Q2 2022 Update

IQEQ

Davy Discovery Equity Fund

For Investment Professionals Only

Performance	1 Month (%)	Q2 2022 (%)	1 Year (%)	3 Years P.a. (%)	5 Years P.a. (%)
Davy Discovery Equity Fund (net of fees)	-6.31	-12.19	-14.87	5.05	6.18
MSCI World Small & Mid-Cap Index[1] (total return)	-7.76	-11.73	-9.73	7.27	6.84

Source: IQ EQ Fund Management (Ireland) Limited (Class A Acc Eur) and Bloomberg as at 30 June 2022
[1] The MSCI World SMID Cap Index shown above does not include fees or operating expenses and you cannot invest in it. The MSCI World SMID Cap Index captures mid and small cap representation across 23 Developed Markets (DM) countries. With 5,250 constituents, the index covers approximately 28% of the free float-adjusted market capitalization in each country.

Fund overview

The investment aim of the **Davy Discovery Equity Fund** (the 'Fund') is to achieve long-term capital growth by investing in shares of small and medium sized companies on a global basis. These companies tend to demonstrate growth potential and represent attractive investment opportunities. Investing during the early stage of a company's life cycle can lead to higher than average investment returns.

Market comment

The equity market correction which began in early January continued through the second quarter, with the MSCI World Index falling by 10.80% in euro terms. This brought the year-to-date return to -13.53% for the MSCI World Index. Euro-based investors benefited somewhat from a rally in the dollar which supported the euro value of US asset prices during the period.

Market direction during the quarter was dictated in large part by inflation data and increasingly hawkish comments from central bankers about the need for higher interest rates. There was also growing evidence towards the end of the quarter of the negative impact that inflation expectations are having on consumer and business sentiment as evidenced from surveys in major developed economies. Recession risk resulted in a renewal of the traditional performance relationship between bonds and equities: as equities weakened in response to the rising risk of recession, bonds began to rally.

The war in Ukraine is also exacerbating inflationary pressures, particularly in the areas of food and energy. Nevertheless, most measures of broad commodity prices ended the quarter lower as recession fears grew. Meanwhile, China's zero-Covid strategy was in full effect during the quarter, with extended lockdowns in some major cities such as Shanghai driving down China's GDP growth expectations for 2022.

Within the equity market, the second quarter pattern followed that of the first as Technology and Consumer Discretionary stocks underperformed while Energy and Consumer Staples outperformed. The Energy sector was alone in producing a positive return during the second quarter, driven higher by energy prices.

Fund performance

The **Davy Discovery Equity Fund** returned -12.19% during the quarter versus an index return of -11.73% (MSCI World SMID Index). The performance of the Fund in 2Q 2022 was broadly in line with its benchmark MSCI World SMID, but smaller companies continue to underperform larger companies. Since the start of 2022, markets have been negatively affected by inflation, war in Ukraine and China's recurring lockdowns. The market is laser-focused on inflation levels and likely policy responses by central banks. These concerns were exacerbated in late June when Federal Reserve Chairman Powell responded to questions about inflation as if the Fed had made a policy mistake. This is probably why the ECB, and the Bank of England, have delayed their policy responses, while the Federal Open Market Committee (FOMC) had opted for a more aggressive pre-emptive strike. For our part, we anticipate self-correcting forces will win out and will soon begin to push inflation rates lower as this is a supply-side shock caused by the resumption of the normal course of business activities post lockdown, resulting in fewer rate hikes than currently anticipated. During periods of uncertainty, we believe patience is key, which is why we have been slow to make significant adjustments to the portfolio. From a style perspective the power of quality as a style was reinforced this quarter with profitability as a factor positively contributing to performance. We are using this environment to seek opportunities in quality ESG stocks whose valuations have become increasingly attractive.

The top five equity contributors to relative performance during the quarter were H&R Block Inc, TravelSky Technology Limited, Masco Corporation, Capcom Co Ltd and Gentex Inc. The bottom five equity detractors from relative performance during the quarter were Tandem Diabetes Care Inc, Cognex Corporation, Nemetschek SE, Endava Plc, Boliden AB.

H&R Block Inc (HRB) is a tax preparation platform offering a combination of online and offline consumer tax services. HRB holds a BBB ESG rating from MSCI having been recently upgraded to reflect its strong corporate governance and ethics. HRB is in the midst of its ESG transition and management is embracing it, using ESG tools to positively affect their business strategy. At the outset of the pandemic, its business model was negatively affected by changes to income tax filing deadlines by the IRS, resulting in revenues and expenses moving outside of historic quarterly patterns, whilst over a 12-month period, HRB's revenues are largely unaffected, as individuals still need to file taxes. Additionally, initiatives to increase customer retention and penetration into new markets, such as mobile banking (Spruce) and offering SMEs accounting, invoice, receipt-tracking, payment processing, payroll and other bookkeeping services via an app (Wave Financial).

TravelSky Technology Limited is the dominant provider of information technology solutions for China's aviation and travel industry, with a BB ESG rating from MSCI. Its core technologies are aviation services, enabling airlines, customers and agents to manage travel information, such as ticketing, baggage handling, accounting, settlement and clearing. Similar to its international peers these products and services are used by all industry participants, but unlike its peers it has a monopoly position in its home market of China. The stock has retreated due to the pandemic and continued uncertainties around air-travel and Covid-19 resurgence in 1H22. We believe negatives are now fully priced in, and with its growth potential in system integration, we expect air-travel demand to improve as 2022 progresses, causing the stock to re-rate.

Tandem Diabetes Care (TNDM) is a medical device company that manufactures, sells and supports insulin pump products, principally t:slim X2 which is able to receive software updates, unlike its peers, according to management. Its features enabling users to better manage their time in their targeted glycaemic range. It holds an AA ESG rating from MSCI, which puts it in the top 29% of Health Care Equipment & Supply companies in its sector. Although the industry has relatively lower carbon emissions risks, TNDM needs to set emission and reduction targets, and management is working towards setting them as part of their ESG journey. Its latest results were solid with revenue growth of 25% year-on-year, management did not raise its FY22 guidance, resulting in the stock selling-off in this value-orientated market. However, we remain optimistic on the long-term drivers for this stock and managements continued delivery, we will look to increase our position size over time.

Cognex Corp. (CGNX) specialises in machine vision technology, an area integral in factory automation. Its dominance in machine vision helps to support a very high level of profitability which we expect to continue due to its technological advantage. This advantage is sustained by a high level of R&D investment. From an end-market perspective demand remains strong for autos, EV batteries and consumer electronics, with factory automation playing a significant role in progressing climate change adaptation. It helps manufacturers speed-up production, reduce inefficiency and waste, lowering carbon intensity at factories. Cognex has been performing in line with many high-growth/high-multiple industrials over the last six months as supply chain pressures and likely lower demand from a major logistics customer is affecting sentiment. Unhelpfully, towards the end of the period there was a fire at a plant in Indonesia where a material portion of the company's finished and unfinished goods and component inventory was lost. While the fire will have a minimal impact on 2Q22 and management should be able to mitigate its impact over the next 6 months, it does present some execution risk. We intend to add to this position at an appropriate time.

Sample portfolio transactions

There were no transactions during the period.

The QQE perspective

Last quarter we noted that despite falling equity and bond prices and the uncertainty generated by the war in Ukraine, investors, by and large, remained confident in the resilience of the economic cycle. This was reflected in the superior performance of the People pillar of our proprietary Quality model. Our Quality model guides stock selection within our equity portfolios. It assigns a quality rank to each stock in a broad universe based on four pillars of Profitability, Persistence, Protection and People.

That confidence was evident through the second quarter as the People pillar continued to perform strongly at a time when Quality, as a style, was out of favour. Towards the end of the quarter, there was some evidence that investors were starting to lose faith in the economic cycle and starting to price in a recession. The most obvious sign was the rally in bonds late in the quarter while equities remained under pressure.

It will be interesting to follow the relative performances of the four pillars of our model in the months ahead as we go through another earnings season in which company managements will describe the current and future business environment. Uncertainty about future economic growth often tempts investors back into Quality companies that can deliver profitable growth for investors. It is this area of the market that we, as bottom-up investors, focus our attention.

Calendar year performance	2021 (%)	2020 (%)	2019 (%)	2018 (%)	2017 (%)
Davy Discovery Equity Fund (net of fees) (EUR)	27.5	9.9	32.9	-10.7	14.2
MSCI World SMID Cap Index (NTR, EUR)	25.6	6.2	29.2	-9.2	8.1
MSCI World Index (EUR)	31.1	6.3	30.0	-4.1	7.5
Endava PLC	118.8	64.7	93.0	-	-
Boliden AB	25.2	21.2	36.5	-28.5	20.4
Nemetschek SE	87.7	3.2	85.3	28.9	36.7
TravelSky Technology Limited	-29.8	0.5	-3.4	-13.4	45.4
Masco Corporation	-29.6	15.8	66.3	-32.7	40.5
Capcom Co Ltd	-18.2	123.6	41.6	23.0	32.7
H&R Block Inc	55.5	-27.8	-3.6	0.5	18.1
Gentex Corp	4.1	19.2	46.3	-1.7	8.4
Tandem Diabetes Care Inc	57.3	60.5	57.0	1508.9	-89.0
Cognex Corporation	-2.8	47.6	45.5	-36.5	92.9

Source: IQ EQ Fund Management (Ireland) Limited (Class A Acc Eur) and Bloomberg as at 31 December 2021. Performance is quoted in local currency unless otherwise stated.

Warning: Past performance is not a reliable guide to future performance. The value of the investment can reduce as well as increase and, therefore, the return on the investment will also be variable. Changes in exchange rates may have an adverse effect on the value price or income of the product.

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The Davy Discovery Equity Fund is a sub-fund of Davy Funds plc, an open-ended umbrella investment company with variable capital and segregated liability between sub-funds incorporated with limited liability under the Companies Acts 2014, authorised by the Central Bank of Ireland as an Undertaking for Collective Investment in Transferrable Securities (UCITS). The Prospectus, Supplement and Key Investor Document for the fund are available in English from Davy Global Fund Management, Davy House, 49 Dawson Street, Dublin 2, Ireland or https://iqeq.com/ucits. Investors should be aware that some of the Directors of the Company (Davy Funds plc) are also employed by the Investment Manager, Promoter and Distributor. Further information in relation to the management of potential conflicts of interest is available upon request.

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We are IQ-EQ, a leading investor services group employing over 4,000 people across 24 jurisdictions worldwide. We bring together that rare combination of global expertise with a deep understanding of the needs of our clients. We have the know how and the know you to support fund managers, global companies, family offices and private clients.

*Information correct as of 3 February 2022

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