

# IQ EQ Discovery Equity Fund

## For Investment Professionals Only

Performance	1 month %	Q3 2024 %	1 year %	3 years p.a. %	5 years p.a. %
IQ EQ Discovery Equity Fund <sup>1</sup> (net of fees)	1.54	5.65	12.73	-2.65	5.09
MSCI World Small & Mid Cap Index <sup>2</sup> (total return)	1.33	5.36	19.57	4.33	8.65

Source: IQ EQ Fund Management (Ireland) Limited (IQ EQ Discovery Equity Fund Class A Acc EUR) as at 30 September 2024.

<sup>1</sup>The IQ EQ Discovery Equity Fund (previously named the Davy Discovery Equity Fund) is a UCITS fund and was launched on 19 April 2013. On 1 May 2024 the Fund name was changed from Davy Discovery Equity Fund to IQ EQ Discovery Equity Fund.

<sup>2</sup>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 **IQ EQ 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

Global equity markets rose by 2.14% in the third quarter, taking the year-to-date return to 17.64% in euro terms as measured by the MSCI World Index (net). It was a relatively volatile quarter, with two periods of declines, one in early August, and another in early September. The August rout was sparked by poor earnings outlooks from semiconductor makers and extreme volatility in

Financial markets during July and August.

September's downward lurch was due, once again, to disappointing forecasts from large technology companies. However, equity markets recovered into the quarter-end on a 0.5% cut in interest rates from the US Federal Reserve ("the Fed") and hopes that the Fed would engineer a soft landing for the US economy, which had shown weakening labour market conditions during the quarter.

Interest rate-sensitive sectors such as Utilities and Financials were among the best performing sectors during the quarter as US interest rates declined in September. There was some evidence from data released during the month of cooling in the US labour market, which drove the move lower in interest rates. The benchmark US 10-year Treasury yield fell from 4.4% to 3.8% during the quarter.

Large technology shares underperformed

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during the quarter on those disappointing outlooks. Meanwhile, energy shares also weakened as the price of a barrel of Brent crude oil fell from \$85 to \$72 on the slowdown in US labour data and a cut in its forecast for global demand from OPEC.

## Fund performance

The **IQ EQ Discovery Equity Fund** returned 5.65% in the third quarter compared to its benchmark MSCI World SMID Index which returned 5.36%. This is an outperformance of 0.29% for the quarter, marking the second consecutive quarter of outperformance. Markets ended the period higher, but exhibited significant volatility, as investors reacted strongly to weak US jobs data for July and feared that the Federal Reserve (“the Fed”) had left it too late to cut interest rates, raising the risk of a “hard landing”. However, resilient corporate earnings and US retail sales, alongside a 50 basis point interest-rate cut, appeared to reassure investors as markets trended higher through September. The easing monetary policy has been a positive for smaller companies with Small and Mid-Caps outperforming their larger peers for the first time this year. The Fund’s performance over the period was driven by positive Stock Selection (Hamilton Lane, Vitrolife and Masco). Asset Allocation and Currency effects moderately detracted from performance. Our lack of holdings in Real Estate and Utilities had the largest negative impact as these sectors are rate-sensitive and particularly benefitted from easing monetary policy. On a regional basis, the Fund saw gains broadly across North America and Japan. Conversely, the UK, Europe ex UK and Asia ex Japan were the geographies with negative attribution. The Fund will continue to focus on key pillars of quality such as profitability and growth when looking for attractive companies.

The **top five equity** contributors to relative performance during the quarter were: Hamilton Lane Inc., Capcom Company Ltd., Vitrolife AB, Masco Corporation, and Rational AG.

The **bottom five equity detractors** from relative performance during the quarter were: Teradyne Inc., Aker BP ASA, Gentex Corporation, Pax Global Technologies Ltd., Burberry Group Plc.

**Hamilton Lane Inc. (“Hamilton Lane”)** is a private markets investment firm. Its clients are pension funds, financial firms, endowments, foundations, family offices, and private wealth. The investment case is about the secular demand for alternative investments in a firm that has greater earnings consistency, well positioned to capture growth in Alternatives given its broad scale, deep industry relationships, and turnkey solutions. Hamilton Lane posted a strong quarterly result to start its fiscal year. Management fees beat, largely on all of the different fee levels such as retroactive fees and performance fees, which offset higher incentive fee compensation, while fundraising was also above expectations.

**Capcom Co. Ltd. (“Capcom”)** is a Japanese producer and distributor of computer games, with franchises such as Resident Evil, Street Fighter and Monster Hunter World. Despite being one of the gaming industry’s original players, it still has some of the fastest growing intellectual property (“IP”) due to continual investment in its hit franchises. This has led to high earnings visibility and profitability, supporting its valuation. Despite having a softer pipeline of new games for FY2024, the market is anticipating solid growth from Capcom’s amusement equipment business and mobile game segments. Margins have been supported by a pick-up in sales of older games such as Resident Evil 2. Given that sales of these games require no new production investment, they are very profitable. Looking ahead, the stock has fared extremely well over the course of 2024 and its valuation currently reflects its high-quality characteristics of strong margins, free cash flow generation and low leverage.

**Teradyne Inc. (“Teradyne”)** is a supplier of automation test equipment for industrial applications and cobots (collaborative robots). Revenue growth in 2024-2026 is expected to be driven by semiconductor testing followed by robotics and LitePoint. The combination of Artificial Intelligence (“AI”) and hyperscalers is providing Teradyne with the best opportunity to grow volume and market share as it can differentiate itself through its ability to seamlessly take designs to testing stage. The company also announced a partnership with NVIDIA to introduce Generative AI (“GenAI”) into its robots which

could further drive revenue growth for the business. The share price has gained year to date, but underperformed last quarter as management delivered lower-than-expected guidance for 3Q24. We remain long-term believers in the stock, and our view is that the market is only starting to anticipate a recovery in the industrial cycle and a new product cycle in robotics in 2H24. Execution by management remains robust, delivering double digit operating margins and free cash flow margins.

**Aker BP ASA (“Aker”)** operates as an oil and gas exploration and production company, focusing on the Norwegian shelf. Additionally, it is the second-largest producer in Norway following its acquisition of Lundin Energy (original holding). It holds an AA rating with MSCI ESG as it has low carbon-emissions intensity coupled with robust decarbonization strategies. Unsurprisingly, its share price is correlated to oil prices, and the 18% decline year-to-date corresponds to a similar decline oil price. That said, its EBITDA margins are an impressive 90% and it is self-financing. In Q2 2024 this translated into Aker realising an average price of \$80 per barrel, \$3bn of EBITDA, and operating cash flow of \$1bn. Strong asset quality and low leverage, coupled with projects weighted towards the energy-transition, make us optimistic on the long-term prospects of the business.

## Sample portfolio transactions

We sold out of Keywords Studios plc following its acceptance of a £2bn offer to purchase the group from the Swedish private equity firm EQT Ventures.

## The QQE perspective

Our Quality model is comprised of four sub-pillars reflecting the attributes that we believe will drive long-term performance for our clients: Profitability, Persistence, Protection and People. The performances of the four pillars reflect investor preferences, which for most of 2024 have been for steady, consistent profits. However, in the third quarter our quality model underperformed, driven by the Information Technology sector, which underperformed. We noted at the end of the second quarter that investors were paying a premium for steady profit growth as reflected in the strong performance from our Persistence pillar, which has a high allocation to technology shares. We wrote at the time that there was little valuation support for the pillar if preferences changed. This trend went into reverse in the third quarter, with the People pillar performing strongest of the four. This pillar reflects companies that reward shareholders with capital repayments, including dividends. These shares fared well during the third quarter as interest rates fell. The performance of the People pillar is also symptomatic of an increase in market breadth, which is necessary if equity market performance is to be maintained into the end of the year.

Calendar year performance	2023 (%)	2022 (%)	2021 (%)	2020 (%)	2019 (%)
IQ EQ Discovery Equity Fund (net of fees)	9.4	-26.0	27.5	9.9	32.9
MSCI World SMID Cap Index (NTR, EUR)	11.7	-13.6	25.6	6.2	29.2
MSCI World Index (EUR)	19.6	-12.8	31.1	6.3	30.0
Aker BP ASA	5.7	19.0	31.5	-20.7	41.9
Burberry Group plc	-27.9	15.0	4.4	-18.8	30.0
Capcom Co. Inc.	9.7	57.8	-18.2	123.6	41.6
Gentex Corp.	21.8	-20.4	4.1	19.2	46.3
Hamilton Lane Inc.	81.3	-37.0	34.8	33.5	64.3
Keywords Studios plc	-38.9	-7.3	2.9	90.9	40.2
Masco Corporation	46.6	-32.1	29.6	15.8	66.3
Pax Global Technologies Ltd.	-4.2	28.1	-16.7	94.9	32.0
Rational AG	28.7	-37.2	19.0	7.4	46.9
Teradyne Inc.	24.8	-46.3	36.8	76.7	118.9
Vitrolife AB	5.0	-66.6	160.2	9.3	34.9

Source: IQ EQ Fund Management (Ireland) limited (IQ EQ Discovery Equity Fund Class A Acc EUR) and Bloomberg as at 30 September 2024. Performance is quoted in local currency unless otherwise stated.

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The IQ EQ Discovery Equity Fund (formerly the Davy Discovery Equity Fund – name change effective 1 May 2024) 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 IQ EQ Fund Management (Ireland) Limited, 5th Floor, 76 Sir John Rogerson’s Quay, Dublin Docklands, Dublin 2, D02 C9D0, Ireland or <https://www.iqeq.com/davy-funds-plc/>. 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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## About us\*

We are IQ-EQ, a leading investor services group employing over 5,000 people across 25 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.

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\*Information correct as of April 2024

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