Setanta Active Multi-Asset Fund Range

Q1 2023

SETANTA
Asset Management

Contents

Fund description

The Setanta Active Multi-Asset Fund Range is made up of three actively managed portfolios that hold a combination of equities, bonds, property, cash and alternatives.

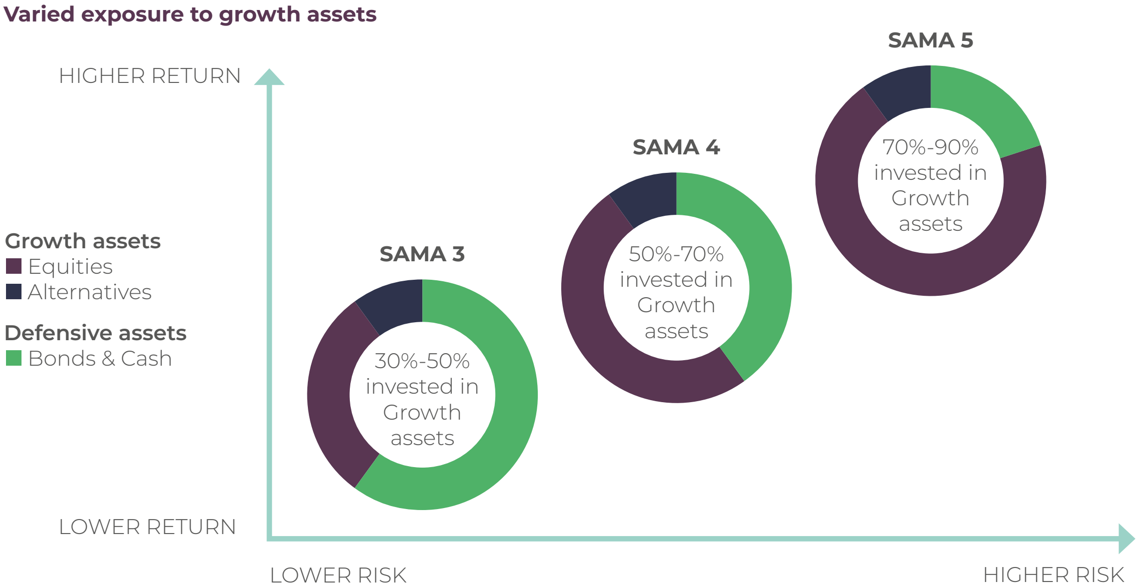
The funds are managed in line with the following core principles:

- **An asset mix that reflects the investment objectives**
  The funds' exposures across different asset types have been designed to meet specific risk and return requirements. These exposures may vary over time in line with the manager's views.
- **Consistent decision making**
  The design of each fund reflects a particular investment objective and attitude to risk. The funds are managed in a consistent manner, with investment decision making implemented consistently across the fund range.
- **Broad diversification**
  The funds are broadly diversified across a range of growth assets like equities and alternatives, and defensive assets like bonds and cash. Excess returns are driven by superior stock selection and active asset allocation.

Three funds, three risk-return profiles

Each of the three Setanta Active Multi-Asset (SAMA) Funds has a different risk and return profile based on its differing exposures across asset classes. Each fund aims to grow your investment over the medium to long term by varying the exposure to growth assets.

Varied exposure to growth assets



Market commentary

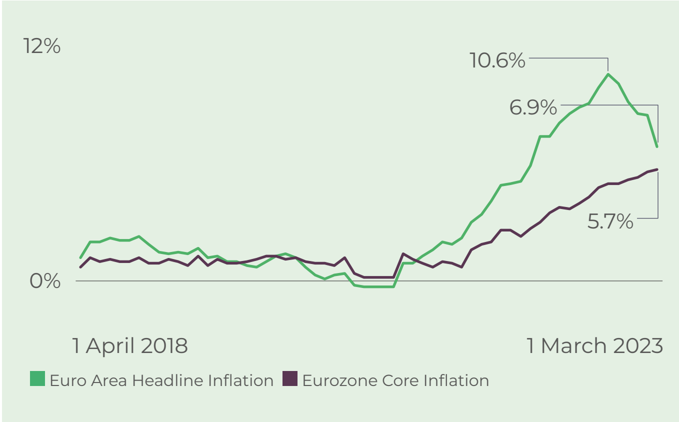
Over the quarter, global growth surprised positively, with strong US and European business survey data, falling energy prices and a rapid rebound in China post the country's reopening from its 'zero-Covid' restrictions. However, geopolitics remain challenging, with the war in Ukraine and ongoing trade tensions between the US and China, while markets had to navigate a flare-up in the banking sector in March.

Markets started strong, rallying in January, as headline inflation declined, increasing prospects of easier monetary policy. Optimism culminated in early rate cuts being priced into yield curves, boosting valuations. The fall in bond yields over the quarter boosted long-duration growth stocks, with the hit to bank shares weighing on the performance of value stocks in general.

Notably, energy's contribution to annual inflation has turned negative, with energy costs well below their previous peaks. This, combined with the expected softening in other key elements (e.g. shelter CPI in the US), increases confidence that inflation's decline will persist, which could bring an end to the global synchronous rate tightening cycles sooner rather than later.

In February, markets then fell on strong economic data, coupled with sticky core inflation, which forced a reassessment of interest rate expectations, the market pricing in higher rates for longer. Labour markets were tight, with low unemployment and rising wages underpinning growth in the near term. Core inflation remained high, with concerns recent wage growth was inconsistent with the central banks' 2% inflation targets.

'Sticky' underlying inflation: headline vs core eurozone inflation



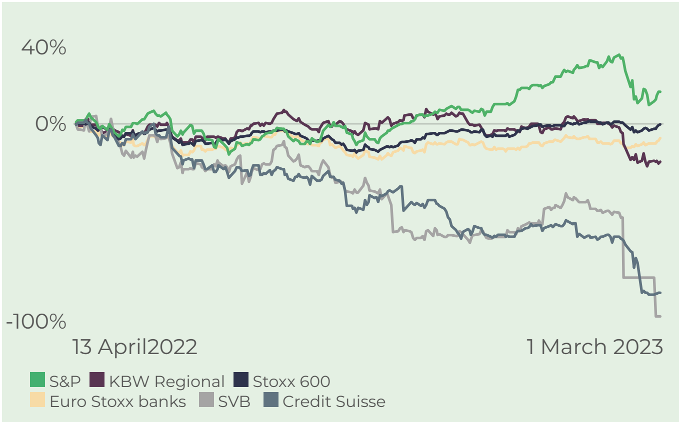
Source: Bloomberg / Setanta

Banking crises

In March, markets contended with the failure of US lender Silicon Valley Bank, the flight of deposits from small US regional banks to larger institutions, and the rescue of 167-year-old Credit Suisse by UBS in a Swiss government orchestrated deal.

Broader concern in the markets proved short-lived, however, as only specific names and specific elements of the financial sector suffered the brunt of the selloff. The financials sector moved quickly to price out any systemic risk, as central banks provided ample near-term liquidity, and bank balance sheets in general are better capitalised than in previous banking crises. Markets rallied on expectations of easier monetary policy in response to the crisis and signs it would be contained, posting positive returns for the quarter.

Banking contagion contained: performance in 2023



Source: Bloomberg / Setanta

Central bank policy

US banks had already started to tighten credit standards before the banking crises. Given the recent turmoil, lending conditions should tighten further on higher costs of funds and greater regulatory scrutiny.

US banks were already nervous

Net percentage of domestic banks tightening standards for commercial and industrial loans to large and middle-market firms, percent, quarterly, not seasonally adjusted

Source: Economic Research Division, Federal Reserve Bank of St. Louis

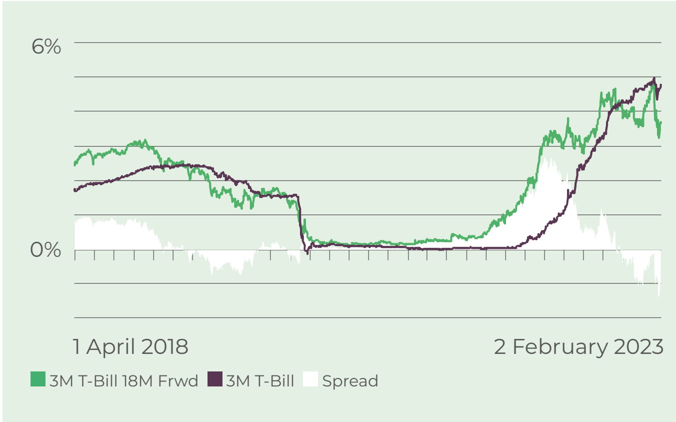
A deterioration in the availability of funding to the economy could make central banks think twice about the magnitude of further interest rate hikes.

> "Frankly, there's good research by staff in the Federal Reserve system that really says to look at the short [end] — the first 18 months — of the yield curve. That's really what has 100% of the explanatory power of the yield curve. It makes sense. Because, if it's inverted, that means the Fed's going to cut, which means the economy is weak."

Fed Chair Powell
21 March 2022

Taking Powell at his word, there is already a steep inversion in the short end of the US yield curve, possibly signalling a recession and rate cuts within the next year.

Powell's indicator: 3M vs 18M forward yield

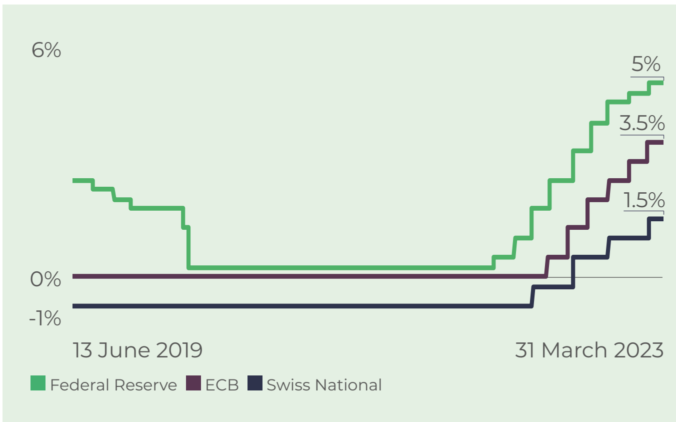


Source: Bloomberg / Setanta

However, with growth resilient and core inflation high, the European Central Bank (ECB) increased rates in March despite the banking turmoil, with both the US and Swiss central banks following suit.

There was ample liquidity provided by the central banks to alleviate the bank crises in March while remaining committed to their hiking schedules, highlighting the ability to be lenders of last resort while still combating inflation.

Central bank rates



Source: Bloomberg / Setanta

Our funds remain well diversified, with a bias towards allocating to assets where valuations look attractive.

Fund commentary

The SAMA fund range gained by +2.1% to +2.7% over the quarter. We saw positive returns across most asset classes despite the collapse of Silicon Valley Bank and the bailout of Credit Suisse, which led to significant volatility in bank shares.

Within the funds, key contributors were listed private equity (+4.1%), emerging market debt (+3.8%) and global equities (+3.8%), benefitting from the positive start to the year.

Our global equites, however, lagged the benchmark return (+5.8%), underperforming by -2.0%. Value stocks faltered compared to Growth, as the banking turmoil was relatively contained and the market priced in rate cuts, supporting a risk-on environment.

Property, including direct local commercial (-2.0%), local residential (-6.4%) and globally listed REITs (-0.8%), fell as headwinds mounted. These consisted of higher capitalisation rates (pushing prices down), higher interest costs (squeezing operating margins) and uncertainty around the future use of real estate (increased vacancies). Meanwhile, few tailwinds were evident for the time-being.

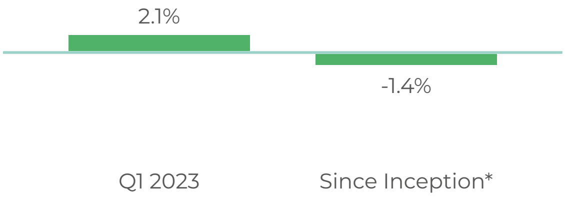
European government bonds and credit delivered low single-digit returns, contributing to overall positive performance.

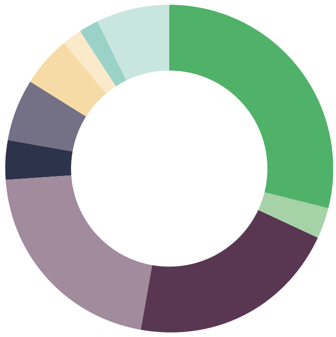
Over the quarter, the funds allocated out of equities and into emerging market debt, high yield and investment grade bonds as yields have risen and credit spreads have widened from historically low levels.

Fund performance and asset mix

SAMA 3

The SAMA 3 Fund offers diversified exposure, including equities, bonds, property, alternatives and cash, with a bias towards bond investments. This fund seeks to provide a lower level of risk and return when compared to the other funds in the SAMA fund range.

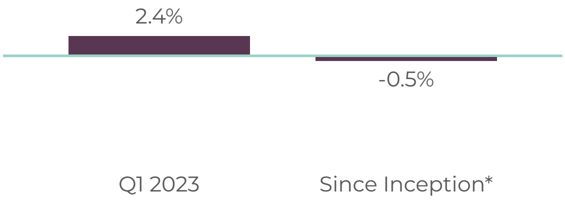


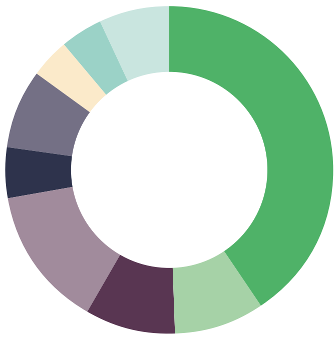


Global Equity	28%
Emerging markets	3%
Total Equities	**31%**
Euro Government Bonds	21%
Euro Corporate Bonds	21%
Emerging Market Debt	5%
Global High Yield Bonds	7%
Cash	5%
Total Bonds & Cash	**59%**
Infrastructure	2%
Private Equity	2%
Property	6%
Total Alternatives	**10%**

SAMA 4

The SAMA 4 Fund offers balanced exposure between equities and bonds. This fund seeks to provide a medium level of risk and return.

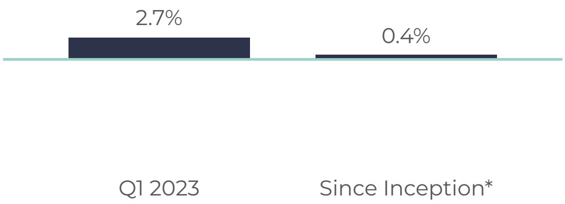


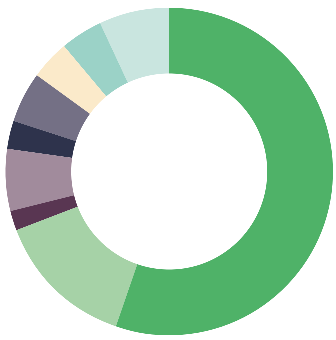


Global Equity	40%
Emerging markets	9%
Total Equities	**49%**
Euro Government Bonds	9%
Euro Corporate Bonds	14%
Emerging Market Debt	6%
Global High Yield Bonds	8%
Cash	0%
Total Bonds & Cash	**37%**
Infrastructure	4%
Private Equity	4%
Property	6%
Total Alternatives	**14%**

SAMA 5

The SAMA 5 Fund offers exposure weighted towards equity investments. This fund seeks to provide a higher level of capital growth.





Global Equity	55%
Emerging markets	14%
Total Equities	**69%**
Euro Government Bonds	2%
Euro Corporate Bonds	7%
Emerging Market Debt	4%
Global High Yield Bonds	5%
Cash	0%
Total Bonds & Cash	**18%**
Infrastructure	4%
Private Equity	4%
Property	6%
Total Alternatives	**14%**

Performance Source: Setanta Asset Management Limited. The actual Fund returns stated are based on the movements in the unit prices of the Fund and are gross of management fees.

*Fund launch date 24 May 2022. Asset class weightings as at 31 March 2023.

Setanta Global Equity Strategy – the growth engine

The Setanta Global Equity portfolio is the growth engine of our multi-asset funds. The portfolio provides capital growth, as the businesses it is invested in compound in value over time.

The Setanta Global Equity strategy is the flagship equity strategy of the firm, with a strong 20+ year track record. It is managed by eight portfolio managers, who work as a team and challenge each investment idea as a core part of their investment process.

Sector distribution

Top 10 equity holdings

Company	Sector	% of fund
Microsoft	Information Technology	**4.9%**
Berkshire Hathaway	Financials	**3.7%**
Oracle	Information Technology	**3.5%**
McDonald's	Consumer Discretionary	**2.9%**
Booking Hldgs	Consumer Discretionary	**2.7%**
Alphabet	Consumer Discretionary	**2.7%**
Costco	Consumer Discretionary	**2.7%**
Nike	Consumer Discretionary	**2.6%**
Samsung	Information Technology	**2.4%**
Keysight Technology	Information Technology	**2.3%**

Geographic distribution

Source: Setanta Asset Management, as at 31 March 2023.

The Global Equity strategy:

Highly selective

We look for good-quality, durable businesses that are out of favour for one reason or another.

Risk averse

We buy conservatively financed companies, which are run by trustworthy management and have a shareholder focus.

Compounding in value

We are diligent and patient investors, expecting the long-term results of the equity portfolio to mirror the growth of the companies within it.

Style rotation supports the market

It's scarcely believable that, in the midst of a banking crisis – albeit one that appears to have been quickly contained – the MSCI World could rise 5.8% (in euro terms) in a quarter, but that's how it turned out in Q1. Banks were certainly headline news, but the other main story was the strong performance of technology, media and consumer discretionary stocks. You may recall these were the worst performing sectors in 2022.

Growth stocks did well more generally in Q1, outperforming the overall market by a wide margin of 7%. It's hard to know the reason for the change in investor mood from last year. However, there is a growing feeling that interest rates may have peaked in the US; interest rates tend to have more of an impact on the valuation of growth stocks whose value is further into the future. Related to this, fears of a recession have increased and may have encouraged investors to take profits on cyclical / value stocks that performed well in recent quarters. Another contributor may have been a spill-over of excitement from AI / ChatGPT, which could provide productivity improvements for a host of industries in the future. At the other end of the spectrum were energy and bank stocks, while real estate, utilities and health care stocks were also relatively weak.

Portfolio activity

We recently added European low-cost airline **Ryanair** to the portfolio. The investment case is predicated on: 1) being one of just two ultra low-cost providers in the European short-haul market with a meaningful cost advantage over peers; 2) competition is weighed down by inefficient cost structures and institutional resistance to change, which helps to constrain supply; 3) a growth runway at attractive returns on capital, through share gains and market growth; 4) smart capital allocation with a history of aircraft orders at low points in the cycle and a willingness to return money to shareholders; 5) strong balance sheet and negative working capital to self-fund growth; and 6) a proven CEO with skin in the game, backed by a capable executive team.

Ryanair plans to hit 225 million passengers by 2026 compared to 168 million in 2023, with the aircraft orders in place to facilitate that and grow at a 4-5% annual clip thereafter. The Covid-19 pandemic has helped to accelerate the demise of some airlines and drive industry retrenchment. For now, the supply outlook looks reasonable. Having experienced some cost slippage in the wake of rostering issues in late 2017, the company has got back on the front foot on managing non-fuel costs. The balance sheet is in good shape with management targeting a net cash position by

March 2024. CEO Michael O'Leary has committed to the role until 2028. Consolidation in the intra-European short-haul market is happening slowly over time, offering some hope for a more disciplined and profitable industry in the longer term. While Ryanair's earnings tend to be volatile, we estimate it was trading at a low-teens normalised price-to-earnings (P/E) ratio at the time of purchase.

We sold out of UK specialist lender **Close Brothers Group** during the quarter. Close Brothers lends to niches of the market that large high street banks either are not interested in or are not good at. It has something of an anti-cyclical lending policy, growing the loan book more slowly in good times and faster when competitors are less willing or less able to lend. All loans are asset backed, so even in the event of a default, the bank would repossess and sell the asset to recoup most or all of its outlay. Historic loan losses were around 1%, which is very favourable compared to a net interest margin of around 8%. We were attracted to Close Brothers' history of earning mid-teens return on equity while growing at high single digits on average. We bought a small position in late-2019.

We sold out because of management's handling of a litigation finance business called Novitas which it acquired in 2017. Novitas financed the likes of disputed will, divorce and personal injury litigation, and management believed its loans had a similar risk profile to the rest of Close Brothers Group. This proved very wide of the mark. The first time investors heard of trouble at Novitas was in October 2021, when management said they had decided to close Novitas to new business and work on existing loans. An undisclosed provision then was the first of many, and the last straw for us was an additional large provision in January 2023, which we estimate brought provisions to date to well over 50% of the Novitas loan book. Luckily, Novitas accounted for less than 5% of group loans, so there was no damage to the balance sheet. However, in our opinion the bank had lost its 'competent management' status (from our 'necessary but not sufficient conditions' for investing in banks): they exhibited poor judgement in getting into litigation finance in the first place and they also failed to contain the problem (continuing to fund existing cases, throwing good money after bad). The impact on the fund was limited by the stock's low weight – at its max, it was 0.7% of the global equity allocation of the fund, around half our typical allocation.

Environmental, social and governance

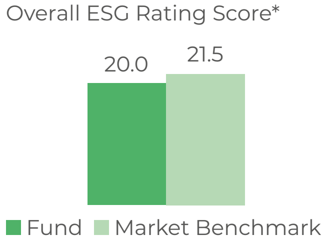
Setanta believes it is its responsibility as an investment manager to consider the environmental, social and governance (ESG) impacts of the companies it invests in. Companies that are actively engaged in addressing ESG challenges are more likely to make a greater contribution to society, which can, in turn, create opportunities for investors. By the same token, those that lag behind can present risks. Setanta integrates ESG factors into its fundamental research process. When it believes there are ESG factors material to its investment decisions, it addresses them in its research reviews and engagements with companies. Setanta is a signatory to the UN-supported Principles for Responsible Investment (UNPRI).

ESG risk score

Risk Score*	Fund	Market Benchmark
Overall	20.0	21.5
Environmental	4.0	4.8
Social	8.1	8.8
Governance	7.4	7.6

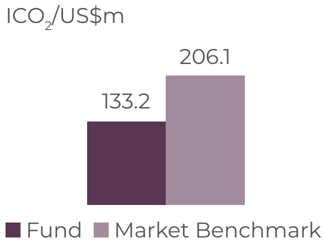
Overall ESG Risk Rating

The Environmental, Social & Governance (ESG) Risk Rating measures the degrees to which a company's economic value is at risk due to not considering ESG factors using a calculation of the company's unmanaged ESG risks.



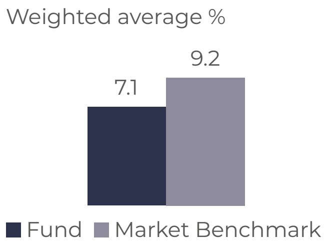
Carbon intensity

Carbon intenstity is a metric used to compare company emissions across industries. The absolute emissions is divided by total earnings with the figure expressed in tonnes of carbon dioxide equivalent per million USD of total earnings.



Fossil fuel

Fossil fuel involvement measures the percentage of earnings that companies get from thermal coal extraction, coal-based power generation, oil and gas production, oil and gas based power generation and oil and gas related products and services.



ESG Metrics based on P-SAMA4 Fund. *A lower score indicates a lower level of unmanaged ESG risk and potential risk to the economic value. Note: ESG Risk Scores and Carbon Metrics are currently calculated for Shares and Corporate Bonds only Information correct as of 31 March 2023.

Key advantages of the fund range

Actively managed

Clear and consistent investment philosophy, high-conviction approach

Value approach

Discipline and patience allow us to take advantage of mispriced opportunities.

ESG built-in

Article 8 Multi-Asset fund range

Global Equity engine

Level of exposure consistent with risk rating of each fund

Investment expertise

Highly experienced, stable and award-winning investment team

Risk rated

Generate long-term capital growth within the appropriate risk parameters

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PRI Principles for Responsible Investment

TCFD Task Force on Climate-Related Financial Disclosures