



P.S. Krøyer's dog "Rac", Study, 1898. Detail. By Peder Severin Krøyer, one of the Skagen Painters. This image belongs to the Art Museums of Skagen.

SKAGEN Focus

Status Report February 2017

The art of common sense



Summary – February 2017

- The fund is a highly concentrated equity fund with a broad all-global mandate. The overall objective is to invest in a few select investments with an exceptional risk/reward profile from an absolute return perspective.
- The target number of positions is 30-35 and the top ten positions should constitute 40-50% of the portfolio. At the end of the month, the fund holds 34 positions, and the top ten positions account for 43.5% of the portfolio. The cash position is 5.3%.
- SKAGEN Focus* was up 4,4% in the month measured in SEK, while the global equity markets (measured as MSCI AC World) were up 6,0%. So far in 2017, the fund is up 3,4% while the global equity markets have gained 4,9%.
- Tesoro, Fila Korea and Philips Lighting were the strongest contributors to the fund's performance in February measured as absolute contribution in NOK. SK Hynix, Gold Fields and Telecom Italia were the main detractors during the month.
- During the month we initiated a new position in Gold Fields, a South African based gold miner. Gold Fields is one of the largest gold exploration companies in the world with a total production capacity of 2.2m ounces and reserves in excess of 50m ounces. See attached fact sheet for more information.
- The fund has a broad mandate to invest in all geographies and sectors. The fund is also market capitalisation-agnostic, and currently small-cap** positions constitute 15% of the fund, while mid-cap and large-cap positions account for 34% and 51%, respectively. These figures may vary meaningfully over time.

* Unless otherwise stated, all performance data in this report relates to class A units and is net of fees.

** Small-cap defined as market cap below USD 2bn, large-cap more than USD 10bn.

Results, February 2017 in SEK, net of fees

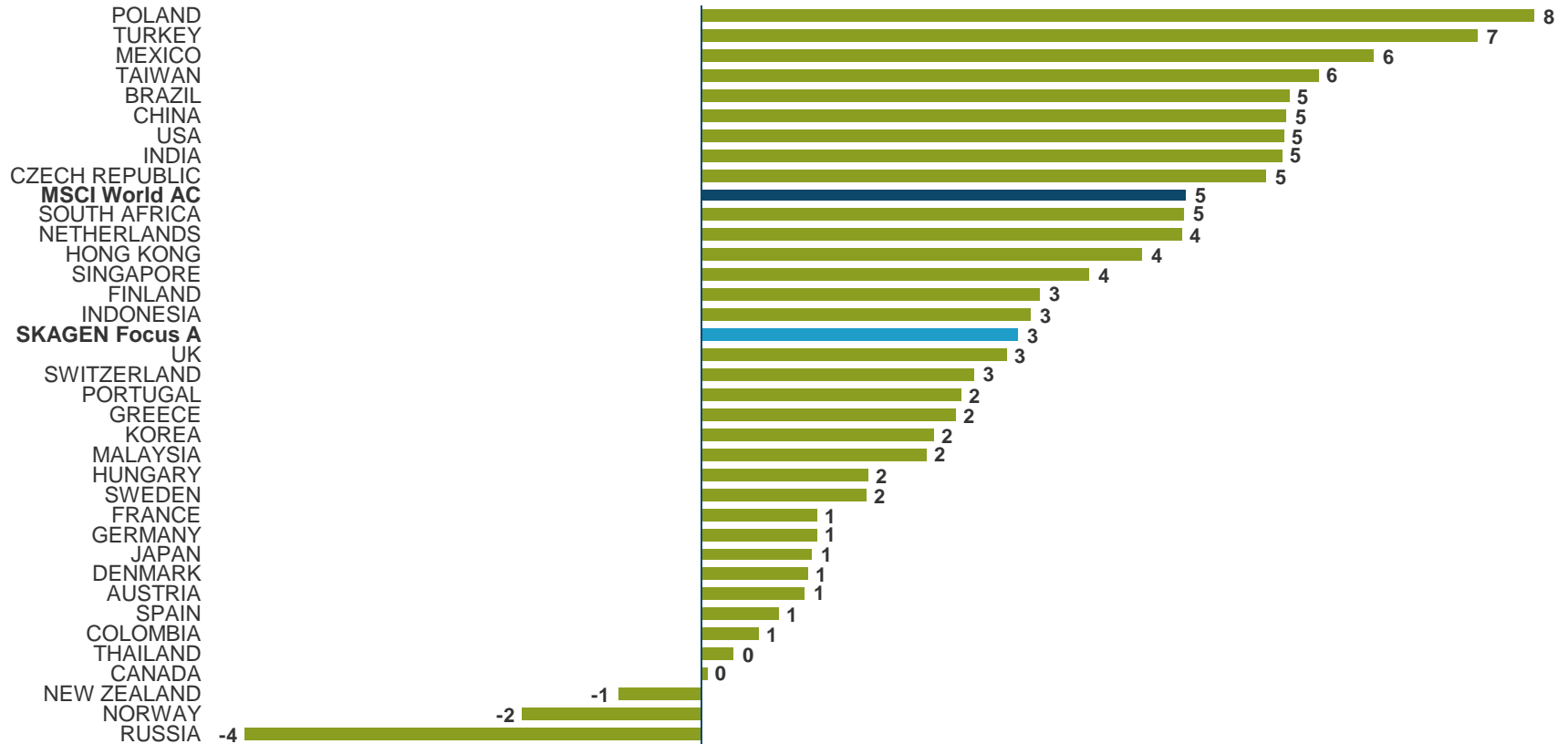


	February	QTD	12 months	Since inception*
SKAGEN Focus A	4,4%	3,4%	37,1%	4,2%
World Index*	6,0%	4,9%	27,6%	6,9%
Excess return	-1,6%	-1,5%	9,5%	-2,7%

Note: All returns beyond 12 months are annualised (geometric return)

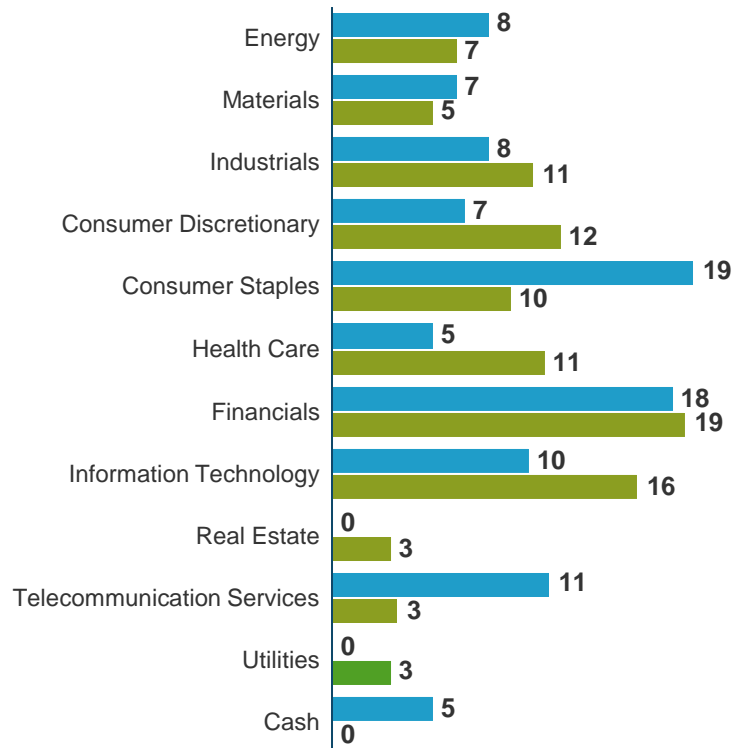
* Inception date: 26 May 2015

Markets in February 2017 in EUR (%)

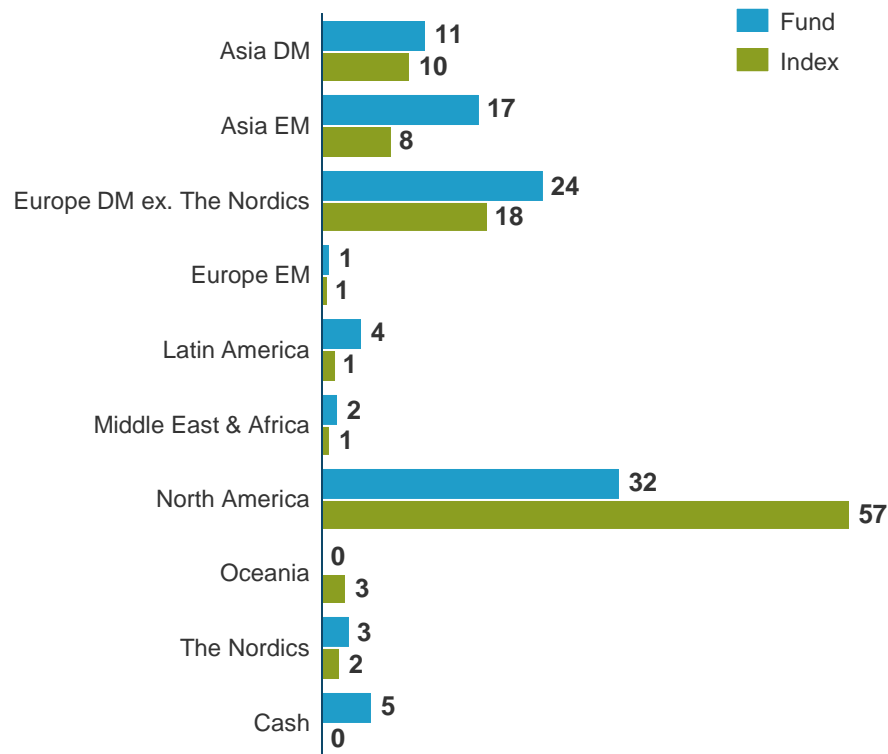


Sector and geographical distribution vs index (Feb. 2017)

Sector distribution



Geographical distribution



Holdings increased and decreased during February 2017

Key buys

- **Gold Fields (new)** - During the month we initiated a new position in Gold Fields, a South African based gold miner. Gold Fields is one of the largest gold exploration companies in the world with a total production capacity of 2.2m ounces and reserves in excess of 50m ounces. See attached fact sheet for more information.

Key sells

- **Jenoptik** – The company has continued to generate solid fundamental results and an impressive order intake. The position was reduced into strength during the month as the share price approaches price target.

Main contributors MTD

Largest positive contributors

<i>Company</i>	<i>NOK (000)</i>
Tesoro	7 791
Fila Korea	7 562
Philips Lighting	6 749
Jenoptik	6 416
Teva Pharmaceutical Industries	6 353

Largest negative contributors

<i>Company</i>	<i>NOK (000)</i>
SK Hynix	-5 358
Gold Fields Ltd	-4 881
Telecom Italia Spa	-2 862
Magforce	-1 782
Softbank Group	-1 690

Value Creation MTD (NOK MM): 56

NB: Contribution to absolute return

Main contributors YTD 2017

Largest positive contributors

<i>Company</i>	<i>NOK (000)</i>
E-MART	13 885
Jenoptik	8 566
Samsung SDI	8 068
Philips Lighting	6 734
Fila Korea	6 331

Largest negative contributors

<i>Company</i>	<i>NOK (000)</i>
Aryzta	-16 783
Telecom Italia Spa	-9 241
Whiting Petroleum	-7 711
AIG	-6 984
Gold Fields Ltd	-4 881

Value Creation MTD (NOK MM): 21

NB: Contribution to absolute return

Most important changes Q1 2017

Q1 Holdings increased



Gold Fields Ltd (New)
Carlsberg
Tesoro
China Telecom
AIG
Telecom Italia Spa
Teva Pharmaceutical
Industries
Philips Lighting
Synchrony Financial
Samsung SDI
Whiting Petroleum
CIT Group
Adient
Alphabet
Fila Korea
Taiheiyō Cement

Q1 Holdings reduced



Aryzta
Jenoptik

Largest holdings in SKAGEN Focus

	Price	P/E 2016e	P/E 2017e	P/BV last	Price target	Upside to target %	Holding size, %
American International Group Inc	63,92	12,8	10,6	0,8	90,0	41 %	7,1%
E-MART Inc	208 000,00	14,3	12,6	0,8	270000,0	30 %	4,5%
Tesoro Corp	85,19	14,2	12,7	1,8	120,0	41 %	4,4%
Jbs SA	11,70	63,9	7,8	1,3	22,0	88 %	4,2%
Teva Pharmaceutical-Sp ADR	35,02	7,4	7,3	1,2	90,0	157 %	4,2%
Telecom Italia Spa	0,77	9,5	11,3	0,8	1,2	57 %	4,2%
Softbank Group Corp	8 362,00	9,7	13,0	2,9	9600,0	15 %	3,8%
SBI Holdings Inc	1 572,00	14,1	14,1	0,9	3000,0	91 %	3,8%
Taiheiyo Cement Corp	395,00	9,2	12,4	1,4	495,0	25 %	3,7%
Philips Lighting NV	26,14	11,0	10,6	1,5	30,0	15 %	3,7%
Top 10 positions		17,8	12,5	1,1		55,5%	43,5%
Total Equity (34 positions)							94,7 %
Cash							5,3 %
Total Portfolio							100,0%

As at 28/02-2017

*JBS is the main owner of Pilgrim's Pride, which is a 1.0% position in the fund. These two positions should be viewed as one, with a total weight of 5.2%.

Key earnings releases and corporate news, February 2017

E-MART (4.5% weight)

Investment case update

E-mart is a Korea-based company principally engaged in the hypermarket business. The company has been struggling with saturation in its core discount format and increasing competition from new online entrants. Several signs of operational improvements were however visible in Q416. Overall sales increased by 8% while operating profit grew 20% over last year. In the core hypermarket segment sales were up 4% with a major margin improvement resulting in an operating profit increase of 15%. Traders and Online Mall grew sales 38% and 32% respectively. The company's subsidiaries, including the convenience store segment (CVS) and the Chinese operation, showed an improvement from last year as the company gradually withdraws from unprofitable operations. We think the now visible improvements in the core hypermarket segment have fuelled the recent re-rating of the shares. Valuation is still quite supportive, with EV/sales multiples around 0.6x and forward EV/EBITDA at 6x, in combination with strong valuation support from property values (85% of the stores are company owned) and a major non-core holding in Samsung Life.

Fact

In Q416 sales increased 8% from last year to KRW 3365bn. Hypermarket sales +3.7%, E-mart mall +32.5%, Traders +38%, CVS (convenience stores) +153%, Chosun Hotel +7%, China -35% (currently reducing store base). Operating profit was up 20% to KRW 151bn over last year. Operating margin increased from 4.0% last year to 4.2% in Q416.

Tesoro (4.4% weight)

Investment case update

The company owns and operates seven refineries in the Western US. They also have a substantial retail operation (selling refined products to gas stations) and a logistics segment (separately listed in a so-called MLP) which owns pipelines for transporting refined products. The company announced Q4 earnings that reflected the general refining environment, which has been characterised by lower refining margins and weaker crude oil differentials. In that context, Tesoro managed to increase its gross refining margin somewhat sequentially due to reduced operating costs. In total, net income from continuous operations rose by 18% YoY, driven by the refining and logistics segment. One of its largest segments, however, the marketing segment, which accounts for around 30% of sales, fell both sequentially and YoY due to lower fuel margins and sales volumes. We believe Tesoro is undervalued with respect to its different assets, and putting a market multiple on the retail business would indicate that the refinery business is implicitly trading at 2-3x EV/EBITDA which is a distinct discount to peers. The company's recent acquisition of Western Refining delays any activist investor involvement, but a future breakup remains a credible catalyst for the investment case.

Fact

Tesoro reported fourth quarter sales of USD 6.6bn and net earnings of USD 78m.

Key earnings releases and corporate news, February 2017 (cont.)

Telecom Italia (4.2% weight)

Investment case update

Telecom Italia is a former state telecommunications monopoly. The company has two main operations: Domestic telecom (75% of revenues) and a majority stake in TIM Participacoes (25% of revenues, 67% owned) which is Brazil's second largest mobile operator. The company is in the midst of a turnaround led by the newly appointed CEO Cattaneo, following a multi-year contraction in core business segments. Released numbers for FY16/Q416 revealed signs that the company might be in the early stages of a turnaround where FY16 revenues in Domestic Telecom were flat over last year while Q416 showed an improvement compared to last year (+5%). The Brazilian unit was down sharply in FY16 compared to last year but there was a substantial sequential improvement in Q416. EBITDA in Domestic Telecom was up 20% over last year with a notable acceleration in Q416 while Brazil decreased by 4%. Capital expenditure was EUR 4.8bn in 2016, down EUR 320m over last year. A strategic plan for 2017-2019 was approved with focus on "substantial" transformation of the company's cost base and a return to growth in domestic telecom and halting the negative development in Brazil, indicating an overall implicit 2019 EBITDA level in excess of EUR 9bn. Investments in Italy will be around EUR 11bn (2017-2019) with 45% related to completing ultra-broadband networks. Net debt to EBITDA is targeted below 2.7x at the end of 2018. Even before these potential fundamental improvements the stock is trading at a substantial valuation discount at 5x EV/EBITDA and at a major discount to the peer group. We think that the gradual market realisation that competitive threats from new entrants are not as bad as perceived and solid cost-cutting potential in line with the company's strategic plan will pave way for a re-rating of the shares in the mid-term.

Fact

In FY16 overall revenues were down 3.5% over last year (EUR 19b) while EBITDA increased to EUR 8.0bn, up 14% over last year.

SBI Holdings (3.8% weight)

Investment case update

Minor positive. Financial Services Business showed a growth of 7% despite a 20% drop in transactions in Tokyo and Nagoya (though only 10% for SBI). The rise in revenue came from FX, banking and insurance and thereby mitigated the fall in profit to only 0.8% YoY. The volatility in markets and FX is positive for the transaction-based business and they highlight the continued political unrest in the West as providing good potential for better earnings. The Asset Management Business (confusingly named SBI Savings Bank), showed positive signs and recorded a rise in of 270% stemming mainly from better performing loans (re-valuation of book and incorporation of Kora banking). Biotech continued to lose money due to more clinical trials – on the positive side they have manage to recoup some cash on milestone payments and licensing agreements.

Key earnings releases and corporate news, February 2017 (cont.)

Softbank (3.8% weight)

Investment case update

Softbank is a Japanese telecom and internet conglomerate with main assets in the Chinese online-giant Alibaba, US based telecom operator Sprint and Domestic Telecom businesses (mainly Softbank Mobile). In Q317, overall sales fell 1% while EBITDA increased 15%. The solid performance in the Domestic Telecom segment continued with an increase in revenues of 2% and EBITDA increase of 8%. Sprint's seemingly successful operating turnaround manifested itself in a revenue increase of 2% and a solid positive contribution to EBITDA, moving from a negative contribution last year. The 35% owned Yahoo Japan continued to perform strongly with revenues up 8% and EBITDA up 18%. The recently acquired ARM Holding is now fully consolidated and generated a positive contribution. The company also announced that the recently launched USD 100bn technology fund is about to close, with anchor investors in Saudi Arabia, Apple, Qualcomm and Oracle. The fund will be managed by Softbank, which will earn a fee for its management services, potentially introducing a new major income stream. Following the quite controversial ARM deal last summer, net debt/EBITDA stands at 4.0x which is supported by the relatively stable cash flows from the domestic telecom business. Management repeated its goal to reduce debt to 3 - 3.5x in the next few years. Considering the major re-rating of the company's holdings, including Sprint, Yahoo Japan and Alibaba over the past year, the implicit share discount to conservative fair value of the underlying assets, assuming the price paid for ARM Holdings is fair in a longer term perspective, is in excess of 30%. Also, there is very little value attached to the myriad of unlisted transport and e-commerce stakes acquired by the company over the last few years.

Fact

In Q317, sales decreased 1% to JPY 2310bn while EBITDA rose 15% to JPY 660bn.

CIT (2.9% weight)

Investment case update

The US specialty finance conglomerate CIT reported a Q416 with several non-recurring items mainly related to the divestment of commercial air and goodwill impairment, which resulted in an overall loss. However, below the surface, rental and finance income were fairly flat over last year while the net finance margin decreased marginally to 3.6%. Core return on equity remains depressed at low single digits. Tangible book value decreased to USD 46/share. Credit quality was a positive as non-performing loans and charge-offs fell, which has been a concern for investors. Capital ratios remain high with common tier one at 13.8%. The sale of commercial air announced last year will free up as much as USD 3.3bn (40% of market cap) and will be distributed to shareholders during 2017, possibly through a tender offer. The core regional bank, the old One West franchise, is currently under-earning compared to other similar regional banks and fundamentally should be able to reach peer group profitability in the mid-term. The equity is trading below book value and with further simplification of the corporate structure combined with peer group profitability in the bank there is substantial upside to the current equity price.

Fact

CIT announced a Q416 net loss of USD 424m from continuing operations (excl. commercial air). Adjusted for non-recurring items, net income was USD 196m (USD 0.97/share).

Key earnings releases and corporate news, February 2017 (cont.)

Teva Pharmaceutical (4.2% weight)

Investment case update

Minor positive. CEO Vigodman who was brought in three years ago as a turnaround specialist has eroded shareholder confidence with a sloppy M&A spree and we view his departure as a necessary step to rebuild trust in the equity story. All else being equal, the stock will likely be range-bound until a new CEO is presented. Assuming the new CEO is a well-regarded executive with a solid track record and a clear mandate to act decisively in the role, it could provide a trigger for a significant re-rating. The main short-term risk at this point is that the new CEO (once appointed) will present a major kitchen-sink to rebase expectations, including the dividend level (currently 4% dividend yield).

Carlsberg (3.0% weight)

Investment case update

The investment case for Carlsberg, the Danish brewer, is that it is “a low growth stable earner with sub-par profitability to peers and which is en route to improving profitability beyond current market expectations”. The annual report for 2016 and guidance for 2017 show that the business is moving very slowly. But at least it is moving in the right direction.

Summary

- Volumes are flat to declining in beer and growing in non-beer. Currency headwinds have negative impact on DKK reporting. The price/mix focus and cost adjustment initiatives have raised the EBIT-margin and more will come in 2017.
- W Europe (55% of clean EBIT) sees continued price/mix upward shift. Grimbergen craft beer sales grew 11% and help the price/mix action plan. Profitability improved as EBIT-margin improved 0.5 percentage points to 14.2% - still below peers.
- E Europe (17% of EBIT) saw non-beer growth and beer being flat. In DKK, revenues declined 6%, but the cost trimming helped as the EBIT-margin improved 0.6 percentage points to 18.0%.
- Asia (28% of EBIT) saw organic revenue growth, but currency took it down to 2%. Profitability improved as EBIT-margin rose 0.9 percentage points to 19.1%. Carlsberg Elephant beer sells well in India and in 2017 the footprint will be expanded to 8 breweries.
- Good cash flow in 2016, so net debt declined DKK 6bn to DKK 25bn. Dividend proposed at 10.
- Guidance 2017 is not very well communicated, but in essence EBIT for 2017 should be DKK 9.0bn and sell side currently has DKK 8.8bn. The stock price decline of 3% on reporting days consequently seems slightly strange.

Key earnings releases and corporate news, February 2017 (cont.)

Infineon (2.6% weight)

Investment case update

Infineon is a German semiconductor manufacturer founded in 1999, when the semiconductor operations of the parent company Siemens AG were spun off. The company produces semiconductors and systems solutions. The company reported solid FY1Q17 sales growth of 6% YoY, with an overall margin expansion of 300 bps. The automotive segment (40% of sales) grew by 15% YoY, while its profitability improved substantially. The industrial power segment grew sales by 6% YoY. Book-to-bill ratio was a solid 1.3 – interestingly, this is while the recent Wolfspeed acquisition was not consolidated in the quarter. The company also provided guidance of a further 100 bps margin expansion in FY2017, which clearly seems conservative based on our recent conference call. The electric vehicle/self-driving/radar trend is in the company's favour, and management stated that while current production of EV is very China-driven, orders from European manufacturers in 2018 and beyond are more than substantial – and this is obviously the core market for Infineon. The company's transition to 300mm silicon production is ahead of schedule. We believe that Infineon holds a unique position with its enviable market positions in the structural shift towards hybrid engines, auto electrification and the autonomous car (especially within radar applications) and the explosive growth from increased semi-content in these areas. As this has started to become reflected in the share price, we have been reducing the position. We still see upside on current valuation and a discount to high quality industrial peers, but have adjusted our position size due to risk/reward. Our target price is EUR 20, which seems increasingly conservative due to the company's asset growth (successful acquisitions) over the past few years.

Fact

Infineon released Q117 numbers; Sales of EUR 1.6bn and Segment result of EUR 246m, at a margin of at 15%.

Adient (2.9% weight)

Investment case update

Adient is a US-based auto-parts supplier. The company was recently spun off from Johnson Control, and is a global market share leader in seating and interior components for passenger cars. The company reported earnings for the first time as a standalone entity. Revenue for the quarter decreased 5% YoY, which was primarily driven by a negative impact from FX. Profitability on the other hand increased by 14% YoY as the operating margin expanded by 120bps to a margin level of 7.2%, which is still low compared to peers. The increased profitability is mainly due to internal cost reductions, a trend which management thinks can continue. The company also earns an equity income from its myriad of Chinese joint ventures, up 7% YoY and which represents a substantial part of earnings. With the new management in place, an inefficient capital structure and low profitability compared to its industry peers, we see several catalysts on the horizon, such as a special dividend from the JVs which are mainly net cash or a restructuring of the company structure or listing or consolidating some of the larger JVs. We see the potential for quite high free cash flow generation in the mid-term which will probably initially go to de-levering the balance sheet.

Fact

The company reported earnings for the first time, as a standalone entity following the spinoff from Johnson Control. Sales for the quarter decreased 5% YoY to a level of USD 4bn, while profitability increased 14% YoY to a level of USD 290m. Equity income for the quarter rose by 7% YoY to a level of USD 106m, representing more than 40% of total EBIT.

Key earnings releases and corporate news, February 2017 (cont.)

Ence
(2.5% weight)

Investment case update

Ence is Europe's leading producer of eucalyptus pulp and the second largest in terms of sales. It is also the leading Spanish company in the production of renewable energy using forest biomass. The company reported fourth quarter earnings after a turbulent 2016 which was characterised by depressed hardwood pulp prices and operational disruptions. These were short-term headwinds which gave us the opportunity to initiate the position at depressed share price levels. In the fourth quarter, the company reported a 25% increase in net sales, driven by both the pulp and energy segment. The hardwood pulp price continued to decline somewhat in EUR but was offset by a pickup in demand and strong volume growth (20%). Going forward the company expects pulp prices to follow an upward trend in H1 and be stable in H2. Ebitda increased by 29% during the quarter, driven by the volume growth and, most importantly, a reduced cash cost level thanks to investments in the Navia mill. Net debt was reduced to a level of 1.9x nd/ebitda. Asset disposals were discussed during the conference call, relating to non-core forest land assets in the southern part of Spain, with a book value of EUR 170m. These will be evaluated for sale and could offer further catalysts in the future. The share price has been strong since we initiated the position in late October, driven by the appreciating USD and improving market conditions. We believe that Ence is well positioned within its fragmented industry, has a solid balance sheet, non-core assets it could dispose of, a long-term oriented ownership structure and generates healthy amounts of cash even in this depressed pulp price environment. Our target price for Ence is EUR 3.2, equivalent to 7x EV/ebitda.

Fact

Ence reported Q4 sales of EUR 174m, EBITDA of EUR 42m and net profit of EUR 14m. The company reported a cash cost level of EUR 340/ton (a reduction of EUR 14/ton vs. Q3).

Massimo Zanetti
(0.7% weight)

Investment case update

Massimo Zanetti, the Italian based coffee producer, operates in three main segments: Private Label (37% of sales), Mass market (37%) and Food services (26%). The company went public in June 2015 at a meaningfully higher share price than the current price, and since then has become 67% family-controlled. The end of 2016 was rather weak for the company with revenue falling to 1.5% over last year, primarily driven by lower volumes. Higher sourcing costs hit gross profit as coffee prices have risen materially over the last year (gross profit per kilo down 4%). However, good control of operating costs brought EBITDA to a largely unchanged level from last year (EUR 22m). The recently acquired Nutricafe's contribution to EBITDA was about EUR 3m. Net debt is up over last year (EUR 220m at year end) following the acquisition of Portuguese coffee leader Nutricafe and the minority stake in Canadian Club Coffee. Guidance for 2017 points to volume growth of 2-4%, EBITDA up 10-12% and net debt below EUR 210m. The company has been hit by higher coffee prices in the short term, but we continue to see outsized opportunities for operating cost-cutting to increase margins in the mid-term. Also, the product mix shift towards the single serve segment will positively impact the margin picture. Mid-term free cash flow yield is potentially above 10% at current levels which is substantially higher than the peer group.

Fact

In Q416, the group reported revenues of EUR 247m down 1.5% over last year. Total volume for the group decreased by 1.3%. EBITDA was EUR 22m, unchanged from last year.

Key earnings releases and corporate news, February 2017 (cont.)

Jenoptik (1.9% weight)

Investment case update

German-based Jenoptik has a leading position in precision optics, traffic monitoring, new laser technologies, production measurement and individual applications in the military and civil vehicle and aircraft equipment. The company reported prel. Q4/FY16 numbers where Q4 sales increased 5% YoY, as revenue growth came from all segments. Higher demand, among other things, from the areas of energy and sensor systems, optical systems as well as laser machines drove sales. Profitability for Q4 increased 24% YoY contributing to a very solid result for the full year, driving full-year EBIT above the top range of earlier guidance. EBIT margin came in at 10% vs. full year guidance of 9-9.5%. The increase in profitability was mostly due to a favourable mix with a greater contribution coming from the Optics and Life Science segment. Following the strong order intake in 3Q, order intake increased 15% YoY in Q4, and 14% for the full year – in fact, orders were even stronger than that, but due to the long duration the orders were only partially booked. The company benefits particularly from major project orders within Defence & Civil Systems and Traffic Safety. Jenoptik continues to deliver solid free cash flow, which by year end resulted in a net cash position for the company. Our position in the stock has been reduced during recent months into strength, as solid fundamentals start to get priced in.

Fact

Jenoptik released prel. Q4/FY16 numbers. In Q4 sales came in above EUR 190m, a YoY increase of 5%. EBIT increased 24% YoY to a level of above EUR 21. The company ended the year with a net cash position of EUR 18m, following a year of strong free cash flow generation. Jenoptik achieved Q416 order intake of more than EUR 182m (15%) and FY16 order intake of more than EUR 730m (14% YoY).

AIG (7.1% weight)

Investment case update

The US multi-line insurer was bailed out by the US government following the financial crisis and has since then started a transformation process aiming at reaching peer-group profitability and exiting non-core assets. The company swung to a net loss in Q416 as a substantial reserve charge of USD 5.6bn was taken. The reserve charge covers the majority of the US long-tail lines reserved for accident years 2015 and prior. The charge was taken in relation to a retroactive reinsurance agreement with Berkshire Hathaway which should reduce concerns regarding AIG's US long-tail commercial reserve adequacy going forward, which has acted as an overhang in the stock. Underlying fundamental trends continued to be weak with normalised ROE of 4.8% vs. 6.6% a year ago. The company also lowered its 2017 return on equity target to 9.5% from 10.0%. The company reaffirmed its commitment to return USD 25bn to shareholders, but cautioned that actions from regulators and rating agencies might impact the capital return capacity following the weak results. Shares fell following the announcement, but we think that in a mid-term perspective recent actions will pave the way for a more predictable earnings stream and effectively remove the reserve overhang. Also, considering the weak results, it is not impossible that AIG activist investors including Icahn will renew their push for structural or management changes. The stock is trading at 0.8x book value with continued bright prospects for capital returns, and with a longer term ROE potential in line with the peer group, even in a non-split scenario.

Fact

The company reported a net loss of USD 3.0bn including a USD 5.6bn charge. USD 3.0bn was returned to shareholders in Q416. Book value at the end of the quarter was USD 76.6/share.

Key earnings releases and corporate news, February 2017 (cont.)

Taiheiyo Cement (3.7% weight)

Investment case update

Taiheiyo Cement is the largest cement company in Japan, also with a quite sizable presence in the US (primarily California). The company reported Q3 results with operating profit up 26% YoY, driven by domestic cement sales volume growth, low input costs and profit growth overseas. Given the risk of higher coal prices, which is one of the company's main input costs, management made no change to guidance, which makes Q3 look particularly strong representing 56% of guidance for the second half of the year. Cement sales volumes in Japan fell 3.7% during the last 9 months, but were up 1% in Q3 as demand bottomed out. As plans to build a Mexican border wall are boosting the prospects of builders and material suppliers with exposure to the region, together with cost reductions, positive operating outlook and a substantial share buyback program, the shares have rerated quite rapidly since we initiated the position. Our price target is JPY 495 which equals 8x midterm EV/EBITDA.

Fact

The company reported Q3 sales of JPY 153bn and an operating profit of JPY 22.7bn.

Aryzta (1.2% weight)

Investment case update

Aryzta, the Swiss baker, announced changes in an attempt to seek stability and restore credibility among investors, following its most recent profit warning. The company, now led by their new chairman and former Smurfit Kapa CEO Gary McGann, made 3 announcements in a statement; 1) The company announced that its CEO, CFO and regional US CEO are resigning. The Board will initiate a recruitment process to identify candidates for the roles. As part of the transition, Aryzta has appointed three new members to the Executive Management, all current COOs from the group's main divisions. 2) The company has managed to increase the covenant headroom for their senior debt from 4x net debt/EBITDA from 3.5x, which gives them additional flexibility. 3) The company also stated that it has started talks with its partner Lion Capital regarding a potential sale of Aryzta's 49% stake in Picard, the frozen food business, and to use the proceeds of any disposal to repay debt.

We welcome these announcements, which we believe are very important strategically for the company. Even though Aryzta still has a long way to go in terms of restoring investor confidence, this is a solid start. We believe that Aryzta is a mismanaged company with an underlying, highly cash generative, solid business model. As the capex cycle peak is behind them, FCF going forward looks attractive, offering a double digit yield for the mid-term.

Key earnings releases and corporate news, February 2017 (cont.)

Pilgrim's Pride (1.0% weight)

Investment case update

The company is the largest chicken producer in the US and second largest in Mexico. 80% of sales are in the US, 12% in Mexico and 8% in other geographies. Brazil-based JBS currently owns 77% of the company. In Q416, net sales decreased 3% while adjusted EBITDA margin rose 130 bps over last year. EBITDA rose to USD 172m, up 15% over last year. The sales shortfall may have been impacted by slower than anticipated ramp-up of prepared food plants following earlier production issues. The stock rose sharply following the results. The recently acquired GNP is apparently on track to be integrated and synergies may exceed the original USD 20m expectation. Related Tyson Foods received notice of a formal investigation into possible chicken price collusion and this also remains an overhang in this investment case, although no such notice was announced at this point in time. The market continues to anticipate a sharply negative turn in the chicken cycle, visible through depressed earnings estimates and a high short interest in the stock (40% of the free float is shorted). JBS is about to list its international assets in Q217 where Pilgrim's would represent a significant part of the new company assets. This may pave the way for another wave of corporate structure simplification which may benefit minority shareholders in Pilgrim's. In the meantime, the stock is trading at attractive multiples of 6x EV/EBITDA and 8-9% free cash flow yield.

Fact

Net sales for Q416 were USD 1908m down from USD 1960m from last year (-3%). Adjusted EBITDA rose to USD 172m from USD 150m (+15%) while overall EBITDA margins were 9.0% vs. 7.7% last year.

Whiting Petroleum (2.9% weight)

Investment case update

Whiting Petroleum is an independent E&P company primarily focused on on-shore oil properties in the US and Canada. The company raised capital in early 2015 after the poorly timed acquisition of Kodiak Oil and Gas in late 2014, funded mostly with debt. Following the capital-raise, the company has struggled in the lower oil price environment. Q416 was yet another quarter of net loss for shareholders (USD -83m vs. USD -88m last year). Production declined 24% from last year as the company has sold assets to de-lever its balance sheet. More specifically, the company has closed its USD 375m sale of midstream assets and used proceeds to pay down debt and since the beginning of 2016, the company has sold USD 725m of non-core assets. Net debt/EBITDA is just below 4.0x following this exercise. Production will increase following higher oil prices and updated guidance calls for 25% growth from Q117 to Q417. Overall capital spend will be around USD 1.1bn, which is higher than previously estimated. De-levering of the balance sheet remains key to the investment case and we see further opportunities for asset sales in mid-term. In the mid-term, we continue to see the company as attractively valued, both in relation to its reserve base and its normalised earnings power (5-6x EV/EBITDA).

Fact

The company reported a net loss of USD 83m in the quarter compared to a loss of USD 88m a year ago. The production in the quarter totalled 10.9 MMBOE, 84% crude oil/natural gas liquids, which was a 24% decrease over last year.

The 10 largest companies in SKAGEN Focus



AIG is an international insurance company serving commercial, institutional and individual customers. The company provides property-casualty insurance, life insurance and retirement services. AIG was at the very centre of the financial crisis as the central bank for mortgage insurance – it was bailed out in a USD 180bn bail out. The company has two core insurance holdings: Sun America and Chartis that it intends to keep.



E-MART Inc. operates E-Mart discount stores. The company retails food, clothing, household goods, electronics and other items through several branch stores. Revenue breakdown: E-mart offline 70%, Traders 6% (wholesale), E-Mart mall/online 5%, Hotel 16%, With Me (convenience format/CVS) 3%. Market share 48% in core discount format in South Korea.



Tesoro Corporation refines and markets petroleum products and provides transporting services. The company operates refineries, as well as a network of retail and refuelling stations in the western United States. Tesoro also markets gasoline and diesel fuel to independent marketers and commercial end users.



Brazil-based JBS has transformed itself from a mid-sized local beef producer to the world's largest animal protein processor in just a few years since its IPO in 2007. It is now the world's #1 beef, #2 poultry and #3 pork producer by sales. The company operates in six main segments: JBS USA Beef (40% of sales, US beef processing), Moy Park (14%, UK-based chicken and foodservice provider), Pilgrim's Pride (14%, 2nd largest chicken producer globally; separately listed in the US; PPC US, JBS ownership 75%), JBS Mercosul (13%, Brazil-based beef processing), JBS USA Pork (10%), JBS Foods (9%, prepared foods and poultry processing).



Teva's history can be traced back to Jerusalem in the 1930s. Today Teva is the world's largest producer of drugs that have gone off-patent. HQ in Israel; presence in 60 countries; 45k employees. Teva's strategy is to focus on 1) Central nervous system (CNS) 2) Respiratory system and 3) Improved versions of existing drugs (not just Teva drugs) and 4) Production of biosimilar drugs. In July 2016, The US Federal Trade Commission granted Teva approval for the acquisition of Allergan's generics business (Actavis).

The 10 largest companies in SKAGEN Focus (cont.)



Telecom Italia S.p.A., through subsidiaries, offers fixed line and mobile telephone and data transmission services in Italy and abroad. Telecom Italia is a former state telecommunications monopoly. The company has two main operations: Domestic telecom (75% of revenues) and a majority stake in TIM Participacoes (25% of revenues, 67% owned), Brazil's second largest mobile operator.



Japan-based Softbank is a telecom and internet conglomerate. The company's main assets are 1) the Chinese online giant Alibaba Group (32% holding). Alibaba is the leading online commerce platform in China, active both in retail and wholesale; 2) US-based telecom operator Sprint (80% ownership) which provides wireless services in the US and is the third largest wireless network operator after Verizon and AT&T; and 3) domestic telecoms (mainly Softbank Mobile, third largest telco in Japan after KDDI and NTT Docomo).



Japanese company established in 1999 as an online financial services company, incubation arm of Softbank. Acquired E*Trade Securities in 2003, Softbank sold out in 2006. Three main businesses: i) Financial services; ii) Asset management, iii) Biotech Financial services. Building an ecosystem to offer full range of financial services: SBI Securities: Dominant provider of online securities services in Japan, #3 in new tax-saving NISA behind Nomura and Daiwa. SBI Sumishin Net Bank: pure-play internet bank. Also active within insurance (Life & Non-life), Mortgages (through securitisation), trading system and FX trading.



Largest cement company in Japan and 13th largest globally with approximately 40m tons total capacity (about 60% in Japan). Japanese cement market is an oligopoly with three players following consolidation. Geographic revenue mix: Japan 80%, US 15%, Other 5% (Singapore, Vietnam, HK, Philippines, Australia). Segment revenue mix: Cement 65%, Mineral resources 10%, Environmental business 8%, Construction materials 10%, Other 7%); private/public 50/50. Integrated with minerals business providing large part of internal raw material needs.



Philips Lighting was spun off from Royal Philips and is the global market leader in the c. EUR 70bn lighting industry. Total sales of EUR 7.5bn roughly split between 43% LED / 57% Conventional lighting (2015). Industry in the midst of a technology transition in which traditional lamps are being replaced by LED. As a result LED share of sales will be more than 50% in 2016. Business model is also changing from in-house production selling to distributors (old lamps) towards outsourced production and direct solution selling which includes professional services and long-term contracts.

Gold Fields Ltd (GFI SJ) ZAR 46



History, what they do and how case was found

Gold Fields Ltd is one of the world's largest gold exploration companies with total production capacity of 2.2m ounces and reserves of 50m ounces. The company was formed in 1998 with assets from Gold Fields and gold assets from Glencore. The company is headquartered in South Africa, but the bulk of the assets are located outside of South Africa, in Australia (50%), South America (7%) and West Africa (35%). The one asset in South Africa is South Deep, which is one of the largest gold reserves in the world. The company currently operates with an AISC/ounce of USD 960.

ESG - The company has historically had issues with safety in South African mines, but these are relatively minor compared to the other operators in South Africa. Most South African assets and attached potential liabilities were spun off into Sibanye Gold (SGL SJ) in 2013.

Rationale for investment

- The market perception of reserve life is fairly pessimistic, especially with regard to the Australian asset base. We think the market may underestimate the potential for reserve conversions in the mid-term.
- The asset in South Africa, South Deep, may be at an inflection point and is currently valued at an implicit negative value. Most of the major investments have been made in this asset and expectations of production guidance may be too depressed.
- The stock is trading at the same depressed valuation (3x EV/EBITDA at steady state gold price) as the other South African operators despite the fact that the asset base is located outside South Africa. South African assets are in general plagued by wage inflation and other cost pressures.
- Strong balance sheet with potential to move into net cash position beyond 2019.

Potential triggers

- Improvement in mine life extensions through reserve conversions beyond current market expectations.
- Better than anticipated development in the South African mine South Deep, which may reverse the current negative implied value in the stock price attached to this asset at current stock valuation.
- Corporate restructuring – a change of domicile and listing of the company's shares (Australia would be logical) could help reduce the unjustified valuation discount to other non-South African operators (NCM AU, EVN AU).

Risks

- Exposure to gold price (operations are more or less unhedged)
- Potential technical difficulties in extracting potential of South Deep resulting in production disappointments
- Stronger AUD vs. USD since over half of the production is located in Australia
- Higher than estimated capital expenditure in the mid-term

Target price

We set a target price of ZAR 84 which is 5x EV/EBITDA, which still represents a discount to other non-South African domiciled operators.

KEY FIGURES:		
Market cap	ZAR	38.9bn
	USD	2.9bn
EV/EBITDA 17E		3.5x
P/E 17E		11x
Net debt / EBITDA		0.9x
EV/sales		1.5x
Owners:		
Blackrock		12.3%
Investec		8.9%
State Street		6.2%
Vanguard		3.5%



www.goldfields.co.za

3U addition to fact sheet

Unpopular

- The gold price actually hit a peak in 2011 at about USD 1900/ounce and has since been more or less on a downtrend trend which has created a general lack of interest in the sector. The stock fell over 55% from mid-summer 2016.

Under-researched

- The company's asset base is not well understood as the main assets are located outside South Africa, despite its domicile. Analysts seem to take an overly pessimistic view of reserve life in the Australian asset base and the South Deep longer term potential.

Under-valued

- The stock is currently trading at 3x EV/EBITDA which is a major discount to fair value and to the peer group outside South Africa. We set a target of 5x EV/EBITDA which seems like a reasonable valuation considering current earnings power.

For more information please visit:

Our latest [Market report](#)
Information on [SKAGEN Focus A](#) on our web pages

Unless otherwise stated, performance data relates to class A units and is net of fees.

Historical returns are no guarantee for future returns. Future returns will depend, inter alia, on market developments, the fund manager's skill, the fund's risk profile and subscription and management fees. The return may become negative as a result of negative price developments. KIIDs and Prospectuses for all funds can be found on our website.

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