SOMERSTON ASSET MANAGEMENT

SOMERSTON MULTI ASSET FUND

INVESTMENT LETTER No.28 AS AT 31 MARCH 2024

The Somerston Multi Asset Fund (US0 class) rose by +3.2% in the month and rose by +4.4% over the last three months.

The MSCI World Equity Index rose by +3.4% during the month and a composite of UK, German and US Government bonds rose by +1.3% in the month. Our composite reference index rose by +2.7% in the month and rose by +6.5% over the last three months.

Performance (%) US0 Class

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Year
2017				0.9	2.7	-0.9	0.6	0.6	-0.5	0.6	-1.2	1.9	**4.5**
2018	4.8	-3.7	-1.0	-1.0	0.8	-0.2	0.9	0.3	0.0	-2.3	1.8	-0.4	**-0.2**
2019	1.1	-0.6	2.8	1.3	-1.8	5.6	0.7	0.6	-0.6	2.1	2.8	3.3	**18.5**
2020	-0.3	-5.9	-8.5	6.9	2.4	1.8	7.4	3.1	-2.2	-1.0	5.2	5.2	**13.6**
2021	-0.3	0.8	-0.1	2.3	2.5	-0.2	2.2	0.5	-5.1	5.2	-1.7	3.2	**9.3**
2022	-5.9	-1.1	2.6	-3.5	-1.4	-4.1	4.3	-3.8	-4.9	1.3	3.7	-1.5	**-14.0**
2023	2.5	-4.0	2.9	1.1	-1.3	2.0	2.5	-1.2	-2.5	-0.6	6.3	4.7	**12.6**
2024	0.0	1.2	3.2										**4.4**

Total return since inception 55.0%

Top Ten Equity Holdings

Name	**% Fund**
LVMH	4.7%
Mastercard Inc	3.6%
Alphabet Inc	2.8%
Assa Abloy AB-B	2.7%
Microsoft Corp	2.5%
Diageo PLC	2.2%
UnitedHealth Group Inc	1.9%
SGS SA	1.8%
ASML Holding NV-NY Reg Shs	1.8%
EssilorLuxottica SA	1.7%
Total for Top Ten	**25.7%**

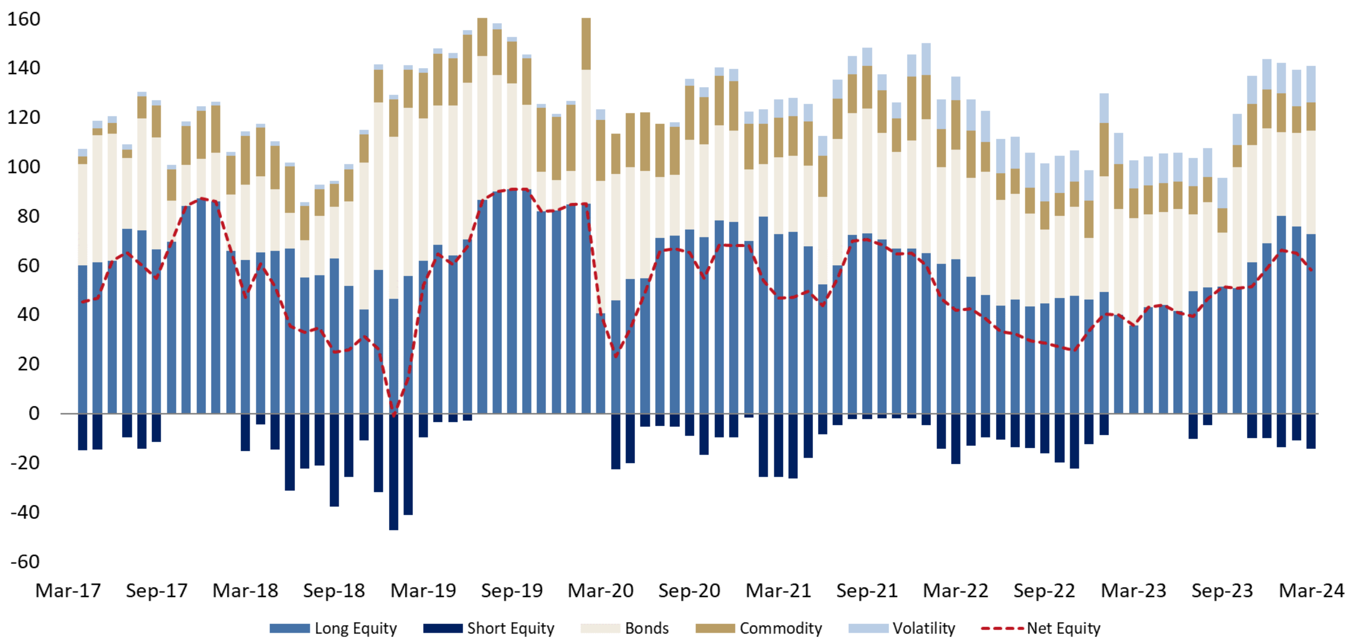
Currency Allocation

USD	79.2%
JPY	7.0%
GBP	4.7%
SEK	2.7%
EUR	2.3%
NOK	2.3%
CHF	1.8%
Total	**100.0%**

Asset Allocation

	Long	Short	Net	
Core Equity	41.4%		41.4%	↓
Small Cap Equities	4.9%		4.9%	↑
DM Equities Ex US	4.9%		4.9%	↓
Real Estate	2.6%		2.6%	↑
Resources	4.8%		4.8%	↑
Equity Long Short	14.1%	-14.4%	-0.3%	↓
Equities	**72.7%**	**-14.4%**	**58.3%**	↓
Nowegian Govt Bond	2.3%		2.3%	↓
Corporate Bonds	4.7%		4.7%	↓
US Govt Ultra Long Bond		-6.1%	-6.1%	↑
US Govt 2 yr. Bond	24.5%		24.5%	↑
US Govt TIPS	16.6%		16.6%	↓
Bonds	**48.0%**	**-6.1%**	**41.9%**	↑
Silver Derivatives	2.9%		2.9%	↑
Gold Miners Equities	2.8%		2.8%	↑
Gold Bullion Derivatives	5.7%		5.7%	↑
Commodities	**11.4%**		**11.4%**	↑
Volatility and CTA	14.7%		14.7%	↓
Total All Assets	**146.8%**	**-20.5%**	**126.3%**	↓

Evolution of Asset Allocation for Somerston Multi Asset Fund



Performance

- The Fund enjoyed a good Q1, appreciating +4.4%.
- Core Equites contributed +3.8% however our underweight equity allocation detracted from relative performance.
- Macro Equity positions added +0.3%
- Bonds detracted -0.5% from performance.
- Allocations to commodities and precious metals were additive to performance, contributing +0.6%
- Volatility also performed well, contributing +0.8%.

Commentary

Macro

Financial markets have evolved during the first quarter of 2024 but much of what we wrote about in our year end letter remains as pertinent today. Earnings remain on trend and financial conditions remain constructive as the US continues its magic trick of stimulating the economy while tightening monetary conditions. Bond markets continue to be range bound as the highly inverted yield curve caps how far the bond market can move.

The main development in Q1 is the now universal 'carefree tone' of the market, which in our opinion, is forcing many risks to be mispriced:

- Options are cheap as few are interested in paying the insurance premium to hedge.
- Buying investment grade credit risks now earns you a paltry 1% premium for taking that risk.
- Buying 'junk' gets you 3% more than treasuries, down from 6% eighteen months ago.
- The current earnings yield on the broad US equity market is 3.9%, below yields offered on Government 3- month cash T Bills that offer 5.4%. This difference, where cash is yielding of 1.5% more than earnings yields has not been seen since 1999.
- Stable dividend paying stocks have been shunned in favour of growth and cyclicality. The US Dividend Aristocrats – stocks that have paid a growing dividend stream over 25 years - are trading at a rare discount to the overall market.

Just recently, the Federal Reserve indicated its willingness to cut rates three times in 2024. With many financial markets at all-time highs, and an elevated level of investor complacency, the Fed's actions only forces risk premiums lower still and the eventual unwind will be that much more unpalatable.

Low levels of risk premiums can continue for some time, but we are fortune enough to observe some very attractive 'risk off' strategies that we are allocating to.

1. The Fund's allocation to Long Volatility strategies is at 14.7%, the highest level since the fund launched. With volatility so low, we are afforded protection from erosion in option premium, while rising volatility is about the only certainty in adversity.
2. Secondly, we continue to allocate to cheap defensive equities and short expensive cyclical stocks. While the net position is close to zero, we are long 14.1% and short the same.
3. The fund has been the beneficiary this quarter of its allocation to Gold, and the recent diversification into Silver and Gold Miners. In total the fund has 11.4% invested in precious metals.
4. We have also implemented curve steepening trade which profits from the curve steepening and offering premium to longer duration assets.

Over the medium term, we believe our core equity book will do well, but valuations are becoming stretched along with the rest of the market. These risk off strategies offer considerable balance to the portfolio.

Not everything is overvalued, however. Smaller companies, resource companies, emerging markets and many areas of Non US Developed markets appear well below historic averages. Our macro equity strategy has 16.9% exposure.

Activity During the Quarter

1. **Core equity:** During the period the Fund initiated positions in Nvidia, Meta, Eli Lilly, Novo Nordisk, Visa and Synopsys. The Fund entirely divested from Estee Lauder. The rationale is discussed below.

2. **Macro Equity:** We have gone long Small Caps, Real Estate and Resources and initiated positions to be long Defensive sectors and short Cyclical sectors. All these positions have been initiated on valuation grounds.

3. **Bonds:** We are positioned to benefit from a curve steepening with minimal duration exposure.
4. **Commodities:** We have maintained exposure to Gold bullion, Silver and mining stocks.
5. **Volatility:** With volatility near low levels we have modestly added to long volatility strategies.

Core Equity

Top contributors were LVMH (+1.9%), ASML (+1.8%) and Mastercard (+1.0%). The largest detractors were Adobe (-0.6%), Estee Lauder (-0.5%) and Apple (-0.5%).

During the quarter we have been opportunistically taking advantage of share price strength to raise cash and at quarter end 6.9% of the Fund was allocated to cash. We look for opportunities to deploy this.

ASML was a strong contributor to performance during the quarter, with the stock returning 28.4%. **ASML's** importance in the AI industry is clear; it is the only company with the capabilities of producing the EUV technology necessary to manufacture advanced chips. **ASML** reported a strong quarter in late January, which saw the share price jump to an all-time-high. This high has since been surpassed, and we have grown more cautious of the company's valuation. We therefore trimmed the position and invested the proceeds in **Synopsys**. Like **ASML**, **Synopsys** is a 'picks-and-shovels' play on the semiconductor industry. The US-based company develops electronic design automation (EDA) software, which is used in the entire chip design process. The company also owns and licenses semiconductor intellectual property (IP) that chip designers rely on. The combination of software sales and licensing revenue gives the company an attractive recurring revenue profile and the attributes of a 'quality compounder'. We see several important industry trends that should support growth at **Synopsys**. These include the growing prevalence of in-house chip design leading to additional software demand, and increasingly advanced chip designs requiring greater IP spending.

Intuitive Surgical was a strong performer for the Fund, up 18.3% in the quarter. In March, **Intuitive Surgical** received FDA approval for the company's fifth-generation robotic system, da Vinci 5. The product roll out will be gradual but is instrumental in increasing the addressable market of da Vinci procedures. The investment case for Intuitive Surgical is compelling; robotic assistance in surgery can bring significant cost and performance benefits yet remains significantly underpenetrated. It is the market leader in its field, however, despite these merits, in our view, the stock remains expensive. For this reason, we have been active in taking profits and will wait to take advantage of potential future weakness.

During the quarter we completely sold our position in **Estee Lauder**. Historically, the company has been a strong performer, but has recently faced a number of headwinds due to demand weaknesses in China and a misallocation of inventory that built up during the pandemic. We sold the position and invested the proceeds into existing holding, **LVMH**. **LVMH** has since reported an impressive quarter, which saw the shares gain almost 12% on the day of the announcement. Though there had been market fears that overall luxury demand would experience a period of weakness, the reality has been more nuanced. We have seen a bifurcation in the sector, with high-end outperforming aspirational luxury. **LVMH** remains well positioned in this regard, with a portfolio full of some of the most-renowned brands in the industry. The company was the largest position in the Fund and was the top contributor to performance in the quarter.

Adobe was the largest detractor from the Fund during the quarter, with the stock falling 15.4%. As discussed in our January letter, we viewed **Adobe** as one of the likely winners for the AI race, but we started to take profits on valuation grounds. Since then, the market's enthusiasm for **Adobe's** AI offering has come under pressure following the release of 'Sora' from OpenAI, which sparked fears of increased competition in the digital creation space. It was in this context that a solid set of results in mid-March underwhelmed the market for not sufficiently addressing competition concerns. While we consider competition an important risk, we believe the market has been too quick to write off **Adobe**. We note that this quarter showed many areas of strength, such as Firefly adoption rates, and we continue to view management's AI strategy as sensible. With the stock down c.22% from its early-February high, we felt the market was discounting the risks too heavily and that the valuation looked more attractive. We therefore added to the position following the post-earnings declines.

Apple shares have been under pressure this quarter, falling 10.8%. The US Justice Department sued **Apple** for violating antitrust laws by blocking rivals from accessing hardware and software features on its devices. Simultaneously, there was an EU antitrust announcement on 'big Tech' generally. The lawsuits have drawn parallels to the 1998 anti-trust case against Microsoft. **Apple** is a mature company that is able to use its 2 billion user base to provide services with annuity-style revenues. It has a huge net cash balance of $72 billion and, with free cash flow over $100 billion, it is priced with a 4% free cash yield. While growth is moderate, we consider the **Apple** ecosystem as attractive. Much of the accusations at **Apple** would potentially compromise the speed, responsiveness and security of the platform and are defensible, whereas other practises may well need refining.

During the quarter, we initiated positions in two prominent pharmaceutical companies, **Novo Nordisk** and **Eli Lilly**. In recent years, both companies have emerged as leaders in the obesity treatment market. The breakthrough GLP-1-based medicines have a significant addressable market. Initial demand has been strong, both companies are currently supply constrained and actively expanding production. The long-term runway for growth is substantial, and we expect to see further adoption as costs come down and an oral version of the treatment becomes available. In addition, GLP-1s are increasingly finding use in non-obesity treatments. In the case of **Novo Nordisk's** Wegovy, the recent FDA approval for use in treatment of heart disease significantly increases the total addressable market for the drug. Trials are ongoing for use of GLP-1s in treating a range of other conditions, including Alzheimer's disease, fatty liver disease and sleep apnea. Since purchase, **Novo Nordisk** has returned 14.2% and **Eli Lilly** has returned 3.7%.

Nvidia is a leader in the semiconductor market and has been a holding in the Somerston Technology Fund for several years. The recent release of the Blackwell chip reinforced our view that **Nvidia** is now fundamentally a platform business. We expect revenue to become less cyclical over the years and more reliant on services than products. We have now purchased the name in the Core Equity Fund as we consider the company to have shifted its business model to one which aligns with the mandate of the Fund. The company is not solely reliant on the buildout of AI infrastructure and is primed to deliver compounding revenue from its strength in AI model inference and its growing software business. The share price gains over the past year are significant, yet the earnings improvement has largely matched the stock price. We consider the valuation to be reasonable considering the significant runway for growth. Our current position is modest, but we will look to add when the opportunity is presented. The holding has returned 16.9% since purchase.

We initiated a small position in **Visa** during the quarter. Visa plays a vital role in the global payment ecosystem through its position as a major credit and debit card network. The business has significant barriers to entry, which protect high margins and attractive returns on capital. We are positive on the long-term growth outlook for card networks due to the further scope for the digitisation of global payments, particularly in the business-to-business space. The Fund also holds a position in fellow card network Mastercard, which was a top contributor during the quarter.

Meta was purchased due to its impressive execution in advertising and its strategic intention in artificial intelligence. The digital ads industry had a tough 2023 with ad prices weak across the sector, yet **Meta** was a standout from the pack. This is particularly encouraging considering the changes to **Apple's** IDFA policy, and TikTok's share gains which posed a material headwind to the company. In our view this strength clearly demonstrates **Meta's** effective deployment of AI technologies to improve the underlying performance of its advertising platform. **Meta** has acquired significant AI infrastructure and intends to provide a platform for AI applications accessible to its 4 billion installed user base. We believe the company has significant scope for further growth in the coming years.

Nick Wakefield

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