HORODS

JANUARY 2020

Dear co-investor,

We end a year that has been marked, as you know, by (very) high volatility in equity markets, caused by global political and economic uncertainties. As we have stressed in previous letters, this environment has led investors to seek out companies with more stable businesses or those that are currently more popular. The result is that these companies are becoming more and more expensive relative to smaller or more cyclical businesses.

This trend has slightly reversed in the last quarter of 2019, giving a boost to those who, like us, invest in stocks with a high margin of safety and which are precisely the least popular in this context of uncertainty. Perhaps the progress made in the trade negotiations between the United States and China, or the likely Brexit outcome in the United Kingdom, explains this recent change in investors' sentiment.

However, valuation divergences are still very pronounced, and we remain convinced that our portfolio is best suited to generate attractive and sustainable returns *over the long term*, as evidenced by its high upside potential. We are aware that it is sometimes difficult to deal with this volatility. That is why we are very grateful for your confidence. We are sure that patience will eventually pay off.

My best wishes for 2020.

Yours sincerely,

Javier Ruiz, CFA
Chief Investment Officer
Horos Asset Management

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The importance of mental flexibility

An uncertain and doubting mind leads to fresh world visions and the possibility of new and ever-changing realities.
— Michael Shermer

In 2002, Donald Rumsfeld, the former Secretary of Defense under President George W. Bush, in a Department of Defense news briefing where he was questioned about the Iraq War and the lack of evidence regarding the sale of Iraqi weapons of mass destruction to terrorist groups, said the following:

> *Reports that say that something hasn't happened are always interesting to me, because as we know, there are* ***known knowns****; there are things we know we know. We also know there are* ***known unknowns****; that is to say we know there are some things we do not know. But there are also* ***unknown unknowns****—the ones we don't know we don't know. And if one looks throughout the history of our country and other free countries, it is the latter category that tend to be the difficult ones.* [1]

Although, at the time, this kind of gibberish sounded ridiculous, especially to critics of the Bush Administration, the reality is that this terminology became increasingly popular, mainly in the business strategy field, as it presented an interesting decision matrix. In the investment community, it was Nassim N. Taleb, whom we have already mentioned on previous occasions, who gave it the definitive boost with his book *The Black Swan*. Specifically, and without going too deeply into the concept, Taleb defined a **black swan** as that highly unlikely event that falls into the category of unknown unknowns:

> *A gray swan concerns modelable extreme events,* ***a black swan is about unknown unknowns****.* [2]

We value investors usually say that, when choosing where to look for investment opportunities, we should limit ourselves to only those industries and businesses that are within our **circle of competence**, that is, those that we understand well and can reasonably foresee their prospects in the near future. Or, turning the reasoning around, if one is not able to foresee the situation of a company and its industry in a few years from now, then it is better to avoid investing there. If we

[1] Bold added for emphasis. DoD News Briefing - Secretary Rumsfeld and Gen. Myers (February 12, 2002).
[2] Bold added for emphasis. Taleb, Nassim N. (2008): *The Black Swan, The Impact of the Highly Improbable*. Great Britain: Penguin Books.

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use the classic fishing analogy, there will be rivers and types of fish where we will have an edge and our skills will make a difference. However, on many instances, we will have to assume that **not all rivers and not all fish are made for us**.

Based on what we have discussed so far, an alternative way of interpreting our circle of competence could be to think that it is comprised of what we know we know, that is, by our *known knowns*. While what we know that we do not know (*known unknowns*) and what we do not know that we do not know (*unknown unknowns*) would be outside our circle of competence.

In an ideal world we would know with absolute certainty what our true knowledge of things is, and we would be able to perfectly delimit this circle (what we know we know). However, reality rarely fits what we would like it to be. For this reason, it is essential to be intellectually as honest as possible, so as not to fall into that dangerous mental trap called the **illusion of knowledge**. In this way, we will avoid investing in situations in which we are unable to delimit the risks, no matter how hard we try:

> *If you play games where other people have the aptitudes and you don't, you're going to lose. (...) You have to figure out where you've got an edge. And you've got to play within your own circle of competence.*[3]

However, although it is often stressed (justifiably) how necessary it is to try not to go beyond the boundaries of our true circle of competence, we cannot fall into complacency thinking that the world does not operate and evolve outside it. This way of acting will only make us more ignorant, because the unknown unknowns will continue to increase as time goes by and, whether we like it or not, will affect what we think we know, **leading us to fall, precisely, into that illusion of knowledge we try to avoid**. Technology, or more precisely technological advances, are a good example of all this.

As those who have been following us for some time know, we have been stressing for years the importance of taking technological advances into account in the process of analysing industries and companies. This approach has allowed us, in our humble opinion, to strengthen our circle of competence, increasing our conviction about what we believe we know and, consequently, investing (or avoiding) in those situations in which we are more convinced about the impact of technology. Specifically, our analysis tries to estimate which players (known as "disruptors", because they alter the traditional functioning of an industry) will benefit the most

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[3] Quote from "Understanding your Circle of Competence: How Warren Buffett Avoids Problems" (Farnam Street Blog).

from these developments, which ones are still resilient to the technological challenge and, finally, which companies should be avoided, because their business is at risk from this paradigm shift.

It has been a long time since the mantra of not investing in technology companies, traditionally rooted in value investors, ceased to have its *raison d'être*. The dean of this investment philosophy and the main historical critic of investing in technology, Warren Buffett, holds Apple as the main publicly listed company in his Berkshire Hathaway holding firm and, a few years ago, both he and his partner Charlie Munger admitted the big mistake they made by not investing in Google:

> *We could see in our own operations how well that Google advertising was working and we just sat there sucking our thumbs, so we are ashamed.*[4]

For this reason, our job as the fund managers of Horos is to try to build a portfolio of businesses that, in addition to meeting our investment principles, are not being significantly affected by technological advances, as well as by companies that are benefiting from them. In the first category, without going into the particularities of each case, we could include our investments in commodities, real estate or financial businesses. In the second category, we have names such as Alphabet, Naspers and Baidu. Being shareholders in the latter category has enabled us, among other things, to understand the Chinese technology ecosystem and its potential advantages over the West's. It has also helped us to invest in some companies and discard others, depending on the impact of these technology giants on their industries. We will dedicate the rest of the letter to the Chinese case, as it is, in our opinion, very enlightening.

The new Space Race

To people here, AlphaGo's victories were both a challenge and an inspiration. They turned into China's "Sputnik Moment" for artificial intelligence.
— Kai-Fu Lee

On October 4, 1957, the former Soviet Union launched Sputnik 1, the first artificial satellite in our history, into orbit. That moment shook American society up, which until then was convinced of its technological and space superiority at the global level. This event ended up being called the "**Sputnik Moment**", as it awakened

[4] Roche, Julia (May 4, 2019). "Why Warren Buffett feels worse about missing Google than Amazon." Yahoo Finance.

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Americans from their lethargy, giving a strong boost to the Space Race, whose culmination would be the arrival of Neil Armstrong on the Moon and the confirmation of the United States as the global leader.

Sixty years later, in May 2017, **AlphaGo** (an artificial intelligence computer program developed by DeepMind, a subsidiary of Alphabet) beat Ke Jie, the best Go player in the world.[5] This ancient game, much older than chess, has a board that contains a possible combination of moves superior to the atoms of the universe, which made it *impossible* for a machine to beat a human. Well, the impossible happened and was viewed by almost 300 million Chinese citizens, great fans of this game, generating a kind of "Sputnik Moment" for the country. Shortly afterwards, **the Chinese government announced its goal for 2030, to turn the country into the world's greatest artificial intelligence power**.[6]

You are probably among those who think that this is an overly ambitious, not to say insane, goal. Today, the United States is the world's greatest technological power, and obviously its leadership in the development of artificial intelligence is no exception. Companies like Amazon, Google, Microsoft or Facebook guarantee that this will continue in the future, right? Or does the Chinese government's plan have more substance than we might initially think? To answer this question we have to understand, first, where we are in terms of the development of artificial intelligence.

According to Kai-Fu Lee, one of the world's leading experts on artificial intelligence and author of the book *AI Superpowers: China, Silicon Valley and the New World Order*, artificial intelligence is entering what he calls the **age of implementation**, after many years in the age of discovery of new capabilities. The latter one was the exclusive focus of all the development of artificial intelligence (its "creation"), so the essential ingredient for its mastery was highly specialized human capital. Since the best engineers and programmers were primarily concentrated in the United States, this country has been the undisputed leader of this era. However, in the current age in which we are entering, human capital, although still relevant, will no longer be so critical. We are entering a phase in which the main goal is to implement these artificial intelligence developments and make them scalable. For this reason, computing power and, particularly, so-called **big data** are the drivers that will make the most difference in improving the algorithms. This is precisely one of the reasons why China can tilt the balance in its favor against the United States, as we will see later on.

[5] A year earlier, in March 2016, AlphaGo also beat South Korean Lee Se-dol, one of the best Go players of recent times. The duel was immortalized in Netflix's excellent documentary entitled *AlphaGo*.
[6] "Notice of the State Council Issuing the New Generation of Artificial Intelligence Development Plan." State Council Document [2017] No. 35.

On the other hand, as we mentioned above, the Chinese government aims to achieve world leadership in artificial intelligence. Thus, it has set the country's entire machinery in motion towards this goal, encouraging local authorities in all provinces to facilitate its implementation, through measures such as tax incentives, rental subsidies for newly created companies, favourable financing or, in more extreme cases, even evacuating an entire neighbourhood to another destination in order to relocate the city's technology centre. Possibly no other country has such an aggressive and far-reaching incentive plan for its implementation.

Finally, **the peculiarities of the Chinese society with regard to personal data processing and intellectual property, as well as the massive adoption of mobile devices, generate a unique virtuous circle**. In the next sections we will see why.

The Wild East[7]

Word of advice, kid. This may be the Wild West down here, but you ain't a cowboy. You're not even a boy in a cowboy suit.
— Caitlin Kittredge

Contrary to what we may still think in the West, China has long since overcome that phase in which it copied, with greater or lesser fortune, the business models of Western companies. A phase, however, that was inevitable and necessary for the Asian giant. Just think that, at the end of the 1990s, the United States had an internet penetration of 30% of its population, when in China it was practically non-existent. As China continued its process of industrialisation and development, the country's entrepreneurs began to look for models that had worked in other countries, to try to implement them (literally) in their image and likeness.

An eloquent example can be found in the figure of **Wang Ching**, who was given the significant nickname of "The Cloner". Wang copied absolutely everything from Facebook and Twitter to launch Xiaonei (later named as Renren) and Fanfou. In 2008, Renren was the leading social platform in the Asian country. However, its position was threatened by the entry of a new competitor called Kaixin001, whose platform integrated video games for the first time. In spite of this, Kaixin001 had a problem that turned out to be its downfall. The Kaixin web domain was already registered and, as it was a company with few resources, it did not have the means

[7] The following sections are largely based on Lee, Kai-Fu (2018): *AI-Superpowers: China, Silicon Valley and the New World Order*, Boston: Houghton Mifflin Harcourt.

to acquire it, so it had to use the peculiar name of Kaixin001. Renren, the country's undisputed leader and much stronger financially, acquired the Kaixin domain. As if that were not enough, he copied exactly the interface of Kaixin001 and, displaying his ruthless competitiveness, put the phrase "the real Kaixin network" on the new website. Chinese users did not know which was which and began to sign up for this new website, thus benefiting Renren. Finally, Renren merged with the *new* Kaixin. Obviously, Kaixin001 denounced the situation, but the damage was already done. Although Renren and Fanfou eventually became very popular in the country, the rise of mobile devices and the intervention of the Chinese government put an end to both businesses.

It is important to understand that this copying era laid the foundation for entrepreneurial development and human capital accumulation, to the extent that **Chinese entrepreneurs began to improve on the Western business models and products, innovating and adapting them to their society's needs**. These types of innovation and adaptation are fed by a ruthless competitive environment, as we have just seen, in which intellectual property is not respected and groundless copying and smearing of competitors is not frowned upon. This may explain, in part, how leading companies in the West, such as Uber, eBay or Groupon, had to give up on their goals of gaining a foothold in the Chinese market. While the business culture of American start-ups has always focused on implementing a new concept or meeting some kind of idealistic target, the Chinese business culture encourages making money, almost at any cost.

Again, the figure of Wang Ching can serve as an example of this great transition from clone entrepreneurs to innovative entrepreneurs. In 2010, Wang founded the company **Meituan** with a business model very similar to that of Groupon (coupon platform). However, especially since its merger with Dianping, Meituan's business has been developing in the competitive Chinese ecosystem, to become a platform with a multitude of services. Today, the Meituan application allows its users to, for example, book hotels, apartments, restaurants, buy movie tickets, pay in stores or order food at home. In short, a rich ecosystem designed for its users to purchase all these services with and from Meituan. The end result of this development? The current market cap of Meituan is eighty billion dollars, while that of Groupon is below two billion and its stock price is near all-time lows.

An endless manna of data

It is a capital mistake to theorize before one has data.
— Sherlock Holmes

As we discussed above, one of the biggest advantages for China's future vis-à-vis the United States can be found in the huge volume of data that Chinese companies (and the government) have access to. How is it possible for China to be ahead of the West, when it has always been lagging behind in internet adoption? The explanation for this can be found in the technological leap that took place in the country with the rise of smartphones (today's mobile phones that have an endless number of features). Many Chinese citizens experienced the internet for the first time through their mobile phones, as computers were too expensive to purchase. This created very different needs around the mobile phone. **Instead of a phone with internet access similar to a computer, the Chinese wanted a device that would help them in their daily needs as they moved around the city**.

All of this has resulted, on the one hand, in China having the largest number of internet users in the world (more than the United States and Europe combined), which gives it a ***quantity-based* data advantage**. On the other hand, what Chinese users do on the Internet is more relevant than in the West, where the internet is mostly used to click on ads or give "likes". In China, however, it is used massively for real-life situations, which gives them a ***quality-based* data advantage**. This quantity and quality of data has allowed the development of an alternative, and in many cases even superior, technological business ecosystem to that of the West. Companies like Tencent, Alibaba, Baidu, JD.com, Pinduoduo, iQiyi, Tencent Music, Meituan, Ctrip, Didi or Bytedance, to name a few, have nothing to envy (sometimes the opposite is true) to their American counterparts.

For example, Tencent, Alibaba, Baidu or Meituan, as we saw before, have created the **Super App** model: a huge ecosystem around some of their applications, which allows the user to purchase any service or consume products without leaving the application. Facebook, seeing the opportunity, has started recently to develop some of these features in their mobile apps. Another example can be found in the so-called **Social E-Commerce**. In this case, applications from Taobao (Alibaba) or Pinduoduo combine videos about products with the social network concept, increasing their sales very significantly. Well, Amazon launched Amazon Live in 2019 following a very similar concept and YouTube expects to develop the same idea through YouTube Shopping. Finally, China has popularized around the world the concept of **short-lived social video** with the application of TikTok (ByteDance). Platforms such as Snapchat or Facebook are also trying to imitate this concept, to protect themselves against the unexpected global appearance of this Chinese application.

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However, we would like to end this letter by focusing on the company that we think has the best data ecosystem in China and of which we are shareholders through Naspers: **Tencent Holdings**.

A Super App to bring them all together

One Ring to rule them all, One Ring to find them, One Ring to bring them all and in the darkness bind them.
— Gandalf (The Lord of the Rings)

Can you imagine a company that includes, among others, businesses such as EA Sports or Nintendo (video games), Netflix (video streaming service), Spotify (music streaming service and online advertising), Facebook (online advertising and social networking), YouTube (online advertising and video-sharing platform), Google News (news), PayPal or Visa (electronic, online and physical payment services) and Amazon Web Services (cloud services)? Can you imagine this company making strategic investments in leading and disruptive companies in all of these industries globally? Can you imagine such a company, with all of the above services being coordinated through a (very) advanced version of Whatsapp (social chat) that also allows for a host of additional features to the businesses just mentioned? Well, this company is **Tencent**. In order to understand how **Tencent** has managed to create this unique ecosystem, it is essential to explain what a platform is and why it can become an outstanding business.

A platform is a business that enables value-creating interactions between third-party producers and consumers. [8] To put it more simply, it is a digital place where (usually commercial) exchanges between platform users are enabled. For example, Booking.com or Airbnb allow their users, through their platform, to search and book accommodations that have been listed on these portals. In return for enabling these transactions, Booking.com and Airbnb charge a commission. Therefore, these companies offer accommodation services without owning any property, i.e. to a certain extent, they benefit from the capital investments (property, in this case) made by other companies. This is why platforms can become very profitable companies:

[8] Parker, Geoffrey G., Van Alstyne, Marshall W. and Choudary, Sangeet Paul (2016): *Platform Revolution: How networked markets are transforming the economy and how to make them work for you*. New York: W.W. Norton & Company, Inc.

> *The best business is a* ***royalty*** *on the growth of others,* ***requiring little capital*** *itself.*[9]

This type of business has experienced a major growth explosion in recent years, thanks to the massive adoption of the internet and mobile phones, with platforms emerging wherever they can appear. Today, most of the world's largest companies are, to a greater or lesser extent, platforms that benefit from this trend. Amazon, Alphabet (Google), Microsoft or Facebook are examples known to all. Now, if they are such profitable businesses, how is it possible that not many competitors will arise to try to get a piece of that delicious pie? Because network effects, once reached a certain scale, make this "attack" by the competition unfeasible.

To understand the concept of **network effect**, think about how a highly contagious disease is spread. The infected person initially passes it on to very few people, but these people know others and the process, after reaching a **tipping point**, accelerates exponentially until it becomes an epidemic. Despite the negative connotations of the analogy, this is essentially a network effect: a kind of epidemic that spreads through society and for which there is no cure. Going back to the example of Booking.com and Airbnb, the millions of users that use those platforms (epidemic) ensure that it is more attractive for users and accommodation owners to use these web portals rather than smaller or less successful alternatives. **The more users and accommodation supply increase, the more attractive the platforms will be to all users and the more powerful their network effect will be.** This is the reason why they are so difficult to attack:

> *I'm not sure that I would regard one type of moat as stronger than another, with the possible exception of a network effect.*[10]

In short, platforms are businesses that need little capital to operate, which is why they are highly profitable, and are protected by powerful network effects. Why have we delved into these concepts? Because **Tencent** is a business that has one of the most powerful platforms in the world, which in turn feeds (and is fed by) other platforms: Weixin/WeChat (hereinafter WeChat).

WeChat is the fifth most widely used application in the world, with over 1.15 billion users. To understand its magnitude, a few numbers are enough, such as that in 2018 Chinese citizens sent more than 45 billion messages *per day* through this app,

[9] Bold added for emphasis. Quote from Huber, John (2019): "Warren Buffett 1997 Email Exchange on Microsoft."

[10] Quote from "Exclusive Interview with Pat Dorsey on Moats" by Manual of Ideas (July 2012). Pat Dorsey is considered one of the leading experts in the analysis of competitive advantages of businesses. I recommend his book *The Little Book That Builds Wealth*.

or that WeChat accounts for more than a third of total mobile data traffic in China. How has WeChat achieved such dizzying numbers? By acting as the first and possibly the biggest and most important **Super App**. The WeChat user can do everything imaginable through this application (you can check the very different businesses we mentioned at the beginning of this section to get a vague idea of what this ecosystem actually is):

> *WeChat is a sort of digital Swiss Army Knife for modern life.*[11]

This vast ecosystem also benefits from Tencent's strategic investments in companies in such diverse industries as video games (Ubisoft, Activision Blizzard, Epic Games or Bluehole, among others), music (Spotify), e-commerce (JD.com or Pinduoduo), electric vehicles (Tesla or Nio), social networks (Snapchat), transportation (Didi), internet search engines (Sogou) or the Meituan platform, mentioned above.

All this allows Tencent to have one of the largest and growing databases in the world and to know, in real time, virtually everything that its users do every day, which gives it an extraordinary ability to make money. In short, Tencent has a large number of very profitable platforms (or on the way to becoming so), fed by its network effect and by the platform that brings them together, feeds and strengthens them: WeChat. This is why Tencent is so difficult to attack (in a significant way) by its competitors and why we think it is such a high-quality business, of which we are shareholders through Naspers.[12]

Current Affairs

As for the most relevant news about Horos, this quarter I would like to highlight our **First Annual Conference**, undoubtedly the event we are most proud of this year. We tried to explain the present market context and why we think we can benefit from it with our current fund portfolios, giving specific examples of several of our investments. We encourage you to watch the video (see **here**), as well as a subsequent video in which Alejandro and I answer some of the questions that were left unanswered (see **here**).

On the other hand, Rodrigo Blanco, one of the members of our investor relations team, recorded the following video (see **here**) to explain the importance of

[11] Lee, Kai-Fu (2018): ibid.
[12] If you would like to learn more about our investment in Tencent, we encourage you to view the talk I gave at Value School in 2018 (see here).

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investing in a **pension plan**, something that, by the way, should never be delayed until the end of the year.

Finally, continuing with our commitment to transparency, we have uploaded to our YouTube channel a video (see **here**) by Alejandro explaining our investment thesis in **Asia Standard International**, one of our main investments in the international portfolio.

Horos Value Iberia

The fund can invest in stocks listed in Portugal and Spain. In addition, it can invest up to 10% in Spanish or Portuguese companies listed on other markets.

Horos Value Iberia returned 12.9% in the fourth quarter, compared to its benchmark index return of 4.7%. Since its inception on the 21st of May of 2018 to 31st of December of 2019, the fund's cumulative return has been -7.3%. In the same period, its benchmark returned -0.3%. The results achieved in such a short period of time are merely anecdotal and should be considered as such. As an indication of the importance of a long-term investment horizon (remember that the minimum recommended investment period for our products is five years), the annualised return obtained by an investor who has invested along with this portfolio management team since its inception would be 12.3% versus 7.3% of its benchmark (for more information, you can consult the annex in the final part of this document).

In this quarter, the largest positive attributors to performance were **Ercros**, **Aperam** and **Sonae Capital**. As for Ercros and Aperam, the stock market recovery of companies with more cyclical business, following progress in trade negotiations between the United States and China, as well as the outlook for a potential earnings bottom, explain the recent upturn. With regard to Sonae Capital, we do not find any noteworthy reasons that can explain this positive performance.

On the negative side, the major detractors from the Fund's return were **Renta Corporación** and **Sonaecom**. In both cases, we think it is possible that the decline is due to money outflows from some of its institutional shareholders, probably as a result of increased liquidity requirements by the Spanish regulator or investors exiting their funds.

The fund's portfolio had one entry (**Inmobiliaria del Sur**) and one exit (**Bolsas y Mercados Españoles**) during the quarter.

Inmobiliaria del Sur is a property development and management company with a family shareholding (owns more than 65% of the shares) that has been in business for 75 years. This shareholding structure may explain its conservative approach to managing the development business, which, together with the support of the property management business, explains why Inmobiliaria del Sur was the only

publicly listed developer that did not face any debt restructuring during the great real estate crisis of 2008. We analyzed the company in 2015 and visited its main assets in Sevilla and surroundings in 2016, although we could not invest due to the illiquidity of the stock and the (understandable) refusal of the company to sell shares at the very low prices at which it was trading at that time (6.5 euros per share). A new entry opportunity has opened up this quarter, so we have taken advantage of it to invest in a business that meets all our investment principles. We believe that, as the company executes its growth plan, the number of institutional investors will increase and the huge discount at which the company is currently trading will gradually close.

Regarding the exit of **Bolsas y Mercados Españoles** (BME), it followed a takeover bid by the SIX Group (Swiss Stock Exchange) at 34 euros per share, which left the stock without any upside. We took advantage of this to liquidate our investment and increase our weight to other alternatives in the portfolio with high upside potential, such as **Meliá Hoteles**, **Catalana Occidente** or **Elecnor**.

At the end of the quarter, **the *theoretical* upside potential of the fund for the next three years is around 75%**, which would be equivalent to an annualised return of 20.5%. For the calculation of this upside potential, we performed an individual analysis of each holding that makes up the portfolio. These theoretical returns are no guarantee that the fund will perform well over the next three years, but they do give an idea of how attractive the current time is for investing in Horos Value Iberia.

Portfolio Structure

At the end of December, the portfolio of Horos Value Iberia comprised 23 holdings and was concentrated in one major theme. Nearly **78%** of the invested part of the portfolio is composed of companies that we have known for years that are managed by **families with a significant presence in the shareholding** (which guarantees an alignment of interests with shareholders).

Horos Value Iberia also invests in **Horos Value Internacional (5.3%)**. In this way, the upside potential of the Iberian fund is increased, enhancing the quality of the portfolio and generating greater value for our investors in the long-term. Of course, NO commission is charged on that percentage invested in the house funds.

Lastly, the **cash position** of the fund at the end of the quarter was close to **5%.**

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Top Holdings

Meliá Hotels International (7.9%, family-owned): hotel group with a presence in over 40 countries, of which the Escarrer family controls 52% and has been a shareholder for over 60 years. The company is the leading hotel chain in Latin America and the Caribbean and is the largest global player in resorts and “bleisure” (a combination of business and leisure). Meliá's objective is to migrate to an asset-light business model, which focusses on the management of hotels without owning them. Currently, hotel management accounts for nearly 30% of EBITDA and they expect to reach 50% in seven years. The interesting thing about this investment lies in the valuation of its hotel assets, much higher than its current market capitalisation. This fact allows us to purchase the hotel management business and its future potential contribution to the company *for free*.

Ercros (6.3%, other): company overlooked by analysts due to the complicated situation it experienced a few years ago. It is an industrial group dedicated to the production of chlorine derivatives (necessary, for example, for the manufacture of PVC), intermediate chemicals (formaldehydes, glues and resins, etc.) and pharmaceuticals (active ingredients and generic drugs). After almost ten years of continuous decline in demand for PVC, the capacity shut-downs of the sector in recent years, together with the additional restriction of supply that is taking place, following the ban by the European regulator on the use of mercury technology in chlorine production processes, gives us reasonable expectations for a good performance of this industry in the coming years.

Semapa (6.2%, family-owned): Portuguese investment vehicle managed by the Queiroz family, which controls close to 70% of the paper company Navigator and 100% of the cement company Secil and the animal by-products treatment company ETSA. We believe that the holding company is trading at an excessive discount compared to the valuation of its assets.

Sonae Capital (5.5%, family-owned): it is a Portuguese investment vehicle managed by the Azevedo family, which owns real estate assets and operates in the tourism, energy and industrial sectors. The company seeks to invest in Portuguese niche companies that may have export potential. We believe that the value for the sum of parts of the different businesses is substantially higher than Sonae's current market cap.

Catalana Occidente (5.5%, family-owned): this insurance company has an excellent history of creating value for its shareholders, thanks to the attractive acquisitions they make on a regular basis. Its management team manages the business very conservatively, operating with combined ratios lower than those of the industry, as well as of the balance sheet, and always has a significant excess of reserves. We believe that the current price at which the company trades do not reflect the profitability of the business or its good capital allocation policy.

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Horos Value Internacional

Our international portfolio can invest without geographical restrictions in most of the world's stock exchanges, including the Iberian market. Therefore, Horos Value Internacional includes the best investment ideas that this portfolio management team currently finds available.

Horos Value Internacional returned 11.9% in the fourth quarter, compared to its benchmark index return of 5.8%. Since its inception on the 21st of May 2018 to 31st of December of 2019, the fund's return has been -10.1%. In the same period, its benchmark returned 17.9%. The results achieved in such a short period of time are merely anecdotal and should be considered as such. As an indication of the importance of a long-term investment horizon (remember that the minimum recommended investment period for our products is five years), the annualised return obtained by an investor who has invested along with this portfolio management team since its inception would be 11.0% versus 12.4% of its benchmark (for more information, you can consult the annex in the final part of this document).

In this period, the largest positive attributors to performance were the holdings that have contributed most positively to the fund's portfolio are **Aperam**, **Teekay Corp.** and **Clear Media**.

Regarding **Aperam**, the stock market recovery of companies with more cyclical business, following progress in trade negotiations between the United States and China, as well as the outlook for a potential earnings bottom, explain the recent upturn.

Teekay Corp., besides benefiting from these same factors, saw the value of its subsidiary Teekay Tankers surge on the stock market thanks to the industry's skyrocketing freight rates, given the bottleneck that its sector experienced in recent months. Additionally, the good performance of its subsidiary Teekay LNG (with the announcement of a dividend increase) and the extension of the contract of one of its FPSO (vessels used for the production, processing and storage of oil and gas) also made a positive contribution. In addition, the company celebrated an Investor Day event in November, which helped to provide more information about its businesses to the market and anticipated a likely future change in the IDRs

(additional dividend distribution rights) held by the parent company on its Teekay LNG subsidiary.

Finally, **Clear Media**, the Chinese leader in bus shelter advertising, gained 80% since November, after communicating the possibility that its controlling shareholder, the American company Clear Channel, which is in a weak financial situation, is considering getting rid of its 50% stake in the company. This sharp rise in Clear Media's share price highlights two things. On one hand, the inefficiencies of many listed companies in Hong Kong, where the real value of the business is much higher than its stock market value. And on the other hand, the speed at which these inefficiencies can start to close down, if a catalyst appears.

On the negative side, the major detractors from the Fund's return were the following companies stand out: **Shelf Drilling**, **Renta Corporación** and **Uranium Participation Corp**. While the latter has declined somewhat due to the slight fall in the uranium price, we find no fundamental reasons to explain the performance of the former two. In fact, in the case of Shelf Drilling, the company's recent developments (acquisition of new rigs at very attractive prices, new contracts and extension of some existing ones) further reinforce our investment thesis.

The international portfolio added three new names (**Semapa**, **Warrior Met Coal** and **Tai Cheung Holdings**) and did not exit any position in the period.

Semapa is a Portuguese investment vehicle managed by the Queiroz family, which controls close to 70% of the paper company Navigator and 100% of the cement company Secil and the animal by-products treatment company ETSA. Semapa has been present in our Iberian portfolio for a long time and we believe that, at current prices, an excellent opportunity has arisen to add it to our international portfolio, as the holding company is trading at an excessive discount compared to the valuation of its assets.

Warrior Met Coal is a United States metallurgical coal producer. Warrior exports 100% of this type of coal, which is necessary for the manufacture of steel in blast furnaces. In our opinion, metallurgical coal does not suffer, so intensely, from dynamics that are very difficult to foresee and that today put pressure on the thermal coal sector. Without going into detail, examples could be the impact of political pressure and interest groups to abandon this source of energy, or the growing relevance of ESG (Environmental, Social and Governance) investment criteria in the portfolios of more and more asset managers. As for the industry fundamentals, some global growth in demand for metallurgical coal is expected in the coming years as countries in Asia and South America continue to industrialise.

Warrior has very high-quality coal (close to the best standards of Australian benchmark coal), which allows it to benefit from the growth of these markets. Finally, this is a debt-free company, with a variable cost structure that protects it from tougher environments, an aggressive historical policy of shareholder remuneration (more than 100% of its stock market value returned over two years) and trading at less than 4x its current cash flow generation, given the current price of metallurgical coal.

As for **Tai Cheung Holdings**, this is a property development company specialising in luxury residential properties with assets in Hong Kong and the United States. In addition, Tai Cheung owns 35% of the Sheraton Hotel in Hong Kong. This is a family business, in which the management team controls around 50% of the shares, which clearly aligns its interests with those of the rest of its shareholders. This translates into very conservative management of the balance sheet (no debt) and an attractive policy of shareholder remuneration, with a growing and sustainable dividend over time (today the dividend yield is close to 6%). Lastly, we believe that the company's relative illiquidity, as well as the current challenging socioeconomic situation in Hong Kong, contribute to Tai Cheung's trading at around 70% discount to the value of its assets.

On the other hand, we want to highlight the weight reductions, due to lower upside potential, in companies such as **Clear Media**, **AerCap** or **LSL Property Services**. We have used these proceeds to increase the portfolio weight in companies that underperformed during the period, such as **Naspers** or **Qiwi**.

At the end of the quarter, **the *theoretical* upside potential of the international portfolio for the next three years is around 135%**, which would be equivalent to an annualised return of 32.9%. For the calculation of this upside potential, we performed an individual analysis of each holding that makes up the portfolio. These theoretical returns are no guarantee that the fund will perform well over the next three years, but they do give an idea of how attractive the current time is for investing in Horos Value Internacional.

Portfolio Structure

The portfolio is made up of 39 holdings and four major themes that account for the bulk of it. The main one comprises **commodity-related companies (30%)**, especially uranium, stainless steel and oil. Another important theme is the one that includes **overlooked emerging market stocks (22%)**, mainly Asian companies that are underfollowed by the investment community. The investment in **technological**

platforms (12%) with a strong network effect that are still trading at very attractive prices, as well as in **UK companies (8%)** impacted by Brexit fears, are the two other major investment themes in the portfolio.

Finally, the **cash position** of the portfolio at the end of the quarter was around **3.9%**.

Top Holdings

Uranium Participation Corporation (4.8%, commodities): investment vehicle that buys and stores uranium for later sale. Given our positive outlook for uranium prices and the limited cost structure of this vehicle, we have decided to concentrate our investment in this type of company (we are also shareholders in Yellow Cake, a similar vehicle listed in London) and renounce, at these prices, exposure via mining companies, where we would have to assume a greater risk of loss in an adverse scenario, as well as operational risks linked to the management and development of projects and mines.

Keck Seng Investments (4.7%, overlooked emerging market company): a Hong Kong family company founded in the early 1940s by the Ho family, owner of 75% of the vehicle, so its interests are aligned with those of its shareholders. The holding company specialises in the ownership and management of hotels in the United States, China, Japan, Vietnam and Canada. Keck Seng also has an important residential portfolio in Macao that we expect will benefit from the recent opening of the bridge that connects Hong Kong with this city. The poor liquidity of the share or the fact that the assets are valued at acquisition cost on the balance sheet have contributed to a market inefficiency, which in our opinion is unjustified.

Aperam (4.2%, family-owned): one of the world's leading stainless-steel producers, with strong exposure to Europe and Latin America. After a couple of years of good stock performance, as a result of the rationalisation of the sector's supply and the anti-dumping measures imposed by Europe against Asian producers, the impact of US President Trump's tariffs on this metal have, in our opinion, had an excessively negative impact on the stock.

Meliá Hotels International (4.1%, family-owned): hotel group with a presence in over 40 countries, of which the Escarrer family controls 52% and has been a shareholder for over 60 years. The company is the leading hotel chain in Latin America and the Caribbean and is the largest global player in resorts and “bleisure” (a combination of business and leisure). Meliá's objective is to migrate to an asset-

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light business model, which focusses on the management of hotels without owning them. Currently, hotel management accounts for nearly 30% of EBITDA and they expect to reach 50% in seven years. The interesting thing about this investment lies in the valuation of its hotel assets, much higher than its current market capitalisation. This fact allows us to purchase the hotel management business and its future potential contribution to the company *for free*.

Asia Standard International (4.0%, overlooked emerging market company): a Hong Kong-based investment and property development group that invests in prime areas of Hong Kong as well as major cities in China. More specifically, Asia Standard focusses on real estate development, rentals, hotels and travel, as well as financial instruments related to this activity. The bulk of the ownership is controlled by the Poon family, thus, like Keck Seng, the management team is fully aligned with its shareholders. A complex shareholding structure, as well as an accounting valuation of the assets at acquisition cost far removed from reality, lead to an extraordinary undervaluation of this stock.

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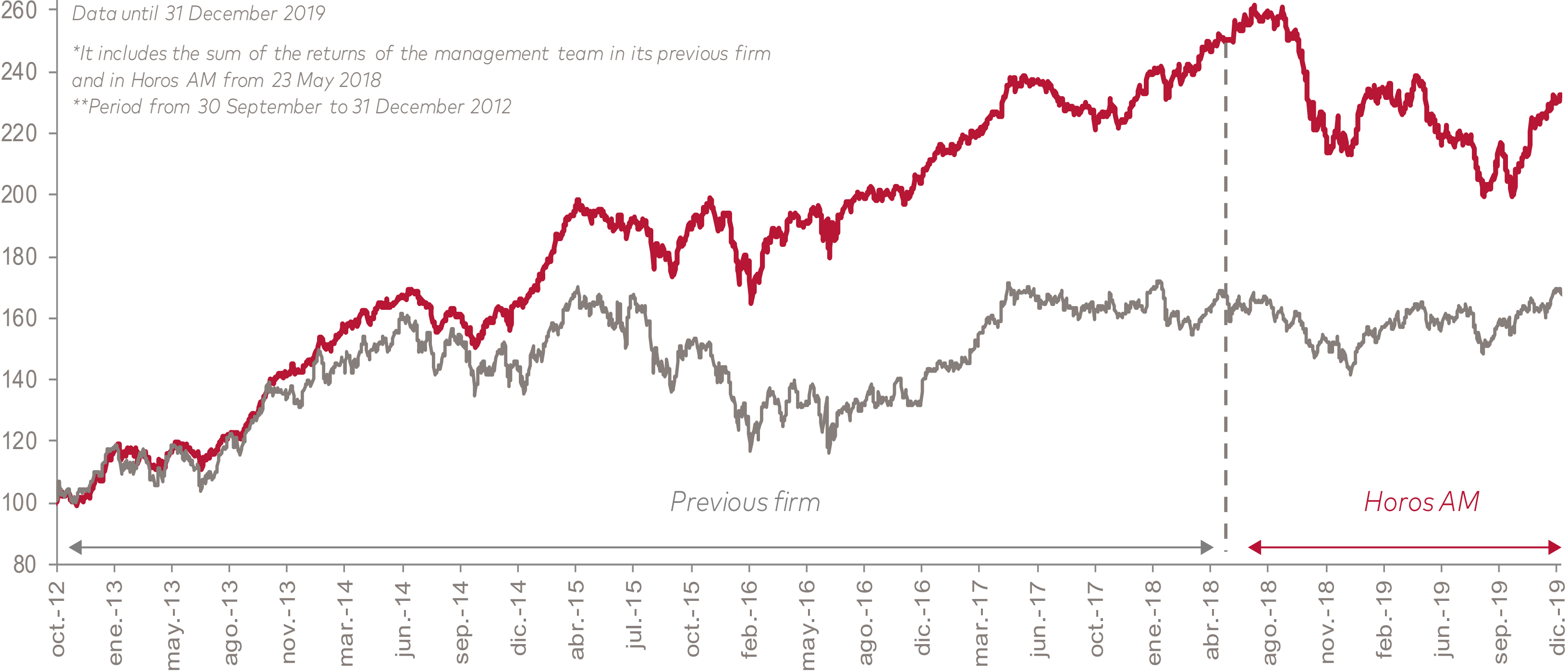
Annex

Returns

Historical returns of the management team in the **iberian strategy**

Net returns	2012**	2013	2014	2015	2016	2017	2018	2019
Management team	7.18%	36.31%	13.45%	17.12%	10.24%	8.73%	-6.45%*	6,66%
80% ITGBM and 20% PSI TR	8.93%	27.95%	2.27%	-0.18%	0.38%	13.57%	-10.56%	15,46%

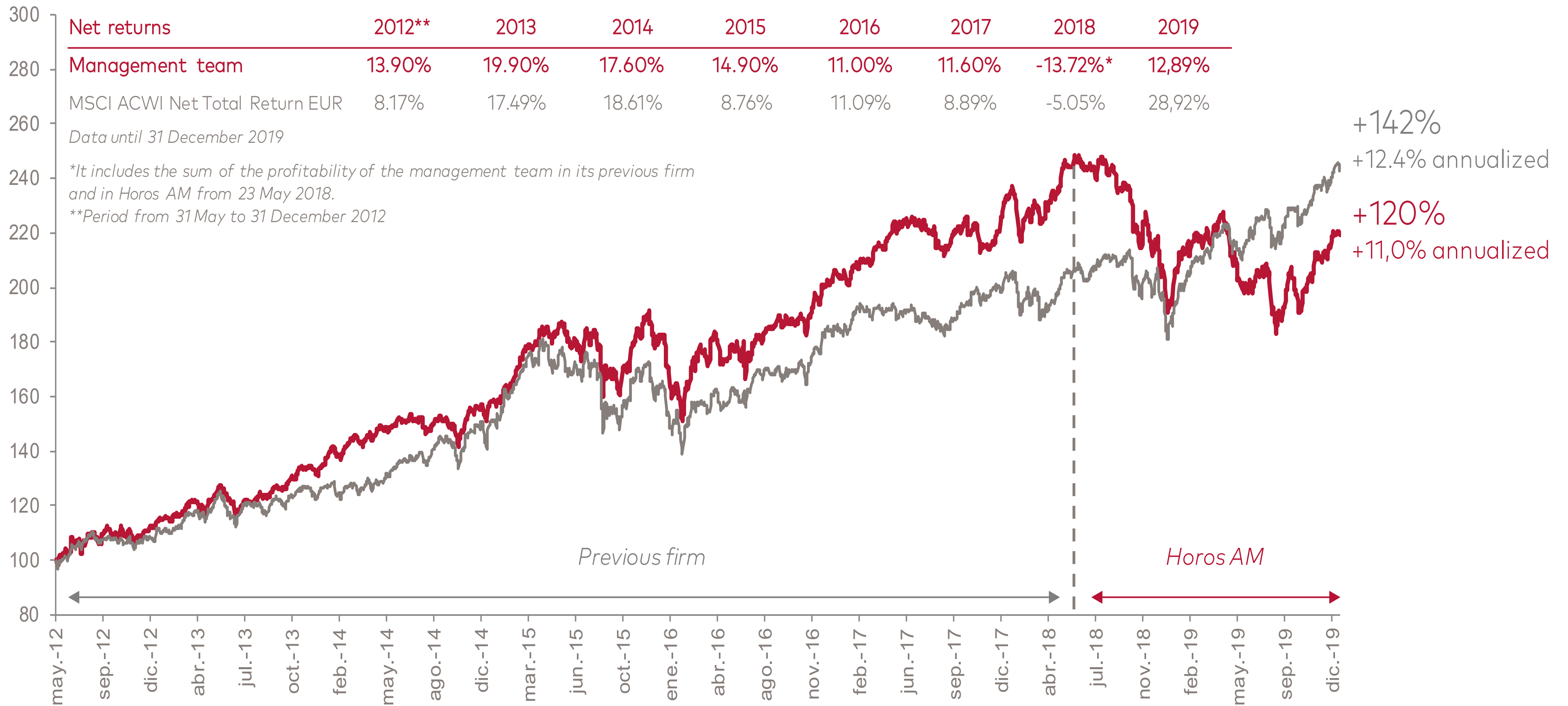


+132%
+12.3% annualized

+67%
+7.3% annualized

Returns

Historical returns of the management team in the **international strategy**



Net returns	2012**	2013	2014	2015	2016	2017	2018	2019
Management team	13.90%	19.90%	17.60%	14.90%	11.00%	11.60%	-13.72%*	12,89%
MSCI ACWI Net Total Return EUR	8.17%	17.49%	18.61%	8.76%	11.09%	8.89%	-5.05%	28,92%

Data until 31 December 2019

**It includes the sum of the profitability of the management team in its previous firm and in Horos AM from 23 May 2018.*
***Period from 31 May to 31 December 2012*

Potential

Historical potential of the management team

Data from 31 March 2014 to 31 December 2019

**Until 21 May 2018 includes the potential of the management team in its previous firm and since then in Horos AM.*