

# Sun Life MFS International Opportunities Fund

FUND COMMENTARY | Q3 2020

*Opinions and commentary provided by MFS Investment Management Canada Limited.*

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## Market review

Markets rallied in Q3 fueled by unprecedented fiscal and monetary stimulus. Cyclical and work-from-home technology beneficiaries led the third quarter market rally, while defensives, financials and energy lagged. This suggests investors expect the global economy to recover significantly and relatively quickly. Technology companies could see secular long-term growth driven by people working and attending school remotely or in a hybrid model for a considerable time to come.

MFS is less optimistic that global economies will return to 2019 levels any time soon. A number of uncertainties to consider include: how a second wave of COVID-19 infections could impact economies; and when an effective vaccine would be widely distributed.

## Portfolio positioning

The portfolio was overweight the consumer staples and materials sectors. Many of the Fund's consumer staples companies have pricing power and derive a significant portion of their revenues from underpenetrated emerging markets countries, which can lead to stronger revenue growth and more stable earnings growth than the overall market. Within materials, Linde and Air Liquide are two of the largest positions in the Fund. These high-quality cyclicals have generated returns above their cost of capital and significant free cash-flow over a full cycle, driven in part by long-term contracts with built-in price escalators.

The portfolio was underweight consumer discretionary and communication services sectors. The Fund's underweight to consumer discretionary stems from the avoidance of multiline and specialty retailers, many of whom are facing pressure from e-commerce competition, and the avoidance of auto companies, which are

investing heavily to meet stringent CO2 emissions requirements. The underweight to communication services is primarily the result of not owning many telecommunications companies, which, the portfolio manager believes, typically do not have sustainable above-average growth or pricing power.

Following are some of the key trades during the third quarter:

- Alibaba was added back into the portfolio based on its relatively inexpensive valuation and potential for margin growth.
- Initiated a position in Chinese software company Kingsoft Corp, which provides games, cloud and office productivity software.
- Exited British specialty chemicals company Croda and German chemical distribution company Brenntag.
- Trimmed L'Oreal and Accenture at higher valuations after solid execution by the businesses led to strong share price gains over the last couple of years.

## Market insights

Significant disruptions to global supply chains due to the Chinese tariffs dispute in 2019 and the global pandemic in 2020 are forcing companies to revisit their supply chains.

MFS believes reshoring is here to stay, though it will take time for companies to make significant changes to their supply chains. Some industries that stand to benefit from reshoring include construction engineering, factory automation, electrical equipment manufacturers, application software companies and industrial gas producers.

## Market outlook

European equities continued to rally throughout the summer, regaining roughly 70% of their first quarter decline before losing ground toward the end of the third quarter. Weaker global demand, due in large part to fallout from the pandemic, has undermined demand for European exports and restrained industrial production. At the same time, a near freeze in international tourism has heavily dented GDP in countries such as Greece, Italy and Spain.

In the United Kingdom, a halting economic recovery from the COVID-19-induced lockdown, along with dwindling prospects for a comprehensive post Brexit trade deal with the EU, have heavily undermined U.K. shares in 2020.

Despite fresh monetary and fiscal accommodation, the effects of the coronavirus pandemic have severely disrupted Japan's economy. Fallout from the pandemic has darkened Japan's employment picture. A stronger yen has been a headwind for Japan in recent months, with the currency's strength compounding the challenges posed by tepid global demand. After flattening the curve in April-June, a second wave of COVID-19 started to hit Japan around mid-July when confirmed cases started to pick-up rapidly. However, the business outlook has begun to improve. Japanese equities outperformed global equities this quarter by 1.3% in U.S. dollar terms.

Early in the COVID-19 crisis, emerging markets equities struggled compared with developed market equities, leading to relative underperformance through the first half of the year. As risk sentiment began to shift, emerging markets equities returned almost 10% in the third quarter versus about 8% for developed markets, closing a large portion of the year-to-date performance gap.

Chinese equities have outperformed developed and other emerging markets meaningfully this year. In addition to local market interventions that have helped to support growth, China weathered the brunt of the coronavirus crisis earlier than most nations. A relatively strict policy on both social distancing and masking seems to be paying off, as measures of production appear to have stabilized earlier than most of the world.

## Significant impacts on performance

### CONTRIBUTORS

#### + Infosys

Holdings of the technology consulting firm bolstered relative performance. The share price benefited from the accelerated digital transformation of enterprises, demand for cloud-based solutions, automation, cost efficiency and consolidation.

#### + Taiwan Semiconductor

An overweight position in the semiconductor manufacturer contributed to relative returns. The company reported strong second-quarter net income and provided third-quarter guidance that exceeded expectations, as it expects higher 5G penetration in the second half of the year to lift revenues.

#### + Namco Bandai

An overweight position in the video game and toy manufacturer benefitted relative performance. The company reported strong operating profits that came in ahead of market expectations, driven by strength in its games segment.

### DETRACTORS

#### — Alibaba Group

The timing of the portfolio's ownership in shares of online and mobile commerce company held back relative returns.

#### — Bayer

Holding shares of the life sciences company detracted from relative returns as the company posted mixed second-quarter financial results.

#### — Rolls-Royce

An overweight position in the diversified industrial manufacturer weakened relative results as the outlook for the wide-body engine market continues to be under pressure from reduced hours flown.

## Fund performance

<b>COMPOUND RETURNS %<sup>1</sup></b>	<b>SINCE INCEPTION<sup>2</sup></b>	<b>10 YEAR</b>	<b>5 YEAR</b>	<b>3 YEAR</b>	<b>1 YEAR</b>	<b>Q3</b>
Sun Life MFS International Opportunities Fund - Series A	8.1	8.1	8.8	8.3	10.2	5.3
Sun Life MFS International Opportunities Fund - Series F	9.3	9.3	10.1	9.6	11.5	5.6
MSCI EAFE	8.8	7.4	5.2	2.8	1.4	2.8

<sup>1</sup>Returns for periods longer than one year are annualized. Data as of September 30, 2020.

<sup>2</sup>Partial calendar year. Returns are for the period from the fund's inception date of September 30, 2010 to December 31, 2010.

Effective June 1, 2020, Sun Life MFS International Growth Fund was renamed Sun Life MFS International Opportunities Fund.

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