Ennismore Global Equity Fund

Investor Newsletter for the month of March 2023

Issued on 12 April 2023

Fund Details

Daily dealing UCITS and Irish Central Bank regulated open-ended investment company with Financial Conduct Authority recognition and registered in Ireland. The Fund size was USD 131m as at 31st March. Total assets under management by Ennismore Fund Management were USD 584m. The number of shares issued by our funds is capped in order to limit the level of assets under management in each strategy. We currently have capacity available in the Global Equity Fund. If you would like more information or to invest please contact Adam Sullivan on +44 (0) 20 7368 4224 or email subs@ennismorefunds.com.

Performance as at 31 March 2023

	Share Class[1]					
	GBP	**GBP A**	**EUR**	**CHF**	**EUR I**	**USD I**
NAV per Share[2]	12.69	12.63	12.55	11.43	9.73	9.99
	% Change					
March 23	0.1	0.2	-0.2	-0.3	-0.1	0,2
2023 to date	1.6	1.6	2.6	3.2	1.1	1.7
Annualised return[3]	3.7	3.7	3.6	2.1	-0.6	-0.0
Since launch[3]	26.9	26.3	25.5	14.3	-2.7	-0.1
Note: All performance figures net of fees. **Past performance is not a guide to future returns.**						

Comments below on performance refer to GBP A NAV per share unless otherwise stated, exclude fx and interest contributions to cash and are prior to expenses.

The Fund's NAV increased by 0.2% in March. Our long book cost 1.0% while our short exposure contributed 1.1%.

After a strong second half of 2022 in a choppy market, the Fund had a rather more pedestrian first quarter of 2023 in a much stronger market environment that was less favourable to our positioning. The Fund was up 1.6% on an average net exposure of 32.5%. Our beta adjusted net exposure averaged 19% during the quarter. With the MSCI World Index +5.1% in GBP terms, we modestly outperformed relative to our implied market exposure. January in particular saw a "junk rally" which was challenging for our short book, whilst decent performance in the major US indices in March was dominated by a small handful of megacap tech companies in an echo of the mid-2020 rally – as you would expect, we are not invested in these names. In this environment we see this as a respectable performance.

Our long book contributed +5.0% from an average exposure of 76.0%, for an implied return of +6.6%. The largest contributors were Buzzi Unicem (+1.2%) which reported strong preliminary numbers for 2022 as discussed in our February letter, and Moneysupermarket.com (+1.1%) where the market has begun to price in the benefit of rapidly increasing UK motor insurance premiums on switching activity. The largest detractors were Schibsted ASA (-0.6% net of Adevinta hedge) which frustratingly appeared to step back from what investors had begun to expect was a near-term distribution of its Adevinta stake and Tucows, Inc (-0.6%) which was weak alongside other US fibre network builders, exacerbated by its significant leverage.

Our short book detracted -2.7% with an average exposure of 43.5%, for an implied stock return of +6.2%. Given the skew of our short exposure and the outperformance of low-quality companies this year, we are not disappointed with this. The only significant detractor was the recently renamed Riot Platforms ("Riot", -1.0%) which benefited from a recovery in the price of Bitcoin. As we discussed in our December letter, we believe crypto mining is a truly terrible business. Riot is using hardware on which it spent multiples of today's replacement cost only 12-18 months ago, yet it trades at a premium to book value. The excess capital that flowed into the industry is illustrated by the rapid increase in the "network difficulty" of bitcoin mining - i.e. how many computations are required to "mine" a bitcoin. This has largely offset a pretty sharp rally in the bitcoin price: since the end of June last year Bitcoin is up 49% in USD but network difficulty has increased 62%. This is outpacing even Riot's share count, at least in the short term! Our view on the sector, and Riot in particular, is unchanged. There were no large contributors in the short book, but we had several strong idiosyncratic short performers, for instance Direct Line Group plc (+0.3%), which profit warned again and replaced its CEO, and Silvergate (+0.3%), one of three prominent US bank failures in the quarter.

[1]Source: Administrator, Net Asset Value, net income reinvested.
[2]Source: Administrator, Net Asset Value.
[3]Since inception of GBP, GBP A, EUR and CHF share classes on 03/10/16, EUR I share class on 03/07/18, USD I share class on 02/01/19

Top Five Contributors and Detractors for March 2023

Contributors	MTD (bp)
Moneysupermarket.Com Group Plc	42
STO SE & Co KGaA	37
Hong Kong software company	33
Silvergate Capital Corporation	29
Deliveroo Plc	29

Detractors	MTD (bp)
Schibsted ASA	-96
Riot Platforms Inc	-56
thyssenkrupp AG	-34
Admiral Group Plc	-30
Ascential Plc	-27

Top Five Long Holdings as at 31 March 2023

Company	Country	Sector	% of NAV
Buzzi Unicem SpA	Italy	Materials	6.1
thyssenkrupp AG	Germany	Materials	4.8
Schibsted ASA	Norway	Communication Services	4.6
D'Ieteren Group	Belgium	Consumer Discretionary	4.3
Admiral Group Plc	United Kingdom	Financials	4.1
			23.9

Exposures as at 31 March 2023

Longs%	Shorts%	Gross Exposure%	Net Exposure%
76.5(73.5)	40.9(43.9)	117.4(117.4)	35.6(29.6)

Figures in brackets refer to previous month end. All exposures are calculated on a delta adjusted basis. All calculations are subject to the impact of rounding.

Exposures by Country, Market Cap & Sector as % NAV and Positions as at 31 March 2023

Country	Gross%	Net%
United States	37.9	-19.4
United Kingdom	25.1	23.8
Germany	9.8	9.8
Norway	7.1	2.9
Italy	6.6	5.5
Sweden	5.7	1.3
Belgium	4.3	4.3
Japan	2.9	2.9
Mexico	2.6	2.6
Hong Kong	2.4	-1.7
Austria	2.2	-0.1
Switzerland	2.1	-0.2
Spain	1.6	1.2
South Korea	1.6	1.6
Ireland	1.2	1.2
Brazil	1.1	1.1
Australia	1.0	-1.0
Other	2.0	-0.3

Market Cap	Gross%	Net%
>$10bn	19.2	1.1
$5bn - $10bn	18.7	9.3
$1bn - $5bn	64.5	27.5
<$1bn	15.0	-2.3

Positions	Mar	Feb
Long	47	45
Short	78	81
Longs Opened	2	2
Longs Closed	0	4
Shorts Opened	4	10
Shorts Closed	7	7

Sector	Gross%	Net%
Communication Services	18.6	12.5
Consumer Discretionary	18.4	5.4
Consumer Staples	6.3	2.8
Energy	0.0	0.0
Financials	14.1	9.7
Health Care	3.9	-3.6
Industrials	18.5	-4.6
Information Technology	18.3	0.6
Materials	16.8	13.0
Real Estate	2.1	0.1
Utilities	0.0	0.0
Other	0.4	-0.4

Geographic analysis relates to country of incorporation or listing. This may not represent the underlying economic exposure of the operating business.

Change to portfolio liquidity requirements

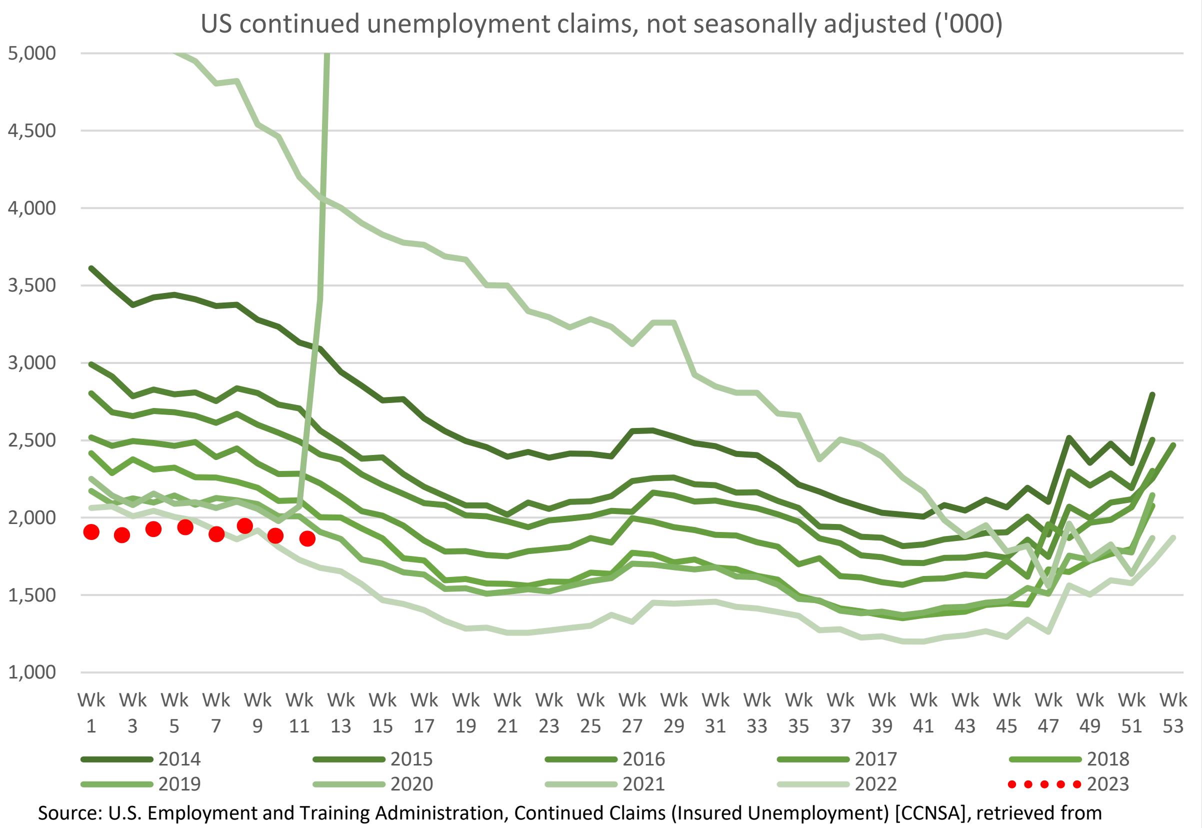
We have always run the Global Equity Fund as a highly liquid vehicle – since inception the portfolio has been managed to be liquid within ten business days, in accordance with the T+10 settlement terms for investors. Part of Ennismore's uniqueness though has always been our keenness to invest in smaller, off the beaten track companies. We have made a modest change to the Fund's liquidity terms to increase the scope for such investments within the portfolio. Under the new policy, we must be able to liquidate 75% of the portfolio within ten business days, and 100% of the portfolio within thirty business days. The portfolio remains highly liquid, but we are able to make a position such as Automatic Bank Services Limited (see our January newsletter) more meaningful for investors. At the end of March 96.5% of the portfolio could be liquidated within 5 days. It's worth noting that currently over 40% of the Fund's AUM is internal money.

Signposts of a credit cycle?

The last few months has felt like a phony macro-driven war in the equity markets between camps with different views of the economic outlook. This is a battle that we try to avoid getting involved in but is helpful to understand as over-extrapolations of macro opinions by others can lead to sharp mispricings on individual companies.

One camp has been convinced for some time that a recession is imminent based on persistently weak leading indicators, weakness in the most cyclically sensitive areas of the economy such as the housing market, and a heavily inverted yield curve. Another camp has been sanguine based on continuing strength in consumer spending – particularly in services (which dominates western economies) – the absence of any broad-based weakness in labour markets, and a perception that central bank tightening is likely almost over. Time will tell, of course, but in the meantime the market is prone to zig-zagging between, and over-extrapolating, different economic scenarios. Last autumn, for instance, many were catastrophising about the outlook for European industrial companies given the pressure from energy prices. We have benefited from the unwinding of this possibility being overly discounted in share prices with our positions in Buzzi Unicem and Thyssenkrupp, amongst others.

In our minds the odds have tilted in favour of the doomsayers in recent weeks. Credit card data shows that US consumer spending growth has slowed materially since February, whilst labour market conditions are clearly loosening: see the chart below of continuing unemployment claims which is not following its normal seasonal pattern. An uptick in consumer credit delinquencies has broadened from subprime to mainstream borrowers. Most dramatically, several large banks collapsed or had to be rescued.



Source: U.S. Employment and Training Administration, Continued Claims (Insured Unemployment) [CCNSA], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/CCNSA, April 11, 2023

We see all of this as characteristic of a credit cycle – which are different each time, of course, but follow familiar patterns. Leverage and excesses build whilst credit is easy and the economy is strong. The labour market and perhaps commodity and other supply chains become tight, driving inflation higher, artificially boosted in this cycle by significant monetary and fiscal liquidity injections. Monetary policy is tightened to reduce inflation by slowing the economy, both directly (for instance curtailing debt-financed spending such as housing and cars) and indirectly (for instance reducing income via fewer hours worked and/or higher unemployment, curtailing lending partly through an inverted yield curve). Monetary tightening takes effect with "long and variable" lags, as Friedman wrote. We first see cracks in the most interest rate sensitive parts of the economy, or the parts where the excesses have been most extreme: housing, cars, commercial property, debt-dependent consumers, and in this cycle VC-dependent businesses. But whilst these cracks emerge, other parts of the economy are typically still humming, so the overall picture is cloudy.

However, those early cracks tend to spread, until eventually the picture becomes obvious. The marginal lending decision is more likely to be a no. Investment hurdle rates increase. Companies which fail to get funding will cut back – on both investments and employees. Investors will place pressure on companies to prioritise profits over growth. Construction projects finish and are not replaced. Consumers and companies must divert more of their income to debt service instead of consumption. Reduced housing transactions pull down associated demand such as appliances and other durables. This all flows into reduced demand, which eventually prompts layoffs as companies seek to defend margins, which can result in a reinforcing cycle. We suspect that in the longer term, the recent spate of bank failures will be regarded as signals (and accelerants) of this cycle playing out once again.

We remain open-minded, and as you would expect we have not positioned the portfolio aggressively to benefit from a recession. But we believe this is a time to be cautious, as reflected in our modest gross exposure, and our low beta adjusted net exposure. We have implemented, and continue to search for, several short positions in fundamentally weak, over-earning cyclical companies. A couple have already played out, after profit warnings prompted rapid sell-offs: for instance Shyft Group – which assembles delivery vans for the likes of Amazon – and Titan Machinery – which is a US agricultural and construction equipment dealer. But we believe this could be a profitable seam of ideas for us over the next few quarters.

Below we discuss the rationale behind our investment in D'Ieteren SA, which is a cyclically resilient business that we expect to perform well in almost any economic environment.

D'Ieteren SA ("D'Ieteren") – Belgian holding company (4.3% NAV)

D'Ieteren is a Belgian family-controlled holding company which owns a couple of automotive-related businesses, a couple of niche distribution businesses, an aspirational consumer brand, and some property assets. So far, so stodgy. There are many family-controlled companies listed on the Belgian market, and many far from inspiring. But this company has been through one of the most impactful transformations we have seen, aided by a huge turnaround in the market environment for its main asset, Belron - the windscreen repair and replacement business that trades under various brand names including Safelite, Autoglass, and Carglass.

Six years ago, Belron appeared to be an underperforming business that was being run for its employees in an ex-growth market, with unpredictable volumes and margins way below best in class. D'Ieteren had recently spent over 20% of its market cap on an expensive acquisition of a subscale aspirational consumer brand (Moleskine) with no connection to its core or its domain of expertise. Shareholders had seen zero aggregate return in twenty years.

D'Ieteren's shareholders have now made six times their money in the last five years. The recent returns have been so good that what was a pretty dismal long-term record is now respectable - since the pre-financial crisis peak in 2007, D'Ieteren has compounded at 13% per year, and by 9% over 25 years. Belron's revenues have grown 60% in five years and its operating profit has increased fivefold over the same period as a major industry tailwind has developed and management has started a journey of efficiency improvement prompted by the entry of a new shareholder and an equity-based incentive programme.

Remarkably, after such a journey, we think the stock remains very cheap.

Belron: a window of opportunity

Whilst the group's longer business heritage is in selling cars, the returns have been driven by Belron. It remains the most important asset, so we'll dedicate most of this note to it. D'Ieteren (with a partner) acquired a 68.3% stake in Belron in 1999 at an equity valuation of about EUR 400m. It gradually increased its stake to 95% through 2013 and then sold 40% in 2018 to a PE firm, CD&R. CD&R then offloaded a little under half of its stake in late 2021. Based on the 2021 transaction, the compounded capital appreciation (i.e. excluding dividends) since D'Ieteren's initial investment in 1999 is over 17% per year. D'Ieteren's achieved return is different than this, given multiple separate stake purchases and the 2018 disposal at a lower valuation.

So why has Belron been able to compound value at high teens rates for over twenty years? Repairing and replacing windscreens doesn't sound like an obviously hard to emulate business proposition. Belron only operates in developed markets, and the number of windscreens that need repairing or replacing in developed markets doesn't really grow - aside from weather-driven fluctuations, demand is closely tied to miles driven, which has grown less than 0.5% per year in the US and declined by a similar amount in Western Europe over the last fifteen years.

We believe there are two key points: scale economies and "friendly middleman" dynamics of Belron’s relationship with car insurers.

Belron is a monster in its industry. The US is by far its largest market, accounting for 60% of revenues. In the US, we think Belron has around 30-35% market share, which is almost 10x the size of its nearest competitor. And the US is far from Belron's most dominant market. In some European countries, we believe Belron accounts for perhaps two thirds of the market. This huge scale gives Belron several advantages. Belron replaced over 9 million windscreens in 2022, which makes it the world's largest purchaser of windscreen glass, even larger than VW and Toyota (which both produced a little under 9 million vehicles in 2022). And we believe this gives it a material procurement cost advantage. A second advantage of scale is the ability to manage a complex supply chain efficiently. Each car model has a different windscreen, and frequently windscreens will be updated when car models get aesthetic overhauls, whilst car models remain on the road for many years - the average age of a car in both Europe and the US is 12 years. When a car owner wants a windscreen replacing, they don't want to hang around waiting for the correct SKU to be delivered from a factory half the world away. All this means that a key element of success in the business is having a wide range of windscreen inventory in stock within reasonable distance of the service location. This is much easier to manage, particularly on the longer tail of car models which are seen less frequently, for a larger business.

Third, most windscreen repairs and replacements are covered by car insurers. Car insurers typically operate nationally. It's obviously easier for an insurance company to contract nationally with Belron than to establish a mosaic of tens or even hundreds of independent operators. There are other reasons that insurers prefer working with Belron too, but we'll come back to those.

Fourth, most of you will recognise a variation of the characteristic Belron jingle ("Autoglass Repair, Autoglass Replace" for those in the UK!). Keeping this jingle in all of your heads doesn't come for free, of course. But for any individual, a windscreen replacement is a rare event; it might happen once every eight to ten years on average. Belron wants to be the first (ideally only) operator you think of when it happens. And this requires regular (even repetitive!) brand reinforcement. Again, the economics of doing so are much tougher for a small business.

Coming back to the relationship with insurers – this is probably the most important leg of Belron's competitive advantage. We described the relationship as a "friendly middleman" dynamic. By this we are referring to a distribution construct that appears in numerous value chains, and which is a consistent and resilient creator of great businesses. There are two crucial elements to the construct: first, that there are three (or more) parties to a transaction, and that the end-customer (in our case the driver of the car) is not the one paying the supplier's bill. And second, that the party who is paying the bill has other purchase criteria which are as important as, if not more important than, price.

Over 70% of Belron's windscreen jobs are distributed through insurers. What is important to the insurer in this arrangement? Like any insurance, car insurance is a product that largely doesn't "exist" - everyone pays, but most customers get nothing back in most years. Windscreen repair or replacement is a relatively high frequency, low-cost claim, which gives an insurer an opportunity to impress its customer. The insurance company associates its brand and its reputation with the windscreen replacement operator it chooses. Insurers therefore want a smooth, easy, fast and uniform customer experience; one that gives an impression of competence and professionalism, and of course a job that is done properly. Belron understands this well and has always focused on delivering a quality experience for the driver, as illustrated by its remarkable net promoter scores (NPS) which have been consistently well above 80 for the last five years (for comparison, Apple’s NPS is 61 and Amazon 73). Speed of execution has cost implications too - insurers will often have to provide a courtesy car for their customer whilst the car is being worked on. The quicker the turnaround, the lower the rental expense. Finally, lowering the administrative burden for the insurer is an important driver - Belron is tightly integrated into the insurers' IT systems in a way that an independent operator will never be able to achieve, and offers the benefit of national coverage in most of its markets, reducing the complexity of the insurers' procurement.

Over the years Belron has steadily gained market share organically, benefiting from the advantages discussed above, and accelerated this process with a steady stream of mostly bolt-on (and self-funded) acquisitions. Growth has been boosted by healthy price-mix trends as windscreens have become larger / thinner / more complex shapes.

The historic, fairly pedestrian organic growth has been turbocharged in recent years by the emergence of a huge industry tailwind as advanced driver assistance systems (ADAS) have become ubiquitous in new cars. When a windscreen with a built-in camera or sensor is replaced, the device must be recalibrated to ensure it works properly. The implications of not doing so are potentially horrible - a malfunctioning camera could cause an accident. The recalibration is charged separately by the windscreen repairer and may as much as double the bill. The margin on the incremental work is higher also (there is no windscreen to buy!). This trend has helped Belron achieve high single digit organic revenue over the last five years, without any material growth in volumes. And in 2022 only 30% of Belron replacement jobs included recalibrations. The penetration of recalibrations alongside windscreen replacements will trend towards 100% over time, so we are still pretty early in the financial impacts for Belron. In the absence of a change in the pricing model, or a stark shift in the competitive dynamics, Belron has many years of highly predictable and high margin growth ahead of it. It's worth noting that the company's relative advantages over independents are accentuated in this area - kitting out a service centre to accommodate recalibrations is not cheap (the machine costs well over EUR 10k), and the catastrophic risk of a failed recalibration increases the appeal of a Belron-certification relative to a normal replacement job.

"Show me the incentives, and I'll show you the outcome" (Charles T. Munger)

D'Ieteren sold 40% of Belron to CD&R, a US PE firm, in 2018 at a EUR 3bn enterprise value (EV) – a paltry price in hindsight. However, this deal appears to have been a significant part of the stark improvement in operating performance. Former employees speak of a more commercial culture after the transaction, which was formalised in the late 2018 "Fit for Growth" cost savings programme. Management was certainly much more incentivised to deliver than it had been before: shortly after the deal an equity incentive plan was put in place whereby about 250 key employees acquired 1.4% of the company for EUR 21m. The plan offered additional "ratchet shares" of up to around 5% of the company if equity return targets were hit - which they certainly were! Based on the valuation of the late 2021 Belron transaction, we estimate this equity plan has created over EUR 1bn of wealth for its 250 managers, who will receive an aggregate dividend of around EUR 70m in 2023.

The improvement was immediate: Belron's operating margin jumped from 6% in 2018 to 15% in 2020, despite demand being suppressed by Covid resulting in no revenue growth over that period. The margin improved again, to 18% in 2021, and management is guiding to 20% in 2023. Belron has moved from a middling 6% post-tax return on assets business to an exceptional 20%+ return on assets business in the space of five years (we don't have sufficient information to calculate return on capital employed).

Belron is now undergoing a more difficult corporate improvement, which involves a substantial IT systems-driven transformation that should extract some further cost efficiency and working capital improvements, although we expect the large majority of the margin improvement has already played out. However, the period of accelerated revenue growth thanks to ADAS recalibration is still in its early stages, and it would be surprising if the business didn't manage to eke out incremental margin improvements from its transformation project and operating leverage. New CEO Carlos Brito of ABInbev fame is not a bad guy to have in charge to help make sure this happens.

What's it worth?

A second PE transaction announced in summer 2021 recognised the attractions of this set-up: CD&R sold almost half of their stake to a couple of buyers, including Hellman & Friedman, at an EV of c. EUR 21bn. Given that we expect Belron's profits to continue to grow at over 10% p.a. for several years, and with relatively modest operating risks, we see 20x our estimate of 2024 unlevered free cash flow as a reasonable valuation. Adjusted for almost EUR 5bn of net debt (after a debt-funded dividend announced last week), this implies D'Ieteren's stake is worth around EUR 8.5bn. D'Ieteren's EV (also adjusted for the Belron dividend) is currently c. EUR 8.2bn. So the current group valuation would be roughly fair if Belron were the only asset.

However, we believe there is another EUR 4bn or so of value in the group's other assets, and that the group is well positioned to compound value into the future. We'll briefly discuss the other assets in the portfolio, and then consider management's approach to capital allocation.

D'Ieteren Auto (fully owned by D'Ieteren) is the exclusive distributor of VW Group brands into Belgium. It accounts for c. 22% of Belgium's new car market. It has broadened its business in recent years, building a used car operation and maintenance and bodyshop services, as well as consolidating its retail footprint and developing some newer mobility business models designed to sustain the business into the longer term such as car sharing, leasing, EV charging, and bike retail. The business has proven to be cyclically resilient, generating profits throughout the financial crisis, the Eurozone crisis and COVID. It has generated annual equity FCF of c. EUR 60-70m on average in recent years, and we believe is likely to deliver closer to EUR 100m p.a. in future as new car volumes recover from depressed COVID levels and the used car business ramps up. We value the equity at around EUR 1bn.

D'Ieteren acquired a 40% stake in TVH Parts ("TVH") in late 2021, buying out one of two family-owners. We understand that whilst an auction process was conducted, the deal was done at a material discount to the highest bid, highlighting that sellers are not always focused only on price, and the value of D'Ieteren's promise of being a long-term, supportive owner which does not seek "hard synergies" between its major business platforms. TVH is a distributor of replacement parts for industrial equipment, particularly forklifts and other material handling equipment, as well as agricultural and construction equipment. It operates globally and is the largest player in the material handling segment. This is an excellent niche, with supportive demand trends (such as warehouse automation), and where stock breadth and availability / delivery speed / service quality are important purchase criteria, not just price. TVH has also established sufficient franchise value that it largely sells non-OEM (original equipment manufacturer) parts from a highly fragmented supplier base, at higher margins than an OEM part would allow. TVH has an excellent financial track record, having delivered 8% p.a. organic growth over twenty years, and with a mid-teens operating margin. The business is not fixed asset intensive but carries significant working capital given the importance of same day delivery for most of its sales. Nonetheless, TVH achieved 17% post-tax return on capital employed in 2021.

D'Ieteren paid EUR 1.2bn in cash for its 40% stake in late 2021 (the business already carried some debt). TVH should deliver sales in 2023 over 30% higher than what it delivered in 2021. We believe this business is worth around EUR 4bn, which reflects a 18-20x multiple of our forecast range for 2023 NOPAT. Net of debt, this would mean D'Ieteren's 40% equity stake is worth c. EUR 1.3bn. We would hope that buying out some or all of the other family's 60% stake is an option at some point.

Parts Handling Europe (PHE) is another niche distribution business. PHE distributes car parts in France, Spain and Italy, mainly to independent garages. Similar to TVH, part availability and delivery speed are key purchase criteria – urban garages are space constrained and need to rotate cars through the lot quickly to achieve decent labour utilisation rates as well as customer service performance. PHE serves a less complex market than TVH (for instance its range of SKUs is smaller) and the automotive OEMs have greater control of the market, whilst the demand trends are weaker. However, delivery speed is even more crucial: over 90% of PHE’s deliveries are within two hours. TVH is the superior business, as reflected in the operating margins: PHE delivers c. 7% overall, albeit materially higher in France, its largest market, vs. mid-teens for TVH.

However, D'Ieteren paid a much lower price for PHE than TVH. D'Ieteren paid an EV multiple of c. 9x 2022 EBIT. PHE's significant debt was transferred across under D'Ieteren's ownership, and after a required (by competition regulators) disposal of a French windscreen replacement operation, the net equity cheque was EUR 440m, against likely after tax profit of c. EUR 80m in 2023. PHE carries substantial debt of a little over EUR 1.2bn, on which the group may well achieve EUR 10-20m of annual interest expense savings when it refinances in a couple of years, particularly after rating upgrades from Moody’s and S&P in autumn 2022 and with the backing of D’Ieteren Group. Within a couple of years this business could be on a transaction PE multiple of c. 3x. We believe the equity is worth more like EUR 1-1.25bn.

Moleskine has become rather a white elephant in the group, both because of its mediocre operating performance and its positioning as a lifestyle / aspirational consumer brand. Frankly it is now rather irrelevant in the context of the group. However, its performance has improved under a new management team in the last couple of years. We value it, probably conservatively, at EUR 350m, which is 12x our expected 2023 NOPAT.

Finally, D'Ieteren has a property arm – mostly focused on redevelopment of existing assets which have become non-core, such as automotive retail sites which are no longer needed. The portfolio generates over EUR 20m of net rental income and is carried on the balance sheet at c. EUR 200m. The market value is realistically closer to EUR 300m, which almost offsets the capitalised value of corporate expenses of EUR 30m p.a..

This leaves a total value of the other assets of c. EUR 4bn or so.

Foggy windscreens or a real problem? Is the market seeing clearly on 2022 results?

2023 is an interesting set-up in our view. The market was not convinced by the 2022 results, particularly the relatively poor cash generation, which was driven by working capital build, mainly in the D'Ieteren Auto business. The stock has underperformed the Stoxx Europe 600 index by 9% since its FY22 results announcement. We see nothing alarming in the working capital build. The largest item is EUR 200m or so of excess inventory at D'Ieteren Auto as in 2022 D'Ieteren was on the other side of VW conducting year-end balance sheet management to please its own investors. These were cars under order, and already delivered to customers within a couple of weeks of the year-end. We think the total of c. EUR 300-400m excess working capital is likely to almost fully reverse over the next 6-12 months, which on top of underlying growth, a full year's contribution from PHE, and the EUR 550m dividend from Belron, could mean D'Ieteren's cash inflow in 2023 is well over EUR 1bn. This in turn means another significant acquisition could be on the cards within the next year or two.

This is obviously a source of risk – we don't want another Moleskine! However, D'Ieteren replaced its CEO in 2019, after the two questionable capital allocation decisions in recent history – the Moleskine acquisition and the underpriced Belron disposal. Under the new CEO, we believe the approach to capital allocation has been professionalised, and the actions so far, albeit from a small sample, are encouraging. Balance sheet management across the group is clearer, and sensible – D'Ieteren is tolerant of non-recourse leverage at its subsidiaries and associates, appropriate for the nature of the operation, but will always maintain a net cash position at the holding company level. Excess cash is swept to the group for deployment. D'Ieteren Auto has been restructured as a subsidiary alongside Belron and others, rather than being within the holding company – which cleans up the structure and makes subsidiary-level financial reporting and management incentivisation clearer. Most importantly, the group has spent EUR 1.6bn on acquisitions of two attractive businesses which in aggregate we would expect to generate over EUR 150m of proportionate net profit in 2023. It has also deployed EUR 150m on share buybacks and lifted the dividend from EUR 1 per share in 2019 to EUR 3 per share in 2022.

Putting it all together, we think D'Ieteren is worth roughly EUR EUR 12.5-13bn, against its current EV of c. EUR 8.2bn. This is also an investment where we have the luxury that time is on our side, in the sense that we expect the main assets, particularly Belron and TVH, to steadily compound in value at attractive rates. If we revisit our valuation assessment in three years' time, for instance, we would anticipate that the fair value of the group has grown to almost EUR 20bn. Holdcos typically trade at a discount of course, but in an optimistic scenario where the group traded at fair value in three years' time, that would imply an annualised return from today's share price approaching 30%. Assuming a 20% conglomerate discount, the annualised return would still be in the low 20%s.

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Monthly percentage return for the GBP A share class of the Global Equity Fund

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2023	0.7	0.7	0.2										**1.6**
2022	-1.7	-3.2	-3.3	3.4	0.4	-5.2	4.6	0.4	-0.4	0.5	4.2	6.2	**5.2**
2021	-2.6	1.4	2.6	3.0	0.7	-0.9	2.2	1.2	1.9	-3.9	1.8	2.3	**10.0**
2020	-4.7	-6.6	-5.4	4.6	-0.9	2.2	-4.4	-10.2	5.3	-0.7	-3.6	2.2	**-21.3**
2019	2.9	1.0	0.3	1.7	-0.2	0.5	1.0	1.8	1.9	0.0	-4.4	0.7	**7.3**
2018	-4.4	5.9	-0.9	3.3	2.9	5.9	1.9	4.0	0.9	0.8	0.5	-3.0	**18.6**
2017	-0.1	-1.4	-1.2	-2.9	1.7	-1.5	1.0	3.2	-2.8	1.3	-1.2	5.5	**1.3**
2016										1.3	-0.8	5.3	**5.8**

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