LIONTRUST

Liontrust Global Dividend Fund: December 2022 review

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The Liontrust Global Dividend Fund returned 4.1% over the quarter, compared with 1.9% from the MSCI World Index and 5.5% from the IA Global Equity Income sector (both comparator benchmarks).

Nike was our top contributor to performance in the quarter (+31%) as the company posted its largest earnings beat in 20 years, catapulting the share price higher in December. We had added to our position in September, taking advantage of share price weakness caused by inventory-build concerns, which although valid, we viewed as a short-term headwind. As a result, expectations heading into the company's quarterly print were unduly pessimistic with little value being assigned to Nike's booming product innovation pipeline.

We invest in Nike because of its industry leading approach to connecting with customers and relentless focus on product innovation. Consumer responses to recent innovations have been constructive which is helping to drive strong-full price sell through – Nike's recently launched football boot (the fastest ever created) scored more goals in the recent World Cup than all other brands combined. The biggest apparel overhaul in 30 years and a refresh of its basketball line are but a couple of innovations in the pipeline which will support the company's top line.

With the inventory peak behind us and the return to growth in China, Nike's immediate challenges are dissipating while the key drivers of value creation for the business are performing strongly: product innovations continue apace and direct-to-consumer ecommerce sales (which are both higher margin and more capital light) continue to grow as a portion of the business. Indeed, Nike Digital had its best ever quarter, growing 34%, fuelled by an increasingly engaged cohort of 160 million active members. We expect the company's continuing direct-to-consumer transformation to bolster profitability going forwards.

Another notable contributor was serial acquirer Diploma (+20%), whose full year earnings came in well ahead of forecasts driven by stronger than expected organic revenue. Diploma is one of the UK's highest quality compounders, which has an exceptional track record of creating shareholder value – compounding total shareholder returns at 27% p.a for the past decade. The company distributes essential products to industrial and healthcare companies (controls, seals, consumables for life sciences and diagnostic instruments), which are typically sourced from niche manufacturers and bundled together or customised for end users to add customer value.

As a distributor, the company is asset light. As a customer-focused innovator, the company has high and stable profit margins underpinned by multi-year customer contracts for many of its products. As a serial acquirer, it has proven to be a highly scalable platform (given its de-centralised model), which still has a significant runway ahead given under penetration of key markets.

Our serial acquirer holdings in general performed well in the quarter (which also include Lifco , Roper Technologies and Halma, exited on price target realisation in the period). We attribute this to their nimble playbooks that allow capital to be deployed at ease. Small private business valuations have fallen significantly this year, and since our serial acquiring companies buy up companies for the long-term, retain management and help them build their business, selling to a Diploma is more attractive for an entrepreneur than an asset-stripping private equity house.

Put simply, these companies are adept at deploying capital at attractive rates of return. Furthermore, they operate in niche markets with strong barriers to competition and where demand is sticky, through good times and bad. Diploma's seals and fasteners are not the most exciting products in the world, but they are deeply embedded in its customers' workflows.

Other strong performers included Tencent (+17%), which benefitted from China softening its zero Covid stance, Universal Music Group (+19%) which will see earnings accretion from Apple music raising its prices, and ASML (+18%) whose order backlog of €38bn sets them up well for the coming year.

On the flip side, our biggest detractor to performance in the quarter was Meta (-35%). The size of the capital investment in AI infrastructure announced by Meta in October caught us by surprise because it highlights how far Meta has fallen behind its major competition − TikTok. Whilst we have been disappointed by Meta's lack of expense control and its unprecedented investment in the Metaverse, we decided to exit our small investment in Meta in November due to management's forecast for capital expenditure in 2023 that highlights that the companies once dominant barriers to competition are waning. This has been one of the most difficult investments we have ever made and feel let down by Meta management, but even in volatile markets if one of the key criteria's (innovation, barrier, execution, returns) breaks down – we exit the position and remove the company from our watchlist.

Alphabet was also a drag on performance (-14%) as we experienced a wider collapse in stock prices for US big technology companies (the FAANG's) amid a rotation out of 'growth stocks' and into old industrial, 'value stocks'. Two major headwinds faced by the FAANG's in the quarter were a lapping high growth and a very strong US dollar that depreciates overseas earnings. While both phenomena can arguably be said to be transitory in nature, a pullback in advertising spend remains a headwind in a slowing economy. That said, Alphabet's Search business (its key profit engine) is holding up better than other platforms owing to its 'bottom of funnel positioning' − as advertisers become more discerning over marketing spend, platforms that can offer the highest return-on-investment for customers become a greater proportion of customer ad wallets, and Google Search is industry leading in this respect. Furthermore, the company's cloud business is well positioned to drive the next leg of growth for the company.

Another detractor was Pool Corporation (-12%), the largest global distributor of pool supplies in the world, which was hit by uncertainties relating to a slowing housing market and construction activity. While results have been robust throughout 2022, new pool construction would be expected to contract more significantly in a protracted recessionary environment. However, serving this end market is a small component of Pool's business and partially mitigated through a Covid-induced renovation backlog bolstering demand. Indeed, two thirds of company revenues are non-discretionary (repair and maintenance), and 80% revenue comes from pools already in the ground, providing some resiliency from an economic downturn which we believe is underappreciated. What's more, is that the company has a two decade track record of holding onto pricing gains, which will be an important dynamic as we start to see deflation seep through supply chains.

Looking into next year, the key headwind for markets looks set to shift from inflation to slowing economic growth. In this tough operating environment, we believe the companies that will emerge as long-term winners will be high-quality innovative companies given their operational resilience, adaptability, superior growth and strong barriers to competition.

Discrete years' performance (%), to previous quarter-end:**

	Dec-22	Dec-21	Dec-20	Dec-19	Dec-18
Liontrust Global Dividend C Acc GBP	-7.8%	16.1%	16.7%	34.0%	-5.2%
MSCI World	-7.8%	22.9%	12.3%	22.7%	-3.0%
IA Global Equity Income	-1.2%	18.7%	3.3%	18.6%	-5.8%
Quartile	4	3	1	1	2

****Source: FE Analytics as at 31.12.22. Quartile generated on 06.01.23**

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For a comprehensive list of common financial words and terms, see our glossary at:
https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms

Key Risks:

Past performance is not a guide to future performance. Do remember that the value of an investment and the income generated from them can fall as well as rise and is not guaranteed, therefore, you may not get back the amount originally invested and potentially risk total loss of capital. The MSCI World Index and IA Global Equity Income sector are comparator benchmarks.

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.

Investment in the Fund involves foreign currencies and may be subject to fluctuations in value due to movements in exchange rates.

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