Discovery Global Equity Feeder Fund

Market background

Global equities had another strong quarter, with several markets reaching all-time highs. This was driven by growing hopes for a soft economic landing, along with ongoing optimism around artificial intelligence (AI). The S&P 500 posted consecutive double-digit gains for the first time in over a decade, while in Japan, the Nikkei index saw its strongest performance since the global financial crisis, propelling it above its previous record high from 1989.

Economic data was broadly positive, causing expectations of a recession in the US to fall. However, inflation was slightly higher than expected in both January and February, which prompted the Federal Reserve to caution against cutting rates. As it stands, the market is currently pricing in three 25 basis point cuts in 2024, down from six at the turn of the year.

At the sector level, IT and communication services led the way, with energy and financials not far behind. Sectors hampered by the prospects of rates being higher for longer – namely real estate and utilities – were notable laggards.

Performance review

For the quarter, the Fund delivered a positive absolute return and outperformed the benchmark.

Stock selection in the consumer discretionary and IT sectors helped drive performance. Tesla continued to underperform following evidence of increasing competition and subsequent demand disappointment. Having no exposure here benefited relative performance. Italian luxury sports car manufacturer Ferrari also added positively to performance, following earnings that beat forecasts in Q4, and a strong 2024 outlook to carry momentum.

In IT, Nvidia rallied following another robust earnings update during the quarter. The share gained further upward momentum heading into its first annual in-person GPU Technology Conference, where it unveiled its latest GPU for AI computing, which it says will provide even better AI training performance and energy efficiency than its popular predecessor. TSMC was another positive contributor as the share outperformed on stronger monthly sales, newsflow suggesting Intel will

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increase outsourcing to them, as well as positive Nvidia data points. Additionally, our large underweight position in Apple helped relative returns. The stock continued to underperform on datapoints reflecting weak iPhone demand, while incremental negative newsflow also confirmed that the DOJ is suing the company on anti-trust grounds. In contrast, owning Meta Platforms was a notable contributor, as the stock surged c.25% in February. The rally came in the wake of the company's financial results and declaration of its first-ever quarterly dividend.

More negatively, stock picking in financials was the biggest detractor from relative performance. AIA Group was a notable drag on performance. Despite posting a decent set of first-half results, sentiment towards Chinese insurers remains weak. Notwithstanding, growth opportunities in the region remain strong and AIA is well-positioned to benefit given its reputation and product range. Valuation is relatively cheap versus history.

In IT, German semiconductor company Infineon was also a laggard on concerns related to Chinese capacity and, by implication, the company's market share in that region. Cloud-based data warehouse platform Snowflake Inc. weighed on performance as persistent industry headwinds caused guidance to miss expectations, further compounded by the unexpected retirement of the CEO. Also in IT, US-based leader in domain name registry and internet services VeriSign bucked the IT sector trend over the quarter as lack of internet domain growth continues to disappoint.

In materials, US company Air Products and Chemicals weighed on returns as delays on a key hydrogen project raised questions over its strategy. We have since exited the position. London headquartered miner Rio Tinto was a laggard as iron ore prices fell sharply on slowing Chinese demand and higher inventories.

Outlook and strategy

Today's market narrative typically suggests the market is pricing in a soft landing. We would suggest a 'no landing' is now closer to being priced in, with the strong outperformance of cyclicals and tech over defensives in the past 18 months. Easing labour market supply pressures have generally allowed this stronger growth not to derail the path to lower inflation and interest rates. However, several normally reliable leading indicators suggest a recession is possible. Some elements of inflation have disappointed recently, and with commodity prices again rising, this may prove to be more than a temporary setback. Among other challenges, the fiscal impulse is turning negative globally, particularly in the US, and is likely to be less supportive of growth in the remainder of 2024.

Surging commodity prices and the price action in gold are also notable this year. We would suggest that, in the short-term, Chinese recovery and goods prices inflecting, and expectations of a new capex cycle are leading to better cyclical tailwinds for industrial commodity stocks. In addition, reasons to own gold today include the likelihood that central banks may well adopt higher inflation targets or that governments are unable to bring down ballooning deficit spending.

There remains a high concentration of market performance from the largest US technology stocks with structural growth drivers. The launch of ChatGPT and newfound public awareness for AI, a transformative technology, seems likely to be at least as important as the arrival of the internet. The danger is the hype cycle is well and truly here and, with the market pricing in most of the potential long-term benefits into current share prices, any disappointment can result in significant de-ratings and falling share prices, despite the long-term growth opportunity. Our investment process is designed to

help us navigate such inflections using our alpha model, with associated fundamental analysis to focus on the latest trends as they emerge.

Outside of the US, recent data in China is encouraging, and incremental policy stimulus continues, but it may not yet be enough to offset persistent drags. The UK, Germany and Japan are trying to emerge from recessions. Russia's relentless bombardment of Ukraine, the threat of escalation in the Middle East, ongoing tensions in the Taiwan Strait and the opportunities as well as threats from de-carbonising the global economy ensure geo-political risks remain high – all of which can feed through to oil price volatility, affecting inflation and rate expectations.

Our sustainability focus as a team leads us to comment on climate change this quarter. Last year was the warmest year since humans evolved. If you include the most recent data and take the 12 months ending 31 January 24, the world has breached 1.5°C above pre-industrial level. There have been a vast number of damaging climate incidents of over $1 billion in the past 12 months, focusing attention on the serious cost pressure of rising insurance premiums.

This complex macro-economic picture is the reason we continue to advocate a balanced approach to portfolios today, through our multi-factor process with a strong emphasis on stock selection and being nimble rather than either stylistically biased or beholden to thematic growth narratives – regionally, sectorally, or otherwise.

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