Portfolio Manager Quarterly Insights

Performance review

The economic momentum of the first quarter of 2024 continued into the second. Initially, investors aggressively dialed back expectations for central bank rate cuts but as the quarter progressed the worst of these worries abated, and soft-landing hopes revived. Returns, however, remained concentrated in the largest US companies. In this environment, the strategy performed generally inline with its benchmark, the Russell 3000 Growth Index. Strong stock selection in industrials, health care, and consumer proved most additive. Positions within communication services as well as our modest underweight to the technology sector detracted from relative results.

Top contributors to relative outperformance included Broadcom (information technology) NVIDIA (information technology), and Fair Isaac (information technology). Our avoidance of Accenture (information technology), AbbVie (health care) and Caterpillar (industrials) also proved favorable. Our underweight to strong performing Apple (information technology) and overweights to Salesforce (information technology), Dexcom (health care), and Lululemon (consumer discretionary) were among the top relative detractors.

Quarterly market highlights

U.S. stocks delivered gains in the second quarter. The quarter began on a weaker note, as stocks declined in April. Concerns about rising inflation and potential hawkish sentiment from the Federal Reserve weighed on investor sentiment and index returns. The S&P 500 Index posted its first monthly decline since October 2023. All S&P 500 sectors declined, with the exception of utilities. From a sector perspective in April, growth-oriented areas underperformed, while cyclical sectors such as energy and materials outperformed.

U.S. markets rebounded in May, with the S&P 500 Index posting its strongest monthly performance since February. Renewed investor optimism about the economy supported most equities. Expectations for declining interest rates, combined with the continued strength of artificial intelligence-related themes within technology and utilities, boosted the Magnificent Seven mega-cap stocks relative to the rest of the S&P 500. Growth continued to lead value. With the exception of energy, all S&P 500 sectors posted gains. On the macroeconomic front, the U.S. economy remained in solid shape, but data released in May pointed to some signs of moderation.

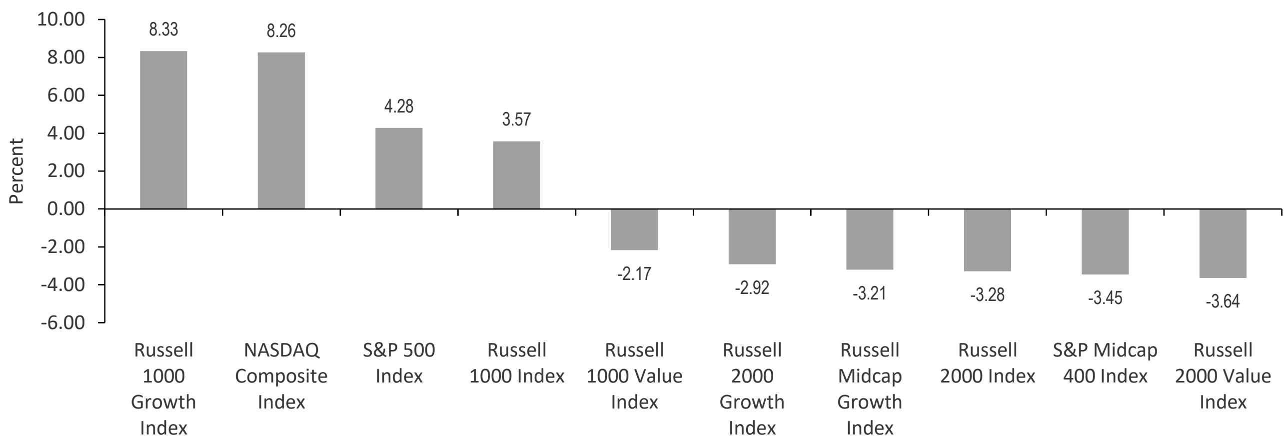
June also brought gains for U.S. equities. Risk assets continued to be in favor for the month. Better-than-expected data on inflation and the narrative of a soft landing for the economy helped drive investor optimism. Growth led value as both the Nasdaq and Russell 1000 Growth Indexes outperformed their value-oriented counterparts. This bias toward growth was also evident in the strong performance of the information technology, consumer discretionary, and communication services sectors. The utilities, materials, and energy sectors declined for the month.

On the macroeconomic front, inflation data came in lower than expected, with headline CPI for May coming in below forecasts at 3.3% year over year. After a string of hotter U.S. inflation readings for the first three months of the year, this reading was welcome news for markets. Also, the Federal Reserve at its June meeting held rates steady at 5.25% – 5.5%. The Fed's updated set of estimates pointed to one rate cut in 2024, down from the three cuts forecast at its March meeting.

For the quarter, U.S. equities, as measured by the S&P 500 Index, returned 4.28%.

S&P 500 Index sectors that gained were information technology (13.80%), communication services (9.37%), utilities (4.69%), consumer staples (1.35%), and consumer discretionary (0.66%). Sectors posting losses were health care (–0.96%), real estate (–1.90%), financials (2.03%), Energy(–2.45%), industrials (–2.89%), and materials (–4.50%).

Major U.S. equity index returns for Q2 2024



Returns are in U.S. Dollars. Indexes are unmanaged and do not incur expenses. You cannot invest directly in an index. Past performance is not a guarantee of future results.

Strategy

The aim of the mandate is to minimize the impact of economic fluctuations by investing in secular growers with defensible moats and high, sustainable returns. We will continue to focus our investments in companies with 1.) high and long-duration growth, 2.) high and/or improving capital returns, and 3.) an ownership culture. The growth profiles for many of the companies held in the strategy are supported by long-tailed themes, and we explicitly take prior-cycle downside capture into account within our risk framework. Our desire to own high-quality businesses with a narrow range of outcomes has benefited relative returns. This framework has served the strategy well in the past, and we expect it to continue to do so into the future.

As far as what has occurred year to date, technology continues to lead the way though there has been a notable increase in breadth within the market (our expectation is this continues). What should continue to widen leadership going forward will be pockets or areas of earnings growth outside of mega cap technology names – including but not limited to Trane Technologies (industrials), Chipotle (consumer discretionary) and Boston Scientific (health care).

Our thematic approach remains a critical part of our investment process and a distinct feature of the strategy. Our newest theme, added this past month, is subscriptions and consumables. This theme reflects the priority we place on revenue visibility, and our focus on recurring revenue. Two key strategies for generating recurring revenue are subscriptions — ongoing payments from customers, and consumables — products or services that must constantly be repurchased. Businesses in our portfolio that benefit from subscription revenue include streaming services such as Apple and Spotify, and technology subscriptions from firms such as Microsoft and Salesforce. For consumables, we own companies that sell mission-critical surgical instruments, as well as those that offer prescriptions, test kits, and other disposable supplies. A prime example in the portfolio today is Intuitive Surgical – a biotechnology company that develops and manufactures robotic-surgical systems and instruments.

Changes in the relative positioning of the strategy are primarily a result of our fundamental, bottom-up process of evaluating the opportunity and risk of individual stocks. As always, sector active weights remain reasonably tight in order to reduce unintended factor risks and accentuate stock-specific risk. Currently, we remain within +/-5% of all sectors. Our largest absolute position is information technology (we are generally in line with the Russell 1000 Growth Index here), followed by consumer discretionary. Consumer staples is our largest underweight at this time. We have no exposure to the energy or utilities sectors. For the strategy's geographic exposure, +95%, remains in U.S.-listed securities.

New positions during the quarter were Regeneron Pharmaceuticals (health care), Vertiv (industrials) and Copart (industrials). Top eliminated positions included Palo Alto (information technology) and Adobe (information technology).

actual results to differ materially from those expressed herein. These risks, uncertainties and assumptions include, without limitation, general economic, political and market factors, interest and foreign exchange rates, the volatility of equity and capital markets, business competition, technological change, changes in government regulations, changes in tax laws, unexpected judicial or regulatory proceedings and catastrophic events. Please consider these and other factors carefully and not place undue reliance on forward-looking information. The forward-looking information contained herein is current only as of 12/31/2023. There should be no expectation that such information will in all circumstances be updated, supplemented or revised whether as a result of new information, changing circumstances, future events or otherwise.

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Data as of 06/30/2024.