CRUX ASSET MANAGEMENT

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This is a Marketing Communication

TM CRUX European Special Situations Fund

Fund highlights:

- Areas of shareholder value creation to Michelin's top 100 managers
- Findings from a meeting with Europe's largest company (Novo Nordisk)
- A proprietary survey on pest pressure in hot and cold States (Rentokil)
- Our new investment in Whitbread

Fund Overview

The fund was up 1.1% in the quarter, outperforming the IA Europe ex UK Sector benchmark which fell -2.2%.

Risk assets broadly retreated in Q3 as real government bond yields rallied to decade highs due to a combination of upward revisions to the pathway of policy rates and rising term premia. Conclusive evidence of a rapid slowdown in the US economy didn't materialise in the period and we use the Macro section to discuss the implications of academic research into the efficacy of fiscal activism, the likely protagonist, as well as update our analysis on whole economy and sovereign debt dynamics.

The top performers in the quarter were Shell, Michelin, Novo Nordisk, Sanofi and Linde with each generating alpha of over 20bps. Key detractors were KBC, Compass, Richemont, Iberdrola and Halma.

Shell rallied in Q3 as oil prices rose in response to further supply side curtailments. It also outperformed the direct peer group as the new CEO committed to greater focus on capex productivity (-$3bn p.a. in 2024 and 2025), operational efficiency (-$2-3bn by 2025) and higher shareholder returns (40-50% of cash flow). Debt has been reduced from $75bn to $40bn since 2020 enabling the capacity to return 35% of its market cap to shareholders in the next 3 years, we believe.

Michelin rose by 7% tracking positive revisions to consensus for group EBIT. Despite raw material pressures abating, pricing has remained firm allowing margins to re-expand reflecting the favourable terms of trade. We were invited to present our perspectives on company strategy to Michelin's top 100 global managers in Lyon during the quarter, which we discuss in more detail later in the letter. We came away feeling positive about management intent to achieve excellence, not just in the traditional group strengths in science/engineering and product quality, but also in manufacturing efficiency and capital allocation.

Novo Nordisk's share price increased c.20% in Q3 following the favourable headline results of the SELECT cardiovascular outcomes trial for semaglutide. The trial achieved its primary objective demonstrating a reduction in major adverse cardiovascular events (MACE) of 20% with all three subcomponents contributing. We had provided the company with our due diligence work including a proprietary survey of 1,000 affluent obese US adults, and subsequently met with Novo's CEO in Denmark during the quarter. The degree of remaining innovation runway is the determinant of whether Novo can be a perpetual franchise rather than a super but time-limited concession and we also discuss our findings in this regard later in the letter.

Finally, both Sanofi and Linde additionally made strong contributions this quarter following upbeat management commentary and upwardly revised full year financial guidance.

KBC was the largest detractor as the ECB's TRIM review of European banks resulted in a risk-weight add-on of €7bn for the group. The supervisory authority appears minded to increase capital requirements for all European banks, potentially in response to the US regional crisis, and we do not think it specific to KBC. Basel 4 is likely to represent a further step back from the use of advanced models although we would still expect RWA inflation to be limited to c.5% for KBC. Perversely, the pathway upon which seemingly the ECB are embarked could have the unintended consequence of incentivising riskier behaviour given the lack of discrimination in capital requirements of the standardised approach towards which regulation is reverting. Inclusive of all prospective add-ons, we still think that KBC retains its position as being amongst the most capital rich (c.15% CET1) and cash generative (250bps CET1 p.a.) banks in Europe, trading on a P/E of only 10x and returning 8% p.a. to shareholders.

Compass, Iberdrola and Halma all fell during the quarter due to bond yield pressure given an absence of any negative new company-specific developments. Due to compounding of continued strong earnings growth, the effect of share price weakness is a de-rating that has already been extensive with Halma now trading on calendar 2024 P/E of 23x versus prior peak of 31x. For a total annual shareholder return of 14%, comprised of cash flow growth and distributions, we think the share looks cheap. Similarly, Compass is now trading on a P/E of 21x for organic revenue growth of 7% and total shareholder return of 15% p.a. including dividends and buybacks, which we also think is far more attractive than the market.

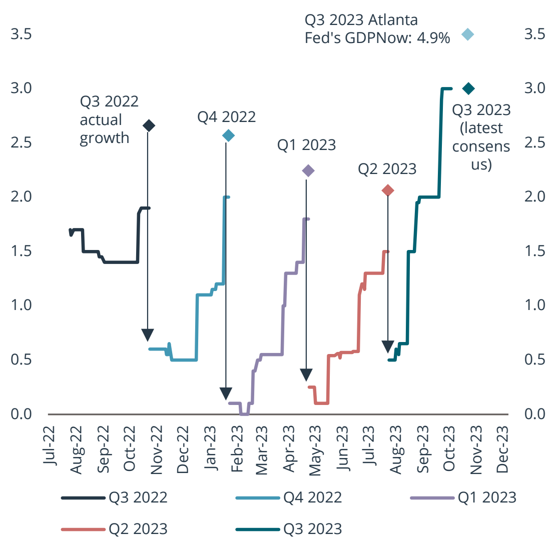
This point can be extended more broadly with the 1 year forward P/E of the fund now only 12.8x approaching the lowest multiple in over a 10 year history and its premium to the market having almost gone. This despite the fund embedding diversified exposure to 10 disparate structural growth tailwinds for whose optionality no significant value is currently attached. The IRR of the portfolio is also now 11%, which we would argue is a substantial safety margin in terms of equity risk premium over government bonds whether Treasuries stabilise at 3% or even 6%.

After a discussion of recent Macro developments below, we then go on to detail work conducted on four holdings of the fund; Michelin, Rentokil, Whitbread and Novo Nordisk. This includes insights from a) a proprietary survey by the team to assess consumer propensity to outsource pest control in the US, b) a presentation of our perspectives on shareholder value creation to the top 100 managers of Michelin, c) a recent meeting with the CEO of Europe's largest company, Novo at their Copenhagen HQ as part of our due diligence and d) a discussion with the management of Whitbread, our newest position, to review its processes for assessment of local market supply and demand dynamics that inform their decision making with respect to capital allocation.

Macro

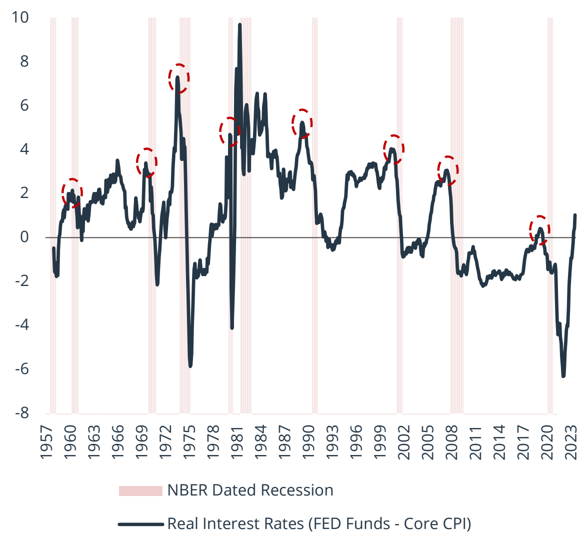
Macro forecasts for the US economy this year have been repeatedly upgraded as growth has proven better than anticipated. Rate sensitivity of the private sector appears to have declined due to the mitigating benefits of excess consumer savings and the move post the GFC away from short-term variable-rate liabilities.

US Economic Activity: Continuously Surprised in 2023
Consensus GDP Growth Evolution (% QoQ SAAR)



Note: Actual growth marked on the day of first release

Real Rates: Termed Liabilities Raises Short Run R*
Federal Funds Rate – Core CPI, %



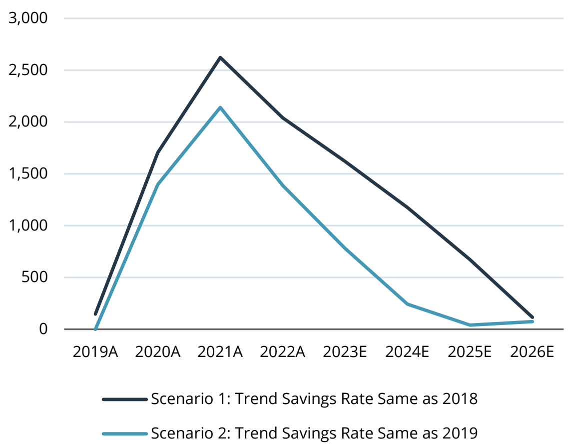
Source: J.P. Morgan

Potentially explaining some of this strength, the Bureau of Economic Analysis has recently made substantive revisions to the historical data which suggests that the pre-Covid savings rate was 6.4% in 2018 and 7.4% in 2019 or about 1.3% lower in each year than thought previously. Under the assumption that the current rate of savings (c.4%) still converges over time with its prior trend rate (6.4-7.4%), but with that trend rate having now been revised downwards (from c.8-9%), excess US household savings may be larger than previously estimated by about $700-1,000bn.

Nevertheless, it is still the case that the current annual savings rate is well below pre-covid trend and to return to normal would require a period of slower consumption expenditure going forward.

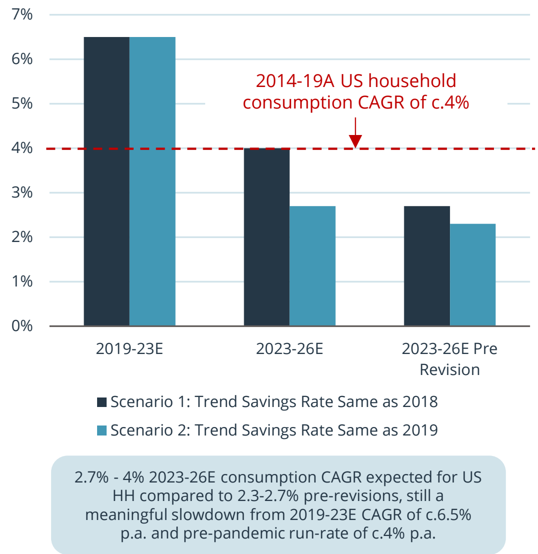
To illustrate this point, even if wage inflation were to remain elevated at 5% p.a., households could only afford consumption growth of c.3% in 2024 compared to 13%, 9% and 6% in 2021-23 if normalising to the trend savings rate.

US Household Savings: Eroding From A Higher Level
Estimated Excess* US Household Savings, $bn



*Defined as accumulated savings vs pre-pandemic savings rate
Source: BEA, Lansdowne analysis

US Household Consumption: Muted Growth Likely
Estimated US Household Consumption Growth* , %



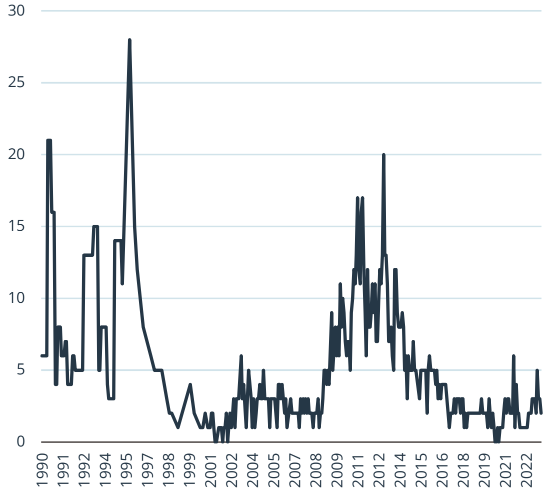
*Assuming 4% Future Personal Income Growth, in-line with pre-mid-cycle pandemic levels
Source: BEA, Lansdowne analysis

With wage growth thus likely to run ahead of consumption expenditure, corporate profitability is set to be squeezed next year. As consumption slows, so too, at least cyclically, should inflation but real yields are already at 2% and would consequently rise further. It is especially difficult for central banks to act pre-emptively this cycle without sufficiently compelling evidence of a downturn so we see a risk that policy rates may remain too high for too long.

Given the surprising strength in the economy this year, we should however also explore the most likely way this thesis may prove an inadequate representation of reality. The expectation of a slowdown in household consumption expenditure is predicated upon the assumption that personal savings rates will rise back up to the pre-covid level, but of course they may not. The savings rate has risen in each month of 2023 on a SAAR basis but still might not fully normalise should households now believe that fiscal transfers would be extremely generous in any future downturn, as they were in response to the pandemic.

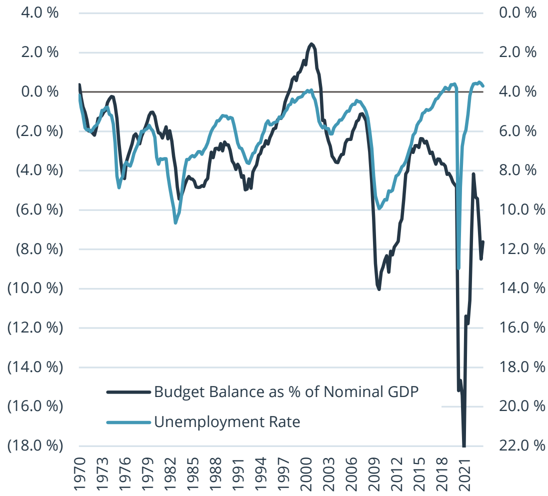
Indeed, the public does not see the level of Federal debt or budget deficit as the major concern right now as per survey results illustrated in the chart below. This is reflected by the advocacy for greater fiscal activism of both Biden and Trump, the two candidates leading in the Presidential polls. But while households may think the political willpower exists, the financial markets still determine the affordability of such policy (at least for now) with the deficit already at an elevated level that has rarely been seen in history at points of similarly low unemployment as today.

US Survey: Federal Debt & Deficit Not Seen As Major Issue
% Saying Federal Debt/Deficit "Most Important Problem"



Source: Gallup, Goldman Sachs. Data as at August 2023

US Budget Deficit: High For Current Low Unemployment
US Budget Balance (LHS, %) vs Unemployment (RHS, %)

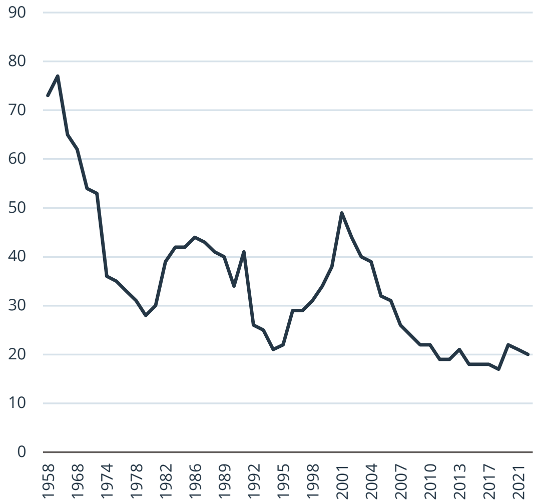


Source: Bloomberg, Lansdowne analysis. Data as at September 2023

Capital markets would presumably make the funding cost of further fiscal stimulus pecuniary without conviction as to it yielding a return on investment. The academic literature is very equivocal in this regard. Six out of seven major studies published since 2001 identify a significant negative correlation between government size in the economy and economic growth in developed countries. Indeed, the Armey curve describes how the initial expansion of the state, from property rights to health and education has a positive effect before a tipping point is reached where marginal government spending becomes negatively correlated with faster economic growth in wealthier countries. The Scandinavian model combining higher growth with higher taxes does stand out as an exception, but the literature suggests this is a consequence of atypically high levels of social trust. In contrast, the Pew Research Centre survey of the US shows a reduction of the proportion of the population who mostly trust the government from 75% in the 1960's to 20% of respondents today. The US General Social Survey also shows that the degree of interpersonal trust in the US has also declined rapidly over the same time period.

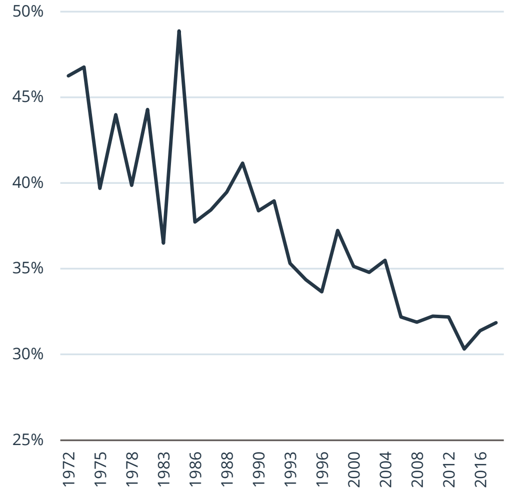
So far, we have therefore not found the evidence that households can safely replace personal savings with reliance on fiscal transfers to be overwhelmingly compelling. The recent sharp increase in bond yields appears empirically to suggest capital markets have not either. Bond investors seem increasingly unwilling to fund the subsidisation of household over-expenditure via further Federal fiscal unorthodoxy so we conclude that it is more likely than not, that savings rates will continue to rise, and the economy to slow.

Trust in US Government: Eroding Over Time
% of US Citizens That Trust In US Government*



Source: Pew Research Centre, Our World In Data. Data as at 2023 *Respondents who said they trust "Always" or "Most of the time"

Interpersonal Trust: Also Eroding Over Time
% of US Citizens That Trust Other US Citizens*



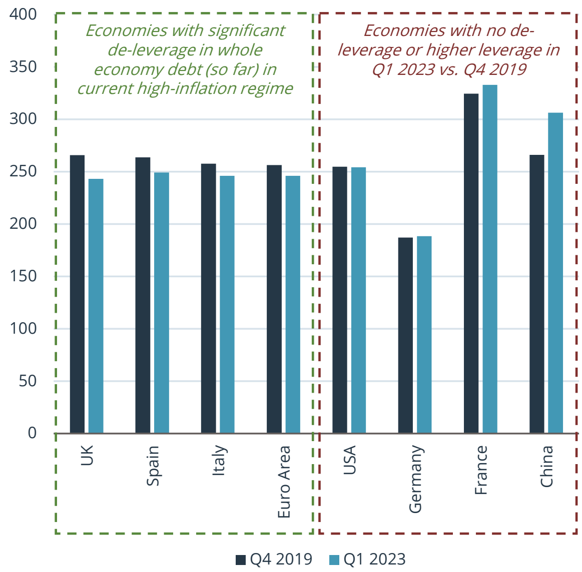
Source: Eurostat, Our World In Data. Data as at 2015 *Respondents who agreed with "Most people can be trusted"

At some point down this path, it does seem possible that policy may evolve to invoke further financial repression, mandating purchases of government debt to secure interest rates below the rate of nominal GDP growth. However, we doubt that such an extreme step would not first require a cyclical downturn as catalyst negating the value of over-positioning for it as this juncture.

Returning now to the subject of whole-economy debt ratios that we have discussed in prior letters, the splurge in inflation has succeeded in inducing a positive inflection down from peak pandemic levels (see chart below). Having updated our analysis of sovereign debt dynamics however, we find that to make further headway is not likely to be that straightforward. This is because nominal GDP growth is now slowing while interest rates have risen. Taking Italy as an example, the required primary budget surplus to stabilise the government debt ratio is +2.7% of GDP at the current spot 7 year interest rate for Italian debt of 4.4%. This compares to this year's primary deficit of -2% of GDP and the 5 year average pre-Covid of +1.5%. A fiscal contraction of about 5% of GDP is thus required to prevent the sovereign debt ratio from rising again, a dynamic similarly faced by most developed economies and something that doesn't feel politically feasible at present.

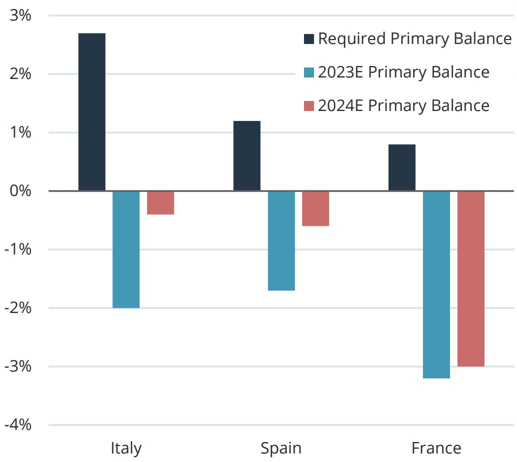
In conclusion, we think elevated interest rates are approaching the zone that increasingly disincentive borrowing for investments that may now yield only marginal returns. Sovereign debt dynamics are not in equilibrium at these levels which likely reduces household confidence in further fiscal transfers. Normalisation of personal savings rates in response to this realisation would pressure corporate profitability and slow economic activity. We have therefore not rushed towards the ‘no landing’ narrative with the portfolio substantively unchanged all year.

Whole Economy Debt Ratios: Now Vs Covid Peak
Total Non-financial Debt/GDP, Q1 2023 vs Q4 2019, %



Source: BIS, Lansdowne analysis

EZ: Spot Rates Incompatible with Debt Sustainability
Required vs. Current Primary Balance*, %



*For stabilising public debt / GDP assuming debt refinanced at spot interest rates, and assuming 2.5% terminal nominal GDP growth for each of Italy, Spain and France
Source: Eurostat, Goldman Sachs, Lansdowne analysis

A slowdown, once discounted, would in many ways be very helpful allowing inflation to recede, policy rates to reset and a new cycle to begin. Given the imprecision in timing such transitions and the elevated uncertainty in terms of policy response, we continue to think our most appropriate focus should remain on fundamental company-level analysis, with factoral balance achieved via position sizing at the aggregate portfolio-level. From a performance perspective, we are hopeful that time is on our side with the P/E of the fund below 13x and offering an IRR of 11% which appears a substantial buffer to risk free rates. At these levels, we are finding some interesting new ideas and have a full pipeline of company due diligence to execute this quarter. By way of a few examples, we hope to do some proprietary consumer survey work on Whitbread’s unique value proposition and visit their properties in Germany, explore the manufacturing barriers to Novo Nordisk generics through discussions with key suppliers, understand perspectives on the Rentokil merger via engagement with the largest unlisted competitor as well as potentially share our views on Michelin with the Group’s supervisory board.

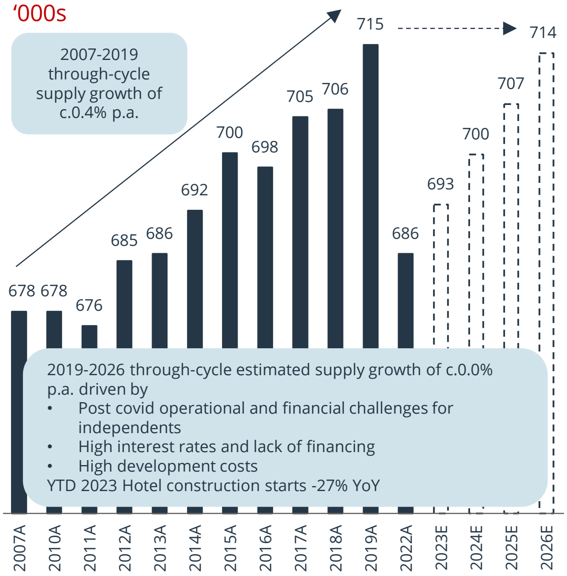
Fund Overview

Whitbread

The only new holding of the fund this year is Whitbread, a low cost producer in a supply-constrained industry in many ways analogous to the investment case for Ryanair. The number of rooms in the total UK hotel industry is not expected to recover to pre-pandemic levels until as far out as 2026.

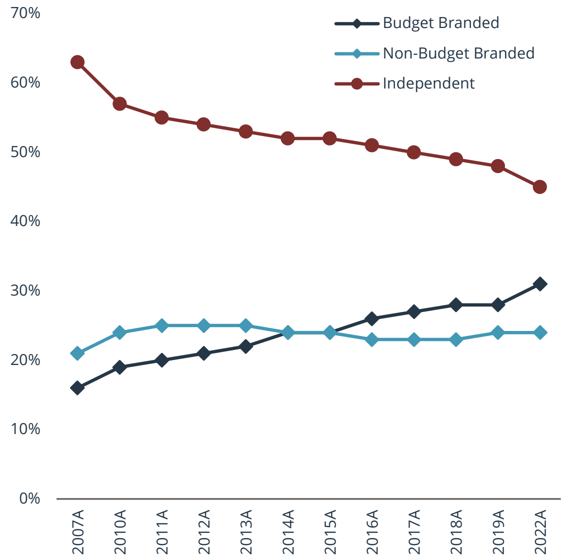
Industry capacity is being severely curtailed at present. Firstly, by the closure of independents due to the accumulation of losses from covid disruptions, ongoing labour shortages and other inflationary pressures. Secondly, due to postponed development pipelines of the established chains that are largely dependent upon leasehold financing that is neither readily available nor sufficiently cheap in the current environment.

UK Hotel Industry: Ltd. Through-Cycle Supply Growth
UK Hotel Supply, Available Room Nights Per Year, '000s



Source: Company Reports, Lansdowne analysis

UK Hotel Supply: Independents Structurally Losing Share
Annual Room Nights, % Share



Source: Company Reports, Lansdowne analysis

Premier Inn, owned by Whitbread, has some unique advantages within its business model that should allow it to continue to grow and take share in this period when its rivals cannot. At its core, Premier Inn's principal strength derives from its superior brand recognition, scale and vertical integration.

Due to much lower customer recognition, a typical independent hotel must pay 5% of revenues to franchise the brand of a well-known chain and pay an additional 10% to online travel agencies such as Booking.com. At the same price point and for the same customer, this means that Premier Inn can generate double the return on capital that is available to a competitor. With a network of 80,000 rooms equating to 20-30% of the UK budget hotel industry, Premier Inn further leverages its size via national-level marketing campaigns, deploying labour across multiple sites and through procurement rebates. Reinvestment in product quality creates a virtuous flywheel of further market share gains that amplify the network effects further.

We think Premier Inn is likely to add c. 2,000 rooms p.a. essentially just filling in for the gap in the market vacated by the contraction of independents. While this would keep the flywheel spinning, it would thus not create additional net capacity at the industry level and at half the pace at which

Premier Inn expanded prior to the pandemic, group ROCE is likely to expand given smaller cross network cannibalisation effects.

Unit Economics: Premier Inn vs Independent Hotel For A New 100 Bed Leasehold Hotel (£m)

£m	Premier Inn UK	Franchised Independent
Revenue	2.5	2.5
- Franchise Fee	-	(0.13)
- OTA charges	-	(0.25)
- Rent	(0.6)	(0.6)
- Other Expenses	(1.2)	(1.2)
PBT	0.7	0.3
Capital Employed	4.8	4.8
Pre-tax ROIC	15%	7%

Assuming REVPAR of c.£70

c.5% average franchise fee from Independent hotels to Brand owners, no cost for PI UK

c.10% typical OTA cost for independent hotels, no charge for PI UK as customer sourcing almost entirely (c.97%) direct

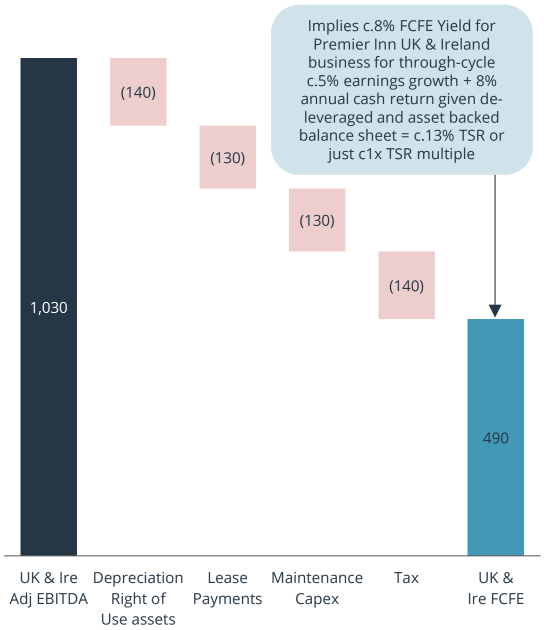
Includes central costs, marketing etc

Capitalised at 8x rent

Premier Inn UK estimated ROIC of c.2x typical franchised independent hotel

Source: Lansdowne analysis

Premier Inn UK: c.8% FCFE Yield for 5%+ Growth FY24E, £m



Source: Lansdowne analysis

Our discussion with the company has focused upon the investment decision making process between capital deployment alternatives, critical in a high fixed cost and long payback industry. Premier Inn has the largest property team in the space and its scale and creditworthiness affords most favoured nation status with developers. The UK is divided for local-level supply/demand analysis into 1,000 catchments with daily occupancy and room rate data available via a third party provider, STR, at a granular level. Here we see a close analogue to Ashtead, where the accessibility of zip code level construction put-in-place data has since the GFC greatly increased transparency and mitigated the risk of poor decisions that could create over-capacity. Premier Inn supplements these inputs with analysis from a group function that assesses room supply in targeted localities themselves to avoid incomplete data coverage, with this in turn fed into with on-the-ground perspectives given the ubiquity of its presence across the UK.

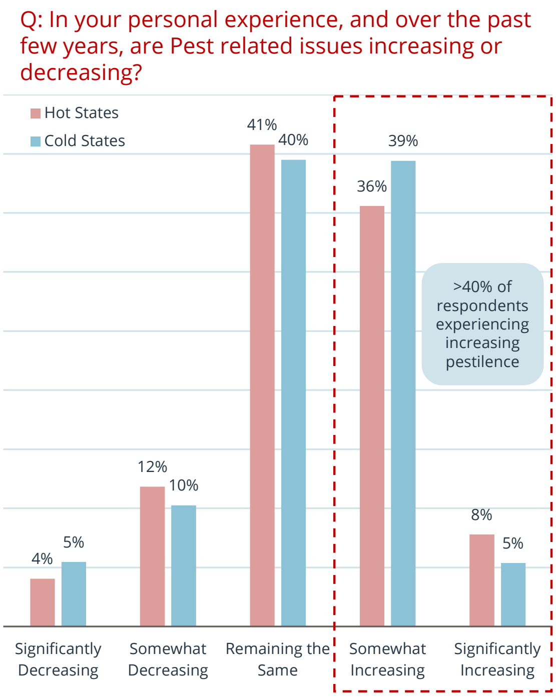
Experience across both the CEO and members of the board at Easyjet feels relevant for the opportunities that Premier Inn may be able to capture, not least with respect to adoption of more sophisticated models for dynamic room pricing. Ultimately, we think the UK business is a low cost producer in a supply-constrained industry that is too cheap for its cash return and growth potential. Subtracting the small German business at 1x capital employed from the current EV, the

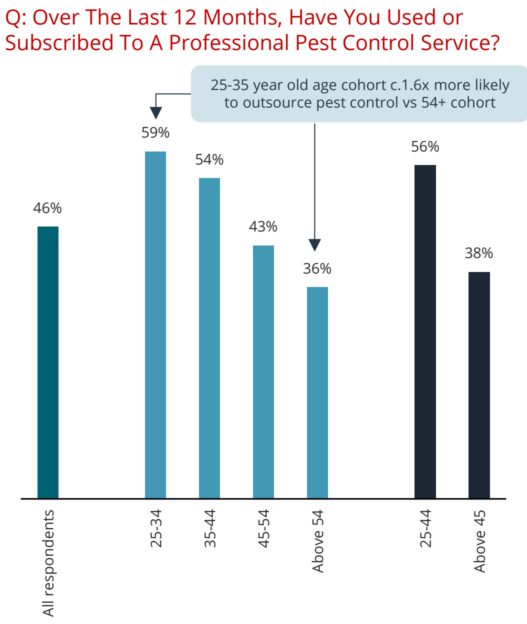
UK franchise is implicitly valued at a FCF yield of 8%, which feels very inexpensive for earnings growth of 5%p.a. and annual cash returns of 8%.

Rentokil

During the quarter we conducted a proprietary survey of 1,000 US citizens to help quantify the size and nature of market opportunity for Rentokil. The evidence is supportive of the thesis that increasing pest pressure is likely to drive demand growth for the company with responses noting both rising pestilence in the States in which the issue is already widespread but also expanding geographic creep into States that traditionally had colder climates and thus less activity. As per the chart below, over 40% of recipients replied that they have experienced greater pest-related problems more recently with less warm regions suffering from this dynamic as much as traditional trouble spots.

An attractive attribute of the pest control industry that we seek exposure to via Rentokil is the sticky, recurrent and relatively economically sensitive cash flow stream from customer contracts. Pleasingly, the survey confirmed these characteristics given that c. 2/3rds of respondents said they are unlikely to change their pest control provider on an annual basis and c. 30% never. Augmenting the opportunity, the survey also demonstrated the potential for market share gains by the outsourced industry from the DIY segment given divergence in generational attitudes with 25-35 year olds having a 1.7x higher propensity to employ a professional provider compared to 54+ year olds.





Q: Over The Last 12 Months, Have You Used or Subscribed To A Professional Pest Control Service?

As previously discussed, the recent acquisition by Rentokil of Terminix propels the group into a leadership position in the US outsourced pest control industry with the top two players alone controlling 50% of the market. We think the survey supports our demand growth assumption of 5% p.a., which in combination with branch synergies implies Rentokil can generate double digit earnings growth through 2026 and a total shareholder return including distributions of 12% p.a for a P/E of 23x. Put differently, the IRR at the current market cap is c. 11% which offers a sizeable equity risk premium to risk free rates for the no.1 player in a cash generative, hard currency, economically resilient business underpinned by regulatory standards, favourable demographic tailwinds and climactic conditions supportive of rising pestilence.

Michelin

The presentation we made to Michelin's 100 most senior managers in Lyon during the quarter gave us a unique opportunity to sense the corporate culture and interact with key personnel.

Michelin has a long-storied history of ground-breaking scientific and engineering innovations including all three of the last century's major inventions; the radial, run-flat and all-weather tire. This is reflected in its consistently superior product performance, strength of brand equity and price premium versus the competition. Despite such an excellent starting position, the total shareholder return in recent decades has not dramatically exceeded the wider European benchmark, that is a CAGR of +8% is good but not great.

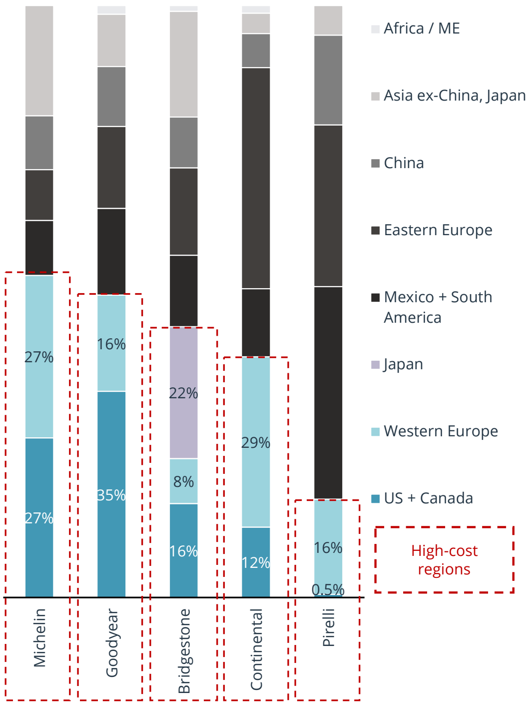
The focus of our presentation was therefore not on the core strengths of the group but rather two other facets of the business, manufacturing productivity and capital allocation, that we believe represent additional levers of substantial value creation.

Michelin's network of production facilities remains overly indexed to small plants in high cost Europe, a consequence of its origins almost two centuries ago when agricultural workers were transitioning to the factory floor and were cheap and non-unionised. Conversely companies such as Continental AG that are much younger were industrialised from the outset operating a much smaller number of very larger plants in lower cost countries.

This disadvantage is rectifiable and indeed Michelin have made some headway with the amount of capacity in low cost countries up from 25% to 35% of total over the last decade. With the impediment to the speed of transition in essence determined by internal corporate culture, we came away positive on recognition of this issue and expect further productivity improvement measures to be forthcoming.

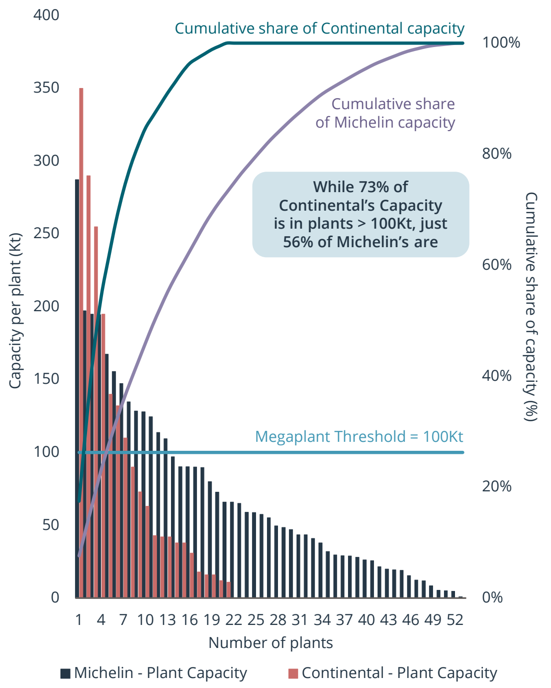
Specifically, this is likely we think to include divestment from the Chinese truck market and further capacity closures in Europe. More fundamentally, we think management understand that value creative M&A is dependent upon a lower cost of capital, which in turn requires demonstration that the core tire business can generate returns in excess of WACC. Footprint productivity is therefore viewed as a key enabler to the group's long term strategy to extract value from its core research and development strengths in areas that lie outside of the current group perimeter to be opened up through acquisitions.

Michelin: Over-Indexed To High Cost Regions
Manufacturer Capacity By Region, %



Source: Tire Business, Lansdowne analysis. Data as at 2022

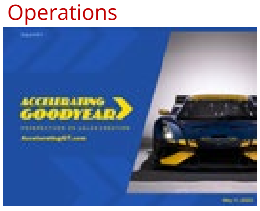
Manufacturing Footprint By Size of Plant
Michelin vs Continental AG



Source: Company Reports, Kepler Cheuvreux. Data as at 2022

The tire industry offers a case study into the criticality of good governance with many of Michelin's principal competitors embroiled in internal disarray. Goodyear is the subject of activist pressure, Pirelli is squeezed between Chinese ownership and a corporatist new Italian government, Continental is siphoning off tire cash flows to absorb conglomerate losses incurred in other divisions while Nokian has lost 80% of its manufacturing capacity as it was located in Russia.

Goodyear: Targeted By Activist Investor Elliott Management Who Seek to Appoint New Directors, Monetize The Retail Store Base and Revamp Operations

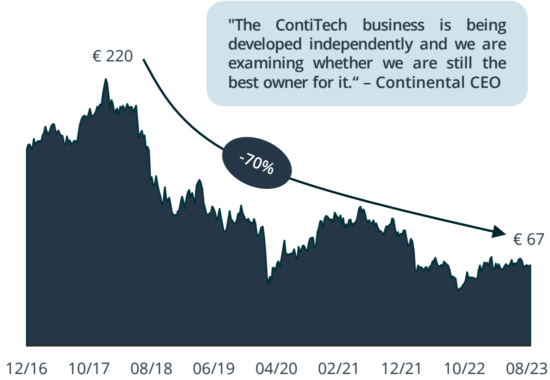


ELLIOTT

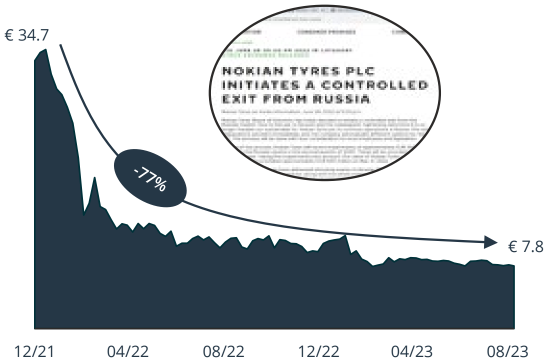
Pirelli: #1 Shareholder Sinochem Blocked by Italian Government From Exercising Right To Appoint CEO Or Set Strategy "To Safeguard Pirelli's Independence"

sinochem
In science we trust

Continental: Share Price Has Fallen and Media Continues To Speculate On The Possibility Of A Group Split



Nokian: Lost 80% of Passenger Tire Manufacturing Capacity That Was Based in Russia Due To The Ukraine War



This leaves Michelin with a compelling window of opportunity to compound its superiority. Inorganic expansion to leverage existing R&D capabilities into a broader span of end markets is likely a core component and we came away feeling that Michelin's approach to M&A resonates with that of Halma, another of our holdings who do this well. Specifically, we are reassured that acquisitions are to be cash funded, in niche and adjacent areas, of businesses that add to the quality not just quantity of earnings and where Michelin already has relevant IP expertise.

The recent acquisition of Flexible Composites Group represents a good start in our opinion, given it combines fast end market growth and low capital intensity with a 40% market share in niche high performance material end-markets (e.g. adventure sports fabrics) in which Michelin can deploy its polymer chemistry expertise.

At 1x invested capital, a P/E of 8x and offering a 5% dividend yield and 5% p.a. earnings growth, we think the risk premium implied in the current share price is well over-stated. It is likely that we will discuss our perspectives with the Group's Supervisory board in coming months which we hope may prove additionally informative as to Michelin's approach to achieving excellence not only in IP but in productivity and capital allocation too. We came away from our last engagement with a degree of optimism in this regard.

Novo Nordisk

Ultimately, the two key determinants of valuation are likely to be the size of the US addressable market for obesity drugs and the ability to maintain this profit pool post expiry of the Wegovy and Cagrisema patents in the 2030's.

Our estimate for the total size of the US GLP1 market is $100bn in 2030 for both diabetes and obesity combined. This is predicated upon approximately 28m people being treated for obesity whereas consensus is closer to 20m.

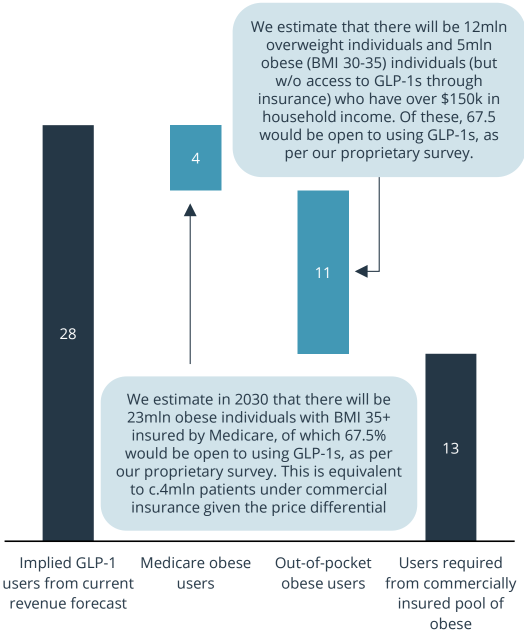
To improve our triangulation, we have conducted a proprietary survey of the US population (1,000 respondents). Of the 20m individuals with a BMI of at least 30 and an annual income of above $150,000, the survey suggests that about 11m are not obese enough to qualify for coverage but would be positively disposed to paying for weight loss treatment with GLP1s out of pocket.

The addressable market is likely to be further expanded via Medicare coverage. The SELECT trial enriches the favourable healthcare economics of GLP1s as it demonstrates efficacy in reduction of related comorbidities such as cardiovascular events. Should coverage extend to obese patients above a BMI threshold of 35 and assuming a price 1/4th that in the commercial market, this would reasonably add another 4m to the addressable patient population.

With 17m patients from the wealthy individual and government-covered cohorts of the population, our overall market size of 28m by 2030 requires a further 15m from the commercially-insured pool of obese but non-diabetic adults.

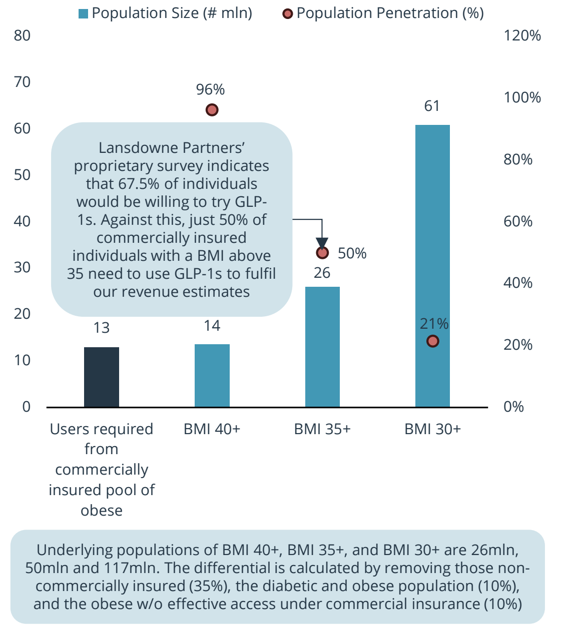
A critical question we discussed with the company is below what level of BMI are corporate healthcare plans likely to limit employee eligibility to access GLP1s. Labour shortages are supportive of greater coverage but the absolute amount of required expenditure is likely a constraint. The chart below shows that even cutting off coverage at a BMI threshold of below 40, i.e. making only those that are severely obese eligible arrives at penetration numbers that are not unfeasible. Unless our stay time assumption for drug usage of 6 months every 6 months is wildly off, we therefore think consensus estimates for peak market size may still prove too conservative.

Modest Commercial Update Drives $100bn Market
Estimated GLP-1 Users By Type, Millions



Source: Lansdowne analysis. Data as at September 2023

Assumed Commercial Uptake: Implies c.50% Penetration
GLP-1 Actual Commercial Users vs Target Cohorts



Source: Lansdowne analysis. Data as at September 2023

Nevertheless, the real issue for shareholder valuation is not the exact peak in revenue but the number of years in which it can be sustained. With patents due to expire within the next 20 years, equity value is considerably more sensitive to the latter rather than the former. The factors that may determine Novo's ability to extend the lifecycle of its obesity concession, and thus make it a franchise, was the central focus of our meeting in Copenhagen with the CEO.

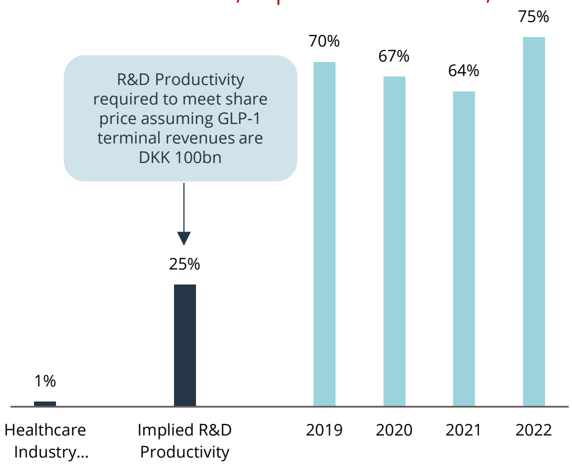
Given the size of the opportunity, we are hesitant to assume that capital or manufacturing process complexity will act as sufficient deterrents to generic entry at patent expiry. More plausibly, the innovation runway in the mechanism of action may be sufficiently long as to render patent expiries on by-then older generations of the drug less meaningful than would appear today. Fat over muscle loss, stay time, post-use rebound weight gain and co-morbidity adjacencies are all dimensions in which differentiation can be achieved. Novo is also likely to have an R&D budget of $200bn over the next 18 years or roughly $11bn p.a. which is 3-4x the budget with which it has established a track record of producing blockbusters.

Terminal Value More Important Than Peak Sales & DCF Upside 2040 Sales (X-axis), Peak Sales (Y-axis)

Peak Sales	(*implied GLP-1 penetration in US Obese population*)	Terminal Revenues (*implied R&D productivity*)						
		100,000	200,000	300,000	400,000	500,000	600,000	700,000
		0.00%	*5.50%*	*11.00%*	*16.00%*	*21.00%*	*26.00%*	*31.00%*
645,000	*25.0%*	-42%	-33%	-24%	-15%	-7%	2%	11%
745,000	*40.0%*	-37%	-27%	-18%	-9%	1%	10%	20%
845,000	*55.0%*	-32%	-22%	-12%	-2%	8%	18%	28%
945,000	*70.0%*	-27%	-17%	-6%	4%	15%	25%	36%
1,045,000	*85.0%*	-23%	-12%	0%	11%	21%	32%	44%

Source: Lansdowne analysis. Data as at September 2023

Valuation: Implied R&D Productivity vs History EBIT Return on R&D, Implied Future vs Past, %



Source: Lansdowne analysis. Data as at September 2023

If one conservatively assumes that Wegovy and Cagrisema lose 80% of their revenue to generics post-patent expiry, the required return on this $200bn of R&D investment to justify the current share price is about 20%. While this is much lower than the return on sunk R&D achieved in recent years of above 70%, it is simultaneously considerably higher than the industry average.

Our position remains relatively small as we develop our due diligence to focus specifically on this area. In the coming weeks, we will also have dialogue with a number of suppliers in the value chain to assess the manufacturing hurdles to post-patent generics. This we hope will allow us to explore other compartments of the GLP1 industry vertical to generate alternative or complimentary investment pathways into this rapidly growing revolutionary market.

Conclusion

The strength of the US economy has repeatedly surprised expectations this year. Recently revised data from the BEA suggests this may be because the extent of post-pandemic excess savings has been underestimated.

Consumption expenditure still appears likely to have to significantly slowdown next year even if annual savings rates are to revert only gradually back to long-term trend. With wages running above householding spending, corporate profitability would be pressured and real interest rates, already at 2%, would implicitly rise further. Central banks need more evidence to ease policy, especially this cycle, and one risk is it takes longer as a result.

If households now perceive fiscal activism as more of a backstop given pandemic largesse, they may not take the savings rate all the way back up to historic levels. We examine the academic literature however and find the evidence uncompelling. Bigger government in developed economies tips into a negative correlation with economic growth in most cases and trust in government and between citizens has been in structural decline. This appears to be reflected recently in the rise in sovereign bond yields which also makes further headway in government debt ratios much harder from here. The primary balance is already too loose to stabilise debt to GDP, so on net we think household savings rates are likely to continue to rise. Eventually, we expect this to allow policy rates to fall a bit creating space for a new cycle.

The fund remains balanced at the portfolio level with focus squarely on individual company analysis. We haved used the letter to discuss our recent presentation on areas of shareholder value creation to Michelin's top 100 managers, findings from a meeting with Europe's largest company (Novo Nordisk), a proprietary survey we have conducted on pest pressure in hot and cold States (Rentokil) and a new investment we have made this year into Whitbread.

The fund is trading on less than 13x forward PE and offers an IRR of 11%. We think this implies limited value for the deep optionality from the ten disparate structural growth avenues to which it is exposed and have only made minor changes in recent months.

We thank our investors for your ongoing support and are confident that it can be well rewarded.

Daniel Avigad, Shashwat Verma, Darren Ho and Valerio Dussizza