SOMERSTON ASSET MANAGEMENT

SOMERSTON CORE EQUITY FUND

INVESTMENT LETTER AS AT 30 JUNE 2024

Portfolio Objectives: To grow capital over the medium term by investing in a concentrated portfolio of high quality companies and to outperform global equities over the economic cycle.

Strategy: We use a fundamental bottom-up approach to identify attractive investment opportunities. We have a 5-year investment horizon. We focus our investments in 15 to 25 high quality companies. We invest in companies that demonstrate strong governance, high profitability, low capital intensity, strong economic moats, and low business risk. We invest globally, without sector/geographic restrictions.

Performance: The Core Equity Fund (US1 class) rose by +2.1% in the month and rose by +1.7% over the last three months. The reference index rose by +3.6% during the month and rose by +5.7% over the last three months.

Performance US1 (%)

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2017				1.2	5.4	-0.2	0.4	-0.1	1.9	1.8	-1.8	2.1	**10.9**
2018	6.2	-4.6	-1.9	0.4	1.2	1.2	4.3	1.3	0.4	-8.5	2.7	-9.0	**-7.2**
2019	6.2	4.2	3.3	3.8	-4.0	5.7	0.6	0.8	-1.6	1.3	5.1	2.5	**31.1**
2020	0.9	-7.3	-14.3	12.5	5.8	2.6	4.4	5.5	-3.4	-3.8	9.7	2.9	**13.0**
2021	-0.6	1.7	3.3	5.0	0.2	3.4	3.1	2.2	-5.1	6.3	-1.6	2.9	**22.2**
2022	-8.3	-4.8	4.4	-9.4	-0.2	-8.8	10.4	-4.5	-8.6	6.6	4.7	-4.8	**-23.1**
2023	2.2	-3.8	5.3	1.8	-1.6	4.7	3.7	-1.1	-5.5	-2.8	8.9	4.6	**17.0**
2024	2.6	3.3	1.6	-4.2	4.0	2.1							**9.6**

Total return since 2017: 83.8%

Geographical Allocation

Region	**% Fund**
North America	55.8%
Europe	36.8%
Cash and Equivalents	7.4%

Sector Allocation

Sector	**% Fund**
Information Technology	24.0%
Health Care	17.1%
Communication Services	11.6%
Consumer Staples	11.4%
Financials	10.0%
Industrials	9.3%
Consumer Discretionary	9.2%
Cash and Equivalents	7.4%

Top Ten Holdings

Name	**% Fund**
LVMH	9.2%
Mastercard Inc	7.1%
Alphabet Inc	6.7%
Assa Abloy AB-B	5.7%
Meta Platforms Inc	4.9%
Microsoft Corp	4.5%
Reckitt Benckiser Group PLC	4.1%
Diageo PLC	4.0%
Intuit Inc	3.7%
Nvidia Corp	3.6%
Total for Top Ten	**53.6%**

This factsheet shows the performance of Somerson's "Core Equity Strategy" from 31 March 2017 to 30 September 2023 then the Somerston Core Equity Fund from its launch on 02 October 2023.

The Core Equity Fund rose 1.7% in the second quarter.

Top contributors were Alphabet (+1.3%), Nvidia (+1.0%) and Apple (+0.8 %). Top detractors were LVMH (-1.5%), Diageo (-0.7 %) and Mastercard (-0.7%).

During the period the fund entirely divested from Intuitive Surgical and initiated a position in Reckitt Benckiser.

Cash stands at 7.4%.

Commentary

US equity markets began the quarter experiencing a period of weakness (losing 5.4% in the first three weeks of April), but a strong earnings season in May and June sent US markets to fresh all-time highs, led by The technology sector. Meanwhile, European stocks largely treaded water during the quarter, but also remain close to all-time highs. Enthusiasm for AI continues to be a defining trend in the current market environment and speaks to the recent US outperformance. The performance of the holdings in the Core Equity fund also reflects the AI trade, with **Nvidia**, **Apple** and **Alphabet** being the three top gainers during the quarter. While AI stocks continue to be in vogue, we are seeing investors become more discerning of the AI companies that they favour. Many of the companies that were initially 'AI beneficiaries' in 2023 have seen their stock prices under pressure in 2024 for not delivering the promised results. This is being acutely felt in the software segment of the Technology sector. This move has narrowed the leadership within the 'AI trade' to focus on those companies that are seeing tangible cash flows today, such as **Nvidia** and **Broadcom**. Consequently, we have seen overall market leadership also narrowing.

Equity valuations are looking stretched, which causes us to adopt a cautious stance. We are therefore taking opportunities to position the portfolio to more defensive equities. These are equities that are relatively less sensitive to economic gyrations, and/or they have a record of paying growing dividend streams and/or they have minimal volatility compared to their peers. Not only do these companies have a history of outperforming in equity bear markets, but they are also presently far more attractively valued and are generally under owned by investors. 'Bottom-up' considerations remain the primary driver for our stock selection in the Core Equity fund and we look for those companies which have compelling growth prospects, high and defensible margins, and attractive valuations.

Portfolio Leaders

Nvidia was the top performer in the fund over the quarter, gaining 36.7%. **Nvidia** was purchased in February when the stock was experiencing a period of weakness, and we added to the position on further weakness in April. Due to the strong share price performance, Nvidia has grown into being a top 10 holding in the fund. Nvidia's impressive gains represent the fact that it is one of the few AI beneficiaries which is translating its AI strategy into material quarterly earnings beats. The company reported an impressive set of results that surpassed even elevated expectations. This caused the company's market valuation to increase past all others to become the most valuable company in the world. At our internal research meetings, we often ask the question 'is this as good as it gets?'. Clearly, this is a question which will only be answered in hindsight, but we believe there are several compelling arguments which suggest that Nvidia's leadership can continue. In this quarter's Technology Letter, we provide a detailed overview of our thoughts regarding Nvidia's outlook. We encourage all investors to take a look.

By **Apple's** high standards, expectations were low heading into the second quarter earnings report. Market concerns were heightened due to a perceived weakness of the iPhone's competitive position in the Chinese market. Despite this, the company posted a solid quarter. While demand for Mac and iPads remained weak in the region, iPhone sales were encouraging and management commentary on the call painted an upbeat picture for growth in important emerging markets, such as India. Services growth is a key strand of our investment case for **Apple**. Growth here was the clear standout from the quarter, up +14%. Encouragingly, the installed hardware base once again reached an all-time-high across all products in all geographies. The installed base is the bedrock from which services revenue stems and suggests that momentum is sustainable. Unlike many companies over the past 18 months, **Apple** has been hesitant to rush an AI strategy to market. Though this has been to the frustration of many market participants, it follows the traditional **Apple** playbook of taking time with significant announcements. At the recent developer day, the company debuted its new AI features, called Apple Intelligence. The announcement was well received by the market, and caused the shares to march higher, reaching an all-time-high in mid-June. The shares gained 23.0% during the quarter.

Alphabet posted an impressive set of results in late April, which fuelled a 20.8% gain during the quarter. The strong performance of the Search business quelled some concerns from investors about the potential impact of ChatGPT on its market position in web search. YouTube was a standout from the advertising business in the quarter. The performance of 'Shorts' continues to be impressive, and the monetisation strategy is gaining momentum. This puts the company in a good position to capitalise on potential disruption to the short format video market if we do see Tik Tok banned in the US. Meanwhile, the Cloud business is seeing the benefit from the increasing demand for computing power. More than 60% of funded GenAI start-ups and nearly 90% of GenAI unicorns are Google Cloud customers according to management. **Alphabet** also announced its first ever dividend payment ($0.20).

Portfolio Laggards

Following a strong first quarter, where the stock tested all-time-highs and was the fund's top performer, **LVMH** shares have experienced a period of weakness in recent months. Shares closed the quarter down 13.6%. Partly this reflects heightened political uncertainty caused by the surprise French election, which has weighed on the French market. While this uncertainty dampens investor sentiment in the short-term, we do not believe it fundamentally undermines the long-term growth prospects for **LVMH**. Outside of the politics, weakness was caused by investor concerns that the post-pandemic period of strong luxury demand is now behind the company. We are inclined to agree, however, we note that the expectations and valuation are now very different to the levels seen in 2022 and 2023. The combination of EPS revisions and the price weakness has resulted in the company's valuation looking much more attractive. Ultimately, we do not believe a continuation of post-pandemic trends is necessary for the stock price to look attractive and we consider the risk/reward trade-off compelling. We continue to monitor demand in China, where we have seen some steps by the government to discourage extravagant spending. **LVMH** remains a high-quality company and is well positioned to produce strong organic growth over the long-term.

Like **LVMH**, **Mastercard** also had a weaker quarter following a strong Q1, with shares losing 8.3%. Importantly, we do not believe the price weakness reflects a deterioration of the company's fundamentals. The long-term transition from cash to digital payments remains very much intact and the card networks (primarily **Mastercard** and **Visa**) have among the strongest competitive positions in the payment ecosystem. **Mastercard** reported a solid first quarter that showed resilient consumer spending trends globally. Management did lower the full year revenue guide from 'high end of low double digits' to 'low end of low double digits'. However, FX headwinds were a key factor impacting the guide, which we consider worth 'looking through' for long-term investors. Cross border volume growth and value-added services were the highlights from the report as both beat lofty expectations, while commentary on new partnership wins was also encouraging. We continue to see **Mastercard** as well positioned for the long term and do not view the soft guidance as undermining our central investment case.

Diageo's price performance has continued to underwhelm in 2024, with the stock falling 14.9% in Q2. Demand has been under pressure in key spirits markets, such as the United States, which has led to concerns that the company's 5-7% organic growth target may be under threat. With initial signs that the painful inventory drawdown cycle is ending, EPS revisions could soon bottom, which would create room for the valuation discount to close. Despite the near-term uncertainty, **Diageo's** portfolio of beverages remains strong. The company has performed well in the beer markets (notable Guinness sales in the UK) and its new tequila products look particularly exciting. The company is increasing its investment in marketing to support near-term growth. While these investments have contributed to the EPS downgrade cycle, the opportunity for growth in the global alcoholic beverage market supports management's capital allocation rationale.

Activity

During the quarter, we sold the remainder of our holding in **Intuitive Surgical**. The company had been a great performer for the fund since initiation, however, as flagged in our prior letter, we had been actively trimming the position as we considered the stock to be unjustifiably expensive. We sold the remainder of our position at a then all-time-high in late May. We continue to believe the investment case is compelling but consider the embedded valuation risk too high for this point in the cycle. We would be happy to repurchase the stock at a more attractive price at a future date.

We sold a material portion of our **Mettler Toledo** position during the quarter. **Mettler Toledo** posted a strong result, which saw the shares jump 18% on the day. We have discussed previously that we believed **Mettler Toledo** entered the year facing undue pessimism on the outlook for near-term sales growth, which made the stock look undervalued. The quarterly report in mid-June acted as a catalyst for earnings revisions and, following the positive price reaction, we believed much of the valuation discount had closed. We therefore made the decision to take profits and recycle the capital to prospects with more attractive valuations.

We initiated a position in **Reckitt Benckiser** during the quarter. **Reckitt** is a company that we have previously held in the fund but have reintroduced due to its defensive nature and attractive valuation. The company produces a range of health, hygiene, and home products. **Reckitt** stock has been under pressure since February due to concerns regarding litigation risk in the US. However, by our calculations the stock price reaction has more than accounted for the likely impact to earnings and we therefore believe the risk is being 'priced in'. More broadly, we see a disconnect between the improving outlook for volume growth at the business and the rock-bottom valuation. **Reckitt** is a high-quality business that we believe is selling at an unjustified discount to its fair value, which makes it a compelling investment for the Core Equity fund.

The Somerston Investment Team

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