

Evenlode Global Opportunities Investment View

November 2023 – Third quarter results

All market data is from FactSet and FE Analytics unless otherwise stated. Past performance is not a guide to future returns.

As we reflect on the third-quarter results of 2023, it is encouraging to observe the robust performance across the Evenlode Global Opportunities portfolio. With 90% of the companies we invest in having reported, we've seen a commendable average organic revenue growth of 8.7%. This growth, coupled with expanding operating margins, is a testament to the competitive strength and resilience of these businesses. The tone from management teams has been cautiously optimistic. While they acknowledge some signs of short-term economic uncertainty, their forward-looking statements reflect a well-considered balance of prudence and confidence in capturing long-term demand and growth. In this investment view, we will delve into a selection of these results and explore the wider trends that have driven performance.

Big tech and cloud computing

In the realm of cloud computing, we've observed a mixed yet informative set of performances from sector leaders Microsoft, Amazon, and Google. Microsoft emerged as a strong performer, surpassing expectations significantly, while Amazon reported in-line results and Google Cloud Platform (GCP) somewhat underperformed. A key highlight has been the re-accelerating growth in Microsoft's Azure, buoyed by a greater than anticipated uptake of AI workloads and cloud migrations. While Alphabet reported an encouraging recovery in search revenues, the progress in cloud was disappointing (note that Alphabet's cloud business also comprises its Workspace suite, which is closer to Office 365 than it is to Azure/AWS). Management continues to highlight ongoing "workload optimisation" within its client base, which is skewed towards smaller enterprises and start-ups. Despite these varied outcomes, it's noteworthy that these three hyperscalers collectively maintain an impressive annualised revenue run-rate of approximately \$192 billion, marking a year-over-year growth of 19%¹. Accenture estimate that only 40% of potential workloads have been migrated to cloud, demonstrating a long runway for growth.

Microsoft also announced the general release of Copilot for Office 365, a significant development in the application of generative AI. While we remain somewhat sceptical of generative AI's potential to revolutionise business models in the immediate future, its capacity to enhance productivity incrementally is undeniable. While our investment case for Microsoft focuses more on the broader cloud adoption trend rather than the sale of the Copilot service specifically, this development demonstrates Microsoft's innovative approach and how their existing relationships with business users can continuously add value.

Spirits and distributor destocking

In contrast to the strong showing in the tech sector, our spirits holdings experienced continued headwinds this quarter. Notably, Pernod Ricard reported an expected low single-digit decline in organic revenues, while Diageo issued a profit warning just days prior to their capital markets day. Pernod Ricard signalled a moderation in inventory destocking in the U.S., with inventory levels now normalising at both wholesalers and retailers. This is a required precursor to returning to higher sales growth in early 2024. While China remained soft, with weakening macroeconomic conditions and a



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tough prior year comparator, there are some indications that sales in October have improved. These indicators of improved performance were met well by the market.

Diageo's challenges were most pronounced in Latin America, where the company anticipates a 20% revenue decline for the first half of their financial year. This downturn is attributed in part to distributors stockpiling inventory in anticipation of Diageo's price hikes, which were a response to rising inflation. This situation was exacerbated by an economic slowdown, limited visibility on actual product sales (owing to the absence of scanner data), and a normalisation from the peak sales observed post-COVID. Consequently, a significant inventory build-up at the distributor level has occurred, which is expected to take time to resolve.

These developments with Pernod Ricard and Diageo highlight the complexities involved in implementing inflationary price increases on long-lived products. Despite these short-term challenges, the long-term outlook for both companies remains promising. The ongoing trend of premiumisation and expanding access to spirits in high-growth markets, such as India, continues to underpin their growth potential.

Financials and consumer credit

Our portfolio also includes companies with exposure to consumer financial health. This segment includes credit card network companies Mastercard and Visa, as well as the credit rating agency Experian; critically, while all are involved in the origination and maintenance of consumer credit, none carries any principal balance sheet risk. Both Mastercard and Visa reported in-line results, each achieving 11% organic revenue growth. A notable driver of this growth has been the increase in cross-border transactions, reflecting the global reopening from COVID-19 and the resurgence of Asian travellers.

The resilience of U.S. consumer spending has been a key theme this year, as wealthier consumers continue to spend on travel and entertainment despite rising interest rates and persistent inflation. Mastercard CEO Miebach commented on the remarkable durability of consumer spending amidst economic uncertainty, a sentiment echoed by Visa, which also reported stable consumer spending levels. Both companies highlighted the growth in additional services, such as fraud prevention and acceptance solutions, illustrating how their extensive network and proprietary data sets can be leveraged to offer value-added solutions to clients.

Experian reported 5% organic growth, significantly outperforming its peers TransUnion and Equifax. The share prices of all three agencies had experienced a decline following TransUnion's unexpectedly soft results at the start of the reporting season. It's important to note the distinct differences between these agencies, including their geographic exposures in the U.S. and their varying levels of involvement in the U.S. mortgage, unsecured lending, and smaller financial institutions. Our preference for Experian stems from its lower exposure to these latter two categories, offering some insulation from the more interest rate-sensitive segments of the U.S. economy. However, it's not to say Experian is entirely immune; the organisation is still navigating challenges such as the continuing decline in auto loan origination in the U.S., as lower income consumers delay significant purchases amidst a weak macroeconomic outlook. While we remain cognisant of the short-term macroeconomic concerns, we are primarily focused on Experian's long-term opportunities. As more transactions are



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digitised and the requirements for credit checking increase, we see the value of Experian's services to clients increasing.

Future expectations

As we conclude our review of the third-quarter results, it's clear that despite some variability in performance across different sectors, the resilience and adaptability of our portfolio companies stand out. This period has undoubtedly presented its challenges, from fluctuating economic conditions to evolving consumer behaviour. However, the underlying strength and strategic agility demonstrated by our holdings, particularly in sectors like technology and financial services, provide a solid foundation for optimism.

Looking ahead, we remain confident in the long-term potential of the businesses in the portfolio. The diverse nature of our portfolio, coupled with our focus on companies with robust business models and strong market positions, places us well to navigate through short-term market volatility and capitalise on long-term growth opportunities. Our commitment remains steadfast in identifying and investing in those opportunities that offer the most promising prospects for sustainable, long-term returns.

Chris (E), James, Cristina and the Evenlode team

20 November 2023

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ⁱBarclays, CQ3 Public Cloud Update, 27 October 2023

