STENHAM
ASSET MANAGEMENT

Q1 2024 Investor Letter

Stenham Equity UCITS Fund

Performance Review

Fund vs. Benchmark[1]	Q1 2024	YTD 2024	Since Inception
Stenham Equity Fund (A1)	**+13.9%**	**+11.7%**	**+216.5%**
MSCI World Index	+8.4%	+4.9%	+158.8%
Relative	+5.5%	+6.8%	+57.7%

Portfolio Attribution

Top Contributors – Q1 2024	Portfolio Weight	Attribution
General Electric	6.8%	+2.1%
ASML	4.0%	+1.3%
Applied Materials	4.1%	+1.2%

Top Detractors – Q1 2024	Portfolio Weight	Attribution
Cellnex	4.3%	(0.5%)

Portfolio Discussion

Semiconductors (ASML, Applied Materials)

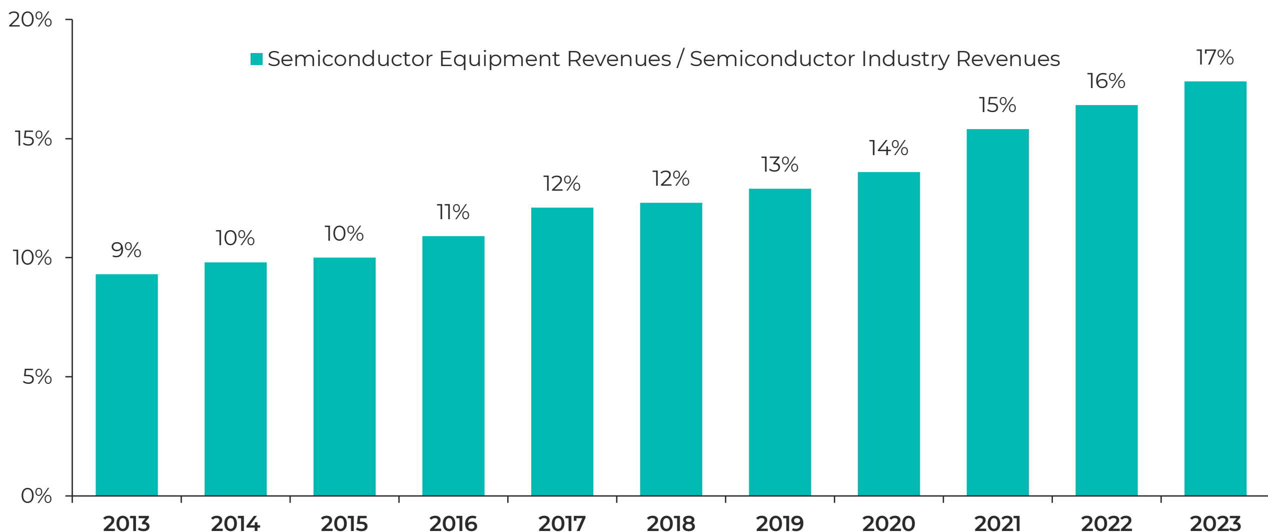
Our semiconductor holdings in **ASML** (ASML NA) and **Applied Materials** (AMAT US) were among the top contributors to performance during the quarter. The PHLX Semiconductor Sector Index (SOX) rallied 17% over the period while ASML and Applied Materials outperformed, returning 31% and 27%, respectively. As capital equipment providers, both companies produce the machinery used to manufacture semiconductors. These companies are benefitting from the long-term secular growth in the cost of producing the most advanced chips as complexity in these processes is increasing exponentially. Ten years ago, the cost of building a facility capable of producing the most advanced chips at the time would require c.$1bn of capital. Today, the cost of building the most advanced chip-making facilities is upwards of $20bn, making just one of these facilities among the three most expensive sites in the world. Typically, ~80% of these outlays are in the machinery

[1] *Performance as of 24 Apr 2024 is presented net of fees. Stenham Equity Fund Class A1 reactivation date 18 Nov 2020. Stenham Equity Long Only Strategy inception date 13 Apr 2012. Past performance does not predict future returns. Source: Stenham, Bloomberg. This is a marketing communication. Please refer to the Fund prospectus and KIID before making any final investment decisions.*

required, meaning the capital equipment companies are significant beneficiaries of the growing costs in semiconductor manufacturing.

More recently, the industry found itself in the crosshairs of geopolitical tensions. Semiconductor sovereignty is becoming increasingly important; as of today, over 80% of the world's semiconductors are manufactured in South East Asia. Other regions, such as the US and Europe, are recognising the importance of semiconductors and are pushing for localised production. In fact, in Q1 2024 alone, Samsung committed to double their capital spending on chip making facilities in the US from $22bn to $44bn while Taiwan Semiconductor Manufacturing Co. (TSMC) committed to increase their spending in the US by $25bn. These investments are hugely significant in the context of a semiconductor equipment market that is worth c.$93bn today, as this will translate into sizeable demand for new equipment for these facilities. Finally, the industry continues to be buoyed by the rising demand for chips being driven by Artificial Intelligence (AI). AI is driving not only the need for more chips, but also exponentially more advanced chips and, as per the above, both will translate into rising equipment demand. For example, the latest generation of iPhones uses Apple's A16 chip, capable of processing 17 trillion operations per second, referred to as 17 TOPS. Meanwhile, Nvidia's latest generation of products used for AI (GB200 GPU) will have 10,000 TOPS or, said differently, the ability to process almost 600x more operations per second than an iPhone 15. While these points clearly reflect our positive long-term view on the space, we are cognisant that near-term valuations in the sector have meaningfully expanded as a result of market euphoria around AI. As such, we are carefully managing our exposure and maintaining our valuation discipline.

Rising capital intensity is driving higher semiconductor equipment revenues as a share of overall industry revenues[1]



Aerospace (General Electric, Safran, Airbus)

Our aircraft engine-maker holdings in **General Electric** (GE US) and **Safran** (SAF FP) were among the top contributors to performance during the quarter.

Through their joint venture CFM International (CFMI), GE and Safran are the world's largest aircraft engine-maker. On the supply side, the industry's stringent performance and safety requirements inherently foster an oligopolistic structure, with CFMI holding a dominant share exceeding 70% of the global narrowbody engines

[1] *Source: Gartner, Bernstein.*

market. On the demand side, the industry is supported by a powerful secular tailwind, as people's propensity to travel rises alongside their wealth, resulting in global miles flown having outpaced GDP by ~2x over the past two decades. In our view, the interplay of these dynamics offers promising long-term prospects for the aerospace industry, in particular for the engine-makers.

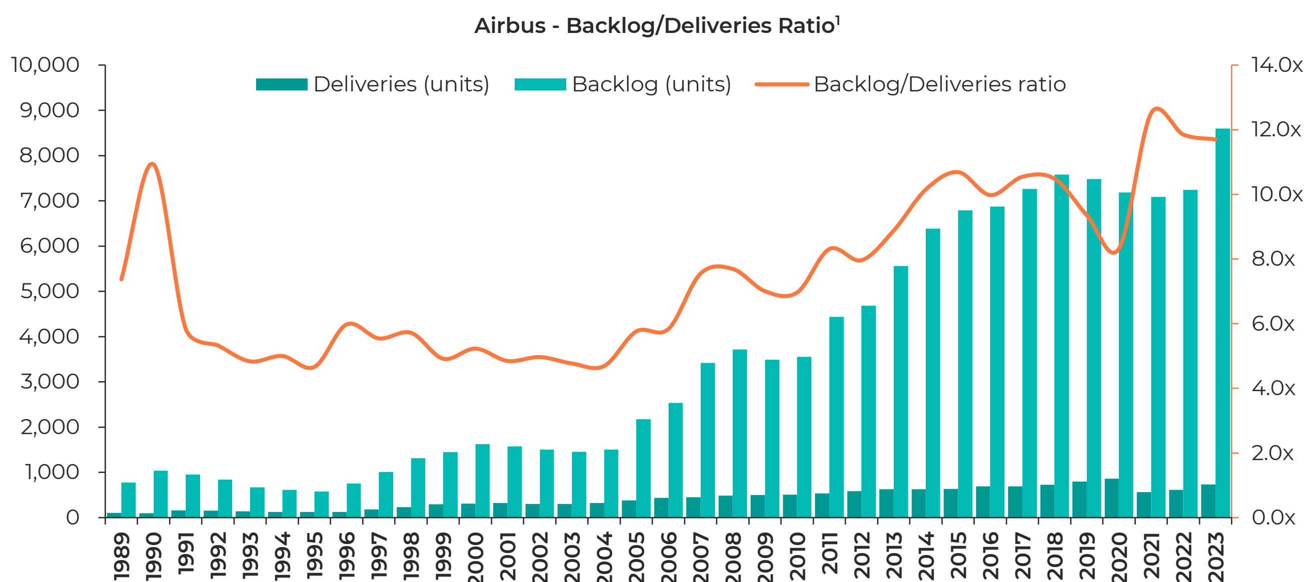
During the first quarter, GE returned 38% and Safran 32% as these factors carried forward strong momentum from last year. As discussed in previous letters, we believe we are in a golden era for the aircraft engine aftermarket, underpinned by the combination of strong air travel and supply chain constraints, translating into a higher-for-longer utilisation of the existing aircraft fleet and, ultimately, an increased demand for engine maintenance. In addition, GE outperformed Safran as our idiosyncratic thesis around the separation of GE Vernova (their power & renewables business) unfolded, with the spin-off successfully executed in early April leaving GE as an attractive pure-play aerospace company.

The outlook for engine makers remains favourable in our view, with aftermarket growth at above-average levels. This positive outlook is supported by the carryover of unfulfilled shop visits from last year, coupled with delays in new aircraft deliveries stemming from Boeing's recent challenges, further intensifying utilisation rates of the existing fleet.

Leveraging some of the insights gathered from our work on the aerospace sector, we initiated a position in **Airbus** (AIR FP) in January.

Similarly to the engine makers, the company enjoys a dominant position in a secularly growing market. Yet, we believe Airbus is also differentiated as it stands at the edge of an inflection in growth. Airbus' deliveries have remained below pre-pandemic levels for the past four years, as airlines initially preserved cash and supply chains were subsequently constrained. During that period, considerable pent-up demand was accumulated and is now poised to be released. Today, the company's backlog stands at an all-time high, with its orderbook sold out until the beginning of the next decade, and deliveries expected to grow twice as fast as their structural rate over the years ahead.

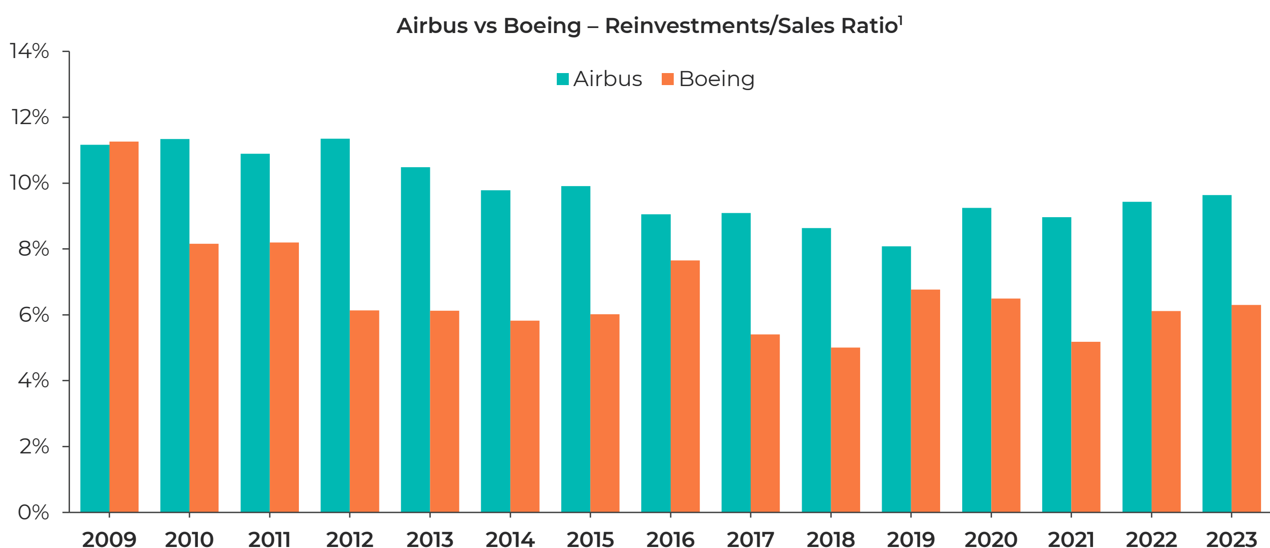
Airbus - Backlog/Deliveries Ratio[1]



[1] *Source: Airbus, Stenham Asset Management.*

In the aftermath of Boeing's door plug incident on Alaska Airlines flight 1282, the company is now facing material delivery and certification delays. With the A320 Family sold out until the early 2030s, Airbus is limited in its ability to exploit Boeing's current quality issues and gain share over the 737MAX. Nevertheless, should airlines doubt Boeing's ability to resolve these issues rapidly, new orders could increasingly skew towards Airbus, fuelling a longer-term market share shift. This was illustrated by key Boeing customers, such as United Airlines, recently fighting for scarce delivery slots on Airbus' schedule.

In our view, corporate culture is an underappreciated factor which can often have profound implications for long-term shareholder value creation. Over the past two decades and especially since its 1997 merger with McDonnell Douglas, Boeing has been reinvesting less into its business in comparison to Airbus, prioritising short-term shareholder gratification at the expense of long-term customer satisfaction, and, ultimately, passenger safety. From our perspective, Boeing's recent challenges are rooted in an inferior culture and should translate into a relative premium for Airbus.



Towers (Cellnex)

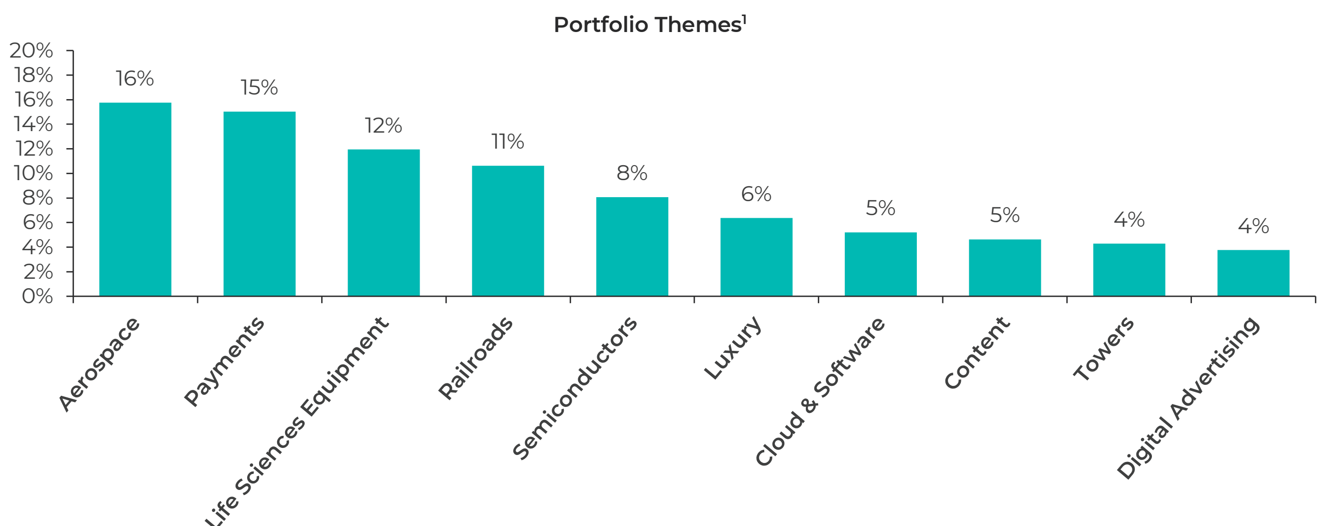
Cellnex (CLNX SM) was the sole detractor to performance as rate sensitive stocks underperformed during the quarter. Typically, tower assets are inversely correlated with yields due to their bond-like characteristics, resulting in a technical weakness in these stocks during periods of rising yields. From a fundamental perspective, however, we note several improvements that were highlighted during Cellnex's recent capital markets day which we attended. Firstly, the business is improving their capital allocation significantly by increasing shareholder return through dividends and buybacks. With dividends growing 7-8% per annum and €4bn earmarked for share buybacks, this alone should deliver a material boost to investor returns over the next several years. Secondly, the company is pursuing non-core asset sales to simplify their tower portfolio, improving profitability and using the proceeds to reduce leverage and accelerate the above mentioned shareholder returns. Cellnex are able to sell assets at highly attractive multiples due to robust demand for towers from private equity and infrastructure fund buyers. These buyers are sitting on elevated levels of dry powder and are prioritising high-quality investments in the current interest rate environment. Several of these buyers have flagged that towers offer the most attractive combination of business quality and secular growth, with the latter due to the growing demand for mobile data. Mobile data traffic is expected

[1] *Reinvestments = Research & Development (R&D) + Capital Expenditures. Source: Bloomberg, Stenham Asset Management.*

to grow close to 20% per annum over the next several years as new applications, such as mobile gaming and video streaming, consume significantly higher levels of data. For example, the average amount of mobile data used in video streaming is over 80,000x greater than simply sending an email. This combined with the rollout of new mobile networks such as 5G is driving greater demand for cell towers over time, benefitting the likes of Cellnex. Finally, Cellnex trades at an attractive valuation multiple of ~13.0x EBITDA which compares to multiples of over 20.0x for assets they are selling, which are of comparatively lower quality to their core business. Applying a fair multiple on a conservative basis of 18.0-20.0x EBITDA would result in an internal rate of return (IRR) of over 20% on a 3-year basis, among the highest in our portfolio today. Overall, we remain convinced in the long-term thesis for Cellnex and we have been using the weakness in the share price over the quarter to add to our position.

Outlook

In the first quarter, equity markets were supported by the resiliency of the global economy, resulting in higher conviction for a soft landing or even a "no-landing" scenario. That said, inflation has remained more sticky than expected, resulting in a material decline in expectations for interest rate cuts. At the time of writing, the market is pricing in just two US rate cuts in 2024, down from a peak of six cuts earlier in the year. Despite this, central bankers have remained relatively unchanged in their view that rate cuts will indeed take place this year. The return of the Fed put, combined with the resilient macroeconomic backdrop, should remain supportive for equities on a forward-looking basis. That said, valuations have also expanded leading us to taking profits in outperformers, most notably in the technology sector, and rotating towards holdings that have been relative laggards.



As always, we appreciate your continued support and investment. Should you have any questions, please do not hesitate to reach out.

Kind regards,

Kevin Arenson, Chief Investment Officer & Co-Portfolio Manager
Giulio Battaglia, Chief Executive Officer
Mihir Kara, Co-Portfolio Manager
Thibault Decré, Equity Analyst

[1] *Data as of 29 Mar 2024. Source: Stenham Asset Management.*

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