Setanta Global Equity Fund
Q2 2020

Fund Description

The **Global Equity Fund** ('the Fund') is managed by Setanta Asset Management Limited ("Setanta") and is a representative account of the Global Equity strategy. The Fund is an actively managed equity portfolio which holds c.80-100 global stocks. The portfolio is managed in accordance with the Setanta investment philosophy by a team of eight global sector specialists, overseen by two lead portfolio managers. The aim is to achieve a sensible level of diversification on a sector and geographic basis. Reflecting this, portfolio sector weights are generally set so as broadly similar to the sector weights in the benchmark. Within each sector, stocks are chosen through bottom-up analysis, based on investment merit. 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 World index over the long term.

Fund Commentary

The Bloomberg headline on the 1st of July pretty much said it all: "S&P 500's Past 100 Days Were Its Best in Almost Nine Decades". That followed the fastest ever 30% decline for the index – 22 days – in February / March.

(Fund Commentary continued on Page 3)

Portfolio Managers

David Coyne & Sean Kenzie, 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

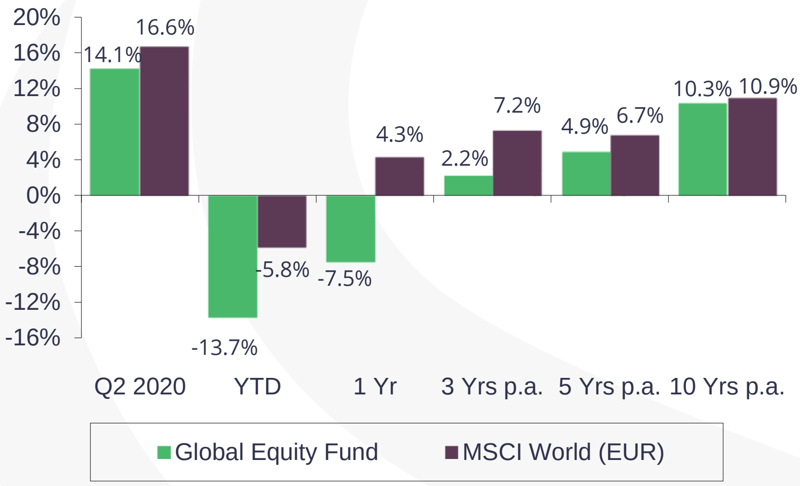
We consider scenarios rather than making forecasts

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 – 30.06.2020 (EUR)



Performance Source: Setanta Asset Management Limited. The Fund returns stated are based on the movements in the unit prices of the ILA/CLI Setanta Global Equity Fund [P-GLB1] and are gross of management fees. The performance will be reduced by the impact of management fees paid, the amount of which varies**. Benchmark:** MSCI World (EUR) **Holdings Source:** Setanta. Sector allocations based on invested portfolio only (excludes cash). **Fund Statistics Source:** Bloomberg

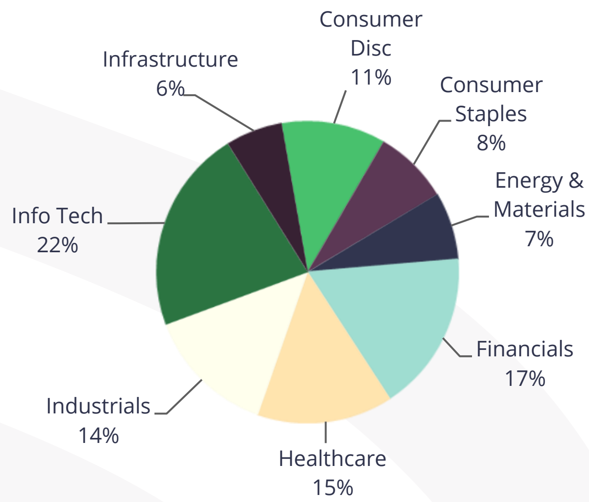
Top 10 Holdings

COMPANY	SECTOR	% OF FUND
MICROSOFT CORP	INFORMATION TECHNOLOGY	4.8%
DCC	INDUSTRIALS	3.1%
BERKSHIRE HATHAWAY	FINANCIALS	3.0%
LANCASHIRE HOLDINGS	FINANCIALS	2.8%
ORACLE CORP	INFORMATION TECHNOLOGY	2.5%
KEYSIGHT TECHNOLOGIES	INFORMATION TECHNOLOGY	2.4%
JOHNSON & JOHNSON	HEALTHCARE	2.4%
CISCO SYSTEMS	INFORMATION TECHNOLOGY	2.3%
JOHNSON CONTROLS	INDUSTRIALS	2.2%
ERICSSON	INFORMATION TECHNOLOGY	2.2%

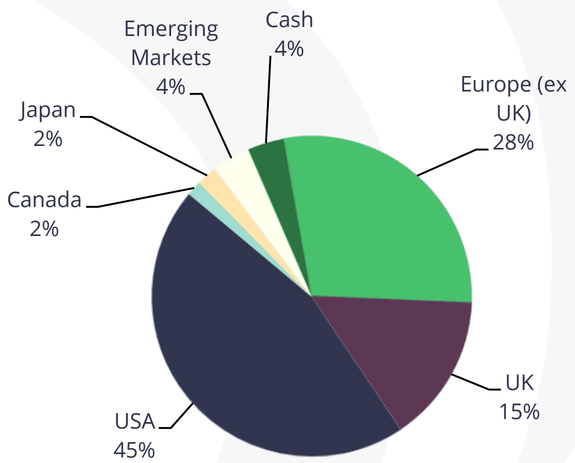
Fund Statistics

PRICE/BOOK	1.7
PRICE/EARNINGS RATIO (FY 1)	17.2
DIVIDEND YIELD %	2.2
AVERAGE MARKET CAP €BN	75.9
NO. OF HOLDINGS	86
ACTIVE SHARE %	85.1
DEBT/EQUITY %	61.6

Sector Distribution



Geographic Distribution



Yearly Performance

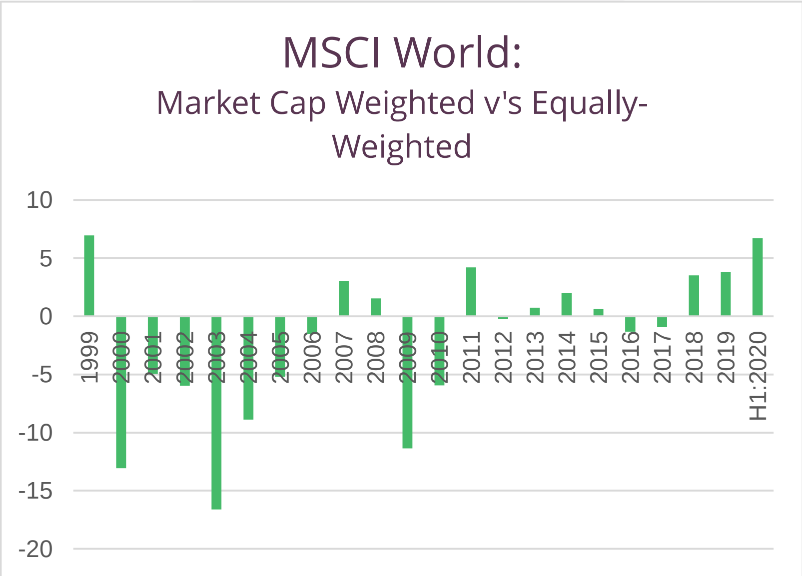
Year %	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
Fund	-1.0	-36.6	32.2	16.2	0.9	14.1	24.5	20.6	9.0	16.2	8.8	-3.9	22.0
Benchmark	-1.7	-37.6	25.9	19.5	-2.4	14.1	21.2	19.5	10.4	10.7	7.5	-4.1	30.0

Commentary

Due to the damaging effects of COVID-19, the OECD recently forecast the global economy to shrink by between 6% and 7.6% in 2020 (depending on whether or not there is a second wave). It will be the worst peacetime recession since the Great Depression. This is despite unprecedented levels of wage and business subsidies by governments around the world, which unquestionably prevented mass unemployment and bankruptcies. While a recovery is expected in 2021 and beyond, this very much depends on economies being able to reopen, with few COVID-induced hangovers (including weening economies off subsidies). That is far from certain.

Quite remarkably, in our opinion, at a general level investors have largely bought into the recovery story. The MSCI World rose 16.6% in Q2 (Euro-terms) and finished the first half of the year down just 5.8% (Euro-terms). The Fund lagged this strong performance by 2.5% in Q2 and year-to-end June was behind by 7.9%.

In contrast to the 5.8% first half fall in the MSCI World, which is a market cap-weighted performance of 1,600 stocks, the 'typical' stock in the benchmark fell by around double that rate (the median fell 12.7% and the simple average stock fell 11.3%). In other words, large capitalisation companies materially outperformed. This can be seen in the chart below, which shows the performance difference between the MSCI World cap-weighted and equally-weighted indices (same constituents) by year back to 1999 when the latter index was created. When large cap stocks outperform, the cap-weighted index outperforms the equal-weight one and vice versa. The cap-weighted index has outperformed by a cumulative 14% over the last 30 months, including a 6.7% difference in H1:20. Granted, it's nothing like the outperformance of the equal-weight index between 2000 and 2006 (when small caps outperformed), but that in turn was a reversal of the large cap outperformance in the mid-to-late 1990s. As we pointed out in last quarter's letter, the fund has a significant overweight in small and mid-cap stocks (23% at quarter end versus benchmark of less than 2%). We estimate this has cost the fund almost 4% in relative performance in H1:20. We are not convinced it is because our small and mid-cap stocks are worse effected by COVID-19. Overall we feel it is undeserved and would hope to recoup performance over time when the market better appreciates their potential.



The outperformance by large cap companies has not been evenly distributed unfortunately – some stocks have hogged more of the limelight than others. At one end of the spectrum is **Berkshire Hathaway**, the $440bn diversified financial conglomerate. Berkshire fell 5% in Q2 leaving the share price down 20% for H1, despite a cheap valuation, a collection of generally good-to-excellent assets and a cash rich balance sheet that should be the envy of the world. The share price performance of Berkshire is all the more confusing seeing as Berkshire owns nearly 6% of Apple (+25% in H1) and which now accounts for over 20% of Berkshire's market cap.

At the other end of the spectrum, there are many high quality companies that we follow but don't own, some of which are currently trading at extremely high valuations (over fifty times earnings). Their valuation premium over the rest of the market has widened again this year, perhaps the result of their near-term earnings certainty combined with ultra-low interest rates. You should not expect us to buy these stocks at these valuations.

If the valuation of some high quality growth names is raising an eyebrow, other areas of the market are truly eye popping. Stocks that are favourites with day traders have in some cases risen by hundreds of percent this year. Nikola Corp (electric trucks) is a good example of this. Its charismatic CEO promises a great future and its share price rose by 550% in the first half of the year, reaching a market cap of $28bn at one point – not bad for a company currently with no revenues. Pinduoduo (ecommerce platform, $100bn market cap, +130% year-to-date), Shopify (ecommerce platform, $115bn cap, +150% ytd), Moderna (biotech, $23bn cap, +200% ytd), Tesla (electric cars, $250bn cap, +200% ytd) and Beyond Meat (plant-based foods, $9bn cap, +90% ytd) are in the same category: loss-making, promising high growth and highly speculative valuations. Of course, some of this crop might one day produce business performances to justify their current valuations, just as Amazon has been a spectacular winner from the 'class of 1999'. However it looks probable that collectively the 'class of 2020' will fail to produce good investment returns. The fund is and will remain underweight these types of companies.

This is without question the toughest 18 month period that our Global Equity Fund has faced in its 20-year plus history. In recent fund reports we have highlighted poor performers, such as **Saga**, **O-I Glass**, **DXC** and **Origin**. While these have certainly detracted from overall fund performance, we have also had outsized winners, such as **Steris**, **Keysight**, **Lowe's** and **Sandstorm Gold**. A balanced assessment suggests the net effect of these positives and negatives accounts for a minority of underperformance, with the net contribution of the top and bottom 5 stocks accounting for circa -2% year-to-date (overall fund underperformance -8%). The rest we believe to be related to the market environment.

The twin challenges for us are the market's narrow focus on large, expensive high quality growth as well as speculative growth companies, cohorts that are winning investor votes over 'value' (including small and mid-cap) stocks. If this environment continues the fund could continue to underperform; were this to happen the valuation spread between growth and value, already the widest it has ever been, would continue to widen. Our investment philosophy centres on identifying quality businesses but crucially being price-conscious, risk averse and long-term orientated – the tenets of our long-held investment approach. We believe our clients will ultimately be rewarded for this discipline.

Portfolio Activity

During the quarter the Fund purchased one new stock and sold two.

The new stock was **SEI Investments**, a US financial services company. SEI offers clients in asset and wealth management a range of technology and services, from full or partial outsourcing of investment functions, to consulting services, to sponsoring a range of 'manager of manager' funds. SEI is often embedded in its clients' processes, making them a critical and long-term partner. It explains why more than 90% of revenues are recurring and why the company has made healthy profits year in, year out since the 1980s. SEI has spent much of the last decade revamping its technology platforms and services, a massive undertaking that is now behind it, and as new clients are signed it should help to restore margins in its largest but least profitable Private Banks division. Historic growth in revenues and profits has been in the 5-6% range, which we expect to be matched or perhaps beaten over time.

Commentary

A particular feature of SEI is a net cash position of $850m, 10% of its market cap. This is especially reassuring when its investment needs going forward are less and, judging by history, the company is unlikely to make acquisitions of note. We expect the company to continue to make material share repurchases. At the time of purchase SEI traded on a P/E of less than 20x. We consider this attractive given the high quality nature of the company, both on an absolute basis and especially compared to companies of similar quality in other parts of the market.

We funded SEI through a sale of **Fairfax Financial**, a Canadian headquartered insurance company with global operations. Fairfax was purchased in 2011 and while money was made on the investment, the opportunity cost versus the benchmark was large. The bottom line is that Fairfax has struggled to make consistent, attractive returns. Insurance companies perform two roles: to underwrite and price policies in a prudent manner, and to invest the 'float' that arises from customers paying upfront. While Fairfax produced a solid margin on the insurance side, its investment returns have been woeful. Over the 9 years it was owned in the fund, Fairfax produced a return on equity of around 6%. With low confidence in management and their ability to improve returns, we preferred the long-term risk-reward trade-off for SEI.

Lastly we sold out of **Covetrus**, a US animal health services company. We received shares in this company in February 2019 in a spin-out from Henry Schein, the market leading distributor of products and services to office-based healthcare professionals. Just prior to the spin, Covetrus merged with a company called Vets First and while we expected some teething problems, the company significantly undershot its own performance projections. Management did not impress on the conference calls and investors questioned the merits of the merger, leading to a collapse in the share price (-85% from spin to March 2020). Following a partial recovery of the shares we fully sold out our holding. Luckily Covetrus was always a tiny position in the fund (0.25% at its highest), so the impact on performance was small. However this debacle caused us to lose a fair degree of confidence in the judgement and motivations of the Henry Schein senior management team, who arranged and wholeheartedly backed this merger and spin. To say that these judgements now look poor would probably be an understatement. Indeed it led us to reduce our position in Henry Schein in the Fund towards the back end of 2019.

David Coyne

Co-Lead Global Equity Fund

Contact Details:

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

Brendan Moran, Tel: + 353 1 612 4962
Email: brendan.moran@setanta-asset.com
www.setanta-asset.com

IMPORTANT INFORMATION

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