

## Long-Term Secular Growth Drivers Technology Advancements

Scout Investments' Small Cap Strategy Team believes that long-term, secular technology advancements play a vital role in driving outsized investment returns. These trends develop over time and help us identify opportunities in the markets that others may miss. Colossal advances in technology since the turn of the millennium are overwhelmingly impressive, whether it is the omnipresent smartphone, successful sequencing of the entire human genome, or the advent of large scale 3-D printing. These innovations define our lives and society in many ways and have helped propel technology to become the largest sector weight in most major equity indices. In this paper, we will discuss several of the technology advancements that are most pertinent today and how the Scout Small Cap Investment Team seeks to take advantage of these trends in its portfolio.

### Artificial Intelligence and Machine Learning

The term Artificial Intelligence (AI) was first introduced during the early days of the computer (1955) with the idea that if you could program a machine to mimic the human brain, you could introduce artificial intelligence. Today, every industry has introduced AI into its operations, from autonomous car driving, to personal assistants like Siri and Alexa, to medical diagnostics. It is involved in every aspect of a company's business from marketing and finance to producing widgets. As a society we are seeing enormous amounts of data generated, which reinforces the importance of AI's ability to analyze and help solve complex problems. As a result of public interest, AI software is expected to grow globally at a compound annual growth rate (CAGR) of over 40% through 2025.<sup>1</sup>

Machine Learning (ML) is a subset of AI whereby a computer analyzes information and learns from experience. ML studies datasets and through algorithms makes predictions based on historical relationships. When new evidence arises, the algorithm adjusts the datasets and determines any changes in pattern. ML continues to grow rapidly as we find ever more uses for the predictive technology, from simple vehicle maintenance to more robust outcomes such as fraud detection and algorithmic trading. Due to the myriad applications and more complex global problems society faces, industry experts expect ML to increase 10 fold worldwide over the next seven years.

AI/ML is the most recent addition to Scout Small Cap's secular growth trends and one that we believe will continue to play a more important role as the industries evolve.

<sup>1</sup>Source: July 24, 2020 news release announcing report, "Global Artificial Intelligence (AI) Software Market, Forecast to 2025" from ResearchAndMarkets.com. Retrieved from <https://www.globenewswire.com/news-release/2020/07/24/2067275/0/en/Artificial-Intelligence-AI-Software-Industry-Outlook-2020-2025-Market-Revenues-to-Grow-at-a-CAGR-of-41-6-Between-2019-and-2025.html> on September 4, 2020.

### Bandwidth Expansion

Internet bandwidth and traffic has seen explosive growth over the past several years as a more interconnected global society emerges. This expansion has become even more stark during the COVID-19 pandemic as more people worldwide work from home and spend more time online to stay connected with friends, family, and colleagues.

Increasing numbers of users and a rapid rise in devices are the primary drivers of continued growth. From 2018 to 2023, the share of global population with internet access will increase from roughly one-half to two-thirds.<sup>2</sup> Meanwhile, one of the largest suppliers of computer networking equipment in the world forecasts global web traffic will more than triple from 2017 to 2022, driven by more connected devices online including mobile phones, automobiles, internet users, etc. By 2023, the number of devices used per capita is forecast to rise 50% from 2.4 devices to 3.6.<sup>3</sup> Faster broadband speeds that enable experiences like video streaming and virtual reality force this progression as well.

Despite some headlines disparaging the acceleration, our worldwide community continues to become more interrelated by the day—and the trend of internet bandwidth expansion is poised to move forward alongside global growth. Given this acceleration, the Scout Small Cap team will continue to seek opportunities where expanding internet access unlocks shareholder value.

#### Global Web Traffic Growth

Global internet traffic will increase three-fold from 2017 to 2022



\* Compound annual growth rate  
Source: Cisco VNI Global IP Traffic Forecast, 2017-2022

<sup>2</sup> Source: Cisco Annual Internet Report, 2018 - 2023.

<sup>3</sup> Source: Cisco Annual Internet Report, 2018 - 2023.

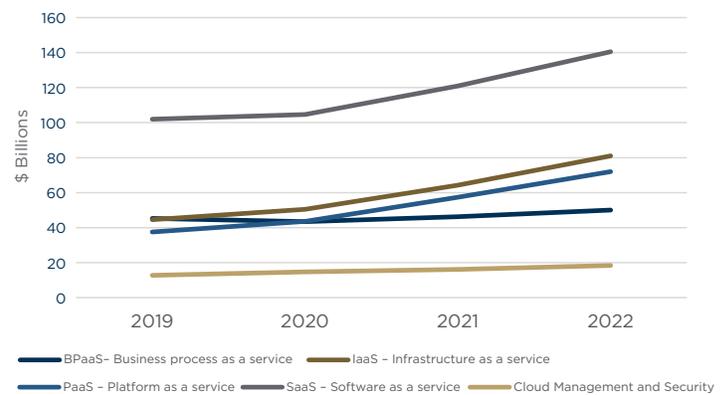
### Growth in Cloud Services

The market for cloud computing has evolved and expanded in a major way over the last decade. Cloud services allow customers to consume everything from software to IT infrastructure in a more flexible manner and permit companies to recognize the cost of those services as a regular expense, rather than as a large capital expenditure.

The evolution of the Software as a Service (SaaS) model has produced benefits for customers and created new business models for companies. Keeping most customers on the same version of a software program allows companies to invest more of their engineering dollars on incremental improvements rather than supporting multiple legacy versions of a program. Companies are also becoming more sophisticated in how they use cloud services, with many adopting some form of hybrid cloud infrastructure, combining the company's private cloud deployment with services from public cloud providers. This evolution has created more demand for all types of related software including security, monitoring and analysis.

While this trend is well established, we believe there is plenty of room for more growth. Indeed, 61% of companies report moving additional workloads to the cloud as a spending priority for 2020.<sup>4</sup> Gartner, a leading research firm, forecasts spending on cloud services will grow 19% in 2021 and nearly 19% again in 2022 as adoption accelerates into the mainstream. Demand for cloud services and the

Worldwide Public Cloud Service Revenue Forecast



Source: Gartner 2020 press release. Retrieved from: <https://www.gartner.com/en/newsroom/press-releases/2020-07-23-gartner-forecasts-worldwide-public-cloud-revenue-to-grow-6point3-percent-in-2020>

services to run a hybrid cloud strategy should continue to grow at a robust pace for the foreseeable future and create opportunities for a wide variety of companies—opportunities that Scout's Small Cap team will endeavor to unearth.

<sup>4</sup> Source: <https://www.flexera.com/blog/industry-trends/trend-of-cloud-computing-2020/> Retrieved 9.5.2020

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