Robotech strategy
Strong results from some of our smaller companies during this earnings season

- Greater than 85% of the holdings in the strategy beat consensus earnings expectations
- Demand improvement in Japanese Automation and Analog Semiconductor companies
- Strength in the Technology and Medtech parts of the strategy

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What's happening?

Global Equity markets rose in May, with the MSCI All Country World Total Return Index rising 4.1%[1] in USD terms. The Q1 earnings season has now almost been completed and corporate earnings results have so far been encouraging for the Robotech strategy. With only 2 companies held in the strategy remaining to report results, greater than 85% of the holdings in the portfolio have beaten consensus earnings expectations compared to circa 60% for the broader market as measured by the MSCI ACWI Index. The earnings beats have been broad based across the strategy, spanning our Technology, Industrial and Healthcare holdings.

Larger companies have significantly outperformed Small and Mid-Cap companies over the last 2 years and we were pleased to see strong results and share price reactions from some of our smaller companies during this earnings season. In addition, we have continued to see an improvement in demand trends in some of the more industrially focussed or cyclical parts of the portfolio such as Japanese Automation companies and Analog Semiconductor companies which have highlighted that after a more difficult period of softer demand and dealing with inventory digestion - trends are stabilising and prospects for the second half of 2024 are better.

Portfolio positioning and performance

The Robotech strategy outperformed the MSCI All Country World Index during the month, with strength in the Technology and Medtech parts of the portfolio, whilst our industrial exposure lagged a little. Artificial Intelligence as an investment theme continues to dominate the market and we believe that the Robotech strategy is well exposed to benefit from both the enabling technologies of AI and the beneficiaries of AI in areas spanning Industry, Automotive, Healthcare and more. "The next industrial revolution has begun"[2] CEO Jensen Huang said in a statement when Nvidia reported results - "AI will

[1] Source: Bloomberg in USD as of 31/05/2024
[2] Source : NVIDIA Announces Financial Results for First Quarter Fiscal 2025, 22/05/2024

bring significant productivity gains to nearly every industry and help companies be more cost and energy efficient while expanding revenue opportunities.”[2]

We saw strong performance from our semiconductor holdings during the month, with notable performance from Nvidia, but pleasingly also saw better results and datapoints from some semiconductor companies that aren’t linked to Artificial Intelligence Data Center trends. Teradyne, a smaller US semiconductor testing company, rose as it reported results showing that it appears to be benefiting from a recovery in the memory market and the associated demand for testing equipment."

We also saw good performance from Infineon, which like other Analog semiconductor companies, now appears to have better visibility in to the prospects for a demand recovery in the industrial and automotive end markets in the coming quarters following a period of weakness and inventory digestion. Our position in Qualcomm performed well as they appear to be benefitting from a recovery in the Chinese smartphone market as well as success in broadening their offering outside of handsets in to areas like Automotive and IoT.

The market was anticipating strong results from Nvidia during the month given commentary from the hyperscale companies that CAPEX spend was increasing materially in 2024. At the start of the year, CAPEX at the hyperscalers (Microsoft, Amazon, Google, Meta Platforms etc), was anticipated to grow circa 25% in 2024 – as the companies reported Q1 results, they updated spending intentions which point to CAPEX increasing circa 35%, with much of this targeting on AI spend. The results from Nvidia continue to be very strong, with Data center revenues of 22.6bn[3] USD in the quarter, representing an increase of 427% year on year.

Nvidia made some interesting comments on their call which support an improvement in the breadth of demand and customer base. Previously, the large cloud companies had represented >50% of data center revenues at Nvidia and in the last quarter, despite the strong CAPEX spend from these companies, this had fallen to a number in the mid 40’s. This improving customer diversification signals that AI is getting increasing deployed outside of the large tech companies – this reduces the reliance on the spending patterns on these companies but also points to the excitement and opportunities for AI outside of large Tech companies. One interesting new market is the concept of “Sovereign AI” - Sovereign AI refers to a nation's capabilities to produce artificial intelligence using its own infrastructure, data, workforce, and business networks. Nvidia commented that the revenues from Sovereign AI was Zero last year and would be high single digit billions of USD this year, indicating just how quickly new markets and opportunities can open up as AI adoption broadens.

In the healthcare space, small cap spinal robotics company Globus Medical performed very well, reporting results better than analysts expected. Globus Medical had recently acquired competitor Nuvasive and investors were fearful that the combination would be disruptive as the two companies sales teams were combined. The integration and associated disruption appears to be progressing better than management had guided for, causing the share price to rise 20% following results. Elsewhere in the Healthcare space, Dexcom, a US companies focused on continuous glucose monitoring for diabetic patients was weaker. We remain optimistic on the launch of its next generation sensor, “G7” but are conscious of heightened investor expectations at present.

Portfolio activity was quieter during the month with no new positions and no exited positions. Towards the end of the month, we trimmed our holding in Nvidia which has continue to perform exceptionally well this year and has become an increasingly large part of the portfolio.

We trimmed our position in Autodesk at the start of the month as the company delayed the filing of its 10-k[4] as they conducted an internal investigation in to some accounting practices around the treatment of multi-year deals. We had no

[3] Source : NVIDIA Announces Financial Results for First Quarter Fiscal 2025, 22/05/2024

[4] Comprehensive report filed annually by publicly-traded companies about its financial performance and required by the U.S. Securities and Exchange Commission (SEC).

insights in to the potential outcomes from this but decided it prudent to reduce a little of our position due to the uncertainty. At the end of the month, Autodesk put out a press release stating the internal audit committee decided there was no need to make any adjustments to previously announced financial results and at the same time announced quarterly results that were better than expectations. Autodesk's share price rose on the first trading day in June reflecting the better than expected results and the removal of the uncertainty with the investigation.

We added to our position in Daifuku a Japanese manufacturer of material handling solutions for the semiconductor and logistics markets. Daifuku reported a strong set of quarterly results but issued guidance that appears to have confused some investors. The company adjusted the timings of their fiscal year ends, to align the year end of their Japanese business unit with the international business unit – these timing changes meant that headline financial year guidance appeared weaker than analysts were anticipating. When adjusting for the date changes, we are comfortable with the guidance and used the apparent misunderstanding and resultant share price weakness to add to our position in the company.

Outlook

The Q1 earnings season has been encouraging, with strong CAPEX trends coming from the semiconductor industry and signs of an improving Industrial economy. During 2023, it was apparent that inventories had been accumulated following the supply chain challenges and the slower than anticipated recovery in Chinese investment activity meant there was a lengthy process for these excess inventories to be worked through. We saw the March Institute for Supply Management (ISM) Manufacturing PM turn positive for the first time in 16 months indicating expansion in the US after quite a lengthy period of contraction. We have also noted other indications of industrial activity such as Japanese machine tool orders continue to recover in 2024. We would note that these data series often exhibit some volatility and would avoid reading too much in to monthly fluctuations, but it is encouraging to see the improvements and we will be carefully watching this trend over the coming months to determine the shape of the recovery in the manufacturing sector.

Moderating inflation has supported equity markets in 2023 and whilst inflation remains above target in the US and other key markets, CPI in the US is down very notably from the 9.1% seen in June 2022. The prospect for a "soft landing" in the US appears more likely with economic data holding up more resiliently than forecast and the labour market remains relatively strong. There continues to be labour shortages that present a real challenge for businesses. For instance, in the manufacturing space or warehousing space, we see fewer workers – particularly younger demographics – that are willing to do these kinds of jobs, given the nature of the roles and the salary. As a result – facing labour inflation and labour shortages – companies are increasingly incorporating Technology and Automation in their processes to increase efficiency and productivity with their existing/shrinking workforce. In simple terms, we anticipate that labour shortages and wage inflation are substantial drivers of automation demand over the next few years. As labour costs go up, the payback periods become quicker from introducing automation, meaning that more and more areas are considered for automation.

The US is trying to reinvigorate its domestic manufacturing via infrastructure spend and capital expenditures (CAPEX). This is important politically as its US Jobs, important geopolitically as it keeps US intellectual property within the US and important for supply chain as its secure stock within the country after the disruption witnessed post-COVID. Government support has evolved over the past few years, whether it be the Trump Administration – with tariffs in the US China trade war – or more recently with the Biden administration and the CHIPS Act signed to ramp up and 'reshore' US technology such as domestic semiconductor manufacturing. US president Biden also passed the Inflation Reduction Act (IRA) and other acts allocating a lot of spend for more domestic US manufacturing, focussed on key technologies. As a result of tariffs, incentives and reducing the risk of supply chain issues, companies are investing again in the US and this comes with technological sophistication, robotics and automation. Whilst these acts were signed in to law a while ago, (Infrastructure Investment and Jobs Act in November 2021, Chips and Science Act in August 2022, Inflation Reduction Act in August 2022), very little of the allocated budget has been distributed and this support isn't anticipated to peak until 2026.

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