Sifter Global Fund

Quarterly Report Q4/2020

"We do not buy stock price returns – we buy business returns."

Hannes Kulvik / Founder of the Sifter Fund

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In Q4 the Fund returned 7.0% and 10.4% in 2020.

Fund Performance

During Q4 2020, Sifter Fund's total return was 7.0% vs 9.9% for the Index (MSCI ACWI Eur), as depicted in table 1.

→ In Q4/2020 The Fund returned 7% (R/I-class) and 7.1% (PI-class)

→ In 2020 the Fund R/I-class return was 10.4% and PI-class 10.9%

→ Annualized return since inception of the Fund is 9.0% (2003/6-2020/12)

→ Since Inception (2003/6), Sifter Fund R/I-class has returned 350% in total, which is 46% better than the benchmark index.

Geographical allocation

United States	56.8 %
Japan	11.5 %
Taiwan	8.8 %
Sweden	7.7 %
Canada	6.2 %
Germany	4.0 %
France	2.6 %
Denmark	2.4 %

Graph 1. Sifter Fund Global NAV changes Q4/2020 (R/I-class)

Fund Performance

	Returns					Annualized returns since inception	
	Q4 2020	2020	2019	2018	2017	(6/2003–)	(3/2015–)
Sifter Fund Global R	7.0 %	10.4 %	31.3 %	-4.1 %	8.5 %	9.0 %	
Sifter Fund Global PI	7.1 %	10.9 %	31.8 %	-3.7 %	8.9 %		8.3 %
Benchmark index	9.9 %	6.7 %	28.9 %	-4.9 %	8.9 %	8.3 %	7.2 %

Table 1: Sifter Fund (R/I-class and PI-class) performance vs Index (MSCI ACWI, Total return EUR).

Best & Worst performers in Q4/2020

Top 3
return in EUR

Safran	+37.3%
Lam Research	+36.8%
Disco	+34.0%

Bottom 3
return in EUR

Ain Holdings	-15.2%
S&P Global	-12.4%
North West	-10.5%

The vaccines were good news for many pandemic-hit industries.

During the 4th quarter, two key events improved the global economic outlook:

→ US elections were held in a reasonably orderly fashion, and several COVID-19 vaccines showed promising test results.

→ The vaccines were particularly good news for many pandemic-hit industries, including aerospace, which supported Safran's prospects.

→ Meanwhile, the semiconductor companies continued to enjoy a healthy operating environment.

→ Dollar depreciation by 9% during 2020 has impacted the euro-based Fund since over 70% of the Fund companies are valued in dollars. During Q4 the dollar depreciated against the euro by 4%.

The weakest performers of Q4 were affected by the pandemic or by strategic moves that increased uncertainty.

→ While pharmaceutical dispensing has been a stable core business for Ain Holdings, the group's results have been dampened by difficulty in dealing with the effects of lock-down measures on its cosmetics stores.

→ Meanwhile, S&P's 44bn dollar mega merger with IHS contains integration risks and leads to a more leveraged entity than S&P as a standalone company.

Top performers in 2020

(Return in EUR)

TSMC	+76.8%
Lam Research	+50.5%
iRobot (invested since April 2020)	+42.6%

The semiconductor companies have enjoyed beautiful growth during 2020.

The year was characterized by the triumph of technology companies. Increasing emphasis on home-based activities accelerated the transition towards digital services and increased the demand for many types of electronics.

Accordingly, Lam Research and TSMC, both involved with high-end semiconductors, have witnessed clear year-over-year revenue growth. Meanwhile, the home-improvement boom has reflected on the demand for robotic vacuums, benefitting iRobot.

In addition to market specific tail winds, the top performers also achieved company specific success. iRobot was allowed to seek refunds on the tariffs earlier paid to the U.S. government and made good progress on initiatives aiming to circumvent them in the future. Meanwhile, TSMC benefitted from Intel's eroding competitive position and manufacturing challenges, as Intel's competitors tend to be TSMC's customers and Intel might eventually contract more of its own manufacturing activities to TSMC.

BACKGROUND **Growing semiconductor manufacturing capacity, IoT spending and data.** In July 2020, the industry association for the electronics industry, SEMI, raised its estimate for semiconductor equipment sales in 2020 and 2021, even though the pandemic had struck the global economy since their previous forecast in December 2019. Meanwhile, IDC continues to forecast strong growth for IoT spending and data created by IoT devices over the next few years, some 11% and 26% CAGR, respectively.

In Q4 we invested in two new companies.

Portfolio changes in Q4

During the quarter, we invested in two new companies: Automatic Data Processing and Novo Nordisk. These investments were primarily financed with the complete sale of Intel, as well as reductions in Cisco and SMC.

Automatic Data Processing (new investment)

In early September, a company called **Automatic Data Processing** [ADP] came through the Sifter screening. Why did we consider ADP as a quality company and a suitable investment for the Fund?

→ ADP provides software, service, and outsourcing to improve its customers' HR (Human resources) operations.

→ ADP is the world's largest Human Capital Management (HCM) and PEO (outsourcing) solutions provider.

→ The value proposition is to improve its customer HR function and help the client survive in the growing regulative jungle.

→ The earnings model is mostly by recurring monthly revenue, which is very predictable.

→ ADP customers are very satisfied. The customer retention rate has remained steady at over 90%. Also switching costs are real and thus clients tend to stay with ADP, on average, for 11 years.

→ The industry is growing and the company is well positioned to benefit from an expected mid-single digit long-term growth in its primary markets.

→ Return on equity (ROIC) of almost 30%. Gross margin of more than 40% also improve Sifter's portfolio business metrics.

→ In the short-term however, the company is likely to face some headwinds from increased unemployment in the US.

10 largest holdings

Representing 53.4% of total portfolio (31.12.2020)

Taiwan Semiconductor-SP ADR	ASIA-PACIFIC
Lam Research Corp	NORTH AMERICA
Microsoft Corp	NORTH AMERICA
Alphabet Inc	NORTH AMERICA
Disco Corp	ASIA-PACIFIC
Canadian National Railway Co.	NORTH AMERICA
Texas Instruments Inc	NORTH AMERICA
Starbucks Corp	NORTH AMERICA
Verisign Inc	NORTH AMERICA
S&P Global Inc	NORTH AMERICA

Novo Nordisk is a classic example of a quality business we like.

Novo Nordisk (new investment)

Novo Nordisk is one of our latest investment. After studying its business model we are fascinated by the company's focused and strong position in diabetes therapy products as well as patented medicines.

→ The global leader in diabetes care products in the form of insulins and other novel treatment methods like GLP-1 analogues.

→ The latter is especially interesting as the GLP-1 treatment has shown great promise and is expected to grow exponentially over the next ten years under patent protection.

→ We expect some pricing erosion in rapid-acting insulins from biosimilar launches, but this will be offset by higher GLP-1 sales and new innovations in long-acting insulins.

→ A promising study on obesity care is nearing completion and will receive regulatory approval in this year or the next, which will provide more upside to this investment case.

→ The company's ROIC is an amazing 60% and gross margins steadily over 80%.

→ Likewise the revenue growth is expected to be mid-single digits over the next five years.

Intel stayed over 7 years in Sifter portfolio and returned 118%, excluding dividends.

Intel (sold)

Intel Corporation primarily designs, manufactures, and sells microprocessors. In 2020, we saw that the company faced several new threats to its business - creating such uncertainty that the investment thesis no longer held ground. The threats were

1. loss of manufacturing technology advantage,
2. increased competition from AMD,
3. future competition from Apple,
4. potential future data centre competition from Nvidia, and
5. uncertainty in M&A activity and management focus.

A drastic loss of sales from one or more business units would seriously affect Intel's margins as the business is very dependent on high sales volume to keep its expensive foundries running. This investment no longer adhered to our investment thesis.

Since 2012 Cisco has returned 173% and also offered 2.8% dividend yield, on average.

Cisco Systems (weight reduced)

Cisco Systems is one the Sifter's oldest investment. Cisco provides networking solutions, primarily hardware. Sifter bought its first Cisco shares in May 2012. By the end of 2020, the share had appreciated 173% in USD terms. During that period, Cisco also offered 2.8% dividend yield, on average.

→ The company is quite well entrenched in the campus network environment, which represents the largest part of Cisco's revenue. However, campus networks face a stagnant growth outlook, partly aggravated by a growing shift towards remote work.

→ Meanwhile, Cisco continues to lose market share in data centres and among service providers.

→ In addition, revenue from Cisco's collaboration & communication solutions has declined as moderate success with Webex has not offset declining revenue from Unified Communication solutions.

→ While Huawei's headwinds could help Cisco capture market share in developed economies, Cisco still faces other capable competitors, and the short-term gains would be partly offset by heightened entry barriers to the lucrative Chinese network equipment market.

→ Cisco is attractively valued relative to its current earnings level, but the growth outlook is uncertain and overall underwhelming.

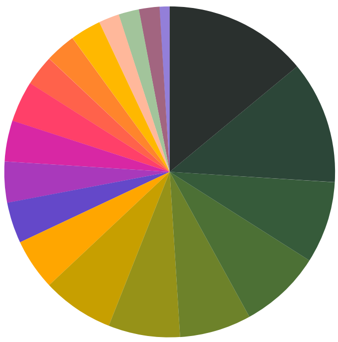
SMC Corporation (weight reduced)

SMC Corporation is a Japanese company which provides pneumatic solutions, primarily for factory automation. The company has fared well (c. 26% in 2020) during the COVID-19 crisis as the large inventory allowed SMC to continue serving customers using the just-in-time method and without major disruptions.

→ However, the departure of SMC's long-term chairman may bring unwelcome instability.

→ Recent management commentary regarding the scale and trend of recurring revenue reflects a more volatile business than earlier thought, calling for a larger safety margin.

→ Overall, we saw that Novo Nordisk should offer better risk adjusted returns and thus reduced the weight of SMC in Sifter portfolio and placed the money in Novo Nordisk.



Sector allocation

Semiconductors **13.1%**
Semiconductor Equipment **12.3%**
Systems Software **8.3%**
Financial Exchanges & Data **8.1%**
Industrial Machinery **6.6%**
Auto Parts & Equipment **6.5%**
Pharmaceuticals **6.5%**
Interactive Media & Services **4.7%**
Railroads **4.4%**
Restaurants **4.3%**
Internet Services & Infrastructure **4.2%**
Hypermarkets and Super Centers **4.1%**
Household Appliances **2.9%**
Data Processing & Outsourced Services **2.9%**
Communications Equipment **2.8%**
Aerospace **2.5%**
Trucking **2.2%**
Food Retail **1.8%**
Drug Retail **1.5%**

We do not buy stock price returns – we buy business returns

We never promise any stock price returns – However, we promise that you and we own quality business. For this reason, we closely monitor the four indicators of our companies' quality (Table 2.). We compare these indicators against the S&P 500 companies.

Main changes in key performance indicators (KPIs)

→ **Return on Invested Capital** improved over 2019 and stands well above S&P500

→ **Operating margin** remained on 2019 level, clearly above S&P500

→ **Sales growth** – slowed down materially from 2019, but remained slightly positive and above S&P500

→ **Net debt/EBITDA** – improved from 2019, as the median Sifter company now holds a net cash position. S&P500 remains comparatively highly leveraged.

→ **EV/EBITDA** valuation metric now implies that Sifter businesses are slightly cheaper than the S&P500.

17% ROIC is one clear indication that we own quality companies.

KPIs	2014	2015	2016	2017	2018	2019	Sifter T12M	S&P 500 T12M
ROIC	14%	13%	14%	15%	16%	15%	17%	7%
Operating margin	20%	20%	22%	26%	26%	25%	25%	15%
Sales growth	2%	4%	8%	9%	9%	6%	1%	-1%
Net debt/ EBITDA	0.4x	0.6x	1.0x	-0.1x	0x	0.5x	-0.2x	2.2x
EV/EBITDA (Current)							16.6x	17.7x

Table 2. Key Performance Indicators (KPI's) for Sifter businesses vs S&P 500.
*Trailing. 12 months, median (31.12.2020)

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This report has been produced by Sifter's Investment Committee (IC) and Advisory Team.

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Do you need help?

If you have any question regarding our investment strategy or want to place an investment in Sifter, please contact Mr. Santeri Korpinen or check www.sifterfund.com

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