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Robotech strategy

We believe that we are on the cusp of a better period for corporates' decision making

- Global Equity markets fell, likely driven by a risk off environment
- Strong performance of our Healthcare exposure, notably our robotic surgery companies
- Mixed trends in the industrial space with signs that companies are delaying CAPEX

Tom Riley
Portfolio Manager, Robotech strategy

What's happening?

Global Equity markets fell in October, with the MSCI All Country World Total Return Index falling 2.2%¹ in USD terms. Markets were stronger in the first half of the month, before declining in the latter stages of October, likely driven by a risk off environment ahead of what appears to be a very close US election and a more mixed earnings season currently seen in some segments of the market.

The Q3 earnings season has now begun and corporate earnings results for the Robotech strategy have been encouraging, particularly when contrasted with the broader market. At the time of writing (1 November 2024), 27 of the 50 companies held in the strategy have reported earnings results so far and of those that have reported, 80%² of the holdings in the portfolio have beaten earnings expectations compared to 52%² for the broader market as measured by the MSCI ACWI Index. The earnings beats have been fairly broad based across the strategy, notably within our Technology and Healthcare holdings. We have continued to see some mixed trends in the industrial space with signs that companies are delaying CAPEX³ decisions until after they have certainty on the outcome of the US election this year and a better interest rate environment. As such, we believe that we are on the cusp of a better period for decision making for corporates and the prospects of a return of more meaningful CAPEX are becoming more positive.

Portfolio positioning and performance

Whilst the Robotech strategy fell during the month, it outperformed the MSCI All Country World Index during the period. This was driven by strong performance of our Healthcare exposure, notably our robotic surgery companies.

¹ Source: Bloomberg in USD as of 31/10/2024

² Source: Bloomberg as of 01/11/2024

³ CAPEX: Capital Expenditures

During the month, there were reports that GXO logistics had received interest in being acquired and the company was reviewing its options – the share price rose sharply following this. At this stage no formal bid has been communicated. So far in 2024 we have had 5 companies in the strategy be bid for and if a bid for GXO does arrive, this will be the 6th. It is noteworthy the intensity of M&A this year and we believe it highlights the value that strategic buyers are seeing in small and mid-caps at the moment, which have been out of favour for several years. It also suggests to us, that companies see sense in acquiring assets in the robotics and automation space at a time when the automation cycle is cyclically depressed, allowing them to be able to benefit as the cycle improves in future.

Within Artificial Intelligence, we saw continued strong performance from Nvidia and TSMC on strong demand for AI chips. AMD was disappointing where strength in its AI chip segment was offset by weakness in other parts of its portfolio including gaming. Google reported good results showing signs of improving cost control and strong growth in GCP – its cloud computing platform. Amazon also reported strong results, with its retail business showing good levels of profitability as it continues to leverage all the warehouse and automation CAPEX they invested during the pandemic. They also gave some interesting colour on Amazon Web Services, saying “AWS’s AI business is a multi-billion dollar revenue run rate business that continues to grow at a triple-digit year over year percentage and is growing more than three times faster at this stage of its evolution as AWS itself grew.”⁴

Elsewhere in semiconductors, our SPE (Semiconductor Production Equipment) names were weaker with ASML reporting disappointing order intake and weakness in China. We also saw some share price weakness at Teradyne where they reported good results and Q4 guidance, but talked about expectations for a more sluggish start to 2025. Our Analog semiconductors, including ON Semiconductor and Infineon continued to be weaker as Industrial end markets and Automotive demand continue to be soft. The main bright spot in results for Analog semis was Chinese EV demand remained very strong. Over the coming months we will be watching carefully to see if the recently announced stimulus measure in China results in a broadening of demand in the region, as well as whether demand global in industrials picks up following the US election.

We trimmed our position in Simulation Software company Altair following a bid from German Industrial company Siemens. We have owned Altair in the strategy since February 2021 and it has been a strong performer for us during this period. The deal by Siemens to purchase Altair serves to further highlight the importance of simulation software and in particular the growing importance of using this technology in designing semiconductors and electronic systems. In January of this year, another of our simulation software holdings was bid for in a similar deal where Ansys was bid for by Synopsys.

We added to our position in Procept Biorobotics prior to them reporting strong earnings results during the month. Shares in Procept had drifted lower during the course of October after rallying strongly in August following the announcement of the launch of a new surgical robot and we saw an opportunity to add to the position at attractive levels. Procept has recently launched a new generation of their Urology Robot and this month’s earnings report confirmed that demand for the new AI enabled Robotic Surgery tool has been well received.

We trimmed our position in Nvidia, as again it became a very large position in the strategy at greater than 8% of the strategy’s assets. We also reduced our position in NXP Semiconductors, an Analog semiconductor company with a strong footprint in the automotive industry. We have seen weaker trends in automotive demand with profit warnings seen from some of the large European car manufacturers and weaker results from other automotive exposed semiconductor companies. Whilst we believe that NXP have managed their inventories levels better than peers and have some interesting design wins that ramp at customers in the coming years, we thought it prudent to reduce our exposure here.

Outlook

⁴ Source : Amazon Earnings call 31/10/2024

With the first US interest rate cut now done, we are on the pathway to interest rate normalisation after an extended period of high rates to bring down inflation. Whilst the speed of rate cuts and the optimal level will be debated by market participants, we believe that the first Fed cut is an important turning point confirming that inflationary concerns are meaningfully subdued and that the focus is now on ensuring economic growth and stability. Additional rates cuts should continue to free up consumer budgets and make companies more willing to invest. With some greater certainty here, we believe that the environment for CAPEX decision making, particularly post the US election, should improve. We are also watching developments in China with interest as the recent stimulus announcements appear to have been well received by the market. China continues to be an important market for many industrial equipment makers and an improvement in demand, after a prolonged period of weakness, would be welcome.

The Q3 earnings season has so far been encouraging, with strong CAPEX trends coming from the semiconductor industry continuing and some tentative 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. The Institute for Supply Management (ISM) Manufacturing PM has improved a little so far this year, but remains volatile and is lacking a clear trend. The US manufacturing environment has been weak for almost 2 years now, and we anticipate that over the coming quarters we should see some of the impacts of the various Infrastructure ACTs start to be more notable in improving activity levels. 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), relatively little of the allocated budget has been distributed and this support isn't anticipated to peak until 2026.

We have also noted other indications of industrial activity such as Japanese machine tool orders continue to recover in 2024 and they have now turned positive, indicating the machinery cycle is improving in Japan. 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. Chinese activity levels continue to be more muted, and whilst the Chinese market remains significant, we believe that its importance has reduced versus prior cycles due to the reshoring/nearshoring activities that are being seen around the world.

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