

Metro takeover offer drives strong end to Q2

Following a record Q1 in terms of absolute return, the fund fell back in May, but recovered sharply in June as several company-specific events contributed positively. These events include the takeover offer by EP Global for German food retailer Metro and continued strong performance in Ivanhoe Mines. We closed our position in Pilgrim's Pride as it hit our price target following a more than 75% re-rating this year.

From a general market perspective, we observe that the spread between US and Japan equity market valuation reached another record high in the period. This affected the fund as just under 25% of our assets are invested in the deeply discounted Japanese equity market mainly at the expense of US exposure, where we observe overly elevated valuation dynamics. We believe the gap between US and Japan valuation ratios have the potential to shrink in the mid-term as capital allocation discipline gradually improves in Japan. This is crucial to bring foreign investors' attention to the Japanese equity market's significant undervaluation.

Global trade tensions uncover opportunities

The ongoing global trade tensions have uncovered investment opportunities for contrarian value investors. Against this backdrop, we have accumulated a position in semi-conductor producer STMicroelectronics as our valuation analysis indicates substantial upside on current earnings power while the company will most likely continue posting solid growth rates over the mid-term. We have also initiated a position in German industrial conglomerate ThyssenKrupp. The ongoing trade dynamics are clearly not helpful for the company. We have also identified a valuation dislocation as the company has announced it is evaluating strategic options for its elevator unit, the crown jewel of the group. At a conservative valuation estimate of the elevator unit, where an IPO or direct divestment are options, we calculate a more than 50% upside in the share.



Photo: Bloomberg

Golden opportunity

During the quarter, we initiated a position in Roxgold, a Canadian-based gold mining company with its key asset, the Yaramoko Gold Mine, located in Burkina Faso, West Africa. While specific areas of Burkina Faso are said to be troubled by jihadist violence, amongst other things, the company's production has never been impacted. However, the negative perception has placed an unduly high discount rate on the company's asset base and future cash flow potential. The shares have also been under technical pressure as active mining funds transform into passive index tracking vehicles, causing substantial underperformance in smaller-cap mining stocks like Roxgold. We think additional catalysts include major owner and mining specialist Appian pushing for actions to remove the undervaluation of the shares, which may include consolidation activity among smaller operators in the region. The shares are trading at an extremely low valuation of less than three times operating cash flow. We set a price target of CAD 1.5/share, which indicates a more than 50% upside in 2-3 years.

Takeover offer in Metro

We initiated a position in German food retailer Metro about one year ago at rock-bottom valuation. At that time, the shares were under significant pressure from a shrinking operating margin situation in Russia and a slower than expected restructuring process at Real. The former main owner Haniel had previously sold a 7.3% stake to EPGC, an Eastern European investment vehicle, including a call option to acquire the remaining 15.2% stake. In addition, the related vehicle EP Global signed an agreement to acquire a 9% stake from Ceconomy. In light of these earlier events, the cash takeover offer initiated in June did not come as a complete surprise. The stock has been rising steadily and has gradually factored in the impending takeover potential, which EP now claims to be a 35% premium over the unaffected share price. Metro has been a strong contributor to the fund over the past year as well as in the quarter. We have sold approximately half the position as the stock has approached our price target.

US-based communications software provider Avaya was approached by private equity interest in Q1, which created a sharp re-rating in the share price. However, a disappointing earnings report set back the timeline and expectations for any such event. At the same time, the company has confirmed hiring JP Morgan to evaluate strategic options. The company continues to trade at very low earnings multiples and a significant free cash flow yield.

We closed our position in Pilgrim's Pride as the stock hit our price target following a more than 75% re-rating in the year. In our opinion, the valuation now fairly reflects the increased likelihood that China will be willing to consider US chicken imports and an overall turn in the chicken cycle.



Photo: Bloomberg

Outlook

As value-based contrarian investors, we like unjustified pessimism because of the prices it produces. Consequently, in this environment we are able to observe major valuation disconnects across large areas of the global equity markets. SKAGEN Focus currently has 35 positions, all of which are substantially undervalued. The top 10 holdings account for 44% of the portfolio at the end of the quarter.

The fund is a concentrated global equity fund with a mandate to invest in all cap-sizes, geographies and sectors globally. With our concentrated portfolio of 30-35 core positions, we aim to generate absolute returns at a controlled level of absolute risk.

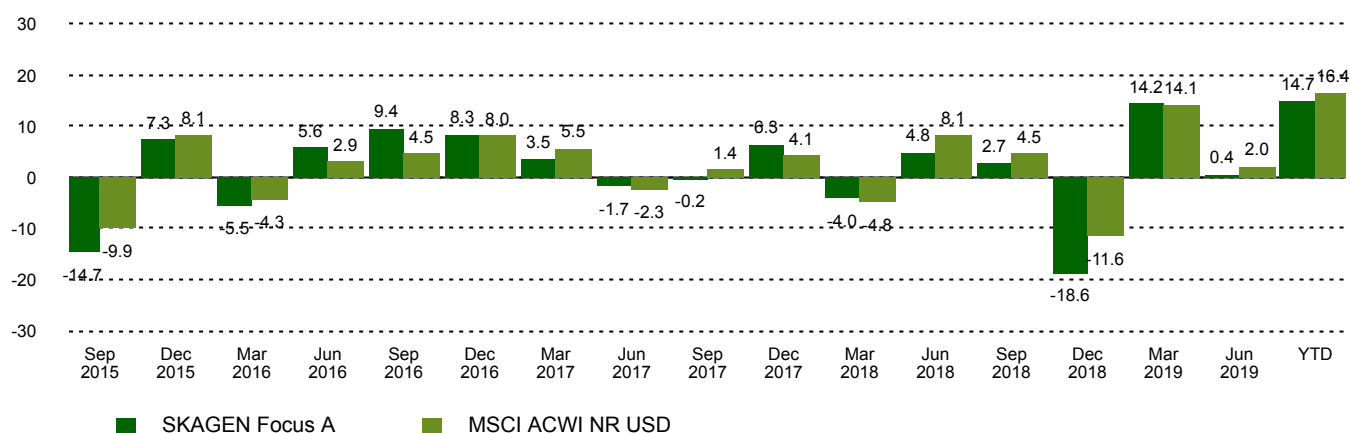
Historical performance (net of fees)

Period	SKAGEN Focus A	Benchmark index
Last month	4.8%	4.1%
Quarter to date	0.4%	2.0%
Year to date	14.7%	16.4%
Last year	-4.1%	7.6%
Last 3 years	7.3%	10.8%
Last 5 years	n/a	n/a
Last 10 years	n/a	n/a
Since start	1.0%	5.5%

Fund Facts

Type	Equity
Domicile	Norway
Launch date	26.05.2015
Morningstar category	Global Flex-Cap Equity
ISIN	NO0010735129
NAV	12.36 EUR
Fixed management fee	1.60%
Total expense ratio (2018)	0.8%
Benchmark index	MSCI ACWI NR USD
AUM (mill.)	186.03 EUR
Number of holdings	35
Portfolio manager	Jonas Edholm

Quarterly Performance



Contributors in the quarter



Largest contributors

Holding	Weight (%)	Contribution (%)
American International Group I	6.98	1.32
Ivanhoe Mines Ltd	4.03	1.21
Pilgrim's Pride Corp	1.44	0.69
Roxgold Inc	2.32	0.46
Sao Martinho SA	4.11	0.41



Largest detractors

Holding	Weight (%)	Contribution (%)
Avaya Holdings Corp	3.12	-1.06
China Unicom Hong Kong Ltd	4.82	-0.64
KCC Corp	2.73	-0.46
OMV AG	4.79	-0.41
Teikoku Sen-I Co Ltd	1.66	-0.41

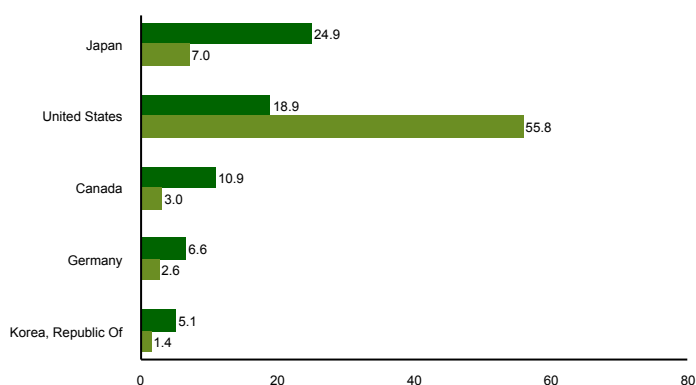
Absolute contribution based on NOK returns at fund level

All data in EUR as of 28/06/2019 unless otherwise stated.

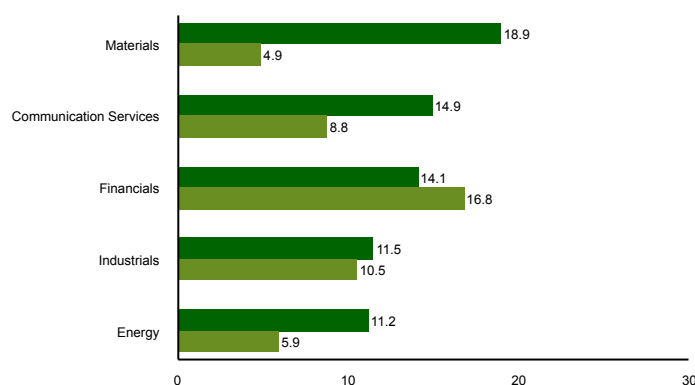
Top ten investments

Holding	Sector	Country	%
American International Group Inc	Financials	United States	7.1
China Unicom Hong Kong	Communication Services	China	5.0
Ivanhoe Mines Ltd	Materials	Canada	5.0
OMV AG	Energy	Austria	4.8
Sao Martinho SA	Consumer Staples	Brazil	4.6
BANK KYOTO	Financials	Japan	4.3
Hitachi	Information Technology	Japan	4.0
Telecom Italia SpA	Communication Services	Italy	3.7
Toyota Industries	Consumer Discretionary	Japan	3.4
Japan Petroleum Exploration	Energy	Japan	3.4
Combined weight of top 10 holdings			45.3

Country exposure (top five)



Sector exposure (top five)



■ SKAGEN Focus A ■ MSCI ACWI NR USD

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