



# 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.*

## Ten years, ten lessons

Gabrielle passed a decade with Troy last November. George will reach the same milestone in June this year. We count ourselves extremely fortunate to do a job we love in an environment ideally suited to our personalities and investment style. You might think that after all this time we have settled on a stable set of habits and ideas. Not quite. The sort of long-term investing that we practise never feels settled or comfortable. It constantly tests our patience and curiosity because the world around us is always changing, forcing us to evolve with it. The investment industry is brutally competitive and to beat the odds and outperform we must constantly upgrade our methods and thinking. Complacency is the biggest risk.

When we look back over the last ten years, our basic investment principles that we hold dear have remained the same. We still think that in order to win over the long term, you must first avoid the losers. Good businesses stand a better chance of delivering satisfactory investment returns than mediocre companies. We continue to believe that the market is inefficient by undervaluing special companies that can grow cash flows, without recourse to

debt, and sustain high returns on capital over many years. There are times when these brilliant businesses can be bought cheaply. Focussing our efforts on these companies and holding for the very long term is the way to go.

But the details of what looks good to us, our preferred financial metrics, and our assessment of value are now notably different. In this Newsletter, we identify the top ten lessons learned over the decade and reflect on how our approach has adapted. We also address the two major issues of the day - inflation and the war in Ukraine – and what they might mean for the Fund.

## Lesson One: From good to great

We have long understood that companies are not created equal and that a select few have the ability to grow consistently at high rates of return. And yet even within this rare sub-set there are important economic differences. The cumulative effect of these are amplified with the passage of time. Simply put, the best quality companies will rise to the top. This is reflected in the Fund's own biggest holdings, which have tended to have made the largest positive contributions to the Fund's historic performance. It is no coincidence that they are among the portfolio's most financially productive. Troy's ownership of Microsoft since 2010 has been instructive because it sets an extremely high bar for all other individual investments. A sharper focus on the truly exceptional has led us to raise our thresholds for quality, passing on a number of potential investments and weeding out companies that have proved to be merely above average. The result is a steadily improving financial profile, measured in higher earnings growth, achieved with less leverage and more cash generation.



In our view, the Fund is demonstrably higher quality than it was ten years ago and we intend to continue to improve it.

## Lesson Two: Concentrated diversification

A deeper understanding of the profound quality of certain companies has made us more willing to own them in greater concentration. The portfolio's number of holdings has dropped below 30 and the capital invested in its top 10 has increased from ~43% five years ago, to ~57% at the end of February. This level of concentration carries risk, of course, in the event that something befalls one of the Fund's big holdings. This is mitigated by a strengthened preference for companies with extraordinary breadth. Visa, for instance, not only operates in more than 200 countries, it also transacts payments for all retail sectors, domestically and across international borders, for both consumers and corporates, online and offline, via debit, credit and pre-paid. This ubiquity is part of its competitive strength and creates a remarkably resilient base of revenues that can withstand setbacks in any one area. In addition, it provides a very broad set of opportunities that allow Visa to adapt and grow year after year. Such diversity permits high conviction in single stocks.

## Lesson Three: Run your winners

One of the great beauties of long-term ownership is that equity owners of special companies can reap the unpredictable rewards of human ingenuity. The very best businesses have an almost magical capacity for serving up positive surprises that we, despite deep research, cannot foresee. Intuit, for instance, has developed an expansive and imaginative innovation programme, complemented by a more ambitious approach to M&A. The company has plugged live online advisory services into its cloud-native software, allowing it to address a large cohort of customers that want expert help with their accounting and

taxes. The recent acquisition of Credit Karma and Mailchimp take Intuit deeper into personal finance and small business marketing services, reinforcing the company's core strengths and vastly expanding its opportunity for many years of valuable growth. None of these opportunities were predicted when we first invested in the company back in 2013.

## Lesson Four: The importance of management

The longer we do this, the more we appreciate the precious difference management can make to investment outcomes. Their contribution cannot be accurately measured by disentangling cause and effect. It can, however, be observed in the divergent progress of companies with ostensibly the same opportunities. We compare our experience with Intuit with that of Sage, a company first owned at Troy from 2006 until it was sold in July 2019. Both Intuit and Sage sell accounting software to small businesses, but Intuit invested early and aggressively in the cloud whilst Sage did not. To the end of February 2022, Intuit's shares have increased (in GBP) +745% (+28% CAGR) since we first became an investor in July 2013. Sage's are up +97% (+8% CAGR) over the same period and remain below the level at which we exited.

A thorough understanding of governance, competitive strategy and capital allocation have always been essential elements of our research. Over the years we have come to prize particular aspects of management significantly higher than before – long-termism and a firm sense of ownership; an entrepreneurial willingness to invest and adapt; and a candour when speaking with investors and other stakeholders. Conversely, we have even less time for hired hands that pander to the gallery whilst optimising for the short term.



## Lesson Five: Shared value

Ten years ago, our focus was mostly on the G in ESG. Environmental and social controversies came up when we assessed risks. This informed, for instance, a long-standing avoidance of various problematic sectors such as defence, gambling or bulk chemicals. It also led us to companies domiciled in regions of the world that routinely meet our exacting governance standards. Today, we see greater potential for companies that go beyond only delivering for shareholders. It is correct to regard 'stakeholder capitalism' with a degree of scepticism. Yet it is also our firm conviction that amidst all the greenwashing there are companies that are better placed to compete and grow because they have invested in all their relationships – with customers, staff and society at large. It is simply good business to do so, making them more resilient and adaptable.

What does this mean in practice? It means we no longer celebrate the exercise of pricing power unless it is justified by external forces (such as inflationary pressure) or enhancements to products or services. We pay closer attention to staff retention and corporate culture. Cost-cutting and restructuring are less likely to be seen as an opportunity and more likely as a sign of strain and capital misallocation. Failure to live up to rising expectations – among shareholders, environmental groups or regulators – is a potential red flag.

## Lesson Six: Technological change

The impact of management's decisions are magnified because we live in an age of disruptive technological change. It is hard to overstate the significance of this. The internet has facilitated the capital efficient growth of businesses on a previously unimaginable global scale. We were initially slow to recognise how we could fully participate in the

vast value creation this has unleashed – doubtful about the longevity of the businesses it had created, and unsure as to how to value them conservatively. Our investment in Google (now Alphabet) since 2013 has taught us an invaluable lesson about the growth and durability supporting the best of these global behemoths. The company spans e-commerce, video streaming and cloud computing, to say nothing of more nascent bets on driverless cars and medical technology. These all tap immature opportunities and yet Alphabet generated over \$250bn in revenues in 2021. The staggering scale and power of companies such as Alphabet also creates enormous opportunity costs for the ownership of inferior businesses, particularly those operating across traditional retail, media and computing that are rendered increasingly obsolete.

## Lesson Seven: Valuation

The first six lessons give the context for how our thinking about valuation has evolved. We are still firmly 'value investors' in so far as we are trying to buy something for less than it is worth. The challenge is to understand what something is worth in the first place. That is perhaps the hardest part of what we do, certainly with any precision. Even we, self-appointed experts in higher quality businesses, failed to fully grasp the rare quality of an Alphabet, a Visa or a Moody's. We were too cheap, too cute, too nervous of what might happen in the short term. We have learned to no longer expect valuation to be a source of return – it is much more a risk to be managed. We now have a stronger conviction in the opportunity available from paying fair prices for exceptional companies. Their resilient and growing cash flows, compounded over many years, will be the ultimate arbiter of returns.

## Lesson Eight: Optimism

The world is a scary place and it has become scarier still in the last two years. Working at



Troy, in close collaboration with our colleagues managing multi-asset portfolios, we are well aware of the risks that we run. Valuation is one of them. We'll go on to address inflation and Ukraine in the next section of this Newsletter. We also recognise that a focussed portfolio of great companies, resilient, growing and reasonably valued, provides solid grounds for optimism. And as the portfolio has increased in quality, we have learned to become more optimistic. That's a hopeful light to hold when there is darkness all around.

### Lesson Nine: Be open minded

There are sound commercial and psychological reasons to narrowly define an investment process. There were times when a company such as Alphabet would not have been seen by ourselves or our investors as 'a Troy stock'. We are fortunate that Troy has always been an outward-looking organisation. Sebastian Lyon, our founder, had the good sense to recognise there are lots of ways to invest and plenty to learn from others. Investment markets are complex and adaptive. What worked historically may not continue to work in the future. So, whilst having a firm sense of who we are and where we want to go, we have to be humble and open-minded enough to continuously question our ideas and methods. This effort is greatly improved by the development of a team of diverse, thoughtful and talented colleagues. They challenge our thinking and we force each other to get better.

### Lesson Ten: Learn from your mistakes!

Great businesses at attractive prices may stack the odds in our favour, but bad things can and still do happen. We will misjudge and miscalculate. Unforeseen events will come our way. Mistakes are an inevitable part of investing because the future cannot be accurately predicted. When they do occur, we are hard-wired to react emotionally, no matter how much we try to overcome our biases.

Alongside our successes, in the last decade we have made errors of commission and omission. They are the inspiration behind this Newsletter. The important thing is to recognise when mistakes are made and to learn from them. Here, too, the investment team has a critical role to play. Our research and decision-making have evolved to surface potential problems and to deal with setbacks with discipline rather than emotion. The task is also cultural. If we are to improve we must be ready to be open about our mistakes, both with each other and with our investors.

### Inflation

Moving on from the lessons of last decade, what now of the present and of the future? Our equity holdings have long been shaped with inflation in mind. Whilst deflationary forces ruled, this was like having insurance for a risk that never materialised. Now that inflation is at levels not seen for a generation we are glad for the inflation protection that our businesses provide. That's not to say that the portfolio is immune. Some companies, such as Unilever or Heineken, turning raw materials into finished goods, are more susceptible to inflationary forces than others. In general, however, the portfolio is well insulated. It consists of innovative companies that sell essential products and services. Experian's customers, for instance, have little choice but to continue to make their purchases even as prices rise. The cost of doing so absorbs a small component of customers' overall budgets, making them relatively insensitive to rising prices. At Moody's, for example, the expense of paying interest on a bond, even at these low prevailing rates, is many times higher than the fees paid to Moody's for their rating. Our companies make the pill of higher prices easier to swallow by continually adding value to what they sell. Microsoft integrates Teams for free as part of its Office suite, helping Microsoft justify higher prices for its productivity software. In some cases, customers won't even notice that



inflation is being passed on. A large portion of Visa's and Mastercard's revenues derive from *ad valorem* fees charged against the total value of transactions. Consider them a royalty on nominal growth.

In aggregate, the portfolio enjoys expected revenue growth that should outgrow cost inflation. The Fund's weighted average gross margins are over 60%, more than double those of the MSCI World Index. Its companies are also close to 3x more cash generative on the basis of comparative cash margins. This provides plenty of flexibility to manage cost inflation, even if it may sting in the near term.

The greatest unknown is how inflation may affect interest rates, bond yields and consequently equity valuations. Markets are clearly in a state of flux as investors figure out how to value equities against this novel backdrop. The portfolio has not escaped this dynamic. We can offer a simple comparison (see Appendix I). The trailing FCF yield for the Fund is 4%, approximately the same as the global stock market index (again, as measured by the MSCI World). Given the Fund's superior growth, capital efficiency and cash generation, which would you rather own?

## Ukraine

Inflation was already at generational highs before Russia's invasion of Ukraine. We are horrified by Russia's wanton and barbaric actions. The Fund is not invested in any Russian or Ukrainian companies, and none in Eastern Europe. On average, we estimate that the Fund derives under 2% of its companies' underlying revenues from Russia and Ukraine. Among the highest are Visa and Mastercard, which generate ~4% of their revenues from these two countries. They have joined many other corporates in withdrawing from Russia. One wonders if they will ever go back. They can afford not to. Such is the strength and

diversity of their growth profile that they can comfortably absorb the loss of revenues.

The indirect effects of the war are likely to be far more significant for the Fund than the direct ones. The Fund is invested in users and producers of data and software. Cyber risk is a growing and unpredictable concern. The Fund is not invested in big producers or consumers of oil and gas. Heineken is one of the more exposed to rising European energy prices because it has a large European business and it takes a lot of energy to make and distribute cans of beer. Its shares have not had a chance to recover from the effects of the pandemic. Now it must meet a dramatically inflating cost bill and perhaps a consumer less able to afford its premium beer brands. A difficult period likely awaits it. We take comfort from the fact that the company is built to endure. Founded in the 1860s and still family controlled, it has weathered many geopolitical and macro-economic crises. Heineken is more diversified than ever before, generating ~70% of its underlying profits outside of Europe. We are confident its shares will recover and believe they offer outstanding value at current prices.

## Conclusion

Whilst the Fund's recent returns are disappointing, the experience of Heineken, among others, highlights the value we see in the portfolio today. Across the companies in which the Fund is invested, the level of financial productivity is exceptional. The growing cash flows they generate can be expected to drive attractive returns over the long term. This is where our attention resides. The lessons of the last decade inform our attitude and behaviour, and we remain focussed on that which is within our control and understanding.

We continue to look for ways to improve the portfolio and we have used recent volatility to add to its strength in depth. This has included



the purchase of Adobe and additions to Mastercard, Meta, Moody's, PayPal and Visa. All are attractively priced for the rare qualities and growth that they possess. We have reduced investments in American Express, Becton Dickinson, Booking Holdings, Roche and Nestlé. These changes also better position the portfolio for technological change and rising ESG responsibilities. The quality of our companies – their resilience over the shorter term, their adaptability over the longer term – underpin our optimism.

We look forward to the next ten years, and thank our investors for their continued interest and support.

Gabrielle Boyle & George Viney  
March 2022



## Appendix I – Valuation and Returns

	FCF Margin (%)	Net Debt/ EBITDA (x)	ROIC (%)	FCF Yield (%)	R&D / Sales (%)	Capex / Sales (%)	Est. Sales Growth (3y fwd, %)
<b>Troy Global Equity Strategy</b>	28.6	0.5	19.1	4.0	12.0	9.4	13.7
<b>MSCI World Index NR</b>	9.8	1.3	8.3	4.2	3.4	5.9	6.6

Source: FactSet, 28 February 2022. 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 a UK UCITS, 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	Troy Global Equity Strategy	MSCI World Index NR	IA Global
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 YTD	-10.8%	-6.8%	-8.8%

Track record (annualised)	Troy Global Equity Strategy	MSCI World Index NR	IA Global
1 year	+9.9%	+15.4%	+7.1%
3 years	+12.9%	+14.1%	+12.1%
5 years	+10.6%	+10.4%	+9.2%
Since Strategy Inception	+13.0%	+12.2%	+10.5%

**Past performance is not a guide to future performance.**

Source: Lipper – O Accumulation shares total return net of fees since launch to 28 February 2022. All references to benchmarks are for comparative purposes only. The information presented shows a UK UCITS, the assets of which are, and have been managed in accordance with Troy Asset Management Limited's Global Equity Strategy. The UK UCITS is a constituent of the IA Global Sector.



### Portfolio Summary

No. of Holdings	28
Total Equity Exposure	99%
Top 10 Holdings	57%
Top 20 Holdings	86%

### Sector Breakdown

Information Technology	36%
Health Care	21%
Consumer Staples	16%
Communications Services	11%
Financials	9%
Consumer Discretionary	3%
Industrials	3%
Cash	1%

### Top 5 Contributors 1 Year to 28 Feb 2022

	Contribution to Return*	Total Return
Alphabet	+2.6%	+39%
Microsoft	+2.3%	+35%
American Express	+2.0%	+51%
Roche Holding	+1.0%	+23%
Intuit	+0.9%	+27%

### Bottom 5 Contributors 1 Year to 28 Feb 2022

	Contribution To Return*	Total Return
Medtronic	-0.0%	-5%
Adobe	-0.1%	+6%
Fiserv	-0.4%	-12%
Meta Platforms	-0.6%	-15%
PayPal	-2.8%	-55%

### AUM

	£m
Strategy	557
Fund	395

### Top 10 Holdings

Alphabet	9.0%
Microsoft	8.9%
Visa	7.5%
Mastercard	6.2%
Meta Platforms	5.2%
Intuit	4.2%
Alcon	4.0%
Medtronic	4.0%
Roche Holding	3.9%
American Express	3.8%

### Country Breakdown

North America	72%
Europe	18%
UK	9%
Cash	1%

### Liquidity<sup>#</sup>

1 Day	94.0%
5 Days	98.9%
30 Days	100.0%

**Past performance is not a guide to future performance.**

Source: Factset and Troy Asset Management Limited, 28 February 2022. Asset Allocation and holdings subject to change.

\*Stock contribution to return is provided as gross absolute returns and does not include the Fund's charges and fees. The reference to specific securities is not intended as a recommendation to purchase or sell any investment.

<sup>#</sup>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.





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