Setanta Dividend Fund

Q4 2018

Fund Description

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

The is an actively managed equity portfolio, which holds 30-50 global high yield stocks. The portfolio is managed in accordance with the Setanta investment philosophy. That is, the managers seek to own good businesses for the long-term at prices below what they think they're worth, carefully considering each investment's risk profile. The Fund further distils this philosophy by targeting stocks where management have both the willingness and ability to distribute meaningful dividends to shareholders.

The fund is managed by three portfolio managers, who also look to leverage off the experience and knowledge of their colleagues. The aim is to achieve a sensible level of diversification on a sector and geographic basis. Stocks are chosen through bottom-up analysis, based on investment merit. The fund can hold up to 10% cash where investments of sufficient quality cannot be found. Rather than focusing on the historic level of volatility of an asset, the portfolio managers regard the probability of permanent impairment of capital as the most relevant measure of risk. In doing so, they seek to maximise downside protection by understanding the risks posed by the valuation, financial, and operational characteristics of the asset. The investment objective of the Fund is to outperform the MSCI High Yield index over the long term.

Portfolio Managers

Richard Doyle, CFA; David Pastor, CFA; Caroline White, CFA

Our Investment Principles

We do not believe markets are efficient

We invest below our estimate of intrinsic value

We invest in businesses rather than buying stocks

Preservation of our clients' capital is key

Investing is a marathon, not a sprint

We are not afraid to swim against the tide

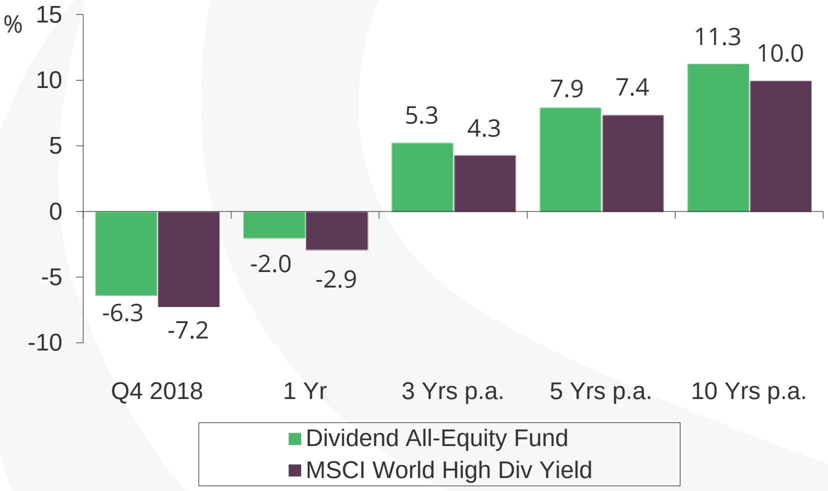
We consider scenarios rather than making forecasts

Businesses we own must have strong balance sheets

We make mistakes and always endeavour to learn from them

We will act with integrity in everything we do

Fund Performance – 31.12.18



Yearly Performance

Year %	2014	2015	2016	2017	2018
Fund	11.9	12.2	11.9	6.3	-2.0
Benchmark	16.7	7.8	12.6	3.8	-2.9

Performance Source: Setanta Asset Management Limited. Benchmark: MSCI High Yield Index (100% Euro). The Fund returns since 30.09.07 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 unit prices prior to this are derived from a net of fee price, adjusted for the management charge to be representative of the gross of fee performance. **Fund Statistics Source:** Bloomberg (metrics include Financials)

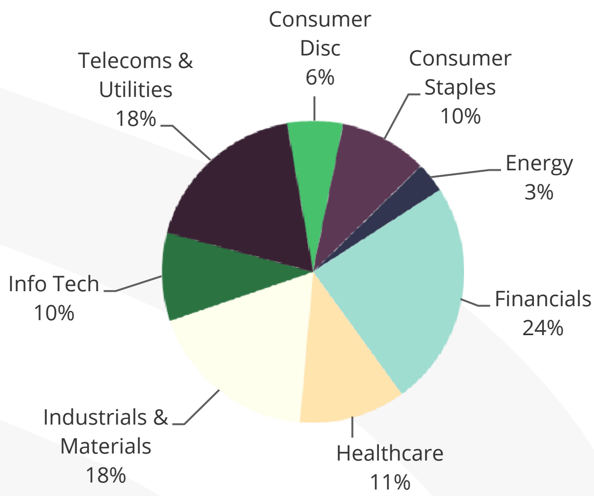
Top 10 Holdings

COMPANY	SECTOR	% OF FUND
FEDERATED INVESTORS	FINANCIALS	4.2%
FORTESCUE METALS	INDUSTRIALS & MATERIALS	3.6%
LANCASHIRE HOLDINGS	FINANCIALS	3.4%
NWS HOLDINGS LTD	INDUSTRIALS & MATERIALS	3.4%
GLAXOSMITHKLINE	HEALTHCARE	3.3%
SMITHS GROUP	INDUSTRIALS & MATERIALS	3.3%
PROCTER & GAMBLE	CONSUMER STAPLES	3.2%
PROXIMUS SA	TELECOMS & UTILITIES	3.1%
NOVARTIS AG	HEALTHCARE	3.1%
YARA INTERNATIONAL	INDUSTRIALS & MATERIALS	2.7%

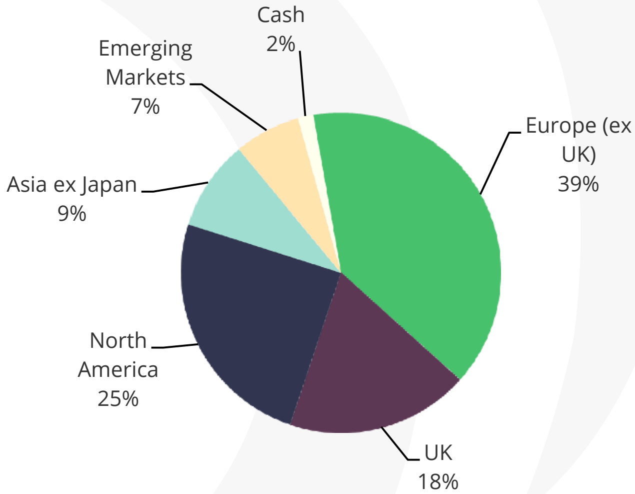
Fund Statistics

PRICE/BOOK	1.7
PRICE/EARNINGS RATIO (FY 1)	13.4
DIVIDEND YIELD %	4.4
AVERAGE MARKET CAP €BN	48.9
NO. OF HOLDINGS	44
DEBT/EQUITY %	53.7
ACTIVE SHARE %	79.1

Sector Distribution



Geographic Distribution



SETANTA
Asset Management

Commentary

After falling earlier in the year, global stock markets generally rose during the second and third quarters of the year, thus continuing their upward trend since March 2009. From its peak, the world market (as measured in euro by the MSCI World Index) then fell 17% in just over three months, its steepest fall in three years. Many reasons have been attributed to this sharp fall, including an end to the 'quantitative easing' of monetary authorities, the escalating US \ China trade dispute, and wider fears about the political and economic relationships between sovereign nations. One could certainly wonder why it is now that these fears are materialising, as market participants have heretofore largely 'shrugged their shoulders' to similar risks in the past.

The MSCI World High Dividend Yield index (-2.9%, euro terms) performed better than the MSCI World Index (-4.1%, euro terms), largely due to a much better performance in the sharp market fall of Q4. After a period of years in which the MSCI World index has been ahead of the MSCI World High Dividend Yield index, this perhaps reflects a view that income-oriented companies are more robust in times of strife, one that we would share. While the Dividend Fund fell just under 2% over the year, it outperformed the MSCI World High Dividend Yield index, its benchmark. Over the much more relevant long-term periods, the fund continues to perform well, rising 5.3%, 7.9% and 11.3% per annum over 3, 5 and 10 years respectively (all gross of fees, euro terms).

We cannot accurately predict the future. However, we can endeavour to position the fund in a prudent fashion for whatever that future might hold. We believe that the fund is well-positioned in this regard, holding companies characterised by sustainable businesses, strong balance sheets, and durable cashflows. While we would be happier for the market to rise further (and thus keep everyone satisfied), we take comfort in the fund's historic ability to perform relatively well in weaker markets. In this report, we discuss the stocks that made the most positive and negative contributions to the fund as well as also reviewing major portfolio changes in the year.

Main Contributors to Fund Performance

Swedish Match, maker of smokeless tobacco products, has been a good investment for us. The company reported good sales growth, improved its operating margin in its core Nordic region, while making a breakthrough with its new 'Zyn' product outside this region. It continued to return substantial amounts of cash to shareholders, both through ordinary and special dividends and large share repurchases. The stock rose very strongly through the first half of the year during which we substantially reduced our position, thus booking gains for the fund.

Stock	***Performance Contribution***	***Stock***	***Performance Contribution***
Swedish Match	0.77%	Harley Davidson	-0.84%
Cisco	0.76%	Vodafone	-0.82%
NWS	0.59%	BASF	-0.72%

Commentary

Under the leadership of a new CEO, **Cisco** is changing from its one-time sale \ hardware-based business model to a subscription \ recurring revenue model. It is in a good position to take advantage of the expected growth in connectivity resulting from increasing wired and wireless communications and the 'Internet of Things'. In 2018, Cisco continued its record of growing sales, profits, and dividends. As we noted in last quarter's review, while Cisco is not as favourably valued as at the time of our initial investment we believe that its high returns are very much sustainable.

NWS continues to both grow revenues and to generally improve its profitability. It is well positioned to benefit from the urbanisation and industrialisation of mainland China, whether in operating toll roads, managing water and waste facilities, or facilitating China's 'belt and road' initiative through rail and port terminals. It has a similar position in Hong Kong, albeit with a tilt towards more economically-sensitive areas, and benefits from the generally constrained supply of land and space for infrastructure.

Harley Davidson continued to report declining unit sales of its motorcycles. This prompted closure of one of its factories, as well as a material restructuring cost. The company was also a somewhat innocent victim of President Trump's trade policies, suffering from tariffs relating both to steel imports and exports to the EU. Despite this, its profitability was sound, while cashflow generation was also good, as Harley's new bikes sold at good prices. While Harley's declining unit sales are certainly a concern, the company is addressing this through investment in both new bikes and broadening the appeal of recreational motor cycling. Harley's disciplined approach to selling (and related pricing power), its huge brand strength, and the discipline of its management continue to underpin the stock. Harley currently has a dividend yield of 4.5%, which is supplemented by substantial share repurchases.

2018 wasn't a good year for **Vodafone**. Competitive dynamics worsened in Spain and Italy, two of its biggest markets, where new entrants have been rapidly capturing market share. The company also had to pay 'top dollar' for its allocation of fifth-generation airwave spectrum in Italy, prompting fears that it will have to pay more than expected in other countries. A weakening economic outlook and uncertainty about the outcome of the relevant authorities' reviews of its proposed acquisition of Liberty Global's assets in Germany and Central Europe exacerbated matters. On the positive side, the German, British and some of its African businesses were strong, and the company's strategic and competitive position is much improved after years of heavy investment. The company certainly faces challenges, but is, in our view, good value, yielding more than 8% at the year end.

The share price of **BASF**, the global chemical company, fell sharply in the second half of 2018, reflecting weak results and lowered profit expectations. This reflected a sharp slowdown in the automotive industry, an important end market for the company, general economic weakness in China, attributed to US \ China trade war concerns, and logistical difficulties at its key German production site due to the exceptionally low level of the Rhine river (a worry, perhaps, not just for the company, but all of us). Our view very much remains that BASF is an excellent company, distinguished by its commitment to creating value through innovation and through its largely unique commitment to integration. It currently yields a dividend of around 5%.

Commentary

Major Changes to the Fund

The Fund acquired eight new holdings during 2018, ending the year with 44 holdings. Of these, we have commented above on **NWS** and in the earlier 2018 quarterly reports on **Coca-Cola Amatil**, **Sampo**, and **Samsung Electronics**. The Fund also acquired positions in Saga, Fortescue Metals Group, Bolsas y Mercados Espanoles (BME), and United Utilities. It entirely sold its positions in People's United Financial and Euler Hermes, while substantially reducing its position size in strongly-performing stocks such as Swedish Match, Sysco and Sandvik.

Saga is a UK financial company that provides insurance underwriting, insurance broking and travel services, including cruise holidays, largely to people over 50. After a profit warning related mainly to the company promising growth that it could not achieve and poor communication, which spooked investors, we took a position in the company. We believe that Saga has many assets including its strong position in a niche market, a good brand, a low-cost base, favourable underwriting model and two brand new cruise ships. We acquired our shares at a multiple of its earnings of around 10x and a dividend yield in excess of 7%.

Fortescue Metals Group is one of the world's largest miners of iron ore. While it typically sells its grade of iron ore at a discount to the market, Fortescue is distinguished by having the lowest cost of production in the industry and it also owns the critical infrastructure necessary to be a key player in this industry. Prior to our acquisition, the company repaid a substantial amount of debt and refinanced the remainder, so that it completed its journey from entrant to the industry to established industry player in just over 15 years, a remarkable outcome. We acquired our position at a price corresponding to a Price\Book multiple of 1.1x and Free Cashflow (five year average) to Enterprise Value of 9.0%.

BME is a financial exchange business that operates the regulated financial market in Spain and associated post-trade infrastructure. We believe there is plenty to like about financial exchange businesses. They are highly cash generative businesses, benefitting from high market share due to their natural monopoly characteristics. Customers are attracted by their main service (access to a liquid trading venue), which in turn creates the high volumes that makes them liquid, a virtuous circle. While BME has had to navigate some choppy water in the last few years, including regulatory changes and increased competition, it has maintained a good level of profitability. We believe most of these headwinds have stabilised, while BME's shareholder-friendly dividend policy (dividend yield over 6.0% yield at the time of purchase) appeals to us.

We acquired a position in **United Utilities**, a UK based water utility and a stock we know well, as it is owned in other Setanta funds. Prior to our acquisition, the stock had been weak on fears relating to Brexit, a tougher regulatory environment and potential nationalisation of utility assets in the event of a Jeremy Corbyn-led UK government. Believing these concerns to be more than reflected in the stock price, we acquired a position at a price to United's regulated asset base of 1.0x and a dividend yield of 7.0%.

Our holding in **Euler Hermes**, the French credit insurer, originated in work undertaken by our Financials analyst. In late 2017, it received a bid from its parent, Allianz, the German insurer. Together, we made the case to the company for a price that better reflected our view of the company's dominance of its industry niche. We were unfortunately alone amongst shareholders taking this active position. We thus accepted the offer, finding solace in the substantial return to the fund from the investment over a short time period.

Commentary

People's United, a US regional bank, operating mainly in the north-east of USA, was sold largely to make way for the new stocks above. We initially took a position in the company on account of its strong capital backing and the expectation that this would position it well for future years. As those future years have materialised, we have been a little disappointed in the company's ability to improve its return on equity. Nevertheless, our decision to sell the stock is less a reflection on it and more on the attraction of the stocks that are replacing it.

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IMPORTANT INFORMATION