Global Growth Commentary

Q2 2021

SGA
Sustainable Growth Advisers

Performance

SGA's Global Growth portfolio returned 7.3% (gross) and 7.1% (net) in Q2 versus 7.4% for the MSCI All Country World Index (ACWI) and 10.0% for the All Country World Growth Index (ACWI Growth).

Highlights

- The rebound in cyclical stocks moderated in Q2 with growth outperforming at the end of the quarter; business quality metrics were rewarded marginally.
- The portfolio trailed its MSCI All Country World Index benchmark with stock selection detracting from relative returns and sector weights benefiting results.
- Stock selection in the Consumer Discretionary sector accounted for much of the underperformance due to significant weakness in New Oriental Education; selection in Financials, Consumer Staples, and Information Technology also detracted, while selection in Industrials, Health Care, and Real Estate benefited the results.
- New positions were initiated in Japanese job search company Recruit and Latin American e-commerce leader MercadoLibre, and the portfolio's position in Kansas City Southern was liquidated.
- The portfolio is positioned in our highest confidence and most attractively valued long-term secular growth opportunities; the portfolio remained overweight the Information Technology and Consumer Discretionary sectors.

Global Recovery Facing Risks

Global equity markets rose sharply with investors betting on a broadening of the global economic recovery as vaccination programs advanced. This outlook, however, faced a growing headwind during the quarter as the more transmissible Delta variant of the COVID-19 virus spread quickly across the globe leading to new restrictions in many countries including India, Thailand, Japan, Australia, and Singapore. While optimism continued in Q2, investors also exercised a bit more caution given the variant threat, concerns over increasing inflationary pressures, rising tax rates, and higher regulatory costs in the U.S. Investors may also be recognizing the largest fall off in fiscal accommodation since World War II and questioning whether this could derail or slow the global economic recovery. This caution led to a change in leadership in the markets with the appetite for cyclicals declining in favor of some higher growth businesses.

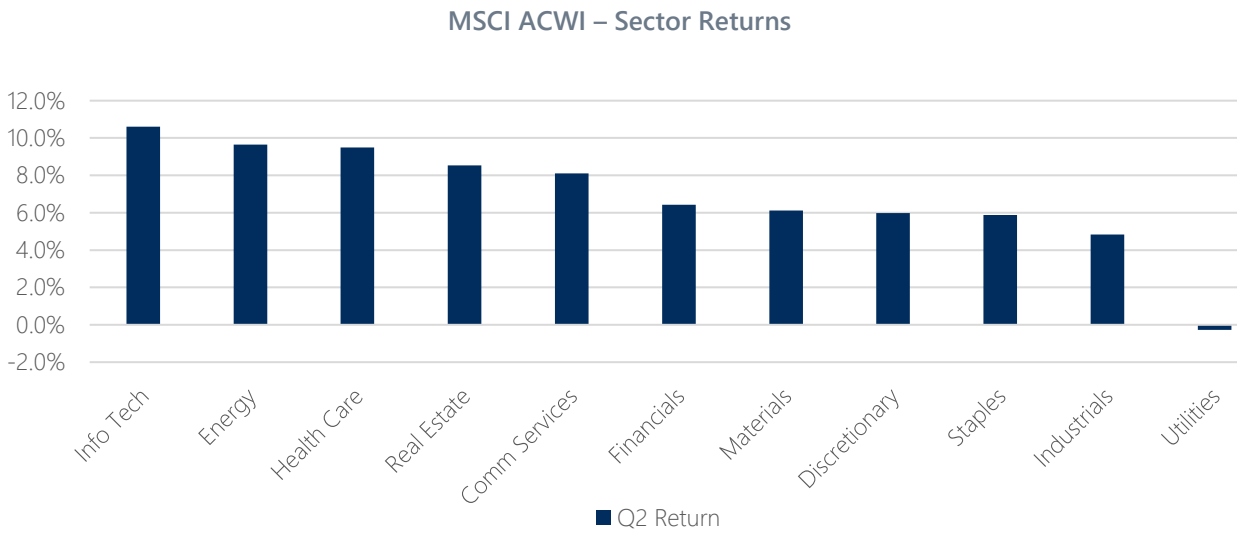
Key Change in China

More news emerged on the trend toward greater Chinese regulation of industry, as China attempts to moderate the power of companies that have either become too dominant in the eyes of the Chinese regulators or are perceived as posing a threat to the Communist Party's image or agenda. Steps had already been taken by the government to weaken Alibaba and Ant Financial, and to restrict foreign capital from supporting excessive profiteering at the expense of local consumers and businesses. During the quarter, this more adversarial and ideological approach by the Chinese government severely impacted the private education industry, with new regulations pending which are expected to adversely affect the market opportunity in the area. The new willingness of the Chinese government to tightly control the operations of businesses, and limit the access to foreign capital is changing the investment landscape in China to a greater degree than anything seen since Premier Deng Xiaoping opened the country to entrepreneurship and foreign capital in the 1980s.

Today's more activist and adversarial approach to the regulation of China's enterprises, especially those listed overseas, and new access to foreign capital heightens the unique risks associated with investing in Chinese companies. Investors must now assess whether businesses and their shareholder bases are viewed as central to advancing the Communist Party's agenda or represent a potential threat. As we research Chinese companies and evaluate their fit within our strategy, we will continue to focus on whether the predictability and sustainability of growth meets our high bar given the evolving risks.

Market Attribution

With greater focus on the impact of the Delta variant on economic recovery, developed markets broadly outperformed emerging markets despite strength in emerging Latin America and Europe. Brazil and Poland generated the best returns (+22.9% and +18.7% respectively) for the period while Chile, Egypt, and Peru performed the worst with returns of -14.2%, -9.2%, and -8.8% respectively. Asian markets in general were among the weakest performers with China returning only +2.3% as investor unease rose with greater government involvement and Japan returning -0.3% as new COVID cases emerged. In this environment, large caps outperformed small caps, and growth outperformed value. Business quality metrics were rewarded marginally with low debt, high ROE, and companies with earnings outperforming. Leadership in the market broadened during the quarter with the Information Technology sector performing best followed by the Energy, Health Care, Real Estate, and Communication Services sectors. Utilities generated the weakest returns followed by Industrials, Consumer Staples, and Consumer Discretionary.

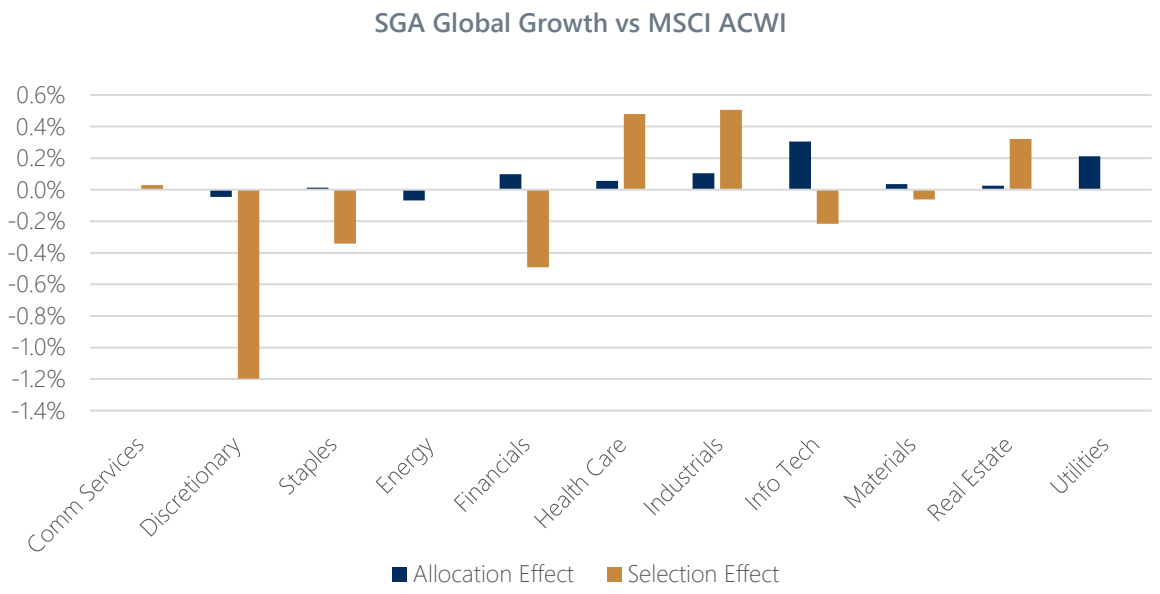


Source: MSCI

Portfolio Attribution

Stock selection detracted from portfolio returns during the quarter due primarily to selection in Consumer Discretionary where the position in New Oriental Education continued to weaken given ongoing concern over new regulatory steps by the Chinese government. Selection in the Financials and Consumer Staples sectors also detracted due to weakness in HDFC Bank and CP All given the terrible impact of the Delta variant in India and Thailand during the period. Positive stock selection in Industrials, Health Care, and Real Estate helped to partially offset the weakness given strong returns from IHS Markit, Kansas City Southern, Novo Nordisk, Intuitive Surgical, and Equinix. Sector allocations contributed positively to relative returns with the portfolio's overweight in the strongly performing Information Technology sector and lack of exposure to the poorly performing Utilities sector having the largest impact. Underweights in the underperforming Industrials and Financials sectors also contributed positively.

The portfolio's overweight in emerging markets relative to the index penalized results during the quarter while selection in the non-U.S. developed and U.S. markets contributed positively. Relatively high vaccination rates in the U.S. and improving rates in Europe together with the expectation that economies in Europe would reopen soon benefited performance in those regions.



Source: FactSet, MSCI

Largest Contributors

Novo Nordisk, a global leader in the treatment of diabetes, was the largest contributor to returns in Q2, as the company's growth accelerated. Multiple new product launches and good execution enabled them to raise 2021 guidance to 6-10% constant currency sales growth and 5-9% operating profit growth. Strong market growth for its injectable diabetes drug franchises in the GLP-1 category seems sustainable given the very positive clinical data supporting the category growth, limited competition, and low global penetration. Novo Nordisk has multiple products in the GLP-1 category, and we are enthusiastic about the longevity of growth for the company, although we are cognizant that the launch of Rybelsus, a new oral formulation in the GLP-1 category, was hindered by the pandemic. Novo Nordisk is also launching a new obesity drug Wegovy this year and is in a strong position to help address the problems of diabetes and obesity through its products. We maintained an average weight position in the portfolio during the quarter.

Internet search leader **Alphabet** was the second largest contributor to performance during the quarter with its shares benefiting from a better-than-expected earnings report. Revenues grew 34% compared to the same period last year on the back of impressive results for its Search business, which rose over 30%. Operating profits and free cash flows rose 80% and 150% respectively, while its cloud segment maintained an impressive 46% growth rate. The company's share repurchase authorization was also increased to $50 billion. We continue to be impressed by the company's execution and growth potential, but remain cognizant of valuation and the rising regulatory risks. We maintained an average weight position during the quarter, trimming on recent strength.

Leading global data center provider **Equinix** was the third largest contributor to performance during the quarter after a strong report showed revenues, earnings, and adjusted funds from operations up 10%, 13%, and 17% year-over-year respectively. Bookings remained strong in North America with low client churn. While the stock was negatively impacted by rising inflationary expectations earlier in the year, some of that may have been an overreaction. The inflation they are seeing is tied to construction costs (such as for lumber) which appear to be transitory in nature. S&P's upgrade of their debt will provide additional buffer to any higher interest rates while also enabling the company more flexibility in its financing. We continue to see attractive growth opportunities for Equinix over our 3-5-year investment horizon and maintained an average weight position in the company while taking some profits on strength.

The fourth and fifth largest contributors to performance were **PayPal** and **Facebook.**

Largest Detractors

New Oriental Education (EDU) was the largest detractor from portfolio performance in Q2. At the beginning of the quarter the company reported strong operating results for Q1 with revenues and enrollment up by 29% and 43% respectively, on a year-over-year basis. The company also provided solid guidance looking forward. However, since that time the stock has been negatively impacted by speculation over the content of new policies and regulations aimed at promoting educational quality and reducing the cost burden on parents of having more children given China's worrying demographic trends. Guidelines approved during the quarter by Chairman Xi call for reducing in-school burden, improving in-school teaching quality, extending school services post-teaching hours, and tightening regulation of after-school tutoring licensing, advertisement, operations, and cash management. Xi also focused on reducing the amount of capital chasing "excessive" profits and the additional anxiety for parents. Final regulations supporting these new guidelines have been pending for weeks, creating considerable speculation in the markets which has led to significant weakness in the stock.

A belief that the Chinese leadership would approach the issue of education quality and regulation from a practical standpoint as opposed to an ideological standpoint was central to our thesis for EDU and our rational for maintaining the position during this period of speculation. We have conducted man overboard drills during the quarter aimed at evaluating and reconfirming our thesis for the business. Based on these reviews, we believed that the government would prefer to see the private education industry heavily regulated to ensure that participants were providing a quality service at a fair price. While the company's profit margins may be impacted, we had expected that the changes would still allow for attractive (albeit more moderate) growth. Further, our view was the demand for tutoring services would be resilient because it has been driven by China's college entry level testing system which was unlikely to change. And, significantly curtailing the provision of tutoring services would only drive tutoring demand underground making it less subject to effective government regulation and potentially more expensive for parents, working against the purposes of the new guidelines approved by Xi.

Today we see a more extreme ideological approach is more likely and such a draconian view is reflected in the stock's price, which is trading significantly below its 52 week high. While the valuation of the stock appears quite attractive considering the company has 60% of its current stock price in cash, the sustainability and predictability of EDU's profit growth has become highly uncertain and we are reevaluating our thesis.

Thai convenience retailer **CP All** was the second largest detractor from performance for the quarter as the company continued to be impacted by closures due to the effects from a second wave of the pandemic in Thailand. Strength at the company's Makro unit was more than offset by weakness at its 7-Eleven and Tesco/Lotus units. With uncertainty over the path of the COVID-19 flare up in Thailand, we lowered our same store sales and gross margin forecasts for the year but expect costs to also come in lower, offsetting some of the impact. While the story is difficult at the moment given the uncertainties around the progress of the pandemic and vaccinations, we continue to see an attractive growth opportunity for CP All in a post-pandemic world. As the Thai economy rebounds and begins to benefit again from renewed growth in the country's middle class and tourism over our 3-5 year investment horizon growth will resume. Despite the impact of COVID-19 in the second quarter, the country has not changed its plan to open for tourism and has recently been formulating plans for how to support it. We expect these moves to benefit the company as they will improve store traffic. We maintained an average weight position in the company during the quarter.

Media and entertainment company **Disney** was the third largest detractor from performance for the quarter trailing other more cyclically oriented stocks. The company reported mixed Q1 results, falling short of optimistic expectations on the part of some investors. Streaming subscriber growth was lower than expected as a result of lighter content due to reduced production during the COVID-19 shutdowns. We expect subscriber growth to accelerate as content productivity ramps back up. At the same time, profits and free cash flow were better than we had expected and Disney has seen attractive demand at its theme parks which have reopened with operating margins exceeding historical levels. Given an improving economic backdrop mixed with some continued uncertainty over the course of the pandemic and new variants, we increased our position in the company to average weight.

The fourth and fifth largest detractors from performance were **FleetCor** and **HDFC Bank**

Portfolio Activity

Turnover during the quarter was average with new positions in MercadoLibre and Recruit being initiated and the remainder of the portfolio's position in Kansas City Southern being liquidated. Additionally, we trimmed positions in Linde, Equinix, Abbott, Alphabet, HDFC Bank, IHS Markit, and Microsoft. Capital was reallocated to our new positions as well in Tencent, Disney, HDFC Bank, and Workday among others.

New Positions

Latin American e-commerce leader **MercadoLibre** was reintroduced to the portfolio in Q2. The company reported strong Q1 results highlighted by strong revenue growth and a return to profitability following Q4's holiday period loss. MercadoLibre continued to capitalize on its improving fulfillment and logistics, with 48-hour deliveries rising from 53% in Q1 2020 to 74% at the end of Q1 2021, illustrating the strength of their position and the reduced competitive threat they may face from Amazon or other omni-channel retailers. Given its strong position in the key emerging FINTech segment and its dominant position in the under-penetrated e-commerce segment in Latin America, we see MercadoLibre as offering the long-duration growth that we seek. E-commerce comprises about 7-8% of Latin American retail today and is expected to grow 15-20% annually over the next 3-5 years. We expect the FINTech market to grow faster than that given that large segments of the population are un-banked or under-banked by a legacy and oligopolistic banking system that charges high fees with outdated service models. MercadoLibre's attractive position in e-commerce is expected to continue to be supported by inefficiencies in traditional Latin American retail which highlight the company's cost and selection value propositions. Additionally, we see the company's Mercado Pagos payment offering becoming the "AliPay" of Latin America, with low take rates on transactions and mandatory adoption on the MercadoLibre retail platform. Overall, we expect the company's disruptive presence in retail and finance to benefit from its low-cost value proposition, which continues to resonate with consumers in the developing economies of Latin America, driving consistent unit share gains, revenue generation, and cash flow. We have great confidence in the company's management team which has proven to be exceptionally stable and consistent in its execution.

Among the key risks we will continue to monitor with MercadoLibre are the success of its competition, the political and currency risks inherent in Latin American investments; regulatory risks related to the internet, e-commerce, and financial technology; and the pace of inevitable growth deceleration over time; and its valuation given much of MercadoLibre's value lies in the out years and estimates are likely to fluctuate widely causing periodic volatility in the stock's market valuation.

Given the stock's high growth rate and our understanding of the risks and opportunities it presents, we initiated a below average weight position in the company and plan to build the position over time taking advantage of volatility.

Japanese media company **Recruit** owns job search engine Indeed.com as well as a variety of other online media and staffing businesses. Indeed is the largest job-focused search engine in the world with over 250 million monthly unique visitors in over 60 countries. The firm's business incorporates a Media & Solutions segment that includes non-staffing Human Resources related functions and classified platforms in Japan, while its Staffing segment includes both Japanese and overseas staffing businesses. Recruit also owns a 39% stake in 51job, a leading online recruiting and HR services platform in China. Indeed benefits from a dominant market share in the mass-market job search field, as well as the difficulty a competitor would face trying to reproduce its service workforce. It also has significant market share in each of its top six Media & Solutions platforms with large scale advantage in Japan. Given its leading market position, the firm has established a reputation for reliability with employers leading to repeat customers and recurring revenues. Our research indicates a strong runway for growth at the firm given the opportunity for both new customers and price increases in the U.S. online hiring market, international growth, and the ability of the firm to gain market share in its Media & Solutions business from offline newspapers.

Among the risks we are monitoring for Recruit are the potential for some level of cyclicality in the staffing, classifieds, and online job advertising businesses. We also need to monitor Indeed's competition from LinkedIn and Google which, to date, have not substantially impacted its business but compete with it for users to some degree. Finally, while the company has a strong track record in its M&A, we want to be sure management is appropriately focused on its existing businesses.

We initiated a below average weight position in the company and plan to build it opportunistically.

Sold Positions

The remainder of the portfolio's position in **Kansas City Southern** was liquidated after significant price appreciation caused its valuation to become less attractive following multiple acquisition offers.

Summary

The reopening rebound continued in Q2 with markets moving up sharply, but the nature of the rebound evolved with growth as a style regaining its leadership for the period, and investors' appetite for risk seeming to moderate with large-caps outperforming small-caps and quality metrics benefiting to a degree. While market trends became more beneficial for our approach during the period, the portfolio's holding in Chinese private education leader New Oriental Education cost about -1.75% in relative return, more than offsetting any of the benefits from selection elsewhere. A broader, more adversarial and ideologically driven approach to regulation and foreign capital infusion became more apparent in China raising the risk associated with investment in the country. This heightened regulation will require investment opportunities to meet an even higher bar for predictability and sustainability of sales in addition to assessing their fit within the new ideological agenda of the Chinese Communist Party.

We continue to expect elevated volatility in equity markets as expectations surrounding the pace of vaccinations, the reopening of economies and new threats posed by COVID variants fluctuate. In addition, speculation regarding the transitory, or not, nature of inflation in the U.S., rising taxes and regulation in the U.S., and myriad geopolitical threats make more volatility likely in a market which has priced in high expectations. In this environment, our disciplined focus on predictable and sustainable growth businesses that we can access at attractive cash flow based valuations should lead us to businesses that can continue to succeed regardless of the economic or regulatory backdrop. While relative results will vary from quarter-to-quarter, we remain confident that our time-tested approach and stable investment team will produce above average revenue and earnings growth which should lead to strong long-term absolute and relative returns over our 3-5 year investment horizon.

Thank you for your continued confidence in our team at SGA. We look forward to answering any questions you may have about the portfolio or our positioning.

Sustainability Report

Q2 2021

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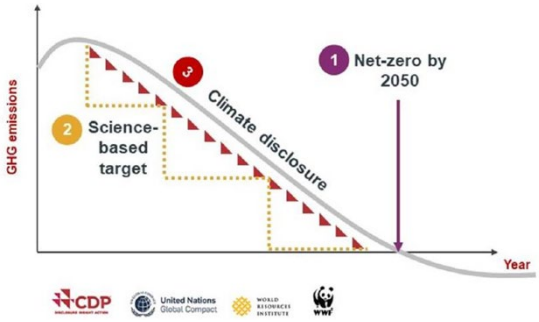
Science-Based Targets: A Firm Priority

Science-Based Targets (SBTs) provide a pathway for companies to meet the goals of the Paris Agreement by developing interim greenhouse gas reduction targets to bridge the gap between the present day and long-term targets. We believe SBTs can provoke real and immediate action, increasing the priority of climate action efforts to management teams and Boards across the globe. At present, a minority of the companies on our Qualified Company List have approved SBTs. We are actively encouraging our portfolio companies to adopt SBTs and are seeing an increasing number of companies commit to setting SBTs in the near-term.

While we conduct the majority of our engagement efforts on a standalone basis, we recognize the effectiveness that collaborating with peers on certain issues can have. As such, we seek to selectively join forces with other organizations to support important ESG causes. For example, in addition to our direct engagement with companies on emissions reduction commitments, we recently joined the Carbon Disclosure Project's 2021 Science-Based Targets Campaign. The goal of the campaign is to create a positive ambition loop between investors and companies that incentivizes companies to set SBTs and accelerates the decarbonization of investment portfolios. The campaign has the support of over 130 investors representing approximately USD 19 trillion in assets.

SBTs on the Path to Net-Zero



Source: CDP

Engagement Highlights:

Regeneron Pharmaceuticals is an American biotechnology company which researches, develops and manufactures medicines to treat a wide array of conditions including eye disease, allergic and inflammatory diseases, cancer, cardiovascular and metabolic diseases. We have owned shares in Regeneron in client portfolios for a number of years with our growth thesis resting in the breadth and depth of the company's drug pipeline, enabled by their proprietary R&D and intellectual property.

Corporate governance of the firm presents a potential risk to our growth thesis; the company maintains a dual-class share structure and has a number of long-serving directors. This may increase the risk of undue deference to management and be detrimental to minority shareholders. This being said, senior management holds significant equity in the company which helps to align interests with shareholders. We have maintained engagement with management over a number of years on these issues, providing our feedback on ways to enhance corporate governance at the company.

Recently, the company adopted a new compensation policy for members of their Executive Committee including CEO Leonard Schleifer and CSO George Yancopoulos. The new policy replaced annual stock options with a grant of front-loaded performance-restricted stock units (PSUs). We are broadly comfortable with the structure of the PSUs which are aligned to long-term Total Shareholder Returns, something we have long advocated for. However, we hold concerns over the magnitude and timing of the awards. Typically, we would voice our concerns through a Say on Pay vote; Regeneron however, holds Say on Pay votes every three years with the next vote not due until 2023.

Hence, we took the opportunity to engage with management regarding the new compensation package and reiterate our concerns regarding items previously discussed including succession planning and tenure of the Board, and voiced our preference for an annual election of Directors and Say on Pay vote. While we understand that the nature of their business requires long-term planning for long-term success, we do not think an annual election and Say on Pay vote will necessarily interfere with those goals. Following discussions with management, our Investment Committee reviewed the engagement and decided it is in the best interests of our clients to vote against the re-election of Director and Compensation Committee member George Sing.

During the quarter we also engaged management on the topic of GHG emissions. Given the nature of the company's operations and relatively low carbon footprint, this has not been an area of high-priority for management. However, we believe the establishment of Science Based Targets ("SBTs") and Net Zero commitments is an important discipline for all companies to pursue, and we are systematically engaging with all companies on our Qualified Company List in this regard. In the case of Regeneron, management has pledged to establish SBTs by 2023 and we expect a Net Zero target to follow. During our meeting with the company we emphasized the importance of these targets and encouraged an acceleration of work to establish a Net Zero goal. Management was very receptive to our feedback and interested to learn about our priorities as stewards of capital.

We have maintained our existing holdings in the company and continue to closely monitor and engage with management on best governance and environmental practices.

Given our approach to investing in companies that can sustainably grow and compound their earnings over the long-term, the average SGA company has a relatively small carbon footprint. When analysing the carbon risk of our portfolios, we prioritise companies with high emissions relative to our Qualified Company List. Along with Linde, Amazon and Kansas City Southern, Thai convenience store operator **CP All** has one of the larger emissions profiles as per MSCI.

CP All is the sole operator of the 7-11 franchise in Thailand with over 10,000 branches. The MSCI analysis is based on carbon footprint per unit of investment. However, in countries like Thailand where the same dollar goes much further, the MSCI analysis fails to capture this. For the same level of investment, one could be operating many more stores in Thailand than in a country like the US. Therefore, it is natural to have a larger carbon footprint. Ideally, one would adjust the data by the purchase price parity and then compare across businesses. That said, over the long term, most companies are committed to Net Zero targets, including CP All.

Management has set an ambitious target of carbon neutral operations by 2030 and publishes detailed information on its environmental footprint, marking its leadership in environmentally sustainable growth in the Emerging Markets. The company's efforts have been recognised by the Carbon Disclosure Project with an A- score.

We engaged with management recently on the subject of their environmental targets in conjunction with long-term growth plans. While procuring renewable energy in markets such as Thailand is challenging compared to Developed Markets, management is working to maximise the resources available to them. Accordingly, the company is investing in solar-based electricity generation projects leveraging their national store and distribution network. At the store level, the company is investing in more energy-efficient air conditioning systems, lighting systems and equipment. Reduction of plastic waste is also a focus as the company moves to natural and biodegradable materials.

While it is early days, we believe management has credible carbon risk management plans (which continue to evolve) and given the relatively low absolute GHG emissions, we do not believe carbon risk poses a significant threat to our growth thesis in the company. We continue to monitor developments in this space.

During a recent meeting with the management of **Visa**, we probed a variety of ESG-related topics including the company's recently issued Net Zero targets, development of Science Based Targets, diversity and inclusion, compensation, employee retention and sponsorship of the Beijing 2022 Olympics. Pleasingly, Visa has committed to achieving net-zero emissions by 2040 and has joined The Climate Pledge, an initiative co-founded by Amazon to accelerate action towards a net-zero world. The company has also announced plans to develop SBTs to define short- and intermediate-term targets. The emissions of Visa's supplier operations are one of the largest obstacles to achieving carbon neutrality however management is confident they will achieve their goals by 2040, if not before.

An increasing trend we are witnessing is the alignment of executive compensation to ESG targets.

Visa made mention of changes made to the calculation of executive compensation as it relates to ESG factors in recent corporate filings, but the disclosure was more limited than we would have preferred. However, after speaking with the company's Senior Counsel overseeing Compensation and Benefits, we were pleased to learn that the ESG weighting within

the calculation for annual executive compensation increased to 25%. Long-term compensation however remains based on Total Shareholder Returns (TSR). Given the long-duration of ESG factors, we raised the suggestion of embedding ESG into the company's long-term incentive plans. While we believe aligning short-term incentives to ESG can create a greater sense of urgency, we also believe there is value in aligning long-term incentives to serve the company's stakeholders more broadly. This is an area we continue to analyse as a team, and have flagged this as an area for future engagement with management of Visa and other portfolio companies.

Proxy Voting Summary Q2 2021

	Number of Resolutions	For	%	Against	%	Abstain	%
U.S.	313	288	92%	24	8%	1	<1%
Global	304	281	92%	22	7%	1	<1%
International	286	272	95%	12	4%	2	<1%
Emerging Markets	167	139	83%	28	17%	NIL	0
Global Mid-Cap	244	228	93%	13	5%	3	1%

Source: SGA, Broadridge

Carbon Risk

	Carbon Emissions[1]	Total Carbon Emissions[2]	Carbon Intensity[3]	Weighted Average Carbon Intensity[3]
SGA Global Growth	12.2	12,221	76.3	56.1
MSCI ACWI	90	89,951	205.8	150.8
SGA Relative Performance	-86%	-86%	-63%	-63%
SGA U.S. Large Cap Growth	10.8	10,791	75.1	67.4
Russell 1000 Growth	9.6	9,618	61.6	33.6
SGA Relative Performance	13%	12%	22%	101%
SGA Emerging Markets Growth	19.2	19,203	54.9	53.2
MSCI EM	213.8	213,753	411.3	279.9
SGA Relative Performance	-91%	-91%	-87%	-81%
SGA International Growth	19	18,975	79.4	76.7
MSCI ACWI ex-USA	148.1	148,073	236.0	185.7
SGA Relative Performance	-87%	-87%	-66%	-59%

Source: SGA, MSCI

[1]Tons of CO_2 emitted/ $M invested

[2]Tons of CO_2 emitted

[3]Tons of CO_2 emitted/ $M sales