Ennismore Global Equity Fund

Investor Newsletter for the month of February 2023

Issued on 6 March 2023

Fund Details

Daily dealing UCITS and Irish Central Bank regulated open-ended investment company with Financial Conduct Authority recognition and registered in Ireland. The Fund size was USD 129m as at 28th February. Total assets under management by Ennismore Fund Management were USD 585m. The number of shares issued by our funds is capped in order to limit the level of assets under management in each strategy. We currently have capacity available in the Global Equity Fund. If you would like more information or to invest please contact Adam Sullivan on +44 (0) 20 7368 4224 or email subs@ennismorefunds.com.

Performance as at 28 February 2023

	Share Class[1]					
	GBP	**GBP A**	**EUR**	**CHF**	**EUR I**	**USD I**
NAV per Share[2]	12.68	12.61	12.57	11.47	9.74	9.97
	% Change					
February 23	0.8	0.7	1.5	1.1	0.6	0.7
2023 to date	1.5	1.4	2.8	3.5	1.2	1.5
Annualised return[3]	3.8	3.7	3.6	2.2	-0.6	-0.1
Since launch[3]	26.8	26.1	25.7	14.7	-2.6	-0.3
Note: All performance figures net of fees. **Past performance is not a guide to future returns.**						

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

The Fund's NAV increased by 0.7% in February. Our long book cost 1.0% while our short exposure contributed 2.1%.

Global Equity markets were largely flat in the month in GBP terms after posting strong gains in January. This translated into our book with no single name contributing or costing more than 50bps of performance.

Buzzi Unicem SpA, which is our largest holding, contributed 28bps during the month. The company reported preliminary results in which EBITDA guidance came in ahead of consensus. We have written an updated stock comment below. Our largest detractor was Tucows Inc costing 37bps. The company reported earnings during the month, and after an initial positive response, the stock sold off sharply in the second half of February. We believe the fibre broadband assets the company is building in small and medium sized US towns are very valuable, potentially worth significantly more than the group's enterprise value within a year or two. Whilst the valuation discrepancy is extreme, and substantial activists on the share register increase the odds of value being realised, the balance sheet risk cautions against a large position size. We added a little to the position at month-end.

Top Five Contributors and Detractors for February 2023

Contributors	MTD (bp)
Hong Kong software company	44
Buzzi Unicem SpA	28
US technology company	23
Hemnet Group AB	21
US electronics retailer	16

Detractors	MTD (bp)
Tucows Inc	-37
Deliveroo Plc	-36
Schibsted ASA	-31
News Corporation	-19
Auto Trader Group Plc	-15

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

Top Five Long Holdings as at 28 February 2023

Company	Country	Sector	% of NAV
Buzzi Unicem SpA	Italy	Materials	5.8
thyssenkrupp AG	Germany	Materials	5.1
Schibsted ASA	Norway	Communication Services	4.8
Admiral Group Plc	United Kingdom	Financials	4.2
D'Ieteren Group	Belgium	Consumer Discretionary	3.7
			23.6

Exposures as at 28 February 2023

Longs%	Shorts%	Gross Exposure%	Net Exposure%
73.5(78.1)	43.9(45.7)	117.4(123.9)	29.6(32.4)

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

Exposures by Country, Market Cap & Sector as % NAV and Positions as at 28 February 2023

Country	Gross%	Net%
United States	39.6	-22.3
United Kingdom	24.5	22.9
Germany	9.0	9.0
Norway	7.6	2.9
Italy	5.9	5.8
Sweden	5.7	1.1
Belgium	3.7	3.7
Japan	2.8	2.8
Hong Kong	2.8	-2.0
Austria	2.6	-0.5
Mexico	2.5	2.5
Switzerland	2.3	-0.2
South Korea	1.7	1.7
Spain	1.5	1.1
Brazil	1.1	1.1
Ireland	1.1	1.1
Other	2.9	-1.0

Market Cap	Gross%	Net%
>$10bn	19.2	-0.7
$5bn - $10bn	19.4	8.0
$1bn - $5bn	66.1	24.2
<$1bn	12.7	-1.9

Positions	Feb	Jan
Long	45	47
Short	81	78
Longs Opened	2	1
Longs Closed	4	4
Shorts Opened	10	9
Shorts Closed	7	5

Sector	Gross%	Net%
Communication Services	19.1	12.7
Consumer Discretionary	17.0	4.1
Consumer Staples	6.1	2.7
Energy	0.0	0.0
Financials	14.9	7.5
Health Care	4.2	-3.9
Industrials	17.0	-4.4
Information Technology	18.4	-0.1
Materials	16.6	12.7
Real Estate	2.9	-0.3
Utilities	0.0	0.0
Other	1.3	-1.3

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

Buzzi Unicem SpA – Italian cement manufacturer (5.8% NAV)

Cement is the second most consumed resource in the world, behind only water. There is no substitute. Family owned and run, Buzzi is a €4bn global company with strong market shares everywhere it operates. This is a typical Italian family-run business – it has been loved and cherished since it was set up in 1907 and then handed down from generation to generation, like only the Italians know how! Foreign expansion, done through partnerships or friendly takeovers, started with a move into Texas in the late '70s and then Mexico in the early '80s. In the early 2000s Buzzi entered Germany and surrounding countries by purchasing the Dyckerhoff family's business and about five years ago it entered Brazil through a joint venture with a local family run company.

We wrote in detail on Buzzi just over a year ago in our December 2021 newsletter but after such a challenging year which saw high inflation, particularly for energy, declining volumes, and war in Ukraine – it feels right to provide an update. The brief version is that Buzzi has come through this test with flying colours, and remains as cheap as ever.

For further information please contact:	Adam Sullivan, Ennismore Fund Management	+44 (0) 20 7368 4224	subs@ennismorefunds.com
For dealing please contact:	Northern Trust International Fund Administration Services (Ireland) Ltd	+353 (0) 1 434 5103	Ennismore_TA_Queries@ntrs.com

There is a saying in investment that “the cheaper it is the less you need to know”. Having positively surprised the market with preliminary 2022 results on 9 February, the stock trades on an historic Enterprise Value (EV) to EBITDA multiple of just 4 times. We don't usually use EV/EBITDA as a valuation measure, but full results including net income will not be published until the end of March. We estimate this translates to a PE multiple of 8-9x. At such a valuation, one might expect that cement consumption was obviously at cyclical peaks and likely on the cusp of a significant decline. It's certainly possible that 2021 marked the peak of this cycle, but US consumption is c. 16% below the 2005 peak. And whilst the US housing market is clearly weakening, we expect that growth in infrastructure spending (which accounts for 40% of Buzzi's US business) as a result of Biden's infrastructure plan will provide substantial offset. Finally, whilst we are of course in the absolute rather than relative return game, it's interesting to note that US-focused cement companies are valued more than twice as highly on an EV/EBITDA basis – which is relevant given that two thirds of Buzzi’s revenue and more of profits derive from the Americas.

2022 highlighted the local oligopolistic nature of the industry through the ability of Buzzi and its competitors to achieve price increases more than offsetting sharp raw material cost increases. The price increases were such that Buzzi’s cement volumes fell by 9.2% yet net sales increased by 16%, or 9.6% on a constant currency basis. The strengthening of sales prices continued in Q4 in all geographic markets. The price increases varied strongly by country: 40% in Italy compensating for volumes down 15%, 10-15% in the US with volumes down 5%, and in Germany prices were only up slightly since there was comparatively little pressure on energy costs with the vast majority being on fixed contracts. 65-70% of Buzzi’s energy supply in Germany comes from alternative fuels, that figure being just 20% in the US and Italy.

In terms of the outlook, this year has started with volumes being slightly lower than last year in January and February, but key is that pricing could be 10-15% higher than 2022 on average, benefiting from the tail effect of progressive price increases realised during the year. In central Europe, where some energy hedges and fixed contracts have expired, management plans to increase prices in the order of 20-25%.

Far more important than the short term is what the future holds. We don’t have a crystal ball – we subscribe to Buffett’s view, in his just released annual letter, that “near term economic forecasts are worse than useless” – but we believe there are a number of pointers to the likelihood of the business continuing to perform solidly:

- As we said at the start, but worth repeating, cement is an essential product with no substitute.
- The industry is locally oligopolistic – cement doesn’t travel well – with Buzzi having strong market shares in all the countries and geographic areas where it operates.
- Cement accounts for 8% of all man-made emissions. The need for CO_2 emissions to be reduced dramatically means that new permits to produce cement are incredibly hard to come by. Thus, the industry’s already high barriers to entry have been moved a few notches higher.
- The emissions problem integral to producing cement will not be solved by the industry alone. EU and government subsidies are necessary – indeed Buzzi enters 2023 with over €500m of carbon credits, received for free from the EU, which do not appear on its balance sheet - particularly so in the area of carbon capture. An example is in Norway where HeidelbergCement has received 80%, from the Norwegian government, of the capital expenditure needed to develop the first ever cement plant with carbon capture and storage (in empty oil wells). In July last year Buzzi, for the first time, issued its CO_2 emissions reduction road map. Management is confident Buzzi will get its fair share of such grants. It is likely, in our view, that such assistance will be focused on larger players, such as Buzzi, who have the financial strength and expertise to deliver. Smaller existing players are unlikely to have the financial wherewithal to deliver the required CO_2 reductions. Consequently, barriers to exit will be lowered. These changing dynamics for both entry and exit barriers naturally favour the existing larger players.

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• From 2026 the EU will introduce the Carbon Border Adjustment so that imported cement to the EU, from Algeria and Turkey for example, will incur a CO_2 tax thus creating a level playing field. This could prove to be just the boost needed for Buzzi's Italian business which is finally starting to recover from years of overcapacity after substantial consolidation.

• The business is family run with four of the family being Executive Directors with a passion for looking after this key member of their family. Several more junior members are working on the shop floor learning their trade. The Buzzi family has a history of treating minorities well. Witness the buying in of saving shares a few years ago at a premium to the ordinary shares. The family has no plans to diversify into other related areas as some competitors have done; they want to stick to what they know best. We're happy to be sat alongside them.

• Buzzi has a history of careful and profitable geographic expansion. Brazil is a good example. Having entered the market in 2018 via a joint venture with a local business, in 2021 it acquired CRH's cement assets in the country. Last year the Brazilian business had consolidated turnover of €400m with an EBITDA margin in excess of 30%. In 2026 Buzzi is very likely to exercise a call option, to buy out its 50% JV partners at 10x the EBITDA of the average of the previous 3 years.

• Unusually, in today's world, there is little threat from China, which consumes around half of the world's 4bn tons of cement each year. Chinese cement is typically only 60% clinker whereas the US Department of Transportation contracts still mandate Portland cement where clinker is 80-85% of the mix, thus preventing imports from China.

That brings us back to the issue of valuation. With a market capitalisation of €4bn and net cash of just under €300m the business has an EV of €3.7bn. Announced EBITDA – sorry, that measure again – was €880m for 2022. Factoring in capital expenditure of around €300m (more than 20% above depreciation), revalued inventory as a result of the higher costs, dividends from the Brazilian and Mexican associates, a small amount of interest expense and the inevitable tax, we estimate Buzzi generated conservatively €350m of free cash flow in 2022. This puts the business on an historic free cash flow yield to EV of almost 10%.

With such high fixed costs inherent in the business, the biggest risk we see is that there is a severe economic downturn. Additionally, the high capital intensity will always limit the return on capital employed that the business can generate to low double digits at best. These two factors, one timing, one structural, rightly limit the valuation, but the discount is currently too harsh in our opinion. The current valuation, allied to the net cash balance sheet position, means that the stock is very well positioned to weather a downturn.

With a conservative dividend policy the stock has a dividend yield of 1.8%, covered seven times by earnings and more than five times by cash flow, and the Board has recently sanctioned a further share buyback of up to 12m shares, roughly €250m. The share count has reduced by about 4% per year since the end of 2019.

It is noticeable that Buzzi is making more of an effort with the investment community than in years gone by, and has employed an excellent Investor Relations manager in Lorenzo Coaloa, to communicate with shareholders. The CEO, Pietro Buzzi, is also meeting investors. Last week, for example, management visited Madrid for the first time to meet shareholders. We were pleased to note that Mr. Buzzi insisted on flying with Ryanair.

With just a small re-rating, as the market reappraises the quality of the earnings, allied to the ongoing cash generation of the business, we believe the shares will deliver a return of at least 30% over the next 12-18 months.

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

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

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