total return basis, reinvesting dividends after the deduction of withholding taxes). Any references to specific securities are included solely as general market commentary and were selected based on criteria unrelated to Bailard’s portfolio recommendations or the past performance of any security held in any Bailard account or fund. <sup>3</sup> The Bailard International Equity and Emerging Markets Equity Strategies are implemented across three separate composites. The Composite performance commentary reflects the EAFE Plus Composite, which represented 21.8% of total strategy assets as of December 31, 2022. **Past performance is no indication of future results.** All investments involve the risk of loss. Please see page 3 for additional performance data and page 4 for important disclosures.

around by volatility in China; the abrupt zero-COVID policy reversal was viewed favorably by markets but has quickly overwhelmed hospitals, with unofficial new-case estimates in the millions. All EAFE sectors posted double-digit gains, with cyclicals favored over defensives. Financials (up 24.1%) and Materials (up 20.7%) rose the most while Consumer Staples (up 10.7%) and Real Estate (up 11.1%) were the weakest.

The Composite's country positioning among EAFE markets was moderately successful but was a detractor overall, due mainly to positions outside of the EAFE benchmark (Canada and emerging/frontier markets). Broadly speaking, stock selection results were least favorable in the Eurozone and Asia ex-Japan, while stock holdings outperformed in Japan and non-euro Europe (including the UK).

### Strategy Review<sup>4</sup>

By our measure, global equity market volatility rose over the quarter to end the year comfortably above the long-term average. Along with central bank tightening and the resulting lower liquidity, this leads the country model to prefer markets with good valuations and improving risks, and place somewhat less emphasis on momentum. Our top-ranked developed markets at the end of December were Japan, New Zealand, Israel, the UK, Hong Kong, Denmark, Portugal, and Singapore. Over the quarter, increased allocations to Europe (including the UK and Eurozone members Germany and Italy) came at the expense of Japan, Australia, and Canada. A new country position in Sweden was established. Japan's sudden year-end move back to the top ranks bears watching, to see if it stands the test of time, before being acted upon. Total emerging and frontier market weight edged down further, ending the quarter just above 4%. The largest overweight sector exposures at quarter's end were in Materials (2.4%) and Energy (1.3%); the largest underweights were in Real Estate (1.7%) and Communication Services (1.6%).

### Investment Outlook

Multiple forces point to a reversal of fortune for non-U.S. equities. We had been anticipating that as

### COUNTRY RANKINGS AT QUARTER END

The environment as of December 31, 2022 favored countries with strong value and momentum characteristics.

#### HIGHEST RANKED

Argentina	Japan
Chile	Korea
Colombia	New Zealand
Egypt	Pakistan
Hungary	Turkey
Israel	UK

#### LOWEST RANKED

Austria	Mexico
Canada	Morocco
Czech Rep.	Netherlands
Finland	Switzerland
India	Taiwan
Indonesia	Vietnam

Source: *Bailard, Inc.*

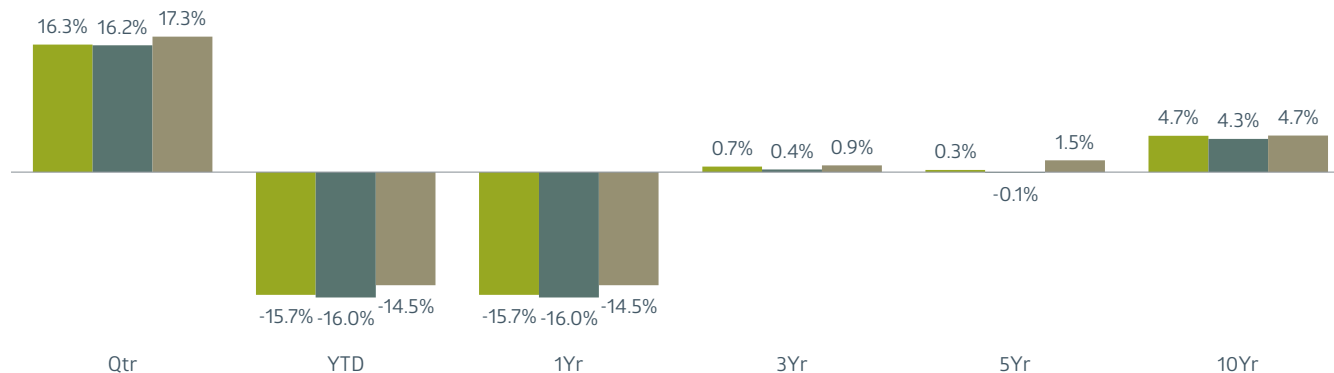
the Fed nears its peak for interest rates and other central banks (notably the ECB and the BOE) look to continue monetary tightening, the trend of dollar strength would reverse. We are seeing evidence of that shift beginning in Q4 and into the first weeks of 2023—boosted by cooler-than-expected U.S. inflation data which has sparked a recovery in risk assets and foreign currencies. This headwind-turned-tailwind has led to short-term outperformance of international equities over U.S. stocks. With valuations on non-U.S. stocks at historic discounts (along with a sectoral mix that may be more attractive than tech-heavy U.S. indices), the messy global picture may actually be one that favors international equities after a decade of underperformance.

<sup>4</sup> Data regarding holdings reflect ownership information as of December 31, 2022 and are not intended to represent any past, present, or future investment recommendations. Holdings are subject to change.

## Bailard EAFE-Plus Composite Statistics<sup>5,6,7</sup>

**PERFORMANCE** total return (%) for periods ending December 31, 2022

- Composite Gross of Fees
- Composite Net of Fees
- MSCI EAFE Index



### PERFORMANCE STATISTICS: 3-YEAR as of 12/31/22

	EAFE-PLUS COMPOSITE		MSCI EAFE INDEX
	GROSS OF FEE	NET OF FEE	
Standard Deviation	19.7%	19.7%	20.0%
Active Return (Net of Fee) vs.			-0.5%
Tracking Error (Net of Fee) vs.			2.2%
Information Ratio (Net of Fee) vs.			-0.24

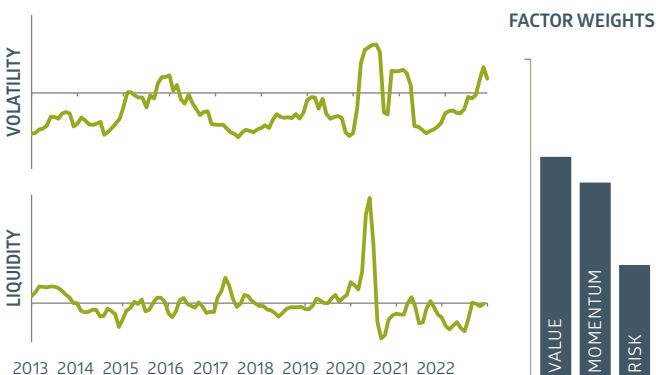
### PERFORMANCE STATISTICS: 5-YEAR as of 12/31/22

	EAFE-PLUS COMPOSITE		MSCI EAFE INDEX
	GROSS OF FEE	NET OF FEE	
Standard Deviation	17.5%	17.4%	17.4%
Active Return (Net of Fee) vs.			-1.6%
Tracking Error (Net of Fee) vs.			2.6%
Information Ratio (Net of Fee) vs.			-0.62

## Environmental Variables and Style Factors

as of 12/31/22

The charts below represent two variables that influence our assessment of the global investment environment and, in turn, dynamically affect the factor weights that are determinant in country selection.



Sources: MSCI, Federal Reserve, Bailard.

<sup>5</sup> Sources: Bailard, MSCI/Datastream. **Past performance is no indication of future results.** All investments involve the risk of loss. Please see page 4 for important disclosures. <sup>6</sup> Three-, five- and ten-year return statistics are annualized. <sup>7</sup> Performance data shown reflect the EAFE Plus Composite. <sup>8</sup> Data regarding holdings reflect ownership information as of December 31, 2022 and are not intended to represent any past, present or future investment recommendations. Holdings are subject to change.

## Representative Portfolio, Bailard EAFE-Plus International Equity Strategy<sup>8</sup> as of 12/31/22

### PORTFOLIO SUMMARY

# of Holdings	126
# of Developed Markets	17
# of Emerging, Frontier, and Other Markets	7
% Developed Markets	94.7%
% Emerging, Frontier, and Other Markets	4.1%
% Cash and Equivalents	1.2%

### REGIONAL WEIGHTS

Continental Europe	42.8%
United Kingdom	20.0%
Japan	17.1%
Pacific ex-Japan	11.0%
Emerging Markets	3.8%
Other Developed	3.8%
Frontier and Other Markets	0.3%
Cash and Equivalents	1.2%



## RISKS

In addition to the possible loss of investment value due to general market price movements, international investments might suffer losses due to unfavorable exchange rate movements or economic and/or political instability in foreign countries. In some cases, financial statement information might not be readily available or might not be reliable for certain foreign markets. International accounting standards might be different from U.S. accounting standards, and financial data might be subject to misinterpretation. Trading in international markets can be more expensive than trading in domestic markets. Stock markets of certain foreign countries, particularly emerging and frontier markets, may be illiquid, and settlements can be delayed. Emerging and frontier markets have greater risks and can have higher transaction costs than their developed market counterparts. There can be no guarantee that this or any investment strategy will achieve its objective.

## PERFORMANCE DISCLOSURES

The Bailard International Equity and Emerging Markets Equity Strategies are implemented across three separate composites with a total AUM of \$718.7 million as of December 31, 2022. All data and performance presented in this publication reflect the EAFE Plus Composite, previously called the Bailard International Equity Composite (the "Composite"), which consists of all discretionary fee-paying accounts that are invested primarily in non-U.S. securities both in developed and emerging markets. As of December 31, 2022, the Composite consisted of a single mutual fund account with a market value of \$157.0 or 21.8% of the strategies' assets, which has been managed using a quantitative methodology in an advisory or sub-advisory capacity since 1995. Prior to that time, the account was managed using a different strategy. The Composite's returns are presented both gross and net of management fees, and assume reinvestment of dividends and other earnings. The returns also reflect transaction costs. Three-year, five-year and ten-year returns are annualized. Composite returns do not reflect a fiduciary fulfillment fee payable to Bailard (where applicable), or custody and other expenses not payable to Bailard which the composite account incurred.

Through June 2009, gross of fee performance was calculated by grossing up the NAV performance by the annual expense ratio. Through March 2006, net of fee performance was calculated by netting down the gross return by a model fee of 0.95% on first USD 250M (applied by reducing monthly returns by 1/12 of 0.95%); 0.90% per annum thereafter. From April 2006 through June 2009, net of fee performance was calculated by netting down the gross return by a model fee of 0.475% on first USD 250M (applied by reducing monthly returns by 1/12 of 0.475%); 0.45% per annum thereafter. This model fee represents the highest management fee for the composite. From July 2009, both gross of fee and net of fee returns are taken directly from Bailard's portfolio accounting system, and net of fee performance was calculated by netting down the gross return by our actual management fee as of the date paid from each account. The composite's complete return history and a complete list of Bailard's composites are available upon request.

Individual account management and construction will vary depending on each client's investment needs and objectives, including liquidity needs, tax situation, risk tolerance, and investment restrictions. Individual accounts may not have the same management fees, expenses, diversification, distributions, cash flows and currency hedging policies as the Composite account. As a result, an account's actual performance may differ from the performance presented in this piece due to among other things, timing of investment, contributions and withdrawals, and the client's restrictions, such as restrictions of

currency hedging. In addition, performance does not reflect the effects of taxation, which can result in lower returns to taxable investors. An investment in this strategy involves risk of loss, and the value of an investment may decrease as well as increase. No representation is made that any account will obtain similar results to those shown here.

**Other Performance Definitions:** Standard deviation is the annualized standard deviation of monthly returns. "Information ratio" is the ratio of added value to tracking error. "Tracking error" is the annualized standard deviation of monthly added value, where added value is [Composite return – benchmark return]. Valuations are computed and performance reported in U.S. dollars.

**Market Indices:** The MSCI EAFE, MSCI Emerging Markets, and MSCI ACWI ex USA indices are free float-adjusted market capitalization indices. The MSCI EAFE Index is designed to measure equity market performance of international developed markets. The MSCI Emerging Markets Index is designed to measure equity market performance of international emerging markets. The MSCI ACWI ex USA Index is designed to measure equity market performance in international developed (excluding the U.S.) and emerging markets. These indices are presented in U.S. dollar terms on a total return basis, reinvesting dividends after the deduction of withholding taxes (if any). The indices are unmanaged and uninvestable and do not reflect any transaction costs.

Unlike the MSCI EAFE Index, the Composite account invests in emerging and frontier markets. Unlike the MSCI Emerging Markets Index, the Composite account invests in developed and frontier markets. Unlike the MSCI ACWI ex USA Index, the Composite account can invest in frontier markets. Unlike all of these indices, the Composite account invests in cash equivalents, depository receipts and exchange-traded funds, and may engage in currency hedging. The Composite often employed different country weights than these indices. The Composite's country weights, security weights, and security holdings may differ materially from these indices.

**Past performance is no indication of future results.** All investments have the risk of loss.

## OTHER DISCLOSURES

The information in this publication is based primarily on data available as of December 31, 2022, and has been obtained from sources believed to be reliable, but its accuracy, completeness and interpretation are not guaranteed. In addition, this publication contains the opinions of the authors as of that date and such opinions are subject to change without notice. We do not think this publication should necessarily be relied on as a sole source of information and opinion. This publication is not a recommendation of, or an offer to sell or solicitation of an offer to buy any particular security or investment product. It does not take into account the particular investment objectives, financial situations or needs of individual clients. Bailard cannot provide investment advice in any jurisdiction where it is prohibited from doing so.

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