



Unboxing Value

One of our clients recently asked us about Morningstar’s Style Box “Blend” designation for the Causeway International Value Fund. **Does this signal change at Causeway to investigate?** Our short answer is no—but let’s investigate.

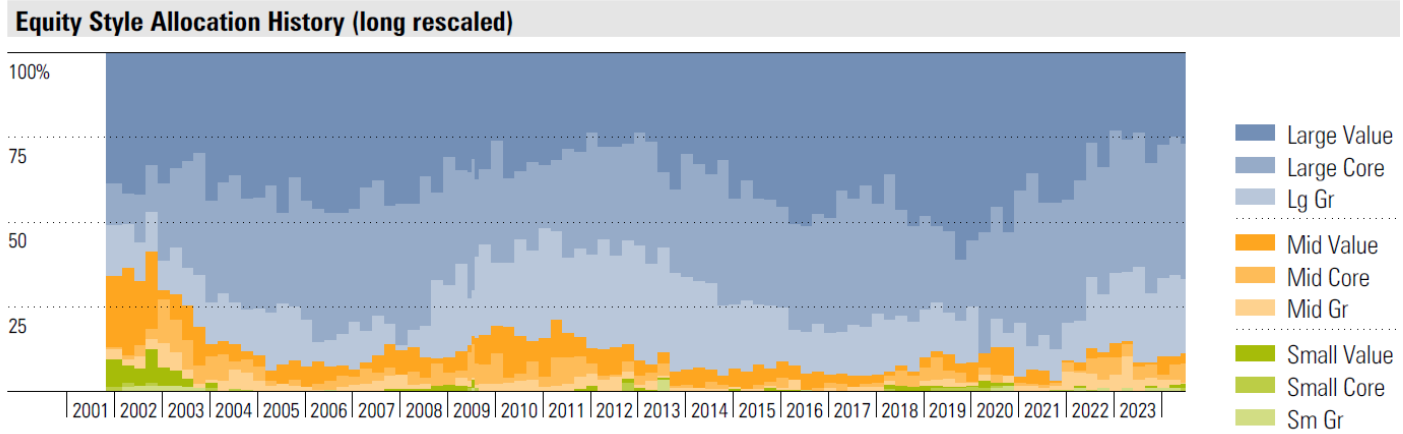
CAUSEWAY’S HISTORICAL STYLE

The Morningstar Style Box can help investors quickly visualize an estimate of a manager's investment approach and serve as a starting point for comparing different funds. However, further research is essential to understand a manager's investment philosophy and process.

Since its inception, Causeway has consistently applied the same value investment process to international markets, supported by a stable team—Causeway portfolio managers have an average tenure of 19 years with our firm as of June 30, 2024. Our investment process seeks to be dynamic to respond to market opportunities. This time-tested process yields portfolio characteristics that generally change with the investment opportunity set.

Figure 1 below shows Morningstar's history of Causeway's International Value Fund style exposure. Since the Fund’s inception in 2001, Causeway's style has moved between value and core categorizations. During client portfolio reviews, we often point out that the portfolio characteristics are between Core and Value. This has typically been true historically and is true currently (as of the last quarter-end). This is partially explained by Causeway's efforts to avoid significant exposure to low-quality stocks in the value index (aka “value traps”).

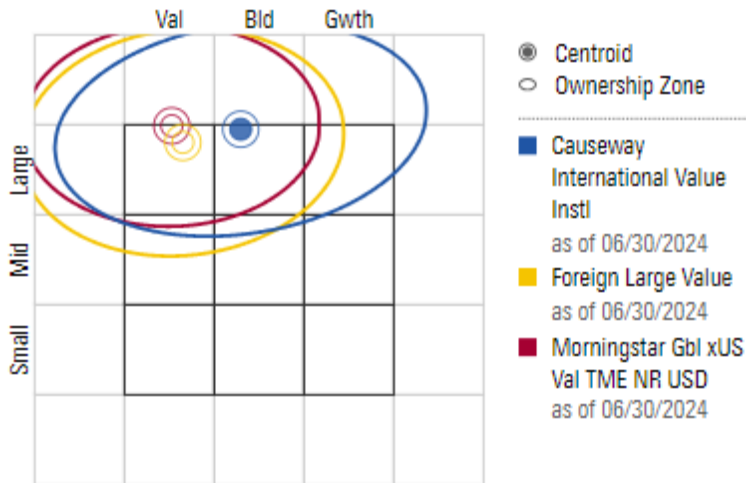
Figure 1
Causeway International Value Fund style analysis over time, as of June 30, 2024



Source: Morningstar

We should note that migrating from one style box to another isn't unusual or unique to Causeway. Morningstar added historical ranges to its style box grid to help visualize this phenomenon. For example, see Causeway International Value Fund ([CIVIX](#)) in Figure 2.

Figure 2



Source: Morningstar

In Figure 3 we look at a manager known for “deep value.” This manager’s fund has spent years in Morningstar’s Category Classification of Foreign Large Blend (FB). It is probably fair to say that active management requires some flexibility beyond standardized style classifications.

Figure 3

Total Return %	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	YTD
Category	-6.32	-3.10	3.34	22.08	-15.44	17.80	0.88	11.83	-9.09	17.51	6.85
Index	-5.42	-8.54	8.92	24.23	-13.99	17.13	0.61	11.88	-9.04	17.41	6.79
Quartile Rank											
# of Invest. in Cat.	348	358	337	317	315	346	352	348	354	380	353
Category Name	FB	FB	FB	FB	FB	FB	FB	FV	FV	FV	FV

USD | YTD Investment as of Jul 26, 2024 | Category: Foreign Large Value as of Jul 26, 2024 | Index: Morningstar Gbl xUS Val TME NR USD as of Jul 26, 2024

Source: Morningstar. FB= Foreign Large Blend; FV= Foreign Large Value.

VALUATION TECHNIQUES

As mentioned earlier, one of the benefits of style box analysis is speed and consistency. The valuation techniques are simplified and standardized for use across diverse investments. However, a particular manager's approach to valuation will almost certainly be different than Morningstar's standardized approach. Causeway, for example, uses a range of valuation methodologies based on a particular investment. Furthermore, Causeway focuses on two-year price targets, which typically require more judgment than historical earnings or shorter-term estimates.

To estimate valuation, Morningstar uses 50% trailing and 50% forward numbers, which do not include two-year estimates. This is a critical difference, essential for understanding Causeway's current categorization.

Causeway likes to buy shares in companies with improving earnings profiles – ideally buying them at *tough, or cycle-low, earnings*. In such cases, a simple reading of a readily available earnings multiple can be misleading.

For example, assume a \$10 stock in the banking industry consistently earning \$1/share—it would trade at a 10x multiple. However, that company may have had some temporary issues or business cyclicality causing earnings to fall to \$0.25/share last year, but Causeway expects it to return to earning \$1/share in two years. (We love buying stocks like these.) We might say, "We know the company, met with management, and believe they're making prudent decisions. It used to trade at 10x earnings, and we think it will again in the next two years." As simple as this sounds, a surface-level reading of earnings would show this stock trading at 40x last year's earnings and 20x next year's earnings.

Table 1

	<u>Earnings</u>	<u>Multiple</u>
Average earnings (5yrs)	\$1.00	10x
Last year's earnings (last twelve months)	\$0.25	40x
Next year's earnings (next twelve months)	\$0.50	20x
Two years forward earnings (fiscal year two)	\$1.00	10x

This is a hypothetical example.

Style boxes struggle with stocks like the bank example above because earnings can grow quickly off the trough. In this example, the bank's earnings will double this year and double again next year. Does this make it a high-multiple growth stock? No, because earnings, like the multiple, will most likely revert towards the company's longer-term trend.

Causeway understands this. Morningstar does, too, but they do not tailor their methodology for each investment they analyze, nor should they. Customizing the analysis would spoil the speed and consistency that characterize the style box grid. Company-specific research and valuation is the work of an active manager like Causeway.

Looking at Causeway's International Value Fund, we see many examples of high trailing multiples and more reasonable forward multiples. In Table 2, we examine the top ten highest multiple stocks based on last year's earnings (LTM) and compare them with their multiple based on two-year forward estimated earnings (FY2). For this subset of high multiple holdings, the average trailing price-to-earnings (P/E), a stock's share price divided by the last twelve months' earnings-per-share is 47x, and the average FY2 P/E is 20x.

Table 2

The highest P/E (LTM) stocks in the Causeway International Value Fund

sorted by P/E (LTM)

	P/E (LTM)	P/E (FY2)
SK hynix	65x	7
SAP	39x	30
AstraZeneca	37x	17
RELX	37x	27
Murata Manufacturing Co.	32x	21
Fanuc Corporation	32x	25
Air Liquide	31x	23
Canadian Pacific Kansas City Ltd.	29x	21
Compass Group	27x	20
Deutsche Telekom	26x	11
Average	47x	20x

Source: FactSet. Data as of June 30, 2024. Weighted average of constituent stocks.

No mention of particular securities may be construed as a recommendation or considered an offer to sell or a solicitation to buy any securities.

For context, as of June 30, 2024, for the overall portfolio, Causeway International Value's FY2 P/E multiple was 11x, right between Core and Value as referenced earlier.

Table 3

Causeway International Value Fund FY2 P/E valuation: between the Core and Value Index

	FY2 P/E
MSCI EAFE Value Index	10x
Causeway International Value	11x
MSCI EAFE Index	13x

Source: Causeway, FactSet. Data as of June 30, 2024. Weighted average FY2 P/E of constituent stocks. No mention of particular securities may be construed as a recommendation or considered an offer to sell or a solicitation to buy any securities.

PERFORMANCE ANALYSIS

What has driven Causeway's strong investment returns, and is this consistent with what we expect? The short answers are "value stocks" and "yes."

Both share classes of Causeway's International Value Fund ([CIVIX](#) and [CIVVX](#)) have outperformed the broad market international equity benchmark, MSCI EAFE Index (Gross and Net), by more than 3.5% annualized for the three years to June 30, 2024. The top ten relative contributors over that period are listed below. Their weighted average earnings multiples (LTM and FY2) are 11x. The top ten relative detractors over the same period should have, in our view, more earnings and share price recovery to go. We believe that upside is reflected in higher multiples and more precipitous drops between trailing and forward P/Es.

Table 4

P/E multiples: Causeway International Value Fund stock-drivers of three-year alpha (return above the benchmark MSCI EAFE Index)

Top contributors

	P/E (LTM)	P/E (FY2)
Rolls-Royce Holdings	16x	24x
UniCredit	6x	6x
Shell	13x	8x
ING Groep	8x	8x
TotalEnergies	7x	7x
BP	11x	7x
AXA	10x	8x
Barclays	8x	5x
Industria de Diseno Textil	26x	23x
CaixaBank	7x	7x
Average	11x	11x

Top detractors

	P/E (LTM)	P/E (FY2)
Akzo Nobel	16x	12x
Fanuc	32x	25x
Reckitt Benckiser	20x	12x
Prudential	14x	9x
Alstom	--	8x
Diageo	17x	17x
Kering	20x	17x
Valeo	--	--
Samsung Electronics	28x	11x
WH Smith	23x	12x
Average	20x	14x

Source: FactSet. Data as of June 30, 2024. Companies with no P/E listed had negative earnings for the period. Average is the weighted average using end-period weights. No mention of particular securities may be construed as a recommendation or considered an offer to sell or a solicitation to buy any securities.

CORRELATIONS

Does Causeway still provide diversification benefits when paired with a growth manager? The short answer is "yes."

As a proxy for "Growth," we use Vanguard's International Growth Fund (VWILX), which employs two growth-oriented subadvisors. Correlations can change over time, especially for actively managed portfolios, so we review three lookback periods for realized active correlations. In Table 5, you can see that Causeway's active returns (fund returns – MSCI EAFE Index returns) are uncorrelated or negatively correlated with this multi-manager international growth fund.

Table 5

	Active Return Correlation
12mo	0.00
36mo	-0.06
60mo	-0.15

As of 6/30/2024. Source: Causeway Risk Lens. Risk Lens is For Investment Professional Use Only. Active performance is fund performance minus benchmark performance. Active return correlations are based on funds' actual returns, as provided by Bloomberg, compared to the benchmark measured over the 12, 36, and 60-month periods ended at the reference date. Correlations range from --1 to +1. A score of 0 means the funds have no correlation, a score of 1 means the funds are exactly correlated, and a score of --1 means the funds are exactly oppositely correlated.

Causeway International Value Fund Total Returns as of 6/30/2024						
	Quarter	1 Year	3 Year	5 Year	10 Year	Since Inception
Institutional Class (Net)	1.24%	10.43%	7.26%	9.08%	4.68%	7.32%
Investor Class (Net)	1.20%	10.14%	7.00%	8.82%	4.44%	7.07%
MSCI EAFE © (Gross)	-0.17%	12.09%	3.43%	6.98%	4.84%	6.43%
MSCI EAFE © (Net)*	-0.42%	11.54%	2.89%	6.46%	4.33%	5.94%

The performance data quoted herein represents past performance. Past performance is not a guarantee of future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth less than their original cost, and current performance may be lower than the performance quoted. For performance data current to the most recent month end, please call 1.866.947.7000. Returns greater than one year are annualized. Total returns assume reinvestment of dividends and capital gains distributions at net asset value when paid. Investment performance reflects contractual fee waivers. In the absence of such fee waivers, total return would be reduced. Investor Class shares charge up to a 0.25% annual shareholder service fee. High relative or absolute performance may not be repeatable. High relative or absolute performance may not be repeatable.

To determine if the Causeway International Value Fund is an appropriate investment for you, carefully consider the Fund's investment objectives, risk factors, charges and expenses before investing. Please read the summary or full prospectus carefully before you invest or send money. To obtain additional

information including charges, expenses, investment objectives, or risk factors, or to open an account, call 1.866.947.7000, or visit us online at www.causewayfunds.com.

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Effective January 26, 2024, the Fund's benchmark changed from the MSCI EAFE Index (Gross) to the MSCI EAFE Index (Net). The MSCI EAFE Index (Gross) is calculated to reflect reinvestment of distributions without any deductions for tax withholdings on such distributions. The MSCI EAFE Index (Net) is calculated to reflect reinvestment of distributions after accounting for tax withholdings on such distributions by applying a maximum assumed tax withholding rate. The Fund believes "net" benchmarks are regularly used by other registered investment companies and generally better align with the tax impact on the Fund's foreign security holdings.

The MSCI EAFE Index is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the U.S. & Canada. The MSCI Value variation is a subset of the referenced index, and target 50% coverage of the index, with value investment style characteristics for index construction using three variables: book value to price, 12-month forward earnings to price, and dividend yield. The indices are gross of withholding taxes, assume reinvestment of dividends and capital gains, and assume no management, custody, transaction or other expenses. It is not possible to invest directly in these indices. MSCI has not approved, reviewed, or produced this report, makes no express or implied warranties or representations and is not liable whatsoever for any data in the report. You may not redistribute the MSCI data or use it as a basis for other indices or investment products. Accounts will not be invested in all the constituent securities of their benchmark indices at all times, and may hold securities not included in their benchmark indices.

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