EAST 72

Lining up with the Cable Cowboy: Liberty Broadband (LBRD)[10]

81 year old John Malone is a storied American operator and investor in the broad media and telecommunications arena. Malone is, of course, the player who frightened the bejesus out of Rupert Murdoch by acquiring 19% of News Corp voting stock in 2004-2006, before agreeing an asset swap in December 2006 to allow Rupert to sleep at night.

The early part of Malone's career is laid out in the 2002 book "Cable Cowboy"[11] which documents the growth of TCI (Telecommunications Inc) from its origination in 1958 controlled by its original founder, Bob Magness. Malone joined up as 32 year old CEO in late 1972 in a period where most of the nascent cable businesses had saddled themselves with outlandish amounts of debt; TCI's debt at the time was equivalent to 17x revenues.

The story of the growth of TCI, where the stock multiplied over 900 fold between 1972 and 1998 prior to its sale to AT&T in 1999, is documented in William Thorndike's "The Outsiders" (Chapter 4)[12] together with a focus on three of Malone's "recipes" to accelerate shareholder returns, usually to his own (as well as shareholder) benefit, namely:

- Liberal use of debt in an appropriate manner against long term cash flows, at low interest rates and with lengthy maturity;
- Use of tri-partite capital structures with A, B and C class shares having respectively 1, 10 and nil votes per share – Malone invariably retains control through ownership of the B shares, as is the case with LBRD;
- Use of spin-outs and "tracker stocks"[13] to make transparent the valuation of individual components of the company. This is best seen in "Liberty Media" where the entirety of the company's assets are attributed to three tracker stocks: Formula 1 (FWON), Atlanta Braves (BATR) and Liberty Sirius XM (LSXM). You can't buy stock in "Liberty Media".

Malone has historically been a marvellous seller of assets to – and buyer of them at distressed prices from – large media/telco conglomerates. This reached an early culmination with the sale of TCI to AT&T in June 1998 for $55billion, settled in March 1999.

Malone had established Liberty[14] in 1991 as a means of separating the more speculative assets (cable programming regional sports) plus a small amount of TCI subscribers from TCI through a complex exchange offer where shareholders in TCI were able to exchange shares in that company in exchange for rights to subscribe to Liberty. Less than one third of the shares were taken up, which gave Malone – on borrowed money – 20% of the "B" class Liberty supervoting stock (of which more below), and 40% voting control. Once the AT&T transaction had settled, Liberty gained additional cash, but left Malone free to explore options in the telco/cable/TV markets.

[10] All values in US$
[11] "Cable Cowboy" Mark Robichaux (John Wiley & Sons) 2002
[12] "The Outsiders" William Thorndyke Jr. (Harvard Business School Publishing) 2012
[13] Tracker stocks are specialty equity securities designed to "track" the performance of an individual business within a larger company and have similar reporting characteristics to any listed corporation. However, the parent company legally retains ownership of the underlying assets/business constituting the tracker stock. Tracker stocks eliminate the need for a total spin-off of the business, but tracker securities can be spun off from the parent entity as has been the case with many components of the "Liberty" group
[14] http://csinvesting.org/wp-content/uploads/2012/09/rights-offering-and-over-subscriptions_final.pdf

Liberty Broadband is one of seven structures, encompassing nine securities including tracker stocks within the "Liberty" empire:

- Liberty Media, noted above which consists of the three tracker stocks FWON, BATR and LSXM;
- Liberty Global plc (LBTY), providing broadband and mobile in Europe;
- Liberty Latin America (LILA), a replica of LBTY across selected countries in South and Central America;
- Qurate Retail (QRTE) a home-shopping entity encompassing HSN and QVC amongst other assets;
- Liberty Trip Advisor (LTRP) which holds a 21% economic stake, but 57% voting position in TripAdvisor (TRIP);
- LMF Acquisition Opportunities (LMAC), a special purpose acquisition corporation (SPAC); and
- Liberty Broadband.

At 31 March 2022, LBRD equity is comprised of the three classes noted above; 22.56m single vote "A" class, 2.54m 10-vote "B" class and 139.9m non-voting "C"; John Malone controls LBRD via his ownership of 92% (2.148m) super voting "B" shares, despite holding only a 2.1% economic interest.

LBRD has two assets:

- GCI Holdings – a specialist communication and entertainment provider to Alaska, acquired in December 2020 for an effective equity value (via stock swap and cancellation of LBRD shares owned by GCI) of $3.06billion; attaching debt of $2.2billion and other liabilities were offset by an investment in Charter (below); and

- 26% interest in Charter Communications (CHTR, Charter) an $81billion equity capitalised (enterprise value ~$174billion) cable network with over 30million residential customers and 2.16million small and medium business relationships[15]; at the share price on 30 June 2022, the CHTR stake is priced at $24.15billion.

Hence, it is clear that the value within LBRD is virtually exclusively driven by Charter, its share price and an intriguing buy-back mechanism (below) which even more inexorably links the two companies.

Charter, which operates as "Spectrum" in 41 US states dates back to 1980, but the formative transactions took place from 1998 onwards, with Paul Allen, the co-founder of Microsoft, as Chair. The company expanded rapidly by debt funded acquisition and concluded 2008 with $21.8billion of debt, against just over $6.5billion in revenues! CHTR filed for Chapter 11 bankruptcy protection in February 2009 but re-emerged with $8billion less debt in November the same year.

[15] As at 31 March 2022

The seminal transactions for the company occurred in March and May 2015 when the company announced the acquisition of Brighthouse Networks and Time Warner Cable respectively, aided by a $5billion equity injection from Liberty Broadband.

The cable business is ostensibly about preventing "churn" – customers coming but staying for short periods of time, thereby rendering their lifetime value to the company lower than the cost of attracting them. The TV side of the business is not especially profitable; neither yet is the wireless business. However, the core cable business, supplying broadband continues to grow – in line with consumption of streaming services – and is a high margin (sunk cost) business. The threat to broadband comes from new technologies such as 5G wireless and fibre to the home which provides potential for "overbuild" of existing cable networks.

Charter has a significant cost competitive advantage which it is able to utilise to price its services under the mainstream competition and provides significant protection. This, together with the sunk capital cost aspect, provides credence to CHTR as an inflation hedge.

CHTR has an equity market value of $81.2billion (173.6million shares at $468); the shares have fallen from highs of $825 in September 2021. CHTR spend round $7 to $7.5billion on capex per annum, against an operating cash flow (post tax and interest) in 2021 of $16.2billion. This provides the shares with a free cash flow yield on equity of 10.6% if maintained; pre-tax and interest, the equivalent FCF yield on enterprise value ($174bn) is around 7%.

Given the likelihood that long bond rates in USA may even have peaked in the short term at 3.5%, these yields, even for a slow growing cable company are very attractive. However, looking out 2-3 years they are accentuated by strong equity buy-back program, which has averaged over $3.5billion a quarter in the past two years which at prevailing prices would theoretically retire close to 30million shares per annum (17% of issued capital).

One aspect that prevents such an aggressive share repurchase, but accentuates our view of holding LBRD as a play on CHTR is the unique arrangement between the two companies. As part of LBRD and Charter's shareholder agreement, LBRD cannot hold greater than a 26% interest in Charter and so sells CHTR shares to Charter as part of that company's buyback program. This is done on a monthly basis, based on CHTR's buybacks in the prior month. In turn, this enables LBRD to repurchase its own shares (if appropriate) from the cash proceeds of the CHTR sales. So LBRD effectively represents a slightly geared (and discounted) entry to CHTR's autosarcophagy whilst also engaging in the same self-cannibalistic practice.

LBRD gains significant cash flow to retire its own shares by the forced resale of CHTR securities to maintain the shareholding at 26% in light of CHTR's aggressive buybacks; in essence two connected spinning cogs.

LBRD has retired a stunning 16.3% (31.6million) of its own "A" and "C" class shares in the fifteen months since end calendar 2020, at an average price of $162/share against the prevailing level at end June 2022 of $115.64. This suggests future buybacks will be as aggressive as responsibly possible.

From an asset value standpoint, we estimate LBRD at $115.64 to trade at an 18% discount to the value of its two assets, after the recent US$170m sale of the Skyhooks business, as follows:

	US$million	
51.554m CHTR shares @$468	24,155	
GCI Holdings (assessed value)	2,400	(cost $3billion so 20% discount)
Est. net debt inc preference equity	(3,228)	
EQUITY VALUE	23,296	164.9m total "A, "B" & "C" class
NAV/share	$141	(18% discount at $115.64)

Amerco: Opacity creates significant opportunity[16]

Amerco (UHAL) is the fourth largest self-storage unit owner in the US, with ownership of just over 50million square feet (4.65million m^2) of these properties, along with management of a further 23million square feet. That's a pretty robust starting asset, but when you combine it with a fleet of 186,000 trucks, 128,000 trailers and 46,000 towing devices under the "U Haul" banner, you have an astonishing integrated, moated moving and storage business across the USA.

U-Haul has a storied history[17] having been established as a "one-way" rental company in 1945, and now having 23,000 locations across North America – 2,100 company owned and 21,100 independent franchise dealers. The company has a near monopoly in DIY inter-city moves having 10times the number of locations as its nearest competitor Penske. Whilst Penske employ a fleet 52% the size of U-Haul, a likely significant (yet undisclosed) portion of the Penske fleet is made of commercial rental vehicles (refrigerated units, semi-trailers etc). Next largest is Budget (Avis) who have a truck rental fleet a little under 6% of that of U-Haul.

Amerco is controlled by the Shoen family – Chairman Joe and family control 42.7% of the small float of only 19.6million shares; at $478 a share, the equity pricing of the company is just under $9.4billion. With an adjusted $3.4billion in net debt, enterprise value is a very low $12.7billion.

We can compare UHAL's in-situ storage portfolio, which it has grown from around 15million ft^2 in nine years with five publicly listed large-scale peer REIT's. We acknowledge this is a theoretical exercise in splitting the "real assets" (storage) from "the business" (trucks) since the Shoen's are highly unlikely to ever securitise the properties because of the massive competitive advantage brought about by the combination. But it's an exercise worth doing to get to the bottom of the magnitude of undervaluation UHAL stock.

By comparison with UHAL, REIT's have an obvious tax advantage, but also benefit in investors' eyes from transparency – if we ignore the fact that some have equity in highly geared unconsolidated JV's or have management income streams, or significant minority ownerships in sub-trusts. These minority interests are especially difficult to cater for. We have made an attempt to deal with these inconveniences for the peers but must concede that our maths has more than the usual caveats.

[16] All figures in US$million
[17] The "storied" includes bankruptcy protection and sons forcing out their father from the board of Directors!

As a guide, the "average" facility in America has around 72,000 – 77,000 ft^2 of available space at ~110ft^2 per unit renting out at ~$18.75 per ft^2pa. Valuations vary widely for obvious reasons. The table below shows the four largest public storage REITs by area, the smallest of which is a smaller size than Amerco, are valued by the equity market at an equivalent EV/ft^2 of $273, which would value UHAL's owned portfolio at $13.6billion, against a current **company** EV of $12.7billion. The comparison becomes even more ludicrous when including managed properties.

Even the second-lowest[18] rated of the five REIT peers (LSI: $153.64 psf) suggests the owned Amerco portfolio to be worth $7.7billion on a standalone basis, leaving $4.9billion of attributable value for the UHAL and insurance businesses.

Millions/$mn	**Cube Smart**	**Extra Space**	**Life Storage**	**National Storage**	**Public Storage**	**Aggregate**
Ticker	**CUBE**	**EXR**	**LSI**	**NSA**	**PSA**	
Issued shares	224.4	134.3	84.3	91.5	175.2	
Price (30 Jun 22)	$42.72	$170.12	$111.66	$50.07	$312.67	
Equity Capn.	9,586	22,839	9,414	4,577	54,770	101,186
Net debt/prefs	3,348	5,198	3,092	3,193	11,791	26,622
Assessed other assets	(117)	(500)†	(215)	(184)	(2,569)††	(3,585)
Enterprise value	12,817	27,537	12,291	7,586	63,992	124,223
Owned ft^2 (million)	43.6	76	80	56	199	455
EV/ft^2	**$293.97**	**$360.55**	**$153.64**	**$136.19**	**$321.56**	**$273**
Managed ft^2 (million)	6.5	88				95
Owned & managed ft^2	50.1	164	80	56	199	550
Adj. EV O&M	12,817	28,037				124,723
Adj EV/O&M ft^2	$255.82	$170.00				**$227**

† management company valuation
†† includes publicly listed stocks PBS and SHUR.BR

Amerco owns two insurance businesses – a property casualty insurer (Repwest) which mainly does claims management for the U-Haul portfolio of vehicles and a life company, Oxford and its various subsidiaries. Both businesses are profitable and have combined equity bases of $736million – not inconsequential. Over the past two years, the two companies combined have recorded average per annum pre-tax profits of $62million.

Based on Deloitte analysis[19], the typical global life company has transacted in a willing buyer-seller deal at 1.15x BV in the past year; the equivalent in the P/C business has been a slightly higher 1.2x. As a consequence, this suggests the Amerco businesses might be worth a combined $860million, equivalent to 13.9x average pre-tax earnings in 2021 and 2022.

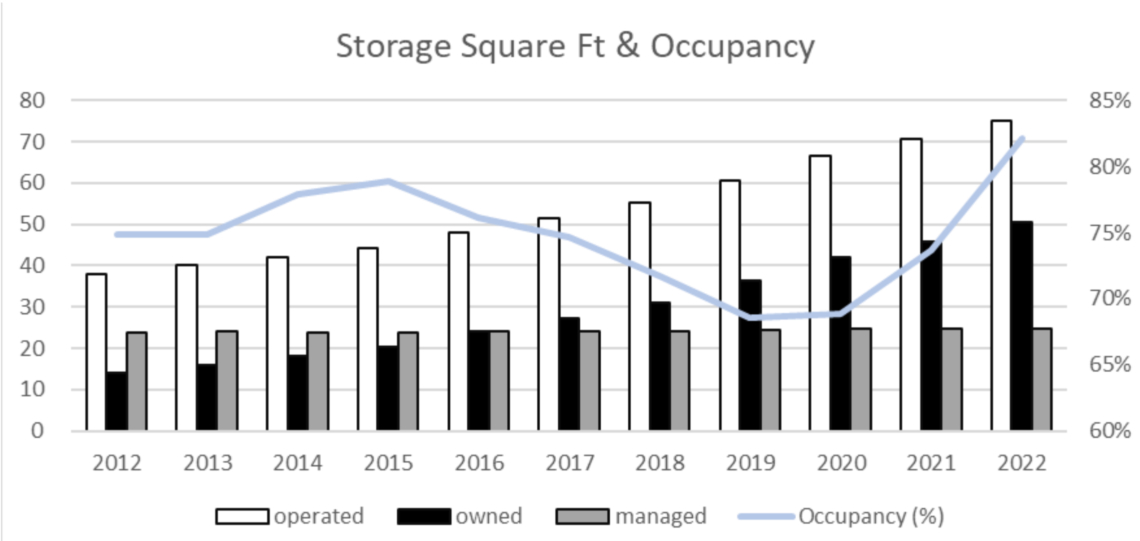
The key piece of opacity within Amerco which mitigates against transparent analysis is the binding together in the segmental accounts of "moving and storage"; in other words the self - storage rental returns – which we are valuing above on an asset basis - are not broken out from the truck and trailer rentals.

18 NSA (the lowest) have various "affiliates", significant minority interests and external management of their properties making equivalences difficult to compute.

19 Deloitte 2021 Insurance M&A outlook (Deloitte)

Hence, the analysis which follows is our own work and not cross-checked with the company to establish what we believe the pure vehicle, trailer rental and parts sales might be valued at by the equity market. With that warning, the good news is that there is respectable consistency across the five large listed REIT peers in respect of costs and revenues per square foot. The good news is that Amerco does disclose REVENUES from self-storage - which have compounded at just under 17% per annum over the past nine years, as the portfolio has continued to grow and occupancy has improved.

As an estimate, based on the cost structure of the peers, but where we expect Amerco to operate at a more parsimonious level; we believe operating cost of about $5 psf pa to be a reasonable and possibly conservative estimate.



Self storage revenues only ($million)

2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
153	182	211	248	287	324	367	419	477	617

On that basis, across the owned portfolio, this would imply operating profit of ~$380million in the year to 31 March 2022 from self-storage ownership on revenues of $617million. Hence, our portfolio estimate valuation of $7.7billion represents an earnings yield of ~4.95%, on an asset which management in its latest earnings call notes is "continuing to fill at historically high rates". It explains why Amerco is not retiring equity despite the apparent discount to value (below). They see further opportunities in the ownership component of the business given demographic change in the US, and shortage of available sites – for others – as well as zoning difficulties in urban environments.

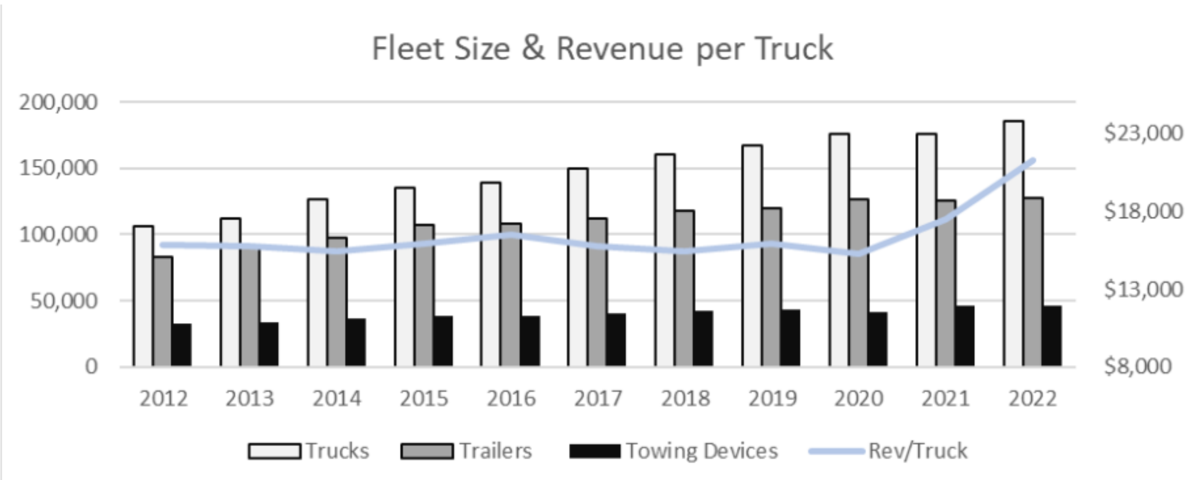
With the self-storage "property" revenues backed out of the segmentals for "moving and storage", we can hazard an estimate of the profitability of "moving", encompassing vehicle and trailer rentals.

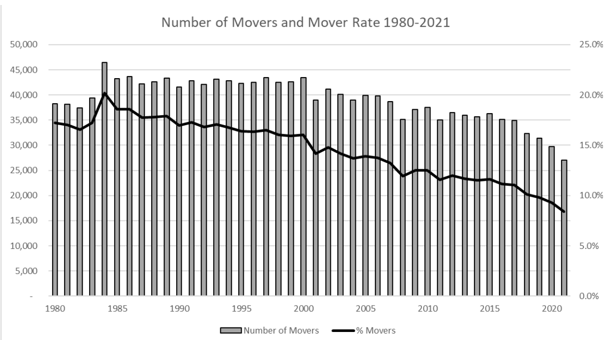
Based on the UHAL segmental profit analysis[20] (reproduced below), this would suggest the remaining "moving and storage" operations to have burgeoned in the past two years with an operating profit of $1.68billion EBITDA in 2022, up from an estimated $1.25billion in 2021 – excluding profits on vehicle sales. Why so strong?

	Year Ended March 31, 2022	Year Ended March 31, 2021
	(In thousands)	
Moving and storage		
Revenues	$ 5,398,267	$ 4,231,674
Earnings from operations before equity in earnings of subsidiaries	1,577,226	906,863
Property and casualty insurance		
Revenues	115,043	86,737
Earnings from operations	49,780	32,498
Life insurance		
Revenues	238,812	232,634
Earnings from operations	19,538	22,876
Eliminations		
Revenues	(12,375)	(9,060)
Earnings from operations before equity in earnings of subsidiaries	(1,547)	(1,090)
Consolidated Results		
Revenues	5,739,747	4,541,985
Earnings from operations	1,644,997	961,147

UHAL have been slowly expanding the truck fleet, adding 10,000 trucks between March 2020 and 2022; however, the key driver has been the average revenue per truck per annum, which has bounced from $15,700 in the 2020 year via $17,520 in 2021 to a hefty $21,872 in the latest year. **That's inflation for you**! 18% compound growth in **revenue per truck** for the two years

We are unsure how sustainable this growth over the past two years will prove to be, but managements insights from the latest earnings call is encouraging with their assessment that: "*About half of the increase was coming from transactions and the other half was split between the number of miles driven by our customers and the rate that we were charging per mile.*"





What is surprising, is that these results have emerged during a period when Americans have been (proportionally) their least mobile since data was tracked, in 1948, with, according to US Census Bureau statistics, only 9.8% of the population relocating!

[20] Page 21, Amerco 10K for year to March 2022

In conclusion, we see Amerco as being able to post significant growth over the next 3-5 years. This will come at the expense of capital management – despite the gap between equity price and value (below) – with management undertaking ongoing expansion plans. Given the massive competitive advantage, this seems reasonable but does mean a lack of free cash flow to fund equity retirement. It also means that advancement in the share price will require the management growth "thesis" to play out; given their stockholding, they have plenty of incentive.

An idea of the gap between listed equity price and underlying value comes from our sum of the parts analysis. This suggests UHAL to be worth between $710 and $1016 per share in its present state, an uplift of 48 – 113% against prevailing 30 June 2022 levels:

$million	**Low case**	**High case**
Self storage property (low LSI; high = average peers)	$154/sq ft	$273/sq.foot
Implied self storage value	$7,682	$13,650
Insurers per noatation above	$860	$860
UHAL moving at 6x EBITDA (av 2021& 2022)	$8,790	$8,790
Debt	(3,380)	(3,380)
EQUITY VALUE	**13,952**	**19,920**
Per share (19.6million)	$711	$1016

Reverse engineering, at the prevailing price of $478/share, and backing out the self-storage property at low values together with insurance, we believe we are paying around $4.2billion for U-Haul, equivalent to less than 3x average EBITDA in the past two years, and very roughly 1x revenues in the year to 31 March 2022.

We believe investing in UHAL represents ownership of an entity with near monopoly attributes in one-way DIY moving; moreover, we view this monopoly as difficult to erode in a product which has little scope for future disruption. Against other comparatives with significant moats to their business, pricing power and a dominant position, we believe the calculated valuation metrics to be extremely low.

For further information:

Andrew Brown
Executive Chair
0418 215 255

Disclaimer

While East 72 Holdings Limited (**E72**) believes the information contained in this communication is based on reliable information, no warranty is given as to its accuracy and persons relying on this information do so at their own risk. E72 and its related companies, their officers, employees, representatives and agents expressly advise that they shall not be liable in any way whatsoever for loss or damage, whether direct, indirect, consequential or otherwise arising out of or in connection with the contents of an/or any omissions from this report except where a liability is made non-excludable by legislation.

Any projections contained in this communication are estimates only. Such projections are subject to market influences and contingent upon matters outside the control of E72 and therefore may not be realised in the future.

This update is for general information purposes; it does not purport to provide recommendations or advice or opinions in relation to specific investments or securities. It has been prepared without taking account of any person's objectives, financial situation or needs and because of that, any person should take relevant advice before acting on the commentary. The update is being supplied for information purposes only and not for any other purpose. The update and information contained in it do not constitute a prospectus and do not form part of any offer of, or invitation to apply for securities in any jurisdiction.

The information contained in this update is current as at 30 June 2022 or such other dates which are stipulated herein. All statements are based on E72's best information as at 30 June 2022. This presentation may include forward-looking statements regarding future events. All forward-looking statements are based on the beliefs of E72 management, and reflect their current views with respect to future events. These views are subject to various risks, uncertainties and assumptions which may or may not eventuate. E72 makes no representation nor gives any assurance that these statements will prove to be accurate as future circumstances or events may differ from those which have been anticipated by the Company.