RIVER AND MERCANTILE

River and Mercantile Global Sustainable Opportunities Fund

Quarterly report to 30 September 2023

For unitholders only

River and Mercantile
GLOBAL SUSTAINABLE OPPORTUNITIES FUND

RIVER AND MERCANTILE

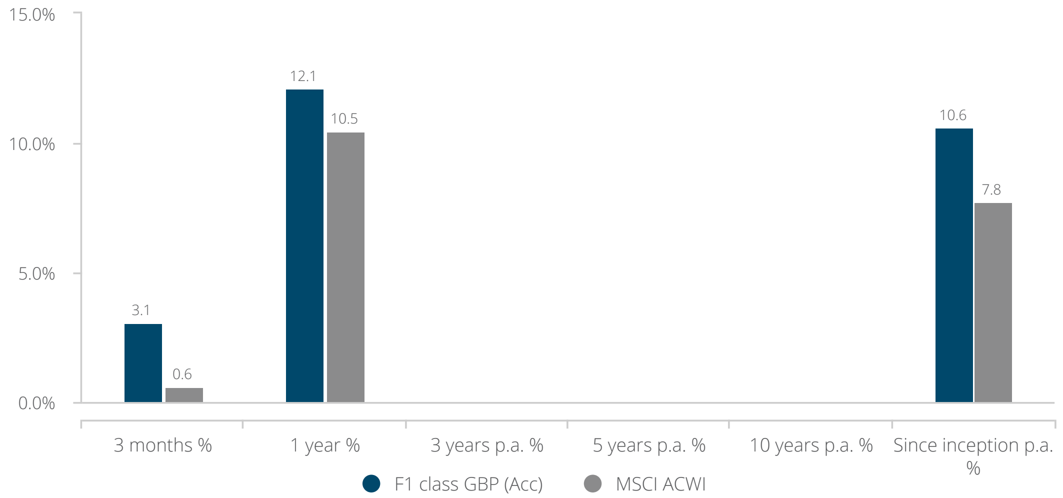
Quarter 3, 2023

INVESTMENT OBJECTIVE

The investment objective of the Fund is to grow the value of your investment over a rolling 5 year period, after the deduction of all fees. The Fund's investment policy seeks to promote environmental and/or social characteristics primarily by fully integrating consideration of sustainability risks and opportunities within the Investment Manager's investment philosophy and process, called Sustainable Potential Valuation and Timing ('S-PVT'). It assesses these through the pillars of People, Innovation, and Environment. The Fund focuses on the absolute improvement of these parameters, rather than selecting companies which are necessarily already leaders in them. In this sense, the Fund is focused on positive change. However, notwithstanding this focus on positive change, certain activities are considered to be in direct conflict with the sustainability characteristics promoted by the Fund and companies known to be engaged in these activities will be excluded.

PERFORMANCE (NET OF FEES)

	3 months %	1 year %	3 years p.a. %	5 years p.a. %	10 years p.a. %	Since inception p.a. %
F1 class GBP (Acc)	3.1	12.1	-	-	-	10.6
MSCI ACWI	0.6	10.5	-	-	-	7.8
Difference	2.5	1.7	-	-	-	2.9



Source: River and Mercantile Asset Management LLP

PORTFOLIO SUMMARY AND KEY RISK CHARACTERISTICS

Fund AUM	£13.7M
Strategy capacity	£6.0B
Inception date	06/07/2022
Number of stocks	49

Portfolio Volatility	8.5%
Benchmark Volatility	9.1%
Portfolio beta	0.53
Tracking error	8.3%
Active money	95.1%

SYNTHETIC RISK & REWARD INDICATOR (SRRI)

1	2	3	4	**5**	6	7

Lower risk — Higher risk

Typically lower rewards — Typically higher rewards

The Synthetic Risk and Reward Indicator (SRRI) is based on how much the returns of the shares have varied over the last five years, or since launch (whichever is the shorter period). The higher the rank the greater the potential reward but also the greater the risk of losing money.

Executive Summary

- Global equity markets ended down in Q3 2023 (MSCI ACWI -3.4% total return in USD), with sharp falls in August and September following a strong July. The key macro story of the third quarter was the return of "higher for longer" sentiment around the likely path for interest rates. US 10-year bond yields marched higher with unerring consistency, from 3.8% to 4.6%. Higher cost of capital has started negatively impacting the valuation of longer duration ("growth") equities despite resilient corporate earnings forecasts.
- The Fund returned +3.1% in Q3 2023, outperforming its benchmark in the period.
- We bought new holdings in Hitachi and Valmont Industries, both industrials which will benefit from long-term spending plans from governments & corporates, with exciting self-help strategies to further enhance future their return on capital. We also initiated positions in consumer staples FeverTree and Kenvue, plus Samsung Electronics. Each has attractive margin upside over the intermediate term. We exited Procter & Gamble (switch to Kenvue), Tokio Marine (reached fair value), and IMCD (weakened investment case).
- Our engagement with Japanese flavour & fragrance company T Hasegawa showed good progress on targets set out last year, with the promise of more positive change in the pipeline.
- The portfolio in aggregate delivers ~14-15% cash return on capital and can grow sustainably at ~10% per year, while valued at an ~8% earnings yield. The relative value opportunity remains the best it has been since at least 2015. The portfolio trades one-third cheaper than the benchmark's asset-based valuation and over the past year return on capital is up 2 percentage points while the valuation is unchanged.
- We now have a third of the portfolio invested in sub-$10bn market cap companies. We detail why we are comfortable with the risk profile associated with these smaller company holdings. We also update on the outlook for capex, particularly as it relates to investment in the electrical grid. We have increased conviction in the robustness and longevity of the opportunity here.

Investment background

Global equity markets ended Q3 2023 with sharp falls in September, following on from losses in August (MSCI ACWI -3.4% total return in USD during Q3). The key macro story of the third quarter was the return of "higher for longer" sentiment around the likely path for interest rates. Higher US rates and weak economic data in Europe and China (alongside concerns around the property market in the latter) challenged the 'Goldilocks' narrative of a so-called soft landing for the global economy alongside moderating inflation. The resurgence of oil prices back to $95 a barrel played a role in the renewed concerns (Brent oil +27% in Q3), contributing to inflationary expectations whilst typically having a constraining effect on future economic growth. US 10-year bond yields marched higher with unerring consistency, from 3.8% to 4.6%. Having broken above 2% in August for the first time since 2009, US 10-year real yields hit 2.4%. The higher interest rate environment, with no sign yet of a 'pivot' towards cuts from the Fed, has started negatively impacting the valuation of longer duration ("growth") equities despite resilient corporate earnings forecasts.

Fund Update

Performance

The Fund returned +3.1% during the third quarter of 2023. In comparison, the MSCI ACWI index returned +0.6% (all GBP). As another reference point, the MSCI ACWI Equal Weighted index also returned +0.6%. Since inception, the fund has returned +13.3%, compared to the global benchmark's +9.7%.[1]

Booking Holdings (+19% in GBP) was consistently strong throughout the 3rd quarter. Booking's Q2 results were a clear demonstration of its 'best-in-class' credentials among online travel agents (OTAs). Room growth (the inventory available on its sites), bookings, revenues and profits were all well ahead of consensus expectations. Full year 2023 guidance is conservative considering management's comments around the current run-rate of trading in Q3, but of more interest is our increased conviction that 2024 consensus forecasts for profit margins are materially too low. The cash generation in the business is exceptional and allowed Booking to buy back 5% of its outstanding shares in the first half alone.

Energy services & technology provider Baker Hughes (+17%) responded positively to its Q2 results, where it raised full year guidance for order intake and operating profits following a strong first half performance. Free cash flow generation has also improved, in line with our investment case, giving us the prospect of a simultaneous acceleration in revenue growth and cash generation.

Danieli (+19%), which manufactures steelmaking equipment, as well as producing its own lower emissions steel products, rose after its full year results provided evidence of the strength of current trading and its longer-term outlook. Its order book is now over €6 billion, driven by steel companies continuing to invest heavily in capex to drive emissions reduction. This compares to a market cap of just €1.9 billion. The large net cash balance of €1.6 billion has started benefitting from the rise in interest rates. Annualising the €50m interest earned in the second half of the year offers investors a ~5% cash yield *from this line alone*.

Our primary negative contributors were both UK-listed. Medical device producer Smith & Nephew (S&N) was among the fund's strongest performers in H1, but its share price fell -19% last quarter. S&N and its US-listed orthopaedic peers all weakened as the stock market assessed that the extraordinary growth in weight-loss drugs (GLP-1) will mean fewer hip and knee replacement procedures in future. For the intermediate term, at least, we see it as equal odds that procedure volumes could be *higher*, given a cohort of severely obese patients will now become eligible for a replacement having previously been excluded. In the shorter term, S&N's profit guidance for 2023 requires strong delivery in the second half of the year.

Asian life & health insurer Prudential (-19%) was, in our view, harshly treated as a 'China proxy'. The performance of its Hong Kong business, which is its largest 'direct' exposure to China, has materially exceeded consensus expectations around its speed of recovery. During the last quarter, Prudential confirmed its earnings figures under new accounting rules for the insurance sector. This is a technical factor which has, at face value, reduced its EPS forecasts by a double-digit percentage. It's feasible that this has caused some market participants to sell the 'downgrades', but there is no change to the cash generation of the business and therefore its intrinsic value. During Q3, new CEO Anil Wadhwani unveiled his medium-term strategy and guidance. This envisions 15-20% New Business Profit CAGR over 2022-27 and double-digit CAGR in "operating free surplus generation", which is akin to free cash flow. The focus on the latter is welcome and delivery on this is central to a re-rating.

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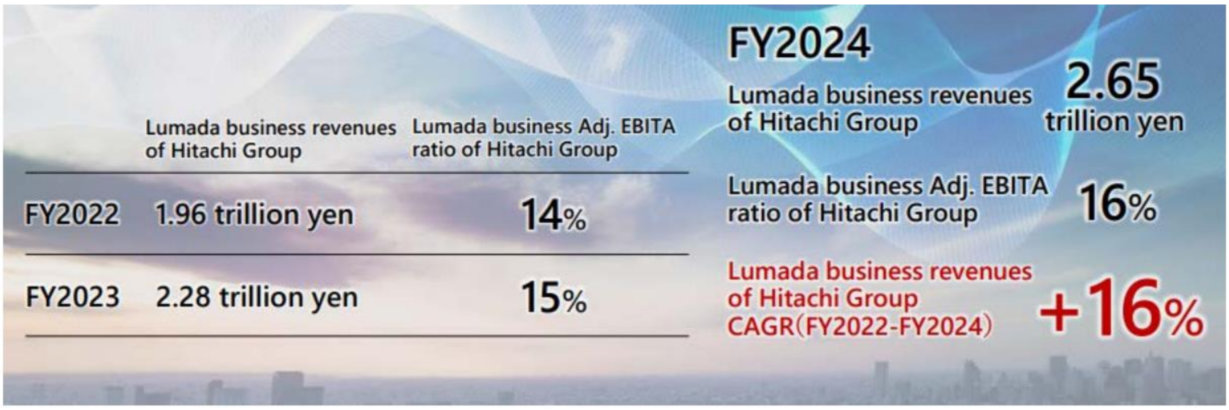
[1] *Inception: 7 July 2022. Fund: F share class (GBP), midday to midday pricing. Benchmark: close-of-business to close-of-business pricing.*

Activity

We bought five new positions during the third quarter: Japanese industrial and technology conglomerate Hitachi, US-listed infrastructure and agriculture equipment manufacturer Valmont Industries, UK-listed premium mixer brand FeverTree, Korean semiconductor & electronics conglomerate Samsung Electronics, and Kenvue, the recent consumer healthcare spin-out from Johnson & Johnson.

Hitachi has streamlined its operations towards exposure to several secular growth areas, including digitalisation (AI and Internet of Things (IoT) digital solutions) and renewable energy (power grid business). Increasing sales mix from its digital consulting business (Lumada) should drive a higher organic growth rate and margin enhancement for Hitachi overall. Our analysis suggests that Hitachi has competitive advantages in AI and we are particularly positive about the prospects for global power grid investment to support Hitachi Energy. While the share price has performed well, on sub-14x our estimate of future earning power it does not yet reflect the group's improved return on capital and growth prospects.

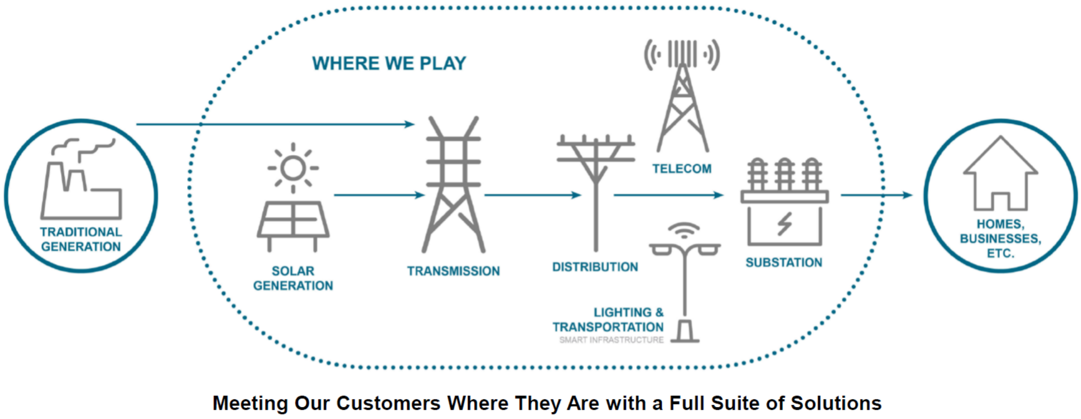
Lumada is Hitachi's general term for the solutions, services & technologies that utilise Hitachi's advanced digital services to create value from customers' data and accelerate digital innovation. It's expected to account for 33% of sales by March 2025 at attractive margins.



Source: Hitachi 2023 investor day presentation.

Valmont Industries has expertise in engineered steel structures which has led to two very well positioned niches for long-term growth. Its Infrastructure segment is a major beneficiary of US grid and highway investment, solar build out, and telco network densification, while its Agriculture business is a global leader in mechanised irrigation. We expect both to grow revenues mid-to-high single-digit over the next 5 years and beyond with twin drivers of government spending (e.g., US IIJA & IRA) and corporate sustainability imperatives. Like Hitachi, Valmont has restructured to focus on business lines & geographies in which it's competitively advantaged, become more price disciplined and has been delivering above market growth via geographic expansion and product adjacencies (supported by bolt-on M&A). Tying this together, we expect attractive growth, significant expansion in operating margins (the company guides +400bps), and improved capital efficiency to lead to return on capital improvement (guide +600bps) and double-digit EPS growth. Concern around short-term irrigation market trends and the CEO's departure (replaced by the CFO) have led to a ~25% pullback. At purchase, the shares priced in ~3% growth in perpetuity and traded on ~16x free cash flow, below its long-term average but with a better outlook, and with peers trading on~20x-plus.

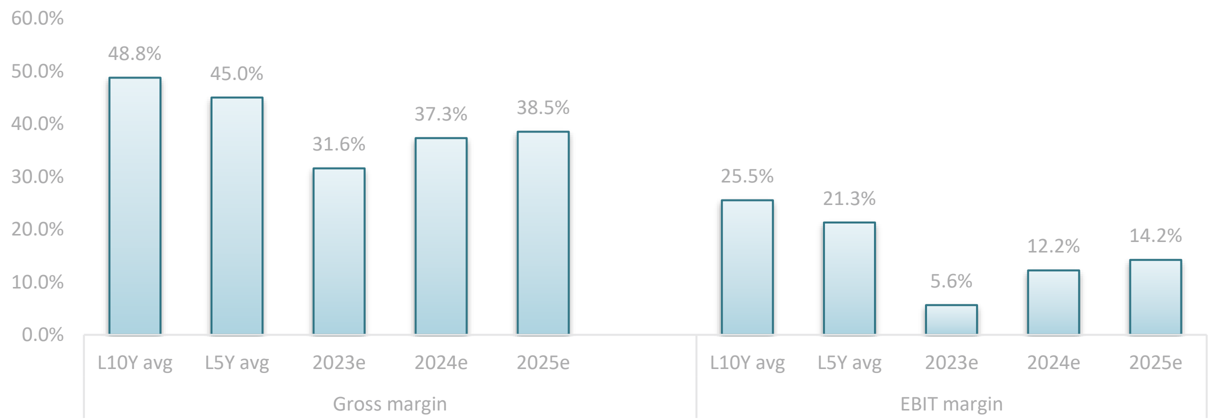
Valmont Infrastructure division sits at the heart of a rapidly evolving energy ecosystem.



Source: Valmont Industries investor day presentation, 23 May 2023.

FeverTree is the pioneer and global market leader in premium mixers. It operates an asset-light model with outsourced bottling and distribution, allowing for self-funded growth and high cash generation. It has attractive margin recovery potential from very depressed levels, as margins collapsed due to a confluence of logistics and cost inflation challenges which are now stabilised or unwinding. On our assessment of recovered margins in roughly three years, we paid a low double-digit earnings multiple for a business that will still be delivering double-digit revenue growth at this point.

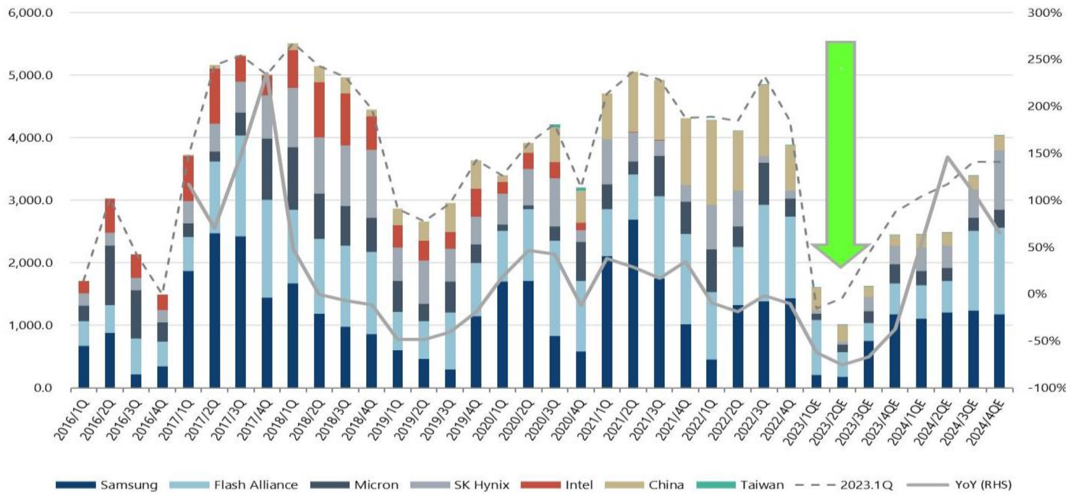
FeverTree's profit margins are depressed versus historic levels, with only modest recovery built into consensus forecasts.



Source: Bloomberg Finance LP, River and Mercantile Asset Management LLP. Data to 9 October 2023.

Samsung Electronics is a recovery investment case where we expect a positive inflection in profitability to drive both earnings growth and a valuation re-rating. The Samsung investment case can appear complex – it has consumer facing businesses (mobile phones), hybrid B2B and B2C businesses (display) and is one of the largest memory semiconductor manufacturers in the world. In truth, we think the investment case is more straightforward, driven by the 'capital cycle' in the semiconductor business. Structurally, this industry is attractive – supply is an oligopoly (Samsung, Micron and SK Hynix) with capital and technological barriers to entry. Long-term demand growth is closely tied to AI, digitalisation, cloud computing and broader data usage, none of which show signs of slowing down. Samsung's valuation today is low, trading close to the replacement cost of its assets. This reflects the current low point in its profit cycle rather than where we are likely to go over the next 1-2 years. We expect capacity restraint from the key players will drive better pricing and set off a cyclical margin upswing. Notably, the strength of Samsung's balance sheet is allowing it to invest in the next generation of manufacturing technology while others are tightening capex, which can help Samsung gain share in the future.

NAND capex is hitting a low point – a positive for future Samsung's future pricing



Source: Jefferies, SEMI World Fab Forecast. Data to 12 June 2023. Y-axis shows global NAND capital investment in $m.

Kenvue operates several brands which are household names and have leading market share (seven #1 global brands and thirty-seven #1 regional brands), such as Listerine, Aveeno, Neutrogena, and Band-Aid. Regionally ~50% of sales are in the US, with Asia Pacific and EMEA at 21% each and the remaining 8% in LatAm. We expect it to grow sales organically in mid-single digits, outpacing overall industry growth through category mix, brand strength and international penetration. As with other spin-outs, we expect it to use the elevated focus of being a standalone company (rather than a division of a larger group) to drive cost efficiencies. These efficiencies, raw material and supply chain normalisation, and operating leverage should lead to 100-150bps of operating margin upside over the next 2-3 years, delivering high single-digit or better earnings growth. We acquired our initial position by buying Johnson & Johnson's shares, which we were subsequently able to exchange for shares in Kenvue at an 8% discount (exchanging $108 worth of Kenvue shares for each $100 of J&J we owned). We therefore had a discounted entry point into what we already considered a cheap share. We funded our purchase of Kenvue, on 17-18x our estimate of current earnings, by selling our holding in Procter & Gamble, trading on 25x when sold with a similar earnings growth outlook.

These were partly funded by exiting the position in specialty chemical distributor IMCD. This remains a good quality business franchise, but we had concerns about both the near-term volume outlook and, on a one- to two-year view, around pricing (to which distributors are more sensitive).

Our holding in the Japanese insurance group Tokio Marine was sold towards the end of the quarter after it reached our estimate of fair value. It has been held since the inception of the strategy and doubled from ¥1800 to ¥3600 in that time. This has taken the price-to-book ratio from 1x to 1.7x, which we think is appropriate for its through-cycle return on equity. Across our other Japanese investments, we also took profits in Toyota Industries. We are researching several Japanese ideas and expect to rebuild our portfolio weighting in this attractive market.

We also materially reduced our position in another strong performer over the past year, the glass bottle manufacturer Verallia. It was trading near fair value and we see some risk that the profitability per tonne produced, which has expanded above the prior trend in the last two years, could mean revert.

Portfolio Fundamentals

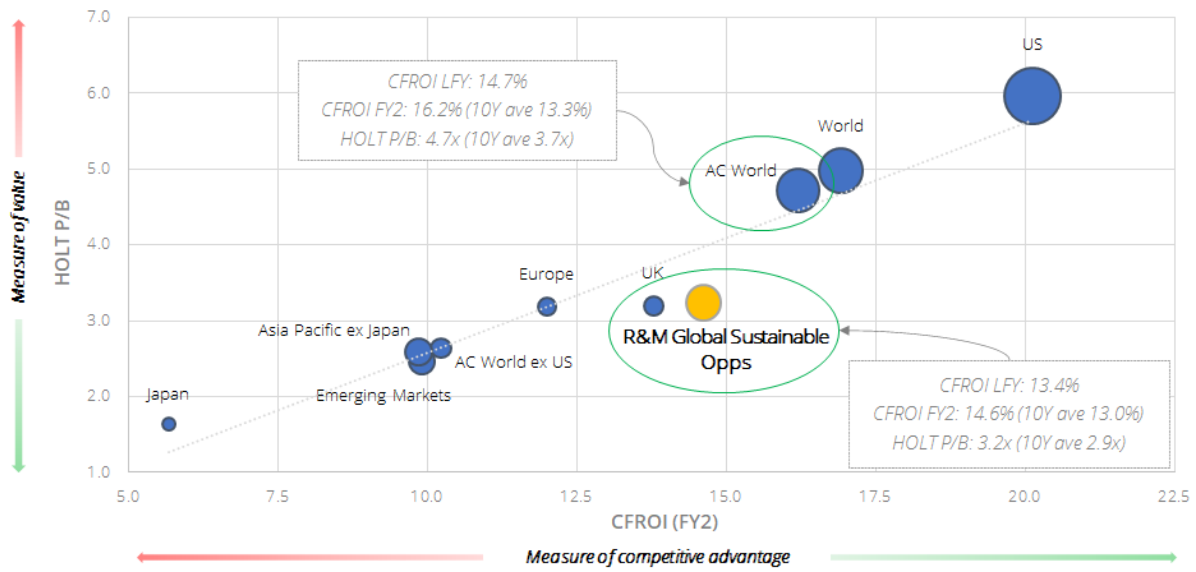
The fundamentals of the companies in our portfolio have improved while valuations are unchanged since the end of last quarter. Overall, we own businesses whose return on capital (CFROI) is ~13% on a historic through-cycle basis and is ~15% on a forward-looking one. Our companies are growing sustainably ~10%, while employing low levels of debt (see table below). Our portfolio is currently trading one-third cheaper than the benchmark based on replacement cost and more attractive cash flow yields. We currently see ~50-55% upside to our base case fair value for the portfolio, based on a weighted-average for each investment, delivered over our typical three to five-year investment horizon.

	R&M Global Sustainable weighted ave	MSCI ACWI weighted ave	MSCI ACWI median
Average market cap ($bn)	117.8	426.8	13.1
Fundamentals			
Cash Flow Return on Investment (5Y average)	12.8%	14.1%	7.8%
Cash Flow Return on Investment change (3Y forecast)	2.1%	1.0%	0.2%
Sustainable growth rate	9.4%	11.3%	3.8%
Debt-to-equity	104%	134%	56%
Valuation			
Forecast earnings yield (+12mths)	8.0%	6.5%	6.4%
Equity Free Cash Flow yield (trailing 12mths)	4.8%	4.2%	2.9%
EV to replacement cost (inflation-adjusted)	3.2 x	4.8 x	1.6 x

Source: Credit Suisse HOLT, Bloomberg Finance LP, River and Mercantile Asset Management LLP. Data to 6 October 2023.

The relative value opportunity represented by the Fund, when compared to other major global equity indices, is the best for any strategy I have been managing since at least 2015. We demonstrate this in the scatter chart below, with a position below the diagonal line representing likely undervaluation compared to the strength of the underlying businesses (as measured by a cash-based and inflation-adjusted return on capital measure). Over the past 12 to 18 months, the portfolio's valuation multiple has remained the same while the (forward-looking) return on capital has increased from ~13% to ~15%. Bubble size reflects the sustainable growth rate.

R&M Global Sustainable Opportunities vs global equity benchmarks: valuation relative to underlying business quality



Source: Credit Suisse HOLT, River and Mercantile Asset Management LLP, MSCI. Data to 6 October 2023.

Engagement

In this section, we share some highlights from the engagement we had with portfolio companies during the quarter around sustainability issues, including key outcomes. Note that this is not an exhaustive list of engagement activity during the quarter[2].

Our key engagement last quarter was with Japanese flavour and fragrance company T Hasegawa. We are encouraged with the progress and direction of travel regarding several items on which we engaged with the management last year. At this year's AGM, a new independent board member will be proposed, taking the balance closer to 50% independence. Crucially, reflecting the fact that the business now generates 45% of its revenues outside Japan (a figure we expect to increase based on our understanding of capital allocation priorities), the new member will be a non-Japanese national with overseas work experience.[3] The company continues to build up a shortlist of suitable foreign nationals and female directors to improve the board's diversity over the coming years.

Regarding its emissions reduction efforts, management confirmed that it is in the process of setting SBTi approved net zero targets. We expect that this subject, alongside other financial and non-financial KPIs, will be included among the targets as compensation structures are modernised away from 100% focus on net income. We have ongoing discussions with the management around this topic, supporting them by providing case studies from companies with which we've had previous successful engagements. We also continue to engage around capital allocation, where our analysis suggests that the company could further reduce cross-shareholdings to 5% or less of its net assets (preferably zero) and materially increase shareholder returns via a special dividend (or buybacks).

Strategy Focus: Small cap equities and risk

Last quarter, we highlighted the exceptional value on offer within global small caps. We have continued to build our weighting in smaller companies, with a third of the fund now in companies with a market cap below $10 billion. Small caps come with the perception of higher risk, so this quarter the focus is on demonstrating why we think larger risks lie elsewhere, with historical analogues, as well as why the characteristics of our smaller companies do not suggest an elevated risk profile.

The level of investor capital concentrated in the largest companies in the global benchmark is reminiscent of two prior periods in equity markets: the 'Nifty Fifty' market of the late 1960s and early 1970s, and the TMT bubble at the turn of the millennium. From the start of 2000, following the bursting of the TMT bubble and subsequent economic recession, the Russell 2000 (a US small-cap index) proved more robust than the large cap S&P 500, returning 18% over the three years to the end of 2003 versus the S&P 500's -20% fall (the NASDAQ 100 index fell -60% over the same period).[4] During the 1970s – a decade plagued by high inflation and economic volatility – US small cap stocks returned 9.0% per year, compared with 5% for US large caps.[5]

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[2] A full review can be found in the Quarterly Sustainability Report.

[3] Another feature for the T Hasegawa board was that any candidate should only have three company directorships to ensure sufficient focus.

[4] Source: Bloomberg Financial LP

[5] Source: Voya Financial, 'US small cap growth: A big opportunity for long-term investors.'

The small cap Russell 2000 index (white) delivered a 38% higher total return than the large cap S&P 500 (orange) from 2000 to 2003.

Source: Bloomberg Finance LP. Data from 31/12/1999 to 30/12/2003.

We consider three primary sources of risk: business fundamentals, financial leverage, and valuation. We have referenced the valuation argument for global small caps more broadly, but our own selection of sub-$10 billion market cap holdings on average trade on 11x our estimate of sustainable earnings. This compares to an average of 15-16x over the past 5 years[6], which we think is more representative of the quality of franchises we own.

There is an element of pro-cyclicality to several of our smaller holdings, reflected in a 3-year beta of 1.1 on average across the group (range: 0.8-1.5). However, cyclicality is not a uniform feature. Dental and medical distributor Henry Schein, specialty food ingredients firm Tate & Lyle, wine producer Treasury Wine Estates, and premium mixer brand FeverTree all have relatively defensive end markets, for example. Despite their smaller size, our holdings are typically market leaders in a niche, which is reflected in an average return on capital of 10.5%, compared to 9.5% for the average company within the MSCI ACWI index.[7]

Financial leverage across these holdings is low. The average net debt to EBITDA ratio is 0.4x[8] and a quarter have net cash positions. The highest leverage among the group is 2.4x, at discount hotel operator Whitbread, where the debt is supported by freehold ownership of over 50% of the Premier Inn estate. As with the remainder of our portfolio, we see the conservative approach of our companies to financial leverage as having the dual benefits of providing resilience against uncertainty and optionality to create shareholder value via sensible capital allocation.

In summary, if investors are wary of risk in global equity markets, then we suggest that they are best to first turn their attentions to larger cap companies. We are excited by the investment opportunities that our robust, under-valued smaller company holdings represent and have put increasing weight behind this view as the valuation anomalies have widened, with a third of the fund now in companies with a market cap below $10 billion.

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[6] *Note, Whitbread removed from this calculation due to highly depressed earnings during Covid skewing its 5-year P/E average up to 60x.*

[7] *Source: HOLT Cash Flow Return on Investment, adjusted for excess cash (last financial year figure).*

[8] *Harley-Davidson is excluded from the calculation – it has a net cash motorcycle business with a captive financing arm, which has modest financial leverage relative to the loan book assets.*

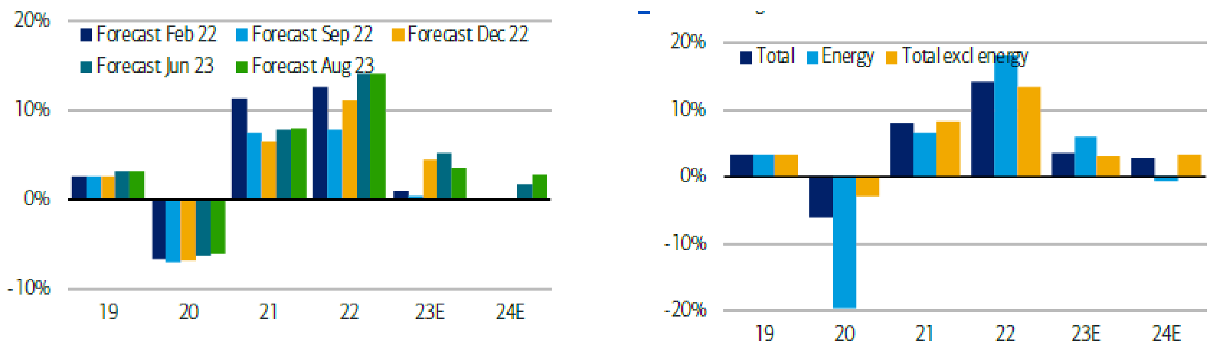
Sustainability Focus: Capex update & electricity grid investment

A year ago, we wrote about our expectation that capex would prove more resilient than market participants were pricing into the shares of relevant companies, due to long-term drivers such as decarbonisation, productivity, and near-shoring supply chains. We drew the following conclusion:

The long-term requirements for investment are relatively well-established by now, but we detect nervousness among investors about how a combination of tightening financial conditions, demand weakness, inflation and earnings forecast reductions will feed into an 'air pocket' and capex cuts during 2023 and 2024. We expect this is conditioned by the experience of the previous cycle, but the evidence is currently incontrovertible that we've entered a different regime. Many companies can't afford not to invest today. Cleansing capitalism's karma – or fixing the 'sins' of the last cycle – suggests casting off the 'lower for longer' playbook of 2010-2020 and instead looking to the 1970s for inspiration. Then, as now, inflation was the 'disease' and investing in the cure – the capex winners – was a profitable strategy.

Bank of America data shows global capex expectations for 2023 increased from +0.5% year-on-year in September 2022 to +3.5% today, while the estimate for 2024 has increased from +2% in June this year to +3% now. Some of 2024's rise appears to have come from 2023 projects being pushed out, as the 2023 forecast was +5% in June.

The forecast evolution of 2023 & 2024 capex growth (left), shown with and without the Energy sector (right).



Source: BofA Global Research estimates. Data to 2 October 2023.

Given inflation is mid-single digit, this does suggest modest declines in real terms. In the context of the structural trends we discussed last year, I expect this to prove too conservative and capex to prove more resilient. There are three core reasons for this:

1. Our meetings with corporate management teams suggest that order books relating to the US Inflation Reduction Act (IRA) are starting to be built in the second half of 2023, with major orders expected to flow in 2024 and therefore capex spend accelerating in 2024-25.
2. Prior underinvestment during the last decade, which we dealt with in detail in the Q3 2022 letter, means companies cannot afford to cut spend aggressively. Supply chain challenges have meant that in several areas (e.g., agricultural machinery) fleets have not been renewed to the extent they might typically be and have been run harder in the meantime, accelerating the ageing / depreciation process. Despite this, consensus has global capex to sales (%) *falling* in 2024 and capex to depreciation ratios at 1.27x are still below the 2010-19 average of 1.4x, both of which are counter intuitive.
3. The technology & telecom sectors have become an increasingly important component of global capex, rising from ~9% in 2013 to ~16%. This segment has witnessed the largest downgrades to

consensus during 2023. This partly relates to semiconductor capex, which is cyclical and we anticipate will increase again within the next 1-2 years (in no small part due to AI), and also the lagged effect of falls in the share prices of large tech businesses in 2022. Revenue growth has improved and share prices have rebounded significantly which, all things being equal, will support higher re-investment once again.

A key area of future spend that we identified was investment in the electrical grid. Our additional work this year on several companies exposed to this market has increased our conviction in the robustness and longevity of the opportunity here.

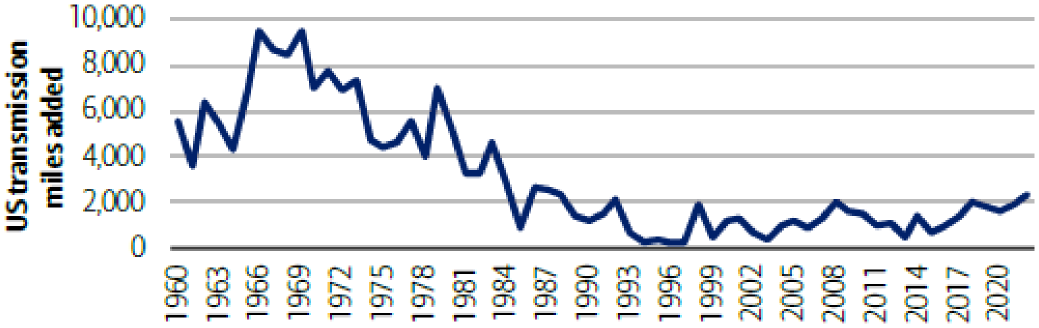
Bloomberg New Energy Finance (BNEF) estimates annual grid spend will rise ~2x from $274bn in 2022 to $424bn p.a. by 2030, while Thunder Said Energy (TSE) believes this figure could be $600bn. Because of greater complexity due to the introduction of a greater proportion of renewable generation, transmission equipment is expected to grow between 6% and 14% under BNEF's scenarios. In the US IIJA ('Infrastructure Act'), $100bn of spending is included for power grid infrastructure and $174bn for EV adoption & infrastructure. There are a further ~$370bn relevant investments included in the IRA. In fact, the stimulus money is less impactful here than in sub-sectors relative to the trillions of dollars of private investment being made but returns on equity for transmission companies are 10-13% so financing is not an issue.

There are effectively three inter-related requirements driving the spend: [1] The need for greater grid capacity, as the world electrifies to lower emissions. The grid is currently the largest bottleneck to progress in Europe and the US; [2] the need to 'smarten' the grid, primarily with investment in software and automation, which would in turn help expand capacity; [3] the need to 'harden' the grid against extreme weather conditions. Our recent investments, Hitachi and Valmont Industries, will both benefit materially – Hitachi primarily via the first two, Valmont the first and last.

In 2022, US utilities invested $27bn on transmission capex and $51bn on distribution capex according to the Edison Electric Institute. This represents an 8.6% CAGR over 2012-22. However, expansion capex represented only ~28% of total transmission & distribution capex, with replacements and upgrades the remaining 72%. Transmission miles added is a proxy for the overall age of US grid equipment. Less than 15% of the US high-voltage lines (>138 kV) were added since 2002. The greatest pace of expansion in transmission was in the 1960s and 1970s, meaning many transmission wires are over 50 years old. Transmission lines typically have a 50-year lifespan.[9]

[9] *~50% of transmission & distribution capex is tied to electrical equipment, with the other 50% going to structures (e.g., towers & wires) and installation costs.*

Transmission wires added to the US grid by year: less than 15% of total US transmission miles were added since 2002.



Source: EEL, FERC, and BofA Global Research calculations.

Consider that on top of this aged grid:

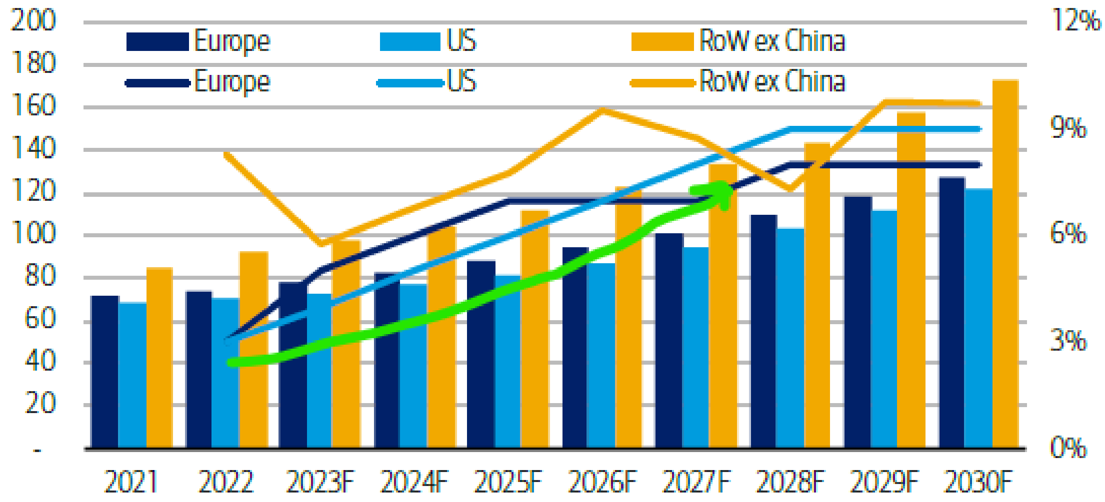
- Renewable generation capacity must double to account for 50% of total electricity generation in North America by 2050.
- A national network of 500K EV charging stations is expected across the US by 2030.
- Transmission capacity must increase by ~ 60% (47K GW miles) by 2030 to support clean energy deployment in the U.S.
- For every GW of offshore wind installed, there is €300-400m of transformer/substation equipment required.

The shape of energy production moving towards renewables is highly significant. Thunder Said has done the best work we have read on this topic. It increases the requirement for inter-connector transmission lines to smooth volatility & intermittency (essentially, minimise the difference in solar output in two inter-connected regions). According to TSE, this is more effective than batteries.

Power transmission also beats batteries as a way of maximizing renewable penetration in future grids. Rather than overcoming intermittency — solar output across Europe is 60-90% inter-correlated, wind output is 50-90% inter-correlated — by moving power across time, you can solve the same challenge by moving them over a wider space. A key advantage is that a large and extensive power grid smooths all forms of renewables volatility, from a typical facility's 100 x sub-10-second power drops per day to the +/- 6% annual variations in solar insolation reaching a particular point of the globe. By contrast, different batteries tend to be optimized for a specific time-duration, while at long durations, the economics become practically unworkable. A new transmission line usually costs 2-3c/kWh per 1,000km. Additional benefits for expanded power grids accrue in power quality, reliability and resiliency against extreme weather.

Finally, from the perspective of our investments, part of the attraction is that baseline BNEF expectations are for grid investment to accelerate through this decade. Note that the scenario shown below is not BNEF's 'net zero scenario' (which requires faster acceleration). This runs counter to typical analyst forecasts, and derived from this equity pricing, which fades growth. Our own estimates for Valmont and Hitachi therefore compound to be materially higher than the consensus once you move three to five years out.

Estimated annual grid capex under BNEF Economic Transition Scenario[10] (US$bn LHS, YoY growth RHS)



Source: BofA Global Research estimates, BNEF.

Outlook

The fund outperformed falling markets, protecting capital better when global benchmark valuations are compressing. We believe that this is a useful attribute based on our view that *the* key market risk is high valuation multiples in long duration equities, in which lots of other investors' capital is still invested. We are doing this with a 'balanced' rather than an outright 'defensive' portfolio, as we are not trying to make a directional bet on the macro cycle. Instead, we are simply staying true to the price discipline at the heart of our investing philosophy & process.

We believe that the price discipline of our strategy is one of our key differentiators in a market that has appeared to favour chasing the share prices of popular companies higher over considering downside protection. It is worth highlighting that, despite falling in August and September, the Tech-dominated NASDAQ 100 index is still up +36% year-to-date. The lack of follow-through from higher rates to the share prices of longer duration ("growth") equities has surprised us thus far in 2023, but sectors of the market with this characteristic, such as Tech and Luxury, have begun to experience downward pressure on their valuations (as in 2022). We are sceptical that the recent weakness here is purely seasonal, not least because investors can find superior risk-reward elsewhere.

Deutsche Bank has excellent long-term data around bond yields and inflation. Out of 225 years' worth of 10-year rolling inflation numbers, 194 (86%) had inflation below 4.5%, whereas 31 were above it. Of these 31, 9 occurred between 1917-1925, 6 between 1947-1952, and 16 between 1974-1989. Sustained US inflation of the magnitude required to have a negative real return from buying US government bonds today (at 4.5% yield) has, therefore, only occurred alongside world wars as well as the global energy shock of the 1970s. In other words, as Deutsche puts it, "Treasuries are likely to be at least a competitive asset class for the long-term value investor."

Despite the re-emergence of a 'proper' yield in the bond market, multi-asset investors must not forget that one can also put together equity portfolios today with very attractive future return profiles and highly

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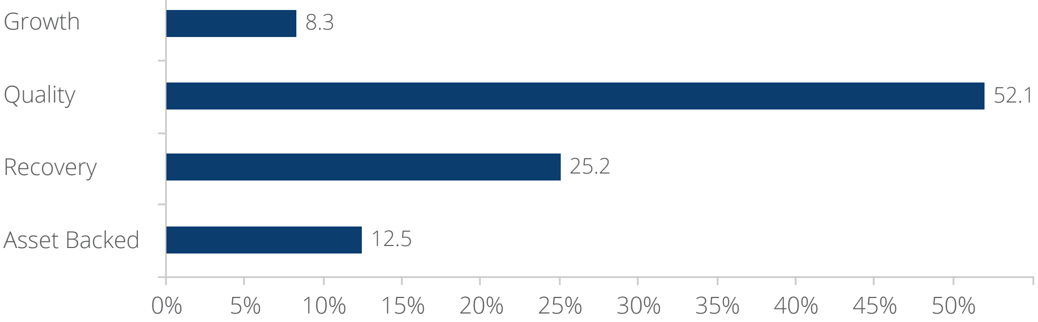
[10] *The basic assumption of this scenario is that no further policy actions are taken beyond what has been announced to date.*

asymmetric risk-reward. Offered the choice of tying up savings for 10 years in a government bond yielding 4.5% or a well-diversified portfolio of equities with an earnings yield of 8% today but, crucially, where that yield should rise to over 20% due to earnings growth, we think investors should select the latter. These are, in fact, the characteristics of our current portfolio, which we think offers outstanding value today.

Thank you for your ongoing support.

PVT CATEGORIES OF POTENTIAL (%)

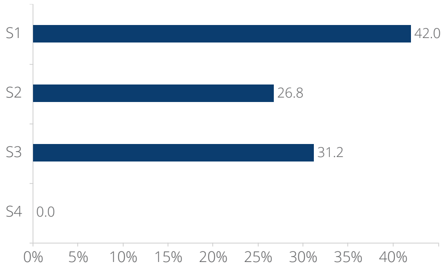
This chart shows the weighting of the fund's holdings across the four categories of Potential, related to the stages of a company's life cycle, as defined within the R&M investment philosophy known as 'PVT' – Potential, Valuation, Timing.



Source: River and Mercantile Asset Management LLP

SUSTAINABILITY ANALYSIS (%)

The weighting of the portfolio across our four sustainability scores



Source: River and Mercantile Asset Management LLP

SUSTAINABILITY SCORES

Our analysis determines a sustainability 'score' for each company we look at. These are broadly categorised as follows:

S1 – a sustainability leader in its field and/or a clear beneficiary of sustainable trends

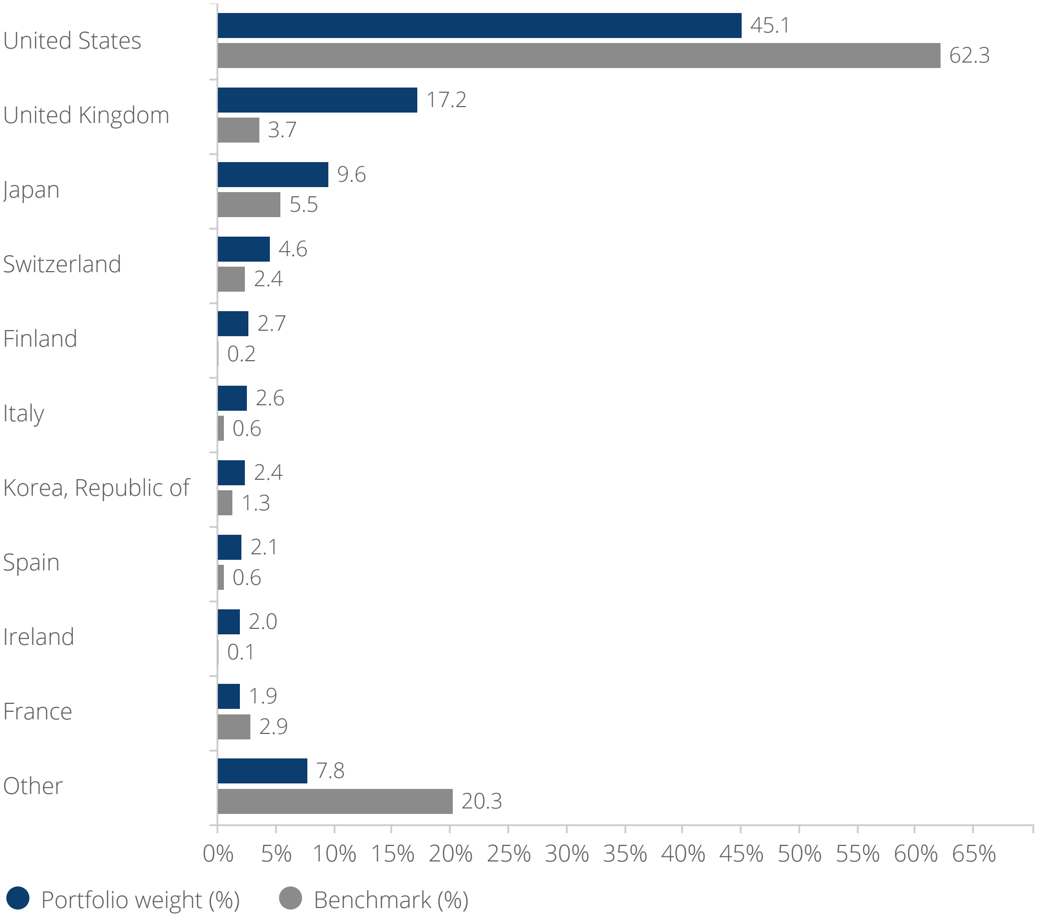
S2 – Solid SPVT credentials and no clear impediment to value creation or share price performance

S3 – SPVT improvement required, but evidence that this has started and/or of engagement potential

S4 – SPVT a clear barrier to value creation, no evidence of improvement and/or low likelihood of engagement success (including failed attempts)

COUNTRY WEIGHTS (%)

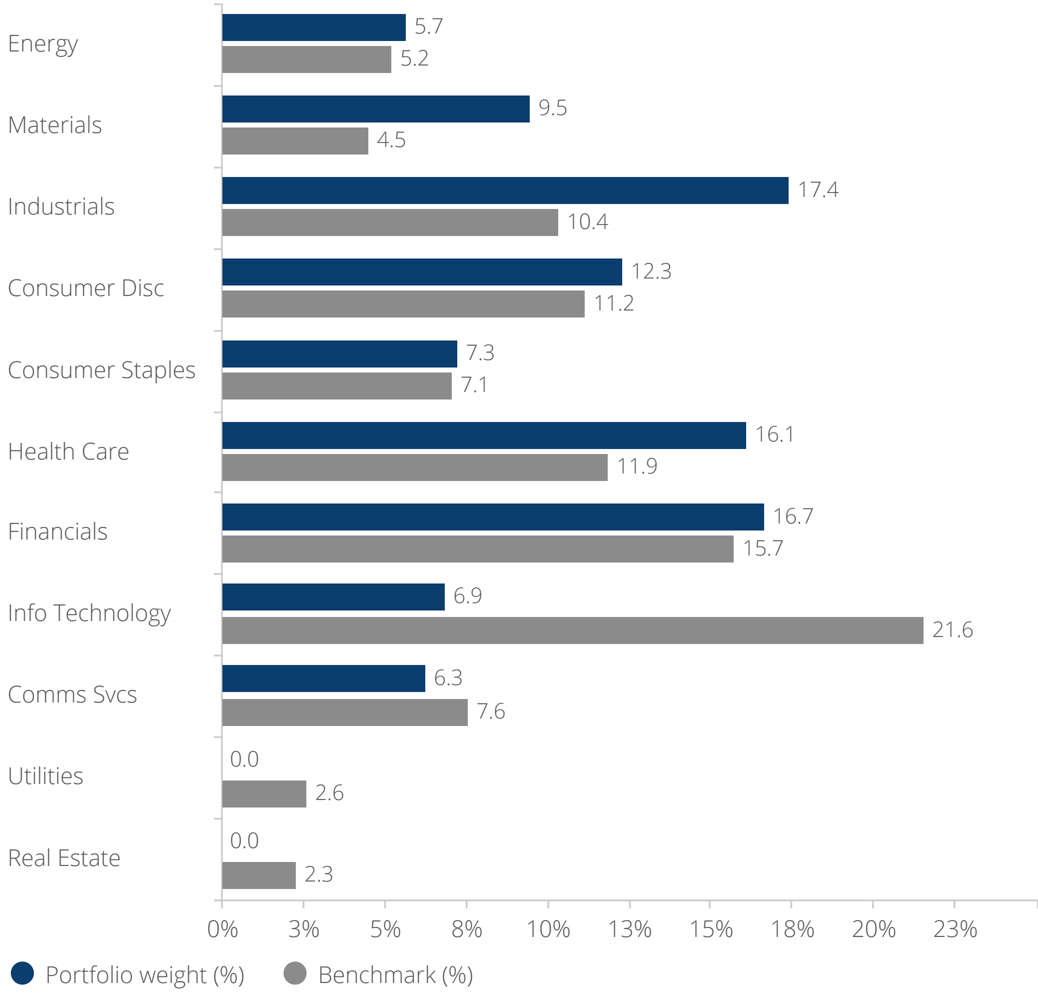
This table shows a comparison of fund and benchmark weightings across a range of company values



Source: Bloomberg LP

SECTOR WEIGHTS (%)

This graph shows a comparison of fund and benchmark weightings across the sectors classified by the MSCI Global Industry Classification Standard (GICS).



Source: Bloomberg LP

TOP 10 HOLDINGS (%)

The ten largest positions by weight held in the portfolio.

	Weight (%)
McKesson	4.1
Baker Hughes	4.0
Booking Holdings	3.9
Fiserv	3.6
Henry Schein	3.3
Alphabet class A	3.2
Sony Corp	3.0
Roche Holdings	2.9
Tate & Lyle	2.6
Danieli & C Officine	2.6

Source: River and Mercantile Asset Management LLP

STOCK LEVEL PERFORMANCE ATTRIBUTION (%)

This table shows the best and worst contributors to the fund's performance relative to the benchmark. The average active weight highlights whether the fund held a larger or smaller position in a stock than the benchmark did, on average over the period. As performance is relative to the benchmark, outperformance of the benchmark can come from the fund holding a larger position than the benchmark in a stock that performs well, or a lower position than the benchmark (or even a zero holding) in a stock that performs poorly. The contribution to active return is the return that the position has contributed relative to the benchmark.

Greatest Positive Contribution	Average Active Weight (%)	Contribution To Active Return (%)
Booking Holdings	3.63	0.64
Baker Hughes	4.05	0.59
Apple	-4.58	0.42
Danieli & C.Officine	2.00	0.36
UBS Group	1.46	0.35
McKesson	3.62	0.24
Mondi	1.75	0.23
UPM-Kymmene	1.19	0.21
Toyota Industries	1.37	0.20
Verallia	1.16	0.19

Greatest Negative Contribution	Average Active Weight (%)	Contribution To Active Return (%)
Smith & Nephew	2.31	-0.51
Prudential	2.09	-0.46
Nikon	1.93	-0.34
Fiserv	3.80	-0.29
Sony Corp	3.08	-0.29
Valmont Industries	1.74	-0.27
T Hasegawa	2.22	-0.24
Kenvue Inc	0.71	-0.22
Roche Holdings	2.67	-0.21
Metso Outotec	1.78	-0.20

Source: Bloomberg LP

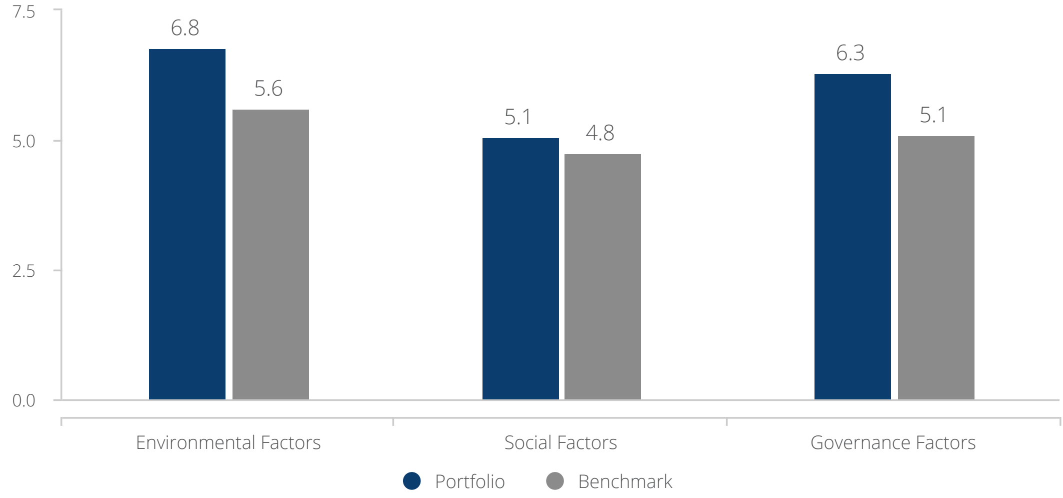
ENVIRONMENTAL, SOCIAL AND GOVERNANCE (ESG) FACTOR ANALYSIS

This report is designed to give a broad overview of the portfolio from the perspective of Environmental, Social and Governance factors. Whilst the portfolio is not run to be optimised with these factors in mind, we may expect to take major risks into consideration when analysing stocks.

This table compares the portfolio and benchmark asset weightings by value with data from MSCI ESG Research.

	Portfolio (%)	Benchmark (%)
Assets covered by MSCI ESG Research	96.2	99.8
Assets scoring in the bottom decile	0.0	0.3

The chart below illustrates how the portfolio and its benchmark compare on average Environmental, Social and Governance scores. Scores are based on a 1 to 10 scale, where 1 is the lowest/worst and 10 is the highest/best.



10 highest rated ESG companies held by fund	Portfolio Weight (%)	Benchmark Weight (%)	Company Rating	Industry Adjusted Score
SONY GROUP CORP	2.97	0.17	AAA	10
TATE & LYLE PLC	2.64	0.00	AAA	10
NIKON CORP	1.67	0.00	AAA	10
METSO CORPORATION	1.42	0.01	AAA	10
SAP	1.35	0.22	AAA	10
HARLEY-DAVIDSON INC	1.24	0.00	AAA	10
MONDI PLC (GB)	2.48	0.01	AAA	9.7
UPM-KYMMENE	1.28	0.03	AAA	9.7
WATERS CORP	2.12	0.03	AAA	9
HITACHI	1.74	0.10	AA	8.5

10 lowest rated ESG companies held by fund	Portfolio Weight (%)	Benchmark Weight (%)	Company Rating	Industry Adjusted Score
DANIELI & C OFFICINE MECCANICHE SPA	2.58	0.00	BB	3.5
FEVERTREE DRINKS PLC	1.24	0.00	BB	3.9
TALGO SA	2.10	0.00	BB	4.1
ALPHABET A	3.23	1.27	BBB	4.7
TOYOTA INDUSTRIES CORP	1.22	0.02	BBB	4.7
KLA CORPORATION	1.47	0.10	BBB	4.8
CARLISLE COS	2.31	0.02	BBB	5.2
VERALLIA SA	0.35	0.00	BBB	5.2
WILLIS TOWERS WATSON	2.17	0.04	BBB	5.7
ROCHE HOLDING GENUSS	2.93	0.32	A	6.1

Source: MSCI ESG Research, ©2022 MSCI ESG Research LLC. Reproduced by permission.

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