Global Focus Fund (EUR) – Q2 2017

Fund Description

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

The Fund is an actively managed, concentrated Global Equity Fund that is invested in circa 20 stocks. As a Fundamental value investor our research is designed to properly understand how each business functions and to consider pertinent risks to the business. We attempt to value each business, incorporating relevant upside and downside scenarios. As such the Fund attempts to invest in the most attractive stocks across all the firm's strategies using a risk-return framework. Investments are made for the long-term and are based on investment merit rather than with reference to benchmark. This Fund is mandated to be fully invested in equities. Due to the concentrated nature of the Fund, performance may be volatile. The investment objective of the Fund is to outperform the MSCI World index over periods of three years or more.

Fund Commentary

The market value of the Global Focus Fund gained by 1.8% (gross of fees, Euro-terms) in the first six months of the year (0.5% behind the 2.4% benchmark MSCI World in the period). This may sound like a skinny return on your investment, but it must be seen in the context of the even skinnier returns currently on offer from other asset classes, especially in bonds; for example, German 10-year bonds yielded less than 0.5% at the time of writing. This is causing investors to take on unusual risks in the search for additional return. This was highlighted in June, when the "bad boys" of the government bond market, Argentina, issued a $2.75bn US dollar-denominated 100 year bond yielding 8%. If history is any guide, this bond will have been defaulted on four times before the principal is due to be paid (i.e. good luck with that!). To our minds, a mere 8% seems grossly inadequate compensation to investors. Amazingly, the issue was in high demand, three-and-a-half times oversubscribed. In that light, we are highly confident in the 100-year prospects of the Fund.

(Fund Commentary continued on Page 3)

Portfolio Managers

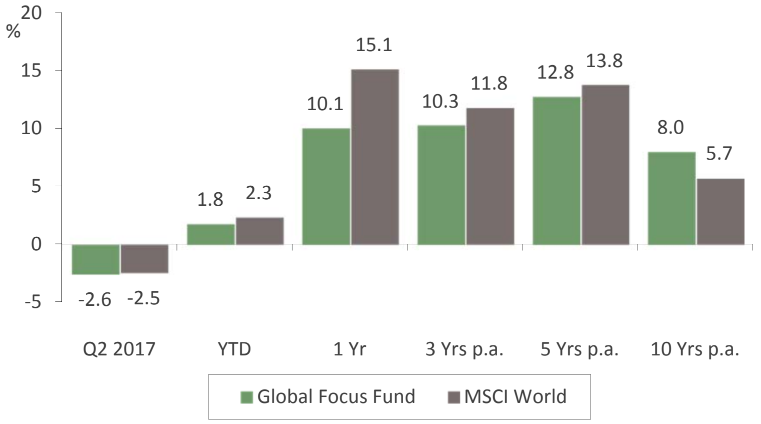
Rowan Smith & David Coyne

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.

Setanta
ASSET MANAGEMENT

Fund PERFORMANCE (EUR) – 30.06.17



Performance Source: Setanta Asset Management Limited. Benchmark: MSCI World. 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 (Valuation) Median ex Financials

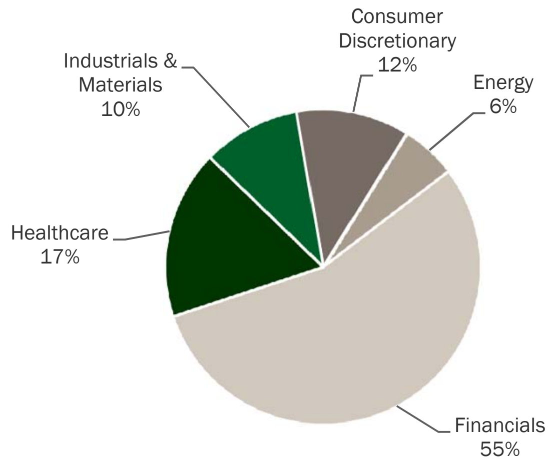
Fund HOLDINGS

COMPANY	SECTOR	% OF Fund
LSL PROPERTY SERVICES	FINANCIALS	8.8%
STERIS PLC	HEALTHCARE	8.3%
JOHNSON & JOHNSON	HEALTHCARE	8.1%
BERKSHIRE HATHAWAY	FINANCIALS	7.5%
MINCON GROUP	INDUSTRIALS & MATERIALS	7.3%
FAIRFAX FINANCIAL HOLDINGS	FINANCIALS	7.0%
LEUCADIA NATIONAL	FINANCIALS	6.7%
MARKEL	FINANCIALS	6.2%
RICHEMONT	CONSUMER DISCRETIONARY	5.8%
GRANITE REAL ESTATE	FINANCIALS	5.7%
LANCASHIRE HOLDINGS	FINANCIALS	4.5%
BROOKFIELD ASSET	FINANCIALS	3.9%
DIAMOND OFFSHORE	ENERGY	3.0%
SWATCH GROUP	CONSUMER DISCRETIONARY	2.6%
RYANAIR	CONSUMER DISCRETIONARY	2.6%
NATIONAL OILWELL	ENERGY	2.4%
DCC	INDUSTRIALS & MATERIALS	2.2%
GREAT EAGLE HOLDINGS	FINANCIALS	1.9%
CASH		5.3%

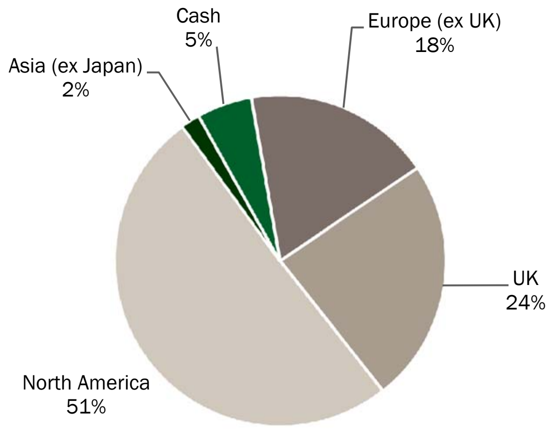
Fund STATISTICS

PRICE/BOOK	1.5
PRICE/EARNINGS RATIO (FY 1)	18.2
DIVIDEND YIELD %	1.5
AVERAGE MARKET CAP € BN	45.1
NO. OF HOLDINGS	18
DEBT /EQUITY %	34.3
ACTIVE SHARE %	98.2

SECTOR DISTRIBUTION



GEOGRAPHIC DISTRIBUTION



YEARLY PERFORMANCE

Year	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Fund	-35.6	3.9	7.6	27.3	17.0	-2.7	-35.2	44.0	28.2	1.5	9.0	20.0	19.1	7.3	11.7
Benchmark	-32.1	11.3	6.5	26.2	7.4	-1.7	-37.6	25.9	19.5	-2.4	14.1	21.2	19.5	10.4	10.7

Humbled

What a difference four years makes. In the June 2013 Fund report I wrote the following: "Over the last 10 years, the Fund has grown by 9.9% per annum (gross of fees), ahead of the MSCI World Benchmark of 6% p.a., a result that ranks us alongside the equivalent of the U.S. Navy Seals of Fund managers."

That self-congratulatory pat-on-the-back was ill-judged. As I write the same report in June 2017, the Fund has lagged the benchmark over 1 year, 3 years and 5 years (to the tune of c.1% per annum). Rowan Smith and I, the Fund's managers, are suitably humbled (though we implore you to remember that the Fund is still ahead over our favoured 10 year period by c.2% per annum).

Given the rest of the Setanta suite of funds have performed well (and in some cases, excellently) over recent years, Global Focus Fund investors may be wondering what's going on.

The first thing to say is that there has been no change to how the Fund has been managed. Nor has there been a change in personnel. Rowan has been on the Fund since 2003 and I joined him in 2006. And we don't believe we have lost our investment "touch" – we are both involved in other funds that have performed well in recent times. Our goals are still the same: to outperform a global benchmark of stocks, with a mindset of increasing the value of our investors' wealth over the long run (the same words were used in the June 2013 Fund report). While we have not achieved the relative goal over the last 5 years, investors have nevertheless seen the absolute value of their investment increase substantially.

Secondly, we are more likely to underperform in strongly rising markets. In the 5 years to end-June, the benchmark return has increased by 14% per annum, which is well above the long-run return for equities. This has resulted in elevated valuations for stocks in general and we have struggled to find enough that were attractively priced. Thus, over the last 5 years the Fund regularly held between 5 and 15%, which clearly had dragged fund performance. While we are only looking to buy 15-20 stocks for the Fund, this very concentration means we have to be extra cautious of what we buy. Cash at quarter-end was just over 5%.

Thirdly, as a concentrated fund, performance will tend to be lumpier than for funds with more holdings. For example, the Fund was c.10%, c.18% and c.9% ahead of benchmark in years 2006, 2009 and 2010. We feel good about the current prospects for the Fund. Five years of under-performance could be reversed in one good year.

Fourthly, while we have had many good performers over the last 5 years, unfortunately too many of our investment choices were below par. Some were clear mistakes, while one or two others have not fully played out yet but we have to be realistic and admit that the evidence is stacking up against us. A synopsis of the three standout offenders is as follows:

- **Tesco**, the UK-head quartered retailer

We thought that Tesco's market leading positions in core markets would enable them to compete effectively with newer, cheaper retail formats. We underestimated the difficulty of the problems. The position was sold mid-2016 having lost over 30% on our investment. We covered this mistake in the Q3:16 Fund report.

- **Diamond Offshore**, the offshore oil & gas driller

We first bought Diamond towards the end of 2013 just ahead of a sharp fall in the price of oil, which has led to a slashing of capex on oil & gas exploration and production. In fact the downturn has been deeper and longer than any time in the last 50 years in many parts of the world according to the CEO of Schlumberger, the largest oil services company globally. For Diamond Offshore this is as bad as it could have got. The share price is down c.75% since our initial purchase and we look back ruefully at the timing of our purchase. We were attracted to the company's history of value creation, the main source of which was the care and patience management took to buying drilling rigs at the right price (i.e. good capital allocation skills). While we knew that the offshore industry could be brutally cyclical, the duration of the downturn and the ability of weak competitors to stay in the game this down cycle has really surprised us. In short, we should have been far more patient in waiting for a depressed share price. The Fund still retains a holding in the company. We know from history that prolonged underinvestment sows the seeds of the next boom.

Demand and supply of drilling equipment can snap into reverse very quickly, which would lead to a scramble by energy companies to lease out Diamond's rigs at far higher day rates than they fetch today. Just as it has taken years for demand-supply to normalise on the way down, supply could lag demand for a long time in the upswing which, if it came to fruition, would result in massively higher profits (and likely a massively higher share price) in the next 3-to-5 years.

- **LSL**, UK retail estate agent

We first purchased LSL in the second half of 2014 and this is one that we feel the jury is still out on. As an estate agent, it has been affected by the low level of housing transactions and fairly stagnant house prices in the UK (stagnant economy, Brexit). Further pressure has come from competition, mostly from traditional high street agents who are all living on more meagre scraps. In addition, the last few years has seen the rise of online estate agents – the best-known of these is Purplebricks – who have a cut-price / cut-service offering. So far the online agents account for a small part of the market (c.5% according to Rightmove, the leading residential property portal in the UK) and so haven't really affected profits at the traditional agents yet. We are not yet convinced that the online estate agent business will be viable long-term. Estate agency costs are mainly people; what you save from not having a high-street presence, you lose by needing to advertise heavily on TV. Can an online agent really offer an appropriate service for a far cheaper price? Regardless, so far investors are convinced. Purplebricks' share price has increased by more than four-fold since its IPO 18 months ago, while the share prices of LSL, Countrywide and Foxtons, the three quoted traditional UK estate agents, have all fallen heavily. Only time will tell who is right, but we have done a lot of homework on LSL. We like the fact that the group Chairman and former-CEO Simon Embley owns 6% of the company, so his incentive is clearly to create long-term value for shareholders like us. The group is pursuing its own self-help initiative and is looking to lift branch profitability across its network. It is quite an entrepreneurial organisation and in the past has built up businesses organically as opportunities arose (e.g. one that deals with repossessed homes for banks, which was material for them during the financial crisis; also they built out a home lettings business). Management has studied the online model for a number of years and have struggled to make the numbers work. However, they continue to look at their options and will launch a competing offering if it makes sense to do so. At the current share price, LSL is valued at 10x our conservative estimate of sustainable profits, which we think gives us an excellent chance of getting a favourable investment return in the fullness of time.

While our tail is between our legs, we will learn from our mistakes and continue to put all of our efforts into producing a good risk-adjusted return for the Fund.

Transactions

We purchased one new stock for the Fund during the second quarter. **Ryanair** will be known to you all. Whatever experiences you may have had as a customer over the years, by all financial measures Ryanair is a fabulous company. Our embarrassment is that it has taken us so long to become a shareholder. The source of Ryanair's greatness is that it is the lowest cost provider and it is also helped greatly by the inefficiencies of the flag-carrier competitors. We believe that Ryanair's cost position is at this point unassailable, an economic "moat" that will deliver value creation well into the future. Despite 30 years of eye-popping growth in passenger numbers, routes and airports, the company still has a lot of runway (ahem) ahead of it. And don't be fooled by the antics of its CEO Michael O'Leary – this is a very conservative and savvy management team. We are aware that the current environment for airlines in Europe is very favourable. Planes are full, which is the key to profitability as the cost of having the last passenger on-board is close to zero. However, this is a cyclical industry and we worry that current high profits has led airlines to place orders for too many planes, that the operating environment in the coming 3-5 years could be more difficult. In such an environment, Ryanair will trounce its competitors, but it would likely hit profits and the share price. Reflecting this, we purchased a smaller than average position in the company. In the short period since then the stock has risen by over 30%. As owners of the stock it's good news, but as we were looking to buy more shares at lower prices we curse the good news!

The Ryanair purchase was from cash. There were no sales during the quarter.

David Coyne – Portfolio Manager

COMMENTARY

Setanta ASSET MANAGEMENT

Contact Details:

Setanta Asset Management Limited,
Beresford Court,
Beresford Place, Dublin 1, Ireland.

Brendan Moran, Tel: + 353 1 704 2028
Email: brendan.moran@setanta-asset.com
www.setanta-asset.com

Setanta ASSET MANAGEMENT