see money differently

Nedgroup Investments Global Equity Fund

Quarter Two, 2023

1. Market Overview and Outlook

Portfolio Manager Commentary

"In a World in which most investors appear interested in figuring out how to make money every second and chasing the idea de jour, there's something validating about the value investing message that it's okay to do nothing and wait for opportunities to present themselves. It's lonely and contrary a lot of the time, but that's what it takes."

Seth Klarman, "The Art of Value Investing" 2013.

There is no doubt that today's idea de jour is Artificial Intelligence (AI), and that excitement about its potential has helped propel the market upwards over the last quarter. The MSCI World Index added 683bps during the quarter, the S&P500 gained 830bps and the NASDAQ 1305bps. Market leadership has been extremely narrow, with the seven largest stocks in the MSCI (all tech, all in the US) delivering 55% of the index return despite being only a 17% weighting. The pockets of outstanding value offered up in the tech sector in 2022 have now all but disappeared.

Artificial Intelligence is an amorphous concept, and ChatGPT and Bard are in some respects just the next step down a road we have been on for some time as computers get ever better at understanding and synthesising knowledge. However, the combination of Natural Language Processing (we can communicate with the computer in plain English or indeed Swahili), massive training data sets (access to the entire corpus of human knowledge available on the internet), and the increasing sophistication of machine learning algorithms (the systems quickly learn from feedback) does feel like a paradigm shift. While we do believe this form of AI will prove useful and often transformative across a wide array of disciplines from developing drugs to producing media to automating administrative functions, we do also believe we are already well into a "hype cycle" and must therefore tread with caution.

The Gartner hype cycle is a graphical presentation that depicts the future expected value of a given innovation in the collective minds of its potential adopting market ("visibility") through time ("maturity"). Each cycle has five phases:

Source: Gartner Research

The dotcom mania is perhaps the best illustration of this concept: the market was initially quick to anticipate the potential impact of the technology but found it very difficult to pick winners or to live with them through the many years of disillusionment until they started to generate sufficiently meaningful adoption and a level of profits that could justify the multiples paid at the "peak of inflated expectations". We expect AI to be similarly transformative, but as with the internet, the timescales, business models and economics remain far from certain. The one thing we do know for sure is that, on average, it is a mistake to pay too much for an uncertain future, or to paraphrase Warren Buffett "you pay a high price for a cheery consensus."

We are strongly of the view that in investing, as in life, patience is a virtue. Sentiment oscillates wildly and typically with far greater amplitude than the underlying intrinsic value of businesses. It is our job to exploit this dynamic, which typically means steering clear of the "idea du jour" and instead paying attention to the darlings of yesterday that have disenfranchised their owners and been unceremoniously dumped into the trough of disillusionment. The sine wave can be surprisingly long, for example, it took almost 13 years for Microsoft's valuation to trough post the dotcom bubble and we are now 10 years into the upcycle in sentiment (and operating performance!) with regard to its prospects in the public cloud. The wave can also be surprisingly short and violent, as we have just experienced with our investment in Meta.

Whilst we are mindful of any potential near term hype cycle, there are companies in the Focus Strategy that should benefit from artificial intelligence as and when it gains further traction. One of the underlying themes in the portfolio has been Public Cloud adoption. Simplistically, it effectively outsources the IT ecosystem/infrastructure to a third party. Alphabet, Microsoft and Amazon are leading players in this market with their respective products Google Cloud Platform (GCP), Azure and Amazon Web Services (AWS). Andy Jassy, Amazon CEO, noted in early July that over 90% of IT infrastructure still remains on-premise and that over time their belief is that the majority of this will move to being delivered by public cloud. To give some context, the global IT spend constitutes a market that is worth $4.5tr in 2023 according to industry analysts Gartner. The three companies mentioned are expected to generate in the region of $185bn in revenues in 2023 and constitute over two thirds of the Public Cloud market. Whilst this is already very significant, it still constitutes only <4% of the total. Global IT spend is clearly not entirely addressable, but it is likely that public cloud penetration can rise materially over the coming decade.

Artificial Intelligence fits into public cloud due to the significant computational power and R&D capability required. It is unlikely that many organisations have the resources and internal skillset to build their own models and systems. This means that they will typically use public cloud vendors to help provide them with this capability that can deliver meaningful process improvements to their businesses. For example, Amazon today already has over 100,000 customers using large language models (a workhorse for AI modelling). So whilst it is still early in the adoption of generative AI tools for instance, one of the most likely places for monetisation of that adoption are the companies listed. The timing and quantum of the opportunity is still highly uncertain, but we believe that we have deployed capital in these companies at a point where the opportunity has effectively been a free option and not contemplated in forecasts. For example, Alphabet trades at a very reasonable 19x 2024 earnings with a significant net cash position. We continue to monitor positions to determine if and when these potential AI opportunities are more reflected in valuations.

Nevertheless, as the crowd is drawn to the AI narrative like a moth to a flame, we believe the best opportunities will be available elsewhere, in the parts of the market that are being ignored. We look no further than our recent investment in out of favour ADP:

Automatic Data Processing (ADP)

ADP is a US-based human capital management and payroll processing company. Simply put, it provides services to help manage human resources and ensure salaries and payroll taxes are paid correctly and on time. It serves over 1m customers in 140 countries and 1 in 6 US workers are paid through their systems. Whilst this sounds relatively simple, a myriad of regulations, benefits and country/state specific factors and tax jurisdictions necessitate a relatively complicated process for employers. The industry therefore has high regulatory compliance factors (e.g., tax collection), and if things go wrong (i.e., payrolls are not getting paid) it can have materially negative implications for a business given payroll will often be the largest expense.

ADP is the largest competitor in the market and services large multinationals down to small and medium sized businesses. Its sweet spot is with small to medium sized employers where the ‘do it for me’ proposition works best and where they have high market shares. These clients typically do not have the size or resources to insource payroll or indeed HR and will often look to ADP to provide a wide array of services. Importantly, the company has been forward thinking in rearchitecting their product offering to be cloud-based, which has been a differentiating feature versus other technology incumbents over the years.

From a financial perspective, the company has enviable characteristics and grew at 7% over the decade to COVID-19, expecting similar levels of growth going forward. It exhibits very limited cyclicality and during the financial crisis only saw EPS marginally contract in its trough year. Capital allocation is also strong, notably increasing its dividend for 48 years consecutively. Finally, the company also has a new CEO in Maria Black, whom is only the 7th CEO of the company since its founding in 1949. ADP is a relatively capital light business, but they are also taking quantifiable actions on ESG matters. For example, the company has a target to reduce Scope 1 & 2 emissions by 25% by 2025 and 30% by 2030, respectively. Their longer-term commitment is to have net-zero GHG emissions by 2050. Importantly, ADP has also gone further than peers by introducing an environment footprint objective in executive compensation. Overall, the company remains focused on all areas of ESG and highly engaged with their shareholder base.

The opportunity to invest in ADP has not come through any concern with its business quality, competitive position, or operational execution. It is driven by the macroeconomic environment. The company is tied to employment trends, and a potential US recession has seen concerns that the unemployment rate will rise and impact the business. This has led to the valuation de-rating to 7-year ex-COVID lows as the market anticipates a softer near-term environment. To note, of 23 sell side analysts covering the company, only 3 (<15%) have it Buy-rated. It is rare to get an opportunity to invest in a business of such quality when it is that out of favour. At Veritas, we take the long-term view and believe that even factoring in near term softness, the company offers attractive absolute double digit returns for the patient investor. Given the nature of the business as an asset of enduring high quality, we believe this represents an attractive risk/reward.

2. Fund performance contributors & detractors for past quarter

Top 5 contributors and bottom 5 detractors

	Portfolio			Index			Attribution
Holding	Average Weight	Total Return	Absolute Contribution	Average Weight	Total Return	Absolute Contribution	Total Effect
Top 5 relative stock contributors							
Amazon.com	4.5	26.2	1.1	1.9	26.2	0.5	0.5
Alphabet	6.4	15.3	0.9	2.4	15.4	0.4	0.3
Moody`s Corp	3.1	14.0	0.5	0.1	13.8	0.0	0.3
Fiserv	4.4	11.9	0.5	0.1	11.6	0.0	0.2
Equifax Inc.	0.8	19.4	0.2	0.0	16.2	0.0	0.2
Bottom 5 relative stock contributors							
Catalent	1.8	-34.0	-0.9	0.0	-34.0	-0.0	-1.1
Bio-Rad Laboratories	2.7	-20.9	-0.7	0.0	-20.9	-0.0	-0.9
Illumina	1.8	-19.4	-0.4	0.1	-19.4	-0.0	-0.5
Thermo Fisher Scientific	3.1	-9.4	-0.3	0.4	-9.4	-0.0	-0.5
Diageo	2.7	-5.0	-0.2	0.2	-3.9	-0.0	-0.4

Source: Veritas Asset Management

Portfolio Attribution Commentary

The portfolio underperformed the MSCI over the three-month period largely due to stock selection of Health Care and US stocks which detracted.

Contributors
Despite **Amazon** reporting that growth had slowed in its Amazon Web Services (AWS) cloud division, raising investor fears about a main driver of the tech giant's profits, the shares performed well over the quarter. During the March quarter, revenue at AWS, which accounts for the bulk of Amazon profits, grew 16 per cent to $21.4bn, ahead of forecasts, but the rate of growth has slowed (it was 37% a year earlier). Overall, Amazon revenue rose 9 per cent to $127 bn, also better than expected, while revenue from the group's online stores was flat at $51.1bn. Amazon said AWS "customers of all sizes in all industries" were trying to save on costs. Customers are continuing to evaluate ways to optimise their cloud spending in response to tough economic conditions. April revenue growth rates are about 500 basis points lower than what was witnessed in Q1. The warning underscores the challenge that major cloud providers, including Amazon, are facing as increasingly cost-conscious customers and a softening economy combine to put pressure on what has been a significant growth market. The long-term outlook for cloud revenue however, remains bullish. Over 90 per cent of global IT spend is still on premise, and much of that is going to move to the cloud. Longer term, Amazon said it would be in a good position to capitalise on the latest trends in "large language models" - the technology behind ChatGPT, the popular chatbot tool from OpenAI - and generative artificial intelligence. Amazon has made investments in custom-made chips that can handle the necessary computer processing, as well as the potential for Alexa, its voice assistant. The company starts from a positive point with Alexa because they have a couple hundred million endpoints being used across entertainment, shopping, smart home and information, and a lot of involvement from third-party ecosystem partners. Like its Big Tech peers, Amazon has been focused on cutting headcount and costs. The company began trimming its spending last year by cancelling some of its warehouse expansion plans and reducing headcount in its facilities through attrition. It accelerated cost-saving measures over the past couple of quarters by cutting 27,000 corporate roles (approx. 9% of its corporate workforce) in different units, including devices, advertising, AWS and Twitch, the popular live streaming platform it acquired in 2014. It has also axed several businesses that weren't bringing in enough cash, such as its healthcare startup Amazon Care, subsidiary fabric.com, and the video calling device Amazon Glow. The company has also said it would shut down its health-focused Halo devices and related membership service on August 1 and it will shut down some of its Amazon Fresh and Go convivence stores and pause expansions as it attempts to find the right formula for its grocery business. Amazon has also paused construction on the second phase of its headquarters in northern Virginia. At a time of cost cutting, some inflationary pressures are easing, including lower shipping rates and electricity costs. This is welcomed as Amazon continues to expand one-day shipping options and has dealt with increased transportation and fuel costs. Amazon spent $19.9 billion on shipping in Q1, up 2%. Whilst most think of Amazon as retail first, along with AWS, advertising is one of Amazon's higher-margin businesses. Advertising brought in $9.5 billion in revenue in the quarter, up 21% over a year ago. Overall, Amazon recorded $3.2bn in net income for the March quarter, a huge reversal from its $3.8bn net loss a year ago. Although the loss was mainly driven by a drop in value of its investment in the electric vehicle company Rivian Automotive. Operating income margins rose to 3.7 per cent, up from 3.2 per cent a year ago and above forecasts for 2.7 per cent. For the current quarter, Amazon said it expects revenue between $127bn and $133bn, in-line with analysts' mid-estimates of $130bn. Amazon is still making some investments and will continue to expand in a number of areas that are further from its core business, such as healthcare, generative AI and Kuiper, a satellite broadband project the company unveiled in 2020.

Alphabet turned in a decent first quarter. The shares were boosted by a good showing from its advertising segments amidst an industry-wide slowdown in digital ad spending. Simultaneously, the company announced a massive $70 billion share buyback program. The company reported first-quarter revenue of $69.8bn, up 3% year-over-year. Its cloud business reported a profit for the first time since its launch, taking in $191m. Whilst, the Google Cloud business is a distant third behind AWS and Microsoft Cloud, it has been growing in momentum. After years of financial growth and booming popularity, Alphabet, Google's parent company, has in recent months faced mounting questions about its future. It has been under the gun to deliver artificial intelligence technology, its sales growth has decelerated, and it is laying off 12,000 employees to cut costs. Against this backdrop, the results were better than expected. Google still faces significant challenges. Its video platform, YouTube, continues to be crimped by the ad slump and rival Microsoft has gained buzz and users after incorporating an AI chatbot into its search engine, Bing. But the quarter results highlighted Google's enviable advantage as a gateway to the web for billions of people around the world, a position that cannot be dislodged quickly or easily. In particular, Google's search engine, the core of the world's largest digital advertising machine, remained strong. Revenue from the search engine rose almost 2 percent to $40.4 billion. The company said travel firms and retailers had spent more to reach customers on the search platform. That said, Alphabet is taking the threat seriously. Artificial intelligence was a big focus on the earnings call, being mentioned 60 times! There have been rumours that electronics multinational Samsung might switch from Google to Microsoft Bing as the default search engine for its Android phones. Microsoft is bringing a more conversational experience to the new Bing search engine. This development led Google to gather resources for a new or upgraded search engine, an undertaking known at the company as "Project Magi" - offering users a more personalised experience. Samsung's contract with Google is nearing its end, with Google reportedly paying Samsung more than $3 billion annually to remain as its search provider. While this is not as much as the company pays Samsung competitor Apple, it could still affect Google's $162 billion search revenues. Alphabet suffered a dramatic drop in its stock price following The New York Times' story on the development. There are a number of counterarguments to consider. The connective tissue built up between Samsung and Alphabet could not easily be replaced. If Google is able to offer up a strong contender, the relationship is likely to hold. While Google is advanced in AI research and development, the tech giant is missing much of the conversational aspect of search that ChatGPT brought to the forefront. Project Magi will help Google pull together all its AI products and features and provide a competing product to effectively challenge ChatGPT. Microsoft is going on the offense on AI, and it makes Google look like they are dragging their feet, when in reality Google is taking a more cautious approach because so much can go wrong with AI. Google has done a very good job in giving search results. They have to build that into their AI. If they can give results which are correct, which are consistent and which can 'read' customer's minds better, they will be well positioned. Alphabet has consolidated its main AI teams into one unit, Google DeepMind, to make quicker progress in the field. The move combined the London-based AI lab DeepMind with Google Brain, part of the company's research division. YouTube ad revenue was down 2.6% in the quarter, but ahead of expectations. The company is continuing to invest in short-form video to compete with TikTok, and YouTube Shorts now has 50bn daily views, up from 30bn this time last year.

"Today, risk no longer escalates sequentially; it multiplies exponentially, forcing leaders to confront risk in new ways."
- Rob Fauber, President and Chief Executive Officer, Moody's

Moody's has two main businesses. Moody's Analytics (MA) recorded its 61st consecutive quarter of growth amid heightened customer demand for integrated solutions, and contributed approximately 50% to overall Moody's revenue, up from 46% in the prior year period. There was strong demand for Know Your Customer and Insurance solutions, as well as ratings data feeds. Foreign exchange rates negatively impacted MA revenue by 3%. Recurring revenue grew 6%, and represented 94% of the total, as MA continues to prioritize renewable products through its ongoing strategic shift to subscription-based solutions. Consistent mid-90s customer retention rates demonstrate the value proposition of MA's mission-critical solutions in an evolving and complex risk environment.

Moody's Investors Service (MIS) saw revenue decline 11% compared to the prior year period. Ongoing uncertainty around inflation, interest rates, and recessionary concerns broadly impacted credit markets, constraining issuance in most sectors. Activity was skewed towards higher-rated issuers, particularly in the investment grade corporate and infrastructure finance sectors, with issuance declines across several asset classes, specifically in structured and leveraged finance. The company expects revenue and earnings to increase in the mid-to-high-single-digit percent range in the year ahead and raised EPS outlook.

Fiserv reported strong Q1 results and raised the bottom end of its 2023 financial guidance. The company expects organic revenue growth in the range of 8%-9%, up from the previous guidance of 7%-9%. Fiserv also boosted its EPS outlook. Results included elevated contributions from card processing, noncard payments, and digital banking solutions. Growth was also strong in all three of its international regions and in merchant acceptance. Accelerating its investment over the last three years, both organically and via M&A, has extended its leadership position among fintech's. This counters the narrative over the last few years that many start-ups in the payments and fintech space would disrupt and potentially replace the legacy companies. As if to highlight its dominance, Fiserv completed the transfer of its stock exchange listing from the NASDAQ to the New York Stock Exchange. The power of its business model is in the virtuous cycle of generating revenue growth across a scaled business, leading to greater operating margins. That profit produces significant cash to reinvest in the business for faster organic growth and value-accretive acquisitions while the remainder is returned to shareholders through share repurchase. For small and medium-sized businesses, Fiserv developed a cloud-based Software as a Service (SaaS) operating system for their payment needs called Clover. Now they are allowing these businesses to easily accept multiple payment types and are seamlessly integrating software services to address broader business needs. For large enterprise businesses, the company developed an integrated omnichannel system called Carat to manage payment needs across in-store and online sales channels and are now adding SaaS-based solutions that improve its client's efficiency and enhance their customers' experiences. For debit and credit issues, Fiserv have already built the most comprehensive suite of solutions and continue to innovate. CardHub was built off of the tools acquired with Ondot and now offers a comprehensive set of modern digital cardholder experiences. More than 1,000 financial institutions are now using CardHub, which can be fully integrated into their mobile banking app, allowing these issuers to offer their customers a unified digital card experience that only a few of the largest financial institutions can provide today. SpendTrack does for a bank's small and medium-sized business clients what CardHub does for its retail customers. This differentiated mobile-first platform covers card management and AI-enabled expense management with workflows specific to business needs. Built from its SpendLabs acquisition, SpendTrack has helped Fiserv win more credit, debit, and network business with banks and issuers that cater to SMBs. For small and medium-sized banks, Fiserv provides a full suite of the digital banking tools that help them compete with the largest banks from mobile apps to spend management to Zelle B2B payments. With the launch of FedNow, Fiserv will help them participate in the new wave of real-time payments, optimized on their NOW network that connects banks to each other, to all payment rails, and to essential applications. NOW is a network of networks connecting financial institutions, billers, consumers, and businesses to real-time money and data movement across all rails, including card, ACH, Zelle, FedNow, and the clearinghouse.

Equifax is the most recent investment and whilst extremely good quality, is a more cyclical business. Equifax is one of the big three US credit rating agencies (CRAs) operating in a competitive oligopoly with significant entry barriers, namely data assets that are very hard to replicate. These barriers are compounded by heavy industry regulation, sensitivity of the data and decades spent cultivating relationships with many thousands of data furnishers. The value-to-cost ratio of Equifax products is typically very favourable for clients. This is a particularly attractive feature through the cycle of US mortgage volumes since the value-to-cost ratio is better here than in any other vertical. You are unlikely to quibble over a few hundred dollars when granting a 25-year mortgage with the risks that involves. But mortgages contribute cyclicity and means there is a wide range of plausible mid-term outcome. US mortgage is 25% of revenues and around a third of profits. It fair therefore that the business is heavily levered to the US mortgage cycle and interest rates. The legacy credit bureau business is mature and lacks pricing power, so each of the big three has spent the last decade diversifying into new adjacencies, making the businesses less homogeneous than was historically the case and resulting in frequent, significant M&A. Equifax has the best adjacency of all, having opened a significant lead in an employment/salary verification business for lenders (EWS); this relatively new business has enjoyed strong pricing power and now accounts for almost two-thirds of the stock's value. The investment case for Equifax boils down to two things. Will US mortgage volumes return to normal levels after troughing in 2023 and can the Workforce Solutions business sustain monopoly-like economics as competition increases and suppliers seek a bigger cut? Equifax US mortgage revenue was down 41% in the quarter but outperformed the overall market by 27 percentage points with estimated US mortgage originations down 68%. The global non-mortgage businesses, which represented about 84% of total revenue in the company's fourth quarter, were very strong with 12% constant currency revenue growth. This strong growth was driven by outstanding performance at Workforce Solutions with 17% non-mortgage revenue growth overall. In addition to accelerating long-term revenue growth, two critical goals of the EFX 2025 strategic framework are significant and consistent earnings margin expansion and the lowering of the capital intensity of the business to drive free cash flow. In 2023, the company is executing a broad operational restructuring reflecting both the acceleration of a cloud transformation and a broader focus on operational process improvements. They expect to reduce the total workforce of over 23,500 employees and contractors by over 10% during 2023.

Detractors

Catalent had spooked investors by twice postponing its fiscal year third quarter results before finally publishing, with the contract development and manufacturing organization (CDMO) citing productivity issues and higher than expected costs. The company was preparing to reduce guidance by more than $400m, but when they did eventually release details, they were better than expected (with shares recovering some lost ground in June). Net revenue for the quarter dropped 19% year-on-year to $1.04 billion, with the firm's Pharma and Consumer Health division remaining constant. However, it was the Biologics division, which includes cell and gene therapy services, that felt the full weight of the COVID cliff – the diminishing contracts and revenues from the overly-robust demand that came with the pandemic – coupled with operational issues across the network. Net revenues stood at $475 million, a 32% decline year-on-year, while the EBITDA margin (operating profit as a percentage of revenue) was only 1.1% compared with last year's 31.1%. Catalent made a slight adjustment to its revenue projection for the year. Now 2023 sales are expected to come in between $4.23bn and $4.33bn as opposed to a previous projection of $4.25bn and $4.35bn. Given the delay had come after some already short-term negative news, sentiment over the quarter has been poor. The company announced that it has suffered unexpected production delays in its Harmans, Maryland gene therapy manufacturing site (i.e., re-tooling the site as production switches from COVID vaccines). This came after the company had received FDA 483 notices at the end of last year. An FDA Form 483 is issued to firm management at the conclusion of an inspection by the FDA when an investigator has observed any conditions that in their judgment may constitute violations of the Food Drug and Cosmetic (FD&C) Act. Observations are made when in the investigator's judgment, conditions or practices observed would indicate that any food, drug, device or cosmetic has been adulterated or is being prepared, packed, or held under conditions whereby it may become adulterated or rendered injurious to health. Whilst that sounds awful, it's quite common for any investigation to result in some notices. The two sites affected were the flagship Bloomington, Indiana biologics plant, and a cell therapy facility in Brussels, Belgium. It is the Brussels facility where Catalent does filling work for Novo Nordisk's much talked about obesity drug, Wegovy. Additionally, Biotech firm, Regeneron received a rejection notice for its new version Eylea drug which it stated was due "solely due to an ongoing review of inspection findings at a third-party filler." Catalent provides the function from its Maryland site. Not helping sentiment, Catalent said that its chief financial officer, Thomas Castellano, had stepped down and was replaced by Ricky Hopson, who was promoted from his prior post as division head for clinical development and supply. In short, not a good quarter for Catalent and a roller coaster of a year so far, having risen strongly in the first quarter. The company is focussing on these issues as its longer-term positioning remain positive. It is regaining productivity at three locations which have been significantly disrupted and addressing the FDA 483 notices. It is also cost cutting and aligning the headcount to the new mix. Importantly, its customers are not going anywhere. It is extending and expanding its manufacturing partnership with Moderna, which will see Catalent support the manufacture of multiple Moderna products in multiple formats across our North American and European biologics drug product network, including helping Moderna advance its robust mRNA pipeline. Additionally, Catalent has expanded its existing manufacturing partnership with Sarepta. Catalent will be the Sarepta's primary commercial manufacturing partner for its leading gene therapy candidate for the treatment of Duchenne muscular dystrophy. A combination of breakthroughs in gene therapy, patent cliffs at most pharmaceutical companies and a positive funding environment, means continued growth in Catalent's total addressable market. The company's strategic investments have materially expanded its total addressable market and provide it with greater future growth opportunities. The addressable market could grow by another 40% to $100 billion across the markets in which Catalent operates.

At **Bio-Rad**, the expected decline in first quarter COVID-related sales resulted in lower year-over-year total revenues, but positively there was continued underlying strength in the core business in Life Science and Clinical Diagnostics. The Life Science segment net sales for the first quarter were $324million, a year-over-year decrease of 7%. Excluding COVID-related sales, Life Science revenue grew 10% and was primarily driven by qPCR, Western blotting, and droplet digital PCR products. Clinical Diagnostics was flat over the year, but stripping out COVID revenues, rose 3% driven by strong demand for diagnostic instruments. Overall, COVID related revenue fell to $2.6m in the quarter against $45m a year ago. What disappointed investors was the currency-neutral revenue growth forecast of approximately 4.5% compared to its previous estimate of 6% to 7%.

Excluding COVID-related sales, Bio-Rad estimates full-year 2023 currency-neutral revenue growth to be approximately 8.5% versus its prior guidance of 10% to 11%. It is now targeting a currency-neutral, compounded annual average core revenue growth rate of approximately 8% between 2021 and 2025 compared to its previous target of approximately 8.9%. Bio-Rad has suffered a number of market and operational challenges, which maybe the reason for the company erring on the side of caution. Firstly, whilst demand was in line with expectations across the portfolio, there was some softness in smaller biopharma companies where there has historically been strong demand for life sciences products. This correlates with funding constraints the industry faced in the first quarter. Along with IT start ups, some med-tech/biopharma companies relied on the banks that suffered in Q1 from a funding mismatch that caused a run on those banks. Secondly, there was a further tightening of sanctions impacting the business in Russia. Bio-Rad assumes this will continue. Thirdly, operationally, the backlog of orders was not reduced at a pace expected due to ongoing supply chain issues. The company had hoped to clear $30m of backorders and achieved $5m. The backorders still exist and are growing but the ramp up in production in the companies Singapore facility has been slower than expected. More positively, the company reported an increase in demand for clinical diagnostics and especially the newly launched ddPCR platform, QX600. The installed base of customers is growing. The company expects to clear the backlog by end of the year and for the Singapore facility to be fully up and running.

Illumina is core to their customers business and revenue generation. The labs cannot function without their machines. The Company leads the market with its next-generation genome sequencing systems and analysis tools. It has a 90% market share of the global sequencing market with over 20,000 active sequencing machines installed throughout 115 countries. The cost of DNA sequencing has fallen dramatically, and Illumina's recently launched NovaSeq X model can perform the task for around $200. Illumina's machines accelerate the advancement of precision medicine applications, and those applications increase as costs fall. It is not inconceivable that genetic mapping will become part of a routine check-up. First the positive news.

The company's 2023 is off to a good start. They have started shipping the first NovaSeq X Plus systems to customers and expect to ship 300 units for the full year. Illumina delivered fourth quarter revenue of approximately $1.1 billion and full year 2022 revenue of approximately $4.6 billion, in line with the upper end of guidance. They placed more than 3,200 instruments in 2022, increasing their installed base to approximately 23,000 instruments worldwide. The company has a broad offering of machines, based on the number of sequenced DNA bases per hour. It's not always necessary to sequence a whole genome. The company has had huge support for the NovaSeq X series launch. There's strong global interest with orders from more than 25 countries, 4x more than in the first quarter of the previous model launch. They reported seeing stronger-than-expected clinical adoption and orders from new to high-throughput customers who are bringing sequencing in-house due to NovaSeq X's ease of use and cost benefits. The NovaSeq X has had the strongest pre-order book of any Illumina instrument launch, and this demand will catalyze a multiyear upgrade cycle. In 2022, the company shipped a record 1,215 instruments in the mid-throughput range and saw the fourth consecutive record year for NextSeq shipments. The fourth quarter of 2022 was also the highest quarter on record for NextSeq 1000/2000 shipments. Close to 25% of NextSeq 1000/2000 units in 2022 were placed with new to Illumina customers. Within the lower cost, low-throughput models, Illumina shipped approximately 1,670 instruments, bringing nearly 700 new customers to Illumina. The low-throughput instruments consistently open new geographies and applications while serving as an effective entry point to sequencing. The clinical markets currently include testing for oncology, reproductive health and genetic disease. In 2022, shipments to clinical customers represented 45% of core Illumina consumables. Beyond oncology, genetic disease testing had a record quarter in Q4 and another strong year in 2022. It will be aided in 2023 by the European Society of Human Genetics updating its guidelines to recommend increased adoption of whole genome sequencing in diagnostics as well as increased coverage for rare and undiagnosed genetic diseases. Within the research and applied markets, consumable shipments represented 55% of core Illumina consumables in 2022.

Whilst ahead of expectations, core Illumina revenue was down 11% year-over-year. The growth driven by pull-through on the increased installed base was offset by delayed recruitment for some large research projects in the Americas and Europe, the ongoing impact of COVID disruptions in China, the year-over-year impact of customer inventory management, the anticipated decrease in COVID surveillance revenue and headwinds from foreign exchange rates. The main reason for the weakness in the share price came down to GRAIL. GRAIL offer a test called Galleri. Galleri is the only multi-cancer early detection test in a $40-plus billion market, and it had the fastest first year revenue ramp in cancer screening test history. GRAIL has established over 60 partnerships with leading health systems, self-insured employers, and other health care stakeholders. In 2022 alone, more than 4,500 providers ordered the test, contributing to the more than 60,000 Galleri test orders that have been received to date. The Galleri test has received FDA Breakthrough Designation. GRAIL expects this momentum to continue and to translate into an expected revenue CAGR of 60% to 90% over the next 5 years. The issue is that when Illumina bought back GRAIL (it once owned as a fledgling concern) for close to $7 bn 2 years ago, it did so without regulatory approval. They argued at the time that the regulators were purposely delaying a decision which would nullify the merger and the penalty of that occurring would be higher than any fine. So they went ahead anyway. Regulators are considering a record-breaking fine that will serve as a deterrent to other companies looking to close a deal without Brussels' approval. The EU commission also unveiled details of a planned order that would force Illumina to unwind the deal, and the FTC has followed. Both are concerned over competition and Illumina being to dominate in the market for cancer tests.

The company's chief executive, Francis deSouza, resigned following a bruising proxy battle with activist investor Carl Icahn (who owns about 1.4% of the company), who led a shareholder campaign criticising the "reckless decision" to close the acquisition against the wishes of Brussels and the Federal Trade Commission in Washington. As well as fighting a fine and the potential divestiture of Grail, Illumina is also contesting before courts in Luxembourg whether it is in the EU's jurisdiction to investigate the merger (as GRAIL does no business in Europe). CEO deSouza stepped down despite securing more than twice the shareholder votes, although the Chair was voted out. Illumina has lost $50bn in market value following the deal as investors have the overhang of a divestment of GRAIL at a loss, although if GRAIL were divested there would be a significant rerating of the company based on the profitability of the main Illumina business. GRAIL was always about the future. The potential is huge should trials like the NHS trial in the UK be successful. On this point and just to complicate things further, in the last month Republican lawmakers, state attorneys general and several advocacy groups have voiced their support for Illumina. The groups filed 14 amicus briefs urging the U.S. 5th Circuit Court of Appeals to reverse the FTC order. Proponents of the deal argued in the court filings that the FTC overstepped its authority in trying to unwind the tie-up that closed nearly two years ago. They added that blocking the companies from merging could harm the development of life-saving technology. Grail needs Illumina to obtain regulatory approval and commercialise production of the test, which are "required steps to delivering the full benefits of these tests to the public and detecting cancer as quickly as possible".

ThermoFisher delivered very strong results, despite the optics of the headline numbers. Revenue for the quarter declined 9% compared to a year earlier, but core organic revenue growth rose 6%. COVID-19 testing revenue came to around $140 million compared with $1.7 billion in the same period in 2022, so it is important to focus on where the business is headed in a post COVID world. The company reiterated guidance, which would have ordinarily been positive, but investors may have been concerned that this puts increased pressure on Thermo Fisher to outperform in the second half of the year, particularly as management acknowledged a "slightly more challenging" macro backdrop since the start of the year. Additionally, Danaher's reported downbeat reading on biopharma clients. However, the quarter demonstrated that the company is still seeing robust organic revenue growth, and its analytic instrument sales were ahead of Danaher's, supporting the argument that the company is differentiating itself via innovation. ThermoFisher is progressing well with its three-pillar growth strategy. Its three main aims are a) develop high impact products, b) leverage scale in high growth and Emerging Markets, and c) deliver unique value proposition to customers. During the quarter, it launched a range of high-impact, innovative new products, including the Thermo Scientific iCAP RQ Plus ICP-MS Analyzer to simplify analysis of trace elements, including identification of heavy metals in water and soil as well as toxic elements in food and beverages; the Applied Biosystems QuantStudio Absolute Q AutoRun sPCR, an automated digital PCR solution to increase productivity for molecular research, including cell and gene therapy and cancer research; and the Invitrogen DynaGreen, microplastic-free magnetic beads for protein purification, helping customers to reduce the environmental impact of life science research. Under the second pillar, the company opened a new cell culture facility in China, and it continued to strengthen its unique customer value proposition by advancing its strategic partnership with the University of California, San Francisco (UCSF), with the opening of a new cell therapy manufacturing and collaboration centre to accelerate development of breakthrough cancer therapies.

It was an active quarter in terms of capital deployment, with the company repurchasing $3.0 billion of stock, increasing its dividend by 17 percent, and completing the acquisition of The Binding Site. ThermoFisher will operate The Binding Site Group as part of its Specialty Diagnostics business segment. Binding Site is developing diagnostic products to detect and monitor protein-based blood disorders, such as multiple myeloma, and caters to clinicians and laboratory professionals. The firm reaches more than 3,000 customers in the form of hospitals, academic institutions and pharmaceutical companies.

Diageo, a global leader in the beverage alcohol industry, experienced a decline in its share price during the second quarter due to revised outlooks from several brokers. The demand for spirits in the US, which is a crucial market for the company, is expected to weaken as a result of the extraordinary growth experienced during the pandemic, potential inventory corrections, and a slower macroeconomic environment.

Diageo boasts an extensive portfolio of brands in spirits and beer, with over 200 brands including renowned names like Johnnie Walker and Guinness. The company distributes its products in more than 180 countries, taking advantage of the significant opportunity presented by the global beverage alcohol market, which is valued at approximately $1.2 trillion and displays long-term growth potential. Consumers are increasingly diversifying their choices by opting for low or no-alcohol beverages that align with their dietary preferences, lifestyle choices, and interest in natural ingredients and craft production. Furthermore, there is a global trend of consumers favouring spirits over beer and wine. In less mature spirits markets, mainstream brands provide quality and affordability, while premium core and Reserve brands cater to the demand for variety and new experiences in more mature markets. This long-term shift towards premium spirits is a key advantage that will benefit Diageo in the medium to longer term.

In the short term, however, Diageo faces persistent inflationary pressures due to higher commodity costs, particularly agave, as well as increased energy expenses and supply disruptions. These factors have impacted the company's sales, especially considering its significant international operations, which make it susceptible to exchange rate fluctuations. Despite these challenges, Diageo maintains a well-balanced portfolio and a global presence that covers both emerging and developed markets. Emerging markets, in particular, are expected to witness the entry of 600 million new consumers by 2032. Additionally, scotch represents the largest category for Diageo, accounting for 25% of the company's total sales in fiscal year 22, with net sales exceeding £3.7 billion. With a portfolio of over 40 scotch brands, Diageo's leading brand, Johnnie Walker, holds the title of the world's bestselling scotch. Moreover, Diageo is the largest international whisky manufacturer. The growth of the scotch category is bolstered by its ability to attract the next generation of Scotch consumers.

Sadly, Diageo's long-time chief executive, Sir Ivan Menezes, passed away after a brief illness. He had planned to retire the following month and had already appointed his successor, Debra Crew, who assumed the role a month earlier. Debra Crew, the first female CEO of Diageo, boasts over 25 years of experience in the food and beverage industry, having held positions at Nestle, Mars, PepsiCo, and Reynolds American, where she served as president and CEO. She joined Diageo in 2019 as a Board Member, later taking on the roles of President of North America and subsequently Chief Operating Officer. Soon after Debra assumed her new role, she reaffirmed the company’s commitment to sustainability and set ambitious goals for the future. The company aims to achieve net-zero emissions across all its distilleries by 2030. Additionally, Diageo targets a 50% absolute reduction in scope three carbon emissions and a 30% improvement in water efficiency by the same year. These initiatives reflect Diageo's dedication to environmental responsibility and align with global efforts to combat climate change.

Despite the challenges posed by the softening outlook for the US spirits market, Diageo remains well-positioned in the beverage alcohol industry. Its market leadership in scotch, strong presence in international spirits, and extensive brand portfolio provide a solid foundation for future growth. With Debra Crew at the helm as the new CEO, building on the legacy of Sir Ivan Menezes, Diageo is poised to navigate the evolving market dynamics and continue delivering value to its shareholders while pursuing its long-term sustainability goals.

3. Current Positioning

Top 10 Portfolio Holdings

Holding	Sector	Country	Portfolio %
Alphabet	Communication Services	United States	6.5
Airbus	Industrials	France	5.4
Mastercard	Financials	United States	5.1
Amazon.com	Consumer Discretionary	United States	5.1
Canadian Pacific Kansas City	Industrials	Canada	5.0
Vinci	Industrials	France	4.8
Intercontinental Exchange	Financials	United States	4.4
Microsoft	Information Technology	United States	4.4
Charter Communications	Communication Services	United States	4.2
Moody`s Corp	Financials	United States	4.1
Total			49.2

Source: Veritas Asset Management

Portfolio Breakdown

Region	Portfolio %
North America	68.5
Europe ex UK	17.4
United Kingdom	9.8
Asia Pacific ex Japan	2.5
Cash and equivalents	1.8
Total	100.0

Sector	Portfolio %
Industrials	28.8
Health Care	25.0
Financials	17.3
Communication Services	10.7
Consumer Staples	6.9
Consumer Discretionary	5.1
Information Technology	4.4
Cash and equivalents	1.8
Total	100.0

Currency	Portfolio %
USD	70.4
EUR	21.4
GBP	5.8
AUD	2.5
CAD	0.0
Total	100.0

Source: Veritas Asset Management

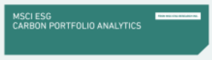
Please refer to portfolio commentary under items 1 and 2 for further information on current positioning and outlook.

4. Responsible Investment

ESG: Environmental, Social and Governance

International Norms and Standards

Proxy Voting Report

Carbon Portfolio Analytics Report 

International Norms and Standards - United Nations Global Compact Screen ("UNGC")

The United Nations Global Compact Screen ("UNGC") identifies companies involved in controversies where the company's alleged actions constitute a violation of one or more of the ten principles that cover environmental, anti-corruption, human rights and labour standards. The framework encourages signatories to share best practices in order to become better, more sustainable organisations.

On a monthly basis, utilising MSCI ESG Research data and an alert system, Veritas reviews all investee companies to determine if a company fails any of the global compact principles. If there are notable changes during the month, our system will distribute an email alert to the Investment Team, Compliance Team, and ESG Team. Veritas will identify which principle has been violated, assess the materiality of the violation, and engage with the business if required.

Fail	The company is implicated in one or more controversy cases where there are credible allegations that the company or its management inflicted serious large-scale harm in violation of global norms.
Watch List	The company is implicated in one or more controversy cases that are serious and warrant ongoing monitoring. However, based on information available to date, it does not constitute a significant breach of global norms according to the methodology.
Pass	According to the methodology, the company has not been implicated in any controversy case constituting a significant breach of global norms within the last three years.

As illustrated in the diagram below, during the three months to 30 June 23, 0% of companies held in the Fund "Failed" the UN Global Compact screen. Three companies in the Fund (16.4%) were listed on the Global Compact "Watchlist". For example, Amazon.com, Inc. is listed on the watchlist for a potential breach of **Principle 3: Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining**, specifically concerning wage disputes. Veritas will continue to monitor the company's progress in this area. Should this flag escalate to a "Fail", we will have cause to engage.

United Nations Global Compact Violations (%)

	Portfolio	Benchmark	Active
Global Compact Compliance Violation (%)	0.0%	0.5%	-0.5%
Global Compact Compliance Violation or Watch List (%)	16.4%	20.5%	-4.1%

Additional Global Norms Framework Violations (%) [1]

Human Rights Norms Violation (%)	0.0%	0.5%	-0.5%
Human Rights Norms Violation or Watch List (%)	12.0%	19.0%	-6.9%
Labor Norms (%)	0.0%	0.1%	-0.1%
Labor Norms Violation or Watch List (%)	12.0%	15.5%	-3.5%

Source: MSCI

Please feel welcome to get in touch with us for more information on proxy voting and carbon analytics and risk management.

Disclaimer

This is a marketing communication. Please refer to the prospectus, the key investor information documents (the **KIIDs/PRIIPS KIDs**) and the financial statements of Nedgroup Investments Funds plc (the **Fund**) before making any final investment decisions.

These documents are available from Nedgroup Investments (IOM) Ltd (the **Investment Manager**) or via the website: www.nedgroupinvestments.com.

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The Fund is authorised and regulated in Ireland by the Central Bank of Ireland. The Fund is authorised as a UCITS pursuant to the European Communities (Undertakings for Collective Investment in Transferable Securities) Regulations 2011 as amended and as may be amended, supplemented, or consolidated from time-to-time and any rules, guidance or notices made by the Central Bank which are applicable to the Fund. The Fund is domiciled in Ireland. Nedgroup Investment (IOM) Limited (reg no 57917C), the Investment Manager and Distributor of the Fund, is licensed by the Isle of Man Financial Services Authority. The Depositary of the Fund is Citi Depositary Services Ireland DAC, 1 North Wall Quay, Dublin 1, Ireland. The Administrator of the Fund is Citibank Europe plc, 1 North Wall Quay, Dublin 1, Ireland.

The sub-funds of the Fund (the **Sub-Funds**) are generally medium to long-term investments and the Investment Manager does not guarantee the performance of an investor's investment and even if forecasts about the expected future performance are included the investor will carry the investment and market risk, which includes the possibility of losing capital.

The views expressed herein are those of the Investment Manager / Sub-Investment Manager at the time and are subject to change. The price of shares may go down as well as up and the price will depend on fluctuations in financial markets outside of the control of the Investment Manager. Costs may increase or decrease as a result of currency and exchange rate fluctuations. If the currency of a Sub-Fund is different to the currency of the country in which the investor is resident, the return may increase or decrease as a result of currency fluctuations. Income may fluctuate in accordance with market conditions and taxation arrangements. As a result an investor may not get back the amount invested. Past performance is not indicative of future performance and does not predict future returns. The performance data does not take account of the commissions and costs incurred on the issue and redemption of shares.
Fees are outlined in the relevant Sub-Fund supplement available from the Investment Manager's website.
The Sub-Funds are valued using the prices of underlying securities prevailing at 11pm Irish time the business day before the dealing date. Prices are published on the Investment Manager's website. A summary of investor rights can be obtained, free of charge at www.nedgroupinvestments.com.

Distribution: The prospectus, the supplements, the KIIDs/PRIIPS KIDS, constitution, country specific appendix as well as the annual and semi-annual reports may be obtained free of charge from the country representative and the Investment Manager. The Investment Manager may decide to terminate the arrangements made for the marketing of its collective investment undertakings in accordance with Art 93a of Directive 2009/65/EC and Art 32a of Directive 2011/61/EU.

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FEES
A schedule of fees and charges is available on request from Nedgroup Investments. One can also obtain additional information on Nedgroup Investments products on our website.

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