

# QUARTERLY INVESTMENT REVIEW

## Quality Fund

### RETURNS (%) (USD)

	Cumulative (%)		Annualized (%)				
	QTD	YTD	1 Year	3 Years	5 Years	10 Years	ITD
Net of Fees (Class III)	11.85	30.01	30.01	11.64	16.76	13.43	9.84
Gross of Fees (Class III)	11.98	30.65	30.65	12.18	17.33	13.98	10.37
S&P 500	11.69	26.29	26.29	10.01	15.69	12.03	9.59
MSCI World	11.42	23.79	23.79	7.28	12.81	8.60	7.68
Value Added (vs. S&P 500)	0.15	3.72	3.72	1.63	1.07	1.40	+0.26
Value Added (vs. MSCI World)	0.43	6.23	6.23	4.36	3.96	4.83	+2.16

### Major Performance Drivers

What a year 2023 was in the markets! The portfolio had its second-best result since inception, as inflation subsided alongside economic concerns and investors processed positive developments on various fronts.

The fourth quarter added to the year-end total nicely, with the portfolio outperforming versus the broader markets. The S&P 500 returned 11.7% while the MSCI World returned 11.4%. Tech stocks were strong, with the NASDAQ up 13.6%. Stock selection in Financials helped returns as the sector was buoyed by declining rate expectations. Consumer Staples and Health Care stocks generally underperformed. The portfolio had no exposure to Energy, the quarter's weakest sector.

The magnitude of 2023 returns for technology companies seems mind-boggling at first glance – the NASDAQ 100 returned 54% for the year – and we addressed the sustainability of those returns in our year-end letter. There is a component of the return reflecting the gains from innovation, e.g., those around ChatGPT and AI, and we believe that several of your holdings in software and semi-conductors are positioned to benefit from that. From our perspective, there were also allocation opportunities around market reaction to AI. In the case of Adobe, we believe that the market has overestimated the benefits of AI to the company and therefore took the opportunity to liquidate the position. For Accenture, on the other hand, we believe that pressure on IT spending this year is masking what is a significant multi-year opportunity to assist major corporations to prepare their data for a different world and added to the position.

However, we see less merit in arguments based on rates or a “natural” rebound for the portfolio's technology-related exposure and we trimmed over the year and in Q4, having found incremental opportunities to put capital to work with what we believe to be other productive users of that capital, some trading at more subdued valuations, in the industrial, health care, and consumer spaces.

Consumer Staples companies, long a mainstay for quality investors, have been under pressure for a while now, and we adjusted several positions in the quarter. These companies were affected by inflation more than most – the costs of the commodities required for production, packaging, and distribution soared just as consumer balance sheets were stressed by rounds of price increases and rising borrowing costs. To add insult to injury, the potential for GLP-1 prescription has cast a cloud over potential consumption, and therefore revenues, for many of the food and beverage businesses, too. Fundamental returns were weak, and valuations were cut. These new valuations are intriguing; reduced expectations for the Staples businesses reduces investor risk. Current share prices give little credit for potential margin expansion should commodity prices ease or other concerns prove overblown.

In addition to the list of challenges for Staples, Diageo was one of several companies hit by inventory issues this year. Assuming the competitiveness of Diageo's product remains approximately stable, destocking issues should shrink into the rearview mirror over time. The shares now trade at their lowest valuation in years, and we added to this position this quarter. We would expect total returns at least in line with potentially double-digit fundamentals from here.

We also initiated a position in Haleon, formerly the consumer health business of Glaxo and Pfizer. Its portfolio of products sits at the intersection of Consumer Staples and Health Care. You will likely know its products, e.g., Sensodyne for your teeth and Advil for your head, even if you're not familiar with the business. Haleon trades at a similar valuation to Diageo, with a similar level of anticipated revenue growth. The point of interest is that Haleon was spun out of Glaxo in 2022 and still bears many of the “big pharma” costs inherited during the carve out. If the company is successful in rationalizing some of these costs as planned, the impact on margin will be material in driving fundamental returns.

Portfolio weights, as a percentage of equity, for the positions mentioned were: Accenture (3.3%), Diageo (1.4%), and Haleon (0.3%).

Inception Date: 6-Feb-04

**Risks:** Risks associated with investing in the Fund may include: (1) Market Risk - Equities: The market price of an equity may decline due to factors affecting the issuer or its industry or the economy and equity markets generally. Declines in stock market prices generally are likely to reduce the net asset value of the Fund's shares. (2) Management and Operational Risk: The risk that GMO's investment techniques will fail to produce desired results. (3) Focused Investment Risk: The Fund invests its assets in the securities of a limited number of issuers, and a decline in the market price of a particular security held by the Fund may affect the Fund's performance more than if the Fund invested in the securities of a larger number of issuers. For a more complete discussion of these risks and others, please consult the Fund's prospectus. Annualized Returns may include the impact of purchase premiums and redemption fees. 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](http://www.gmo.com).

If certain expenses were not reimbursed, performance would be lower. Transaction costs, if any, are paid to the fund to offset the cost of portfolio transactions to invest or raise cash. **Net Expense Ratio: 0.50%; Gross Expense Ratio: 0.51% Net Expense Ratio reflects the reduction of expenses from fee reimbursements. The fee reimbursements will continue until at least June 30, 2024. Elimination of this reimbursement will result in higher fees and lower performance. Gross Expense Ratio is equal to the Funds Total Annual Operating Expenses set forth in the Funds most recent prospectus dated June 30, 2023.**

Performance data quoted represents past performance and is not indicative of future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance data may be lower or higher than the performance data provided herein. The portfolio is not managed relative to a benchmark. References to an index are for informational purposes only.

# QUARTERLY INVESTMENT REVIEW

## PRODUCT OVERVIEW

The GMO Quality Fund seeks to generate total return by investing primarily in equities the Focused Equity team believes to be of high quality.

The team believes that companies with established track records of historical profitability and strong fundamentals – high quality companies – are able to outgrow the average company over time and are therefore worth a premium price. The Fund's disciplined approach uses both quantitative and fundamental techniques to assess the relative quality and valuation of global companies and aims to exploit a long-term investment horizon while withstanding short-term volatility.

## IMPORTANT INFORMATION

**Comparator Index(es):** The S&P 500 Index is an independently maintained and widely published index comprised of U.S. large capitalization stocks. S&P does not guarantee the accuracy, adequacy, completeness or availability of any data or information and is not responsible for any errors or omissions from the use of such data or information. Reproduction of the data or information in any form is prohibited except with the prior written permission of S&P or its third party licensors. The MSCI World Index (MSCI Standard Index Series, net of withholding tax) is an independently maintained and widely published index comprised of global developed markets. MSCI data may not be reproduced or used for any other purpose. MSCI provides no warranties, has not prepared or approved this report, and has no liability hereunder.

**An investor should consider the fund's investment objectives, risks, charges and expenses before investing. This and other important information can be found in the funds prospectus. To obtain a prospectus please visit [www.gmo.com](http://www.gmo.com). Read the prospectus carefully before investing.**

**The GMO Trust funds are distributed in the United States by Funds Distributor LLC. GMO and Funds Distributor LLC are not affiliated.**

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Founded in 1977, GMO is a global asset manager committed to delivering superior performance and advice to our clients. We are privately owned, which allows us to singularly focus on our sole business – achieving outstanding long-term client investment outcomes. Offering multi-asset, equity, fixed income, and alternative strategies, we invest with a long-term, valuation-based philosophical approach.

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