TYPICAL CONTINENTAL EUROPEAN MANDATE

Mid/large cap Continental European equities

Long only managed account fund

December 2022 **Newsletter**

TYPICAL CONTINENTAL EUROPEAN MANDATE

FUND STRATEGY

Our investment objective is to generate absolute or relative returns for investors, depending on the mandate, by investing in Continental European equities

Manager AUM $788m

FUND MANAGER

Stuart Mitchell

Stuart is the Managing Partner and CIO of S. W. Mitchell Capital.

Prior to founding the firm in 2005 Stuart was Head of Specialist Equities at JO Hambro Investment Management.

Stuart started his career at Morgan Granfell where he subsequently took on the role of Head of European Equities

PERFORMANCE (EUR %)

	Fund	Index
Q4 2022	13.12	10.33
YTD	(10.72)	(11.86)
SI	326.09	225.47
2021	26.86	25.36
2020	7.60	2.43
2019	37.75	28.22
2018	(20.44)	(10.10)
2017	14.45	12.27
2016	3.28	3.31
2015	10.77	11.48
2014	4.38	7.23
2013	26.79	23.17
2012	24.62	20.66
2011	(18.31)	(11.63)
2010	28.35	9.56
2009	28.22	29.77
2008	(38.86)	(42.20)
2007	(10.34)	5.94
2006	27.96	22.00
2005	27.28	28.30
2004	10.36	13.60
2003	16.98	19.49
2002	(10.18)	(32.01)
2001	6.17	9.18

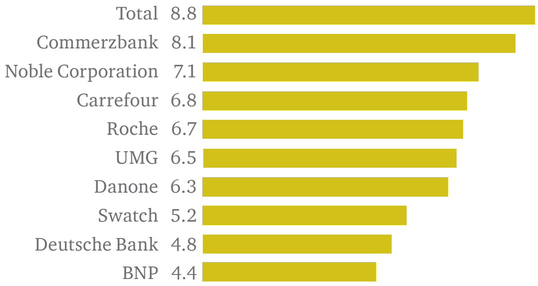
Top Five Contributors

Company	%
Total	1.9
Commerzbank	1.5
Deutsche Bank	1.5
Noble	1.3
UMG	1.0

Bottom Five Contributors

Company	%
Roche	(0.9)
Maersk Drilling	0.1
Danone	0.1
Kering	0.1
Volkswagen	0.2

Top Ten Holdings



Portfolio construction

Number of positions	Top 10 positions as a % of NAV	Gross invested position as a % of NAV	Cash position
21	64.8	99.9	0.1

Country exposure

Country	%
France	41.1
Germany	25.1
Switzerland	12.0
United Kingdom	7.1
Netherlands	6.5
Italy	4.3
Norway	2.3
Denmark	1.6

Sector exposure

Sector	%
Financials	21.6
Energy	16.0
Consumer Staples	13.0
Health Care	11.1
Information Technology	10.9
Consumer Discretionary	10.6
Industrials	7.3
Communication Services	6.5
Materials	2.9

Market capitalisation

Market cap	%
0-€0.4	3.9
€0.4-0.75	—
€0.75-1.5	—
€1.5-7.5	13.5
€7.5-15	20.1
€15-50	29.9
€50+	32.6

Risk characteristics

Risk analysis	Fund
Annualised alpha %	1.72
Information ratio	0.17
Beta	0.96
Up-market capture ratio %	122.19
Down-market capture ratio %	99.87
Annualised volatility %	17.25
Active share %	87.52
Tracking error %	7.74

1. Source: SWMC, FactSet 31/12/22.
2. All performance shown is gross of fees.
3. Index: MSCI Europe ex UK.
4. The Index is displayed purely for comparative purposes of the investable universe. As a reminder, our portfolios are built in a completely unconstrained and benchmark-agnostic manner.
5. Performance shown is for five chain linked typical Continental European Mandates; the first from inception until December 2015,the second from January 2016 to January 2019, the third from February 2019 to April 2020; the fourth May 2020 to June 2020 and the fifth from July 2020.
6. Past performance should not be seen as an indication of future performance.
7. Figures are subject to rounding.
8. Please note that all risk metrics, other than active share, are from inception.
9. Changes in rate of exchange may cause the value of investments to fluctuate.

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COMMENTARY

European markets rose by 10% over the fourth quarter buoyed by a growing belief that inflation is peaking, or may perhaps already have peaked.

We significantly outperformed over the quarter, and 2022 as a whole. The following among our shares performed best in the quarter:

Deutsche Bank	+39%
Total	+24%
Essilor	+21%
Commerzbank	+20%
UMG	+18%

Yet again, our holdings in the German banking sector have been amongst our best performers. We nevertheless still encounter scepticism when presenting these investments. It was of course the case that the sector was severely impacted during the period – still quite recent – when the banking system found itself forced to invest the country's excess savings in German bonds with negative yields.

But that period is over. Interest rates are now rising again, and the impact is dramatic. Put simply, German banks are amongst the most positively levered in the world to higher interest rates. Assuming 3% interest rates, and a 25% deposit beta, Commerzbank could earn almost double the €1bn profit expected for the year just closed. And that's not all. Both Commerzbank and Deutsche are working hard to cut costs further. Commerzbank are well on the way to reducing the number of their branches by no less than 60%, and direct banking will be extended to corporate customers. The bank could generate a 14%+ return on tangible equity in 2024. And yet the share still trades on 0.4 times book value. A valuation only possible in the surreal world of the Baillie Gifford-Cathie Wood tech bubble. A world where the strangest speculations are credited with astronomical valuations…and profitable companies with dominant market shares from the 'old economy' are dismissed as little better than worthless…

The following investments performed poorly over the quarter:

Noble	+1%
Kering	+4%
VW	+7%
Golden Ocean	+11%
Legrand	+12%

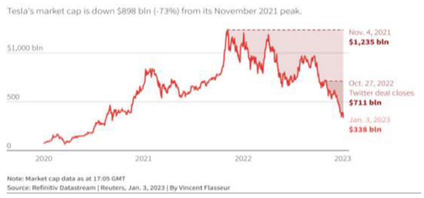
Kering underperformed unsettled by the possible impact of Covid on Chinese sales, as mentioned above. Whilst Gucci has clearly lost market share since 2019, we believe that investors have failed to appreciate quite how well Balenciaga, Bottega Veneta and YSL have performed over the same period. Assuming 11% earnings growth and a multiple of 20 times earnings – we see neither assumption as greatly challenging – the share could easily trade at €950, almost the double the level of today.

* * *

So what of 2023? Almost every conversation that I have had with fellow European fund managers has run roughly as follows.

> Fund Manager. *'So Stuart, it's crazy how far the tech companies and growth stocks have fallen. They must be buys…'*
>
> Stuart. *'Er…'*
>
> Fund Manager. *'And look how all the c**p has acted. It's totally nuts how well the banks and oil companies have performed…'*
>
> Stuart. *'But they are trading on 0.3-0.5 times book and are seeing significant earnings upgrades…'*
>
> Fund Manager. *'Are you feeling OK Stuart? We are all worried about you'*

To put flesh on the bones of all this, let us make a brief diversion to take a look at Tesla. We're all aware, of course of how sharply the value of Tesla has fallen (those of a nervous disposition please look away now):



Source: Reuters

And yet Tesla's market cap remains the highest among all car makers:

	Automaker	Market Capitalization
1	Tesla Inc	$388,970,000,000
2	Toyota Motor Corp	$196,680,000,000
3	Volkswagen AG	$74,510,000,000
4	General Motors	$47,790,000,000
5	Ford Motor Co	$46,760,000,000

Source: Reuters

Yes – even after a share price fall of 73%, Tesla still has a market cap 5.2x that of Volkswagen. Remember now that Volkswagen manufactured almost ten times more cars than Tesla did in 2021…. While disruptors were able to take market share from slower moving incumbents during the years of free money, that age is now over. If the magical thinking which became all pervasive in the world of equity investment yet lingers, we don't see how it can long persist.

In a nutshell,

> **the imminent demise of magical thinking has created one of the most exciting investment opportunities that I have seen in my thirty five years of managing money.**

As the Baillie Gifford-Cathie Wood tech bubble inflated, companies from the 'old economy' were progressively derated to valuations I have rarely seen in all my years as a stockpicker. Coupled with the strength of the dollar of late, you now have to go back to the 1980s to find a time when European assets looked quite so cheap to an American investor. More recently, the war in Ukraine has fuelled a 'final hurrah' for the dollar, reinforcing the view – widely held, but in our opinion wholly misconceived – that Europe has in some way become 'uninvestable'.

At the same time, the extraordinary rerating of American equities we have lived through has now started to run out of steam.

American earnings are now beginning to disappoint relative to Europe. On the one hand, fantastically optimistic earnings forecasts for American technology companies are being downgraded; whilst on the other hand older economy European industries, such as oil & gas and banking, are seeing significant upgrades…The 'new economy' has been so swamped with capital that competition in many 'disruptive' areas such as food delivery has become fierce. How do you value companies which don't grow, which face rampant cost inflation, which don't make a profit and which now have limited access to new capital?! At the same time the 'old economy' has been so starved of investment that many industries may struggle to meet demand for years to come. This should allow them to generate extraordinary returns.

But there is nothing new in finding the manifestly true hiding in plain sight. As Arthur Conan Doyle's Sherlock Holmes said, **"The world is full of obvious things which nobody by any chance ever observes".** [1]

In conclusion, please observe the table below, showing what our current portfolio looks like. When was the last time that you saw one quite so cheap…?

	2023		
	PER (x)	Price to Book Value (x)	Dividend Yield (%)
S.W. Mitchell Capital	8.0x	1.1	4.4

Source: S.W. Mitchell Capital

[1] *The Hound of the Baskervilles, Chapter 3*

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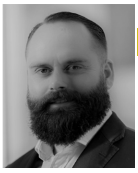
ALL ENQUIRIES



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DISCLAIMER