NATIXIS
GLOBAL ASSET MANAGEMENT

FUND COMMENTARY

Oakmark Natixis Funds

Harris Associates L.P.

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KEY INDEXES REBOUNDED AS INVESTORS ABSORBED THE IMPLICATIONS OF U.S. PRESIDENTIAL ELECTION IN Q4 2016

Immediately following the presidential election, U.S. index futures plunged, and at one point, futures for the Dow Jones Industrial Average dropped nearly 900 points*. Surprisingly, as investors absorbed the implications of this political sea change, key indexes rebounded and ended higher on November 9. The Dow went on to close at a record high level on November 10 and finished up for the quarter. Financials led the advance, first benefiting from investors' hopes that the new Republican administration would roll back industry regulations and second, from the Federal Reserve's (Fed) decision to raise short-term interest rates for the first time in 2016. Citing signs that the economy has improved, the Fed also stated it intends to raise rates three times in 2017. Similarly, optimism that policy makers will carry through on promises of considerable infrastructure spending helped share prices in the industrials and materials sectors and the pledge to expand domestic oil and gas production boosted energy companies' shares.

Conversely, the health care, consumer staples and real estate sectors largely declined in the quarter. The uncertain future of the Affordable Care Act hurt the health care sector and a shift to cyclical stocks pressured defensive names in the consumer staples sector. Investors' concerns about the real estate sector were twofold. First, future interest rate increases could lead to higher mortgage rates, which might hamper growth in the sector. Also, owing to vows from the president-elect, possible mass immigrant deportations could drive a construction labor shortage and thus push real estate building costs higher.

Improving market conditions have prompted investors to realize the earnings potential of some otherwise overlooked companies. We appreciate when the market begins to recognize our perception of the intrinsic values of our holdings. Yet, our approach remains steadfast even when market sentiment turns pessimistic. We know that several policy-related issues are now in flux and the outcome of these could have large economic effects which move markets. Therefore, we remain prepared to capitalize on the opportunities that these events provide for the benefit of our investors.

THE PORTFOLIO

Top Performers: Investors' expectations that a Trump administration and a Republican majority in Congress would lead to increased spending on infrastructure projects and less regulation boosted the share prices of financials holdings, including **Bank of America**, during the quarter. In addition, speculation that Trump's proposed tax reform would enhance economic growth and subsequently allow for interest rates to return to more normalized

* in USD

levels benefited companies in the sector. In our estimation, Bank of America remains attractively priced, even without an increase to interest rates. Given the strong capital markets performance, healthy loan and deposit growth and continued progress reducing the expense base exhibited in the company's Q3 earnings report, we remain confident that management has a solid plan and believe the investment will continue to provide value for our shareholders. In the days following the presidential election, **Goldman Sachs** was one of the four largest contributors to the Dow Jones Industrial Average Index's rise to surpass 19,000 for the first time ever. We liked that Goldman Sachs' Q3 earnings report released in October showed that strengths spanned a range of business segments as net revenue more than doubled in investing and lending, institutional client services were up 17% and the asset management business had $14 billion of net inflows. In addition, revenue increased in three of four business segments, return on equity reached 11.2% and earnings per share ($4.88) handily beat analysts' outlook ($3.82). In our view, all the company's most important capital ratios improved on a quarter-over-quarter basis. Furthermore, the company announced that current CFO Harvey Schwartz and co-Head of the Investment Banking Division David Solomon would take over as new co-COOs upon current COO Gary Cohn's departure. Overall, we like that the company's leadership team remains focused on maintaining its historically strong and liquid balance sheet, while also adding value via share repurchases and dividends. Management and partners own a larger portion of the company than their peers, adding to our confidence in leadership's vested interest in Goldman's success. **Citigroup**'s Q3 results were solid, in our view. Revenue reached $17.76 billion and surpassed market expectations by $48 million (3%), while earnings per share of $1.24 handily outpaced forecasts of $1.15. In addition, management announced it would increase its share repurchase program by up to $1.75 billion and buy back 8% of shares outstanding. We recently met with CEO Mike Corbat and discussed the progress Citigroup has made divesting inferior enterprises and focusing on its best businesses, strengthening the balance sheet, and implementing improvements to its risk systems/behaviors. Mr. Corbat is optimistic that the new Republican administration in the U.S. will reduce financial industry regulations, which would decrease associated costs. We continue to believe that Citigroup remains undervalued relative to its normalized earnings power.

Bottom Performers: Although **News Corp**'s fiscal Q1 revenue was in-line with market projections, earnings fell short of expectations and resulted in earnings per share of $-0.01. Revenues and earnings were also lower than the same quarter last year. Management noted that challenges in its print advertising business and weakness of the pound sterling weighed on results for the period. However, performance in digital businesses helped results, and the company is working to expand its digital offerings. Management pointed out that revenue in its digital real estate segment increased 18% from the prior year and outpaced market estimates. Furthermore, digital revenue grew to 24% of the news and information services segment, a 4% increase from a year ago. While News Corp may face some additional near-term challenges, we think its current share price does not represent the company's true value. **Diageo**'s share price declined from fears that currency valuation disparities prompted by the U.S. presidential election would hinder the company's profitability. Investors were anxious that the U.S. dollar may weaken compared with the pound sterling and euro, as Diageo derives about 50% of its earnings from the U.S. market. Presently, these concerns are unfounded, as the value of the U.S. dollar has increased against both currencies. Furthermore, downward adjustments to the corporate tax rate under the new administration may directly benefit Diageo's U.S. business. In addition, Diageo published its fiscal 2017 financial projections that include organic sales and profit growth along with operating margin expansion. We believe that Diageo is poised to provide meaningful shareholder rewards going forward, and we remain committed to our investment in the company. Considering the pace of **Medtronic**'s

organic revenue growth rate during the past several years, fiscal Q2 organic growth of only 2.3% (+4% total growth) disappointed investors and pressured its share price. Management attributed the slowdown partly to awaiting approval for new product introductions, particularly in the cardiac and vascular group and diabetes. In addition, implantable cardioverter defibrillator (ICD) revenues declined owing to weak replacement sales. However, we think this issue is cyclical, as Medtronic gained U.S. market share for ICDs in the quarter. CEO Omar Ishrak stated confidence that Medtronic would achieve mid-single digit constant currency revenue growth and double-digit constant currency earnings per share growth for the current fiscal year and on a sustained basis into the future.

During the quarter, we initiated positions in **AutoNation**, **Baxter International** and **HCA Holdings**. We eliminated **Applied Materials**, **Principal Financial** and **T. Rowe Price** from the portfolio.

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Contributors and detractors indicated in this commentary are based on the Canadian Dollar.

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