

IA Clarington Inhance Global Small Cap SRI Fund

Manager commentary – Q3 2024

Global equities maintained the positive trajectory that started in early 2024, with the MSCI World Index gaining 9.0% in Canadian-dollar terms. Global small caps also posted positive returns but lagged large caps during the last 6 months (“the period”), with weak performance at the beginning of the period being partly offset by outperformance from July to September.

Despite a favourable backdrop, small-cap performance was hindered by the narrow breadth of the equity rally and higher sensitivity to interest-rate and macroeconomic sentiment, along with relatively weaker sales and earnings revisions (a change to the expectation of a company’s forecasted profitability).

Global equities experienced volatility, particularly in the latter part of the period amid a sell-off sparked by the unwinding of yen carry trades (involves borrowing money to invest, where the rate of interest on the borrowed amount is expected to be lower than the return on, or interest earned from, the securities purchased with the borrowed funds) by investors who used the low and stable interest-rate environment in Japan to raise capital for investment, as well as by concerns over a slowing economy and the response from the U.S. Federal Reserve (the Fed).

In September, the Fed joined other central banks in cutting interest rates, lowering its target federal funds rate (refers to the interest rate set by the U.S. Federal Reserve by 50 basis points).

The Fund’s stock selection in the information technology and real estate sectors contributed to performance. A lack of exposure to the energy sector also contributed as it was the only sector to produce a negative return over the period. The Fund’s overweight position in the real estate sector contributed as well. Individual contributors included Guidewire Software Inc., which performed well given strong quarterly reports in June and September, highlighting strong momentum within its core insurance carrier vertical software market (addresses a need for a specific industry), as well as strong margin improvement (increasing dollar revenue in relation to cost). Belimo Holding AG saw strong share-price momentum relative to European peers in building products and heating, ventilation and air conditioning. The company’s second-quarter results highlighted strong demand from data-centre customers related to the buildout of artificial intelligence infrastructure. Diploma PLC saw strong gains amid reassuring earnings releases, despite a relatively challenging macroeconomic environment for industrials companies.

The Fund’s stock selection in the consumer discretionary, health care, consumer staples and industrials sectors detracted from performance, particularly from companies that experienced outsized reactions

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to earnings reports and/or guidance cuts (the lowering of company's future growth objectives). The Fund's underweight position in the financials sector detracted from performance, as did its overweight position in the information technology sector. Individual detractors included children- and teen-focused discount retailer Five Below Inc., as shares weakened over the summer. The company cited acute pressure on its value (budget friendly) oriented consumers, merchandising missteps and the departure of its long-time CEO. Grocery Outlet Holding Corp. shares were weak, and lingering issues with enterprise resource planning and technology systems led to downward revisions for guidance. Stevanato Group SpA saw considerable weakness after first-quarter earnings results missed expectations and the company lowered its guidance for fiscal year 2024.

New positions included Topicus.com Inc. a smaller, European-focused replica of parent company, Constellation Software Inc., acquiring niche market software businesses. It offers a proven acquisition model with better risk/reward profile compared to most small- and mid-cap software companies. AddTech AB is a Swedish industrial acquirer focused on acquiring high-quality, founder-led manufacturing and infrastructure businesses. Watts Water Technologies Inc. is a leader in plumbing and drainage products, primarily tied to residential and commercial construction. About 60% of its sales come from repair and replacement work, providing more stable revenue than most of its building products peers. Tecan Group AG is a global leader in laboratory automation, serving the diagnostics and life science markets. The company's shift towards recurring revenue and margin expansion (Margin expansion refers to the increase in a company's profits) supports long-term growth potential. Brunello Cuccineli SpA stands out among luxury stock peers with strong growth driven by its focus on ultra-high-net-worth customers. The brand's sales are poised for continued growth off a relatively small base and should prove resilient.

Increased positions included Stevanato Group, Kinsale Capital Group Inc., Five Below, SiteOne Landscape Supply Inc., Grocery Outlet and Dino Polska SA, to take advantage of weak share prices.

Decreased positions included El.En S.p.A., Intertek Group PLC and Four Corners Property Trust Inc., with the proceeds redeployed into new or existing positions that showed better long-term growth potential relative to risk. Nova Ltd., Floor & Decor Holdings Inc., Belimo Holding, Guidewire Software and Diploma PLC were trimmed owing to extended valuations (a measurement of how much an investment is worth) or to take profits.

Eliminated positions included BlackLine Inc., a software company focused on accounting and finance departments of large and mid-sized companies. BlackLine Inc., is having challenges growing their cloud-based subscriptions, and there are concerns around slowing customer growth and declining net retention.

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Regarding Environmental, social and governance (ESG) engagement activities, Vancity Investment Management Ltd. (VCIM) held a call with Five Below to discuss the importance of living wages. The call was meant to ascertain the quality of their wage policy, if the policy is applicable to all employees, and if they have completed a cost-of-living analysis.

VCIM became a signatory of the 2024 Global Investor Statement to Governments on the Climate Crisis, which recently launched. This statement, coordinated by the Investor Agenda, urges governments worldwide to enact the critical policies needed to free up private financial flows for the just transition to a climate-resilient, nature-positive net-zero economy.

VCIM also became a founding signatory of the World Benchmarking Alliance's Investor Statement on Nature, which urges companies to assess and disclose their impact and dependencies on nature.

With a moderated inflationary environment (less pronounced rise in prices of goods and services) and cooling economic data, investor focus has shifted away from inflation and towards economic growth. Markets are expected to remain reactive to data that increases or decreases the probability that central banks can help achieve a "soft economic landing" (a cyclical slowdown in economic growth that ends without a period of outright recession).

The upcoming U.S. presidential election is of significant interest to investors. While some try to position portfolios around potential outcomes, it is difficult to say with any certainty what will happen, regardless of who wins. While volatility is likely to increase, the fund manager is not advocating for any changes to equity allocations. Looking back over the last 15 U.S. presidential elections, the average price return of the S&P 500 Index one year prior to the election and one year after the election has averaged about 9.6% and 8.8%, respectively.

While some risk and uncertainty remain around the U.S. election, future economic growth and geopolitical tensions, the current lower inflationary environment, monetary policy easing (the lowering of interest rates by central bankers) and positive forecasts for economic and earnings growth should support equities.

Fund and benchmark performance as at September 30, 2024	1-year	Since inception (Feb 2023)
IA Clarington Inhance Global Small Cap SRI Fund - Series A	12.6%	1.8%
MSCI World Small Cap Index (CAD) ¹	25.4%	10.9%

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For definitions of technical terms in this piece, please visit iaclarington.com/glossary and speak with your financial advisor.

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The performance data comparison presented is intended to illustrate the Fund's historical performance as compared with historical performance of widely quoted market indices. There are various important differences that may exist between the Fund and the stated indices that may affect the performance of each. The Fund's benchmark, The MSCI World Small Cap Index (CAD) captures small cap representation across 23 Developed Markets (DM) countries. With 4,139 constituents, the index covers approximately 14% of the free float-adjusted market capitalization in each country. The Fund holds securities of companies which meet the fund manager's socially responsible investment principles, while the holdings in the benchmark may not align with these principles. The Fund's market capitalization, geographic and sector exposure may differ from that of the benchmark. The Fund's currency risk exposure may be different than that of the benchmark. The Fund may hold cash while the benchmark does not. It is not possible to invest directly in market indices. The performance comparison is for illustrative purposes only and does not imply future performance.

Indicated mutual fund rates of return include changes in share or unit value and reinvestment of all dividends or distributions and do not take into account sales, redemption, distribution or optional charges or income taxes payable by any securityholder that would have reduced returns. Returns are historical annual compounded total returns.

A mutual fund's "yield" refers to income generated by securities held in the fund's portfolio and does not represent the return of or level of income paid out by the fund.

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