Setanta Income Opportunities Fund

Q2 2020

Fund Description

The **Income Opportunities Fund** ('the Fund') is an actively managed portfolio primarily comprising global equities but with the flexibility to invest in assets which offer attractive income and reasonable value. These assets include fixed income, property (including REITs) and cash. The Fund is not constrained by limitations on the level of any given asset. In practice, the Fund has had its greatest weight in equities, reflecting the breadth of that market, Setanta's expertise in that area, and the option writing strategy employed by the Fund. Nevertheless, property, fixed income and cash have all played meaningful roles in past returns of the Fund, at times, comprising up to 50% of the Fund's assets. The portfolio is managed in accordance with the Setanta investment philosophy. That is, the managers seek to own good assets for the long-term at prices below what they think they're worth, carefully considering each investment's risk profile. 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.

The Fund employs an option writing strategy. This entails the sale of both call and put options in return for a cash premium, representing an income stream that boosts the underlying income yield of the Fund. This strategy is employed in a conservative fashion, as all options written are fully covered.

The Income Opportunities Fund has two investment objectives:

1. To generate an annual income yield at a target rate. This is declared at the start of each financial year.

2. To achieve capital appreciation 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

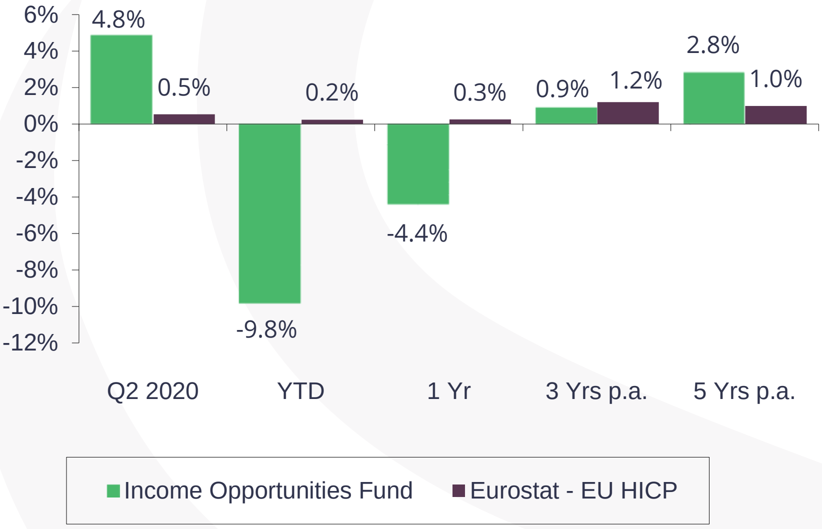
Businesses we own must have strong balance sheets

We make mistakes and always endeavour to learn from them

We will act with integrity in everything we do

SETANTA Asset Management

Fund Performance – 30.06.2020 (EUR)



Yearly Performance

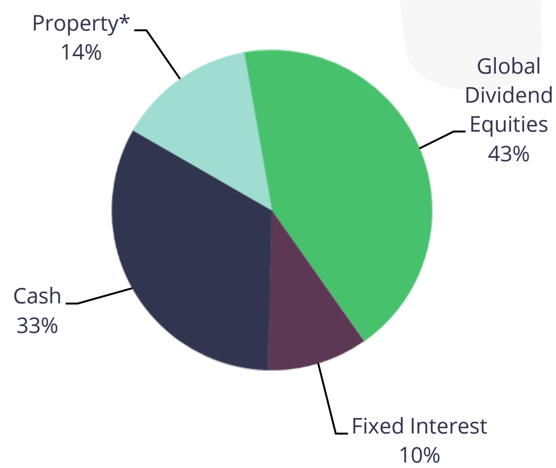
Year %	2015	2016	2017	2018	2019
Fund	10.6	9.7	2.9	-1.2	13.7
Benchmark	0.2	1.1	1.4	1.6	1.1

Performance Source: Setanta Asset Management Limited. The Fund returns stated are based on the movements in the unit prices of the ILA/CLI Income Opportunities Fund [P-INC1] and are gross of management fees. The performance will be reduced by the impact of management fees paid, the amount of which varies. **Benchmark:** Eurostat Harmonised Index of Consumer Prices (EUR). Inception as at 30.09.11 **Holdings Source:** Setanta.

Top 10 Equity Holdings

COMPANY	SECTOR	% OF FUND
CISCO SYSTEMS	INFORMATION TECHNOLOGY	2.0%
SVENSKA HANDELSBANKEN	FINANCIALS	2.0%
COCA-COLA AMATIL	CONSUMER STAPLES	1.9%
EXXON MOBIL CORP	ENERGY & MATERIALS	1.8%
RICHEMONT	CONSUMER DISCRETIONARY	1.7%
SAMPO OYJ	FINANCIALS	1.7%
ZARDOYA-OTIS	INDUSTRIALS	1.7%
DCC	INDUSTRIALS	1.6%
SMITHS GROUP	ENERGY & MATERIALS	1.5%
UNILEVER	CONSUMER STAPLES	1.5%

Asset Distribution



*includes 1.4% in IRES REIT

Historic Income

	Income Earned % of Fund Value
2011	6.2%
2012	5.6%
2013	5.5%
2014	4.8%
2015	5.5%
2016	4.7%
2017	4.1%
2018	3.9%
2019	4.2%

Commentary

Following the fastest 30% decline in history earlier this year, the S&P500 proceeded to record its quickest recovery from a low in almost a century. Global markets were accompanied by suitably elevated volatility[1]. The famous assertion by Ben Graham, father of value investing, that "*in the short run, the market is a voting machine but in the long run, it is a weighing machine*" seems especially apt at this time. We've seen a threefold surge in stock market 'voting' by retail investors in the US this year[2], with some retail platforms giving investing the look of an online gaming platform while numerous popular social media accounts tout stocks as punts without mention of financials. Government and Central Bank participation in markets has also been elevated; for example, the Federal Reserve has injected a massive $3 trillion since the start of the year.

We wish to remind you though, that while everything has changed, in one sense nothing has changed. By this we mean that we continue to live in an unpredictable world and it is for precisely this reason that at Setanta Asset Management we have always sought investments with strong balance sheets and considered their ability to withstand a range of scenarios rather than trying to forecast. These are key tenets of our investment strategy. Strong balance sheets offer protection against the unexpected, in turn enabling us to first and foremost preserve your capital. As a result we entered this situation with a collection of strong holdings. We continue to implement these principles, which we believe are now as important as ever.

Last quarter we spoke about the unprecedented fall in equity and bond markets and the fact that the Income Opportunities Fund had absorbed some of this. The Fund rose by almost 5% this quarter after dropping 14% in the previous quarter. The Fund's conservative asset mix which helped weather the worst of the market meltdown earlier in the year, was a drag on performance in the strong recovery experienced by equity indices in recent months. In addition, after many years of solid returns, the Fund's property assets, a portion of which are dependent on retail footfall, suffered a valuation markdown, reflecting the suspension of physical shopping.

Due to the unusual blanket shut-down nature of the recession it was important for us to reassess the investments we hold and their prospects in the face of the new specific risks, threats and cash commitments facing them. While short term trading has been affected, we believe permanent damage will be limited, with our review triggering a sale otherwise. We believe that overall the investments that we hold are generally well positioned to survive and thrive as they come out the other side of this, with many of their competitors in weaker positions.

Of the Fund's equity holdings, Fortescue, Cisco and Sampo were among the top positive contributors to performance. Low-cost iron ore miner **Fortescue** benefitted from the cyclical recovery of production involving iron ore as economies, in particular China, started to reopen. **Cisco** demonstrated stability in software and subscription revenue streams, its business customers' IT spend proved unexpectedly resilient and its net cash balance sheet reassured investors. **Sampo** recovered 15% during the quarter upon confirmation of low insurance exposure to COVID-19 claims, improved insurance underwriting margins and good solvency. Following regulator pressure on the industry to curtail dividends, the market reacted positively to Sampo paying a dividend backed by its insurance earnings. Although we are comfortable that it will be a valuable long term contributor to the portfolio, NWS, was a detractor from performance over this short time period. **NWS** is currently weighed down by political unrest in Hong Kong, but should benefit from industrialisation and urbanisation trends in China through its toll roads and infrastructure exposure.

[1] While volatility, as measured by the VIX Index, fell during the second quarter of 2020 it remains elevated at circa 50% higher than its 30 year average level.
[2] According to Goldman Sachs Global Investment Research, the number of positions held by Robinhood investors in S&P500 stocks tripled shortly after the market started to decline.

Commentary

Having fallen over 30% since the start of the year we saw an opportunity to acquire a position in **Bangkok Bank** during the quarter. Bangkok Bank is among Thailand's top three banks. It is a well-established commercial bank with a large deposit base and a diversified loan book of large corporates and small to medium enterprises. It enjoys substantial market share in the corporate lending space but prioritises conservatism over market share gains. Cautioned by memories of the Asian and Global Financial Crises, the management team maintain provisions exceeding normal loan losses and the bank prioritises being capitalised well in excess of regulatory requirements. It is generally more conservative in its capital buffers and its loan to deposit ratio than peers.

We acquired our position at an attractive price, while the company was valued at less than half of its book value and offering a dividend yield well above 5%. We had updated our investment case earlier in the year and following share price weakness associated with its acquisition of Permata Bank in Indonesia, we opportunistically took our position. We have been following Bangkok Bank at Setanta for more than 10 years.

Last quarter we prepared for dividend suspensions but believed that our equity holdings were well positioned from a long-term ability to pay standpoint. We are reassured by the fact that relatively few of our equity holdings have deviated from their dividend policy and those which did appear willing to reassess the possibility of paying dividends later in the year. Nevertheless, there is undoubtedly pressure on all primary sources of income, whether dividends, coupons, interest or rent, offset to some extent by the availability of higher option income due to increased market volatility.

While parts of the economy remain closed it is difficult for some of our businesses to prove their comparative resilience and strength for now. Our exposure to COVID-fighting healthcare companies and work-from-home internet businesses is more limited than their representation in broad indices. Is Zoom really worth over 500x earnings or loss-making Novavax worth 300x sales? We don't know but we won't be gambling your money on it. We believe that we hold a set of good quality investments with competitive advantages which should do well over the long term. We would expect fundamentals to eventually be reflected in prices as the world reopens, once businesses can compete with each other again and as we move through the stages of this recession. The Fund will continue to strive to achieve attractive long-term performance through its diversified mix of high quality investments.

**All figures are stated in euro, while those specifically relating to fund performance are also stated gross of fees. This commentary relates only to the Income Opportunities Fund sold in Ireland.*

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IMPORTANT INFORMATION

The Income Opportunities Fund is managed by Setanta Asset Management Limited and is a representative account of the Income Opportunities strategy. The performance shown is the performance of a representative account (ILA/CLI Income Opportunities Fund [P-INC1]). For this life assurance product, investors should refer to the relevant policy conditions available through Irish Life and via www.irishlife.ie. The strategy is also available on a segregated basis or a UCITS mutual Fund via Beresford Funds ICAV. Current and prospective clients should not assume identical performance results to those shown would have been achieved for their account if it was invested in the strategy during the period. Clients of the firm may receive different performance than the representative account. Client performance may differ due to factors such as timing of investment(s), timing of withdrawal(s), client-mandated investment restrictions and the portfolio not being fully replicated for new accounts or new flows. Investors should consider the investment objectives, risks, charges and expenses carefully before investing. See 'WARNING' and IMPORTANT INFORMATION' below.

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