The Art of Saying No: The Investments We Rejected

Part II

October 27, 2025

This is the second installment in our series analyzing investments we researched extensively but ultimately passed on. As we noted in Part I, studying the companies we did *not* ultimately buy offers a unique window into our investment approach—one that's absent if we only examine the companies we did buy.

The Setup

It was January 2019, and a multi-hundred-page presentation caught our eye: a company with an intriguing business model and moat. New models always pique my interest; I've long believed they can unlock powerful investment opportunities. Here, the pitch described a novel financial firm delivering steady 25%+ annual growth — still early in a long runway — with a robust moat, scant competition, and a relatively modest valuation: high growth at an *un*reasonably cheap price. The company was … Burford Capital, circa January 2019.

Background

Burford was (and is) the founder and leader of the field of litigation finance. They fund high-stakes commercial cases both individually and via portfolios, providing capital both directly to companies as well as to law firms, in exchange for a share of the proceeds if and when the litigation is successful. We have discussed Burford Capital often in these pages since our 2020 investment, so I will keep the overview general and avoid excessive detail. The focus here is why we initially rejected Burford Capital for our fund portfolio, after our early-2019 research.

Burford absolutely had an amazing business model, with stellar returns to match. Steady IRRs of 30% on their investment portfolio demonstrated the efficacy of their approach, with a relatively small percentage of losing cases, a solid base of singles and doubles, and occasional outsized home runs that supercharged overall performance. Judicious leverage counterbalanced their operating-level expenses and holding of cash, yielding a similar level of ROE. Litigation finance was, and largely still is, at early stages of growth and can be expected to grow for many years into the future, as courts worldwide embrace it and rising costs make funding ever more attractive.

Burford had a strong competitive moat, combining all the ingredients needed for a major litigation finance player in one firm — in-house top legal talent to assess cases, investment expertise to select and structure deals, vast sums of capital to allow for adequate diversification in investments that can easily reach $100+ million for a single investment, and a conflict-free, disinterested source of capital. Most would-be competitors lacked one or more of these necessary ingredients. Law firms, although obviously brimming with legal expertise, often do not have the necessary investment mindset. They also generally operate as cash businesses with almost no balance sheet, and they would not be able to finance cases handled by competitor law firms due to conflicts of interest. Banks are full of capital and always on the hunt for innovative places to deploy it, but they lack the requisite legal expertise (and it is never a good idea to outsource your key investment analysis). They are also wary of running the reputational risk of funding one side of a lawsuit, inevitably souring business relationships with the other side. Generalist hedge funds and private equity firms, even though they definitely have business expertise and even have a conflict-free, disinterested source of capital, are again lacking the necessary legal expertise and are usually not in a great position to adequately diversify their litigation risk. These dynamics naturally leave litigation finance for the domain of dedicated specialists such as Burford Capital and a few other firms, all of which were much smaller and less sophisticated than Burford, the market leader. The overall setup promised years of compounding returns without fear of commoditization.

Why We Rejected

One word: Valuation.

Burford was a solid business with an attractive and unique business model, with years of growth potentially ahead of it. But at 18 GBP (trading exclusively in London then), the P/E of ~7 (and FCF multiple of ~25) was just a little too rich for us to consider it *deeply* undervalued. And that is the standard for inclusion in the Focus Capital Management portfolio. It was a close call, and I admit to some sense of ambivalence and genuine worry at the time that we would kick ourselves for missing out on investing in a great company. But as deep value investors, our first mantra has to be that valuation always matters. At that price, we had no choice but to pass.

The Rest of the Story

Only a few months later, the risk-reward calculus drastically changed. In August 2019, Muddy Waters released a series of short reports accusing the company of fraud and manipulation in reporting its returns and operating metrics, accounting shenanigans, insufficient liquidity, and having a poor underlying business, capping it off by calling Burford "arguably insolvent." The stock plummeted briefly more than 60%, then bounced up to settle at roughly half its prior level. By definition, this made the stock a far more attractive investment than before. Providing, of course, that one could sufficiently vet and debunk the many allegations made by Muddy Waters.

We dove back into the research with gusto. Burford released detailed point-by-point rebuttals to the allegations together with a ton of detailed information and metrics, which really helped bring clarity to the investment case, while thoroughly demolishing the short report. Subsequent years have vindicated Burford, showing that all of Muddy Waters' allegations as to the business, fraud, accounting issues, and liquidity were indeed false. Although the Muddy Waters report did succeed in muddying the waters and reversing Burford's multi-year stock momentum, I do not complain too much, as this report is what gave us such an attractive entry point. In September 2019, we began building a small starter position.

In March 2020, as the stock market panic-imploded due to COVID-19 fears, Burford shares went on ultra-sale, dropping to even lower levels than those seen directly after the short report was released. We took advantage in a big way, not just doubling down, but more than quintupling down on our original starter position. This investment has worked out very well for the fund, with the stock price having tripled since, although recent pullbacks leave it at about double our advantageous entry point.

In our opinion, Burford remains deeply undervalued and has quite a way to go to reach intrinsic value. In particular, their massive win in the YPF case is a major endorsement of their business model and a huge sum in its own right. (The YPF case is presently undergoing appeal as we write, which should conclude sometime next year. Enforcement of the award is also expected to take time.) Burford's entitlement in the YPF matter is alone more than 3 times the size of their market cap, which is hugely significant even if you assume, as we do, that the endgame will involve some sort of settlement at a discount to face value. And you still get the rest of a growing and profitable business, compounding at attractive rates for years, for free! We still expect great things from Burford. Yet, to highlight our point regarding valuation, if we had bought in at the price Burford was trading at when originally pitched, we would actually still be very underwater today.

Postmortem & Lessons

We feel that so far we have made all the right calls with Burford. We passed originally due to valuation, and then we jumped in when valuation turned in our favor. Our Burford journey is not over, but we believe we are very well positioned for the future.

Moral of the story: Valuation always matters.