Investmentaktiengesellschaft für langfristige Investoren TGV

Investmentaktiengesellschaft für langfristige Investoren TGV
Rüngsdorfer Str. 2 e · 53173 Bonn · Germany

Investmentaktiengesellschaft für langfristige Investoren TGV
Rüngsdorfer Straße 2e
53173 Bonn
Germany

Telefon: +49/228/368840
Telefax: +49/228/365875

E-Mail: info@langfrist.de

Dear Investors

We are enclosing the shareholder letter for our Teilgesellschaftsvermögen “Partners Fund” for the year 2018 written by our sub-advisor MSA Capital GmbH.

Yours sincerely

Investmentaktiengesellschaft für langfristige Investoren TGV

Vorstand: Jens Große-Allermann, Waldemar Lokotsch
Aufsichtsrat: Dr. Maximilian Zimmerer (Vors.), Wolfgang Fritz Driese (stv. Vors.), Alexander Pichler (stv. Vors.)
Eingetragen im Handelsregister Bonn HRB 16143
Investmentvermögen mit veränderlichem Gesellschaftskapital

Investmentaktiengesellschaft für langfristige Investoren TGV
Teilgesellschaftsvermögen Partners Fund
FY-2018 Memo of the sub-advisor – MSA Capital, Dr Mathias Saggau

Bonn, January 2019

Dear Investors,

The share price of the sub-fund (TGV) Partners Fund was EUR 141.97 as of December 28, 2018. Thus, the change in value for the year 2018 including all costs amounts to +0.76 %.[1] The DAX had to face a loss of -18.26 % over the same period.

Year	TGV Partners Fund (1)	DAX (2)	Difference Δ (1-2)
2015 (9 months)	+ 1.48 %	− 10.22 %	+ 11.70 %
2016	+ 16.27 %	+ 6.87 %	+ 9.40 %
2017	+ 20.24 %	+ 12.51 %	+ 7.73 %
2018	+ 0.76 %	− 18.26 %	+ 19.02 %

Per annum	+ 10.00 %	− 3.28 %	+ 13.28 %
Absolut	+ 42.96 %	− 11.76 %	+ 54.72 %

After the first half of 2018 had been rather uneventful for the overall market, we witnessed a turbulent stock market in the second half, and especially in the last weeks of the year. All major indexes in the world have been on diving excursion in the last three months of 2018. In individual segments of the market, there were significant upheavals. As apparent in our new position **Majestic Wine**, at one point or another, the proverbial baby was once more thrown out with the bath water.

To emphasise my stance right away: these fluctuations are normal in the stock market and even healthy from time to time. The market does not always go up in a straight line. You cannot meaningfully protect yourself against downturns, and if you want to invest successfully in the long term, stamina, the right temperament, and some discipline must be brought to the table just to sit it out.

The TGV Partners Fund concluded the year with a slightly positive result. The reported performance in 2018 can be broken down to the following drivers:

Overall, the top-weighted positions ended the year on a slightly positive note. Calculated in Euros, **Tucows** fell slightly, **Alphabet** gained slightly, and **Gruppo MutuiOnline** rose sharply at around + 20% despite the doomsday mood in Italy. Much more important, however, is that all three companies have also developed operationally and that in my estimation, their intrinsic value has grown over the past year.

The development of the share price of **amaysim** was rather catastrophic this year, partly due to the ongoing price war in the Australian telecommunications market. It lost approximately half of its value

[1] Performance calculated according to „BVI-method". The difference in percentages and changes in NAV are due to yearly disbursements from the fund related to taxes.

over the course of the year. This steep drop resulted in a negative contribution to the total assets in the TGV Partners Fund of around -6 % to -7 %.

Other investments such as **TripAdvisor** or **Ahlsell** performed exceptionally well until their sale in the past year, contributing in total around + 5 % to + 6 % based on the total assets.

At this point, especially in the light of the still slightly positive result in the past year, a serious word of warning seems to be indicated. The result of the past year is satisfactory compared to the indices but also owed to the concentration on a select few companies whose good operating performance contributed to this outperformance to the market. The fact that the positive development I anticipated in the medium and long term is becoming apparent in such a weak market phase is admittedly a bit of a fortunate coincidence. There will, or rather, must also be periods of underperformance in the future.

When selecting companies, the overriding goal is a sound and long-term return on investment. This means that I am still looking at five years or more as an investment period. There are many factors influencing short-term stock prices, and stock prices often deviate significantly from the intrinsic value of each company. This cannot be prevented – and again, this is not a bad thing. However, it is important to me to put potentially emerging, unrealistically high expectations of future performance into perspective.

The companies in the TGV Partners Fund

Of the thirteen companies the TGV was invested in on 31/12/2018, as usual, I am listing the ten largest positions in alphabetical order:

- Admiral Group
- Alphabet (Google)
- Amaysim
- Gruppo MutuiOnline
- Interactive Brokers
- Majestic Wine
- National Oilwell Varco
- NOW
- Rolls-Royce
- Tucows

These ten companies represent around 90 % of the fund's assets. The largest company the TGV is currently involved in has a market capitalisation of around 600 billion Euros, the smallest of approximately 10 million Euros.

The central investment principles of the TGV Partners Fund have not changed and will not change in the future. When recommending potential investments, I remain committed to the following criteria:

1. Does the company have a reasonable business model?
2. Does the company have a lasting competitive advantage?
3. Does the management act rationally, with integrity, and does it consider the shareholders to be partners?
4. Can we purchase the company's stocks at a reasonable price?

Changes in the top 10

Although two new names have appeared in the list since the semi-annual report, the material components of the portfolio have remained unchanged over a longer period of time. The weighted holding period is slightly less than three years across the portfolio. Given that the TGV will only enter its fourth year of operation in 2019, this represents a reasonable timeframe, underscoring the long-term investment horizon of the TGV Partners Fund.

Although **Grafenia** has dropped out of the top 10, it continues to be an integral part of the portfolio. We added **Interactive Brokers** and **Majestic Wine** shares to the portfolio during the final weeks of the year.

Ahlsell

Although Ahlsell has not been in the top 10 since December 2018, the company should still be mentioned as it was one of the ten largest investments of the TGV Partners Fund for several weeks. We look at the investment in Ahlsell with one laughing and one crying eye.

Ahlsell is a Swedish wholesaler and distributor that primarily sells plumbing and electrical supplies in the Scandinavian countries. In addition to a large selection, attractive prices and fast and complete delivery play an important role for the customers, mostly craftsmen.

Ahlsell, a company that has been in the market for over a hundred years, has been owned by the private equity firm CVC Capital Partners since 2012 and has gone public 2016. Since I highly appreciate the business model of distributors in general, I have followed the evolution of the company since the IPO. After the IPO, the company developed well and made several meaningful acquisitions.

However, CVC had apparently envisioned the IPO differently: the company still held about 60% of the outstanding shares after the IPO and sold further shares over the next two years until they only held 25% of the shares, still making them the largest shareholder. The stock price of Ahlsell did not benefit from this ongoing so called overhang sell-off. In conjunction with the continually simmering worries about construction in Sweden cooling down, the share price moved mostly sideways in the years since the IPO.

After following Ahlsell from a distance for a while, I visited the company in autumn 2018 together with Marc Profitlich, a good friend and like-minded investor. We visited branches, talked to the people involved, and learned a lot about the culture of the company. The positive image was confirmed, and I recommended the purchase for the TGV Partners Fund.

After the share price of Ahlsell dropped to around 42 Swedish Krona (SEK) in tune with the general market in November and December, CVC announced in early December 2018 that it wanted to fully buy back the company and take it off the stock market at a price of SEK 55. For the shareholders, though, this takeover represents a premium of around +30 % compared to the price Ahlsell traded for on the day before, but virtually no premium compared to the price paid in summer – let alone a price that would in my opinion even remotely come close to the intrinsic value of Ahlsell.

I am in two minds about this: For one, I consider the price offered by CVC quite low ball. Ahlsell has a fantastic market position in Scandinavia and a very stable business model. Due to their long ownership, CVC knows the company inside out and understands exactly where the opportunities and risks lie.

The possibility of another bidder appearing is low, so CVC is likely to get away with the bid. Ahlsell is a great company, and I have spent much time understanding its business model. Knowing its best days are yet to come and having to sell at such a low price hurts.

On the other hand, this takeover also provides a decent mark-up at a time when other prices were falling sharply. The forced sale of Ahlsell offers liquidity, which can be reinvested at a very advantageous time. For this reason, TGV Partners Fund sold the shares of Ahlsell and, with the liquidity freed up, acquired shares of the British company **Majestic Wine**, which was particularly affected by the price drops in December.

Majestic Wine

Majestic Wine is a British company that is probably unknown to most German shareholders, but its German counterpart will be known to almost everyone. In many respects, the wine shops of Majestic Wine are similar to those of Jacques' Wein-Depot in Germany, a subsidiary of the publicly listed **Hawesko**.

Even today, the stationary wine retail shop is still a major part of the business of the company. However, 2015 saw a groundbreaking change for Majestic Wine. Majestic acquired **Naked Wines**, which was founded a few years earlier and still managed by founder Rowan Gormley. Rowan brought his team, became CEO of the entire group, and one of the largest shareholders in the company.

Naked Wines is the modern interpretation of a wine club and a fantastic idea: wine lovers ("Angels") who are registered with Naked Wines, pay a monthly amount into a savings account, which is used to crowd-finance winemakers. Through the combination of direct shipping, the omission of various middlemen, and a secure funding for the winemaker, good wines can be offered at significantly lower prices than in stationary retail. This price advantage is passed on to the "Angels". The business has developed extremely well in recent years. Naked Wines has several hundred thousand regular customers ("mature Angels") in the United Kingdom, the United States, and Australia.

The first time I came into contact with the company was about three years ago, and I am fascinated by the story of Naked Wines and the team around Rowan. Having met Rowan and many other members of his team on several occasions, I have no doubt that the entire team is passionate about what they are doing and determined to shake up their own marketplace. Rowan and his team are among the main motivations to invest in Majestic Wine.

As is common with subscription business models, Naked Wines incurs a good deal of customer acquisition costs before establishing a customer relationship. Simply put, the more customers are won, the higher the costs. The higher the number of customers, the higher the value of the customer base.

If one is confident that the recruited customers have a good value compared to their acquisition costs, then it makes sense to invest as much as possible – even if it deflates the current results in the short term. That's what Rowan has understood and internalised. Much better still, he manages to see this approach, which is not particularly popular with all market participants, through to do "the right thing".

It will be exciting to see if and in what dimension Naked Wines will "crack" its own markets and how succsessful the business model can be in the long term. Especially the US, a huge market in which wine is on average much more expensive for consumers than in Germany or Great Britain, is a crucial factor.

Especially there, the Naked Wines model comes in handy. Better wine at lower prices – that should work everywhere – but especially where the prices and the number of intermediaries are particularly high.

Due to a number of circumstances, Majestic Wine is being viewed exceptionally sceptically on the stock market. The first perceived issue is that the company is undertaking a potentially poorly understood change in the business model from a pure retailer to an Internet subscription business. Another reason is that all retail companies are currently being watched with extreme scepticism due to the "rapid amazonization". In addition to that, Majestic Wine has its headquarters and a good portion of its business in the UK, and the simmering issues surrounding Brexit as well as its consequences are sparking much uncertainty.

As a result, in November, Majestic Wine's shares suddenly and massively depreciated in a weak market environment following a content-wise unspectacular mid-year result. In the weeks that followed, profit warnings issued by other retailers in the UK did not contribute to brightening sentiment, but to further declining prices. Hence Majestic Wine shares have lost almost half of their value since the summer. In my opinion, this is an extremely exaggerated reaction of the market on a good company with an exceptional management team, so the TGV Partners Fund used this opportunity to purchase its shares.

Operational development vs price development vs valuation

In contrast to the almost unchanged price of the TGV Partners Fund, 2018 was a very pleasing year for most companies in the TGV Partners Fund. I presume that – after presenting the final annual results in the spring of 2019 – on average, "our" companies will have improved their results compared to the previous year. In the long run, these operational results are the primary driver for the success or failure of the TGV.

Tucows[2] had a mixed year in 2018, but the general trend is positive. Due to the acquisition of Enom in 2017, results for the entire domain business have improved significantly in 2018. If in the past I have been cautious about "stagnating as expected" business, I stand corrected as Elliott and his team have managed to also increase the gross profit organically. Meanwhile, the number of users of the mobile communications business Ting Mobile stagnated. The business of Ting Internet, which is providing fibre-optic internet access, suffered some minor delays in local construction in 2018, but it is becoming increasingly clear that the "fibre-optic experiment" will be a very real and soon profitable business. I expect more "Ting Cities" to be added to the portfolio over the next few years.

Gruppo MutuiOnline[3] has had an eventful year. In addition to robust growth in its core business, brokerage business, and in Business Process Outsourcing (BPO) business, three acquisitions were initiated.

On the one hand, 50 % of "Agenzia Italia", a BPO service provider and market leader in its niche, was acquired as a first step. The company specialises in the management of rental and leasing goods. Gruppo MutuiOnline plans to acquire the rest of the company within the next few years. On the other hand, the remaining 49% shares of the price comparison subsidiary "7Pixel" were taken over. Last but

[2] A detailed description of Tucows' business model is included in the annual report 2016 and the first semi-annual report of 2017.

[3] A detailed description of the two divisions of Gruppo MutuiOnline is included in the annual report 2015.

not least, shortly before the end of the year, the acquisition of “Eagle & Wise”, a rating agency for banks, was announced.

Gruppo MutuiOnline remains one of the most impressive examples, demonstrating how a company’s own core business can be expanded systematically and consistently over a long period. MutuiOnline is now on the way to becoming a full-service provider to the Italian financial sector. In total, almost 60 million Euros were invested in 2018. Whoever knows the two founders Marco and Alessandro, knows that the chances for a positive value contribution to these investments are excellent.

The share price of **amaysim**[4] has had a terrible year. Operationally it has been a bit better than I expected after the price cuts. After the events in the Australian telecommunications market described in the summer half-year, there were some additional news. The network operators TPG Telecom and Vodafone Hutchinson Australia have merged, which is actually excellent news. After the quick departure of CEO Julian Ogrin, Peter O’Connell, one of the founders of amaysim, has switched from the Supervisory Board to the CEO chair. In this role, Peter initiated a review of the overall strategy and initiated a cost-cutting program. The effects will become visible in the coming quarters.

In the past year, the companies in the oil and gas sector (**NOW** and **National Oilwell Varco**)[5] displayed operational signs of stabilisation. Especially at NOW, it became apparent that the high operational leverage of the business model can also provide positive surprises in the event of a lasting recovery. Whether this short-term stabilisation will last long after the sharp and repeated slump in the price of oil since October 2018, will only become apparent in the coming quarters. I sincerely hope that the experience in the oil and gas sector can be described with a quote from André Kostolany: “*On the stock market you earn compensation for personal suffering, first comes the suffering, then the compensation*”. So far, in any case, the pain clearly outweighs the gain in this area.

The year 2019 and beyond

Since the price of the TGV Partners Fund has remained largely unchanged over the year, it means that while the profits of the companies have grown significantly, they have become cheaper in their valuation. How cheap? Unfortunately, there is no direct correlation between “cheap” and falling or rising prices on the stock exchange. Forecasting stock prices is not my job, but in recent months I have found more attractive ideas than the TGV has free funds available. A good sign. Above all, I find it a much more pleasant task to have to choose between “good” or “better” than to choose between “mediocre” or “ bad”.

It may well be that the falling stock prices all over the world are a portent of an economic slowdown. Who knows? As I stressed in the past, I am by no means afraid of a recession. Recessions, crises, Brexit, and lurid headlines are part of everyday market life. I rate the quality of our companies, their structural growth opportunities, and the people involved as so high-quality that they should be able to weather these occasional crises without endangering their existence.

[4] A detailed description of amaysim’s business model and development is included in the first semi-annual report of 2017 and the first semi-annual report of 2018.

[5] A detailed description and thoughts on the companies in the oil and gas sector are included in the annual report 2015 as well as the annual report 2017.

Investor meeting

The Investmentaktiengesellschaft für langfristige Investoren TGV will hold its annual investor meeting on Saturday, June 29, 2019, in Bonn-Bad Godesberg.

As a partner in the TGV, you will receive an invitation shortly. Since my first days with the Investmentaktiengesellschaft, the number of participants has grown every year. Especially for new partners, it is an excellent opportunity to get a personal impression of the people involved.

With this in mind, I wish you a happy new year and thank you for your continued trust.

Kindest regards from Bonn,

Mathias Saggau