Ennismore Global Equity Fund

Investor Newsletter for the month of September 2018

Issued on 5 October 2018

Fund Details

Daily dealing UCITS and Irish Central Bank regulated open-ended investment company with Financial Conduct Authority recognition and registration in Ireland. The Fund size was USD 277m as at 28th September. Total assets under management by Ennismore Fund Management were USD 897m. We plan to reopen the Fund and take in a limited amount of new capital over the next few months. Further details are given later in this letter.

The Fund is managed as an absolute return fund with the objective of generating positive returns irrespective of market conditions rather than performing relative to any benchmark index.

Top Five Long Holdings as at 28 September 2018

	Company	Country	Sector	% of NAV
1	SES SA	Luxembourg	Consumer Discretionary	8.7
2	METRO AG	Germany	Consumer Staples	7.3
3	TPG Telecom Ltd	Australia	Telecommunication Services	5.1
4	Inmarsat Plc	United Kingdom	Telecommunication Services	5.1
5	Schibsted ASA	Norway	Consumer Discretionary	5.0
				31.2

Exposures as at 28 September 2018

Longs %	Shorts %	Gross Exposure %	Net Exposure %
92.6 (94.5)	43.9 (48.0)	136.5 (142.5)	48.7 (46.5)

Figures in brackets refer to previous month end. All exposures are calculated on a delta adjusted basis.

Exposures by Country, Market Cap & Sector as % NAV and Positions as at 28 September 2018

Country	Gross%	Net%
United States	33.4	-2.6
United Kingdom	28.0	12.5
Germany	24.3	12.8
Luxembourg	9.2	9.2
Australia	6.3	5.6
Norway	5.0	5.0
Ireland	4.7	4.7
Netherlands	4.6	4.5
France	3.5	2.8
South Africa	3.3	1.8
Cayman Islands	2.5	-1.8
Other	11.7	-5.8

Market Cap	Gross%	Net%
>$10bn	40.7	17.2
$5bn-$10bn	47.9	39.9
$1bn-$5bn	35.1	-0.7
<$1bn	12.8	-7.7

Positions	Sep	Aug
Long	45	46
Opened	2	2
Closed	3	1
Short	76	77
Opened	2	6
Closed	3	3

Sector	Gross%	Net%
Consumer Discretionary	34.2	20.7
Consumer Staples	12.8	10.1
Energy	0.5	-0.5
Financials	4.0	0.5
Health Care	8.3	-0.2
Industrials	21.9	12.2
Information Technology	38.2	1.9
Materials	2.8	-2.8
Real Estate	1.4	-1.3
Telecommunication	12.1	8.4
Utilities	0.3	-0.3
Other	0.0	0.0

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

Performance as at 28 September 2018

	Share Class				
	GBP	GBP A	EUR	CHF	EUR I
NAV per share[1]	**12.95**	**12.93**	**12.75**	**13.15**	**10.71**
Period	% Change				
September 18	**0.9**	**0.9**	**1.4**	**2.1**	**0.9**
August 18	4.0	4.0	3.7	1.2	**3.8**
July 18	1.8	1.9	1.1	1.1	**2.2**
2018 to date	**20.6**	**20.6**	**20.7**	**17.2**	**7.1**
12 month rolling	**27.3**	**27.4**	**27.0**	**24.5**	**-**
Annualised return[2]	**13.9**	**13.8**	**13.0**	**14.7**	**-**
Since launch[2]	**29.5**	**29.3**	**27.5**	**31.5**	**7.1**

[1]Source: Administrator, Net Asset Value. [2]Since inception of GBP, GBP A, EUR and CHF share classes on 03/10/16, EUR I share class on 03/07/18. Note: All performance figures net of fees. **Past performance is not a guide to future returns.**

Attribution %		GBP	EUR	CHF
Long	Q3 18	8.1	7.4	6.1
	Q2 18	20.4	19.4	17.9
	Q1 18	0.6	1.8	2.3
	Q4 17	6.6	5.8	7.8
Short	Q3 18	1.3	1.3	1.3
	Q2 18	-3.9	-3.9	-3.9
	Q1 18	1.2	1.2	1.2
	Q4 17	0.9	0.9	0.8

Attribution figures exclude cash returns and are prior to expenses

The Fund's NAV per share increased between 4.4% and 7.1% in Q3, depending on currency.

Long positions added 8.1% to NAV (in the GBP share class). The largest contribution (3.3%) came from TPG Telecom Limited. In August the company announced a planned merger with Vodafone Hutchison Australia ("VHA"), the third largest mobile operator in the country. The terms of the deal as a merger of equals were favourable for TPG, with VHA's parent companies keeping AUD 4.8bn of its debt, which we think reflects the strength of its planned mobile offering (discussed in our March 2018 letter).

Grocery wholesaler METRO AG contributed 1.7% in the quarter. Czech investor Daniel Křetínský and his partner Patrik Tkáč acquired a 10.9% stake in the company, and call options over another 20.6%. They have stated that they expect to exercise these options, which would require them to then make a full bid for the company. We don't know what they see in METRO, but to us the attractions are obvious. We believe the property portfolio alone, which has never been revalued, is worth substantially more than the current market cap.

SES SA contributed 1.6%. We explained this position in our last quarterly letter. The process for C-band monetisation continues. It's not a certainty, but it looks more and more likely. If it does go ahead the upside is potentially huge. Italy's auction of 3.7 GHz spectrum cleared this week at an average price of over USD 0.40 per MHz / pop. This is above what we were assuming for the US, where spectrum has historically sold at a significant premium to the rest of the world.

We sold our position in TripAdvisor Inc. after its Q2 results. We are less confident today that its position in the hotel shopping value chain is unassailable. Its key asset, the network effect around its reviews, is not as unique as it was. Its largest (and very large) customer, Booking Holdings Inc., seems to be doing a good job of replicating it.

The short book contributed 1.3% in the quarter.

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Two year review; reopening the Fund

A year ago, we said we are not in this business to produce single digit returns. That is still true. It is also still true that we focus on the inputs – our investment process and stock selection – which have delivered for us in the past. We are happy with the Fund's portfolio today and believe our approach will yield a very good return for our investors over time.

When we launched the Fund we said we wanted to show that Ennismore's well-worn investment approach could be successfully applied to the new strategy, which invests in more liquid stocks and more outside of Europe, before we took in new capital. Two years is not long term, but in the context of Ennismore's track record we don't think it is insignificant either. We also said we would manage the Fund to be highly liquid so that any redemptions could be met within 10 days (the settlement period for the daily-dealing fund). Today the average liquidity of the portfolio is around 2 days, so we will be able to manage your money in the same way even with a larger pool of capital.

We have never spent much time marketing. It comes with an opportunity cost - time we could have spent doing research. We have decided to do one further capital raise now, capping the amount we take in to stay comfortably within our liquidity constraints for the Fund, and then to hard close again for the foreseeable future. Limiting the raise in this way will mean that the additional capital can easily be invested in the current portfolio. As promised when the Fund launched, existing investors will be given priority. Please contact Eleanor Scott on +44 (0) 20 7368 4219 or email subs@ennismorefunds.com if you would like more information or to make an investment in the Fund. Redemptions can be made through the Administrator in the usual way.

Exactly how many monkeys do you need?

At two years old the Fund is still toddling but we hope it will follow in the footsteps of Ennismore's more established funds. These have delivered a double digit annualised return, after all fees, over a period of nearly 20 years. This is significantly better than the market, whatever comparable index you choose, despite the fact that net exposure has averaged less than 50%. Simplistically, Ennismore has delivered a much better return for half the risk. Of course, what matters today, for you and for us, is what future returns will be. To get some insight into that it would help if we knew what explains Ennismore's past outperformance, so we can see how likely it is to continue going forward.

Let's start with the big known unknown. Dumb luck. After all, with enough monkeys typing you can supposedly reproduce the works of Shakespeare (you'd need a lot more monkeys than there are atoms in the universe though). How probable is it that out of thousands of funds one delivers returns like ours by chance? In any given year it's not unusual at all. We estimate that, on average, about one in five funds investing in a similar universe will do better than our annualised return over 12 months, just by chance. Over 20 years, though, the odds are so low you wouldn't expect even one in ten thousand to. Perhaps more intuitive is the fact that our long book has outperformed relative to the market in 17 out of the 20 years we have been in business, and the short book 16 of 20. That doesn't mean there is no luck in our returns (of course there is). It doesn't even tell us if luck contributed positively or negatively. It does mean it's reasonable to ask what else could explain Ennismore's performance.

That's the Ennismore way

We are pretty sure the answer is not individual genius. For starters, we have met us. We'd say we are smart and work hard but a lot of people fit that bill. In fact, quite a few have at Ennismore over the years. None of the original team are managing money today. 20 years from now we think the individuals will be different again. We strongly believe investment decisions are best made by individuals but there is no "Special One" here (or, it seems, at Man United either). No one with their name up in lights, or on a fund. Ennismore is more than that.

Some features of our business model are probably significant because they attract people who are suited to long term investing, where a lot of time usually passes between effort – doing research that highlights a probable mispricing – and reward. We don't hire in senior fund managers and the path to becoming one is long. It is also clear, with equity ownership and remuneration that is transparent and tightly correlated with long term return on capital. It's our version of the Stanford marshmallow experiment – people who can't wait don't work here.

We don't have a sales driven organisation. No career analysts pushing ideas to fund managers inside the firm. No one selling our products outside of it. No investor relations, no marketing people. Most important, though, is what we do do. We manage as much money as we think is consistent with maintaining our returns, not maximising our bottom line. And we do our own research. It's not outsourced externally to the sell side, which has all the wrong incentives to do it

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thoroughly and independently. It's not outsourced internally either. The fund manager does the work and then backs themself. Glamorous it ain't - our office is more like a library than a trading room - but we think it is a great environment for making well thought-through decisions.

Other features of our business model are probably significant because they give investors who work here a sustainable edge (although we recognise these are impossible to quantify). In an earlier letter (October 2016) we talked about our time horizon as one. The key point is not that we are able to time our investments, we almost never are. What we are able to do is hold for the long term. It is well documented that equities have historically outperformed less risky investments over most periods of more than a decade, but trading volumes show that the average shareholder today is extremely short-lived. We can think like the owners of a business we invest in because we are the owners of our business. We have always tried to make sure that clients understand and share our investment philosophy (one kindly pointed out to one of us recently that nothing had changed since the last time we met, ten years earlier, other than our hairline). We may even be getting better with age. After all, a long successful track record puts short term fluctuations into meaningful context.

Less tangible, but important, is the way our set up protects the individual from excessive pressure. We have discussed the benefits of a long / short portfolio before (again in October 2016), including the fact that it reduces our exposure to wild swings in market value (in either direction - hubris may be as hazardous for your wealth as panic). But we think a bigger advantage is our multi-manager model. Each of our funds is run by several individuals. Each has sole discretion over their own book and is remunerated based on the performance of this, not the overall fund. As clients you will never know how any individual within our team is performing (that's one reason we don't disclose how assets are split between us). What we can guarantee is that everyone will have a bad year from time to time. When they do there is strong support within the firm. It takes years to be given a large capital allocation at Ennismore; it would take years of underperformance to lose it (provided, of course, there is no departure from our fundamental belief in margin of safety investment). The same individual managing a fund on their own will face much more pressure to deliver short term performance, which we think is probably an oxymoron. That allows us to be better at being greedy when others are fearful, and fearful when others are greedy.

Knowledge is power

The most clear-cut advantage we ever get, though, is information. We spend most of our time doing our own research and sometimes we are able to piece together information about a company that most counterparties in the market are unaware of. Our due diligence on Sirius Minerals PLC customers in China later in this letter is a good example. It's easy to justify allocating a lot of resources to a position in the Fund, but we make relatively few investments each year and most of the research we do is inconclusive. On average we probably have to invest a similar amount of effort into a dozen or more ideas to find one that really convinces us it is worth risking capital on.

By way of example, over the last couple of years we looked into one company that was delivering hyper-growth. We were intrigued because most of this was reportedly coming from a related party acquisition. When we examined historic filings and press coverage for this entity there seemed to be material discrepancies with what its now parent company was disclosing. A look at the building it was operating out of also suggested it was smaller than claimed (with, for example, tens rather than hundreds of employees). Our thesis was that sales could be overstated and we went to work checking if this could be disproved. Step one was to find a way to track sales volumes. We were able to do this by periodically purchasing from the company. The numbers seemed to stack up but that wasn't definitive evidence. Step two, we commissioned a market research survey to see if the brand penetration of its target customer base matched reported sales. The result was inconclusive. At this point our thesis was looking shaky, but not broken. Several months later we were able to visit the company's main distribution centre. What we saw brought our doubts back to the surface – the level of traffic and floor space for the acquired business seemed way too small. We recommissioned the market research study, with a year having passed since the original one. This time the result seemed clear. It implied sales were a tiny fraction of what the company reported and that they were declining (whereas for other comparable brands the numbers seemed reasonable). We literally didn't believe it so we had the survey re-run. Same result. By this point we were getting a little bit excited - you could make a strong argument for short selling this company's shares based on the survey data we had. But we are not interested in winning arguments. We want to be right. We needed to explain this data, or work out why it was wrong. We commissioned yet another survey focussing on the youngest demographic possible, to see if the company's high exposure to this segment was skewing the result. The answer was maybe. Finally, we signed up to use data from a market research firm that specialises in this industry. The service is too broad to use on the off chance it contains something interesting, but at this point we had a clear anomaly that it could either confirm or disprove. What it told us about our own data would be critical. After dozens of hours of research, two trips, several calls to other people in the industry and repeated surveys, the result was in. We were wrong. We were not unhappy about that, we just moved on to the next idea.

For some specific positions, then, we are confident our edge comes from information we have found. It's hard to aggregate this up to the portfolio as a whole, as other factors will also drive share prices, but we are pretty sure it is material over time. Ennismore has advantages from longevity here too. There is a lot of valuable information in 20 years of notes, for example - the best bits are usually one company talking about another.

We believe we do more stock specific research than most other investors, but everything we do can be replicated. If it is such an edge, why isn't it competed away? The answer may be pretty simple. An increasingly large part of our industry – tracker funds - does not even try to gain an advantage this way. We actually think this makes more sense than what most institutions do, charging a low management fee that reduces returns but may not add enough resource to their research effort to compensate. Larger funds will, of course, have more income, but size forces them to invest in the most liquid large cap stocks where you are much less likely get an advantage from information anyway. That is why we have always capped assets under management.

Sirius Minerals PLC

On 20th July Sirius Minerals PLC ("Sirius") announced that its offtake agreement with Dian Huang Peony had been terminated. The press release gave no reason for this but if you have read our previous comments on Sirius (in October 2016 and June 2018) you might not be that surprised. When we met Dian Huang Peony in 2016 its CEO told us the company had no firm commitment to buy from Sirius and the business consisted of little more than a few field trials.

The market took the news the agreement had ended well because two new Chinese offtake customers were announced at the same time. This is the third time in as many years that Sirius's customers in China have changed, with Dian Huang itself a replacement for Yunnan TCT Yong-Zhe (a change that again went unexplained). Pinning down Sirius's future prospects there is a bit like a game of Whac-A-Mole. Undeterred, we have tried again to assess the quality of its counterparties.

Acme Corporation ("Quality is our #1 dream")

The July announcement specified offtake agreements with two new customers, Yantai Service Agricultural Science and Technology Co Ltd ("YSA") and Guangzhou Eiliseng Biotech Co Ltd ("Eiliseng"), each potentially worth well over USD 100m a year in sales at peak volumes. The press release went on to state that YSA is a strategic partner of Yantai Agricultural Means of Production Corporation ("Yantai AMP") and that Eiliseng is part of an "established agricultural group". We therefore had four entities to try to identify and evaluate.

We started with the named distribution partner, Yantai AMP. We called the company on 23rd July to discuss the Sirius contract and its relationship with YSA. The manager of its import-export division stated he was not aware of any such contract. Another employee we spoke to stated that YSA is not a strategic partner of the group. The same employee noted that YSA's general manager, Zhang Ya Bin, left Yantai AMP several years ago and made a point of saying that meant it was unlikely he would be representing Yantai AMP in any contract negotiations.

We emailed Yantai AMP to confirm our previous conversations (although we were not in doubt about the content). We did not get a reply. A few days later we called again. Despite speaking to same manager, this week the story was different. He confirmed the offtake agreement with Sirius did exist but was unaware of the details of it (he also referred to Sirius by an incorrect Chinese name when saying he knew of the company). The manager also stated that YSA has been a strategic partner of Yantai AMP for over 10 years.

YSA was incorporated in 2017. SAIC filings show that its registered capital of RMB 1m has not been paid in. We were unable to find an office, website or any recruitment ads for the company. Its registered address is a tech incubator park roughly half an hour's drive from Yantai, a small rural town in the northern province of Shandong. Most of the park is under construction with only building number 8 finished and occupied. The guards did not recognise the company name when we asked for it and one suggested YSA was probably just using the building as a registered address, with no actual operations based there. We later called the management company for the building which stated that 700-800 companies use the address as a virtual office. After we visited the address we called YSA and spoke to general manager Zhang Ya Bin. He confirmed the building was YSA's main address. He also said it has about 20 employees and has been up and running for 3-4 years. Unfortunately, he was out of town and said we would not be not able to meet with him or anyone else from the company while we were there.

Eiliseng was incorporated in 2014. SAIC filings show its registered capital of RMB 1m has also not been paid in. According to the Financial Times, which interviewed general manager Jing Hai Shan at Sirius's offices, it has 400 staff and handles over 600,000 tonnes of seeds and fertilisers a year. We were unable to find an office or warehouse, website or working email / phone number or any recruitment ads for the company. Its registered address is about an hour's drive from the city of Guangzhou. The receptionist at the building confirmed that the address is correct but that it is only a virtual office with thousands of companies are registered at the building. She did not have any contact information for Eiliseng. We tried various phone numbers and email addresses listed on SAIC filings but none of these were for Eiliseng specifically. The phone number that worked was shared with hundreds of other companies and the person that answered could not put us through to anyone at Eiliseng. We checked at its old address, a serviced office in Guangzhou. The receptionist there told us the company left in 2015 and gave no forwarding address. We were also able to identify three other entities apparently associated with Jing but none seemed any more substantial – one has the same virtual address as we had visited for Eiliseng, one is suspended and one defunct. Finally, we also obtained a personal mobile phone number for Jing. He was happy to talk to us about the size of the Eiliseng, both in terms of sales and staff (although the numbers he quoted were quite different to the ones he had given to the Financial Times), but he then refused to disclose any operating address for the business or which "established agricultural group" it is a part of. He offered us only a private email address to contact him. As of writing he has not replied to our written request for more information.

According to a sell side firm that covers Sirius, the company "has conducted extensive due diligence, including multiple visits to the businesses" of its new Chinese customers.

That's all Folks!

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