QUARTERLY INVESTMENT REVIEW

Quality Investment Fund

PRODUCT OVERVIEW

The GMO Quality Investment 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.

ANNUALIZED RETURNS (%, QUARTER-END)

	Quarter-End	YTD	1-Year	3-Year	5-Year	10-Year	Since Inception
Quality Investment Fund (net)	5.58	21.14	35.15	12.85	16.44	14.16	14.04
MSCI World	6.36	18.86	32.43	9.08	13.04	10.07	10.21
Value Add vs. MSCI World	-0.79	+2.28	+2.72	+3.77	+3.40	+4.09	+3.83

ANNUAL RETURNS (%, PRIOR 10 YEARS)

	2023	2022	2021	2020	2019	2018	2017	2016	2015	2014
Quality Investment Fund (net)	29.04	-15.56	25.53	17.49	30.40	0.00	28.02	9.05	1.01	11.98
MSCI World	23.79	-18.14	21.82	15.90	27.67	-8.71	22.40	7.51	-0.87	4.94
Value Add vs. MSCI World	+5.26	+2.58	+3.72	+1.59	+2.73	+8.71	+5.62	+1.54	+1.88	+7.05

Inception Date: 10-Nov-10

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KEY CONTRIBUTORS AND DETRACTORS

For several quarters, investors have debated the size of a potential recession. The third quarter saw minor sell-offs and a brief but significant one in Japanese stock markets. Despite this, global equities had a fourth consecutive positive quarter, with the MSCI World returning 6.4%. The Quality portfolio slightly underperformed this benchmark, making up ground during sell-offs but faring less well when Nvidia, the S&P 500, and Growth stocks were buoyant. Essentially, the Quality portfolio provided relative protection during market volatility.

There was a shift in market drivers, with Growth stocks underperforming for the first time in several quarters. NASDAQ's growth slowed compared to that of broader markets. Sectors likely to benefit from falling rates, such as Utilities and Real Estate, performed well, with Financials and Industrials also doing well. These dynamics were reflected in the Quality portfolio's performance: Quality Growth stocks underperformed, while Quality Core and Quality Value stocks had better returns. Not holding utility or real estate companies, which historically have been tricky to find high-quality companies in, hurt relative performance.

PORTFOLIO REVIEW

This quarter, we reclassified Oracle and SAP from Quality Core to Quality Growth due to their successful embrace of cloud computing. Oracle's infrastructure addresses cloud security and speeds up AI model training, making it the largest contributor to relative returns. SAP's software aids clients' cloud transitions with re-engineered code for effective deployment.

On the downside, our semiconductor positions suffered in the tech/growth sell-off. However, we took this opportunity to invest in ASML, a leader in lithography essential for high-powered semiconductor manufacturing used in AI, 5G, and more. Additionally, our investment in TSMC, a key semiconductor manufacturer for companies like Apple and Nvidia, boosted returns.

MARKET OVERVIEW

The Magnificent 7 have significantly influenced markets, with many of these companies classified as Quality Growth. Currently, 40% of our portfolio is in Quality Growth, with the rest in Quality Core and Quality Value. After years of strong performance by growth stocks, especially in the US, we have evaluated whether 40% is the proper allocation. Our steady allocation to Quality Growth has reflected significant profit-taking over the years. For example, at the end of 2016, the portfolio had 18.5% in Microsoft, Alphabet, and Apple. Without trading, this would now be 37.5%, but we currently hold around 15%. We have reduced our allocation to big growth when the market presented good opportunities to do so.

INVESTMENT OUTLOOK

Today, there's a clear divide in valuations between defensive consumer staples in Core Quality and dynamic companies in Quality Growth. Defensive staples like Nestle and Diageo are trading at their lowest relative valuations in a decade, making them attractively priced. We've also been buying more Haleon from Pfizer as it reduces its stake. These staples have strong fundamentals and the potential for revaluation gains.

Quality Growth companies have the potential for higher returns over time but need to justify their higher current valuations. As Growth stocks have outperformed, we've gradually sold some, making our portfolio's returns more correlated with Value indices than Growth indices this year. Looking ahead, we aim to maintain a diversified portfolio with investments across different categories of Quality businesses, keeping an eye on valuation to ensure balance.

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IMPORTANT INFORMATION

Comparator Index(es): 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.The S&P 500 (Net) Index is an independently maintained and widely published index comprised of U.S. large capitalization stocks. The return reflects the dividend reinvestment after the deduction of withholding tax. 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.

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Investors and potential investors can also obtain the prospectus and key investor information, in English and other languages, and a summary of investor rights and information on access to collective redress mechanisms at the following website: https://www.gmo.com/europe/product-index-page/equities/quality-strategy/quality-investment-fund---dqf/

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