LOMBARD ODIER
INVESTMENT MANAGERS

LO Funds
Global FinTech
Newsletter

Thematic Equities • Equities

30 September 2024

LO FUNDS–GLOBAL FINTECH

PERFORMANCE COMMENTS

September was another strong month for the Fund, which was up in both absolute and relative terms. There were two main factors influencing performance positively. First, and most importantly, was the shift away from mega-caps towards large and mid-cap companies. We have no exposure to the mega-caps given our purity constraints, so this factor is important to the strategy. As the market continues to broaden, attractively valued, quality large- and mid-cap companies are being picked up, which we benefit from within our FinTech coverage. The second driver was the broad-based stimulus measures announced by the Chinese government. Policy rate cuts, lower bank reserve requirements, cheap funding helping firms to buy back their own shares and further expansionary measures resulted in Chinese indices bouncing from multi-year lows to year-to-date highs in the course of a week. The Fund is truly global and, through its 10% allocation to China, benefited significantly from the rally. Among the top ten contributors in September, six were Chinese holdings.

In September, two of our holdings held investor days: Global Payments and Intuit. Despite a clear strategic focus, organisational streamlining, a solid three-year outlook of low-teens earnings per share growth and buying back 30% of its shares in the next three years, Global Payments still traded down as investors took a wait-and-see approach on execution. The company's preliminary 2025 outlook for 10% earnings growth was also slightly below market expectations and the share price fell 7% during the month. To us, the current valuation of 8x FY2 earnings, with no growth or execution whatsoever priced in, is a good starting point for outperformance. Intuit's investor day also showcased a long runway for structural growth driven by its broad-based AI platform and a shift to higher-value product offerings. The stock also traded down slightly during the month, given high investor expectations. In terms of results, Accenture surprised positively and reassured investors with a solid outlook driven by large bookings, in part due to strong AI demand from clients.

During the month, the sector allocation effect was negative but more than offset by positive stock selection. Sector allocation was negative as Financials lagged the overall market while Consumer Discretionary outperformed on hopes of a cyclical recovery driven by central bank rate cuts. Stock selection was very positive in Financials, primarily due to our Chinese holdings. Established FinTech performed best (+3.6%), followed by Upcoming FinTech (+2.2%) and Enabling Technology (+2.0%) in line with the market. The stocks that contributed most to the Fund's relative performance in September were Hong Kong Exchanges (+38.8%), Lufax (+53.7%) and Yusys Technologies (+49.0%). The detractors for the month were Endava (-20.1%), Global Payments (-7.6%) and Verint (-19.7%). The portfolio's current positioning comprises 45% Established FinTech, 37% Enabling Technology and 18% Upcoming FinTech.

MARKET REVIEW

Bond yields continued to trend lower, with central banks cutting rates globally. Yield curves have nevertheless turned slightly positive now on economic recovery hopes, with the US 10-year ending September at about 3.8% and European rates declining a bit more. The Bloomberg Commodity index rose 4.4% during the month, driven by metals and agriculture, while energy declined. The VIX increased from 15 at the end of August to close to 17.

THEMATIC INSIGHTS

FinTech stocks provide natural hedges against rising inflation and a potential economic slowdown. Physical payment companies (payment processors and merchant acquirers that focus on physical stores as opposed to e-commerce) tend to benefit most from this natural hedge. Fundamentals for payment companies have been strong and the outlook

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remains positive. We do see a slowdown on the software side, which is why we have repositioned the portfolio away from the more expensive software names and towards the cheaper, quality payment companies. We also believe high-quality companies will benefit more than their loss-making hyper-growth peers, as long as access to credit is declining and borrowing costs are rising. This is because quality companies can fund growth from their profits and cash reserves. Management can also make a substantial difference, and most high-quality companies have a team that has gone through several economic cycles and can navigate most market conditions.

C-suite level discussions are focused on digital strategy, which has moved from “nice to have” to “must have” to remain competitive and meet the needs of all stakeholders. Shareholder rewards have gone to digital leaders: clients expect services to be able to continue in the event of another lockdown, and staff expect the right tools to perform their jobs in a work-from-home environment.

PORTFOLIO ACTIVITY

We made no noteworthy changes during September. We only traded to accommodate fund flows.

OUTLOOK

The FinTech sector benefits from strong secular growth trends, such as the move away from physical cash, the digitalisation of financial services and the rising role of cybersecurity. The pandemic accelerated these trends through both push and pull forces – businesses have started to invest more in digital infrastructure so they can remain open during any future lockdowns, and consumers are demanding digital services for reasons of health, user experience or convenience.

Our investment process aims to select the highest-quality companies that can benefit from these trends to build a well-diversified portfolio. We believe the most important factors to watch are company-specific fundamentals such as revenue and earnings growth, return on equity (ROE), cash flow return on investment (CFROI) and balance sheet conditions. We also monitor macroeconomic factors such as interest rates, inflation and growth. We diversify between Financial and Technology companies, aiming to create a stable, disciplined portfolio that can weather a multitude of market conditions. Within our FinTech mandate, our portfolio management style is best described as “quality growth at a reasonable price”.

Certain segments of the FinTech market are extremely interesting from a valuation perspective. Payments, for example, is a segment that has been sold by many generalists and is only held by a handful of specialist long-only funds. Despite the extremely good fundamentals, active managers and passives all accumulate positions around the Magnificent 7 stocks. As a result, the quality growth at a reasonable price strategy proliferates, particularly in the payments sub-sector where growth (both earnings and topline) is higher than the market; quality is extremely high (this segment produces the top 10% of CFROIs globally) and valuations show a discount to the market.

Sincerely,

LO Funds–FinTech investment team

PERFORMANCE

30.09.2024	INCEPTION	AUM	MONTH-TO-DATE	YEAR-TO-DATE	INCEPTION-TO-DATE	2023	2022	2021
LO Funds – Global FinTech PA	6 April 2020	USD 78 mn	2.59%	6.69%	41.00%	15.29%	-28.90%	9.97%
LO Funds – Global FinTech NA			2.67%	7.37%	46.47%	16.27%	-28.29%	10.91%
Benchmark [3]			2.32%	18.66%	104.48%	22.20%	-18.36%	18.54%

Past performance is not a guarantee of future results. Performance is presented net of fees.
[1] Dividend accumulated private client share, net performance in USD.
[2] Dividend accumulated institutional client share, net performance in USD.
[3] MSCI All Countries World USD ND

RISK AND REWARD PROFILE

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Lower Risk Higher Risk

The following risks may be materially relevant but may not always be adequately captured by the synthetic risk indicator and may cause additional loss:

Concentration risk: To the extent that the fund's investments are concentrated in a particular country, market, industry, sector or asset class, the fund may be susceptible to loss due to adverse occurrences affecting that country, market, industry, sector or asset class.

Emerging market risk: Significant investment in emerging markets may expose to difficulties when buying and selling investments. Emerging markets are also more likely to experience political uncertainty and investments held in these countries may not have the same protection as those held in more developed countries.

Active management risk: Active management relies on anticipating various market developments and/or security selection. There is a risk at any given time that the fund may not be invested in the highest-performing markets or securities. The fund's net asset value may also decline.

Before taking any investment decision, please read the latest version of the prospectus, the articles of incorporation, the Key Information Documents (KIDs) and the latest annual report and semi-annual report. Please pay attention to the Appendix B "Risk Factors Annex" of the prospectus.

Incorporation of extra-financial risks into the investment decision process may result in underweighting of profitable investments from the sub-fund’s investment universe and may also lead the management of the sub-fund to underweight investments that will continue to perform. Sustainability risks may lead to a significant deterioration in the financial profile, profitability or reputation of an underlying investment and may therefore have a significant impact on its market price or liquidity.

The Fund has been classified as a financial product subject to Article 8 of Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial sector (the “SFDR”). The Fund promotes, among other characteristics, environmental or social characteristics, or a combination of those characteristics, provided that the companies in which the investments are made follow good governance practices.

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Netherlands. Representative: Lombard Odier Funds (Europe) S.A. – Dutch Branch, Parklaan 26, 3016 BC Rotterdam, Supervisory Authority: Autoriteit Financiële Markten (AFM).
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