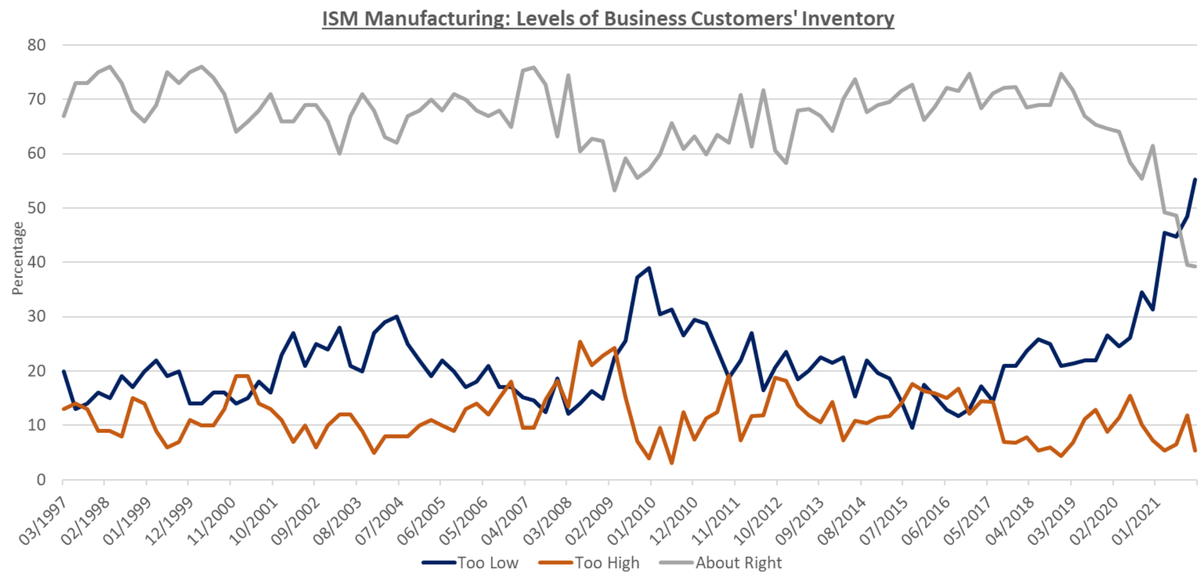
"It is better to sleep on things beforehand than lie awake on them afterwards" - Baltaser Gracián

The rapid spread across the globe of the Omicron variant meant that the usual December rally in equity markets did not emerge until the week before Christmas. However, despite UK travellers being banned from travel to France and Germany, throwing many a winter ski holiday into disarray, few global governments were prepared to cancel Christmas for the second year in succession, and investors finished the year with festive cheer and a more upbeat perspective on the forthcoming year.

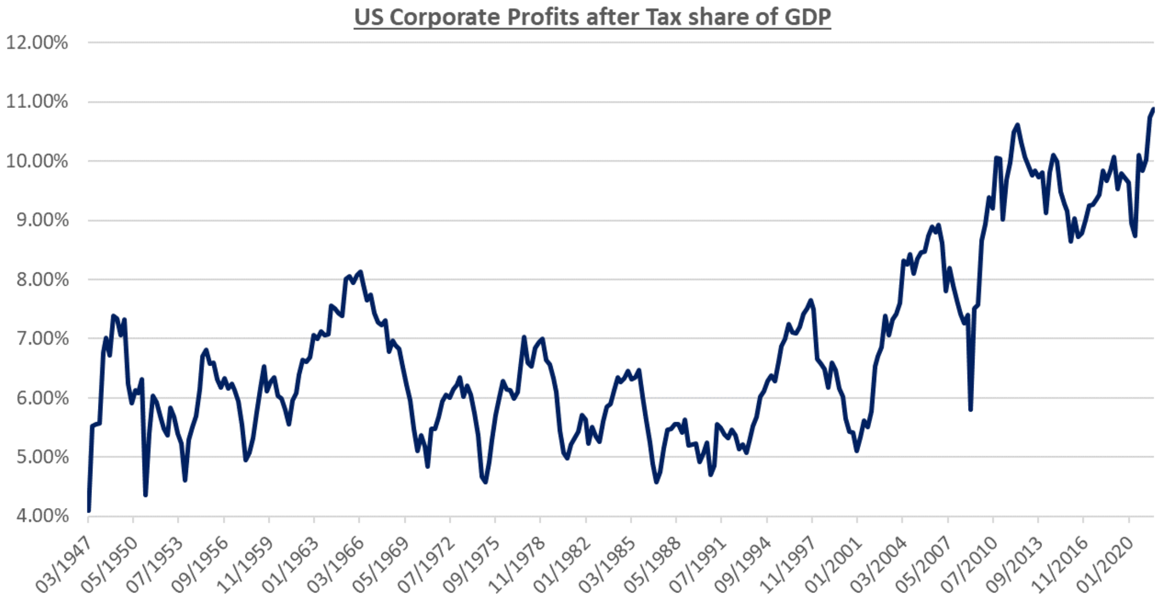
Across the Atlantic, the anticipated $1.75 trillion Biden social spending bill & climate package appears unlikely to reach the White House desk for the President's signature after the Senate Majority Leader, Chuck Schumer, announced that he was not going to support the bill. Given the 50-50 split in the Senate one vote against party lines can make or break much of the Biden agenda, and in the November mid-term the administration may well see itself lose control of the Senate (14 of the 50 Democrat seats are up for election) and possibly the House, where it holds a five-seat majority.

In recent communications we have argued that many companies will start 2022 with better visibility than most have seen for multiple years, given the pent-up demand seen during the back end of 2021. These orders are just as much of a factor of record levels of demand as the well documented shortage of supply caused by the multitude of constraints experienced since the summer months. With inventory levels at record lows, we expect that companies are likely to be unwilling to risk running balance sheets with such low stock levels again for the foreseeable future and therefore demand for raw materials and components will remain higher for longer.



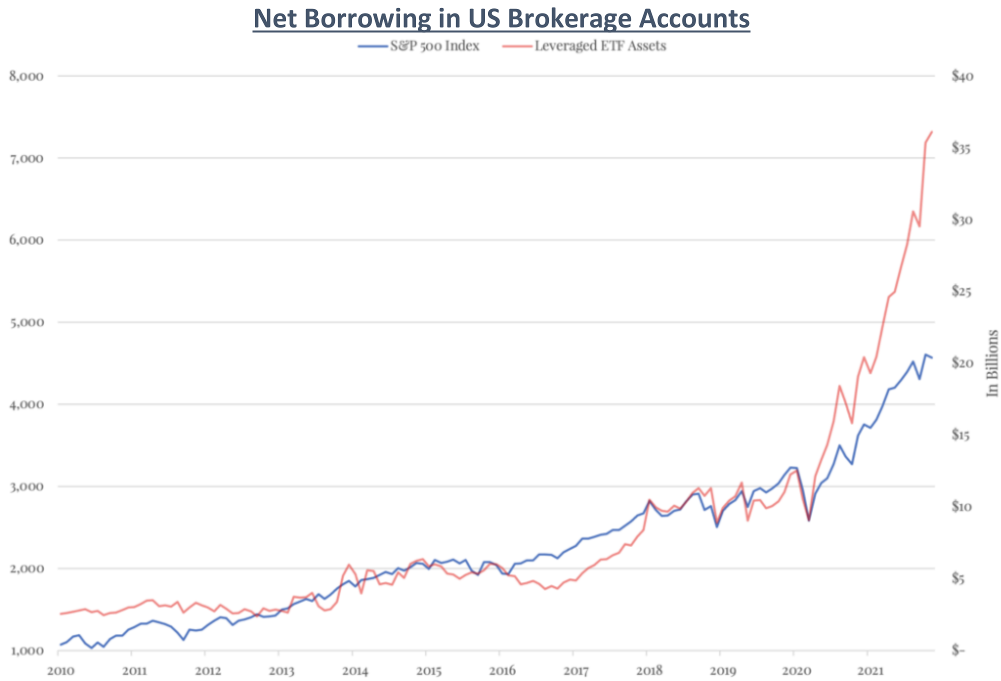
Source: TIM/Institute for Supply Management

We also note that, despite all the raw material headwinds and input cost inflation, company profit levels are close to the post WW2 highs, when quarterly data started to be reported, while after-tax profitability are at all time highs; prior to WW2 the data was annual and the previous post-tax high was 9.1% in 1929. This would suggest that price increases are being passed through by many companies and given the level of companies talking about implementing price increases, and in many cases warning that the rate of increase of input costs has led to a lag effect, there is scope for this profitability to remain elevated in the next couple of quarters.



Source: TIM/US Bureau of Economic Analysis

One of our concerns going into 2022 is the level of leverage present in brokerage accounts as investors seek to benefit from the rise in equity markets since the depths of the pandemic. This is occurring at a time when Insider selling is also at multi-year highs, which is concerning as one would like to think that CEOs and CFO's have a better understanding of the outlook for their industries than speculative investors.



Source: The Felder Report

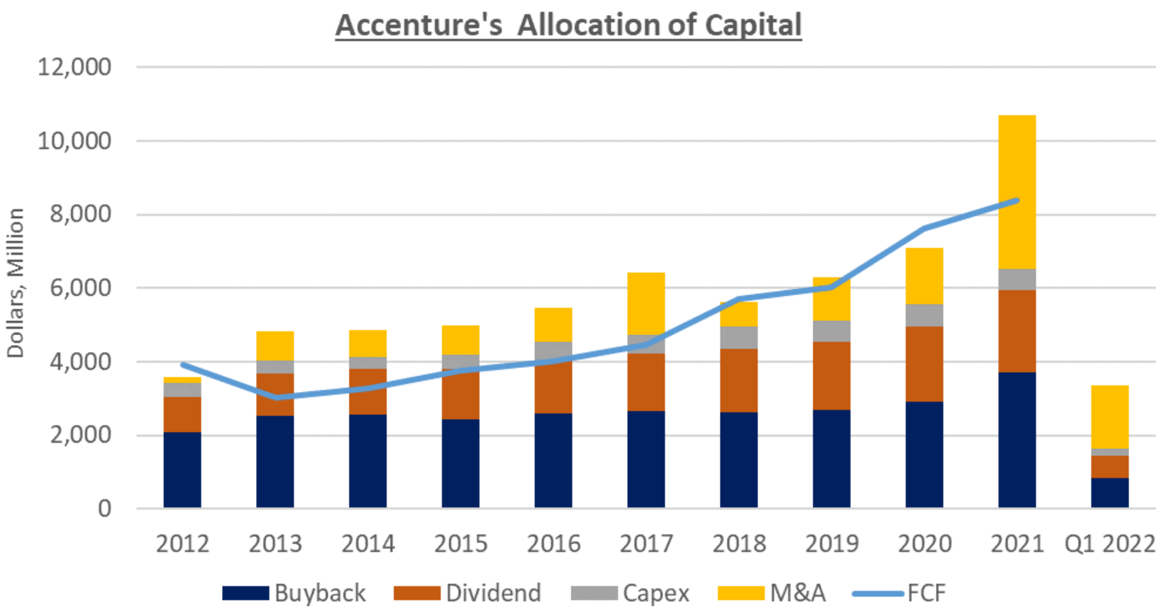
As cautious investors, we are concerned that excess leverage has a well-documented history of ending badly. Common sense investing is a key mantra of the Fund, and therefore we do not adopt of policy of momentum investing and try to avoid heuristic tendencies by focussing on the long-term fundamentals of the companies in which we invest or look to invest in; as Warren Buffet famously remarked, "only when the tide goes out do you discover who's been swimming naked".

For the 16th month in succession Global equities managed to mark a new all-time high during the month and the Fund followed suit. The VT Tyndall Global Select Fund B Acc (GBP) rose 2.51% during the month, bringing the year-to-date returns to 21.76%.

Fund Activity and News

A little over five years ago we initiated a position in the consulting business, Accenture, in the Fund, and during this time it has more than quadrupled in value on a total return basis. Despite being the largest player in its field Accenture is growing three times faster than the industry average through robust organic growth of 7-9%, supplemented by multiple bolt-on acquisitions to add to its ever-expanding skill set.

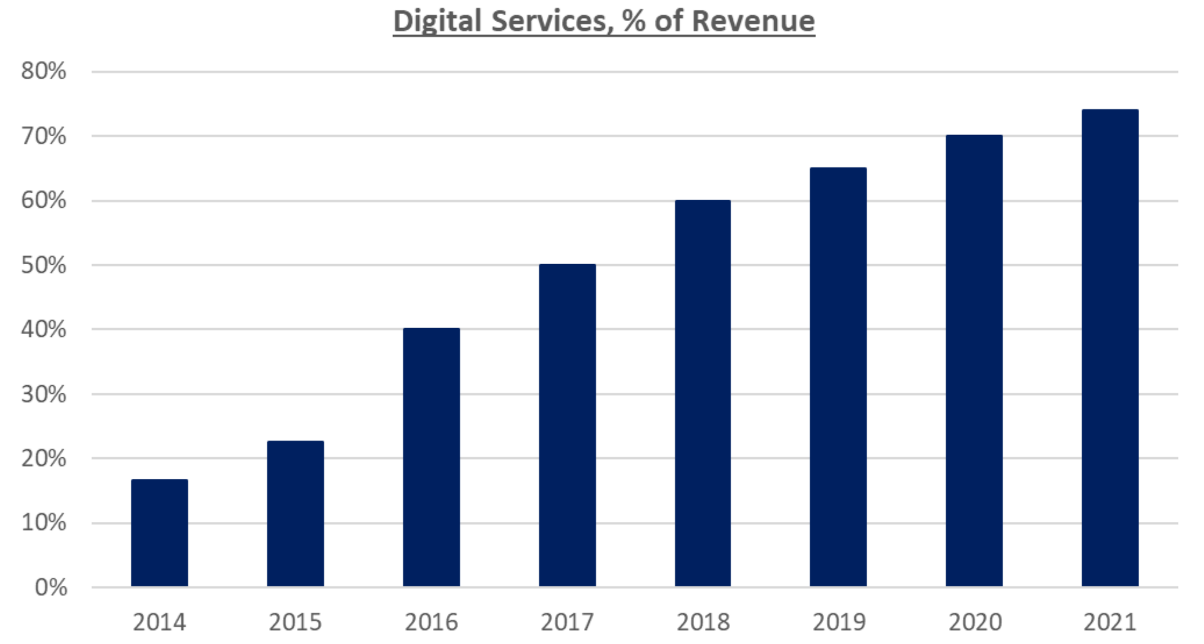
This month the company released its latest earnings update where it increased its full-year forecasts based on strong growth of more than 15% across all its verticals, an impressive $16.8bn of new bookings and $349bn of free cash flow in the quarter. Over the past 10 years Accenture has spent 1/3rd of its cash on investment and returned 2/3rds to shareholders through dividends and buybacks whilst maintaining a net cash balance sheet with net debt/EBITDA of -0.7x.



Source: TIM/ Redburn/ Company Reports

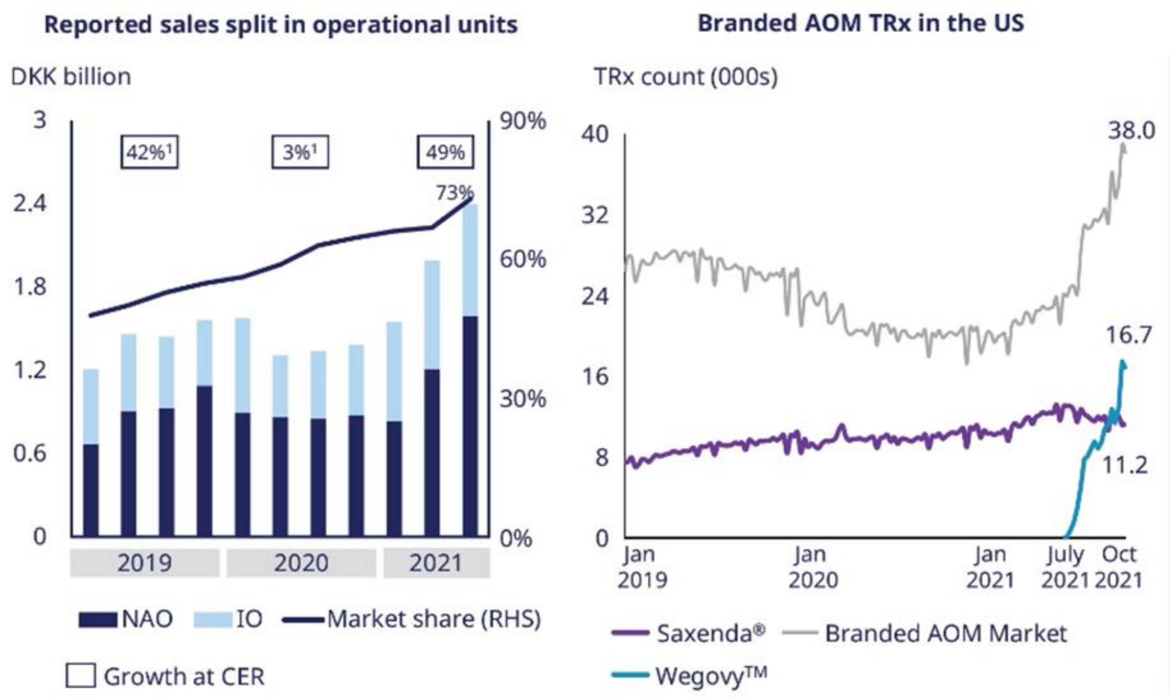
The management guidance for 2022 is for $7.7-8.2 billion of Free Cash Flow, with $4bn spent on acquisitions, and capital return of $6.3bn through dividends and share repurchases. We expect that the Free Cash Flow number may be raised further, as the company has increased operating margins, and Free Cash Flow has a record of easily exceeding net income, every year for over 15 years.

One of the competitive advantages of the company is its reputation and capability to offer an end-to-end service offering for its clients from consulting to systems integration and maintenance. The proactive management means that Accenture has been at the forefront of the world of digital transformation and is now the provider of choice for companies seeking to implement a digital strategy. Digital services are growing at double digit rates and now accounts for well over 70% of group revenues.



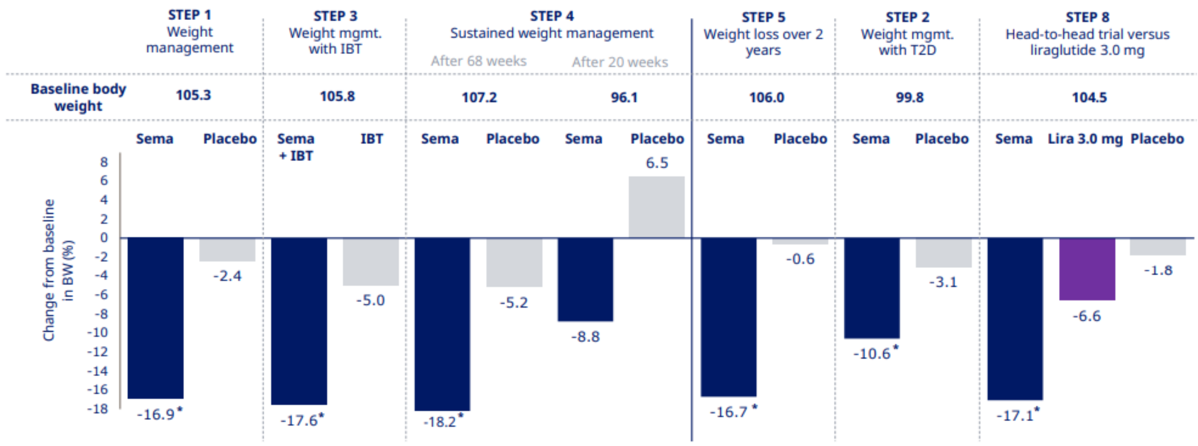
Source: TIM/ Company Reports

On the other end of the performance spectrum, our holding in Novo Nordisk disappointed this month. After the positive trials and distribution of its new obesity drug, Wegovy, the shares had made a 79% return from April to mid-December. The efficacy of Wegovy is such that Novo already has double the patients than it has for its previous drug, Saxenda.



Source: Novo Nordisk 30/09/21

The obesity market is even larger than that for diabetes (463m people) with an estimated 650m people suffering from the condition, yet only 2% are medically treated, so as the clear market leader, the opportunity for Novo Nordisk is huge. Obesity currently costs the global medical system $1 trillion per year and this is expected to increase by 20% over the next five years, so the benefit of prescribing treatment is compelling. As yet, the once weekly Wegovy semaglutide injection is only approved in the US, while Saxenda has approval in both the EU and the US, however submissions are in for the EU and Japan.



Source: Novo Nordisk

Unfortunately, this month the contact manufacturer (CMO) that Novo Nordisk uses for filling its vials received current good manufacturing practice (cGMP) notification from the FDA for one of its factories in Europe, and as such has stopped deliveries and manufacturing until the issue is resolved. Although Novo Nordisk has other production sites due to come online next year, global capacity will be temporarily reduced by 60-90% so the timing is rather unfortunate. The consequence is that Novo Nordisk will have to focus its efforts on supplying existing patients and restrict expansion plans until the cGMP issue is rectified and other facilities come online.

Novo Nordisk believe that the CMO in question needs to replace some equipment and undergo re-validating, which should be straightforward as long as it can ensure supply of the spare parts. After this, the company must undertake a couple of investigations in quality management systems, so Novo Nordisk has delayed its expectations to meet US demand to H2 2022.

Despite this set back, Obesity remains a significant opportunity in the short, medium and long term and from 2023 the supply situation should be more diverse and enable Novo Nordisk's growth trajectory in this field to resume. We have held a position in the company for over 11 years and through extensive research and development the company remains the leader in diabetes treatment which like obesity has a large and growing unmet demand, so the investment case remains as strong now, as it did in early 2011.

Richard Scrope, Fund Manager, VT Global Select Fund, 31st December 2021
Data source (unless otherwise stated): Bloomberg.

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