Setanta
ASSET MANAGEMENT

FACTSHEET

Setanta Irish Equity Fund – Q4 2011

Fund Description

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

The Fund is an actively managed mandate that will typically be invested in c. 10-20 stocks. Consistent with all Setanta funds, the Fund adheres to a fundamental value approach. By fundamental, we mean we view stocks as fractional ownerships of businesses that we try to understand. By value, we mean we strive to buy stocks below our assessment of their worth, taking into account risks and scenarios. We favour financially sound companies with good track records, where we can make reasoned projections of future profits.

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 Manager

David Pastor

Investment Principles

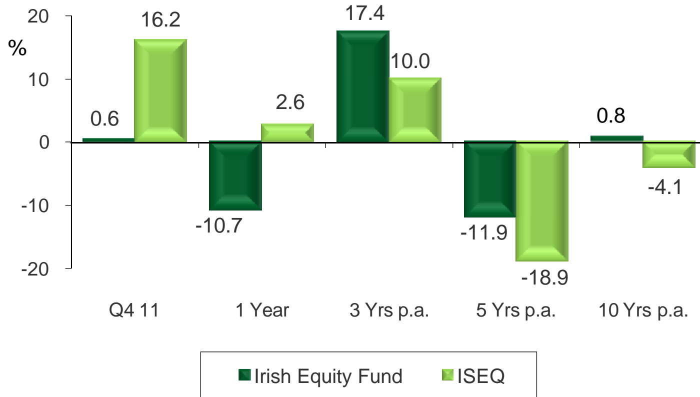
- We do not believe the market is efficient.
- We aim to make investments at a price below our assessment of intrinsic value.
- We make an investment in a business rather than trade securities.
- We believe risk is the possibility of permanent impairment of value.
- We make investments for the long term.
- 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.

Contact Details:

Setanta Asset Management Limited,
College Park House, 20 Nassau Street,
Dublin 2, Ireland.

Alan Hickey, Tel: + 353 1 612 4903
Email: alan.hickey@setanta-asset.com
www.setanta-asset.com

Fund Performance 31.12.11



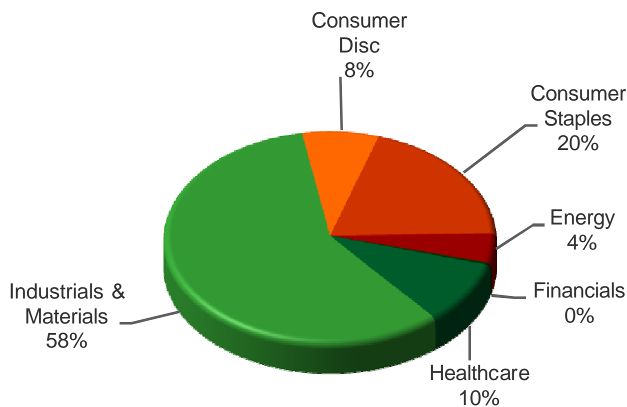
Yearly Performance

Year	2006	2007	2008	2009	2010	2011
Fund	31.9	-18.2	-59.8	51.4	19.6	-10.7
Benchmark	30.7	-24.5	-65.0	29.8	-0.1	2.6

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

Performance Source: Setanta Asset Management Limited. Benchmark: ISEQ. 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.

Sector Distribution



Fund Statistics

PRICE/BOOK	1.3
PRICE/EARNINGS RATIO (FY 1)	14.4
FREE CASH FLOW/EV %	6.2
DIVIDEND YIELD %	2.6
AVERAGE MARKET CAP €BN	2.1
NO. OF HOLDINGS	17

Top 10 Holdings

COMPANY	SECTOR	% OF FUND
DCC	INDUSTRIALS & MATERIALS	9.7
ICON	HEALTHCARE	9.6
TOTAL PRODUCE	CONSUMER STAPLES	9.2
KINGSPAN	INDUSTRIALS & MATERIALS	8.9
ABBEY	INDUSTRIALS & MATERIALS	8.6
IRISH CONTINENTAL	INDUSTRIALS & MATERIALS	8.1
CRH	INDUSTRIALS & MATERIALS	8.0
RYANAIR	INDUSTRIALS & MATERIALS	7.8
CPL RESOURCES	CONSUMER DISCRETIONARY	7.6
C&C GROUP	CONSUMER STAPLES	6.0

The last quarter of 2011 put an end to yet another bumpy year, with the ISEQ returning 2.6% in the year, but with sharp oscillations along the way. From the 53 components of the index at the beginning of the year, only 14 ended it showing advances in the share price; at the very top was Elan whose rating more than doubled in the last twelve months.

The performance of the Fund fell short of the benchmark, with an absolute return of minus 10.7% for the year on a pre-management fees basis. Although it is disappointing to report this underperformance, we are confident that the investment style that helped us obtain such a good performance relative to the benchmark in previous years, will also prove its worth in the future. As we regularly point out in this and other newsletters, we believe that the best timeframe to judge money management skills is 3 to 5 years or longer. Our performance on this basis remains superior to both the benchmark and the median of our peers.

This has been another eventful year in the global economy. Governments around the world debated between the need to stimulate economic activity and the growing balances of public debt. Austerity policies were implemented in a number of countries as a means to consolidate debt, in an effort to regain the confidence of the financial markets. In this context we saw how what started as largely a financial crisis, developed into a sovereign debt crisis (in peripheral Europe), then mutated into a European institutional crisis questioning the very existence of the Euro as a currency, and the role of a number of European Institutions (ECB, EFSF, the Stability and Growth Pact…). In Ireland, after the IMF-led bailout of November 2010, and with spiralling bond yields, the government-commissioned capital adequacy assessment of Irish financial institutions for 2011 resulted in the effective wipe-out of their existing shareholders.

The performance of the Irish economy was weak indeed, with a depressed domestic demand somewhat offset by export growth coming from the highly competitive healthcare and information technology industries located in Ireland. Unemployment and disposable income metrics continued to deteriorate, although showed some signs of stabilisation.

This is a time for predictions for the year ahead. While they do make an interesting read, and surely help us understand what the consensual outlook for the economy is, this is an area where we normally do not like to dwell. The track record of Setanta in this and other funds has relied on our ability to pick stocks, regardless of the macroeconomic environment. We will continue to develop and apply our skills to identifying undervalued securities, offering the best combination of returns with a low probability of impairing your capital.

As we remember the turbulent past year, we would like to take this opportunity to reflect on a number of the tenets of our value investment philosophy, which, if anything have been reinforced over time.

Debt aversion

After binging in debt for the better part of the last two decades, the world is now embarking on a process of painful deleveraging. Corporates with damaged balance sheets are in a process of asset sales and balance sheet consolidation while companies in a strong financial position have been able to maintain or improve their market shares and have protected their shareholders' interests. Not surprisingly, over the year, some of the Fund's worst performers have been amongst the more leveraged names, this being again the case of the Irish financials.

If we add a low market valuation of a company to the premise of a strong balance sheet, a world of possibilities opens for the creation of shareholders wealth. We think a good example is **CPL Resources**, the Irish Recruiting and Staffing services company. We bought CPL for the Fund at the end of 2010 in the region of €2.20 a share, €1.20 of which backed by unencumbered cash and deposits in the company's balance sheet. Founded in 1989, the company grew to become the biggest recruiter in the Irish market. As the crisis struck, management reduced capacity, and overheads, while taking the opportunity to snatch assets from bankruptcy from failing peers. The company outlasted multinationals like Robert Half, who decided to exit the Irish market in the last few years. The founding management is still at the helm, owning 33% of the company, they pay themselves frugally and when we talked to them they struck us as genuinely honest and motivated. Earning 11c per share, we bought at what we considered a very cheap price. With too much cash on the balance sheet and already paying out a nice dividend it was only a matter of time before management decided to distribute some of that extra capital. This finally happened over the last quarter via a tender offer, whereby the company bought back 30% of its shares outstanding.

Given the way this operation was designed, it was in our best interest to tender our shares, but still seeing value in the company we worked to rebuild our original position in the Fund, this time for a greater share of the business (as the number of shares had reduced). The point is that those companies with strong balance sheets have flexibility and, if management is worth its salt, they should be able to take advantage of any available opportunity to create value for shareholders in the stock, debt or the mergers / acquisitions markets.

Many of the Fund holdings exhibit this financial strength that we like. Companies such as Abbey, Ryanair, ICON, amongst others have surplus cash, and are in a process of returning cash to shareholders, or are expected to begin it in 2012.

Diversification, knowledge and control

In the words of Marty Whitman, Third Avenue Chairman and Value Investor "extraordinaire", *diversification is only a poor surrogate for knowledge*. If we may add to this thought, diversification based on a **hypothesis of market efficiency** is a very poor surrogate for knowledge. In our mind, index-based investment makes little sense.

Through the year, we have met with / spoken to a number of the management teams of the companies we hold in the Fund, as well as devoted time to carefully read their periodic financial disclosures. All this effort tots up to what we think is a good understanding of how these companies generate profits, what risks they are undertaking and managements' ability to allocate capital if applicable.

There is an important caveat though. We find it is a healthy habit to question our, as well as other people's, judgement. We are well aware of the fact that even if we were able to collate and correctly process all the public information available for a given company, we would still require a healthy degree of diversification to protect ourselves from the "illusion of complete knowledge". Even if we had instant, non-public, management-like information for a given company we wouldn't bet the farm on it either. There are simply too many "unknown unknowns" and even if we were in a certain world, the non-controlling nature of our holdings, would prevent us from putting all our eggs in the same nest.

Lack of control, uncertainty and bounded human rationality are all reasons why we can very rarely justify Fund weights above the 15% mark. CRH is a case in point. In it we see many of the features that we like and seek; a strong balance sheet relative to its peers in the industry, a well-diversified asset base, management with a good track record and a return on capital culture. It is cheap too! At year end it was trading at €15 a share, roughly ten times the average earnings they have been able to deliver over the past ten years. We expect it to do well in the future and for this reason it has a place in the portfolio, however, we can hardly justify the 25% weight it commands on the ISEQ index for the reasons explained above.

Exhibiting this concentration, we expect the performance of the Fund to diverge, sometimes markedly, from that of the ISEQ. If CRH was to rerate faster than the rest of the Fund's holdings (as it happened in this last quarter), the result would be a period of relative underperformance and vice versa.

Margin of safety

The last of the concepts we want to elaborate upon in this newsletter is maybe one of the most important ones for us. Margin of safety is at the heart of everything we do here in Setanta. If you sat with us in our investment meeting you would quickly see how important a "margin of safety" is for an idea to be granted the "go ahead".

Margin of safety cannot be measured quantitatively; we don't buy Euros at fifty cents. In our mind, margin of safety is a qualitative process where once we handicap any potential Fund candidate for all the risks we can think of, we still require an extra cushion to break our fall in case something goes wrong: competitive advantages erode, capital gets misallocated, business model strengths are misunderstood., etc …

As we write this, it is our belief that all of the Fund holdings are currently trading at significant discounts to their asset or earnings-power based intrinsic values, which in our opinion, augurs well for the future performance of the Fund.

At the end of the day, we want to convey that we believe that by adhering to our value investing principles, we are confident that we can match, and hopefully surpass, the Index performance But, importantly, we can do it by incurring a lower level of risk than by just replicating the index. It is this conservative, risk-based approach that we think better defines our investment style, which given time we hope will produce a satisfactory return on your investment.

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 overleaf.

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WARNING: Past performance is not a reliable indicator of future results. The price of units and the income from them may go down as well as up and investors may not get back the amount invested. The return may increase or decrease as a result of currency fluctuations. Forecasts are not a reliable indicator of future performance.