WAVERTON
INVESTMENT MANAGEMENT

# EUROPEAN CAPITAL GROWTH STRATEGY

FUND FACTSHEET - AS AT 30 SEPTEMBER 2020

## OBJECTIVES

### FUND AIM

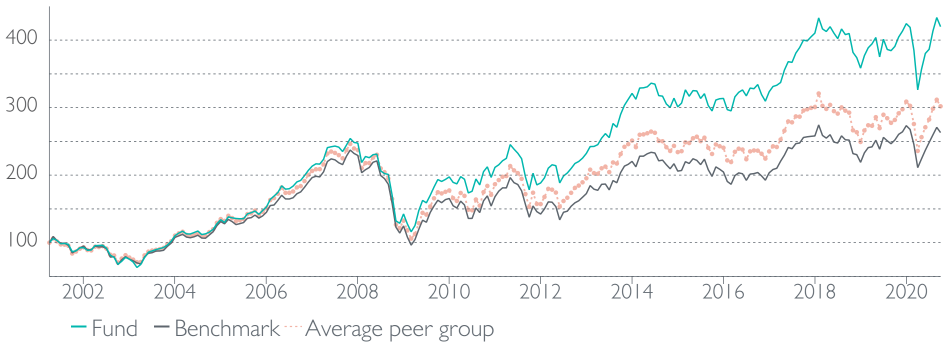
The investment objective is to generate capital growth by investing in a concentrated portfolio of equities selected from European markets. Overwhelmingly, but not exclusively, the managers invest in companies that are at the larger end of the capitalisation scale.

### INVESTMENT STYLE

The Fund invests in wealth creating companies at attractive valuations. Building concentrated portfolios from the bottom up, unconstrained by the composition of the Fund's benchmark index, the managers seek to make a small number of long-term investments, primarily in growing companies, with strong management and operating in favourable business environments.

## PERFORMANCE

### PERFORMANCE SINCE INCEPTION




**Risk Warning:** Past performance is no guide to future performance. The value of holdings may fall as well as rise and investors may not get back their initial investment.

Important Information: Performance displayed is for the I EURO Share Class of Waverton European Capital Growth Fund which is a UCITS fund registered in Europe and therefore not suitable for US Investors. The Waverton European Capital Growth strategy can be offered to US investors in a segregated account format. Performance is displayed net of fees and assumes income is reinvested.

| Period | 1 Month | 3 Months | YTD | 1 Year | 3 Years* | 5 Years* | Inception* Apr 01 |
|---|---|---|---|---|---|---|---|
| **Portfolio (%)** | **-3.1** | **8.7** | **-1.1** | **7.5** | **1.6** | **7.3** | **7.7** |
| Benchmark (%) | -2.9 | 5.9 | -3.8 | 4.4 | 0.9 | 5.8 | 5.2 |
| Morningstar Peer Group (%) | -3.2 | 6.9 | -2.3 | 7.3 | 0.9 | 5.6 | 5.9 |
| Quartile | 2 | 1 | 2 | 2 | 2 | 1 | 1 |

*Annualised

### DISCRETE CALENDAR YEAR PERFORMANCE

| Period | 2019 | 2018 | 2017 | 2016 | 2015 |
|---|---|---|---|---|---|
| **Fund (%)** | **18.4** | **-12.6** | **26.9** | **3.1** | **4.2** |
| Benchmark (%) | 24.8 | -15.1 | 26.8 | -0.6 | -0.7 |

### STANDARDISED PERFORMANCE

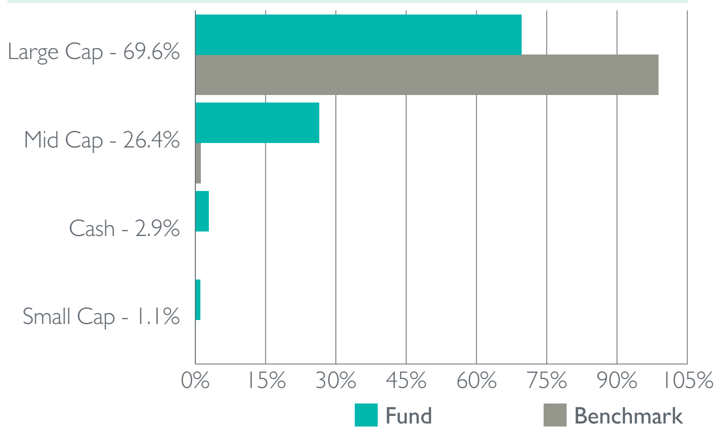
| Period 1 year to | 30/09/2020 | 30/09/2019 | 30/09/2018 | 30/09/2017 | 30/09/2016 |
|---|---|---|---|---|---|
| **Fund (%)** | **7.5** | **-4.7** | **2.4** | **19.7** | **13.3** |

## PORTFOLIO SUMMARY

### TOP 10 HOLDINGS

| | |
|---|---|
| Nestle | 7.0% |
| Novartis | 5.7% |
| Air Liquide | 5.0% |
| Linde | 4.9% |
| Novo Nordisk | 4.9% |
| Deutsche Post | 4.7% |
| Deutsche Telekom | 4.2% |
| Husqvarna | 3.8% |
| Swedish Match | 3.6% |
| Konecranes | 3.6% |
| **Total** | **47.4%** |

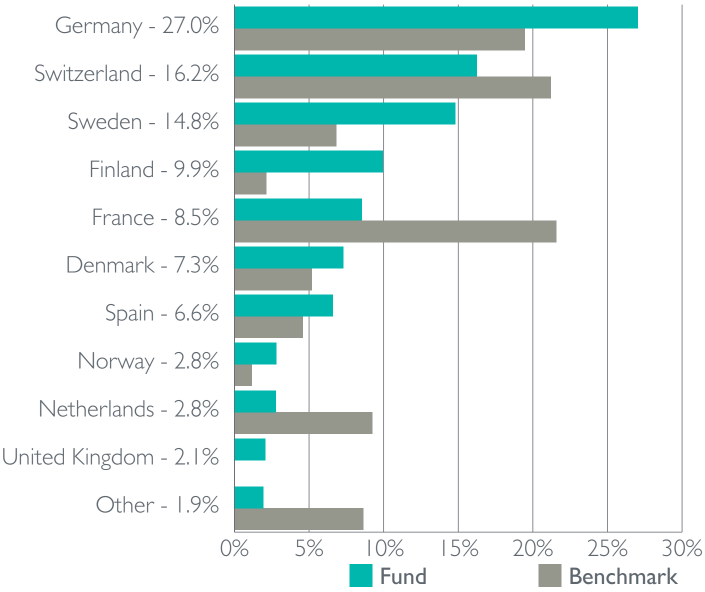
### MARKET CAP



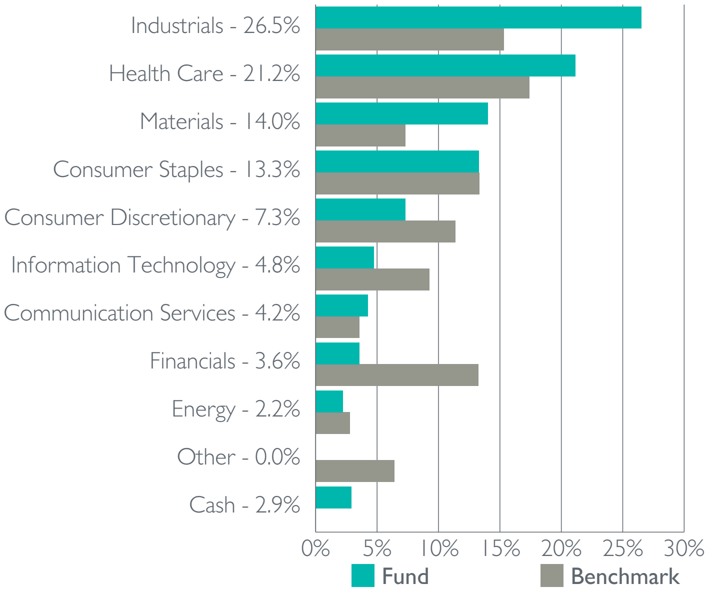

**Sources:** Waverton Investment Management, Morningstar.

## PORTFOLIO SUMMARY - CONTINUED

### COUNTRY




### SECTOR




## PORTFOLIO ACTIVITY

| Purchase | Month | Sale |
|---|---|---|
| - | **Jul - Sep 2020** | Imerys, Navigator, Neles |

## MARKET REVIEW

After the steep bounce of the second quarter, European markets managed further modest gains in the third quarter. The best sector was industrials, closely followed by consumer discretionary and the worst, yet again, oils and banks.

The EU Green Deal is the centre piece of its fiscal stimulus programme. The deal targets carbon neutrality by 2050 through the sponsorship of both renewable and decarbonised energy. For the gases industry this is likely to present opportunities for both blue hydrogen (hydrocarbon feed stock with carbon capture) and green hydrogen (electrolysis) with existing and new end markets. This very much plays into the Fund's holding in Linde and Air Liquide.

On 22 September, Chinese President Xi Jinping made a surprise and bold announcement that China will target carbon neutrality by 2060. The details have yet to be unveiled, but this may well involve China raising gas in its energy mix from 7-8% currently to 15% by 2030; natural gas being the easiest way to phase out coal rapidly and on a large scale. If China were to target a 20% natural gas mix by 2035 (with LNG imports representing 25% of Chinese gas supplies) it would put Chinese LNG imports at roughly 181mtonnes by 2035, or 2.8x more than today's level. Excellent news for GTT, a French company in the Fund with a monopoly on membrane technology for gas transport ships.

Banks remain out of favour with governments and investors. In September the Swedish government proposed a new banks tax from 2022 that will reduce the net earnings of the bigger banks by around 5%. Rather unfairly small banks will be exempt. The pressure is relentless and Handelsbanken announced the decision to halve its branch network in Sweden. For a bank that has consistently held its branch-led strategy as the key to its success, and it has been far more successful than any other we know of, it must have been a tough decision.

## PERFORMANCE REVIEW

The Fund's Q3 total return in dollars was 8.7% versus Europe ex UK index of 5.9%. In line with our history this all came from stock selection. Asset allocation and currency effects were minimal. The lion's share of the alpha came from Industrials, specifically Cargotec (1%), Konecranes (0.9%) and Deutsche Post (0.8%). Husqvarna

(0.82%) and Elekta (0.79%) were also good. We lost on Eramet (0.59%) and Bayer (0.51%).

Of the stocks mentioned above, Deutsche Post, with its DHL division, is the largest in the Fund. Its large fleet of cargo planes have been a direct beneficiary of Covid as passenger planes, who take 50% of world air cargo in their bellies, are grounded. Added to this is the ever increasing importance consumers place on reliable and quick delivery. They are super excited about the potential of the $1.3 trillion B2B delivery market where they forecast that speed and timing of deliveries will follow the B2C e-commerce trajectory.

## STOCK EXAMPLE

Bayer's profit warning after the market's close on 30 Sept undermined our confidence in the management's ability to deliver on our 5 key attributes. We sold the next morning. The warning was based not only on the division that investors were most excited by, namely Crop Science, but also based on its projected 2021 earnings. It is rare for a company to warn on a year that has yet to start and implies that the outlook in this key division is murky indeed.

The bull case had been that ex litigation the stock was cheap. Whilst litigation progress has been made, it is certainly not a done deal. No doubt made more difficult by thus far Bayer losing every court case. Another area of concern is the proposed cut to the dividend pay-out ratio, on the reduced earnings to 30%, from 40%. This indicates either a serious misalignment with ordinary shareholder's interests (more earnings dilutive acquisitions?) or a management fear that earnings will be insufficient to service the debt + litigation liabilities.

Over the years we have been asked about Bayer many times. It seemed cheap on a single digit prospective P/E. Despite the stock halving, so have earnings in a set of businesses that are supposed to be relatively stable. The risk is that the company is now broken up, releasing value, but in the absence of this the outlook is very uncertain. We plan to switch the money into a stock where management seems in better control of its destiny.

## OUTLOOK

Should one back super cheap Value or expensive Growth? – Neither…

Value is seeing the capital cycle at its most brutal. Banks, oils, telcos, subscale engineers and most autos have all suffered from static end markets and management teams driven by market share. Combined with fragmented markets and largely undifferentiated products, pricing has been under increasing pressure. Most of these markets are not even beginning to stabilize. Banking is fragmenting further with internet start-ups, oil is being substituted, telcos show no sign of consolidating and whilst Peugeot has bought Fiat, competition abounds in autos from new players, new technology and new rules.

Neither are we a fan of super high P/E 'safe' Growth stocks. We have simply seen too many disappoint. Remarkably, of the nine largest US tech companies by capitalization at the height of the dot com boom in March 2000, six never achieved a similar market cap again and a further one went bust.

We are navigating a fairly narrow path (in terms of the numbers of stocks available) between the two. We often refer to the stocks we like as 'dirty pearls'. They are neither Growth, basking on 40x peak margins, nor deep Value. Their common traits, in our view, are troubled earnings now but not a few years out. We really like the recently announced merger of Konecranes and Cargotec. On port automation they fit hand in glove. The port related business would represent around 40% of the merged entity, and its combined global port equipment market share could be around 35-45% but much higher in some sub-segments that may catch the eye of the competition authorities. This is a prime example of the capital cycle in action. Ports will be offered essentially either Finnish engineering/software or Chinese. With the modest rating (both are on a P/E of roughly 11.5x 2021) it is a high conviction holding; together they are 8% of the fund.

We also like travel stocks Amadeus, Fraport and Aena. Fraport is one of the most heavily shorted stocks on the German market. Clearly near term news is bad and not widely held but our thinking is that investors should be able to look out a year or so. To be bearish now assumes there will be no progress on 1. Vaccines, 2. Testing, 3. EU-wide uniform traffic light system, 4. The North Atlantic re-opening post the US Election (most likely first in an air bridge form), or 5. Consolidation/bankruptcies (possibly smaller airports?). Together these holdings are also 8% of the fund; these sorts of stocks tend to give the fund great draw down data as they are not widely held and if we are correct have a lot of upside.

# BIOGRAPHIES

### CHRIS GARSTEN

Chris has managed the European Capital Growth Fund with Charles Glasse since its inception in 2001 and came to Waverton upon the acquisition of 2CG Senhouse which he co-founded in 2001. The first decade of his career was spent as a member of the Europe ex-UK equities team at Credit Suisse Asset Management, where he was Director and Lead Manager of an award winning Netherlands Country Fund. Chris read Business Studies at London Guildhall University, graduating in 1986.

FUND MANAGER

Chris Garsten

### CHARLES GLASSE

Charles has managed the European Dividend Growth Fund (formerly named the European Income Fund) with Chris Garsten since its inception in 2005 and came to Waverton upon the acquisition of 2CG Senhouse which he co-founded in 2001. The first 13 years of his career were at M&G (1987-2000) where he ultimately headed the Continental Europe Team and, for over a decade, managed the flagship M&G European Dividend Fund. Charles graduated from Queen's College, Oxford in 1987 with a degree in Chemistry.

FUND MANAGER

Charles Glasse

### JOHN BUCKLAND

John has been the Research Analyst on the European Capital Growth Fund and European Dividend Growth Fund since 2015. John joined Waverton with the acquisition of 2CG Senhouse in May 2016 and is responsible for the investment process and stock selection. He has broad experience in fund management, investment banking and equity broking, having worked for Credit Suisse, Daiwa SMBC, HSBC, MF Global and MainFirst for over 20 years as a well-regarded equity analyst covering the automotive sector and European industrial companies. John has a BSc Honours Degree in Mechanical Engineering and an MBA.

ANALYST

John Buckland

# FUND DETAILS

## FUND FACTS

| | |
|---|---|
| Launch Date | 1st April 2001 |
| Morningstar Category | Europe Ex-UK Large Cap Equity |
| Benchmark | MSCI Europe ex UK Index |
| Fund Size | $227.3m |
| No. of Holdings | 29 |
| Domicile | Ireland |
| Sedol | BF5KTG8 |
| Bloomberg Code | WAVECIE |
| Fund Type | OEIC |
| Base Currency | EUR |
| Other Currencies | GBP |
| Ex Dividend Dates | 30th April |

| RISK STATISTICS | FUND | AVERAGE PEER GROUP |
|---|---|---|
| 3Y Annualised | | |
| Fund Volatility (%) | 17.0 | 18.0 |
| Index Volatility (%) | 16.6 | - |
| Sharpe Ratio | - | - |
| Information Ratio | 0.1 | 0.1 |
| Tracking Error | 4.7 | 4.5 |
| Alpha (%) | 0.7 | 0.1 |
| Beta | 1.0 | 1.0 |
| Active Share (% - Current) | 84.3 | - |

## FUND INFORMATION

| Share class | ISIN | Minimum | AMC | INC/ACC | NAV | Historic yield (%) | Ongoing charge (%) |
|---|---|---|---|---|---|---|---|
| I EUR | IE00BF5KTG81 | 1,000,000 EUR | 0.75% | INC | 2.729 | 1.40% | 0.95% |
| L EUR | IE00BF5KTD50 | 500,000 EUR | 1.00% | INC | 2.643 | 1.15% | 1.20% |
| I GBP | IE00BF5KTH98 | 1,000,000 GBP | 0.75% | INC | 2.022 | 1.35% | 0.91% |
| R GBP | IE00BF5KTF74 | 10,000 GBP | 1.25% | INC | 190.196 | 0.87% | 1.40% |

# CONTACT DETAILS

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