Manager's Letter
1st Quarter 2019

Andrew Dalrymple

The final quarter of 2018 was a painful one for equity investors, and the Strategy suffered a good deal of damage, eradicating all of the gains made during the year. It is therefore a relief, and very pleasing, to see much of that lost ground being regained.

Fortunately, as has quite often been the case in the last ten years, **the fears that prompted the slide in markets at the end of 2018 have so far proved groundless**. There was much comment about a slowdown in China, and great concern about an escalating trade war between China and America. After the US economy had recorded very strong growth for the first half of 2018, it looked likely that the Federal Reserve would continue to raise interest rates, and at an accelerating speed. In the event, Chinese GDP data was solidly reassuring, and the Federal Reserve has made it clear that with little or no inflationary pressure in America, the likelihood of material rate rises in 2019 was low. Bond yields fell back, and equity markets have enjoyed a very good spell.

As is so often the case, the real impetus in January, which set the tone for the quarter, came from our **US equity exposure**. The fourth quarter results season went extremely well, with excellent figures being reported by many of our American holdings. **Exact Sciences** (colon screening) guided 2018 revenues to a 71% increase, while **Tactile Systems** (lymphedema treatment) stated that it expected fourth quarter revenues to be substantially higher. **Intuitive Surgical** (robotic surgery) and **Abiomed** (heart pumps) completed this robust medical devices picture, reporting sales growth of 17% and 30% respectively. All of these stocks made excellent progress in January, and indeed, **Exact Sciences** gained 43%. Elsewhere, **Paypal** and **Visa** both confirmed the robust health of the payment services sector.

February saw further gains as the last of the fourth quarter results season drew to a close. **Match**, the provider of the ubiquitous Tinder application, announced a 17% growth in subscribers, and a 21% increase in revenues. **Chegg**, which provides online educational facilities, also revealed extremely strong sales growth, and maiden profitability. Finally, both **ServiceMaster**, and **Zebra Technologies** came out with outstandingly good figures, sending both stocks up by around 15% over the month.

Your Investment Manager undertook a **research expedition to America in early March**, from which a number of strong prospects were identified, and **Dexcom**, the leader in constant glucose monitoring devices for diabetics, was repurchased. Type One Diabetes is a potentially disastrous affliction if not properly managed, and **Dexcom** has developed a discreetly wearable device, which monitors blood sugar levels, and which can be read via an App on a smart phone. It replaces the painful, and in many ways unsatisfactory alternative of finger sticking, and is life changing for diabetics. The stock has risen a long way since the company started to generate substantial revenues in 2014, but the opportunity still seems astonishingly good, especially as they are starting to address the huge, and massively expanding, Type Two Diabetes market.

Although the Strategy had another **positive month in March**, the outperformance would have been more significant, but for one or two recalcitrant, medically orientated holdings. **Abiomed** (heart pumps) and **Tactile Systems** (Lymphedema treatment) were notably weak. Despite reiterating strong revenue guidance at the start of March, **Tactile Systems** lost 30% over the month, without any obviously reason, whilst **Abiomed** was sold down after announcing that they had acquired a stake in another heart pump specialist. This seemed a poor reason to provoke a 15% slide in the share price.

Nevertheless, the rest of our US holdings performed perfectly well in March, with cosmetics retailer, **Ulta Beauty**, recording a solid 12% rise, following a mid-month announcement of very good fourth quarter results. **Adobe Systems** also reported strong first quarter sales growth, although recent lower margin acquisitions held back profitability. Finally, uniform rental leader, **Cintas**, released solid, third quarter numbers, and propelled by a fresh wind from the stock market, **Penumbra**, **Amazon**, **Zoetis**, **Paypal**, and **Visa**, all rose by between 5% and 10%.

At the end of last year, we expressed the strong opinion, that **Asian markets looked very good value** and we moved to add **TAL Education**, one of China's pre-eminent online education providers to the portfolio in January, as well as leading kitchen appliance maker **Hangzhou Robam**. Most Asian soldiers and sailors were severely wounded in battles at the end of 2018 and had been recovering in the sick bay since. But by the end of January they were showing good signs of life. Accordingly, **Alibaba** (e-commerce) reported third quarter results, with revenues 41% higher than a year ago, and earnings per share up by 32%. The shares rose by 23% over the month. Hard on its heels was **Baozun,** which, in contrast to it's 17% fall in December, the stock rose by 22.5% in January.

Asian markets also benefitted from the prospect of a trade deal between China and the USA, and increased optimism about earnings prospects. Although nothing tangible has yet been announced, the trade talks are said to be making progress, which must surely be a good sign. This clearing of the skies had a particularly beneficial effect on our US listed China ADRs, which are primarily focussed on e-commerce. **Alibaba** gained almost 10%, in February, while **TAL Education** rose by 14.7%.

Baozun (logistics) posted a rise of 11% and saw annual sales rise by over 40%, while sportswear retailer, **Li Ning**, also exceeded forecasts, sending the shares up by 10%. Top performer was hot pot flavouring specialist, **Yihai**. Hot pot restaurants seem to be all the rage in China, given that sales rose 63% in 2018, with profits more than doubling. Sometimes such news is "in the price", but not this time, since the shares gained 41% in March alone, making them the top contributor to the Strategy progress for the entire quarter. There was little significant corporate news in India, but with the Sensex Index up by around 8%, **Bata Shoes** rose by 9%, while watch and jewellery retailer, **Titan**, gained 11%. Both companies reported some entirely unimpeachable third quarter results in February.

As at the end of Quarter 1 **the Strategy is fully invested and remains heavily weighted towards America and Asia**, still the two highest growth areas of the world. In Asia, the Strategy is invested only in consumer facing companies, which, in our view, represent a long term, sustainable, and much less cyclical growth opportunity. In the United States, the focus is very much towards technology, medical technology, and the services sector, all areas where we believe Americans tend to excel. We look forward to and expect to be able to report on further good progress at the end of June.

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