ValueInvestor INSIGHT

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The Leading Authority on Value Investing

Rough Neighborhood

There are many broad-based macroeconomic reasons why share prices worldwide are under pressure. Matthew Fine explains why he's finding the U.K. to be one area where that's creating incremental investment opportunity.

One category of recurring opportunity often cited by value investors is when macroeconomic, geographic or industry-specific clouds dim a company's near-term prospects enough to open a gap between its share price and estimated intrinsic value. The more indiscriminate the selling, the greater the potential for case-by-case overreactions on which to capitalize.

Third Avenue Management's Matthew Fine suggests that the United Kingdom is fertile ground for bottom-up stock picking in an area with lots of top-down negativity. There's economic weakness exacerbated by rising inflation and interest rates. The war in Ukraine is wreaking havoc on regional energy supplies and prices. Brexit has proven more complicated than billed,

INVESTMENT SNAPSHOT

Ashmore Group
(London: ASHM)

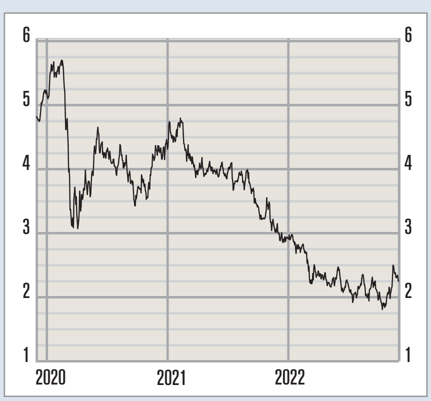
Business: London-based institutional investment manager with particular focus on fixed income securities in emerging markets.

Share Information
(@11/29/22, Exchange Rate: $1 = £0.84):

Price	**£2.25**
52-Week Range	£1.78 – £3.04
Dividend Yield	7.5%
Market Cap	£1.48 billion

Valuation Metrics (@11/29/22):

	ASHM	S&P 500
P/E (TTM)	16.7	19.1



Bottom Line: Matthew Fine believes the stock of this out-of-favor business in an out-of-favor market has minimal downside and upside that is well beyond its pre-Covid price of more than twice the current level.

S4 Capital
(London: SFOR)

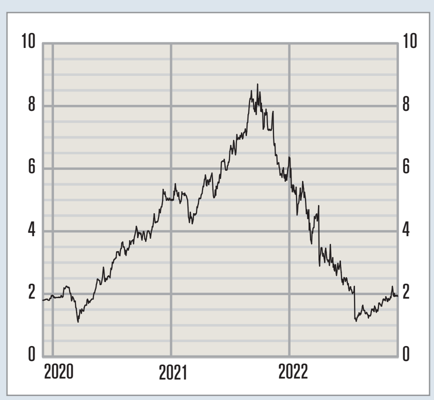
Business: Holding company, founded by Martin Sorrell, that provides digital advertising and marketing services worldwide.

Share Information
(@11/29/22, Exchange Rate: $1 = £0.84):

Price	**£1.92**
52-Week Range	£1.10 – £6.52
Dividend Yield	0.0%
Market Cap	£1.07 billion

Valuation Metrics (@11/29/22):

	SFOR	S&P 500
P/E (TTM)	n/a	19.1



Bottom Line: The company has taken shareholders on a rocky ride, but if its growth trajectory remains intact, Matthew Fine believes the shares within the next two to three years can trade at closer to £4.50.

easyJet
(London: EZJ)

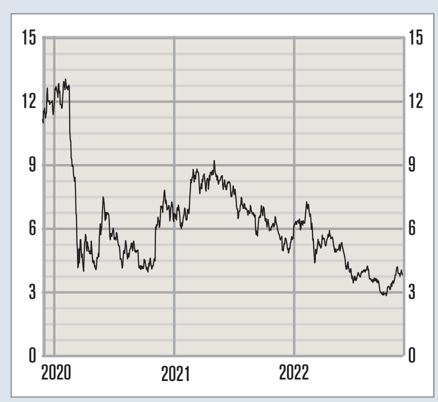
Business: Discount airline based in the United Kingdom that serves more than 900 routes to 150 airports throughout Europe.

Share Information
(@11/29/22, Exchange Rate: $1 = £0.84):

Price	**£3.83**
52-Week Range	£2.77 – £7.29
Dividend Yield	0.0%
Market Cap	£2.89 billion

Valuation Metrics (@11/29/22):

	EZJ	S&P 500
P/E (TTM)	n/a	19.1



Bottom Line: Nothing has been easy of late for this European discount airline, says Matthew Fine. At 6.5x enterprise value to what he considers the company's normalized EBITDAR, the stock would sell for £6.

Sources: Company reports, other publicly available information political dysfunction is rampant, and the British pound has only just moved off lows not seen in 35 years. “Our radar is trained to look for trouble,” Fine says. “That’s fairly easy to find at the moment in the U.K.” From zero earlier this year, the country's weight in his global portfolio is now above 10%.

His initial U.K. purchase in May was **Ashmore Group**, a London-based investment manager with around $55 billion in assets under management. The company’s specialty is fixed-income investing in emerging markets, an asset class that has endured outflows for years as investors have disproportionately favored dollar-denominated equity investments in the U.S. The pariah status of Russia, which makes up 4-5% of typical emerging-markets indexes, has only heightened fear around the asset class.

With headwinds galore, Ashmore’s stock has been relegated to the bargain bin, says Fine. In the mid £5s pre-Covid, the stock closed recently at £2.25, around 6.6x enterprise value to forward EBITDA and with what he considers a funded dividend yield of 7.5%. Cash and various seed investments account for nearly 50% of the company's £1.5 billion market cap, he says. Given the strength of the balance sheet and dividend payout, he considers the downside in the shares today to be minimal, with upside well beyond the pre-Covid price if emerging-markets investing returns to favor – as he expects – during his multi-year holding period.

One of the “growthiest” investments Fine has ever made is digital advertising and marketing firm **S4 Capital**, which has been built largely through acquisition by Martin Sorrell after his ignominious 2018 departure from WPP, the giant ad holding company he founded and ran for 33 years as CEO. S4 focuses exclusively on creating and executing digital-only advertising and marketing campaigns, the secular-tailwind side of the market that has helped fuel the company’s 25% annual revenue growth.

Shareholders have been on a ride, however. The stock took off after the onset of Covid – hitting a high of £8.70 in September 2021 – but has since crashed to earth. First, accounting errors related to revenue recognition for acquired companies caused a delay in reporting and ultimately a relatively modest restatement of results. Then a profit warning in July blamed on overzealous hiring further damaged the company's credibility and the stock took another leg down, falling below £1.15. At a recent £1.90, the stock trades at less than 10x forward EV/EBITDA, says Fine, for a business he thinks can continue over the medium term to maintain its 25% top-line growth. If he’s right about that growth and that management's integrity remains intact, at the 20x EV/EBITDA multiple he believes the business would deserve on his estimates two to three years out the stock would trade at closer to £4.50.

His latest U.K. purchase, discount airline **easyJet**, is surrounded by less controversy but has had its share of vexing industry headwinds. The company flies point-to-point routes mostly to primary European airports, a business that has been buffeted by a slow recovery from the pandemic, high fuel costs, terrible airport congestion and staffing issues over the summer, and a declining European economic outlook. Its shares, now at £3.80, are off 47% from their February high.

“The probability is in our favor that things won't be this hard forever,” says Fine, who notes that easyJet's passenger traffic has recently hit 90% of pre-Covid levels. He's comfortable being patient for that recovery to play out because of easyJet's strong asset position, exemplified by his estimate that its owned aircraft, net of all debt, are worth roughly 15% more than the company's current market value. Putting what he considers a reasonable 6.5x multiple on his estimate of normalized EBITDAR (earnings before interest, taxes, depreciation, amortization and rental costs) on today’s asset base, he believes the shares are worth at least £6. VII

P/E TTM: The price-to-earnings (P/E) ratio is the ratio for valuing a company that measures its current share price relative to its per-share earnings over the trailing twelve-months.

Dividend Yield: The dividend yield, expressed as a percentage, is a financial ratio (dividend/price) that shows how much a company pays out in dividends each year relative to its stock price.

Enterprise Value to forward EBITDA: EV/EBITDA is a ratio that compares a company's Enterprise Value (EV) to its Earnings Before Interest, Taxes, Depreciation & Amortization (EBITDA). The EV/EBITDA ratio is commonly used as a valuation metric to compare the relative value of different businesses.

S&P 500 Index - The S&P 500 Index, or Standard & Poor's 500 Index, is a market-capitalization-weighted index of 500 leading publicly traded companies in the U.S.

FUND RISKS: Risks that could negatively impact returns include: fluctuations in currencies versus the US dollar, political/social/economic instability in foreign countries where the Fund invests, lack of diversification, and adverse general market conditions. For a full disclosure of principal investment risks, please refer to the Fund's Prospectus.

Past performance does not guarantee future results.

Please see top Ten Holdings here.

Earnings growth is not a forecast of the Fund's future performance.

Holdings and dividends are subject to change.

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