

TM Cerno Global Leaders

UCITS Global Equity Portfolio (Class A)

Q4 2018



Investment Objectives

TM Cerno Global Leaders invests in global companies with sustainable competitive advantages delivering above average returns. Its target is to deliver performance in excess of MSCI World Total Return (GBP) on a 3 year rolling basis. The fund will hold 25-30 securities, equally weighted, selected according to a distinct investment thesis that accents industry structure, the sustenance of return on capital and secular growth. The fund does not invest in banks, commodity, fossil fuel or tobacco companies. The portfolio is fully invested at all times.

Fund Data

NAV/Share (Class A Acc)	£9.46
Fund Size (£mn)	56.5
Strategy Assets (£mn)	82.1*
Currency Share Class	GBP (Base)
Investment Management Charge	0.65%
Ongoing Charges Figure	0.94%**
Dealing Frequency	Daily
Legal Structure	OEIC (UCITS)
Number of Holdings	27
Active Share	96%
Lead Manager	James Spence
Inception Date Fund	2017
Inception Date Strategy	2014
Performance Jan 18 - Dec 18	-5.2%
Performance Since Inception	-5.4%

*Includes all assets within the fund as well as other Cerno managed assets invested directly in to this strategy

**OCF includes the Investment Management Charge

Invention

In this quarterly we consider the importance of invention and adaption in the context of long- term equity ownership. They are perhaps two sides of the same coin.

One of the pleasures of 2018 was reading Simon Winchester's new book "Exactly". The book is subtitled "How Precision Engineers Created the Modern World". Many of the detailed corporate histories described within are connected to, or more directly are progenitors of companies we hold within the Global Leaders strategy.

The modern world immediately makes one think of the 20th Century but in truth is a much longer span of time that began in the very early decades of the 19th Century. That period: 1820-1880 was a rich time for invention, particularly within the newly united Kingdom. For example, James Watt had already drafted designs for the steam engine in Glasgow but then joined up with John Wilkinson in London in 1775. Watt's designs were a break-through but he could not practically make them work in his Soho workshop due to cylinder failures until Wilkinson offered his pioneering metal boring techniques to construct a cylinder that could withstand steam under pressure. From this workshop sprang the engines which powered the world.

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Invention

In other cases, an ardent technologist needed the company or a skilled salesperson: most notably in the case of the coupling of Charles Rolls with the engineer Henry Royce. High quality motor-vehicles were the sole province of small-scale French marques until Rolls Royce entered the business by reverse engineering and then redesigning every aspect of the car.

There also features a very striking anecdote about Japanese wristwatch manufacturer, Seiko. The company, which had been founded in 1881 invented the quartz watch – a revolutionary departure from mechanical watches which it and every other manufacturer had assembled hitherto. The quartz watch was a runaway technology and signalled the demise of the firm’s traditional watch assembly techniques. The traditional watch line was duly closed although the commitment to service extant watches was retained. However, after a few years, the company



Exactly: How Precision Engineers Created the Modern World
Source: *The Times*

acknowledged that in doing so, something special has been lost and the skilled watchmakers were hired back by Seiko in the 1980s and the traditional workshops were reopened, having been mothballed. Today, they carry on in the same facility where quartz wristwatches are made: but at a fraction of quartz output and high prices to match.

What every anecdote seems to relate is the marshalling of human curiosity to push the boundaries of available technology, stories that are replicated in many of the portfolio’s holdings. Examples within the portfolio include Rockwell (read more on Rockwell below) which is a leader in factory process and monitoring systems, TSMC the global leader in semiconductor foundry, Renishaw the designer of precision engineering tools that is essential in the miniaturisation of technology hardware and Ansys who lead the world in the creation of prototypes via software rather than physical construction.

- James Spence

**SIMON
WINCHESTER**

EXACTLY

**HOW
PRECISION
ENGINEERS
CREATED
THE
MODERN
WORLD**

'A REAL TREAT'
NEW YORK TIMES

*'AN
ENTERTAINING
READ'*
SUNDAY TIMES

*'AN
EXTRAORDINARY
PROPULSIVE RIDE'*
*WALL STREET
JOURNAL*

*'MESMERISING
AND FASCINATING'*
*NEW YORK
JOURNAL OF BOOKS*

SHORTLISTED FOR THE ROYAL SCIENCE BOOK PRIZE

Exactly: How Precision Engineers Created the Modern World
Source: *Simon Winchester*

Adaption

Adaption is a crucial quality for companies within the Global Leaders portfolio. Our approach is to access returns on a multi-year view through superior stock selection and limited turnover. To achieve this means owning leading companies capable of compounding earnings both through building upon existing sources of revenue, and through adding new, productive streams of income. This is no mean feat for a business. Maintaining a competitive edge in the current market place while simultaneously striving to be a driver, not a passive consumer, of disruption amounts to a form of corporate cognitive dissonance. To maintain, and increase, their relevance over time adaption must be built in to the institutional fabric of a company.

In 1885, the three Johnson brothers of JnJ were inspired to go into business after hearing a speech by antiseptic advocate Joseph Lister, in 1885. Certainly, the company's initial focus, surgical dressings and sanitary products, suggests some truth to this original story. From this narrow, initial base one of the world's largest, most diverse consumer facing companies was born. From the invention of the Band-Aid in 1920, to the purchase of Janssen Pharmaceutica in 1961 and Acuvue's pioneering of disposable contact lenses, JnJ has achieved growth in attractive adjacent spaces through both organic innovation and selective M&A.

However, a balance must be struck: portfolio breadth versus product relevance. Companies which grow in this way sometimes slide into mediocre conglomerate status with the inevitable discount for inefficiency attributed by the market. This is where JnJ has excelled. As a result of its unusual, decentralised organisational structure, innovation is fostered, but so is active portfolio management. Beyond the need to hit certain financial targets its 200 business units can manage in the way each sees best. Importantly however products must be either global market #1 or #2 or be on course to achieve this position, otherwise they are disposed of. This is enforced adaption. Currently some 75% of JnJ portfolio ranks #1 or 2 in their respective market places.

Another company that has achieved adaptation through its long corporate history is Rockwell Automation, which began life in 1903 making industrial componentry including rheostats and compression motor controllers under the Allan-Bradley name after founders Dr. Stanton Allen & Lynde Bradley. For the better

art of the century hardware remained its core competency and the company maintained strong R&D discipline even through 1929 Great Depression. In the 1970s, Rockwell's engineer Odo Josef Struger pioneered the programmable logic controller (PLC), a type of digital computer used on industrial machinery and assembly lines for relay, motion, process and network control, replacing the conventional relays and closed-loop controllers that were expensive and cumbersome to update and replace.

Rockwell was also very early to recognise the importance of IT in an industrial context, having launched its first software system in 1994, and introduced the signature Logix platform in 2007 that is uniquely capable of combining discrete and process automation procedures onto a single platform. The Connected Enterprise initiatives to converging information technology with operational technology arrived at an opportune time when data and analytics are ever more mission critical in the age of digitisation to drive manufacturing efficiencies and productivity. Today, software represents an integral part of Rockwell's business, accounting for 45% of group sales, alongside its hardware division under the original Allan-Bradley brand, which just had its 115th anniversary.

- James Spence

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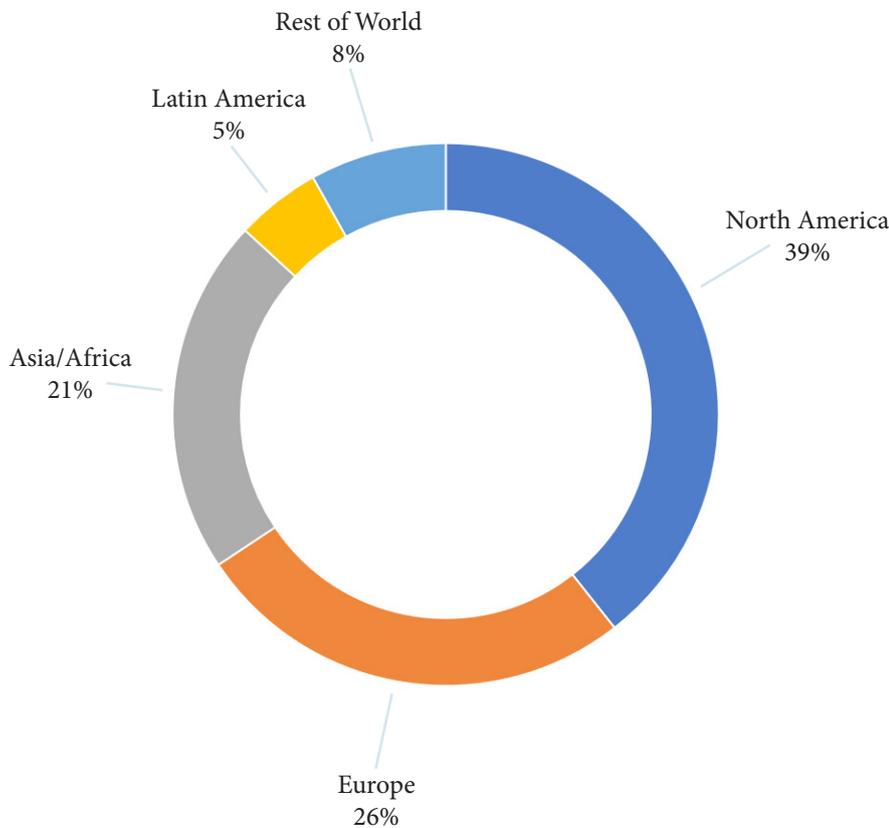
Holding History

Company Name	Description	Holding Period*
Samsung Electronics	Dominant in semiconductor memory chips and leader in smartphones	>5 years
Nestle	Diversified global food & beverage company	>5 years
Visa	Largest global electronic payments network	>5 years
Zimmer Biomet	Leading orthopaedic care specialist	>4 years
Linde	Largest industrial gas provider in the World	>4 years
Renishaw	Engineering specialist focused on equipment for precision measurement	>4 years
Johnson & Johnson	Global healthcare company spanning pharma, medical devices, consumer	>4 years
Fedex	Leading provider of Express Delivery services in the US	>4 years
PPG	Coatings company leading in the industrial/specialty business	>4 years
Sonova	Largest global producer of hearing instruments	>4 years
Reckitt Benckiser	Innovative leader in consumer health, hygiene and home products	>3 years
Coloplast	Global healthcare provider focused on ostomy and continence care	>3 years
Shimano	Dominant supplier of cycling componentry	>3 years
Givaudan	Leading player in the Flavours and Fragrance industry	>3 years
Novozymes	Produces enzymes which application in a wide variety of daily products	>3 years
Assa Abloy	World's leading manufacturer of security locks and automatic doors	>3 years
LVMH	The largest luxury goods conglomerate and most diversified	>2 years
Rockwell Automation	Largest pure play in industrial automation and control processes	>2 years
Luxottica	Vertically integrated producer of luxury, fashion and sports eyewear	>2 years
Oracle	The largest database and enterprise software company in the world	>1 year
Ansys	Leading developer of digital simulation software for product development	>1 year
Fresenius Medical	The foremost player in dialysis care active along the entire value chain	>1 year
3M	Manufacturer with leading brands in industrial and consumer products	>1 year
Waters	World leader in specialty measurements focused on the life sciences sector	>1 year
Heineken	Brewer with a strategic bias to premium beer, interests in low alcohol/craft	>1 year
Atlas Copco	Dominant producer in air compression and vacuum techniques	>1 year
TSMC	World's largest pure-play semiconductor foundry	<1 year

**Holding periods relate to the entirety of the strategy within Cerno Managed Assets*

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Sales by Geography and Valuations



Global Leader companies are, by definition, global in their sales. Their domiciles are not an investment consideration and most of the companies have outgrown their home market base many decades ago.

The perceived reliability of the earnings of constituent companies and the fact that they have commanding market shares in their industries means that they will trade at a premium to wide equity market aggregates. The question is how much? The portfolio has an aggregate Return on Equity of 23.1% versus 13% for the World Equity Index.

We aim to rationalise margins, earnings consistency and economic value against the price paid. The fund's approach to valuation could be described as growth at a reasonable price (GARP).

Characteristics	Global Leaders*	S&P 500	MSCI World
Price/Earnings (1Y Forward, x)	18.4	13.5	12.7
Return on Equity (%)	22.8	16	13.4
Return on/Cost of Capital (%)	1.3	N/A	N/A
Gross Margin (%)	54.6	33.9	31.5
Operating Margin (%)	22.7	13.4	12.1
Net Debt/Equity (%)	20.2	62.1**	45.3**
Dividend Yield (%)	2.1	2.4	3.0

* This data refers to the underlying holdings
 **ex financials

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Key Fund Information

Investment Objective	Returns in excess of MSCI World Equity Index (TR) on a three-year rolling basis
Sector Exclusions	Banks, Fossil Fuels, Commodities, Tobacco, Armaments
Savings Structures	Suitable for SIPPs and ISAs
Key Fund Documents	https://cernocapital.com/tm-cerno-global-leaders
Counterparties	Authorised Corporate Director: Thesis Unit Trust Management Trustee: NatWest Trustees Custodian: Northern Trust Auditor: Grant Thornton UK LLP
Contact	Tom Milnes 0207 036 4126 tom@cernocapital.com

Fund Codes

	ISIN:	SEDOL:	Bloomberg:
A Acc	GB00BF00QK62	BF00QK6	TMCGLAA LN
A Inc	GB00BF00QJ57	BF00QJ5	TMCGLAI LN



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