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Liontrust SF Managed Growth Fund: Q3 2022 review

Fund managers: Simon Clements, Peter Michaelis and Chris Foster

The Fund returned 3.0% over the quarter, outperforming the IA Flexible Investment sector average of -1.0% (which is the comparator benchmark)*†.

The Fund performed well over the early part of the quarter as the market focus shifted away from macroeconomic drivers and focused back on how individual companies were faring in an increasingly challenging economy. Earning season in July was closely watched, and we were pleased with the way in which the majority of our companies performed. This led to strong Fund performance over the early part of the quarter.

As we moved into September, macroeconomic factors once again began to dominate equity market performance, and relative style performance drove stock markets. Inflation across the world, and particularly in the US, continues to surprise to the upside, and this continued to drive bond yields higher. Yields had moved from around 3% at the beginning of the quarter in the US, to above 3.8% by the quarter end. We were pleased to deliver a strong quarter of performance, in spite the headwind of rising yields.

We do not attempt to forecast or anticipate these moves in macroeconomics. Our focus is resolutely on our 20 sustainability themes that over the long-term should provide strong and stable growth, regardless of the business cycle, and on finding the rare companies that can harness this positive growth and can generate persistently high returns on capital.

Among the top performers was Schwab, a long-term holding under our *Saving for the future* theme as the largest investment platform in the US, offering low-cost products to the mass market. Schwab reported strong Q2 numbers in July, with net income coming in ahead of the average estimates at \$1.8 billion, compared with \$1.4 billion for the first quarter. While Schwab reported lower trading revenue, it more than made up for that with interest generated from holding clients' money – its biggest source of revenue. Net interest revenue rose 31% to \$2.5 billion as trading revenue slid 7% to \$885 million.

PayPal bounced back strongly in the third quarter having seen its share price halve this year as the company has faced pressures in recent quarters from supply-chain disruptions and once-in-a-generation levels of inflation that has hindered e-commerce spending.

PayPal said earlier this year it was pivoting away from a previous strategy of trying to add millions of new users and instead is seeking to encourage existing customers to use its app more frequently. The firm showed progress on that front, reporting in its Q2 earnings that payment transactions per active account climbed 12% to 48.7 in the quarter. In addition, the company boosted its forecast for adjusted earnings per share for the year to a range of \$3.87 to \$3.97, compared with earlier guidance of \$3.81 to \$3.93.

Also among the top performers was Cadence Design Systems, following the release of robust Q2 earnings. Cadence reported revenue of \$858 million, compared to revenue of \$728 million for the same period in 2021, attributing the results to the company's relentless focus on innovation, continued strong execution and emblematic of the megatrends of the long-term strength of semis, systems companies investing more in silicon, and the convergence of system and chip designs.

Cadence continues to broaden its chip design software offering to new customers, as the likes of Amazon, Google and even Tesla invest in chip design teams. Cadence's software offering is essential to this design, and demand from these businesses, as well as more traditional chip manufacturing customers, will drive growth over the

short and long term. This type of innovation delivers better efficiency, which is key to our *Improving the efficiency of energy use* theme.

Masimo – a holding in our *Enabling innovation in healthcare* theme – was another notable contributor over the quarter. Shares in the medical device company jumped at the halfway point of the period following news that an activist investor had taken a large stake in the company. In addition, the company also reported that Q2 core healthcare revenues rose 17% year-on-year to \$357 million. Masimo reported \$565 million in total revenue in the quarter and guided analysts to revenue of between \$1.985 billion and \$2.045 billion for the full year.

On the other side of the ledger, shares in Adobe fell over the quarter after the company announced it had entered into a definitive merger agreement to acquire Figma, a leading web-first collaborative design platform, for approximately \$20 billion in cash and stock. While the market reacted badly to the acquisition price, the combination of Adobe and Figma is said by Adobe to "usher in a new era of collaborative creativity".

Over the period, Bright Horizons Family Solutions reported an 11% increase in Q2 revenue to \$490 million, primarily attributable to enrolment gains at its centres and expanded sales and utilization of back-up care services. However, its shares fell after the company announced that it would be trimming its 2022 guidance due to the ongoing impact of the Covid-19 pandemic.

Bright Horizons provides high-quality educational services, chiefly for 0-4 year olds, that are paid for by the employees but subsidised as part of benefits. This gives the opportunity for full-time working households to continue their careers, while ensuring their children are in the best possible setting. The company's share price was volatile during the pandemic, but we continue to believe that the aim of a better work-life balance and reducing stress for parents is a key long-term part of a more sustainable future when the world is able to look past the pandemic.

In terms of portfolio changes, we initiated a position in US firm Advanced Draining Systems, the leader in the supply of plastic-based storm water drainage in the US. Fitting into our *Delivering a circular economy* theme, ADS's products are made from recycled plastics and replace concrete based drainage systems, which are a poorer quality product as well as being more carbon intensive to manufacture.

We also added Agilent Technologies, a global leader in quality control and testing, ensuring the food we eat, the air we breathe and the water we drink does not contain harmful chemicals and contaminants. Exposed to our *Better monitoring of supply chains and quality control* theme, it is also a leader in the supply of Research & Development tools in the area of increasingly cutting-edge technology related to gene-editing.

Vestas Wind Systems was another new addition over the quarter. This Danish firm, one of the three main players outside of China, is the quality leader in the supply of wind turbines globally, which are key to the transition away from Russian gas and fossil fuel dependency. Vestas' strategy to shift away from *just* turbine manufacturing towards turbine design, optimising connection to grid to yield highest cashflow and profitable service revenue look set to help them grow profitability for the next decade and beyond.

In terms of sells, we exited our position in Prudential, which has been a disappointing investment as its business fundamentals have weakened.

We also sold our position in US integrated waste services firm Waste Connections. The company has performed well, but with the majority of the waste it collects being diverted to landfill, rather than being recycled, we decided to use our position to focus on a better thematic fit for our *Delivering a circular economy* theme, namely Advanced Drainage Systems.

We sold Splunk over the quarter, as we were concerned that its technological lead in unstructured data and big data analysis is coming under pressure from new competitors. Splunk's technology is increasingly adopted as a form of network digital security, and as this moves into the cloud, there is an increasing number of surveillance software competitors. We believe this may pressure pricing and returns for the business going forward.

**Discrete years' performance*, to previous quarter-end
Past performance does not predict future returns**

	Sep-22	Sep-21	Sep-20	Sep-19	Sep-18
Liontrust Sustainable Future Managed Growth 2 Acc	-18.5%	22.7%	27.0%	9.5%	16.3%
IA Flexible Investment	-9.2%	18.3%	0.9%	3.2%	5.4%
Quartile	4	2	1	1	1

*Source: FE Analytics, as at 30.09.22, primary share class, total return, net of fees and income reinvested.

For a comprehensive list of common financial words and terms, see our glossary at:

<https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms>

Key Risks and disclaimer

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