

# Setanta Global Focus Fund

Q2 2021

## 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 equity portfolio which holds c.20 global 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. Stocks are chosen through bottom-up analysis, based on investment merit. Due to the Fund's concentrated nature, investments require an even greater than normal margin of safety. The Fund can hold up to 30% 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.

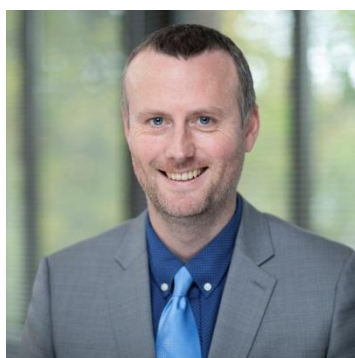
## Fund Commentary

Although the global economy is set to grow by an impressive 6% in 2021, this is off a depressed level of output in 2020 and what's more the IMF forecasts that the US will be the only large economy to have a higher level of GDP in 2022 than before the pandemic. In our opinion, stock markets were already richly valued 18 months ago, so against that sobering backdrop, we find it hard to fathom how global stock markets have increased 22% (Euro terms) since the start of 2020, the eve of COVID-19.

*(Fund Commentary continued on Page 3)*

## Portfolio Managers

David Coyne & Rowan Smith



## 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

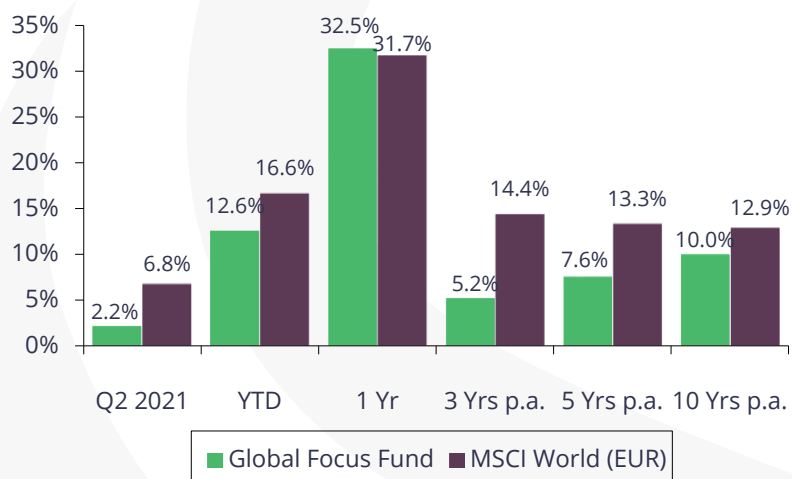
We consider scenarios rather than making forecasts

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 – 30.06.21 (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 Focus Equity Fund [IEC4001] 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
BERKSHIRE HATHAWAY	FINANCIALS	9.4%
RICHEMONT	CONSUMER DISCRETIONARY	9.3%
STERIS PLC	HEALTHCARE	8.2%
SAMSUNG ELECTRONIC	INFORMATION TECHNOLOGY	7.8%
RYANAIR	INDUSTRIALS	7.6%
JOHNSON & JOHNSON	HEALTHCARE	7.5%
MINCON GROUP	INDUSTRIALS	6.9%
DCC	INDUSTRIALS	6.6%
LSL PROPERTY SERVICES	INFRASTRUCTURE	5.4%
MELROSE INDUSTRIES	INDUSTRIALS	5.1%

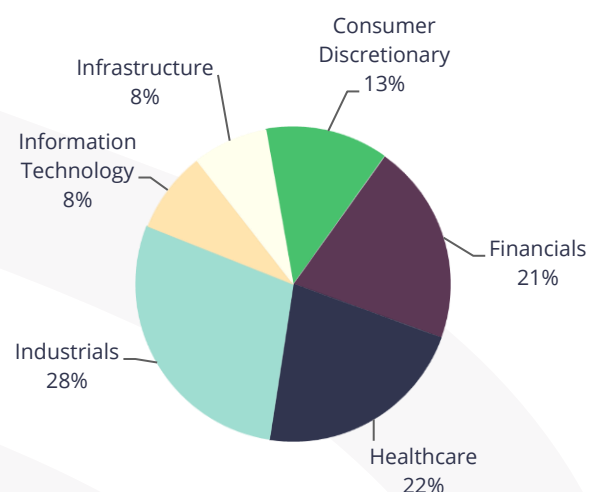
## Yearly Performance

Year %	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
<b>Fund</b>	-35.2	44.0	28.2	1.5	9.0	20.0	19.1	7.3	11.7	9.7	-6.4	17.8	-2.2
<b>Benchmark</b>	-37.6	25.9	19.5	-2.4	14.1	21.2	19.5	10.4	10.7	7.5	-4.1	30.0	6.3

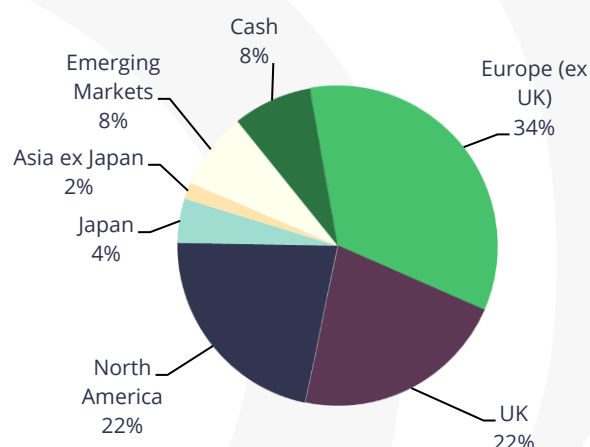
## Fund Statistics

PRICE/BOOK	1.7
PRICE/EARNINGS RATIO (FY 1)	17.8
DIVIDEND YIELD %	1.0
AVERAGE MARKET CAP €BN	93.9
NO. OF HOLDINGS	15
DEBT/EQUITY %	33.2
ACTIVE SHARE %	94.5

## Sector Distribution



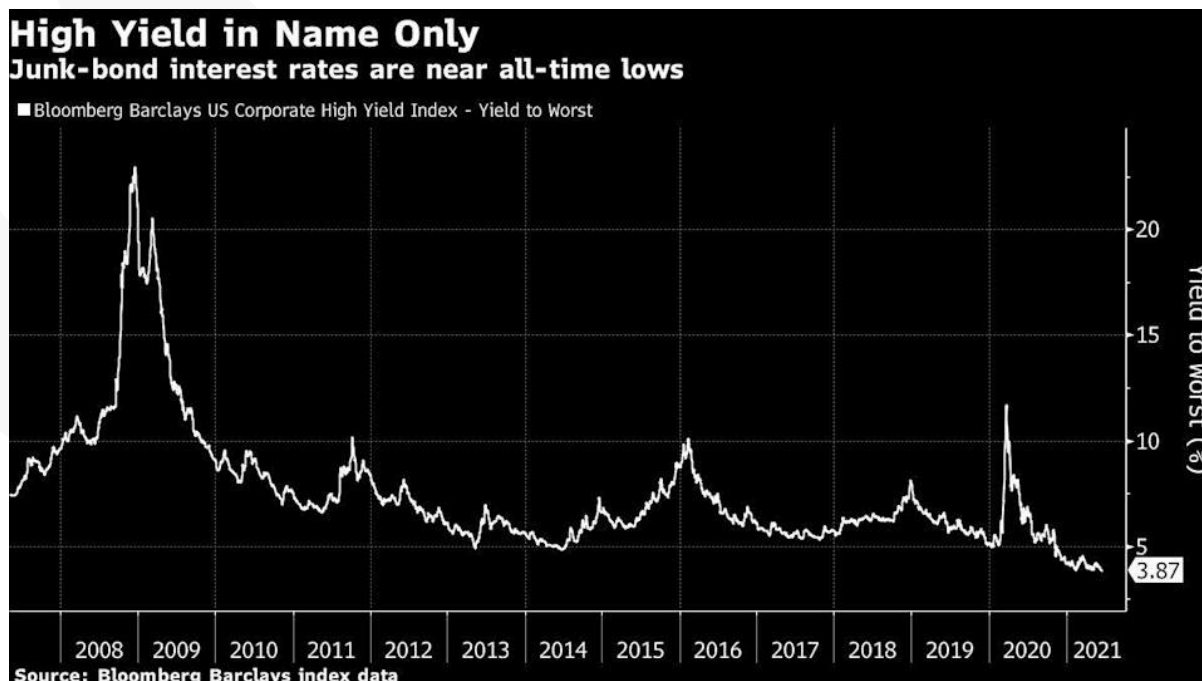
## Geographic Distribution



# Commentary

Of course, investing is always a case of relative value. The low / zero / negative interest rate environment that has endured for more than 10 years has elevated valuations of all asset classes. It's for this reason the phrase the everything bubble was coined. How much is warranted and how much is exuberance is the million-dollar question, but there are warning signs.

In the bond market for example, US junk bond yields fell below 4% in June, despite a record level of issuance in H1:21. The headline yield understates the extent of the decline in returns being accepted by bond investors. From a recent article in the excellent investment publication Grant's, *"Rapidly retreating debt covenants, or fine-print legal protections for lenders, accompany those extra dollops of debt. So-called covenant-lite structures featured in 85.2% of total loans outstanding in May, per S&P's LCD unit, up from about 66% five years ago and just 17% in 2007."*



So too eyebrows are raised in equity markets. The Financial Times reported that investors put \$580bn into equity funds globally in H1:21. If this rate continues in H2, it will surpass cumulative equity inflows for the previous 20 years! Also, retail investors continue to be prominent, accounting for c.10% of total US stock market trading volumes in June, according to Morgan Stanley, having peaked at 15% last September. 'Influencers' continue to cause a lot of retail investors to funnel trades into a relatively small number of (meme) stocks.

It's not just low interest rates that makes these times so extraordinary. We are spending a lot of our time trying to understand where and how competitive landscapes may be shifting. A great illustration of this is at the intersection of finance and technology, where both Big Tech and innovative fintech start-ups are set on disrupting the traditional banking industry. The disruption has been made possible by a confluence of forces in recent years: common standards (allowing interoperability between companies), new regulation (e.g., Open Banking in Europe, a secure way for customers to share financial data with 3rd parties), new business models (e.g. Banking-as-a-Service, which allows brands to embed financial services without needing to become a regulated bank themselves) and new consumer behaviours (less branch visits, more internet banking). Although the impact on the sector to date has been limited, the situation warrants close attention for what may happen 3, 5 and 10+ years into the future. Traditional banks' technology is old, costly to maintain and inflexible – and worse still, for a variety of reasons it's extraordinarily difficult to rip out and replace. To date, FinTechs and neobanks have mostly focused their efforts on niches — for example younger, lower-income or previously unbanked customers, with products that are more convenient and cheaper. It's not hard to imagine that in the future FinTechs will zero in on banks' juiciest income streams, such as in business banking where sums are larger, and margins are fatter. All this comes on top of the significant advances Big Tech is making in the area of payments.





# Commentary

Longer term, thoughts must incorporate the likes of Distributed Ledger Technology (which threaten to cut out layers of middlemen, perhaps including parts of banking) and Central Bank Digital Coins (which could greatly diminish the fractional reserve banking system). With so many potential sources of competitive attack and disruption, traditional banks that don't adapt could face existential questions. Naturally, it's not necessarily all doom. Banks have valuable licences and compliance know-how and have vast experience in pricing risk and dealing with defaulted loans. Also, customer inertia could stave off the effects of competitors long enough for banks to adjust their business models. In the old days' banks operated a 3-6-3 model: borrow at 3%, lend at 6% and on the golf course at 3pm. If we can be certain of anything it's that banks will never have things as easy as that again (and not just because of zero interest rates). By studying and contemplating, we hope to better avoid the casualties of disruption and, perhaps, find ways to capitalise.

## Fund Commentary

Global stock markets rose strongly in the April to June period, with the benchmark MSCI World up almost 7% (Euro terms) in the quarter and 16.6% (Euro terms) in the half year. The Setanta Global Focus fund rose by 2.2% (Euro terms) in the quarter and 12.6% for the year to June.

The fund had a number of performance laggards in the quarter and the year to date. For the most part we are puzzled by this as their fundamentals are good and / or their valuations are inexpensive. We are confident of a performance recovery in due course.

For example, specialty insurer **Lancashire Holdings** is beautifully positioned to take advantage of the better insurance pricing environment. The company raised capital in 2020 and has put this to work this year at what should be very attractive returns. It's a stark contrast to most of its competitors, who are having to retreat and clean up their underwriting mistakes of recent years. Yet Lancashire was down 15% in the year to end-June.

Another example is **Melrose Industries**, which during the quarter disposed of one of its businesses at a good price and will use much of the proceeds for paying down debt. This, coupled with the brighter outlook for its aerospace division, should have put a better gloss on the share price. Instead Melrose was down 12% in the year to end-June.

The fund's worst performer in the quarter and year-to-date was Japanese drug distributor **Alfresa**. The company's profits have fallen materially in the last 12 months, chiefly related to COVID-19 as Alfresa gave some price concessions to its struggling pharmacy customers. Management has guided the coming year to be equally tough, but that over the coming few years it should recover lost profits. We concur, but most other investors have either taken fright or are too impatient. Further weighing on the stock, Alfresa was removed from some stock indices, forcing index funds to sell. The stock fell 30% between last September and June, from an inexpensive starting valuation. Even at the current level of profits the stock is reasonably valued, but of course should profits recover we believe there is far greater upside. Alfresa has a super-strong balance sheet, with around 40% of the current market cap in cash. While recent news flow has not been good, but Alfresa operates in an attractive consolidated industry, is a good operator and is financially strong. This should give investors a lot of downside protection and in a recovery situation the stock should recover a lot of lost ground.

On the plus side, there were strong performers, including UK estate agent **LSL** (+48% ytd), luxury goods companies **Richemont** and **Swatch Group** (+38% and +33% ytd respectively), as well as HK property group **Great Eagle** (+29% ytd). All of these names are beneficiaries of the re-opening of the global economy.



## Transactions

The fund sold out the remaining position in **NOV** during the quarter. This stock did not work out the way we envisaged. NOV provides equipment to the oil and gas industry. It has very strong market shares – sometimes it is the only supplier – giving it good negotiating power with its customers. However, NOV's historic business strength has been in offshore drilling and production, the worst hit area of the energy sector's depression over the last 7-8 years (the depths of which were during 2020 when oil prices briefly went negative!). Offshore is typically a high cost source of energy, which means NOV's recovery potential is very unclear and at best will be much delayed. This makes valuing NOV extremely challenging. With the stock 60% off its October 2020 low, we sold the fund's remaining shares.

**David Coyne, Co-lead Portfolio Manager**

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The Global Focus Equity Fund is managed by Setanta Asset Management Limited and is a representative account of the Global Focus Equity strategy. The performance shown is the performance of a representative account (ILA/CLI Setanta Global Focus Equity Fund [IEC4001]). For this life assurance product, investors should refer to the relevant policy conditions available through Irish Life and via [www.irishlife.ie](http://www.irishlife.ie). The strategy is available on a separate account basis to institutional investors however 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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