Evenlode Global Income Investment View

February 2025 – Results and evolving themes

Equity markets continue to move upward into 2025, albeit with a change in leadership from the US to Europe. We expounded on the valuation picture for global markets focused on the US in last month's investment view[i], along with an analysis of performance of the portfolio in 2024. Given the further general upward movement, that analysis still stands at the market level, but there have been some shifts in the underlying tone that we'll highlight below.

Before that we can get into some detail of what's going on at a business level in the portfolio as we're about two-thirds of the way through the annual corporate reporting season. Ever fascinating as a sign of the economic times, we have more than a smattering of geopolitical interest to add into the mix at the moment. Company reports cut through to what is happening on the ground, so we'll focus on that here across a few different sectors.

Business Services

Demand from professionals for software and data-driven solutions is robust if results from RELX and Experian are anything to go by. RELX's risk business continues to grow strongly, but interestingly in the current AI context, the mature segments of Science, Technology & Medicine (STM) and Legal are experiencing higher growth rates than in recent years. RELX's Lexis Protégé is a legal AI personal assistant, and in STM three AI tools were launched in 2024. One, ClinicalKey AI, helps physicians quickly search for information on complex cases from curated content from journals, textbooks and clinical overviews, an understandable use of the technology. It's early days for these add-ons but they do seem to be helping with the top line as well as likely cementing the business' strong competitive position.

However, in industry, discretionary spending has somewhat stalled. IT consultancy and outsourcer Capgemini reported that business demand is mainly about efficiency programmes rather than investments in expansion. Where there is demand, AI is the number one area of spending, followed by cyber security, certainly a sign of the times. For the year just gone there was an improvement in bookings in the fourth quarter, but revenue growth is forecast to be relatively muted in 2025 all the same. In a similar line of business US-listed Accenture did see an improvement in the final quarter of the calendar year (its first fiscal quarter), with less exposure to industrials likely to be helpful compared to Capgemini and the Communications, Media and Technology segment recovering spending after a post-covid slump.

Health Care

Characterised as a slow and steady sector, Health Care is showing the merits of solid demand and service delivery through innovation and efficiency. Pharmaceutical companies Roche and GSK posted high single digit revenue growth. Sanofi was ahead in the double digits as its blockbuster autoimmune disease therapy Dupixent continued to gather pace, as well as other launches and a solid showing in its vaccines business. Lab services providers Quest Diagnostics and Sonic Healthcare are now out of the coronavirus testing boom and the subsequent impact on cost structures, with cash generation improving in excess of solid sales growth. Eyewear giant EssilorLuxottica half falls into the Health Care sector with its vision correction and professional optician business. Its Stellest myopia treatment lenses are seeing strong take-up with sales increasing +50% in China.

Health Care is a sector where we see good value in the market and decent dividend yields[ii] with prospects for growth, a triumvirate that is difficult to find in many sectors at present.

Consumer

Dampened consumer sentiment around the world continued into the fourth quarter of 2024, with revenue growth for consumer goods companies slowing to the low single digits on average in the portfolio. At the weaker end were the alcoholic beverage businesses with six-month revenues up marginally for Diageo and down a little for Pernod Ricard. Destocking trends are persisting, although there are some signs of stabilisation with Diageo expecting a sequential improvement in the first half of the calendar year (second half of the company's fiscal year). For Pernod, volumes are improving, but revenues declined due to the mix of products being sold, a trend expected to continue in the short term before stabilising in the coming year. Interestingly Europe is proving relatively resilient in sales terms, something also seen at cosmetics market leader L'Oréal. Whilst slowing down through the year sales from the Old Continent were still up +5% in the final quarter. North American revenues increased only slightly and those from Asia declined, led by China. Brighter spots at other businesses included Unilever's turnaround which seems to be bearing fruit, with the company posting consistent revenue growth across geographies and segments led by its Beauty & Wellbeing division. Encouragingly this is led by volumes, with a lesser contribution from price increases. However, the sudden departure of CEO Hein Schumacher indicates that the company believes this performance could be even better. He has been replaced by well-regarded CFO Fernando Fernandez, who we have met as CFO and will engage with in due course to find out more about his further plans for the business.

Spending on items at the more discretionary end of consumer purchases was mixed. Luxury conglomerate LVMH grew sales marginally in the year and the fourth quarter was more resilient than many feared. Again, spending in Europe held up relatively well, while in China it was weak. In a completely different consumer area, bicycle components maker Shimano seems to be emerging from the volatility of demand seen through the coronavirus pandemic. The company is expecting to return to trend growth rates and China was unusually strong for bike sales last year in the context of a consumer recession, with Europe a drag. This is expected to reverse this year, with the important European market returning to growth and coming more into line with the fast-moving consumer goods companies in geographic terms. The other half of EssilorLuxottica, which is mainly a consumer goods business in the form of sunglasses, experienced strong growth in its Sunglass Hut franchise and its Europe, Middle East and Africa segment has grown for 15 quarters. The market has got very excited about the prospects for its tie up with Meta for their smart glasses range which has seen strong demand. We think this is a good opportunity for the business, but the valuation of the company does look relatively rich now and we have reduced the fund's position accordingly.

Information Technology

The hot sector of the day, one of the biggest investment questions *du jour* is whether the benefits of and, ultimately, value derived from AI will meet the hype. It's a big question because big sums of money are being poured into the development and delivery AI tools, and big market values are being placed onto those companies deemed to be in the AI sphere. Business service companies Wolters Kluwer, RELX and Publicis have been brought into the AI orbit in market valuation terms. As noted above there are some signs that revenue growth rates are increasing as a result of delivering AI tools to customers. We are not AI sceptics but do think that the market is putting a reasonably full value on these business' enhanced prospects, so we have reduced position sizes to reflect that view.

In terms of pure IT players Microsoft is the most significant holding in the portfolio. It is one of the big spenders of capital on AI model and service development, and also on related cloud service infrastructure along with the other 'hyperscale' providers such as Alphabet (Google). As investors, we're keen to see growth in revenue and profitability come through as a result of this spending, but equally understand that technology adoption takes time despite the rapid pace at which the world seems to turn in the 2020s. Microsoft's revenue growth is impressive, up +12% organically in the final quarter of 2025, but is not yet correlated with the large increase in spending; we keep a watching brief on this. Networking kit and security provider Cisco has found favour in the market reflecting its role in data infrastructure rollout. After a choppy couple of years where demand for its hardware surged and then waned as customers installed the surplus kit they ordered, it has seen sequential improvements in sales and orders.

Evolving market themes

The movement of equity markets around themes is as old as the markets themselves but seems even more so at the current time. Over the last two years, AI improved prospects for banks in the rising rate environment, and stellar sales of weight loss drugs have been dominant in moving the market. Over the last two months these themes have been joined by a recovery in Consumer Staples and a reawakening of Health Care as some of the resilience and, perhaps, valuation appeal in these sectors shows through. Geopolitically the outlook for defence spending in Europe and the US is a big theme, as are the prospects for oil and gas prices as the US administration works on domestic production and arresting conflict in Europe and the Middle East.

The US administration is clearly the biggest current affairs story of the time and is certainly making waves when it comes to international diplomacy and trade. We're not alone in wondering where it all goes and how to distinguish signal from noise in a 'flood the zone' era of policy blitzkrieg. So, we double our focus and attention on corporate performance and valuations, whilst keeping an open ear for news that might materially affect portfolio companies and the wider universe of businesses that meet our criteria. Healthy margins, cash flow and return on capital do a lot to protect companies from what might be more stormy seas, but we continue to assess whether the economic walls are likely to be breached. So far in this results season those fundamentals remain intact in the portfolio, but with a patchy demand picture from both consumers and industry.

Ben P, Chris E, Rob, Ben A, Phoebe and the Evenlode team

25 February 2025

Evenlode has developed a Glossary to assist investors to better understand commonly used terms.

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Market data is from S&P CapIQ, Bloomberg and FE Analytics unless otherwise stated.

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[i] *Reflections on 2024*

[ii] *Dividend Yield – A Dividend is a payment made by a company to shareholders. Dividend yield is calculated by dividing the dividend per share by the current share price.*