Q3 2024 Investor Letter

Stenham Equity UCITS Fund

Performance Review

Fund vs. Benchmark[1]	Q3 2024	YTD 2024	Since Inception
Stenham Equity Fund (A1)	**+3.7%**	**+14.0%**	**+223.1%**
MSCI World Index	+6.0%	+17.5%	+189.9%
Relative	(2.3%)	(3.5%)	+33.2%

Portfolio Attribution

Top Contributors – Q3 2024	Portfolio Weight	Attribution
Cellnex	5.5%	+1.1%
Adyen	3.7%	+1.1%
Thermo Fisher Scientific	7.1%	+0.9%

Top Detractors – Q3 2024	Portfolio Weight	Attribution
ASML	4.5%	(0.9%)
Universal Music Group	4.5%	(0.6%)
Alphabet	3.4%	(0.4%)

Market Commentary

The old adage of 'sell in May and go away' is often used to explain the seasonally weaker market performance during the summer period. The theory comes from when trading was conducted in person on stock exchange floors. Investors would depart for their vacations meaning minimal trading activity, low liquidity and subsequently lacklustre returns - a period often referred to as the summer lull. Yet, this summer we saw US President Joe Biden dropping out of the 2024 election, an assassination attempt on former US President Donald Trump and markets pricing in large fluctuations in election polling with the emergence of Kamala Harris as the Democratic candidate. And that was only July. From there, we saw the Japanese equity market registering its largest single day decline since Black Monday in 1987, the Federal Reserve's first rate cut in over

[1] *Performance as of 30 Sep 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.*

four years and a 25% rally in Chinese equities in less than two weeks in response to government stimulus measures.

One would be forgiven for thinking equity markets would be treading water given the sizeable uncertainty brought on by these events, yet the MSCI World returned 6.0% in Q3 2024. We are once again reminded that trying to predict the short-term direction for markets remains a near impossible exercise. With the upcoming US election, rising geopolitical tensions and the unclear path ahead for monetary policy, we have no doubt there will be more debate for markets near term. However, *time in* the market is more important than *timing* the market in our view and, particularly over the long run, markets have an uncanny ability to climb the wall of worry. We remain aware of these issues in the context of our portfolio but our emphasis remains on the long-term fundamental value of the businesses we own and the predictability of these businesses to navigate various macroeconomic environments.

Portfolio Commentary

Adyen

Adyen rallied close to 12% following the publication of their H1 2024 results, which reflected the continued acceleration in growth of the business. We have been encouraged by Adyen's execution since the publication of their H1 2023 results last year, where investors lost confidence in the outlook for the company amid escalating competitive pressures, primarily from US payments peer PayPal. This has been reflected in the share price recovery we have seen with Adyen outperforming peers in the payments space by almost 2x since then. The management team's commitment to not cut pricing in order to regain market share, but instead focus on delivering a superior value proposition to customers, has been evidenced through a string of large customer wins including luxury retailer Prada, digital wallet business Cash App, US grocery service Instacart, and many others. Moreover, competitive pressures from PayPal have waned as their new management has changed the strategic direction of the company, emphasising profitable growth rather than growth at any cost. This has led to Adyen increasing their volumes at a growth rate over 2x that of PayPal's competing business more recently. The outlook for Adyen remains positive, as the company's significant workforce expansion over 2022 and 2023 is expected to drive continued market share gains and growth re-acceleration from 2025 onwards. In addition, as the company's hiring cycle concludes, we should see material margin improvement take shape, helping the company deliver a 24% growth CAGR in EBITDA and 23% growth CAGR in free cash flow per share over the next few years. The market is currently ascribing a multiple of ~1x the company's forward growth rate, or ~25x EBITDA, which we view as attractive given the scarcity of businesses with similar fundamental quality. Adyen is one of only twenty developed market companies in our total investable universe expected to grow revenues above a 20% CAGR over the next 3 years while exceeding 50% EBITDA margins.

Semiconductors (ASML, Applied Materials)

The market enthusiasm around Artificial Intelligence (AI) and the implications for the semiconductor space took a respite during the quarter, with semis being among the worst performing industries over the period. With valuations for the semiconductor index reaching a 10-year peak on a relative basis versus the broader market, investor positioning had clearly become extended. We had been reducing the fund's exposure to our semiconductor holdings, namely ASML and Applied Materials earlier in the year, on the basis of valuation.

However, the outsized underperformance of these names meant that they were still a detractor to overall fund performance. In our view, the long-term fundamental outlook for the semiconductor capital equipment industry remains positive. Firstly, the demand for the overall semiconductor industry continues to be supported by several secular growth trends for emerging applications, such as AI data centres, electrification, autonomous vehicles and others. Secondly, the growing complexity of producing the most advanced chips used in these applications increases the spending towards equipment manufactured by the likes of ASML and Applied Materials, meaning that they should outgrow the broader semiconductor industry. And finally, the semiconductor industry has become one of the focal points in global geopolitics. While this carries near-term risks, the long-term implications are positive as the duplication of semiconductor supply chains results in higher equipment spending with countries around the world seeking to establish domestic semiconductor manufacturing facilities.

Luxury (LVMH, Christian Dior, Hermès)

Luxury underperformed this quarter, driven by rising concerns over China's economic outlook and given its position as the largest luxury consumer by nationality. The sector is undergoing a period of normalisation, transitioning from the post-pandemic euphoria back to its structural growth rate, compounded by a challenging macro environment. In this context, the polarization between high-desirability and lower-desirability brands has intensified. More recently, China’s stimulus measures have provided some relief to the sector, as investors viewed these initiatives as a sign of Chinese policymakers' commitment to addressing the country’s significant economic challenges. Stabilising China’s real estate and stock markets are seen as crucial steps toward restoring consumer confidence and, ultimately, boosting luxury spending. Despite China’s weak economic backdrop, we remain positive about the luxury sector’s long-term growth prospects. Over the past decade, one of the most profound structural changes we have seen in luxury has been the rise of social media, where average usage has increased >40% to nearly 2.5 hours per day[1]. As a result, we believe consumers are increasingly driven to showcase luxury as a means of projecting their idealised self image and asserting their status, whether in China or elsewhere. Moreover, China's high savings rates and relatively low luxury market penetration point to significant untapped potential. Given these supportive factors, we see the sector’s long-term outlook as strong and have capitalised on this opportunity by strategically adding to our luxury holdings at favourable valuations while enhancing the resiliency and predictability of our exposure, notably by initiating a new position in Hermès which we discuss in greater detail.

Portfolio Company Overview

Founded in 1837 by Thierry Hermès, the business began as a harness and saddle workshop in Paris, catering to the city’s elite, coinciding with the modernisation of Paris’ avenues where nobles flaunted their wealth on carriages. As automobiles replaced horses, the company’s focus shifted to leather bags and accessories. The 20th century saw the introduction of Hermès’ most iconic products, including the Birkin bag, named after Jane Birkin, and the Kelly bag, named after Grace Kelly. Despite the challenges of potential takeovers, Hermès remained a family-owned business, with the 6th generation maintaining the leadership of the company to this day, ensuring its legacy of craftsmanship continues.

[1] GWI, *DataReportal.*

Hermès' Uniqueness: Impossible to Replicate

The essence of luxury lies in both desirability and exclusivity, yet this creates a paradox: the more desirable a brand becomes, the more it sells but the more it sells, the less exclusive it becomes. We believe the uniqueness of Hermès lies in its unparalleled ability to address this dilemma by carefully managing the tension between demand creation and supply restriction. This fine balance sets Hermès apart from its luxury peers, allowing it to maintain both desirability and exclusivity better than any other luxury brand.

Desirability is embodied in the economics of its iconic handbags, the Birkin and Kelly. On the secondary market, a used Birkin or Kelly typically sells for 1.5 times its retail price, while a brand-new one can fetch up to 2 times its original cost. The vast majority of the most expensive handbags ever sold at auction are Hermès bags, often commanding several hundred thousand dollars.

Exclusivity is not merely a function of price – it extends into the purchasing experience. Even customers who can afford a Birkin or Kelly are not guaranteed the opportunity to buy one. Access to these iconic items requires a commitment to the brand which goes beyond wealth alone. The process involves becoming a loyal Hermès customer by building a purchase history across various product categories. Only after this step, can the customer join an informal waiting list, which can span over a year before they are offered the chance to purchase their first Birkin or Kelly.

This unique approach to desirability and exclusivity is evident in Hermès' unconventional marketing practices. Unlike its competitors, most of which spend over 10% of their revenue on advertising, Hermès allocates less than 5%, focusing instead on maintaining a structural undersupply of its most desirable products. The company's real marketing investment lies in the opportunity cost of deliberately limiting production. For instance, in the early 2010s, Hermès once halted the production and destroyed the inventory of a bag that had become too popular in Japan, reflecting this commitment to scarcity.

This undersupply of products is also a function of the company's production process, which is nearly impossible to replicate at scale. With more than 5,000 France-based saddle leather workers, each undergoes two years of training before starting in a workshop and typically an additional three years before they are allowed to work on Birkin or Kelly handbags. This extensive training cultivates a level of craftsmanship that is rare and highly specialised. Each Birkin or Kelly takes about 30 hours to make, with a single artisan typically dedicating two weeks to its production.

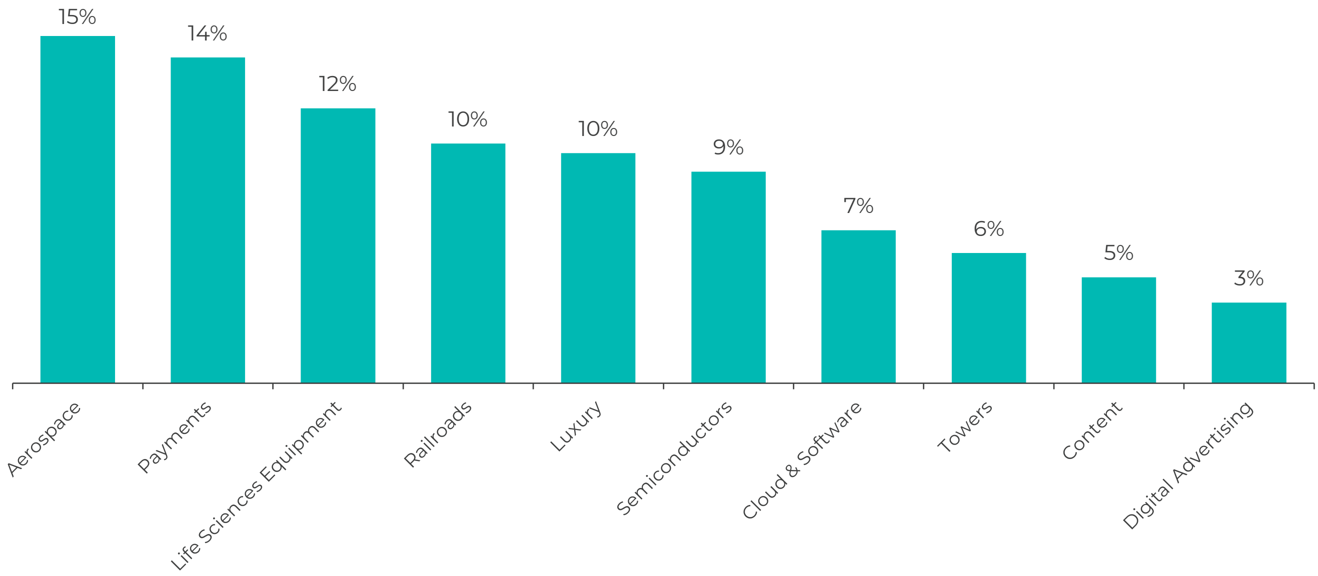
Capitalising on the Opportunity

We believe the recent de-rating in the luxury sector has created an opportune moment to invest in Hermès, initiating our position following significant multiple compression and approaching a multi-year low in relative valuation. In our view, Hermès' elevated multiple is a reflection of its untapped earnings potential, particularly when factoring in the structural undersupply of Birkin and Kelly bags. Factoring this in, we estimate that Hermès' multiple could be nearly half of its current level, aligning more closely with that of its luxury peers. We believe Hermès consistently holds close to a year of demand visibility for its iconic handbags, along with considerable latent pricing power. This demand buffer, coupled with its elite customer base, reinforces the brand's structural resilience and predictability. Given these factors, we think Hermès offers a compelling opportunity to enhance our luxury exposure and believe the company's unmatched ability to combine desirability with exclusivity ensures it will continue to be the pinnacle of luxury for generations to come.

Business Update

Earlier this year, we decided that adding an analyst to the team would benefit both our research process and the long-term performance of the Fund as we explore new industries and look to uncover more extraordinary businesses. After an extensive hiring process, we are delighted to introduce the newest addition to the team, Gabriel Moraes, who joined us in October. Originally from Rio de Janeiro, Brazil, Gabriel brings experience from his prior role as an equity research associate at Diamond Hill Capital Management in the US. We look forward to updating you in the future with new investment ideas as Gabriel builds his research coverage with us.

Portfolio Themes[1]



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, Senior Equity Analyst
Gabriel Moraes, Equity Analyst

[1] *Data as of 30 Sep 2024. Source: Stenham Asset Management.*

DISCLAIMER

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