Trojan Global Equity Fund Newsletter

The investment objective of the Trojan Global Equity Fund (the "Fund") is to achieve capital growth over the long term (at least 5 years). Our strategy seeks to exploit a persistent market inefficiency that misprices rare businesses that can grow at sustainably high returns on their capital. We invest for the long term in companies that have the resilience to withstand unexpected shocks and the adaptability to thrive in a dynamic global economy.

Press Pause

The past few years have felt a bit like watching a movie in fast forward. Global pandemic was followed by war in Ukraine, a rapid increase in inflation, and the most aggressive upward move in interest rates since the Second World War. The tightening of credit conditions is beginning to expose the fragility of a system accustomed to very low interest rates. Once venerable, Credit Suisse was 166 years old when it collapsed. Momentous events have been squashed into a few short years.

There is much to worry about in the world today.[1] Tried, tested and important economic signals are pointing clearly to a recession in the United States. Firstly, there is the steep 'inversion' in the Treasury yield curve – i.e. short term rates on US government bonds are higher than those available on equivalent longer-dated bonds. This distorts the so-called carry trade that earns a return on capital by borrowing short to lend long. Silicon Valley Bank's demise in part stems from capitalism's natural order of things being turned on its head. The damage is likely to spread further. There have been eight yield curve inversions since I was born in 1968 and every single one has presaged a recession.[2]

Secondly, a key measure of money supply in the United States has been running negative since the Autumn of 2022.[3] The various interventions throughout the pandemic resulted in an extraordinary expansion of the money supply. It should not therefore have been too much of a surprise that, after a bit of a lag, there followed a period of significant inflation. Now the money supply is contracting markedly, a spell of lower inflation, and possibly a recession, is increasingly likely. Sebastian and our colleagues in Troy's Multi-Asset team have written several times on this subject and suffice to say we see macro-economic trouble ahead.[4]

Magic Numbers

So, how does this rather troubling view of the world fit with our fully invested Trojan Global Equity strategy today? Firstly, some context: these seismic global events can be absorbing and terrifying, but ultimately distracting from the day job of studying, analysing and investing in companies for the long term. We must regularly remind ourselves that over the short term the

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[1] Although I don't recall a time when there wasn't a lot to worry about! Even for a worrier like me, there is a lot going on.

[2] https://www.newyorkfed.org/research/capital_markets/ycfaq#/interactive

[3] The 'M2' measure of money supply, which includes cash, bank deposits and other forms of money that are readily convertible to cash.

[4] See Investment Report No. 76

stock market is irrational, unpredictable, and overly emotional but over the long term it reflects the value that companies create. Since its inception in 1927, the S&P 500 Index in the United States has delivered an average annual return of just under +10%. Not bad! And that's despite all the horrors suffered by humanity over a little less than a century. In fact, over 20, 30, 50-year periods the annualised nominal returns have all been around the magic +10% level. What about inflation? The average inflation rate in the United States over the past 50 years has been close to +4% a year (similar to the average inflation rate in the UK). Inflation-adjusted returns for the stock market have been around +6.5% over the very long-term. [5]

We aim to do better than this. The Troy Global Equity Strategy has delivered an annualised return, since its inception almost 10 years ago, of +11.5% (*Appendix II*). After what has been a volatile 18 months, the Fund is just shy of 10% off its all-time high reached in December 2021, having recovered well from the recent lows in June 2022.

In the first quarter of 2023, the Fund is +7.2%, ahead of the benchmark MSCI World index return of +4.8%. We are clearly not out of the economic woods yet, but we believe that if our stock selection is sound and we don't pay too much for our great companies, strong investment returns will follow. Patience is required.

Resilience

A critical element of our long-term investment approach is to select companies that we think are resilient and adaptable to the economic, social and technological change we are witnessing. These companies shine in adversity and are deliberately not selected based on any macro-economic forecast. Instead, they have the capacity to survive and thrive in a variety of economic environments.

Inflation and higher costs of borrowing are squeezing incomes and corporate profits. It is more important than ever to invest in companies that have predictable revenues and exercise control over the major inputs for profitability.

The Fund's holdings provide essential and differentiated products and services for their customers, allowing them to charge premium prices. Collectively they require little capital to grow, such that they generate phenomenal amounts of surplus cash and maintain solid balance sheets. All these features combine to make them resilient.

Adaptability

At the same time, we recognise that the world is complex and dynamic. Companies need to be adaptive. Alongside a very challenging macro-economic backdrop, we are experiencing an era of extraordinary technological change – highlighted most recently by all the excitement surrounding Open AI's ChatGPT and the commercialisation of Artificial Intelligence. Although many are quick to compare the launch of ChatGPT to the first release of the iPhone in 2007, it is still too early to say how this type of technology will impact consumers and companies. It is, however, an important reminder that companies must be responsive to technological change if they are to survive and prosper far into the future.

This is true for all the companies in the portfolio, not just the likes of Microsoft and Alphabet, which are in the vanguard of change. When we

[5] all returns quoted in local currency terms.

think about the adaptability of the Fund's investments, we are encouraged to note that the average company chooses to consistently reinvest significant sums back into both R&D and capital expenditure to grow their products, services and infrastructure. They have higher than average revenue growth rates underpinned by diversified revenue streams, doing business around the world and across multiple product lines. They have plenty of room for expansion. Less tangibly, they are run by management teams that are alert to competitive threats and think creatively about how to grow their companies. We aim to own businesses that are genuinely run for the long-term to maximise the duration of growth and returns.

But what about the valuation?

There is no doubt that years of cheap money elevated the valuation of most asset classes. Notwithstanding the upsets of last year, global equities are no exception. Rule 101 of financial economics is that a rising risk-free rate mathematically compresses the value of future cashflows. With interest rates where they are, sensitivity to valuation is heightened in today's environment. Our approach to valuation is to review it from all angles, focus on cashflow, and ask the simple questions of 'what are we paying, and what are we getting in return?'.

On a free cash flow yield basis, the Fund trades on a small discount to the wider market, despite its significantly superior financial productivity and growth characteristics (see *Appendix I*). In addition, when we compare the Fund to its own history (*Figure 1*), it is more financially productive than before, with higher free cashflow margins and higher returns on invested capital. Reinvestment and growth rates are also higher, shown by reinvestment in R&D and sales growth, and the balance sheets of our companies are as robust as ever.

Figure 1	**Av. Since Inception**	**2023 YTD**
RESILIENCE		
FCF Margin (%)	22.5	23.7
Net Debt/ EBITDA (x)	0.8	0.8
ROIC (%)	17.5	20.3
FCF Yield (%)	4.7	4.5
ADAPTABILITY		
R&D/Sales	11.5	14.4
Capex/Sales	7.8	10.1
Sales Growth (3Y fwd Est)	7.9	8.5

Source: FactSet, 31 December 2013 to 31 March 2023. FCF based on trailing figures over the last 12 months.

In an uncertain economic environment, where corporate earnings are likely to be under pressure, we are reassured that the Fund is invested in an exceptional collection of companies, with superior financial productivity and growth prospects, for which we are not having to pay a material premium.

Patience is a virtue

The harsh reality is that, even with a global opportunity set, there just aren't that many truly fabulous businesses that can be owned at a fair valuation. When we find them, we tend to hold on to them. I have spent the past year or so revisiting the writings of Warren Buffett and Charlie Munger, and however well-thumbed they may be, I can't recommend them highly enough to anyone who is interested in investing in the stock market. One of Warren Buffett's famous quotes is that 'if you aren't thinking about owning a stock for 10 years, don't even think about owning it for 10 minutes'. George and I, and the team at Troy, embrace this long-term thinking, recognising that the market consistently underestimates the compounding power of exceptional businesses, particularly at times of stress.

The average company owned in the Fund has been held for over 10 years and portfolio turnover is low. But low turnover does not mean no turnover. There are always improvements to be made and the volatility of the past 18 months has presented some attractive opportunities to make changes. We have added a few new investments (London Stock Exchange Group, for example) and others have departed. In addition, we have increased some longstanding investments as their share prices have languished (e.g. Heineken), and right-sized others after they have significantly outperformed over the longer term (e.g. Microsoft). Overall, we are pleased with the balance and diversity these changes bring whilst maintaining a patient and far-sighted perspective.

No drift

The uncertain outlook calls for businesses that are both resilient to a variety of macro-economic conditions, and adaptable to the many changes we observe. The portfolio is deliberately concentrated in exceptional companies that can be held with confidence for a decade or more, but despite their obvious quality, we view their average valuation is better than fair with the free cashflow yield trading at a discount to the wider market. We are very fortunate to be managing money at Troy, which is a relative haven of stability and common sense in a world of 'hot takes' and rapid change. This allows us to stick to our investment strategy in difficult markets. We are clear in our purpose to achieve long-term capital growth and the Fund's strategy has not changed. The last year-and-a-half have reinforced our belief that markets persistently underestimate the compounding power of rare businesses that can grow at high rates of return on their invested capital.

As ever, we thank you for your interest in the Fund.

Gabrielle Boyle & George Viney
April 2023

APPENDIX I - RESILIENCE AND ADAPTABILITY

	Resilience				Adaptability		
	FCF Margin (%)	Net Debt/ EBITDA (x)	ROIC (%)	FCF Yield (%)	R&D / Sales (%)	Capex / Sales (%)	Est. Sales Growth (3y fwd, %)
Troy Global Equity Strategy	23.7	0.8	20.3	4.5	14.4	10.1	8.5
MSCI World Index NR	8.4	1.3	9.3	4.3	4.9	6.0	5.4

High returns · Low leverage · Reasonable valuation → **Greater resilience**

Higher reinvestment rate → **High revenue growth and adaptability**

Past performance is not a guide to future performance.

Source: FactSet and Troy Asset Management Limited, 31 March 2023. FCF measures are based on trailing figures over the last 12 months. Asset allocation subject to change. Estimates may not be achieved. Characteristics are shown excluding Financials. Asset allocation subject to change. Estimates may not be achieved. All references to benchmarks are for comparative purposes only. Holdings subject to change. The information presented shows the performance of a representative mandate, the assets of which are, and have been managed in accordance with Troy Asset Management Limited's Global Equity Strategy. Please refer to Troy's glossary of terms.

APPENDIX II – PERFORMANCE STATISTICS

Calendar returns	Trojan Global Equity Strategy	MSCI World Index NR	IA Global TR
2014	+15.0%	+11.5%	+7.5%
2015	+12.3%	+4.9%	+4.1%
2016	+19.2%	+28.2%	+24.4%
2017	+13.2%	+11.8%	+13.8%
2018	+1.1%	-3.0%	-5.6%
2019	+24.6%	+22.7%	+22.1%
2020	+13.5%	+12.3%	+14.8%
2021	+21.7%	+22.9%	+18.0%
2022	-15.7%	-7.8%	-11.1%
2023 YTD	+7.2%	+4.8%	+4.1%

Track record (annualised)	Trojan Global Equity Strategy	MSCI World Index NR	IA Global TR
1 year	-3.4%	-1.0%	-2.8%
3 years	+10.9%	+16.5%	+14.1%
5 years	+10.9%	+10.8%	+8.7%
Since Strategy Inception	+11.5%	+11.2%	+9.4%

Past performance is not a guide to future performance.

Source: Lipper – O Accumulation shares total return net of fees since inception (31 December 2013) to 31 March 2023. All references to benchmarks are for comparative purposes only. The information presented shows the performance of a representative mandate, the assets of which are, and have been managed in accordance with Troy Asset Management Limited's Global Equity Strategy. The fund is a constituent of the IA Global Sector.

TROY
ASSET MANAGEMENT

PORTFOLIO SUMMARY

No. of Holdings	27
Total Equity Exposure	96%
Top 10 Holdings	53%

SECTOR BREAKDOWN

Information Technology	32%
Health Care	19%
Consumer Staples	14%
Communication Services	13%
Financials	9%
Consumer Discretionary	6%
Industrials	3%
Cash	4%

COUNTRY BREAKDOWN

United States	63%
Switzerland	13%
United Kingdom	10%
France	5%
Netherlands	6%
Cash	4%

AUM

Strategy	£566m
Fund	£415m

TOP 10 HOLDINGS

Alphabet	7.2%
Visa	6.5%
Microsoft	6.2%
Heineken	5.9%
Roche Holding	5.7%
Mastercard	5.3%
Fiserv	4.6%
Meta Platforms	4.0%
Booking	3.7%
Novartis	3.7%
Total Top 10	52.8%
17 other holdings	43.7%
Cash	3.5%

LIQUIDITY

1 Day	92%
5 Days	97%
30 Days	100%

Past performance is not a guide to future performance.

Source: Factset and Troy Asset Management Limited, 31 March 2023. Asset Allocation and holdings subject to change.
#Liquidity is monitored by calculating what proportion of the equity portfolio can be sold, assuming trading at 20% of the previous 90 days' average daily volume.

Disclaimer

The Fund was originally launched as the Trojan Capital Fund, which focused on investing in UK equities with the flexibility to invest in overseas equities and other asset classes. The strategy was changed to a global equity strategy in December 2013. The Fund has been a constituent of the IA Global sector since April 2012. Prior to this, the Fund was in the IA Flexible Investment sector.

Please refer to Troy's Glossary of investment terms here. All information in this document is correct as at 31 March 2023, unless stated otherwise. The document has been provided for information purposes only. Neither the views nor the information contained within this document constitute investment advice or an offer to invest or to provide discretionary investment management services and should not be used as the basis of any investment decision. The document does not have regard to the investment objectives, financial situation or particular needs of any particular person. Although Troy Asset Management Limited considers the information included in this document to be reliable, no warranty is given as to its accuracy or completeness. The views expressed reflect the views of Troy Asset Management Limited at the date of this document; however, the views are not guarantees, should not be relied upon and may be subject to change without notice. No warranty is given as to the accuracy or completeness of the information included or provided by a third party in this document. Third party data may belong to a third party.

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