Global Focus Fund (EUR) – Q3 2016

Setanta
ASSET MANAGEMENT

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 virtue of simplicity

When we describe the investment theses behind the fund's holdings to external parties, we are aware that sometimes these may sound quite simplistic. Perhaps on occasion the audience is left wondering how something so straightforward could be expected to produce superior investment returns. By contrast, investment theses that appear more complex are perhaps more appealing to some – the audience can perhaps believe that evaluating this investment case requires special skill, skill rare enough so as to exclude most other investors, reducing 'competition' for that investment proposition and positioning the investment manager to earn outsized returns.

Well whether the above is true or not, we plan to continue to avoid complexity, the dangers of which we think are greatly under-appreciated. Complexity, as it pertains to investments, can come in many forms but often it involves the investment case hinging on multiple sub-plots.

(Fund Commentary continued on Page 3)

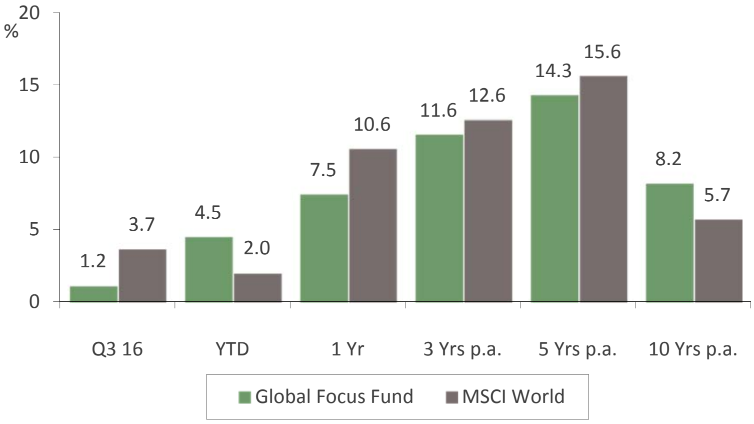
Portfolio Managers

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.

FUND PERFORMANCE (EUR) – 30.09.16



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

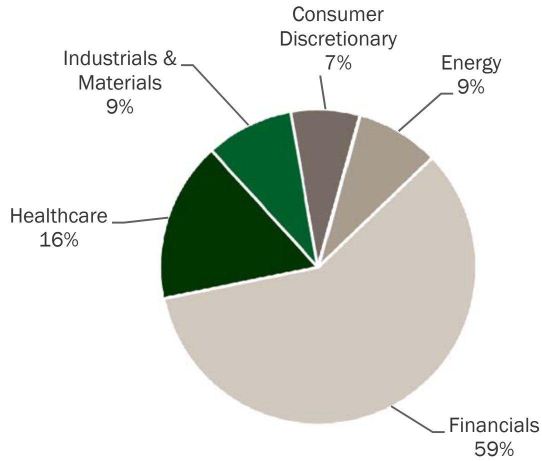
FUND HOLDINGS

COMPANY	SECTOR	% OF FUND
FAIRFAX FINL HOLDINGS	FINANCIALS	9.3%
LEUCADIA NATIONAL	FINANCIALS	7.4%
STERIS PLC	HEALTHCARE	7.3%
JOHNSON & JOHNSON	HEALTHCARE	7.1%
LSL PROPERTY SERVICES	FINANCIALS	6.3%
BERKSHIRE HATHAWAY	FINANCIALS	6.3%
BROOKFIELD ASSET MGMT	FINANCIALS	6.2%
MARKEL	FINANCIALS	5.8%
MINCON GROUP	INDUSTRIALS & MATERIALS	5.1%
DIAMOND OFFSHORE	ENERGY	4.8%
LANCASHIRE HOLDINGS	FINANCIALS	4.3%
GRANITE REAL ESTATE	FINANCIALS	4.3%
RICHEMONT	CONSUMER DISCRETIONARY	4.2%
DCC	INDUSTRIALS & MATERIALS	2.8%
NATIONAL OILWELL	ENERGY	2.6%
SWATCH GROUP	CONSUMER DISCRETIONARY	2.0%
GREAT EAGLE HLDGS	FINANCIALS	1.6%
BROOKFIELD BUSINES	FINANCIALS	0.1%
CASH		12.7%

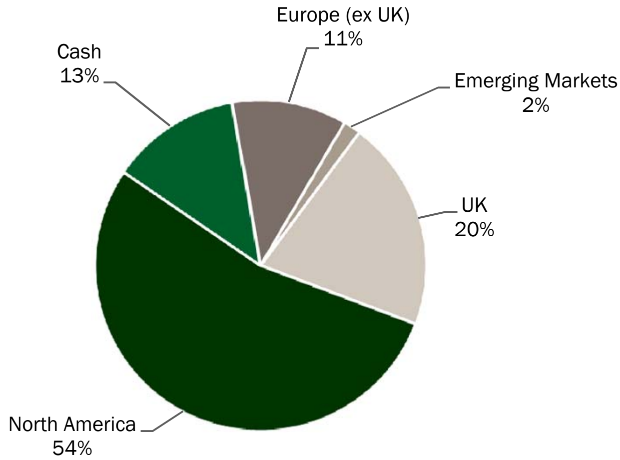
FUND STATISTICS

PRICE/BOOK	1.4
PRICE/EARNINGS RATIO (FY 1)	18.6
DIVIDEND YIELD %	1.9
AVERAGE MARKET CAP € BN	41.5
NO. OF HOLDINGS	18
DEBT /EQUITY %	38.9
ACTIVE SHARE %	98.2

SECTOR DISTRIBUTION



GEOGRAPHIC DISTRIBUTION



YEARLY PERFORMANCE

Year	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Fund	-19.7	-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
Benchmark	-12.2	-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

An example will explain further. I am considering an investment in Company A – the success of the investment case is contingent upon the successful resolution of five elements, each of which has a 90% chance of a favourable outcome. Therefore the chance of the investment case playing out as desired is only around 60%. The investment case behind Company B on the other hand depends on just two elements, each of which has a 90% probability of a successful outcome. The chance of this investment case playing out as desired is around 80%. Investment in 'B' is preferable. This example is grossly simplified. In the real world we cannot dissect investment cases into distinct, mutually exclusive elements, never mind allocate accurate probabilities to each. However the principle is rock solid and I think many investors struggle in calibrating comparisons between these kinds of investment opportunities.

Over the years we believe we have been successful in regularly identifying less complex investments that are also more attractively priced than their more complex brethren. In a competitive market where many practicing investors would consider themselves to be quite numerate why might we have had this opportunity? Behavioural Finance might have some light to shine here; investors in general are probably over-confident with respect to their skills and people generally seem to struggle somewhat with probabilities. But there is possibly also something almost instinctively off-putting about simplicity in investing – *"that can't really be a ten euro note on the ground, because if it was real, it wouldn't be there"*. Meanwhile we think many investors are not even thinking about these issues – they are too busy whimsically buying and selling, just trying to make it to the end of the quarter.

To be clear – simplicity should not be confused with ease. As Warren Buffett says, "investing is simple but not easy". We strive to avoid unnecessary complexity because too often it is not apparent that the potential returns justify bearing this complexity. However investment success is very hard to earn and requires the consistent application of a range of skills honed over many years. Simplicity is an investment virtue hiding in plain sight and we will continue to seek it out.

Transactions

Sysco

US Foodservice company Sysco Corp, which was added to the fund in Q4 2009, was sold from the fund during the most recent quarter. While the operating environment over this period was not easy, Sysco's business model, as we expected, remained resilient throughout. The stock delivered a substantial return over the period of ownership and we took the opportunity to sell to fund more attractively priced alternatives, such as Richemont and Swatch (discussed below).

Tesco

The remaining position in Tesco was sold. Tesco was added to the fund in 2012 and the fund regrettably incurred a significant loss on the investment (over 30%). We believe there were four key factors behind the failure of the original investment case:

1. We underestimated how effective the discounters (especially Lidl and Aldi) would be in taking market share, including how well they have tailored their offering to the UK market. For example, greater availability of local produce and clever national advertising campaigns such that some shoppers now see shopping at the discounters as a badge of honour.
2. We underestimated how customers would increasingly split their weekly shop between different formats. Most customers have continued to shop at Tesco but too many have reduced their Tesco purchases and supplemented this with smaller purchases at competing discount or convenience store competitors.
3. We believe Tesco's executives did a poor job for much of this period. When we acquired the position we could see that there had been a costly over-reach into new markets by Tesco. As we had expected this has been largely corrected by now but the management problems were ultimately deeper than this. We believe the immediate predecessors of the current CEO and CFO did a poor job – look no further than the accounting scandal around "commercial income" which involved aggressive recognition of incentive payments expected to be received from suppliers.
4. As we knew from the beginning, the grocery retailing business model is low margin and operationally geared, such that relatively small changes in sales can have outsized effects on profits. The factors above had a significant effect on Tesco's profitability.

The ongoing analysis of the Tesco investment case during these past years involved multiple members of the team and has consumed more man hours than probably any other investment that Setanta had made. The stock remained quite widely held across Setanta portfolios during this period. This was because the stock price fell faster than the business case was believed to be deteriorating and in a market of inflating earnings multiples, we did not think it made sense to liquidate the position earlier. This was an error in judgement. The Global Focus Fund management team decided to sell the remaining position in the most recent quarter and reinvest the proceeds in Richemont SA, as we see this as being better positioned and more attractively priced.

Our Tesco experience prompted much soul-searching. Unfortunately, as painful as they are, mistakes cannot be completely eliminated from any investment process, no more than they can be eliminated from one's life. We take mistakes very seriously and try hard to avoid repeating them. We believe we have been reasonably successful in this respect, as evidenced by the strong long-term track record we have produced over the years across the range of funds managed by Setanta.

Having added a small position in Swatch earlier this year, we added a position in a competitor, ***Richemont SA***.

Richemont is a global luxury goods company headquartered in Switzerland. It manufactures and sells a range of luxury watches, jewellery, as well as some other items, but watches and jewellery account for essentially all of the group profits. Its brands include Piaget, Jaeger LeCoultre, Dunhill and Mont Blanc, and others, but its flagship brand is Cartier, which accounts for the bulk of company profits. Cartier was established in the mid nineteenth century, and became "jeweller to the kings". We believe that today this brand is tremendously valuable. Richemont has been well managed over the years, with sustained investment in the brands and infrastructure overseen by the well-respected Chairman, Johann Rupert, who is also the company's largest shareholder. The luxury goods business had been under some pressure over the past year or two. Luxury watches have been especially affected with particular weakness in Greater China, most notably in Hong Kong. Government induced pressure on "extravagance" spending in China is at least partly to blame. There is little evidence that a floor in spending has been reached yet, and recent results for both Swatch and Richemont have been poor. As is always the case, we don't know where the bottom is and we don't believe investors can make money by trying to time such things anyway. We are however confident that, like Swatch, Richemont has more than enough financial wherewithal to withstand a very severe downturn. Should this scenario emerge, the stock would almost certainly trade lower than current levels, but we believe this would be temporary and eventual recovery will be helped by long-term growth in the middle classes in Asia. So we see these pressures as cyclical rather than structural and believe the weakness in Richemont's stock over the past couple of years has provided us with a good entry point.

Richemont has similar economic drivers to Swatch, which the fund also owns a small position in, and therefore careful consideration has been given to position sizing.

Melrose PLC

To refresh the original investment case for Melrose: its strategy is to buy under-performing businesses, improve and then sell them, return the proceeds to shareholders and await the next deal. The businesses Melrose acquires tend to possess good quality, durable assets but have been poorly managed, suffered the effects under-investment, misguided strategy and misaligned staff incentives. By taking the business private, changing personnel and incentives, and improving resource allocation Melrose aims to improve profitability and subsequently sell the revalued business. Melrose's management has an extremely impressive track record in executing its strategy over many years. We initially acquired a position in Melrose in 2014 and the investment case has played out as we expected. In the most recent quarter Melrose announced the acquisition of Nortek, a diversified manufacturer headquartered in the US. We spoke to Melrose management about the opportunities to improve Nortek, and we believe this is a classic Melrose transaction. We participated in the rights issue to fund the acquisition. The stock has performed extremely well since and we chose to sell the position in the Global Focus Fund.

Don't believe everything you're told

CRH Falls to Lowest in Over a Year; ISEQ Index Little Changed

By Bloomberg Automation

Crh Plc fell 77 percent while the country's benchmark index advanced.

The shares fell to 7 euros, the lowest level in at least a year, from 30.50 euros. Trading volume was 1.5 times the 30-day average of 681,008 for this time of day.

The above graphic is from a story published by Bloomberg Automation on September 9th. It claims that CRH shares, clearly trading at over €30, had fallen 77% to €7 per share. There are at least two lessons from this. Firstly, robots are not yet ready to take over the world. Secondly, don't believe everything you're told.

Rowan Smith – Portfolio Manager

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