LOMBARD ODIER
INVESTMENT MANAGERS

LO Funds
Global FinTech
Newsletter

Thematic Equities • Equities

31 August 2024

LO FUNDS–GLOBAL FINTECH

PERFORMANCE COMMENTS

August was another strong month for the Fund, which was up in both absolute and relative terms. There are two main factors influencing performance positively. The first and most important one is the move away from mega caps to large and mid-cap companies. As we have no exposure to the mega caps, this shift is beneficial to the strategy. As the market broadens, attractively valued, quality large- and mid-cap companies are being picked up, including those within our FinTech coverage. The second driver is a potential Trump victory. With Trump likely to (over)stimulate the economy, this would give an additional boost to macro-sensitive companies (in our universe, that would be the payment companies). In addition, the government would be likely to take a tougher stance on Wall Street and the big banks, which again bodes well for our strategy from a relative perspective versus the financials industry, given the payment companies would not be subject to additional rules and capital requirements. The Trump victory factor played a bigger role in July's outperformance, as Harris' chances of winning the presidential elections in November improved substantially in August. For the FinTech strategy, the broadening of the market is clearly the most important driver, followed by the potential political tailwinds. Given the strength of this market broadening, it is likely to continue for the rest of this year. If 120% growth for Nvidia (which beat broker expectations) is no longer enough to keep valuations where they are, then we are likely seeing the beginning of a structural shift in market dynamics.

To us, as those of you who have been with us for a while know, only fundamentals and valuations matter. The disconnect has been significant for quite some time, and performance has been challenged, as no one wanted to own the high-quality compounders in the FinTech space. With the Q2 earnings season behind us, fundamentals remain strong. The portfolio saw healthy 6.5% sales growth and 12.5% earnings growth in August. The Chinese holdings disappointed in terms of growth, but US payments and software companies made a robust contribution. Given our global diversification, we can capture these dynamics quickly and reallocate as appropriate. The market is slowly warming to these quality names again, as evidenced by the reallocation of capital.

During the month, both sector allocation and selection contributed positively to overall portfolio performance. Payment names in particular achieved a strong relative performance within Financials. Within IT, the allocation was positive, but the selection within that was negative, mainly driven by the Fund not owning big-tech names. The stocks that contributed most to the Fund's relative performance in August were MercadoLibre (+23.5%), PayPal (+10%) and Global Payments (+9.2%). The detractors for the month were Worldline (-19.3%), Lufax (-20%) and Verint (-12.7%). On Lufax in particular, we received a stock dividend, which softened the absolute negative performance a bit. The portfolio's current positioning comprises 43% Established FinTech, 38% Enabling Technology and 19% Upcoming FinTech.

MARKET REVIEW

While bonds dropped across the world in July, August was a relatively stable month for yields. US 10 years ended at about 3.9%, close to the 4.05% of the previous month. The Bloomberg Commodity index dropped about 2% during the month, driven by Energy, Metals and Agriculture. Gold was the exception, rising 1.5%. The VIX was flat at around 15 for the month, but intra-month volatility was high, with a peak of 38 at the beginning of the month.

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

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opposed to e-commerce) tend to benefit most from this natural hedge. Fundamentals for payment companies have been strong and the outlook 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 August. 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

31.08.2024	INCEPTION	AUM	MONTH-TO-DATE	YEAR-TO-DATE	INCEPTION-TO-DATE	2023	2022	2021
LO Funds – Global FinTech PA	6 April 2020	USD 80 mn	3.36%	3.99%	37.44%	15.29%	-28.90%	9.97%
LO Funds – Global FinTech NA			3.44%	4.58%	42.66%	16.27%	-28.29%	10.91%
Benchmark [3]			2.54%	15.97%	99.84%	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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France. Representative: CACEIS Bank, Rue Gabriel Péri 89-91, 92120 Montrouge, Supervisory Authority: Autorité des marchés financiers (AMF).
Germany. Representative: DekaBank Deutsche Girozentrale, Mainzer Landstraße 16, D-60325 Frankfurt am Main, Supervisory Authority: Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin).
Finland: Finanssivalvonta (Fiva) - Financial Supervisory Authority (FIN-FSA), Snellmaninkatu 6, P.O. Box 103, FI – 00101 Helsinki, Finland; Website: http://www.finanssivalvonta.fi.
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