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MARKET REVIEW

European equities declined modestly as slowing economic growth in the eurozone heightened concerns about a potential recession. The region's business activity contracted sharply and unexpectedly in September, with the HCOB Flash Eurozone Composite Purchasing Managers' Index (PMI) dropping below 50.0 for the first time in seven months, to 48.9, from 51.0 in August. The manufacturing downturn accelerated, particularly in Germany, while services activity grew at the slowest pace since February after the Olympics-related boost to business faded. Eurozone employment was modestly lower, yet the drop in staffing levels was the largest since December 2020. Eurozone headline inflation slid to 1.8%, from 2.2% in August, below the European Central Bank's (ECB's) target for the first time in three years. Core inflation ebbed marginally to 2.7%. Against a weaker economic backdrop and subsiding inflation, the ECB lowered interest rates by 25 bps, signaling that borrowing costs will likely remain on a "declining path" in the months ahead. The central banks of Switzerland and Sweden also cut interest rates, while the Bank of England left policy unchanged.

Germany ended the month higher, even as leading economic institutes downgraded the country's GDP growth forecast for 2024 to -0.1% and the ZEW Indicator of Economic Sentiment plummeted to a 12-month low. In France, President Emmanuel Macron named the EU's former Brexit negotiator Michel Barnier as the new prime minister in an effort to forge a stable government that could survive a hung parliament.

The MSCI Europe Index Net returned -0.4% for the period. Within the index, four out of 11 sectors declined over the period. Energy and health care were the bottom performing sectors, while materials and real estate were the top performing sectors for the month.

FUND PERFORMANCE AND ATTRIBUTION

- The fund underperformed the index for the period.
- Security selection was the primary driver of relative underperformance. Weak selection in industrials was partially offset by selection in health care and energy. Sector allocation, a result of our bottom-up stock selection process, contributed to returns. Allocation effect was driven by our overweight to health care and overweight to industrials, but partially offset by our lack of exposure to utilities and underweight to financials.
- At the issuer level, our top two relative contributors were not owning Novo Nordisk and AstraZeneca, while our top two relative detractors were an out of benchmark allocation to Elis and an overweight to Rheinmetall.
- Novo Nordisk shares fell in September. The company reported data from a trial of monlunabant for treatment of obesity and metabolic syndrome. The drug achieved meaningful weight loss compared to the placebo, but higher doses did not lead to significant additional weight loss. Participants reported gastrointestinal and neuropsychiatric side effects. Management will reexamine the optimal dosing for efficacy and tolerability. Shares of Elis fell during the period after the company announced an acquisition offer for Vestis, the former uniform rental and workplace supplies company for Aramark. The market reacted poorly as concerns grew with respect to Elis' appetite for future acquisitions and ability to realize positive effects from the deal.

FUND POSITIONING AND OUTLOOK

European markets ended September slightly down, on the back of mixed economic data with progress toward lower inflation while concerns about economic growth in the Europe remained. Overall, the European economy continues to be bifurcated with the periphery outperforming the core and services outperforming manufacturing. European central banks hinted at a more aggressive cutting cycle (or at least did not push back when the market was pricing for this). The ECB cut its deposit facility rate by 25 bps to 3.5% over the month to ease monetary policy restrictions, based on improving inflationary conditions. Those regions and sectors within Europe most geared towards rate cuts started to show some initial signs of economic activity inflecting. Subsequently, cyclical sectors outperformed in September.

Against this backdrop, European materials, real estate and utilities were the best relative performers, while energy and health care were the worst relative performers. We saw a factor reversal with European Value indexes outperforming growth by 180bps this month. We continue to monitor inflation and longer-term yield levels, recession risk, the situation in Ukraine and the Middle East and the evolving European regulatory framework. We assess companies for their long-term fundamental attractiveness based on our investment criteria and incorporating the implications a recession may have on this. Stocks must fulfil our criteria of a superior structural free-cash-flow and earnings growth outlook and a very strong competitive positioning combined with attractive valuation levels. We think that especially as it regards the competitive outlook many so-called growth stocks are currently wrongly priced.

Over the month, we added to existing positions in financials and consumer staples sectors, and trimmed portfolio exposures in industrials. We initiated positions in Ryanair and Bank of Ireland and eliminated positions in Alfa Laval and Hikma Pharmaceutical. We will continue to use volatility to opportunistically adjust our positioning. We think the portfolio is well positioned, despite potential for near term volatility.

At the end of the period, our largest overweight was industrials and we were most underweight to health care and information technology. From a market perspective, our largest overweights were United Kingdom and Belgium. We were most underweight to Switzerland and France.

PAST PERFORMANCE DOES NOT PREDICT FUTURE RETURNS. AN INVESTMENT CAN LOSE VALUE.

Fund performance is based on EUR S Acc share class and are net of fees and expenses. Other share class performance may differ. Index used in the calculation of attribution data: MSCI Europe. Fund performance is net of actual (but not necessarily maximum) withholding and capital gains tax but are not otherwise adjusted for the effects of taxation and assume reinvestment of dividends and capital gains. If an investor's own currency is different from the currency in which the fund is denominated, the investment return may increase or decrease as a result of currency fluctuations. The views expressed are in the context of the investment objective of the Fund only and should not be considered a recommendation or advice.

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