QUARTERLY INVESTMENT REVIEW

Quality Cyclicals Strategy

Performance returns (USD)

ANNUALIZED RETURNS (QUARTER-END)	Quarter-End	YTD	1-Year	3-Year	5-Year	10-Year	Since Inception
Quality Cyclicals Strategy (net)	7.35	7.35	18.83	6.68	–	–	17.66
Quality Cyclicals Strategy (gross)	7.48	7.48	19.40	7.19	–	–	18.23
MSCI ACWI	8.14	8.14	23.15	6.94	–	–	14.64
Value Add	-0.79	-0.79	-4.32	-0.26	–	–	+3.03

Major Performance Drivers

The GMO Quality Cyclicals portfolio underperformed the MSCI ACWI in the first quarter.

There was a wide gap between winners and losers in equity markets this quarter. This was evident across sectors, with a 13% return differential between the strongest, Information Technology, and the weakest, Real Estate. From a geographical perspective, the U.S. outperformed one of the weakest major markets, Hong Kong, by 22 percentage points. And almost unimaginably, there was a 38% performance gap between the subgroups of the GICS Technology sector, with Semi-conductors in vogue while Tech Hardware decidedly was not.

This quarter was 2023 redux in markets; the true driving force was Artificial Intelligence and particularly Nvidia, and not the work of an acronym[1]. Nvidia's stock rose 82% but there were other ways to gain exposure, even if you don't fancy your chances with Nvidia; Super Micro was up 255%! More materially to your portfolio, there was broad strength in the AI supply chain, with holdings Micron and Lam Research performing well. At the same time, certain customers of Nvidia's were going great guns too – Meta has worked hard in recent years to press home its scale advantage in AI-targeted advertising, while Alphabet is also at the leading edge of AI development. All of these companies share drivers with Nvidia and Super Micro, but not their high multiples. Not owning Nvidia stock was an opportunity cost in terms of potential returns but one that was largely mitigated by other, more attractively priced AI beneficiaries.

Despite not owning Nvidia or Super Micro, Quality Cyclicals did own two of the top 10 performers this quarter, Meta and GE. Meta is perhaps coming to the end of its purdah after being perceived as profligate with investment, perhaps unfairly, in 2022. As if to underline CEO Zuckerberg's seriousness about capital allocation, Meta appointed Hock Tan, CEO of Broadcom and so far an outstanding capital allocator, to its board in the quarter – a positive sign in our view. GE largely completed its long-term transformation from industrial conglomerate to jet engine specialist by spinning out its Vernova power business. We believe that the jet engine joint venture between GE and Safran (also held, also contributing strongly to returns this quarter) is likely to propel earnings for years to come.

Credit was another bright spot in the portfolio. Wells Fargo benefited from further easing of the constraints placed on it after its difficulties a few years ago while American Express continues to grow robustly and reiterated confidence in its ability to do so in the medium term.

Composite Inception Date: 30-Apr-20
Performance for the year of inception is less than a full calendar year. Returns shown for periods less than one year are not annualized.
Risks: Risks associated with investing in the Strategy may include Market Risk - Equities, Management and Operational Risk, Focused Investment Risk, Non-U.S. Investment Risk, and Currency Risk.Returns shown for periods greater than one year are on an annualized basis. To obtain performance information to the most recent month-end, visit www.gmo.com. **Performance Returns: Performance data quoted represents past performance and is not predictive of future performance.** Net returns are presented after the deduction of a model advisory fee and incentive fee if applicable. These returns include transaction costs, commissions and withholding taxes on foreign income and capital gains and include the reinvestment of dividends and other income, as applicable. Fees paid by accounts within the composite may be higher or lower than the model fees used. **GMO LLC claims compliance with the Global Investment Performance Standards (GIPS®). A Global Investment Performance Standards (GIPS®) Composite Report is available on GMO.com by clicking the GIPS® Composite Report link in the documents section of the strategy page. GIPS® is a registered trademark owned by CFA Institute. CFA Institute does not endorse or promote this organization, nor does it warrant the accuracy or quality of the content contained herein. Actual fees are disclosed in Part 2 of GMO's Form ADV and are also available in each strategy's Composite Report.** The portfolio is not managed relative to a benchmark. References to an index are for informational purposes only. The local market in which some accounts in the composite are priced was closed for Good Friday on March 29, 2024. Therefore, the performance for the strategy and corresponding benchmark will utilize March 28 for purposes of the ending valuation for the March return and the starting valuation for the April return. Gross returns are presented gross of management fees and any incentive fees if applicable. These returns include transaction costs, commissions, withholding taxes on foreign income and capital gains and include the reinvestment of dividends and other income, as applicable. If management and incentive fees were deducted performance would be lower. For example, if, before fees, the strategy were to achieve a 10% annual rate of return above its hurdle rate each year for ten years, and an annual advisory fee of 1% and incentive fee of 20% of net returns above the hurdle rate were charged during that period, the resulting average annual net return (after the deduction of management and incentive fees) would be approximately 7.20%. The portfolio is not managed relative to a benchmark. References to an index are for informational purposes only.

Major Performance Drivers Cont.

At the other end of the performance spectrum, your portfolio's exposure to Clean Energy names continued to detract from performance. At the start of the quarter your portfolio held positions in Darling Ingredients, Neste, Grain Plains, and SolarEdge. All were weak, connected by weaker carbon markets and investors recoiling from the area. We met with management from Darling Ingredients in the quarter and continue to believe that the company's locked-in feedstock supply creates a measure of hedging within the business. Neste has an element of similar advantage – we added on weakness in the quarter. We also met with SolarEdge who again lowered expectations this quarter. Rather than commit more capital to SolarEdge we initiated a new position in Enphase, the other supplier of high-quality invertors for solar installations. Data from distributors suggest that inventories continued to be worked down and we would hope for better news later this year. We believe that Clean Energy stocks are in a revulsion phase and represent potentially excellent value at this point. We have written a recap of the case for Clean Energy, which is available at www.gmo.com.

Real Estate and Other Resources also detracted from returns. Your Real Estate exposure comes via holdings in two U.K. housebuilders – Berkeley and Persimmon. After a strong Q4, Persimmon gave back some of its gains. Persimmon trades at the lowest multiple of book value since the GFC and we believe has the opportunity to earn a strong return on that book value.

We added a third position in the Real Estate silo, also in the U.K., Howden Joinery. Howden is the scale player in kitchen refurbishment in the country – it has a strong business model based around selling to kitchen fitters rather than end buyers and has built a dense network allowing it to deliver higher availability to the fitters than the competition. We also initiated a small position in IMCD, the Dutch-listed leading distributor of specialty chemicals. IMCD has contracts to represent dozens of large chemical producers to supply smaller customers. At the same time, IMCD is able to offer technical sales to those smaller customers, thereby adding value for both suppliers and customers. IMCD runs a capital-light model and is able to grow both organically and inorganically, as their broader network means they can improve the return on capital of purchased businesses.

Your portfolio remains oriented to the better-quality businesses in more cyclical areas of the markets, where we believe that management can exploit their competitive advantage to deploy capital productively through the cycle.

Nvidia (0.0%), Super Micro (0.0%), Micron (3.5%), Lam Research (3.0%), Alphabet (2.6%), Meta (3.1%), GE Vernova (1.5%), Safran (3.8%), Wells Fargo (3.5%), American Express (3.7%), Darling Ingredients (2.1%), Neste (1.6%), Green Plains (0.6%), SolarEdge (1.0%), Enphase (0.4%), Berkeley Group (2.1%), Persimmon (1.3%), Howden Joinery (0.6%), IMCD (0.6%).

[1] The Magnificent 7 have been instrumental in or are likely to benefit from advances in AI of course. They have other commonalities too. For example, they are global companies with exposure to the world economy, with geopolitical benefits and risks associated with their shared U.S. domicile. Because of their fortress-like competitive advantages, which have led to their dominant market positions, they have tended to attract more regulatory scrutiny than the average business. Nevertheless, they don't necessarily win or fail together – this quarter both Apple and Tesla fell in rising markets.

PRODUCT OVERVIEW

The GMO Quality Cyclicals Strategy seeks to generate total return by investing in leading cyclical businesses. Leveraging their long-term disciplined approach to investing in high quality companies, GMO's Focused Equity team selects from a high-conviction universe of cyclical businesses that are of higher quality than their industry peers. The team believes that quality cyclical businesses are structurally underappreciated by the market and that times of elevated stress can create extraordinary opportunities in quality cyclicals.