Jackson Square Partners International Growth

COMMENTARY | 09/30/21

PHILOSOPHY

We believe that attractive returns can be realized by maintaining a concentrated portfolio of companies that we believe have enhanced business models, strong cash flows, and the opportunity to generate consistent, long-term growth of intrinsic business value.

AVERAGE ANNUAL TOTAL RETURNS (PERIODS ENDED 09/30/21)

	3Q21	Since inception 12/31/20
Jackson Square International Growth Composite (*Gross*)	-3.13	5.36
Jackson Square International Growth Composite (*Net)*	-3.32	4.74
MSCI ACWI ex USA (benchmark)	-2.99	5.90

Source: Jackson Square, MSCI ACWI ex USA Index

Past performance is not indicative of future returns. Investing involves risk, including possible loss of principal.

MARKET REVIEW

COVID-19 continued to be a driving factor in market volatility in the third quarter. The Delta variant forced companies across industries and geographies to reassess forecasts for the second half of the year as the timing and breadth of re-opening became increasingly less certain. This uncertainty drove broad underperformance in healthcare names, while continued supply chain issues and inflation uncertainty plagued the consumer discretionary sector. Inflation fears spiked at the end of the quarter, weighing on long-duration growth names, which underperformed after having made up some ground relative to the value rotation that has largely dominated 2021. In addition to these concerns, the breadth and depth of Beijing’s intervention in the Chinese economy accelerated, furthering that market’s selloff. The markets remain focused on near-term catalysts and are seemingly awaiting further evidence of economic recovery to assign credit to longer-term trends of fundamental performance.

CONTRIBUTORS & DETRACTORS (PERIOD ENDED 09/30/21)

Top contributors relative to the benchmark	
Atlassian Corp. Plc Class A	Information Technology
Sartorius Stedim Biotech SA	Health Care
Recruit Holdings Co., Ltd.	Industrials
Stevanato Group SpA	Health Care
Adyen NV	Information Technology

Top detractors relative to the benchmark	
Bilibili, Inc. Sponsored ADR Class Z	Communication Services
Wix.com Ltd.	Information Technology
StoneCo Ltd. Class A	Information Technology
Farfetch Limited Class A	Consumer Discretionary
Fiverr International Ltd.	Consumer Discretionary

Strategy Review

For the third quarter of 2021 the International Growth Portfolio underperformed its benchmark, the MSCI All Country World Index ex USA. While performance was largely driven by our stock exposure, on a sector level, communication services were the largest detractor and health care was the largest contributor to performance.

TOP CONTRIBUTORS AND DETRACTORS

Contributors

Atlassian Corp. Plc Class A, an enterprise software company focused on productivity and workflow management, was a contributor to performance during the quarter. The company reported strong growth in its subscription business following the end of permanent on-premise software license sales in its prior quarter. Subscription growth was above 50% compared to company guidance of mid 30s. This reflects the early success of Atlassian's business model shift and highlights the potential for accelerating revenue and expanding margins as the company laps the end of life of license sales. We believe Atlassian is very well positioned for a cloud-based world and will have a much greater ability to create enterprise specific products and effectively upsell its wide range of customers over the next few years.

Sartorius Stedim Biotech SA, a provider of equipment and consumables for the manufacture of biopharmaceutical drugs, was a contributor to performance during the quarter. Stedim reported exceptional 2Q21 results that exceeded Street expectations for sales and EBITDA by 5% and 9%, respectively. Consequently, Stedim raised 2021 guidance, which is now expected to be 24% and 45% ahead of Street expectations for sales and EBITDA, respectively, as compared to estimates at the beginning of the year. Despite Stedim's outperformance, we remain excited about the long-term risk/reward profile given the expected secular growth for biopharmaceutical drugs and Stedim's strong competitive positioning.

Recruit Holdings Co., Ltd., a provider of HR and business technology and staffing services, was additive to performance during the quarter. The company reported blowout FQ1 earnings in August and subsequently raised their full year revenue guidance by 5% and Adjusted EBITDA by 30% as their HR Technology segment is seeing incredible demand for hiring. In the quarter, HR Technology, which includes Indeed and Glassdoor, saw revenue increase 148.9% with Adjusted EBITDA margins reaching 37.7%, the highest in company history by over 1400 bps. While these margins are likely to decrease over the course of the year as Recruit continues to invest behind ongoing international expansion, we believe it highlights the powerful model of the business and where margins may be headed over the coming years. The media and solutions and staffing segments also saw strong rebounds from COVID-impaired comparables a year ago despite some continued covid headwinds in Japan and other international markets.

Detractors

Bilibili, Inc. Sponsored ADR Class Z, a popular video entertainment platform in China, performed poorly in Q3 2021 amid regulatory pressure in China. We think Bilibili is positioned favorably relative to its technology peers due to its size and domain. With regard to youth gaming, it has taken proactive steps to monitor and collaborate with the government. Bilibili has also diversified revenue streams with advertising and live streaming. Lastly, third party data shows Bilibili's monthly active users trend is weaker than usual post summer. This has been true for all major Chinese internet platforms in China and isn't a Bilibili specific issue. We continue to believe there is a sustainable runway for growth in both users and revenues and that the company will continue to evolve into the dominant user-generated video content platform in the Chinese internet sector.

Wix.com Ltd., a cloud-based web development platform, reversed strong year-to-date performance after the company reduced its 2021 guidance. The company, like most other internet businesses, saw weakness in demand in the last few weeks of the quarter. Despite the temporary moderation of demand, we are impressed by the implied continued strong levels of growth. Longer–term, we believe the opportunity remains attractive, due in part to the fact that there are over 400 million small and medium size businesses in the company's target market--the majority of which have yet to obtain an online presence. We believe such a presence is becoming more necessary given COVID-19 disruptions and other challenges to the physical presence of many companies, along with the need to efficiently market online to customers.

StoneCo Ltd. Class A, a financial technology solutions company, was a detractor from performance during the quarter. While the Brazilian political, macroeconomic, and COVID dynamics all remain tumultuous, Stone also mis-fired out of the gate in its small and midsize business (SMB) credit opportunity and was too aggressive in its underwriting, causing a sizable write-down and one-time earnings headwind, which has impaired management's credibility. This caused the company to pause lending until further notice and pivot the future model to an 100% asset-lite partnership. Most recent commentary suggests the worst of the loan losses have passed, though the market will need to see evidence. We believe the core merchant acquiring thesis is fully intact with stable SMB take rates (excluding credit), still only ~6% (and rising) share of total SMB payment volumes, and 30+% total payments volume growth over the next 3-5 years. The stock has corrected significantly to the point where our underwriting suggests the core merchant acquiring business is substantially undervalued on its own, with micro-merchant acquiring (TON), software (Linx acquisition), and banking all purely free options. In the midst of both macro and execution uncertainty we believe the risk of an abrupt rebound in the short-term is low, and we look to the coming quarters for signs of stabilization.

Market Outlook

The economic backdrop remains accommodative to equity prices, although with a sustained higher level of volatility and market concerns over the potential inflation impact of a return to normal business activity. The U.S. market has possibly passed the peak of negative impacts brought by the Delta variant and investors have now turned their attention to assessing the level and profile of economic recovery. The back and forth between growth and value factors noted above demonstrated investors' wrestling with the nature of the recovery: will a post-COVID world unleash an unrestricted economic boom that favors the most cyclical companies; or are there enough limiting factors in play to put a cap on economic growth and therefore favor secularly-growing companies, those more in control of their own destinies? Furthermore, there is increasing investor focus on assessing the impact of potential Biden Administration policy changes, including the latest political battles—some inside the administration's own party—on how far to go on aggressive spending programs in infrastructure and social services. The third quarter demonstrated the tension between recent periods of growing enthusiasm of economic recovery, only to end with a month of concerns over the pace of economic recovery, the impact of a potential higher interest rates, and political battles clouding clear fiscal policy outcomes. Much like the third quarter itself, the translation of these complicated factors to equity prices makes the market outlook for the fourth quarter and into 2022 less clear, especially given the strong absolute equity returns already posted this year (albeit varied considerably depending on market capitalization segments).

At Jackson Square, our portfolio turnover increased at the onset of COVID in early 2020 as we took advantage of market volatility to purchase companies at some of the largest discounts to intrinsic business value we have seen since the Global Financial Crisis over a decade ago. We have returned to a lower, more typical level of turnover in recent periods, though we continue to seek to rebalance into asymmetrical risk/reward in our highest conviction holdings. We remain vigilant in watching for volatility that may give us more opportunities to enhance and refine the portfolio.

Regardless of policy outcomes and oscillating investor sentiment, we remain consistent in our long-term investment philosophy: we want to own what we view as strong secular-growth companies with great competitive positions that can grow market share and have the potential to deliver shareholder value in a variety of market environments.