

AI: A TRANSFORMATIVE MEGATREND

August 2020

People today are creating more data than ever before. Emails, instant messages, credit card purchases—even locations are collected and stored. For anyone to make sense of things at this scale—with individual datapoints in the billions of records—a new toolkit is required.

That toolkit is Artificial Intelligence (AI).

Now, the funny thing about AI is that it has been discussed since 1955¹, so why hasn't it become a "megatrend" sooner? For AI to be used in more mainstream applications, three distinct capabilities needed to evolve²:

- + **Computer storage or memory:** In the late 1950's, the price for one megabyte of storage was nearly \$10,000. Today, the price of that same amount of storage is one one-thousandth of one cent. In other words, it has gone from inaccessible to so inexpensive that we don't even think about taking our photos with high resolution and storing them in multiple places.
- + **Average transistor prices:** Let's assume that a transistor cost roughly \$100 around 1970. In today's terms, a transistor would cost roughly one ten-thousandth of one cent. To give this perspective, in 2019 iPhones, Apple has released its A13 Bionic chip which had 8.9 billion transistors³.
- + **Internet connection speeds:** Transferring data over the internet used to be quite taxing, with one megabit taking substantial time to make its way to its destination in the 1980's and 1990's. Now, speed is measured in megabits per second, and people don't think twice about downloading files multiple gigabytes in size, all within minutes.

The fact that we can now store, process and transfer very large amounts of data lead to AI's potential to influence society on the scale of a megatrend.

MANY STRATEGIES EXIST

What follows represents a summary of methodologies of select indices that focus in various ways on artificial intelligence. In some cases, this focus might be more tangential—such as a focus on automation or robotics—and then in other cases it might be more direct. Investors should keep in mind that the respective methodology documents cited would contain the full methodology details.

NASDAQ CTA ARTIFICIAL INTELLIGENCE INDEX⁴

The Consumer Technology Association (CTA) is a trade organization that has an Artificial Intelligence working group and is very focused on developments in the space. CTA is also responsible for the annual Consumer Electronics Show (CES) in Las Vegas, known as the biggest technology trade show of each given year.

¹ Source: Childs, Martin. "John McCarthy: Computer Scientist Known as the Father of AI." The Independent. 1 November 2011.

² Source: "Drastic Falls in Cost are Powering Another Computer Revolution." Economist. 12 September 2019.

³ Source: Hollister, Sean. "Apple Says its new A13 Bionic Chip Brings Hours of Extra Battery Life to New iPhones." Circuit Breaker. 10 September 2019.

⁴ Source: Nasdaq CTA Artificial Intelligence Index Methodology, November 2018.

Their judgements and experience in looking at AI technologies is what ultimately forms the selection and categorisation of AI companies within the Index, which is reconstituted on a semi-annual basis.

Categorisation delineates how companies within the AI ecosystem are put into three groups:

- + Engagers (50% of the Index):** These are companies that are directly productizing AI for their customers. Most of the revenue that they receive comes from selling something to a customer who can then benefit from utilizing AI processes and approaches more directly.
- + Enablers (40% of the Index):** These are companies that help to provide the foundation upon which the engagers operate. For example, there are certain semiconductor companies that focus on building these components in precise ways that allow for different types of AI to run more efficiently.
- + Enhancers (10% of the Index):** Some of the largest companies in the world are making massive investments into AI, but it would be untrue to state that most of their revenues comes from directly selling AI products and services. While these companies are important and they are included, they are not emphasized with large individual weights.

Within each of these categories, CTA is analysing each company for its exposure to and involvement within artificial intelligence. The results of CTA's individual company-by-company research is captured within an "intensity score". A higher intensity score, all other things being equal, means purer exposure to AI in CTA's view. The top 15 scores within each category comprise the ultimate index. Since constituents may have the same score (a tie), this may not equate to only 15 companies in each category and only 45 companies in the Index (3 categories x 15 companies). Tie scores would lead to the potential for more than 15 companies within each category.

Within each category (Engagers, Enablers, Enhancers), companies are equally weighted.

STOXX GLOBAL AUTOMATION & ROBOTICS INDEX⁵

This approach is defined as all companies from the STOXX Global Total Market Index that derive more than 50% of their most recent total annual revenues from sectors linked to the Automation & Robotics business, with this threshold lowered to 45% for current components. Revenue data comes from Factset's Revere Business Industry Classifications (RBICS) Datafeed, which then aims to use this data to more precisely define the business of a specified company. To give a sense of the scale, the taxonomy of the RBICS system defines 317 industry groups, 781 industries, and 1,455 sub-industries⁶.

RISE OF THE ROBOTS INDEX⁷

The index is composed of a dynamic basket of shares whose companies are involved in the development of artificial intelligence, automation and robotics or will benefit from the use of these advanced technologies. During the quarterly rebalancing process, the approach is designed to select 150 companies.

The strategy is investing in companies from three main sectors: 1) Information Technology 2) Healthcare and 3) Industrials. Algorithmic approaches along with human judgement are used to drive toward the final selection of companies. Fundamental characteristics in focus include 1) Research & Development expenditure on net sales, 2) return on invested capital and 3) 3-year sales growth.

⁵ Source: STOXX Index Methodology Guide, July 2020.

⁶ Source: "At a Glance: Factset Revere Business Industry Classification Datafeed." Copyright 2020. <https://insight.factset.com/resources/factset-revere-business-industry-classifications-datafeed>

⁷ Source: "The Rise of the Robots." Lyxor ETFs. February 2020.

ROBO GLOBAL ARTIFICIAL INTELLIGENCE INDEX⁸

Each company in the ROBO Global Industry Classification System is assigned a score based on the company's level of revenues and investments in artificial intelligence activities, as well as market leadership in the field of AI. These scores range from 1-100 with 100 representing significant levels of AI revenues and investment. A company must have a minimum AI Score of 50 to be considered for inclusion in the index. Companies are weighted by dividing each company's individual AI score by the sum of the total scores among index constituents.

STOXX AI GLOBAL ARTIFICIAL INTELLIGENCE INDEX⁹

STOXX worked in partnership with an Artificial Intelligence company, Yewno, whose proprietary AI algorithms are used to identify index constituents from the universe of the STOXX Developed and Emerging Markets Total Market Index. The key criterion used in the selection process is patent filings related to AI intellectual property, thereby identifying AI innovators as well as AI adopters. Yewno is able to employ machine learning, computational linguistics and knowledge graph techniques to accomplish this screening process.

Yewno uses their capabilities to measure company involvement in AI along two spectrums:

- + **AI Intellectual Property Exposure:** This is defined as the ratio of the number of AI patents awarded to a company over the most recent 3-year period to the total number of patents awarded to that company over the same period.
- + **AI Contribution:** This is defined as the ratio of the number of AI patents awarded to a company over the most recent 3-year period to the total number of AI patents awarded to all companies in the indices' universe.

Companies which fall above the 25th percentile in these measures can be included, assuming they hit and qualify along the other necessary metrics for index inclusion.

Performance: Tying indices accessing the AI theme to the recent market environment

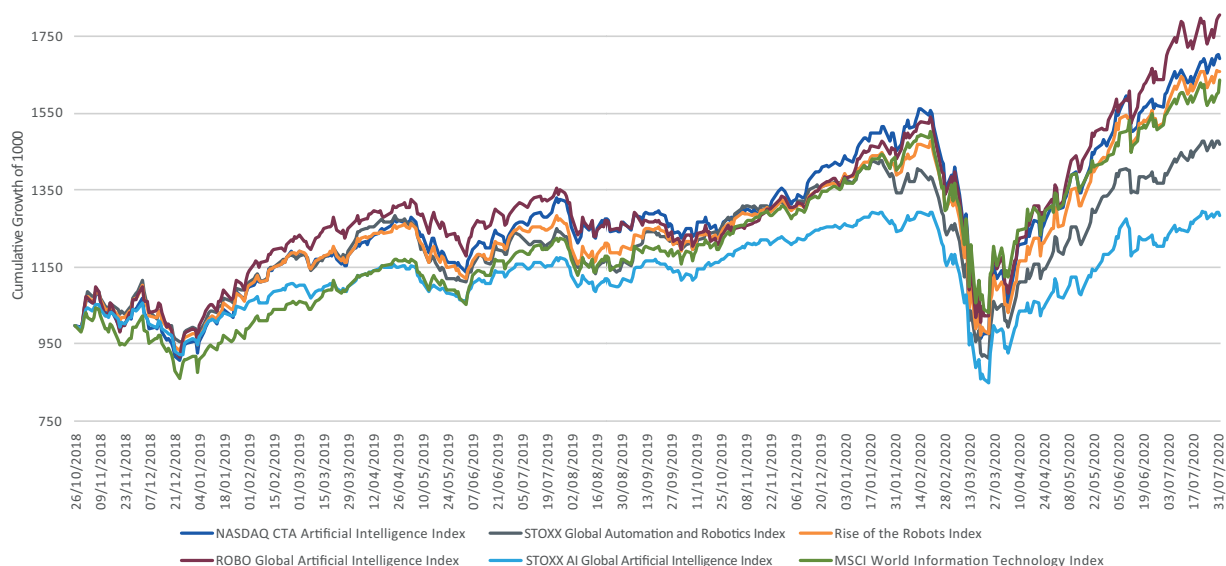
Broadly speaking:

- + If we see that the different AI-focused indices have performed in very similar fashion, this would tell us that they were defining or tapping into a very similar trend within the market.
- + Similarly, if the different AI-focused indices have exhibited widely divergent performance, then this could be a catalyst to lead investors to explore the aforementioned methodologies, as well as the resulting exposures more deeply.
- + It is also important to relate both the performance and correlation of the strategies back to the broader MSCI World Information Technology Index benchmark. We must assume that this is an example of a benchmark strategy that can be easily accessed, so any strategy not differentiating itself well from this return stream may not be as attractive when viewed through the standard of defining a differentiated megatrend.

⁸ Source: Rules for the Management of the ROBO Global set of Indices, 1 April 2020.

⁹ Source: STOXX Index Methodology Guide, July 2020.

FIGURE 1A AND 1B: STRATEGIES THAT FOCUS ON ARTIFICIAL INTELLIGENCE IN DIFFERENT WAYS CAN EXPERIENCE WIDE VARIATIONS IN PERFORMANCE OVER TIME (26 OCTOBER 2018 TO 31 JULY 2020)



Index Name	Avg. Ann. Return	2019 Year	Covid-19 Initial Market Drawdown	Covid-19 Post Drawdown Initial Rally	YTD 2020	Avg. Ann. Std. Dev.	Correlation to MSCI World Information Technology Index
NASDAQ CTA Artificial Intelligence Index	34.81%	48.37%	-37.30%	73.57%	19.37%	28.59%	0.92
STOXX Global Automation and Robotics Index	24.27%	38.17%	-34.15%	60.69%	7.00%	23.88%	0.84
Rise of the Robots Index	33.28%	40.36%	-33.93%	70.19%	21.04%	26.80%	0.94
ROBO Global Artificial Intelligence Index	39.77%	37.61%	-33.47%	76.37%	32.46%	30.95%	0.95
STOXX AI Global Artificial Intelligence Index	15.14%	30.08%	-34.30%	51.01%	2.24%	22.97%	0.89
MSCI World Information Technology Index	32.19%	47.55%	-31.31%	58.68%	20.56%	30.13%	1.00

Source: Bloomberg. Period selected due to the live performance of the NASDAQ CTA Artificial Intelligence Index, where the initial base date is 26 October 2018 but where live calculation begins on 29 October 2018. The STOXX AI Global Artificial Intelligence Index is initially calculated in EUR terms, net of reinvested dividends. To match the currency of the other indices, these returns are converted into USD terms, net of reinvested dividends. This does impact the risk and return measures in these figures. Within Figure 1b, the periods shown are as follows: “Avg. Annual Return” refers to 29 October 2018 to 31 July 2020; “2019 Year” refers to 31 December 2018 to 31 December 2019; “Covid-19 Initial Market Drawdown” refers to 19 February 2020 to 23 March 2020; “Covid-19 Post Drawdown Initial Rally” refers to 23 March 2020 to 31 July 2020; “YTD 2020” refers to 31 December 2019 to 31 July 2020. **You cannot invest directly in an index. Historical performance is not an indication of future performance and any investments may go down in value.**

Figures 1a & 1b show that while the cumulative returns over the period for many of the indices shown in 1a arrived at a similar level, for the most part, over the period, there were significant variations in the performance experienced within the overall period. This tells us clearly that these indices are tapping into the AI megatrend in differentiated ways.

To undertake further analysis of different measures of exposure based on specific holdings, in Figure 2 we have connected the indices that we have previously discussed to different UCITS Exchange Traded Funds (ETFs) that are designed to track their performance after fees. It is not always possible to review holdings solely at the index level.

FIGURE 2: ARTIFICIAL INTELLIGENCE LANDSCAPE IN EUROPEAN ETPS

Fund Name	Fund Ticker	Fund TER	Fund Inception Date	Fund Underlying Index
WisdomTree Artificial Intelligence UCITS ETF	WTAI	0.40%	05/12/2018	NASDAQ CTA Artificial Intelligence Index
iShares Automation & Robotics UCITS ETF	RBOT	0.40%	12/09/2016	STOXX Global Automation and Robotics Index
L&G Artificial Intelligence UCITS ETF	AIAI	0.49%	02/07/2019	ROBO Global Artificial Intelligence Index
Lyxor Robotics & AI UCITS ETF	ROAI	0.40%	18/09/2018	Rise of the Robots Index
Amundi STOXX Global Artificial Intelligence UCITS ETF	GOAI	0.35%	11/09/2018	STOXX AI Global Artificial Intelligence Index

Source: Bloomberg. Data was looked up as of 31 July 2020. **Historical performance is not an indication of future performance and any investments may go down in value.**

Sub Industries as the window into Megatrend exposure

When considering exposure to different Megatrends, it is important to approach with a greater degree of precision than when considering broader, passive indices. Looking from sectors to industries and getting down into sub industries can be very useful. Figure 3 details the sub industry exposures of an array of strategies focused on the AI megatrend in different ways.

- + WTAI has a very large exposure to Semiconductors. There is no question that increases in semiconductor capability are the fuel for increases in AI capability. However, we think it is more important to recognise that the various strategies—all of which are focused on AI in different ways—have very different exposures to this particular sub industry. The benchmark MSCI World Information Technology Index had 13.31% exposure to this sub industry as of 31 July 2020.
- + AIAI & WTAI had significant amounts of exposure to Application Software and Systems Software. Stepping back, this is an accurate reflection of what AI currently is—software that various customers can use to help in accomplishing certain tasks. The benchmark MSCI World Information Technology Index had just over 30% exposure to these two sub industries as of 31 July 2020. ROAI was also notable with more than 30% exposure to Application Software by itself.
- + Importantly, there is no such thing as a “good” or a “bad” sub industry exposure, as no one knows ahead of time which will perform the best. However, we keep coming back to the concept of what an investor might be looking for. There are ways to concentrate exposure more towards AI directly, and there are ways to be broadly exposed to many sub industries that may benefit from using AI.

FIGURE 3: SUB INDUSTRY EXPOSURE FOR SELECTED STRATEGIES.

GICS Sub Industry Name	WTAI	RBOT	AIAI	ROAI	GOAI	MSCI World Information Technology Index
Semiconductors	36.24%	19.19%	8.34%	11.88%	8.66%	13.31%
Application Software	28.16%	20.60%	23.91%	30.59%	11.58%	12.71%
Systems Software	11.30%	3.00%	12.88%	8.03%	5.20%	19.17%
Communications Equipment	3.89%	0.00%	1.51%	0.66%	3.67%	3.36%
Research & Consulting Services	3.78%	0.00%	1.48%	0.73%	1.25%	0.00%
IT Consulting & Other Services	3.38%	0.00%	5.61%	2.49%	3.15%	5.01%
Automobile Manufacturers	2.51%	0.00%	1.87%	1.29%	2.25%	0.00%
Electronic Equipment & Instruments	2.42%	11.07%	1.30%	6.23%	3.12%	2.28%
Auto Parts & Equipment	2.28%	1.48%	0.00%	0.00%	1.64%	0.00%
Internet Services & Infrastructure	1.88%	0.00%	6.43%	0.90%	1.31%	2.58%
Internet & Direct Marketing Retail	1.44%	0.00%	9.93%	2.73%	2.30%	0.00%
Interactive Media & Services	1.05%	2.54%	6.69%	4.45%	2.79%	0.00%
Wireless Telecommunication Services	0.67%	0.00%	0.00%	0.00%	1.43%	0.00%
Technology Hardware, Storage & Peripherals	0.54%	4.55%	0.94%	2.65%	6.38%	21.25%
Interactive Home Entertainment	0.44%	0.00%	1.28%	0.00%	3.86%	0.00%
Other GICS Sub-Industry	0.00%	37.58%	17.85%	27.37%	41.41%	20.33%

Source: Bloomberg. Data is as of 31 July 2020. For GOAI the data is based on Bloomberg figures in PORT as of 31 July 2020 from latest holdings reported as of 28 May 2020. Sub industries selected are those found within WTAI and the NASDAQ CTA Artificial Intelligence Index, since we could not show all 158 GICS Sub-Industries. "Other" refers to GICS Sub-Industries that are not included in those shown. **Historical performance is not an indication of future performance and any investments may go down in value.**

To concentrate or not to concentrate—a critical question

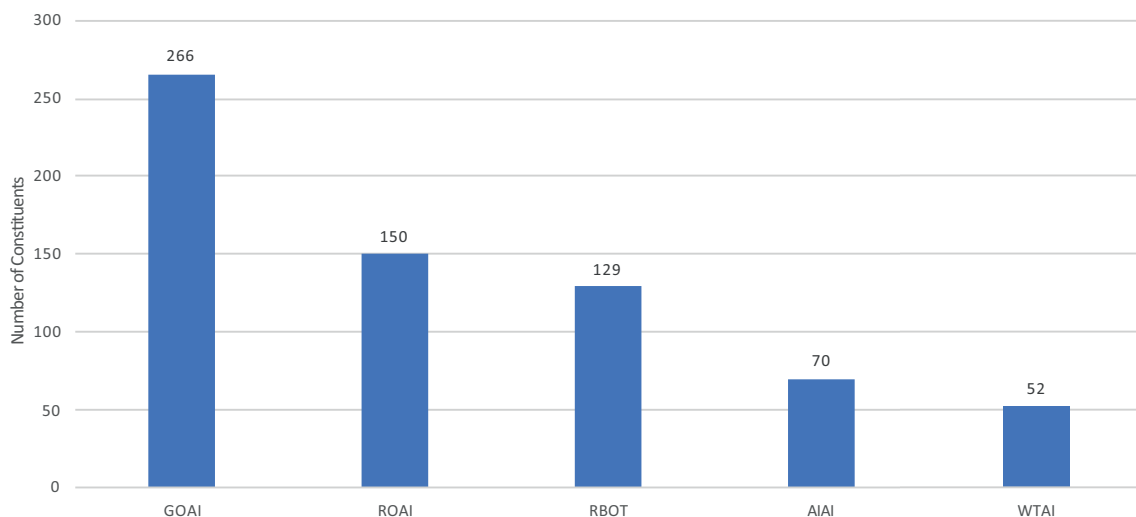
There is no "one way" to build a thematic portfolio. Some might tilt toward a particular theme and include many stocks, while others might opt for a more concentrated approach where every stock has a relatively high bar to clear in order to gain inclusion. While there isn't any way to know which might outperform ahead of time, we feel it is most important that clients understand the difference in these approaches and how that could ultimately relate to the performance experienced.

In Figure 4, we see:

- + GOAI stands out, having 266 positions as of 31 July 2020 and tracking the STOXX AI Global Artificial Intelligence Index. The primary selection methodology for this index centres upon patent filings and makes certain distinction from there in various ways. Fortunately, many companies have patents that relate to AI and AI innovations. The other side, however, is that not all patents are equally related to the revenue generating activities of a given business.
- + WTAI is on the opposite end of the spectrum, having 52 positions as of 31 July 2020 and tracking the NASDAQ CTA Artificial Intelligence Index. The methodology behind this index is driven by a team of experts at the Consumer Technology Association (CTA) studying individual businesses to determine the intensity of their exposure to AI.

A larger number of positions is one way to decrease the risk in a strategy that any single position ends up having a severely negative result and strongly impacting performance. However, another way to consider the same situation is to indicate a greater potential for similarity to “the market.” A more selective approach can have greater risk, as there must be more confidence in each position, but at the same time the concentration could lead to greater differentiation against the market.

FIGURE 4: PORTFOLIO CONCENTRATION VARIES AMONG STRATEGIES



Source: Bloomberg. Data is as of 31 July 2020. Data shown is from the PORT function and represents the most current available, setting the system to 31 July 2020 and running the software on 2 August 2020. In the case of GOAI, data was referenced against number of holdings on the 31 July 2020 fund fact sheet. **Historical performance is not an indication of future performance and any investments may go down in value.**

Exposure to Cloud Computing: A Major Explanation of 2020 Performance Trends

During the first 7 months of 2020, the cloud computing megatrend has encompassed some of the top-performing companies in global equities, as many of these companies have seen increased demand for their services during the Covid-19 Pandemic. Artificial Intelligence and Cloud Computing are closely linked. Importantly:

¹⁰ Source: Casado, Martin & Matt Bornstein. “The New Business of AI (and How it’s Different from Traditional Software).” Andreessen Horowitz. 16 February 2020.

- + For startups in AI, computing infrastructure is frequently one of the largest individual expenses, at times encompassing something on the order of 25% of revenues¹⁰. It is often the case that these firms will rent data storage and computational power from the likes of Amazon Web Services, Microsoft Azure, Google Cloud or others.
- + Developers of cloud computing software will frequently look to include different types of AI and machine learning functionality that can over time improve the experiences of the users.
- + In a way, cloud computing represents the future of how we expect software to be consumed by both businesses and private consumers, whereas AI represents a specific set of tools that can help users make sense of massive amounts of data and improve the insights they can gain from it.

What is a 'Cloud Computing' Company?

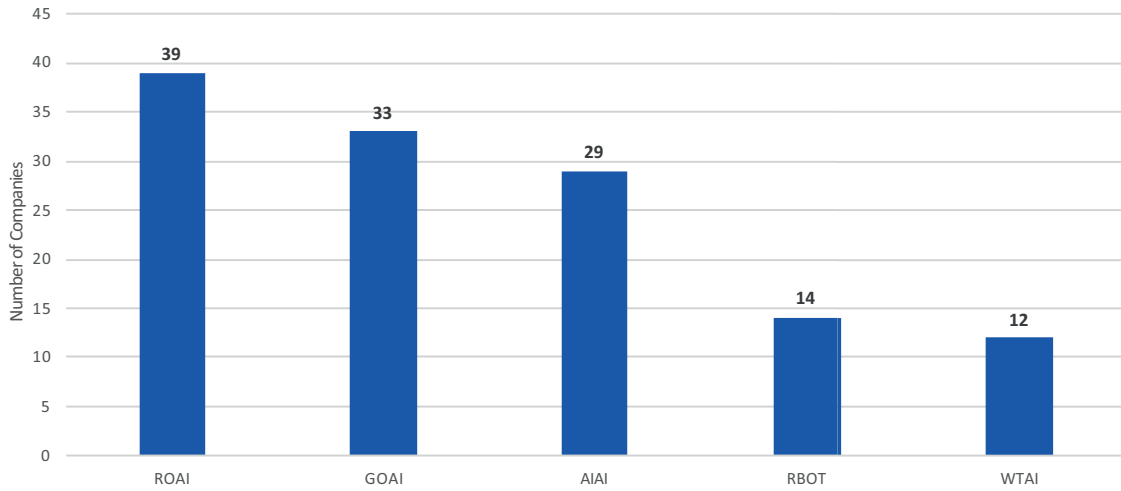
There is no universally accepted definition of a 'cloud computing' company, but there are different strategies that seek exposure to this megatrend. If we had the comprehensive list of companies included within these different strategies, we could then compare it back to the holdings of the different AI strategies that we discussed in this piece. In this way, we'd have a better way to gauge how much (or how little) the AI strategies were directly tapping into cloud computing. While tapping into this megatrend would have contributed positively to performance during the first 7 months of 2020, it's possible that other components of the technology space would outperform it at different points in the future. The cloud computing strategies are:

- + WisdomTree Cloud Computing UCITS ETF (WCLD), which tracks the performance of the BVP Nasdaq Emerging Cloud Index.
- + First Trust Cloud Computing UCITS ETF (FSKY), which tracks the performance of the ISE CTA Cloud Computing Index.
- + HAN-GINS Cloud Technology UCITS ETF (SKYY), which tracks the performance of the Solactive Cloud Technology Index.

Figure 5a shows the number of "cloud companies" in each of the AI strategies that we have been discussing in this piece. Again, a 'cloud company' is one that is included in at least one of the following 3 strategies: WCLD, FSKY or SKYY.

- + AIAI is notable—it only had 70 total constituents in Figure 4. 29 of them were included at least once within the 3 cloud strategies.
- + GOAI, on the other hand, had 266 constituents in Figure 4, so it's natural that it would have more of the so-called 'cloud companies.' ROAI, similarly, had 150 constituents in Figure 4, so again having more total stocks could lead to a higher chance of holding more cloud companies.

FIGURE 5A: NUMBER OF CLOUD COMPANIES WITHIN THE AI STRATEGIES, AS OF 31 JULY 2020

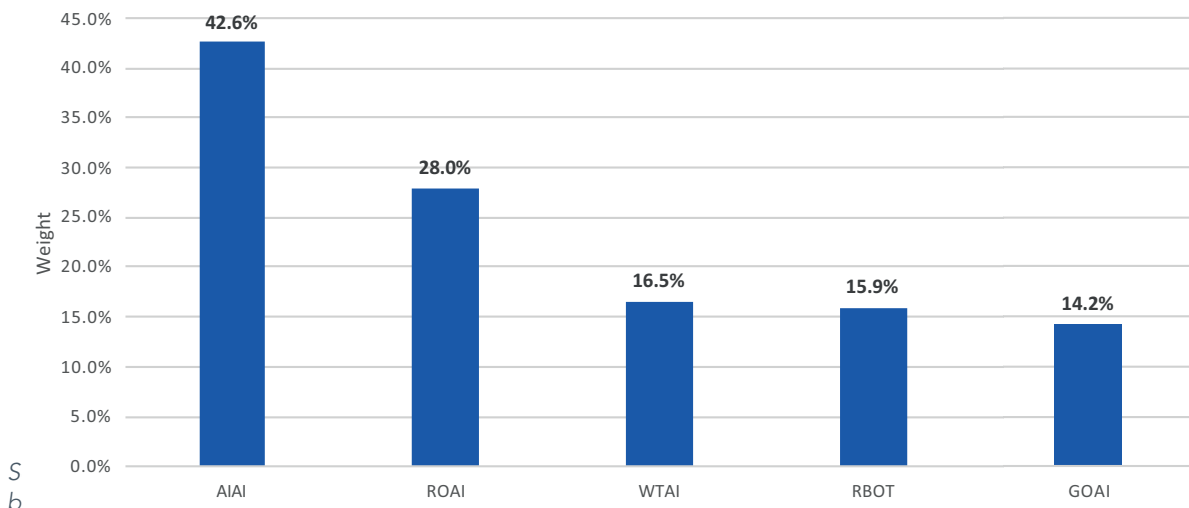


Source: Bloomberg, specifically through the PORT function. Holdings data accessed within the PORT function is not always updated for all funds on all business days. For GOAI the data is based on Bloomberg figures in PORT as of 31 July 2020 from latest holdings reported as of 28 May 2020. Number of companies refers to those that were included at least once within WCLD, FSKY or SKYY, the “cloud strategies.” **Historical performance is not an indication of future performance and any investments may go down in value.**

Within Figure 5b, we indicate the weight of these ‘cloud companies’ within each of the AI strategies.

- + AIAI had the highest exposure to these companies by weight.
- + WTAI, RBOT and GOAI were clustered at a similar level by this metric.

FIGURE 5B: WEIGHT OF CLOUD COMPANIES WITHIN AI STRATEGIES, AS OF 31 JULY 2020



of 31 July 2020 from latest holdings reported as of 28 May 2020. Weight of companies refers to those that were included at least once within WCLD, FSKY or SKYY, the “cloud strategies.” **Historical performance is not an indication of future performance and any investments may go down in value.**

Within Figure 5c, we indicate the top 10 holdings of AIAI and GOAI, so as to compare the strategy with the highest weight to the cloud companies against the strategy with the lowest weight to the cloud companies.

- + AIAI saw 4 of the cloud companies within the top 10 holdings. It's noteworthy that the weight to each was above 1.8%—in some cases it was even close to 2.0%. Remember—AIAI was among the more concentrated of the AI strategies, with only 70 positions as of 31 July 2020.
- + GOAI saw 1 of the cloud companies within the top 10 holdings. GOAI was the least concentrated of the AI strategies, with 266 positions as of 31 July 2020. This is why no company in the top 10 had even a 1.0% weight, as the weight is being spread across a much larger range of companies.

FIGURE 5C: COMPARISON OF TOP 10 HOLDINGS FOR AIAI AND GOAI, AS OF 31 JULY 2020

AIAI			GOAI		
Company Name	Weight	Cloud Company?	Company Name	Weight	Cloud Company?
CLOUDFLARE INC - CLASS A	1.96%	Yes	SUNRUN INC	0.74%	No
VEEVA SYSTEMS INC-CLASS A	1.93%	Yes	INFINERA CORP	0.56%	No
ALTERYX INC - CLASS A	1.92%	No	TESLA INC	0.53%	No
TESLA INC	1.87%	No	XPERI HOLDING CORP	0.52%	No
AMAZON.COM INC	1.84%	Yes	SQUARE INC - A	0.52%	Yes
SPOTIFY TECHNOLOGY SA	1.84%	No	STAMPS.COM INC	0.52%	No
VERACYTE INC	1.84%	No	ADVANCED MICRO DEVICES	0.51%	No
TENCENT HOLDINGS LTD	1.83%	No	SPOTIFY TECHNOLOGY SA	0.51%	No
SQUARE INC - A	1.81%	Yes	GIGABYTE TECHNOLOGY	0.49%	No
NUANCE COMMUNICATIONS INC	1.81%	No	UNITED PARCEL SERV.	0.49%	No
Sum of Top 10 Weights	18.64%		Sum of Top 10 Weights	5.38%	

Source: Bloomberg, specifically through the PORT function. Holdings data within PORT may not be updated for all strategies on all business days. In the case of GOAI, the top 10 holdings and weights on the 31 July 2020 fund fact sheet were used. "Cloud Company?" refers to those that were included at least once within WCLD, FSKY or SKYY, the "cloud strategies." **Historical performance is not an indication of future performance and any investments may go down in value.**

Always look under the hood

When creating a strategy focused on AI, we believe it is necessary to look under the hood of the business model of each underlying company to understand how it connects directly to improving or pushing forward the AI ecosystem. Similarly, when investors are considering AI strategies, we think that investors should take the time to understand details like the number of constituents or the semiconductors exposure. While no one could ever tell which strategy would outperform any other ahead of time, doing it this way allows investors to choose the risks they want to take in gaining exposure to the AI megatrend.

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