From the moors north of Skagen, 1885. By P.S. Krøyer, one of the Skagen Painters. This image belongs to the Skagens Museum.

SKAGEN Global

Status Report October 2016

The art of common sense

SKAGEN

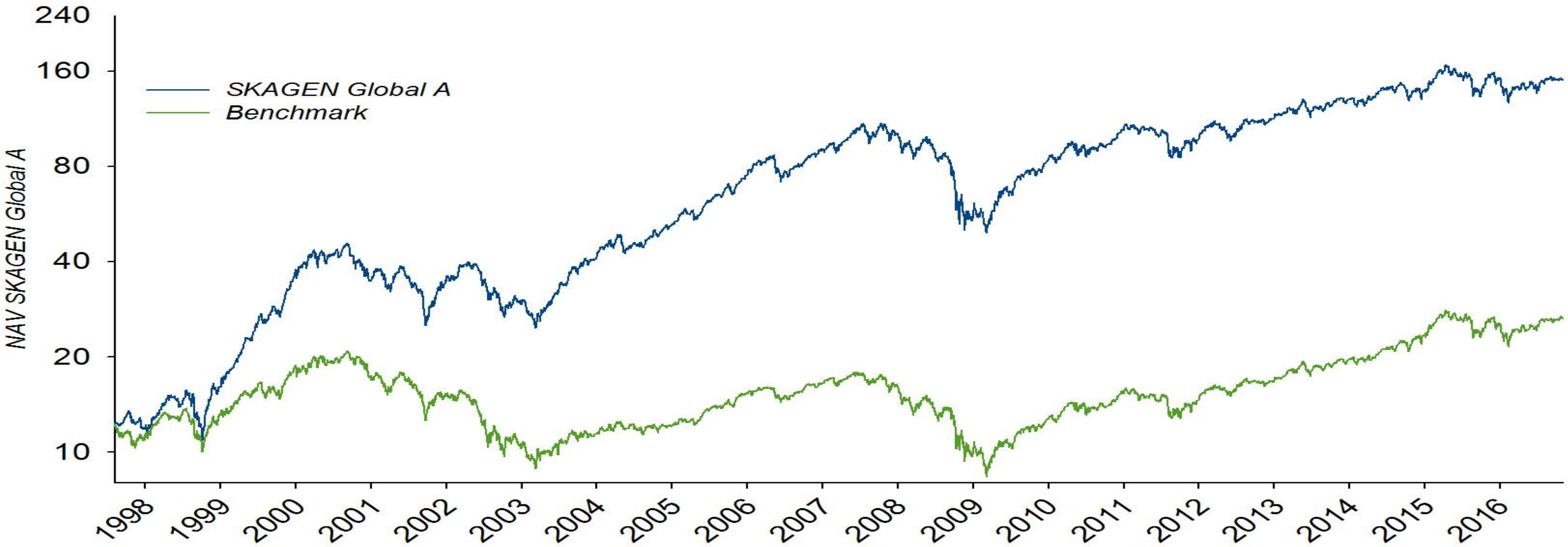
Summary – October 2016

- SKAGEN Global underperformed its benchmark index by 1.2% in October. The fund had a return of 0.0% while the benchmark MSCI All Country World Index gained 1.2% (measured in EUR).*
- In 2016, the fund has lost 1.6% while the benchmark is up 4.1%. Hence, the fund’s year-to-date relative performance is -5.7%.
- AIG, Citigroup, and Microsoft were the three best monthly contributors to absolute performance while Cap Gemini, G4S, and Roche were the three largest detractors.
- As a shareholder in Johnson Controls International we received shares in their spin-off of automotive seating supplier, Adient, which began trading as a public company on October 31.
- We sold out of WM Morrison Supermarkets and continued to reduce our exposure to a number of companies that have rebounded following their Brexit-dip.
- The fund’s top 35 holdings trade at a weighted Price/Earnings (2017e) of 12.8x and a Price/Book of 1.4x vs. the index at 14.9x and 2.0x, respectively.
- The weighted average upside to our price targets for the fund’s top 35 holdings is 36%.

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

SKAGEN Global A results, October 2016

EUR, net of fees



	October	QTD	YTD	1 year	3 years	5 years	10 years	Since inception*
SKAGEN Global A	0,0%	0,0%	-1,6%	-1,5%	4,6%	9,2%	5,8%	13,9%
World Index*	1,2%	1,2%	4,1%	2,8%	10,9%	13,2%	5,0%	4,1%
Excess return	-1,2%	-1,2%	-5,7%	-4,3%	-6,3%	-4,0%	0,8%	9,8%

Note: All returns beyond 12 months are annualised (geometric return)
** Inception date: 7 August 1997*
*** Benchmark index was MSCI World in NOK from 7 August 1997 to 31 December 2009 and MSCI All Country World Index from 1 January 2010 onwards*

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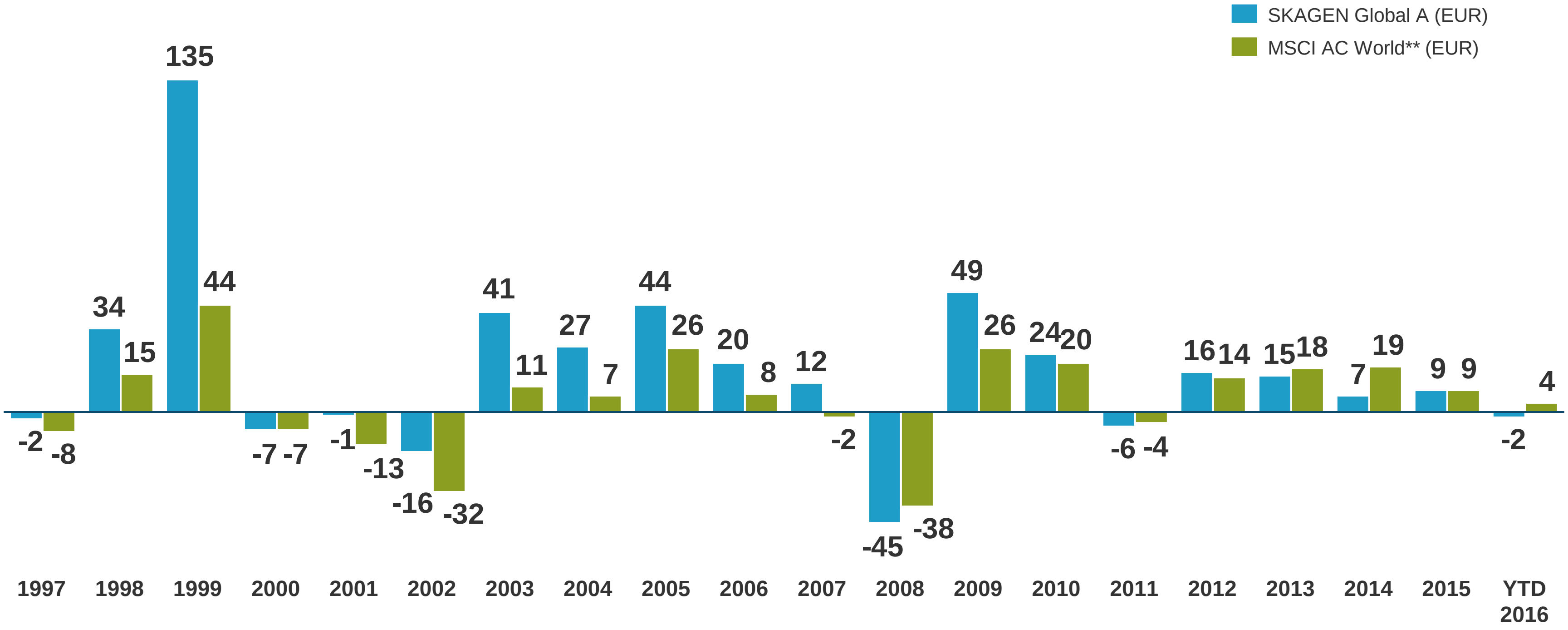
Annual performance since inception (%)*

SKAGEN Global A has beaten its benchmark 15 out of 19 years



Note: All figures in EUR, net of fees

** Inception date: 7 August 1997*

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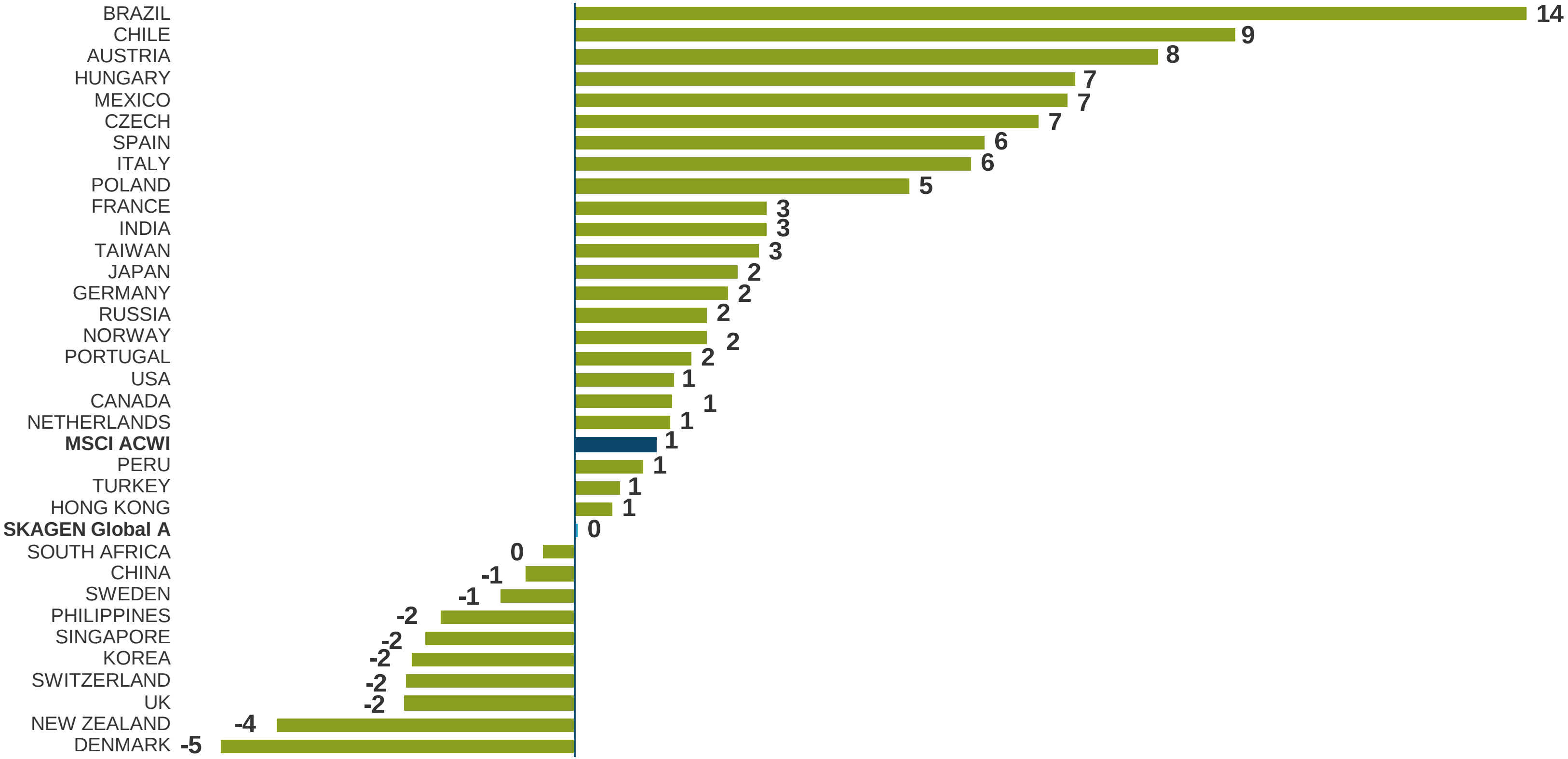
Markets in October 2016, EUR (%)



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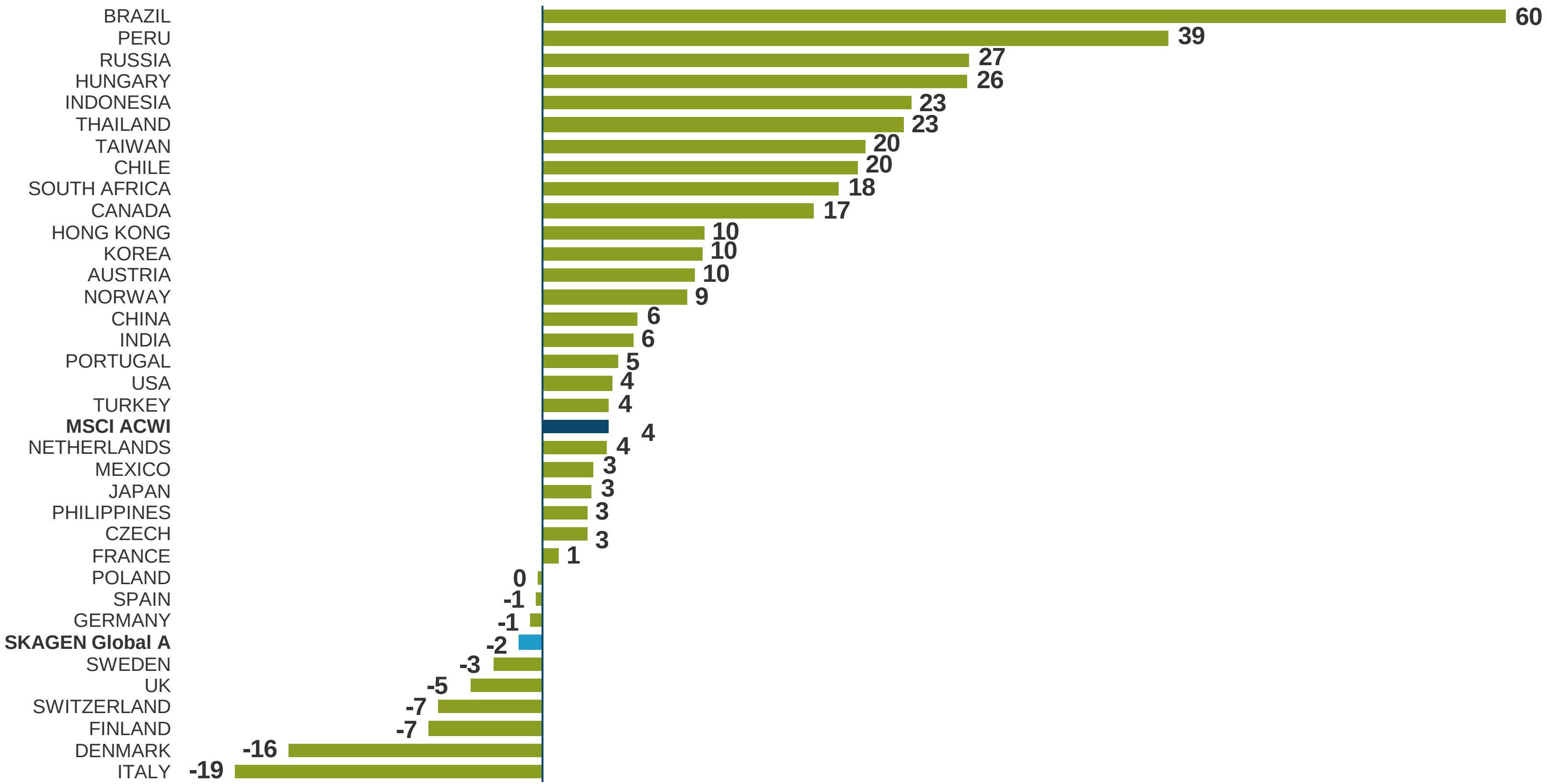
Markets in YTD 2016, EUR (%)



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Main contributors QTD 2016

Largest positive contributors

Company	NOK Millions
AIG	138
Citigroup	132
Microsoft	83
Sanofi	43
Philips	32
Goldman Sachs	32
General Electric	25
ServiceMaster Global Holding Inc	23
Alphabet	20
Adient Plc	20

Largest negative contributors

Company	NOK Millions
Cap Gemini	-69
G4S	-55
Roche Holding	-50
Kingfisher	-38
Teva Pharmaceutical Industries	-38
Unilever CVA	-36
Merck & Co	-35
Autoliv	-30
Comcast	-20
Johnson Controls International	-18

Value Creation QTD (NOK MM): 204

NB: Contribution to absolute return

Main contributors YTD 2016

Largest positive contributors

Company	NOK Millions
Samsung Electronics	181
DSM	143
Johnson Controls International	124
Sony	108
Philips	86
Lundin Mining	79
Xcel Energy Inc	77
Lundin Petroleum	74
Merck & Co	69
IRSA	65

Largest negative contributors

Company	NOK Millions
Teva Pharmaceutical Industries	-355
Roche Holding	-296
Citigroup	-229
G4S	-204
Credit Suisse Group	-202
AIG	-200
Autoliv	-152
NN Group	-143
General Electric	-139
Lenovo Group	-128

Value Creation YTD (NOK MM): -2458

NB: Contribution to absolute return

Most important changes Q4 2016

Holdings increased

Q4

Adient Plc (New)
Unilever CVA
China Mobile

Holdings reduced

Q4

WM Morrison Supermarkets (Out)
AIG
Philips
Toyota Industries

Holdings increased and decreased during October 2016

Key buys

- As a shareholder of Johnson Controls International we received shares in their spin-off of automotive seating supplier, **Adient**, which began trading as a public company on October 31.
- We have used the past month's weakness in **Unilever** and **China Mobile** to add to our positions in these stocks.

Key sells

- **WM Morrison Supermarkets** was sold out after the shares hit our target price.
- Similarly, **AIG, Toyota Industries** and **Philips** were scaled back as strong share price performance has reduced upside to our target prices.

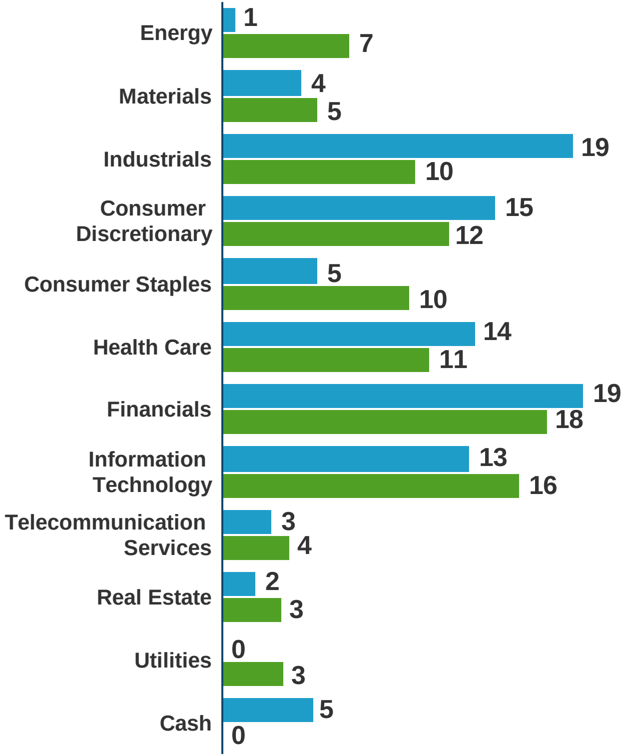
Largest holdings in SKAGEN Global

	Holding size, %	Price	P/E 2016e	P/E 2017e	P/BV last	Price target
AIG	6,5	61,7	15,3	11,2	0,7	90
CITIGROUP	5,7	49,2	10,5	9,6	0,7	70
ROCHE	4,4	227,5	15,4	14,4	10,5	360
SAMSUNG ELECTRONICS	4,4	1 317 000	8,7	7,4	1,0	1 500 000
GENERAL ELECTRIC	4,3	29,1	19,5	17,3	3,2	36
MERCK	4,2	58,7	15,6	15,1	3,7	76
CK HUTCHISON HOLDINGS	4,2	96,0	11,8	10,7	0,9	140
MICROSOFT	3,9	59,9	20,4	18,6	6,6	68
NN GROUP	3,7	27,5	9,3	9,1	0,4	35
G4S	3,2	220,0	14,4	12,9	4,7	380
Weighted top 10	**44,6**		**13,0**	**11,5**	**1,1**	**37 %**
Weighted top 35	**88,2**		**14,3**	**12,8**	**1,4**	**36 %**
MSCI AC World			**16,7**	**14,9**	**2,0**	

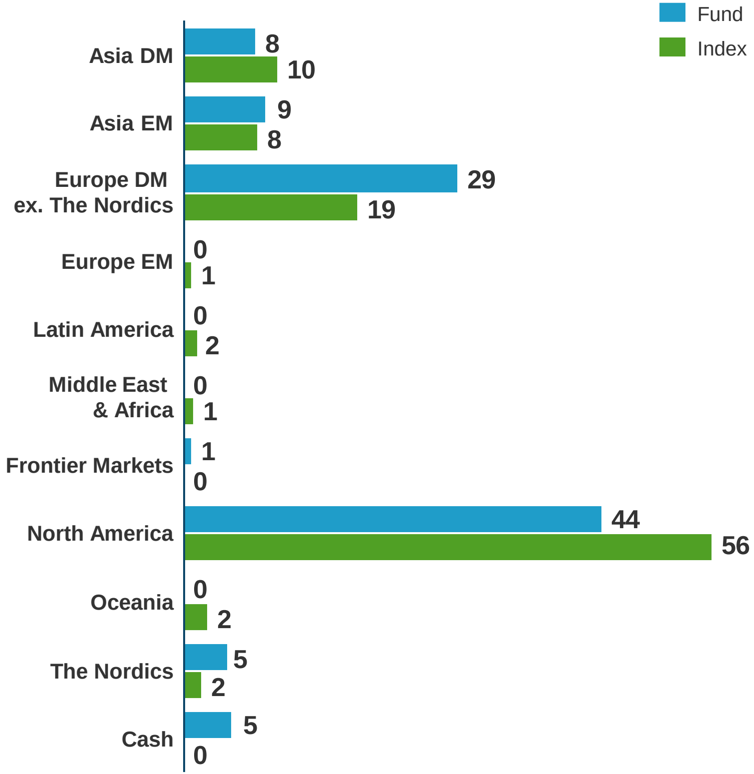
As of 31 October 2016

SKAGEN Global sector and geographical distribution

Sector distribution



Geographical distribution



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Key earnings releases and corporate news, October 2016

Citigroup

(5.7%)

Solid quarterly performance driven by bond trading

Summary: Relative to 2Q 2016 results, Citigroup reported higher net interest income (+2%) as average earning assets rose 1.0% (full quarter inclusion of the Costco portfolio) while net interest margins remained flat. Non-interest income was stable as weak investment banking and equity trading were matched by very strong FICC revenue. Operating costs were also stable, while loan loss provisions increased (building reserves due to the inclusion of the Cotsco portfolio). This resulted in earnings before tax declining marginally (-3%). The company bought back almost 2% of shares outstanding in the quarter. Assets in the bad bank (Citi Holdings) were further reduced in the quarter and are now down to only 3% of total assets.

Investment case implications: 3Q 2016 earnings beat expectations on a strong rebound in fixed income trading. More importantly, the result showed the underlying characteristics we are looking for: i) revenue increasing faster than costs, ii) reduced asset base in the bad bank, combined with iii) consumption of DTA. All of these support our case for significant generation of free cash flow over the coming years. With Citi now allowed to return cash to shareholders, we think the market should start to realise that you buy an underlying growing free cash flow stream at a very attractive starting yield.

Merck

(4.2%)

Merck reports solid Q3 results and receives speedy approval for Keytruda

Summary: The US pharma company Merck reported Q3 sales of USD 10.5bn (+3% YoY) and USD 1.07 EPS (+12% YoY), both numbers ahead of consensus but somewhat helped by early shipments to Japan. Gardasil (vaccine) sales were above expectations, Januvia (diabetes) was in-line and Zepatier (HepC) below expectations. The new immunotherapy drug Keytruda received early approval for first line non-small cell lung cancer treatment (with PD-L1 >50%), but was not awarded compendia listing. Bolt-on M&A remains an option but large-scale M&A is not on the agenda as per management.

Investment case implications: A quarter without significant surprises though the early approval of Keytruda is important as Merck needs to replace old drugs with new pipeline assets to maintain/grow earnings power. As we have stated earlier, we believe the immuno-oncology race will ultimately have more than one winner. The market assumes Keytruda peak sales of USD 3-4bn by 2020, a number we think may carry upside risk. Estimates for the immuno-oncology market keeps rising – from USD 25bn to as high as USD 100bn. Merck has been seen by the market as the dark horse in this race after industry leader Bristol-Myers Squibb; however, this perception may now slowly be shifting.

Key earnings releases and corporate news, October 2016 (cont.)

Samsung Electronics (4.4%)

An eventful month

Summary: The month did not get off to a great start with Samsung announcing that it is permanently withdrawing the Galaxy Note 7 from the market after continued problems relating to overheating and fires. Consequently, the company lowered its operating profit guidance for 3Q 2016 due to the Note 7 costs (recall, exchange, lost revenues, and scrapping costs). Later in the month, funds managed by Elliot Management Corporation announced they had taken a stake in Samsung and sent a letter to the board of directors. Elliott argues that the company is grossly undervalued and proposes a four-step plan to close the gap: (1) separating the company into an operating and a holding company, (2) paying a special dividend, (3) listing the operating company on NASDAQ, and (4) improving corporate governance. Elliot also suggested paying out 75% of FCF in dividends going forward. The month ended with Samsung releasing 3Q16 operating profit in line with its revised guidance. Note that the Samsung preference shares had a *positive* return of 2% in local currency in October.

Investment case implications: Samsung has handled the Note 7 problems in an acceptable manner towards customers. However, as the Note 7 issues have attracted significant attention from mainstream media, we fear they will have some medium-term impact on brand image. Note that the earnings impact released from the company does not include any impact from cannibalisation of sales for other models. While we do not expect Samsung to react by lowering retail prices, advertising spend might tick up temporarily. However, this is not a disaster and we are very certain that the incident will lead to an overhaul of its quality assurance routines. How management responds to Elliot's request will be very important since a more shareholder-friendly capital return policy constitutes a major trigger for our investment case.

Microsoft (3.9%)

Cloud growth remains strong

Summary: Total revenue +3% with cost flat YoY, leading to 31.8% operating margin. Hybrid cloud (Azure) sales grew c. 120% YoY. Commercial cloud revenue now has a USD 13bn annual run-rate (Microsoft's total annual revenues are c. USD 85bn). Normalised FCF increased by 8% YoY. EPS +14% YoY.

Investment case implications: Neutral. Minor positive and in-line with investment thesis. The cloud operations continue to show good momentum while opex is prudently managed by the shareholder-friendly management team. As the digitisation trend rages on across the world, Microsoft looks well positioned and reasonably attractively valued to capitalise on this trend.

Key earnings releases and corporate news, October 2016 (cont.)

Comcast

(3.0%)

Strong execution continues

Summary: Continued strong subscriber trends (recently quarterly trends are the best in 10 years). Comcast has now added 170k video subscribers over the last 12 months, with +32k in Q3 (vs. -10k consensus). Broadband added 330k customers in Q3, slightly ahead of +325k estimates. Rising programming costs are putting pressure on the margin – this is the largest cost item and Comcast now sees it growing "slightly above" 10% in 2016 (vs. "approximately" 10% previously) and being "slightly elevated" in 2017 before returning to historical growth of 7-8%. NBCU was better than expected driven by Film (partly helped by DreamWorks closing 22/9). Also fuelled by USD 1.6bn in Olympics-related revenues (advertising and distribution). Sentiment has however taken a hit due to AT&T's aggressive new headline pricing of DTV Now at USD 35/month although it is not yet clear what this product will look like. It is possible that AT&T is mostly trying to appear "pro-consumer" to smooth the regulatory process for clearing the recent Time Warner-deal.

Investment case implications: Q3 results were solid with better cable subscriber metrics and better results from NBCU. Video and broadband ads were both at record levels and came in well above consensus expectations and continue to benefit from lower churn.

GE

(4.3%)

Execution required

Summary: GE reported Q3 Sales +1% and EPS +10% YoY. Operating margin (ex-Alstom) flat YoY at 17.3%. The Healthcare segment saw orders grow 12% YoY (US, China), the strongest number in five years. On the other hand, Oil & Gas orders were down 21% YoY. Organic equipment orders (ex-Alstom) -13%. Organic growth guidance for the year lowered from 2-4% to 0-2%. 93% FCF conversion. Total signings for GE Capital at USD 193bn at 1.1 P/TNAV. Buybacks increased by USD 4bn with GE now targeting USD 30bn total cash return for 2016. Later in the month, GE announced that its Oil & Gas division has merged with Baker Hughes to create a free-standing, publicly traded company in which GE will own 62.5% of the shares.

Investment case implications: Neutral. The sluggish global growth environment presents a (known) headwind to GE. Equipment orders continue to be pretty weak with Oil & Gas being particularly hard hit with low visibility. After several years of mismanagement, GE still has several levers to pull to offset macro headwinds and we continue to believe that there is value to be unlocked through disciplined self-help and capital return measures. Note that the whole management team's compensation plans are based on reaching the 2018 targets and this provides alignment of interest with investors. We see the deal with Bakes Hughes as a clear indication that management is on the right track.

The 10 largest companies in SKAGEN Global

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 that it intends to keep: Sun America and Chartis.

Citi is a US financial conglomerate with operations in more than 100 countries worldwide. The bank was bailed out by the US government during the credit crisis and subsequently raised USD 50bn of new capital. Consists of two units: Citi Holdings which is a vehicle for assets that are to be run down and sold and Citi Corp which is the core of the going concern business. In Citicorp 60% of revenues are derived from outside the US - mainly from emerging markets.

Roche is a leading pharmaceuticals and diagnostics company based in Switzerland. Half of group sales and 2/3 of EBIT are derived from the company's Big 3 oncology franchises: HER2 (breast cancer), Avastin (colorectal cancer), and MabThera/Rituxan/Gazyva (blood cancer), each about USD 7bn of revenue. These businesses all come from Genentech, in which Roche has been a majority owner since 1990, and bought the last 46% in 2009.

Samsung Electronics is one of the world's largest producers of consumer electronics. The company is global #1 in mobile phones and smartphones, the world's largest in TV and a global #1 in memory chips. Samsung also produces domestic appliances, cameras, printers, PCs and air conditioners.

Founded in 1892 by Thomas Edison et al., General Electric (GE) operates two divisions (GE Industrial and GE Capital) contributing approximately the same proportion of group earnings. GE is the world's 10th largest publicly-traded company and boasts the 6th most valuable brand. The industrial segment is a play on global infrastructure with a high-margin service business and a large installed base producing a wide variety of capital goods ranging from aircraft engines and power turbines to medical imaging equipment and state-of-the-art locomotives.

The 10 largest companies in SKAGEN Global (continued)

Founded in 1891, Merck & Co is a US large-cap pharma company (and #7 worldwide by revenue) with a broad pharma portfolio and a solid pipeline (R&D 16-17% of sales). HQ in New Jersey and 70,000 employees. Sales by division (2014, USD 42bn): Diabetes (14%), Infectious Diseases (18%), Vaccines (13%), Animal Health (8%), Oncology (2%), Other (45%). Consensus expects legacy drugs sales to shrink by single-digit percent annually.

Founded in 1950 as a plastics manufacturer by its current main shareholder Li Ka Shing, CK Hutchison Holdings is now a multinational conglomerate. The company holds the non-property businesses of the former Cheung Kong and Hutchison group. The group owns assets in (% of 1H 2015 total EBITDA): Infrastructure (37%), Telecom (20%), Retail (15%), Ports 13%), and Energy (11%).

Microsoft is the world's largest software company and delivers software to a number of applications from PCs to servers and cell phones – its most famous product is Windows and the affiliated Office Software Suite. In recent years the company has also diversified into video game consoles, ERP systems, internet search and cloud-based computing. Despite a strong push for diversification 80% of the company's revenues and nearly all its profits come from three main areas: Windows OS, Windows Server and the business division (Office Suite).

G4S is the world's largest security company operating in more than 110 countries with over 620,000 employees. The group was formed in 2004 by the merger of UK-based Securicor plc and Denmark-based Group 4 Falck. By activity (FY2014): Security Services (84% of sales; 74% of EBITA) and Cash Solutions (16%; 26%). Main source of business opportunity is in emerging markets where the company has an unrivaled presence with >30% of sales. New management team installed in 2013.

NN Group is the former European and Japanese insurance arm of the financial conglomerate ING that was spun off in July 2014 as required by the Dutch government in return for providing state aid to ING during the financial crisis . NN's on-going business operating result before tax is split as follows (2014): 51% Netherlands Life, 14% Insurance Europe, 13% Investment Management, 11% Japan Life and 11% Netherlands Non-Life. NN has 12,000 employees and its history dates back to 1845.

For more information please visit:

Our latest Market report
Information on SKAGEN Global 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.

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