



Setanta European Equity Fund – Q3 2011

Fund Description

The **European Equity Fund** ('the Fund') is managed by Setanta Asset Management Limited ("Setanta") and is a representative account of the European Equity strategy.

The Fund is an actively managed equity portfolio, with a long-term investment horizon.

Our aim is to invest in European companies that are trading below their intrinsic value. Our investment process seeks to invest in companies that exhibit a combination of low financial risk, low operational risk and low valuation risk.

We believe that if we can invest in companies that possess these characteristics then we can reduce the risk of a permanent loss of capital and enhance our chances of outperforming our benchmark over the long term.

Investment Philosophy

We in Setanta do not believe the market is efficient. Our aim is to purchase and own assets at a price below a reasonable assessment of their worth. This is where we focus our resources. Our process is akin to assessing a part ownership of a business rather than trading a security. This assessment of value must always encompass a thorough understanding of where this value is derived. We have a long term investment horizon and risk management is always central. We regard risk as the potential for permanent impairment of value. Integrity is a key tenet of our professional DNA and we embrace a culture of continued learning.

Portfolio Managers

Rowan Smith, Fergal Sarsfield & David Byrne



Investment Principles

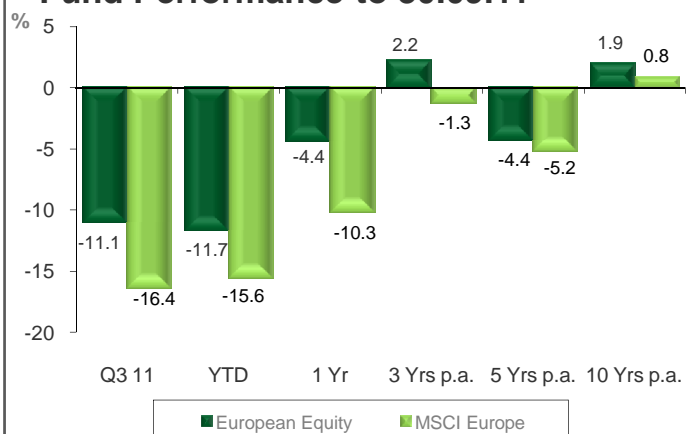
- We do not believe the market is efficient.
- We aim to make investments at a price below our assessment of intrinsic value.
- We make an investment in a business rather than trade securities.
- We believe risk is the possibility of permanent impairment of value.
- We make investments for the long term.
- We invest where we see value and are not afraid to be contrarian and swim against the tide.
- We don't make forecasts, we consider scenarios.
- We demand financial strength from the companies we invest in.
- We will act with integrity and communicate with our clients in a manner representative of our investment style.
- We have the humility to know we make mistakes and embrace the need to continue learning through both experience and study.

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Fund Performance to 30.09.11



Fund Statistics

PRICE/BOOK	1.6
PRICE/EARNINGS RATIO (FY 1)	9.7
FREE CASH FLOW/EV %	7.7
DIVIDEND YIELD %	5.1
AVERAGE MARKET CAP €BN	36
NO. OF HOLDINGS	29

Yearly Performance

Year	2006	2007	2008	2009	2010
Fund	18.9	-4.4	-38.4	34.1	8.3
Benchmark	19.6	2.7	-43.6	31.6	11.1

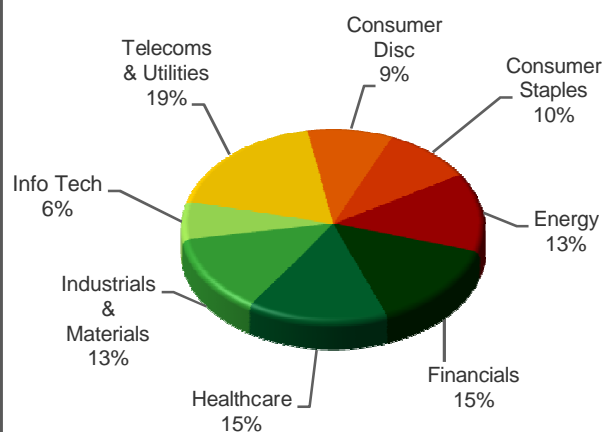
The investment objective of the Fund is to outperform the MSCI Europe index over periods of three years or more.

Performance Source: Setanta Asset Management Limited. **Benchmark:** MSCI Europe. The Fund returns stated are based on the movements in the unit prices of a representative account, based on mid to mid prices, and are gross of management fees. The performance will be reduced by the impact of management fees paid, the amount of which varies. **Fund Statistics Source:** Bloomberg Median ex Financials.

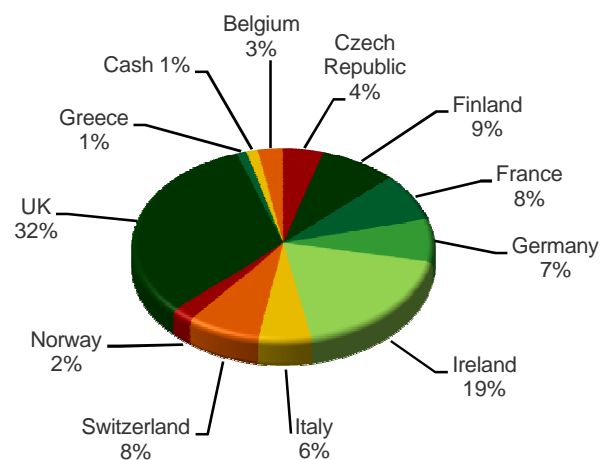
Top 10 Holdings

COMPANY	SECTOR	% OF FUND
NOVARTIS	HEALTHCARE	5.6
KINGSPAN	INDUSTRIALS & MATERIALS	5.1
DIAGEO	CONSUMER STAPLES	4.9
BP	ENERGY	4.9
C&C GROUP	CONSUMER STAPLES	4.7
GLAXOSMITHKLINE	HEALTHCARE	4.7
SANOFI	HEALTHCARE	4.5
UNITED UTILITIES	TELECOMS & UTILITIES	4.4
BELGACOM	TELECOMS & UTILITIES	4.4
DCC	INDUSTRIALS & MATERIALS	4.0

Sector Distribution



Geographic Distribution



Thoughts on risk

There are NO certainties in investing. Having observed market events unfold since 2008, this does not need mentioning. However it is this belief that helps to form the bedrock of our investment approach. Risk is unpleasant but cannot be avoided. That risk is unavoidable and should not be a surprise. Driving your car or crossing the street requires some risk-taking. Recent experiences highlight that cash in the bank or AAA-rated sovereign bonds are not risk-free assets. Both are subject to the pernicious effects of inflation or even outright default. We can't avoid risk so we must adapt our thinking to manage it.

In relation to equity investment, when we speak of risk, we are referring not to price volatility, but to the possibility of permanently losing money. Speaking very broadly, there are three conduits for permanent capital impairment:

- **Operating Risk:** refers to the likelihood that the profitability of the business deteriorates such that the real value of our investment degrades. Causes include (but are not restricted to) an increase in competition; decline in demand; deterioration in pricing; an unfavourable regulatory change.
- **Financial Risk:** refers to the likelihood that the financial structure of the enterprises might change in a manner unfavourable to equity investors. For example bankruptcy caused by excessive debt-levels or a cash-crunch; dilutive share issuance; expensive re-financing.
- **Valuation Risk:** refers to the likelihood that the investor pays too much to acquire the investment or disposes of the investment for a price that is too low. In such instances, losses can be incurred even absent any operating or financial deterioration.

Risk, and our consideration of it, is dynamic not static. For example, an investment might be unattractive at a stock price of €10 because of concerns around the sustainability of profits. That same investment might be considered attractive at €7, as the lower valuation risk might be deemed to offset the operating risk. In other words, all else equal, a lower price creates greater upside potential and lower downside potential for the price. All else equal a lower price means lower risk. In theory, even the most risky investments are worth making if the price is low enough. Occasionally, attempting to implement this theory in practice is not advisable as the investment case might be too complex or opaque to properly appraise.

Of course, on the flip side, low operating and financial risks should engender some willingness to undertake some additional valuation risk (i.e. paying a higher price to make the investment). These considerations are entirely subjective: there are no formulae to dictate a specific course of action here. Experience, skill and good judgement are all crucial inputs. It is this risk-return framework that we endeavour to employ in appraising our investment opportunities.

Given the stock's awful performance thus far in 2011, a brief overview of the fund's position in Wincor Nixdorf is timely. Wincor Nixdorf is a Germany-based manufacturer of Banking ATM systems and Retail Point of Sale systems, which it sells worldwide. In Banking, Wincor is world number two with a circa 20% market share. The top three companies (including US companies NCR and Diebold) have a combined global market share of over 60%. In Retail, Wincor is ranked number three in the world, with its share plus that of NCR and IBM making up over 50% of the global market. Wincor has especially strong market positions in Germany and the rest of Europe, which accounted for 29% and 43% of 2010 revenues respectively.

Wincor's business proposition is to enhance transaction efficiency through automation, thus improving the cost-effectiveness of business processes for its clients. Wincor was listed in 2004 after periods of ownership within the Siemens Group and by Private Equity. The fund has been invested in Wincor since 2008. Since the listing in 2004, the company prospered, albeit with a favourable economic tailwind. From 2004-2008, free cash flow grew by approximately 9% p.a., with almost no assistance from acquisitions and whilst maintaining a clean Balance Sheet. The business has naturally suffered some effects from the global recession: from 2008 to 2010, free cash flows fell by a total of roughly 25% with Net Profits down by around 15%. Thus far the recovery has remained patchy and management announced in May 2011 that profits would be largely unchanged this year versus last. It is this announcement, alongside already jittery markets, that has contributed to the stock falling by over 40% so far this year. Wincor has been amongst the very worst performing stocks in the fund this year. Business fundamentals over the next year or two may deteriorate, but we believe the current stock price is very attractive and we hope this will provide the platform for outsized investment gains in the coming years. Why do we believe this?

Firstly despite its clean financials, low debt and good record, the stock appears very inexpensive and is pricing-in a lot of negativity already. At €34 Wincor Nixdorf is trading at just 11 times 2010 free cash flow per share. We believe these cash flows could prove to be cyclically-depressed, but even if this is not the case, at a circa 9% free cash flow yield and dividend yield of 5%, the business is clearly not priced for value-enhancing growth. Using smoothed, five year average free cash flows as a potentially more meaningful base, the stock currently trades at a circa 11% FCF yield. Contrast that with 10 year German Bunds yielding just 1.8%.

Secondly while Hardware sales may prove lumpy, around 50% of the group's sales come from software and service revenues, which have been and should remain more stable. This includes revenue for servicing/repairing hardware, annual software maintenance fees, and other activities such as consulting. Software/service revenues have increased as a portion of group revenues from around 30% in 2000 and we expect that its share should increase further in the future.

Thirdly, as with many technology companies there are concerns about obsolescence/replacement risk – in the same way that Apple and co have devoured part of Nokia's business, could Wincor be victim of a similar phenomenon? We can rule out nothing but we believe Wincor's business is far more defensible than many technology companies. Wincor does far more than simply supply a box. Wincor provides automation solutions that begin with customer interface but extend deep into the client's IT infrastructure. Wincor's products are quite embedded into its clients' networks and we believe Wincor will not easily be dislodged.

Fourthly, we are continually impressed with management's conservative behaviour; behaviour that is surprisingly rare amongst public companies. Management has avoided the temptation to make large, expensive acquisitions and remains focused on the company's core capabilities. Whilst returning surplus cash to shareholders, management remains committed to maintaining low levels of debt. In observing their actions and from our conversations with management over the years we have been consistently impressed with their conservative behaviour. We spoke with management again in August and we remain fans of their approach. In the context of the aforementioned risk-return framework, we believe that Wincor Nixdorf scores well and merits its continued presence in the fund. We added to Wincor during the quarter.

Transactions during the Quarter

We added a new holding during the quarter, Micro Focus International, a UK based software company. Micro Focus software programs allow customers to develop, test, assess and modernise business applications. Micro Focus' primary software offering facilitates clients' use of COBOL, a well-established, important and widely used programming language. Due to Micro Focus' long-standing strength in this market and customer's dependence on COBOL, we believe this will be a relatively steady cash flow generator for the company. In recent years the company has diversified into new areas such as software for Applications Testing and Modernisation & Migration. We are less confident about the prospects for these businesses. However, with a clean Balance Sheet and trading at less than 9 times last years earnings, we felt the risk return-profile was attractive and began to accumulate shares in the company. Unfortunately the stock rallied before we had finished buying and because we are price-sensitive we currently own only a modest position in the stock.

IMPORTANT INFORMATION

The Fund is currently available in Ireland via a unit-linked offering of Canada Life Assurance (Ireland) Limited. For this life assurance product, investors should refer to the relevant policy conditions. The strategy is also available on a segregated basis. Investors should consider the investment objectives, risks, charges and expenses carefully before investing. See 'WARNING' and 'IMPORTANT INFORMATION' sections below.

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