Ennismore Global Equity Fund

Investor Newsletter for the month of June 2019

Issued on 5 July 2019

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 513m as at 28th June. Total assets under management by Ennismore Fund Management were USD 1,145m. The Fund is currently open. 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.

Top Five Long Holdings as at 28 June 2019

Company	Country	Sector	% of NAV
Vivendi SA	France	Consumer Discretionary	6.4
Naspers Ltd	South Africa	Consumer Discretionary	6.1
SES SA	Luxembourg	Consumer Discretionary	5.9
Bayer AG	Germany	Health Care	5.8
Ryanair Holdings PLC	Ireland	Industrials	5.1
			29.3

Exposures as at 28 June 2019

Longs %	Shorts %	Gross Exposure %	Net Exposure %
87.0 (85.0)	57.4 (55.5)	144.4 (140.5)	29.6 (29.5)

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 June 2019

Country	Gross%	Net%
United States	35.3	-4.9
Germany	22.2	7.4
United Kingdom	13.6	5.9
France	11.9	8.0
Cayman Islands	8.2	-8.2
Norway	8.0	1.6
South Africa	6.7	5.7
Luxembourg	7.2	6.9
Netherlands	5.3	4.9
Ireland	5.1	5.1
Italy	3.8	-0.5
Other	17.1	-2.3

Market Cap	Gross%	Net%
>$10bn	58.3	21.8
$5bn-$10bn	39.4	17.0
$1bn-$5bn	36.6	-4.1
<$1bn	10.1	-5.1

Positions	Jun	May
Long	47	47
Opened	2	3
Closed	2	4
Short	94	101
Opened	0	7
Closed	7	4

Sector	Gross%	Net%
Consumer Discretionary	32.8	22.2
Consumer Staples	8.0	6.3
Energy	0.4	-0.4
Financials	6.5	3.5
Health Care	12.6	-0.7
Industrials	19.2	4.1
Information Technology	36.7	-15.3
Materials	1.9	-1.9
Real Estate	1.9	-1.9
Telecommunication	23.8	14.3
Utilities	0.6	-0.6
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 June 2019

	Share Class					
	GBP	GBP A	EUR	CHF	EUR I	USD I
NAV per share[1]	**13.56**	**13.52**	**13.29**	**13.47**	**11.08**	**10.69**
Period	**% Change**					
June 19	**0.5**	**0.5**	**-0.4**	**-1.2**	**0.4**	**0.7**
May 19	-0.1	-0.2	-2.4	-3.9	-0.3	**-0.1**
April 19	1.7	1.7	1.9	3.7	1.6	1.7
2019 to date	**6.4**	**6.4**	**6.7**	**5.4**	**5.6**	**6.9**
Annualised return[2]	**11.8**	**11.6**	**10.9**	**11.5**	**-**	**-**
Since launch[2]	**35.6**	**35.2**	**32.9**	**34.7**	**10.8**	**6.9**
	Discrete 12 Month Rolling Performance					
To 30 June 19	**11.9**	**11.8**	**10.8**	**7.0**	**-**	**-**
To 30 June 18	**20.7**	**20.7**	**20.6**	**25.9**	**-**	**-**

[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, USD I share class on 02/01/19. Note: All performance figures net of fees. **Past performance is not a guide to future returns.**

Attribution %		GBP	EUR	CHF
Long	Q2 19	7.4	4.0	3.6
	Q1 19	12.7	17.0	16.3
	Q4 18	-10.1	-11.0	-12.0
	Q3 18	8.1	7.4	6.1
Short	Q2 19	-4.0	-3.8	-3.8
	Q1 19	-6.3	-6.6	-6.5
	Q4 18	9.2	9.2	9.2
	Q3 18	1.3	1.3	1.3

Attribution figures exclude cash returns and are prior to expenses

Top 5 Contributors and Detractors for June 2019

Contributors	MTD (bp)
METRO AG	108
Bayer AG	81
Naspers Ltd	43
UK software company	34
Electronic Arts Inc	33

Detractors	MTD (bp)
Tencent Holdings Ltd	-51
ASOS PLC	-48
US energy company	-39
German media company	-26
French financial services company	-24

Individual stock attributions relate to GBP A shares and are gross of fees and expenses (including financing/stock borrowing costs).

The Fund's NAV was little changed in Q2, up 2.0% in the sterling share class but down a little in other currencies.

For the quarter, long positions added 7.4% to NAV (in the sterling share class). The largest positive contribution came from The Walt Disney Company ("Disney"), adding 1.2%. In early April the company held an investor day which focused on its planned streaming service, Disney+. This was well received by the market.

The other major positive was METRO AG, contributing 1.0%. Towards the end of June the company received a takeover bid from its largest shareholder. The small premium suggests this was made to allow it to exercise options to take its stake over 30%, in which case a bid would be mandatory under German law anyway. The company has rejected it and we don't expect a higher price will be offered. We continue to believe the company is undervalued.

The short book cost us 4.0% of NAV in Q2.

Across the universe

The universe of potential investments our Fund can make may not be expanding at an accelerating rate but it is still plenty big enough. We don't claim to be able to cover every inch of it, but we do want to find as many seriously mispriced stocks as we can. One way we do this is to focus on business models; get to know one that delivers a high return on capital and then see where else we can find it. That doesn't just mean looking across the same industry because businesses with a similar economic model can show up in lots of different places. We wrote before (in December 2017) about the monopoly power of marketplaces. We have invested in companies that obviously fit this description – like stock exchanges – and ones that don't, like classified adverting and social media, because they have much the same characteristics. In this letter we want to focus on another kind of business, ones that benefit from superstar economics.

When goods are similar but quality varies people will, on average, pay more for the better made product. If the range of quality is distributed linearly then prices should be too – a car that is 10% more efficient should, all other things being equal, be worth

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10% more. But where having the best (or, sometimes, being seen to have the best) really matters to the buyer, the highest quality seller can demand a much bigger premium. Lamborghinis are not much better than Audis on any objective measure (in fact they often share a lot of the same technology), but they sell for much more. Many industries exhibit this in a limited way, as brand value. But the phrase superstar economics really applies where demand is highly skewed to a small number of players, giving them a disproportionate amount of influence over the market – think show business. We'll call this box-office appeal, to borrow a phrase.

Superstar economics get really interesting in industries where the marginal unit cost is very low. Take English football. When the main way of watching games was at a ground the marginal cost was providing an extra seat, a tangible expense because you had to build and maintain the stadium (and pay for other costs, like policing). Now it is mostly watched on TV. The added cost when one more person switches on is negligible, so superstar economics applies to much, much more inventory (2-3 orders of magnitude more for the Premier League). When the wage cap on English footballers was removed in 1961the highest paid player was Fulham's Johnny Haynes, earning about GBP 114,000 a year in today's money (GBP 100 a week then, which was about 10 times the average income). In 2019 the highest paid player in the Premier League is on GBP 21.7m a year (closer to 1,000 times). That is supercharged superstar economics in action. What we want, as investors, are businesses that can earn this kind of return on the capital they invest.

Disney owns a lot of superstars. In 2009 it bought the comic book franchise Marvel Entertainment Inc. ("Marvel") for USD 4bn. Marvel had recently released a successful film based on one of its superhero characters, Iron Man, which grossed nearly USD 600m. In April this year it released Avengers: Endgame, the 22nd film in this movie franchise (known as the Marvel Cinematic Universe, "MCU"). It took in USD 1.2bn in its first weekend and, although it is just short of the record held by Avatar, will gross nearly five times as much as Iron Man. In fact, five of the top ten grossing films of all time are now from the MCU franchise. We don't believe that's because they are the best films ever made. We don't think the same films with unknown characters would have done nearly so well either. These were not just any action movies, the box-office appeal came from the superstar characters that Disney owns.

Marvel is not unique for Disney. It has a lot of superstar franchises - its other releases this year include Captain Marvel, Dumbo, Aladdin, Toy Story 4, The Lion King, Frozen II and Star Wars: Episode 9 (it now owns Avatar as well, but those sequels aren't slated to start until 2021). These titles are often so strong that Disney can cast relatively unknown actors in lead roles, as it did for a lot of the MCU characters, allowing it to keep more of the economics. What's really interesting to us, though, is that the number of ways that it can profit from a franchise does keep expanding. Beginning in the 1980s it benefitted hugely from the arrival of home video and cable / satellite TV. These allowed it to resell old classics like Snow White and the Seven Dwarfs - which was already fifty years old by then - at little extra cost. Later this year it will launch its own streaming service and we think this has similar potential – after all, they have the superstars, and streaming means they will be delivering them direct to customers at close to no marginal expense. That's before we even talk about licensing, which is – we would argue – the ultimate supercharged superstar economics revenue stream. We own Disney shares, but most of this letter looks at another company where the benefits of superstar economics are real, but not quite as obvious.

Another one bites the dust

The Maltby Capital Limited ("Maltby") annual report for the year ended March 2008 reads like a cry for help. Management was watching the wheels come off. Spend on development was being gutted, with sales of new product down around 60% in five years. Staff numbers were less than half what they had been a decade earlier. This against a backdrop of falling industry sales, which had slumped back to 1975 levels in real terms. Instead billions of units were being distributed online for nothing. It looked like bye, bye, baby for Maltby, another old economy casualty of the internet. Welcome to the music recording industry a decade ago.

Most companies facing that kind of challenge don't turn around. In one way Maltby didn't either. It was the investment vehicle Terra Firma Capital Partners Limited ("Terra Firma") took EMI Group Limited ("EMI") private with for over USD 6bn in 2007. Four years later it defaulted and Citigroup Inc., the main lender on the deal, took over, selling the assets off to two different buyers a few months later. But in a more important sense the business that was EMI, and the music recording industry in general, was able to shake it off. It started to recover from the trauma of digital distribution soon after changing hands. Sales have been growing since 2014 and that looks set to continue for the foreseeable future. Over the next few years we think the remaining record labels will be more profitable than ever before.

To see why we are so confident, let's go back to just before the start of the decade. Recorded music industry sales were close to all-time highs, after years of solid growth. The largest labels were increasingly dominant, with distribution concentrated into only a handful of players. If it wasn't exactly a bed of roses for the music industry, it wasn't far off. No one was really focussing on the effect of a technology that allowed consumers to easily copy and share music for free, even though it had been invented more than 15 years earlier. But the wind of change was blowing. Five years later industry sales were as much as a third lower and some major labels had started to deliver heavy losses to their owners. That technology was, of course, the cassette tape. And the decade was the 1980s.

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The recorded music industry survived the cassette by persuading consumers to switch to a new, higher fidelity medium, the compact disc ("CD"). In fact, from its earliest days the value of the recorded music industry has varied considerably as the technology used to consume it has changed. Mass produced recorded music began with the automated gramophone and shellac discs at the end of the nineteenth century. By the start of World War I there was one spinning around in every three British homes. The first challenge came soon after. In 1920 music was broadcast over radio waves in England for the first time and the first national station, the BBC, came in 1922. The supply of free music over the air took a toll on the profitability of the recorded music industry but it eventually responded by effectively enforcing copyright, making radio a large source of royalties income, and co-opting it as a major promotional channel (more on that later). In the Depression era jukeboxes, which effectively spread the cost of ownership, became an important source of income too – in 1939 the Decca label operated a quarter of a million of them, consuming 13 million discs a year (more than half its sales volume). After World War II demand for recorded music again grew rapidly; in Britain the real rate of growth was 9% between 1955 and 1978. Technology changed – electric amplification, magnetic recording and vinyl discs came in – but tended to be backwards compatible. Only in the early 1980s, with the cassette tape, was it again seriously disruptive because this medium could easily be copied at home. Although the CD lead a strong revival right up to the late 1990s, the technology to easily rip these, and to share recordings as digital MP3 files, led to another wipe out – the one that did for EMI.

Today another change is driving a revival of music label fortunes. Their accounts are comfortably back to black and we think the best is yet to come for this industry. More than half of recorded music revenue now comes from fast-growing streaming services, where consumers pay a monthly fee for unlimited access to a vast library of recordings. There were 255 million paid subscriptions to one of these at the end of 2018, up by more than a third from a year earlier. In the US, the most advanced market for digital music, only about half of households have a subscription. In Japan, the second largest music market in the world, only about one in ten do. We expect global subscriber numbers will top 500 million within 5 years as most people in developed markets move to consuming audio this way. At the same time recorded music revenue from other sources will probably only decline modestly, with physical (25% of 2018 revenue) and download (12%) sales fading out but royalty revenue from live performance, radio and video (16% combined) still growing. All in we expect high single digit top line growth over the next decade. That would still leave recorded industry sales some way below the 2000 peak in real terms.

Opportunities (let's make lots of money)

So far we have really only talked about recorded music, and particularly new recordings, but to understand the economics of a music label – to see how sales fall through to profits – we need to split the revenue streams up three ways. The first cut is the deepest, separating out publishing. This is actually a different business to recorded music. Publishing relates to the song writing, which may or may not be done by the recording artist (even if it is the publishing label will often be different to the one owning the rights to the recording). Publishing accounts for around 15% of revenue at all of the major labels. A sale is made every time a song is played publicly as well as when it is bought as a recording, so publishing was always less dependent on physical revenue (even in 1999 CDs only accounted for about 60% of publishing sales). Other revenue streams like radio, TV and live performances meant that it was pretty stable even as recorded music went down the pan. And it remained highly profitable, giving the labels a first step to redemption. Song writers get about half of the top line. Below that it's the label's job to make sure a royalty is collected every time a song is used. These administration costs are relatively low - EMI's publishing margin was between 25 and 30% every year even in the decade it collapsed; Warner consistently reported similar profitability over the last ten years – and fairly fixed. Margins should go up now that recorded music is adding to publishing royalties again.

We also think it is helpful to split recorded music revenue into sales of new music and the back catalogue. This is not nearly as clear cut as the distinction between recordings and publishing. There are obvious blurred lines. Marketing spend on an artist with a new record is also likely to boost catalogue sales, for example. And in fact most of the labels don't disclose this breakdown in their financial reports. Again it's EMI in 2008 that opens a window (in fact one of us also modelled the decay rate of sales from this catalogue for a potential private equity bidder back in 2007). Working back from the numbers given in the Maltby narrative it looks like about two thirds of sales that year came from the back catalogue. Of course, that was a very unhealthy business struggling to bring commercially viable new product to market. Five years earlier the split went more the other way and we estimate that the industry as a whole is probably more like one half catalogue sales. As with publishing, the economics of the model are very attractive, with back catalogue only needing a low fixed cost base. Even in 2008 EMI's margin on it was 28%. This should be higher today, for much the same reasons as publishing.

Record labels don't get this money for nothing. The heart of the business is the artists and repertoire ("A&R") division, which scouts for new talent and develops and promotes signed artists. It's comparable to R&D, so if that part of the company isn't working the other revenue streams are just a declining annuity. Artists sign with a label because it gives them certainty – an upfront advance – and access to other talent, like song writers and producers, and the exposure they need to get noticed, like a TV spot or advertising. The major labels also have negotiating power that even the most established artists can't deliver on their own. For example, revenue earned per streamed song is on average higher than what independent labels or artists can command. The upfront investment the labels make in A&R is risky. New music is expensive to produce and market – spending USD 1m on an unproven act is not uncommon. To put capital at risk the labels demand long term rights over the end product.

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That is, security over earnings from the artists that do make it (that's why catalogue sales are so profitable – they are mostly of artists that have made it). New music margins are not high. On the one hand, for artists that aren't well established the odds they will sell in volume are low (maybe not one in a million, but not good). The labels take a risk on a lot of them and often lose money. On the other, artists that are already successful can dictate better terms from the labels once their contract comes up for renewal; labels rightly make less from their new recordings because they are taking less risk.

Labels don't usually disclose how much they make from new music but it is important for us to have a good understanding of its value to them. We estimate it a few different ways. One is to start with the loss EMI disclosed in 2008. Obviously that wasn't representative, but it gives us a number to work back from. If we run the sales mix back several years, based on what's disclosed in the annual report commentary, we get to new music being more like half of the total. Assuming catalogue margins were similar to the 2008 level that implies EMI's new music margin at the start of that decade would have been somewhere in the low single digits. We arrive at a similar number another way. Between 1989 and 1993, the five largest multinationals spent 22% of sales on A&R. When you think that cost only really applies to new music, and a third of sales go out as royalties and (in those days) perhaps another 15% on the physical cost of product, it is clear that margins must have been low then too. There will be some operating leverage from overall market growth, but holding on to it will not be so easy. There's much more room for costs to be variable – not just royalties but also advances, production and marketing costs as well. One way or another the money will probably get spent. After all, if publishing and catalogue sales become more valuable, as we expect, then the investment that can be justified to acquire them will go up too. Overall the blended operating margin for the majors was about 15% last year, up from more like 10% five years ago. We think operating leverage will see blended margins increase by a similar amount over the next five years, to more like 20%.

Working my way back to you

The music industry has had halcyon days before but, as we've seen, stormy weather always returned. We are not naively saying this time is different but it does seem like some of the problems of the past are less likely to repeat. Disruption from new technology is harder now that streaming is the main distribution channel. It is already technology agnostic – you can listen on pretty much any device – and quality standards, the big selling point of CDs, are easily upgraded without requiring any investment from the consumer. People have the ability to share music for free illegally and are choosing not to use it. Social attitudes may change but as things are most consumers seem happy with the value they are getting from a streaming subscription. In fact the music industry may have better pricing power than ever in a world where most music is listened to this way for two reasons. First, as a streaming customer you can listen to whatever you want, whenever you want. The marginal cost of hearing another song is nearly zero so consumption should increase (the data backs this up, with the number of songs streamed up 50% in the last quarter of 2018, compared to subs up a third). Second, when the choice is do you buy a twenty dollar CD or not the answer is often going to be that it's not worth the money. When it's do you pay 5% more a year or have repeated interruptions from ads a no seems less likely. That should make sales less cyclical in future too.

You may think we are missing the obvious - streaming is the new technology and the labels don't control it. Won't that be the disruption that cuts into label profits? We don't think so. The mentality in Silicon Valley today often seems to be that if a company spends aggressively enough in almost any industry the winner takes it all (with no antitrust response, naturally). Netflix, Inc. embodies this ethos in video streaming, burning through billions of dollars a year in its pursuit of world domination. Everybody wants to rule the world but music streaming doesn't look like it will work out that way (we are not convinced video will either, but for different reasons – one being Disney). The largest music service is Spotify Technology SA ("Spotify"), which estimates it has a 38% share of the market. But this share doesn't seem to be growing, and in the US it's just been overtaken by Apple Inc ("Apple"). That's actually a similar level of concentration to the recorded music industry, where the major labels control about 70% of the market. There's a big difference though – the streaming services are all selling a homogenous product, each label has a unique catalogue. If a major label refuses to supply a streaming service it will lose a lot of sales, but it will get them back - because the streaming service will lose almost all of its customers if it can't deliver 20-30% of the music they want to hear. The labels have the power here.

To us streaming services look a lot more like radio stations in the music industry value chain – that is, a huge source of royalties and the best marketing channel available. It will be hard for them to extract significant value from the labels. It is illegal for a radio station to take payment from one in return for playing a track – this is known as payola – and we think the same would apply to streaming services promoting songs for money as well (Spotify prohibited its users from accepting payment for playlist slots in 2015). It will be hard for them to disintermediate the labels too. Spotify reportedly has it written into its supply contracts that it cannot act as a label itself. The majors always have a gun pointed to its head because they can stop supplying content (as one recently did in India), so it's not surprising the labels collectively dumped their Spotify equity soon after it listed. Long term the profitability of streaming services will always be under pressure from the weight of the big labels' negotiating leverage; assuming, of course, that they continue to control most of the content.

Concentration has always been high in the music industry but it fell significantly in the 1950s and 1960s. In 1947 the four largest labels took 79% of the market in the United States. By 1972 that was down to 47%. Although it quickly began to increase again it would be helpful to understand what caused the decline, and if it could happen again. If it does the labels will be hit twice, losing sales and negotiating power. Unfortunately there's not a clear answer. The independent labels that took share tended to focus on narrow genres that reflected the changing tastes of kids in America. This was probably helped by a change in technology – frequency modulation ("FM") – that allowed a proliferation of radio stations that didn't try to appeal to everyone (TV had become the mass market medium). But that wouldn't explain why the majors were soon able to get back the share they had lost. It is easy to see some parallels today – the idea that the long tail of product becomes more important as online distribution allows more choice is very popular – but the facts tell a different story. If anything the share of sales going to the biggest hits is still increasing a little, and the majors are not losing sales to independents. We don't expect this to change – new music needs a lot of capital upfront, doesn't make much money and is very risky, because you don't get to know in advance which acts will make it. If a label is small, or focussed on a niche, it often won't have enough hits to make a profit (in one sense we think it's comparable to writing high risk insurance, although in this case it's the earnings not the losses that are skewed). The fact that music is a superstar business, with highly skewed earnings over a long time period, probably explains why the market is concentrated in a few major labels.

A similar but subtly different threat is that artists instead contract directly with streaming services. This is technically possible today because you no longer need the physical distribution that was controlled by the major labels, and 3% of industry revenue was direct to artists last year. But distribution was never the main reason to sign for a label. Getting on the shelf is one thing, getting people to take you off it depends on box-office appeal. That buzz is not easy to create. Artists can do it themselves, and it may be easier today with social media, but we are not convinced it will ever be a major route to music stardom. Ed Sheeran was one the most successful at doing this, working on his own for years to get noticed. He made several records, getting one to number 2 on the iTunes chart; the video for another had millions of hits. He did all that without a label, and then he signed for one anyway because it could take him to a level he might not ever get to on his own (we think it worked out ok for him). Widespread direct distribution by artists would change the industry dramatically and we will watch closely how this develops. Only time will tell, but we think it is more likely that the more ways there are to get noticed, the harder it will be to get heard above the noise. Even if you have the best song ever, the major labels are still the surest way of making it a hit today.

Counting stars in the music business is easy. Consumers don't care what label musicians are on, especially for the majors, so why don't the most popular artists take all the value? The biggest acts do earn on a similar scale to top sportsmen, but how they make it is subtly different and that makes a big difference to label profitability. In 2017 the top earner was U2 with income of USD 54m; USD 52m of that came from touring. The same is true even for artists at the top of current sales charts – Ed Sheeran made nearly two thirds of his USD 31m that year from live performances. The average for the top 40 earners was about 75%. Superstar economics applies to the music industry, of course, but not quite as you might expect. Remember it gets supercharged where marginal costs are extremely low, because the same product can be sold over and over and almost all the additional price paid is profit. That's not concert seats, it's recorded music. The major labels benefit much more from this than the big artists (although, as you can see, they do ok). That's why they are much more profitable than the average Premier League football club (that and the fact that the market is dominated by only three suppliers). One big difference is longevity. Labels can invest a lot more than sports clubs do in promoting young talent because they have a much bigger impact on how their careers pan out – and they get longer, more valuable contracts in return. Successful acts do, of course, renegotiate once their deals come up for renewal. They can play the labels off each other or set up one of their own. This is nothing new. In the late 1950s Elvis Presley was responsible for nearly a quarter of record sales made by the Victor label; the biggest recording artists of them all brought in a similar proportion of EMI revenue in the 1960s. Few can bargain with this kind of strength and, in 1967, right at the peak of their power, The Beatles set up their own label, Apple Corps Limited ("Apple Records"). In 2010 their back catalogue was finally made available for sale digitally; these royalties had to be negotiated separately because old contracts tended to be specific about which media sales can be made in. Apple Records reportedly keeps half the revenue, which is several times an artist's typical take. But income from this still pales in comparison to live performances, which brought in USD 16.8m of the USD 20.5m Paul McCartney made in 2017 – half a century after Yoko Ono came on the scene. For an artist it is much more important that they have hit music than to make money from it, because hits sell concert tickets.

Vivendi SA ("Vivendi")

We have talked a lot about the music industry as a whole so far but, as with all of our investments, we started from the bottom up. The major label we are interested in is Universal Music Group, Inc. ("Universal"). It's the biggest of them all, bringing in about 30% of global music sales, and has the best product mix - about 70% of its recorded music sales are from the back catalogue (partly from having bought EMI's recorded music business from Citigroup in 2011, which takes us right back where we started from at the beginning of this note). Unfortunately you can't buy a share of it directly, only through owning its parent company, the conglomerate Vivendi (although if that wasn't the case it might not be available to buy for what we think is a good price). Because it's a conglomerate, a share gives you other assets as well. We'll get them out of the way first because we don't think they are material relative to the value of the music business. There are two large minority holdings in listed companies (Telecom Italia SpA and Mediaset SpA) and, through Universal, a stake in Spotify (which it has promised to distribute the value of to its artist roster). We hedge these, in effect freezing their value at about EUR 3.5bn. Vivendi's main unlisted assets are French pay-TV business Canal+, media agency Havas and book publisher Editis. We value these at around

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EUR 5bn (c.13 times operating profit), EUR 2bn (10 times) and EUR 900m (cost of acquisition in January) respectively. These are not particularly precise estimates but we don't think they need to be. In 2018 Universal made EUR 0.9bn operating profit, on EUR 6bn of sales. We forecast more like EUR 2bn on about EUR 9bn sales five years out, and EUR 3bn on over EUR 12bn after another five – delivering close to EUR 15bn in free cash flow in the meantime. These are, of course, not likely to be the real numbers they report but we think the direction and scale are about right. We estimate Universal is worth EUR 30-35bn. That adds up to total group assets of EUR 40-45bn in the Vivendi conglomerate, compared to a current market cap of EUR 31bn with about EUR 3bn net debt.

One of the attractions of making this investment today is that we will probably soon know if we are right about how much the Universal asset is worth (or, at least, what price tag potential buyers are willing to meet). Management has committed to offloading half of the music label and the sale process is well underway. It is likely to be done within the next year. Given the upside we see relative to Vivendi's current market capitalisation, we think the risk of ownership is now well worth it.

PS you might have noticed a few song titles cropping up in the headers; we also included a couple from Universal's catalogue in each paragraph about Vivendi and the music industry. Feel free to see how many you can find (each title is at least two words long). We did this partly to show just how broad, varied and deep its catalogue is, and partly because it was fun (and we think people work better when they are enjoying themselves). The songs used should in no way be taken as a reflection of the musical taste of Ennismore Fund Management Limited employees.

Bang bang

We would have to be blissfully unself-aware to be discussing superstar economics without looking in the mirror. The investment management industry has often done a good job of convincing its customers that there are star investors out there. If there are, all other things being equal, supercharged superstar economics applies – investing USD 10bn instead of USD 100m in the same stocks comes with little marginal cost. But in the universe we live in the laws of physics do apply, particularly gravity. Size matters. When a superstar cools it collapses under its own weight. What's left is a black hole.

This seems like a good time to mention that we recently hired two trainees to join the Fund's team. The job description is copied underneath. We were not looking for stars:

> "We are looking for a trainee to join our global equity team. Duties might include getting the coffee, arranging meetings and occasionally even loading the dishwasher. Ennismore is a small firm so you can expect to be asked to help out with anything. Of course, most of our work is looking for companies that look like anomalies. Companies that can be bought for a lot less than they will earn in future. Companies that are not what they claim to be.
>
> The day job, once we are working on a company, is reading about the industry it is in to learn how it works, then doing tests to check if we understand it. Most of your time will be spent doing this kind of analysis: finding facts on the ground by making site visits, collecting and processing industry data, conducting market research, and a lot of calls to people who might know better than us. We also have databases that need maintaining - one on company financial and operational data and one on interesting people. These require some VBA coding (this can be learnt on the job but any programming experience would be welcome).
>
> If you are excited by the fast-paced action of a trading floor then you might want to apply to Axe Capital instead. We work slowly and quietly. We will teach you how to forensically analyse accounts and how to value a business, two things we think Ennismore has proven to be good at over the years. If you are also good at these things this role will naturally lead to an investment management job in the firm. A degree is not essential and non-finance subjects are more than welcome, maybe preferred. Very strong numeracy is needed, though - the first step in the recruitment process is a timed maths test (without a calculator). After that we use the Justice Potter Stewart definition of who is the right candidate. If you think it's you please contact recruitment@ennismorefunds.com with "Trainee" in the subject line and tell us why."

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Risk Warning

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We hereby disclose that as at the date of first issue of the report to which this is an Appendix, we held positions in the companies discussed in that report and we are thus subject to conflicts of interest in respect of these companies. The analysis presented on these companies has not been prepared in accordance with legal requirements regarding the independence of investment research and as such is considered non-independent research, as defined by COBS 12.3.2R of the FCA Handbook and as a marketing communication.

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The examples of specific investments included herein are not representative of all of the companies purchased, sold or recommended for the Fund. The Fund's portfolio contains a much larger number of positions than the examples set forth herein and, accordingly, the examples are not intended to indicate the overall composition of the Fund's portfolio. It should not be assumed that investments in the companies identified will be profitable, that recommendations made in the future will be profitable or will equal the investment performance of those discussed herein, or are representative of investments that will be made in the future. There is also no guarantee that any of the positions are currently or will remain in the Fund. The information included in this document should not be considered a recommendation to purchase or sell any particular security or other financial instrument. All statements and expressions are the sole opinion of Ennismore and are subject to change without notice.

The list of winners and losers presented herein has been calculated by including those positions that contributed most significantly, either positively or negatively, to the performance of the Fund's portfolio during the period. This is not meant to be indicative of the performance of all positions contained in the portfolio. Past performance is not indicative of future results.

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