Made in Italy Fund

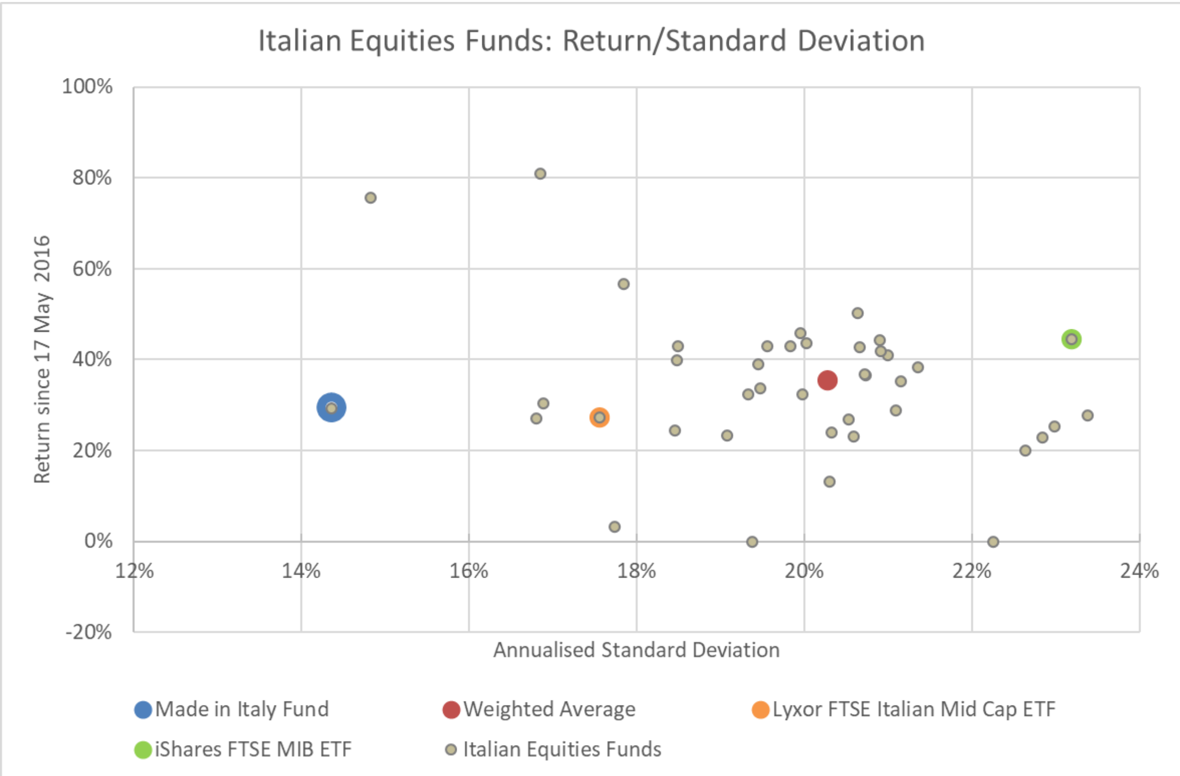
Bayes Investments

Investor letter – Fourth Quarter 2020

Dear Fellow Investors,

The Made in Italy Fund (MIF) had a return of 10.0% in the fourth quarter of 2020. The return since inception (17 May 2016) is 29.4%. Returns are net of fees and all administration costs.

In the quarter the MIF was behind the Italian Equities fund universe, whose weighted average return since MIF's inception is 35.4%:



Source: Factset

The MIF return remains above the 27.3% return of the most comparable ETF – the Lyxor Mid Cap Fund – but is below the 44.5% return of the main Italian Equities ETF – the iShares FTSE MIB.

The MIF return continues to be accompanied by lower volatility. The annualised standard deviation of its daily returns is 14.4%, compared to 20.3% for the weighted average fund, 17.6% for the Lyxor ETF and 23.2% for the iShares ETF.

Fourth Quarter 2020

Our 10.0% return for the quarter compares with a weighted average return of 14.1% for the Italian Equities universe, 11.8% for the Lyxor ETF and 16.9% for the iShares ETF.

Q4 was a volatile quarter for global equities and in particular for Italian equities, with a strongly negative October followed by an extraordinarily positive November. Our Fund fell in line with the main market in October, but less relative to the reference Small Cap index, thus recouping the September underperformance. However, despite registering a vigorous rebound in November, it could not keep pace with a roaring rally in the broader market. This was partially compensated by another positive month in December, ahead of a nearly flat market performance. But the net result for the quarter was a lagging relative performance, which, combined with a poor Q3, delivered a subpar outcome for second half of the year.

Many of our stocks did well in the quarter. Above all our June IPO investment **CY4Gate**, which shot up 95%, closing the year at 8.6 euro, 173% above its 3.15 euro IPO price. We had doubled our position in September at 4.4 euro. **Landi Renzo** was up 56% in the quarter, strongly rebounding from its Q3 decline and well on the way to regaining its pre-pandemic price level at which we presented the company at the Spanish Value Investing conference in April 2019. Other strong performances came from **Be Shaping the Future**, up 37% in the quarter and 18% in the year, **Openjobmetis**, up 29%, **Longino & Cardenal**, up 23% in a healthy recovery from its Q3 fall – we increased our position in October – and once again **SeSa**, up 20% in the quarter and 116% in the year, coming on top of a 109% appreciation in 2019. The other June IPO **Sebino** also did well, up 18% in the quarter to 2.8 euro, 40% above its 2.0 euro IPO price. Two other Q3 decliners, **Expert System** and **B&C Speakers**, registered good rebounds in the fourth quarter, up 13% and 11% respectively, while **Finlogic** had a more modest recovery, up 6% in the quarter but ended the year almost unchanged, thanks to a positive performance in the turbulent first half. In keeping with its high volatility, and testing our resolve to stick with a company we continue to think of as a great investment opportunity, **Askoll EVA** added to its Q3 fall in October but was up 49% in November, only to fall again -10% in December and ending the quarter down -1%.

Decliners in the quarter included our recent addition **Portale Sardegna**, down -18%, and **MailUp**, down -12%. There was no reason for either price move. **Renergetica** was down -5% in the quarter, but thanks to its positive performance in the previous two quarters ended the year up 36%.

During the quarter we sold out of four positions and participated in two new IPOs:

Esi is a renewable energy operator providing Engineering, Procurement and Construction (EPC) and Systems Integration services. The EPC unit provides turnkey solutions for alternative energy projects, including the development and revamping of photovoltaic systems. The System Integrator unit engages in the implementation of integrated technologies for the supply of electricity to remote areas and for building renewable energy storage systems. The company has a market capitalization of 16 million euro and is expected to report 2020 revenues of 16.5 million, with a 14% EBIT margin. Both sales and margins will grow in the next few years as the company pursues its ambitious expansion programme at very high returns on invested capital. We paid an IPO price of 2.1 euro per share in October and the stock ended the year up 39% at 2.9 euro.

Tecma Solutions provides technological solutions for the real estate sector, including property investment, space planning and marketing services. The company came to the market in November at a valuation of 22 million, with 2020 revenues expected to be around 8 million and Net Income of 2 million, both expected to grow rapidly in the next few years. The IPO was priced at 4 euro per share and we doubled our position in mid-December at 5.8 euro. The stock ended the year up 65% at 6.6 euro.

The current sector composition of the Fund is the following:

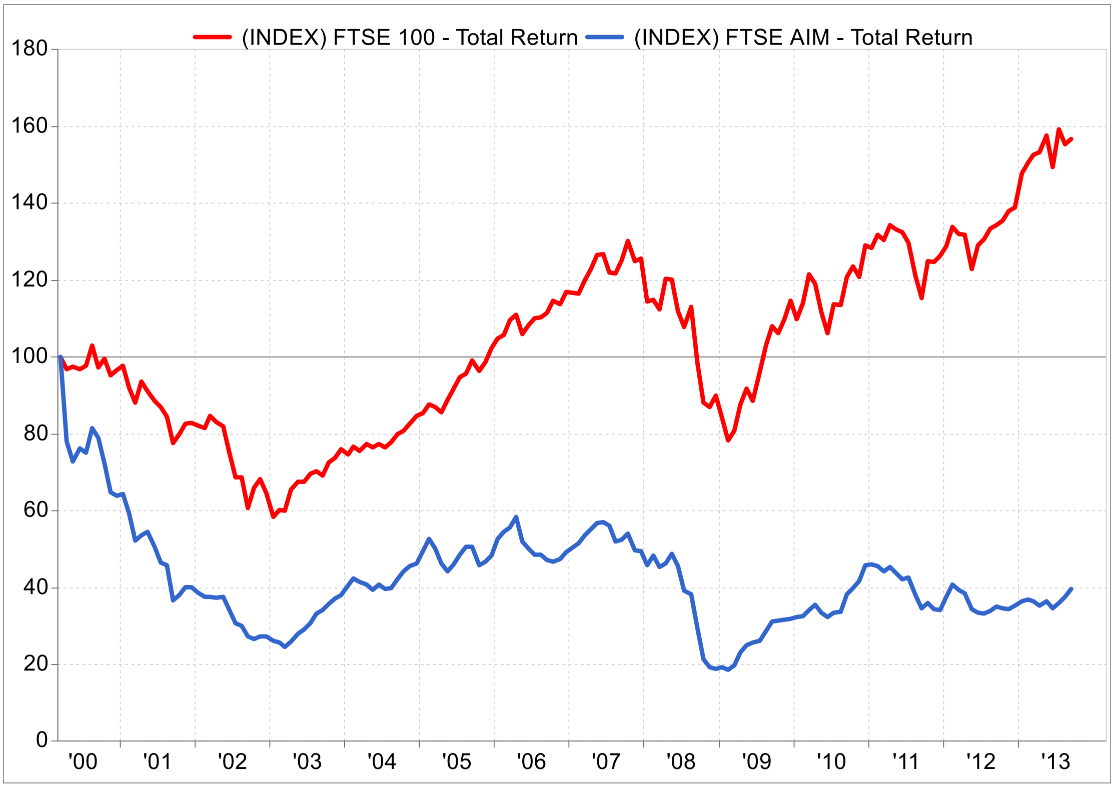
	Number of companies	% Weight
Producer Manufacturing	5	14.2%
Electronic Technology	1	1.9%
Process Industries	3	13.2%
Consumer Non-Durables	1	2.7%
Consumer Durables	2	6.3%
Industrial Services	1	5.5%
Commercial Services	4	15.8%
Consumer Services	2	5.3%
Technology Services	7	21.6%
Health Technology	1	1.8%
Communications	1	4.8%
Utilities	2	5.9%
Total	30	98.9%
Cash		1.1%

A one year reset

As a result of the second half relative weakness, the advantage gained by the Fund in the first half of the year turned into underperformance for the whole year, with the MIF down -10.5%, versus -3.7% for the weighted average fund, -4.6% for the Lyxor ETF and -3.9% for the iShares ETF.

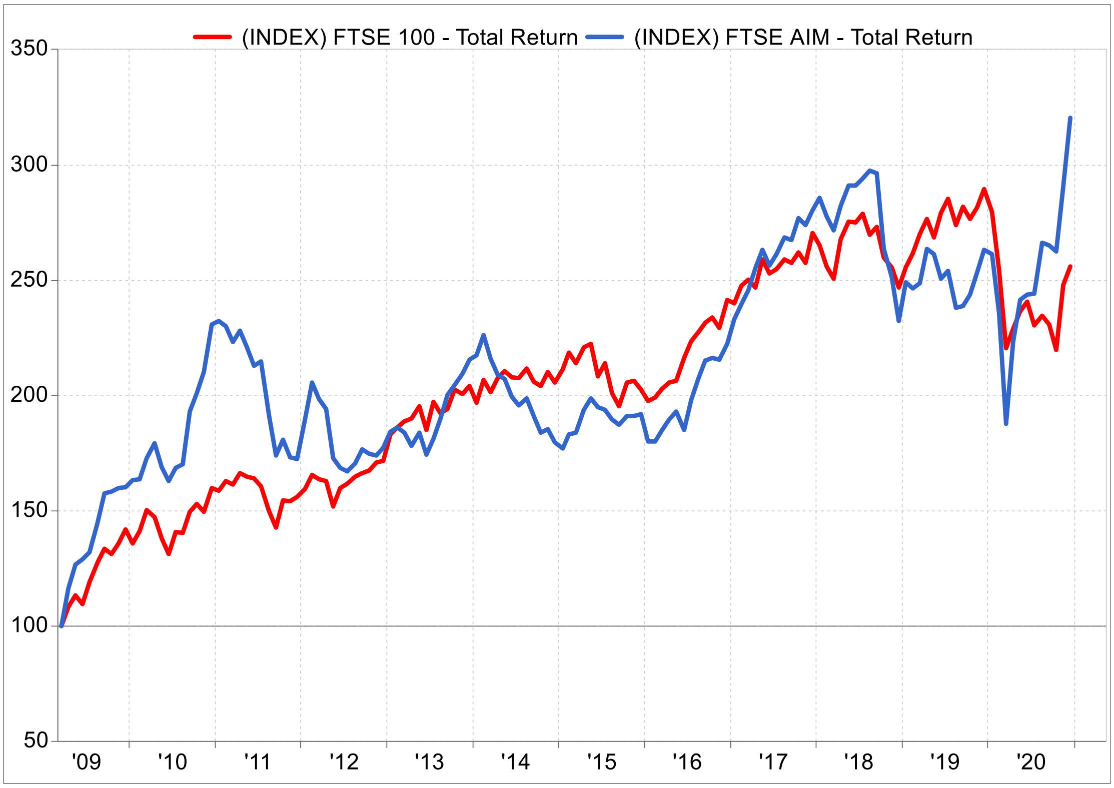
The year started well, with the Fund regaining its 2017 High Water Mark in mid-January, after a negative 2018 and the subsequent recovery in 2019. But, soon after, the pandemic derailed the process, causing the downturn documented in our Q1 letter. Markets had a partial recovery in Q2 and, while in negative territory, the Fund ended the first half ahead of most market indices, also thanks to the continued outperformance of small cap stocks that started in Q4 2019. However, the recovery stalled in Q3 and – as we have just seen – resumed in Q4 at a subdued pace, resulting in a disappointing year-end outcome.

We have seen in the Q3 letter how this is related to our move towards smaller capitalisation stocks, mostly quoted on AIM Italia. We have also seen that AIM Italia has been underperforming the broader market for several years, unlike its UK and Euronext counterparts. We can see here, however, that AIM UK itself had teething troubles in its early years:



Source: Factset

and that only after becoming a more mature market – notably towards the end of the 2008 global equity falloff – it started to express its pent-up value:



Source: Factset

We started 2020 with the expectation that it would have been a good year for smaller capitalisation stocks, after two years of underperformance that had just started to reverse, and before the resumption of PIR investments in the wake of the new PIR law that had just been approved. The pandemic forced upon us a major reset. But at the beginning of 2021 we believe at least as strongly that conditions are again in place for a significant move. In fact, the sluggish second half performance increases our confidence for the new year and bodes well for our recent SCM alliance.

SCM alliance

We are glad to report that at the beginning of December Bayes Investments signed an important agreement with SCM SIM.

SCM SIM is an Italian asset management and advisory company quoted on AIM Italia, with one billion euro assets under control. SCM has been the first financial institution to launch an investment line for the management of Alternative PIR accounts, and has chosen Bayes Investments as the advisor for the management of the 70% Italian equities component.

We are also happy to report that, following the SCM agreement, Antongiulio Marti has joined Bayes Investments as co-manager of the Made in Italy Fund and the SCM PIR line.

Antongiulio has been an equity manager with SCM SIM from 2015 to 2020, where he was also responsible for corporate advisory and Club Deals. In 2020 he founded HOOP**,** a company specialized in majority or minority investments in Italian SMEs, listed and non-listed, through the Club Deal formula. HOOP's mission is to extract value, in the medium term, from the Italian entrepreneurial fabric. In recent years he has completed several activist transactions on Italian listed companies, starting corporate turnaround processes through governance changes.

Antongiulio graduated in Economics and Finance from Bocconi University in Milan. He is also a founding member and President of AIEDA – Italian Association for the Exercise of Shareholders' Rights – a non-profit association created with the aim of promoting and encouraging the activism of the shareholders of Italian listed companies and the presentation of lists of candidates for the election of members of corporate bodies.

The launch of Alternative PIRs is a very important step, not only for us and SCM, but for Italian companies, savers and the entire financial system. So let us review the subject once again in more detail.

Like the original PIRs (Piani Individuali di Risparmio: Individual Savings Plans) launched in 2017, Alternative PIRs enjoy a significant tax advantage: exemption from capital gains tax – currently 26% – after a 5-year holding period. Both are also exempt from inheritance tax.

This substantial incentive stems from the legislator's desire to increase the share of Italian savings invested in the country's small and medium-sized enterprises (SMEs) in order to promote and finance their growth. To this end, both original and Alternative PIRs must be invested for at least 70% in securities of Italian companies.

But there are two important differences between original PIRs and Alternative PIRs:

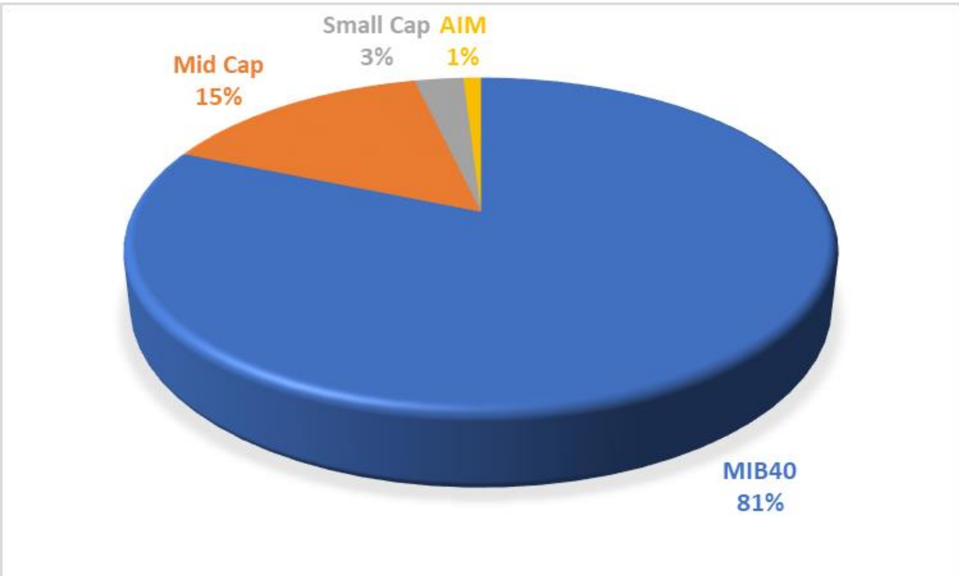
1. In original PIR accounts, only 5% of 70% – or 3.5% of the total – must be invested in SMEs. The rest can be invested in the top 100 stocks in the market – the top 40 included in the MIB40 index and the next 60 included in the Mid Cap index.

In Alternative PIR accounts, on the other hand, the whole of 70% must be invested in SMEs.

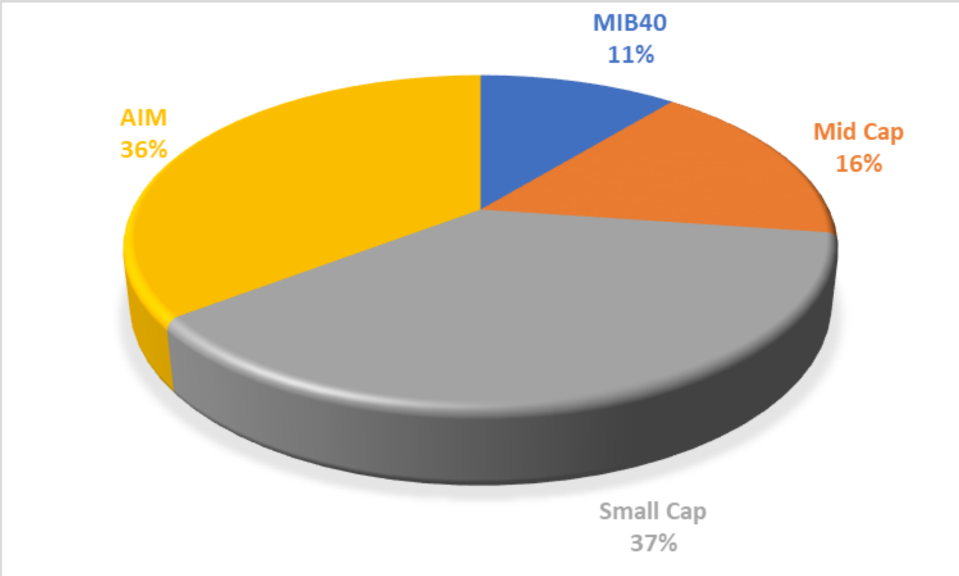
2. In original PIRs it is possible to invest up to a maximum of 30,000 euro per year.
   In Alternative PIRs, on the other hand, one can invest ten times as much, up to a maximum of 300,000 euro per year.

Therefore, Alternative PIRs respond in a much more targeted and effective way to the goal of channelling Italian savings to the country's SMEs.

There are currently about 370 companies listed on the Italian Stock Exchange, for a total value of about 590 billion euros. Of these, the top 40 in order of capitalization are included in the MIB40 index and have a total value of about 480 billion, or 81% of the total. The next 60 are included in the Mid Cap index and have a total value of 88 billion, or 15% of the total. Thus the top 100 companies account for 96% of total market value. The remaining 270 companies are worth only 4% of total. These are the SMEs that most need the support of Italian savers. About half of them are listed on the main market and are worth about EUR 16 billion, while the other half are listed on AIM Italia and are worth around EUR 6 billion:



The 3.5% allocated to SMEs in the original PIRs is therefore equivalent to their market weight. Original PIRs offer an incentive to invest in Italian companies, but, despite the dictates of the law, they are not specifically aimed at SMEs. It is only with Alternative PIRs that the fundamental objective of the PIR Law is fully achieved. In Alternative PIRs, the entire 70% destined for Italian companies must be invested in SMEs. SMEs account for only 4% of total market value, but are almost three quarters of the number of listed companies:



270 companies with a total value of about 22 billion. This is the universe on which Alternative PIRs will focus. By channelling Italian savings to listed SMEs, Alternative PIR will make an essential contribution to financing their growth, enhancing their value and increasing their liquidity.

Against this background, SCM and Bayes expect high returns for the Alternative PIR investment line. Returns will be made even more attractive by the substantial tax advantage, which at the end of 5 years will grant exemption from capital gains tax, equal to more than a quarter of the cumulative return.

To see first-hand the importance of the tax exemption, let us assume an investment of 100,000 euro and an average annual return of 10%. At the end of the 5 years, the value of the investment will have risen to 161,051 euro, making a capital gain of 61,051 euros. If this were taxed at 26%, the gain would be reduced to 45,178 euros. The difference, equal to 15,873 euro, is the extra return resulting from the exemption. In percentage terms, the cumulative yield is 61.05%, compared with 45.18% of an equivalent taxed return. The extra yield is therefore 15.87%, or 26% of gross yield. In order to have the same return, an investment subject to taxation would have to achieve an average annual return of 12.79%.

With the new year, we would therefore encourage our Italian tax resident readers to consider an investment in the Alternative PIR investment line of SCM SIM.

With the new year, we would therefore like to encourage our readers with an Italian tax residence to consider an investment in the Alternative PIR investment line of SCM SIM, of which we summarize the considerable advantages:

1. A high expected return from investing in the most attractive Listed Italian SMEs.
2. A substantial tax advantage, equal to 26% of the cumulative return.
3. A zero inheritance tax.
4. Highly competitive SCM SIM management costs.
5. A contribution to the country's economic growth, through financial support to SMEs that are most in need of capital.

Here you can find the [SCM SIM brochure.] We are at your disposal for any further information.

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