Q1
March 2023

Investment Objective: To achieve long-term capital appreciation and to exceed the returns of the MSCI All Country World (ex U.S.) Index through the active management of a focussed portfolio of listed equity investments in family-backed holding companies.

The World Economic Forum introduced 2023 as the year of the "polycrisis": *a cluster of related global risks with compounding effects, such that the overall impact exceeds the sum of each part.*

Investors might well empathise with this assessment; however, markets have rallied higher, with the MSCI AC World index returning +7.0% in local currency terms during the first quarter and the Nasdaq up +20.5%.

Within this context FHC returned +1.4% in the first quarter, which compares to a +5.0% return for the benchmark, the MSCI ACWI ex-US (€).

The collapse of Silicon Valley Bank and the ensuing market volatility has generally led to a widening of discounts. Combined with disappointing short-term developments at Schibsted (discussed below), the portfolio weighted average discount widened from 30.0% to 33.6%, acting as a significant headwind to performance. On top of this, the fund suffered -223bps drag from currency, making for a frustrating quarter.

Performance review

FEMSA, the Mexican holding company that owns the leading convenience store chain OXXO, was the standout performer with the shares returning +22%.

In February 2023 FEMSA concluded its strategic review and took considerable steps to unlock the sum-of-the-parts discount at which the company trades. The conclusion of the review will see FEMSA simplify its group structure and re-focus on its core businesses. Most pertinently, the company announced that it intends to exit its stake in Heineken, which prior to the announcement was worth €7.4bn or 28% of FEMSA's market cap (gross of tax). Shortly following the announcement, FEMSA sold €3.2bn of Heineken / Heineken Holding stock in an accelerated book build and issued a €500m bond exchangeable in Heineken Holding shares.

The company will also monetise other non-core assets, the most notable of which is US specialty distributor Envoy Solutions and return excess capital to shareholders, with a new targeted leverage ratio of 2x Net Debt to EBITDA. Our estimates suggest that inclusive of further Heineken sales, the company could well have excess capital of ~$9bn, or 29% of its market cap.

We view these developments highly favourably. The company has taken concrete steps to unlock value and shine light on the value of FEMSA Comercio – an expertly managed and scale-advantaged operator with strong unit economics, improving margins, and a long growth runway. The stub currently trades at 8.4x forward EBITDA vs. closest peer Walmex at 13.4x. Such a discount feels increasingly unjustified given the measures taken, with a cleaner equity story and capital structure conducive to both a narrowing of the discount and the prospect of increased shareholder returns.

Other strong performers include **Christian Dior** (+21% as the world's largest luxury market re-opens) and **EXOR** (+11% on account of strong FY results from Stellantis, Ferrari and CNH).

Turning to the other end of the portfolio, **Schibsted** was the most significant detractor (-94bps). The shares declined -6% over the quarter as initial strength was offset by considerable weakness in March. During the month the company held an investor day in Oslo, which we attended. The day was (almost) entirely focused on Schibsted's unlisted Nordic Marketplace assets and the shift to a vertical operating model. We came away impressed with the strategic vision and growth potential.

However, this was entirely lost as two separate issues drove the shares price -11% on the day. **1)** Management poorly communicated a not-that-surprising and not-that-material guidance cut for Q1 as performance in the New Media division deteriorated; **2)** A lack of clarity on their stake in Adevinta, where comments made by the controlling shareholder on the day of the CMD dampened expectations of a near-term distribution.

Following the setback Schibsted B shares trade at a 45% discount to NAV, with the stub trading at an implied 6.6x EBITDA and an implied discount on the unlisted assets of 70%. The global classified peer group trades at 18.5x NTM EBITDA. This equates to an average EV/EBITDA/Growth multiple of 1.3x, versus the Schibsted stub at 0.5x. Some discount is warranted given the conglomerate group structure and the more cyclical nature of the News Media division; however, the current discount is unduly wide, reflecting structural not fundamental issues.

We believe the status-quo poses risks to long-term value creation and continue to engage privately with all key stakeholders. We will provide further updates when we are in a position to do so. We added to the position over the quarter.

Other notable detractors on the global side include **Aker** (oil price weakness and FX headwind) and **News Corp** (which we discuss below).

Q1 portfolio activity

During the period we initiated a new position in **News Corp** – the Murdoch family-controlled holding company. At period end the company was a 3.3% weight.

Whilst the current structure was established in 2013, the relevant history dates back to 1952, when a 21-year-old Rupert Murdoch returned to Australia from Oxford to take over what was left of his father's newspaper business – which had been much diminished by death duties and taxes. From this he built one of the most dominant media empires of the 20th – and indeed 21st – century, amassing vast wealth and notoriety in the process.

Today we believe News Corp is one of the most misvalued and misunderstood companies in our universe, trading at an 53% discount to our estimated NAV. The NAV is principally comprised of the following assets: a 64% listed stake in REA Group (37% of NAV), the Australian real estate classified marketplace, and unlisted assets Dow Jones, HarperCollins and Move accounting for 38%, 13%, and 8%, respectively.

In particular, Dow Jones is a crown jewel asset that has successfully evolved to become a thriving digital consumer business, whilst both organically and in-organically building a high-quality information services business that warrants a premium multiple reflective of its growing, high margin, sticky, recurring revenues. The value and quality of this business is misunderstood by the sell side and ignored the market.

We estimate Dow Jones alone is worth nearly 3x News Corp's stub value. The stub trades at just 2.7x EBITDA, with EBITDA expected to grow at an +9% CAGR 2023-25e. This compares to the S&P Communications Services sector median multiple of 10.4x, the New York Times at 16.6x and Info Services peers at 22.3x.

Management are highly aware of, and dissatisfied with, the current valuation. Although not consummated, the recent proposed sale of Move (8% NAV) indicates a willingness to make structural changes to unlock value, with multiple potential levers. These include the sale of Move, a monetisation of Foxtel, increased disclosure at Dow Jones – or the holy grail distribution of REA Group, which accounts for 78% of News Corp's market cap.

Whilst timing is uncertain, the attractive underlying nature of the NAV means we can afford to be patient and makes time our friend. Returns from NAV growth and discount narrowing appear attractive.

Over the quarter we also built a new position in **Haw Par** (4.3% weight). Haw Par is a Singaporean holding company that owns listed stakes in United Overseas Bank and United Overseas Land, which combined with net cash equate to 144% of its market cap. As such the market is implicitly ascribing a heavily negative value to Haw Par's unlisted Tiger Balm business, a branded analgesic heat rub used to relieve muscle aches, pains and tensions. Tiger Balm has considerable exposure to travel/airport retail, with a recovery in earnings here a key catalyst for a re-rating of the unlisted stub. If the stub were to re-rate to a zero implied value this equates to share price upside of +44% from here.

These purchases were principally funded by trimming EXOR and Pershing Square Holdings.

Outlook

"*This is the most complex, disparate and cross-cutting set of challenges that I can remember in the 40 years that I have been paying attention to such things*" - Lawrence Summers, Former US Treasury Secretary

The above quote is in fact from late 2022, prior to the collapse of Silicon Valley Bank, when the lagged effects of monetary policy tightening, its (un)intended consequences, and the contradictory nature of price stability and financial stability were laid bare. Undoubtedly the world has become more complex since, with the yield curve now the most inverted since 1981 and indicating a high probability of a US recession.

We don't profess to have a crystal ball and to know exactly what this means for markets. Our experience shows that the key to driving successful long-term returns is to focus on the bottom-up fundamentals – and this is exactly what we are doing.

We have assembled a concentrated yet diverse collection of attractive high quality yet lowly valued companies. Valuations – as indicated by the 34% portfolio weighted average discount – have become cheaper and there are numerous catalysts to narrow discounts and drive NAV growth. The families with whom we have aligned your capital think in generations not quarters and have compounded wealth from generation to generation through numerous market regimes. We expect this to continue.

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IMPORTANT INFORMATION

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