

World Class Companies
Bigger does not necessarily mean better

Historical Performance of Small Caps
Global small indices have outperformed large-cap indices

Large Opportunity Set
A dedicated small cap team to find investment opportunities

Fund Facts

Number of stocks	83
Total Fund Size	\$211.1m
Inception Date	13 December 2002
Total Management Costs	W Class: 1.12% p.a.
Index	MSCI World Small Cap
Minimum Investment	\$20,000
Buy/Sell Spread	+0.25%/-0.25%
Distributions	Annually
APIR Code	LAZ0012AU

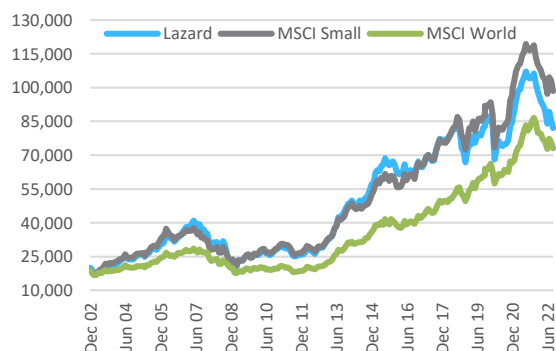
Investment Characteristics

	Lazard	Index
Forward Price/Earnings	11.6	14.2
Forward Return on Equity (%)	15.6	11.0
Price/Cash Flow	8.6	8.5
Weighted Average Market Cap (\$m)	7,606	5,626
Active Share (%)	96.9	-
3 Year Turnover (% pa)	57.0	-

Performance¹ (%)

	Lazard	Index	Excess Return
1 Month	-3.9	-4.3	0.4
3 Months	-2.2	1.3	-3.6
1 Year	-21.7	-15.8	-5.9
3 Years (pa)	0.0	4.3	-4.3
5 Years (pa)	2.6	6.6	-4.0
10 Years (pa)	11.1	12.8	-1.7
Since Inception (pa)	7.4	8.6	-1.2

Growth of \$20,000¹



Allocations (%)

Sector	Lazard	Index	Overweight/underweight
Communication Services	0.8	2.7	-1.9
Consumer Discretionary	13.1	12.1	1.0
Consumer Staples	6.4	4.9	1.5
Energy	4.7	5.2	-0.5
Financials	14.8	14.5	0.4
Health Care	13.2	11.4	1.7
Industrials	18.4	18.5	-0.1
Information Technology	10.0	11.2	-1.2
Materials	4.8	7.3	-2.6
Real Estate	8.8	9.0	-0.2
Utilities	3.4	3.1	0.3
Other	-	-	-
Cash	1.6	-	1.6
Region			
Europe ex UK	17.3	11.4	5.9
United Kingdom	5.1	5.1	0.0
North America	60.4	65.5	-5.1
Japan	11.3	11.2	0.1
Asia Pacific ex Japan	1.3	5.7	-4.4
Middle East	-	1.1	-1.1
Emerging Markets	3.1	-	3.1
Cash	1.6	-	1.6

Top 5 Holdings (%)

	Lazard	Index
Commerce Bancshares	3.7	0.1
East West Bancorp	3.1	0.2
Icon	2.2	0.0
Envista	2.0	0.1
Armstrong World	1.9	0.1

¹ Performance is presented net of W Class fees, please refer to www.lazardassetmanagement.com for performance of the I Class.

Investments can go up and down. Past performance is not necessarily indicative of future performance. Net returns are quoted after the deduction of Management Costs. Performance assumes reinvestment of all distributions.

Market Overview

Global small cap markets fell sharply in the quarter in USD terms as investor concerns continued to rise regarding central bank policy, yields, inflation, and a slowdown in economic growth. Given the strength of the USD, however, global small cap markets rose modestly in AUD terms. The energy sector once again led, rising in absolute terms, and significantly outperforming all other sectors. Healthcare also did well on a relative basis, while real estate and communication services lagged. On a relative basis, the United Kingdom and Continental Europe lagged materially while the United States was a notable outperformer. The USD strengthened significantly against most other currencies in the period. The DXY Index rose 7% in the quarter (and is up nearly 17% year-to-date as of 30 September 2022).

Commentary

Portfolio outperformance during a difficult September was offset by underperformance in July and August, resulting in negative attribution for the quarter. Currency and industry headwinds, as well as negative stock selection impact, detracted from relative performance in the period. The portfolio's underweight to USD stocks—via EUR stocks in particular—detracted as the EUR fell to a 20-year low and broke parity. The portfolio's underweight in fossil fuels and related industries (due both to sustainability risks as well as to frequently low financial productivity) continued to serve as a headwind in the current environment. Positive stock selection impact in the financials and industrials sectors was offset by negative stock selection impact in the health care and information technology sectors.

PGT Innovations (industrials) – a US-listed window and door manufacturer – contributed positively to relative performance in the period. The shares rose alongside the release of strong quarterly results that demonstrated robust pricing power, solid demand, and disciplined cost control in an inflationary environment. The portfolio continues to hold the shares.

Jafco (financials) – a Japan-listed venture capital and private equity manager – contributed positively to relative performance in the period. The shares rose following the disclosure of a large holding by an activist investor. The portfolio continues to hold the shares.

Catalent (health care) – a US-listed Contract Development Manufacturing Organization (CDMO) serving pharmaceutical customers – detracted from relative performance in the period. The share price fell alongside a mixed set of quarterly results that included a larger-than-expected decline in the company's COVID-19 related operations and a subsequent FDA notice regarding operations at a production facility for the Moderna vaccine. The portfolio continues to hold the shares.

Crayon (information technology) – a Norway-listed value-added software reseller – detracted from relative performance in the period. The share price fell following the release of a mixed set of quarterly results that included weaker-than-expected profitability. The portfolio continues to hold the shares.

Outlook

Concerns about inflation, rates, central bank policy, and recession continue to rise as economic data continues to soften.

Business conditions in Europe are particularly challenging: the European Central Bank was unable to significantly stimulate growth while monetary policy was extraordinarily easy, and it is now forced to tighten to fight inflation. Meanwhile, dependence on Russian gas will likely become more problematic with the onset of colder weather. Chinese economic activity has improved since spring pandemic lockdowns, but remains soft due to weak household consumption, continuation of zero COVID-19 policies, property market difficulties, and a deteriorating global export environment.

Equity and credit markets, however, have begun to discount slowing economic growth. As difficult as equity markets have been, 5-year US Treasury yields are up nearly 300 basis points in less than a year, indicative of the worst bond market in nearly a century. The yield curves in many bond markets have also inverted, typically a precursor to a recession. Due to their higher sensitivity to changes in the economic cycle, small cap equities have suffered more than large caps. Over the last twelve months, they have trailed large caps by approximately 620 bps in US Dollar terms. The MSCI World Small Cap Index now trades at a 10% discount (2023 P/E) to the MSCI World Large Cap Index, nearly two standard deviations and approximately 1,700 bps below the 20-year average. While not unprecedented, small caps rarely trade at a discount to large caps. In fact, they have traded at a 12% premium to large caps on average over the last two decades. In addition, just as small caps tend to drop more than large caps during periods of economic contraction, they tend to rise more in periods of economic growth. While we cannot predict when equity markets will stop falling, we are confident small caps will outperform when the upswing occurs.

In the meantime, we continue adding capital to positions, new and old, where we have the highest conviction and can do so at attractive valuations. These changes are happening across a variety of sectors, in both defensives and cyclicals. We have also increased our focus on balance sheets to ensure portfolio companies can weather a recession. Finally, we are keeping a close watch on our “wish-list” of companies to enable quick action as extraordinary buying opportunities continue present themselves.

For more information, call us on 1800 825 287
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