Wellington Global Health Care Equity Fund

WELLINGTON MANAGEMENT®

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MARKET REVIEW

Global equities rose in September. Stocks fell sharply at the beginning of the month after declines in some mega-cap technology stocks and signs of a cooling US economy rippled across the globe and stoked concerns about the state of the global economy. However, stocks rebounded following a sizable 50 basis points interest-rate cut by the US Federal Reserve and a more forceful Chinese stimulus that bolstered market sentiment. Lower energy prices helped to ease inflationary pressures, and resilient labor markets in the US, Europe, and Japan reinforced the view that the global economy could achieve a soft landing. However, some key economic indicators were mixed across many developed nations, with services PMIs remaining in expansionary territory, while manufacturing PMIs continued to show sustained weakness. In China, markets were encouraged by more substantial policy support from the People's Bank of China, which aimed to revitalize the country's economic recovery. Politics garnered greater attention amid a close US presidential race and leadership changes in other countries; Shigeru Ishiba was elected as Japan's prime minister, Michael Barnier became France's prime minister, and Claudia Sheinbaum was sworn in as Mexico's first female president. Geopolitical risks intensified, with escalating conflict in the Middle East threatening to ignite a broader regional war after Israeli forces killed Hezbollah leader Hassan Nasrallah in Beirut.

The MSCI World Health Care NET returned -3.0% over the period. Within the index, three out of four sectors declined over the period. Biopharma mid cap and biopharma large cap were the bottom performing sectors, while medical technology and health care services were the top performing sectors over the period.

FUND PERFORMANCE AND ATTRIBUTION

- The fund underperformed the index over the month.
- Security selection was a driver of relative underperformance. Weak selection in biopharma large cap and health care services was partially offset by selection in biopharma mid cap. Sector allocation, a result of our bottom-up stock selection process, also detracted from returns. Allocation effect was driven by our overweight to biopharma mid cap and underweight to medical technology, but partially offset by our underweight to biopharma large cap and out of benchmark allocation to biopharma small cap.
- At the issuer level, our top two relative contributors were an out of benchmark allocation to Vaxcyte and an overweight to Argenx, while our top two relative detractors were an overweight to Daiichi Sankyo and an out of benchmark allocation to Acadia Healthcare.
- Shares of Vaxcyte rose during the period due to the release of positive results from a Phase 1/2 study of VAX-31, a vaccine candidate for invasive pneumococcal disease in adults over the age of 50. The study showed that VAX-31 was well tolerated and elicited strong immune responses in all doses studied, leading to plans for Phase 3 trials and expanded research. Shares of Daiichi Sankyo declined during the period due to mixed results from a late-stage trial of non-small cell lung cancer drug datopotamab deruxtecan that is being developed in partnership with AstraZeneca. While the treatment showed improvement over chemotherapy, the data did not meet expectations.

FUND POSITIONING AND OUTLOOK

Biopharma remains a rich environment for innovation. We are excited about developments among GLP-1 and next-generation metabolic medicines, antibody drug conjugates for cancer treatment, and various modalities of genetic medicines. US drug pricing remains a risk to watch, but the first round of Medicare negotiated prices released in August were generally within expectations. Ultimately, we think pricing risks are manageable and continue to find opportunities in companies with rich pipelines and strong track records of productive business development. We are selectively finding attractive valuation opportunities in large cap biopharma. A number of SMID-cap biopharma companies remain well positioned as sources of innovation and potential solutions to pipeline gaps for larger companies, and the subsector may benefit from moderating inflation and lower interest rates. Recent positive clinical readouts across therapeutic areas underscore the quality and breadth of the opportunity set today.

We believe medical technology innovation has never been stronger due to advancements in technology development, engineering capabilities and integrated informatics. Product cycles and biopharma innovation are creating investment opportunities. Areas of most interest to us now include interventional cardiology, robotics, and diagnostics including liquid (blood) biopsy.

Health care services companies remain well-positioned to help solve the societal challenge of rising health care costs and to benefit from the ongoing transition from a fee-for-service to a fee-for-value care system. Higher utilization and rate pressures remain medium-term headwinds for Medicare Advantage but long-term opportunities remain robust. Providers should benefit from higher utilization and behavioral health companies have bipartisan political support in the US. Broadly, we favor companies focused on improving patient outcomes while reining in costs as well as scaled-based players with rising regional market share.

At the end of the period, our largest exposures were biopharma large cap and health care services and we were least exposed to biopharma small cap and biopharma mid cap. From a regional perspective, our largest exposures were North America and Developed Europe & Middle East ex UK and we were least exposed to Emerging Markets. We had no exposure to Developed Asia Pacific ex Japan.

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