Sustainable Growth – monthly bulletin

May 2023

In May, we saw the coronation of a new monarch here in the UK, and indeed one with his own high sustainability standards. According to *The Guardian*, King Charles' Aston Martin runs on a biofuel composed of surplus wine and cheese by-products. Unscalable as this quaint solution to the climate crisis is, it sets the tone from the very top regarding the importance of sustainability. As much as we would like to say that sustainability was the fuel for improved performance in the Sustainable Growth portfolio in the year so far, it is the 'growth' element that has bolstered returns of late. Some names most bruised by the market's aversion to growth stocks over the past 18 months have been back in vogue this year. That has supported double-digit returns in US dollar terms and a three per cent outperformance of the benchmark year-to-date.

May had little bearing on these numbers, with a modestly positive net-of-fees performance, a smidge ahead of our comparative index. However, growth stocks were certainly in favour, particularly those exposed to generative artificial intelligence (AI) technologies. Chief among these was the California-based designer of graphics processing units NVIDIA, whose shares were up 37 per cent in the month. NVIDIA's chips are well-suited to AI applications because of their ability to perform high-volume, low-complexity calculations in parallel. First-quarter results announced in May were pleasing, with revenues coming in ahead of expectations. But it was the outlook for the second quarter that showed how the company is thriving in a world of innumerable AI applications. Management guided for $11bn of revenue in the second quarter, a whopping $4bn higher than expected. We trimmed the position slightly as it had reached our 5 per cent limit for individual stock positions, but it remains a large holding, reflecting our enthusiasm for its position as a critical piece of infrastructure for this exciting new technology.

The Canadian ecommerce platform Shopify also saw its share price appreciate. The stock featured among the detractors from relative returns for much of 2022 owing to its committed approach to building for the future by investing heavily in a range of customer-pleasing features. Such approaches have been out of favour in an environment of rising interest rates. However, we were pleased to see strong results announced in May, with good growth in gross merchandise volumes driven by an increased take rate, the fees it receives for enabling third-party transactions. Interestingly, the company also announced it is withdrawing from its logistics business. The announcement described it as a 'side quest' that could distract from an emerging 'main quest'; features powered by generative AI. Shopify's personal assistant tool 'Shop' is an early example, allowing customers to discover products through conversation with an intelligent chatbot. Few companies have done a good job of curating content online so that customers buy products they were not initially searching for. This could be a change of course that unlocks many more increases in the Shopify take rate over the coming years, and founder Tobias Lütke has experience with these sorts of pivots, having previously adapted to a mobile-first offering at a rapid pace.

However, generative AI has not been a boon for digital education provider, Chegg. The company started in textbook rental services for US college students, and made a successful pivot of its own early in its life, moving online and providing bespoke tutoring services and access to banks of worked examples. The firm had a tough pandemic as courses were paused, and then it endured a long period of slow growth as enrolments failed to pick up post-lockdown. New tuition services such as Thinkful (coding) and Busuu (languages) helped, but our conviction in the sustainability hypothesis waned as we gathered evidence of students using the platform to cheat on coursework. We have engaged with the management team on this issue and were largely reassured by its response. However, this month the company conceded that ChatGPT was now impacting on new student sign-ups, with many opting to use OpenAI's free service to discuss and explain the complex topics covered in its degree courses. Chegg has announced chatbot functionality of its own in response, but it is still far from launching, and time is of the essence for a business that needs to completely replace its user base every three or four years. We fear the damage may have already been done, so we decided to sell our position.

Elsewhere, we sold two further holdings for reasons entirely unrelated to the dawn of AI. Twilio is a cloud communications platform that allows software developers to build communications features into apps, for example, the messaging service used by Uber. Although revenue growth has been impressive and the business has been scaling quickly, it has failed to show any evidence of increasing profitability. More importantly, we have growing concerns about the governance of the company. High levels of executive management change and excessive amounts of stock-based compensation have raised questions about culture. We are much less confident in the company's ability to execute profitably, and as a result, we have chosen to sell the investment from the portfolio.

We have similar concerns about growth at Cosmo Pharmaceuticals, an Italian biopharmaceutical company specialising in developing and manufacturing therapies for gastrointestinal diseases. Having been in the portfolio since 2016, we were attracted to its technology, which can deliver drugs direct to the large intestine instead of through absorption into the bloodstream. This technology was proven to have fewer side effects and is a lower-cost treatment than alternatives. However, growth has been unimpressive over the past few years. We think it is unlikely that the company will continue to deliver steady earnings growth over the long term and have sold our holding.

Proceeds of these sales were used to add to positions in eyewear retailer Warby Parker, which has just a sliver of the US market and lots of room for growth, as well as Google's parent company Alphabet, where we see many opportunities to deploy considerable knowledge and experience in AI.

The UK's coronation concert concluded with a spectacular drone display featuring a blue whale, a bumblebee and a butterfly, all set to Simple Minds' *Don't You (Forget About Me)*. A sustainable alternative to a fireworks display made possible by rapid advances in AI. A glimpse of a more sustainable, technology-led future, perhaps.

Performance

Annual past performance to 31 March each year (net %)

	2019	2020	2021	2022	2023
Sustainable Growth Composite	1.7	-5.0	107.1	-19.0	-20.8
MSCI ACWI	3.2	-10.8	55.3	7.7	-7.0

Annualised returns to 31 March 2023 (net %)

	1 Year	3 Years	5 Years	Since Inception*
Sustainable Growth Composite	-20.8	9.9	5.1	10.3
MSCI ACWI	-7.0	15.9	7.5	9.4

Annualised returns to 31 May 2023 (net %)

	Composite Net (%)	Benchmark (%)	Relative (%)
May 2023	0.1	-1	1.1
3 Months	1.4	3.6	-2.3
One Year	-2.8	1.4	-4.2
Three Years (p.a.)	-0.6	10.6	-11.2
Five Years (p.a.)	4.2	7.3	-3.1
Since Inception*	9.8	9.3	0.5

Source: StatPro, MSCI

Benchmark: MSCI ACWI Index

Based on the Sustainable Growth composite, in USD

Global Stewardship was renamed Sustainable Growth in 2023. *Inception date: 31/12/2015. Past performance is not a guide to future returns

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