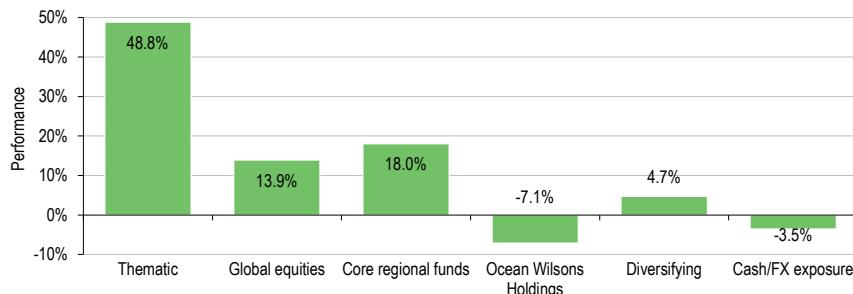


Hansa Investment Company

Brazil – game-changer or sideshow?

Hansa Investment Company (HAN/HANA) fund manager Alec Letchfield argues that investors should not be overly distracted by the fund's exposure to Brazil through a c 11% position in maritime services company Wilson Sons (WSON). While the holding could prove beneficial as global economic growth and trade continue to recover, the remaining c 90% of the portfolio is much more significant, and Hansa IC's persistent 30%+ discount to NAV is arguably unwarranted given its healthy mix (via funds and direct equities) of growth, value and defensive/uncorrelated strategies. Recent performance has shown an improving trend versus peers, and a 13.3% local currency increase in WSON's share price since the start of 2020 (outperforming the main Bovespa Index by 11.5pp) has not been reflected in Hansa IC's discount to NAV, which moved by just 0.4pp from 33.9% to 34.3% (A shares) from 1 January 2020 to 4 May 2021.

Silo performance from 1 January 2020 to 31 March 2021



Source: Hansa IC, Edison Investment Research. Gross time-weighted performance in sterling.

Why consider Hansa IC now?

Hansa IC performed strongly in its financial year to 31 March 2021, with all its underlying strategies ('silos') posting gains. While this is partly the result of base effects (with global markets having sold off significantly in March 2020, just prior to the start of the period), performance from most of the silos was also positive over the period including Q120 (see chart above). The portfolio is positioned to benefit from both a continuation of structural growth trends in areas such as technology, and the recent market rotation into more value and cyclical stocks (mainly through the direct equity allocation, but also via some small changes in the funds portfolio). Meanwhile, positive global GDP and trade trends should support returns from its indirect strategic stake in Brazilian ports operator WSON.

The analyst's view

Investor perceptions remain key to tackling Hansa IC's persistently wide discount, which is arguably unwarranted by the quality and breadth of its underlying holdings. The WSON stake, at just under 11% of NAV, arguably should not be 'the tail that wags the dog', nor, in our view, seen overwhelmingly as a negative (see page 5), given the pick-up in global trade and commodity prices and strong operational and share price performance. The recently announced 3.2p per share dividend for FY22 (flat y-o-y) puts the A shares on a current and prospective dividend yield of 1.5%.

Investment companies
Global multi-asset

6 May 2021

Price Ord.	214.0p
Price A-share	211.0p
Market cap	£254.4m
AUM	£385.6m
NAV*	321.3p
A-share discount to NAV	34.3%
Ordinary share discount	33.4%
*Including income. At 4 May 2021.	
Yield (A-shares)	1.5%
Shares in issue	120.0m
Code Ord/A-share	HAN/HANA
Primary exchange	LSE
AIC sector	Flexible Investment
52-week high/low*	217.0p 145.5p
NAV** high/low	321.3p 239.1p
*A-shares. **Including income.	

Gearing

Net gearing at 31 March 2021 0.0%

Fund objective

Hansa Investment Company was created in 2019 through the redomiciliation of Hansa Trust from the UK to Bermuda. It aims to achieve medium- to long-term growth through a diversified, multi-strategy approach, combining a strategic stake in OWHL with a portfolio of global equities and predominantly third-party managed funds, giving access to primarily non-UK equities, along with more thematic and diversifying funds. Hansa IC does not have a benchmark.

Bull points

- All parts of the portfolio performed positively in FY21 (ended 31 March).
- Flexible silo structure is supportive of future gains and can offer downside protection.
- Significant re-rating potential given wide discount.

Bear points

- Could be under-exposed to value cyclical areas if market rotation persists into the medium term.
- Investors seem unwilling to view the strategic stake in WSON in a positive light.
- Given the discount has persisted in a period of strong performance, there is little obvious impetus for a re-rating.

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The manager's view: Staying focused on quality

Having been dominated by growth and technology, global stock markets are showing signs of rotation into cyclicals and value. Letchfield argues that at this stage it is unclear whether this is purely cyclical, as economies rebound from last year's lows, or more structural. Regardless of the outcome, he believes Hansa IC offers a good balance between growth (at a reasonable price) and high-quality value and cyclical names, and says it is therefore 'well positioned for whatever markets throw at us'. Rob Royle, who selects stocks for the global equities portfolio, has a value tilt to his investment approach. Elsewhere, almost half of the fund's assets (excluding the diversifying portfolio, where short positions in some hedge funds might distort the totals) are invested in North America, with nearly a quarter (c 23% at 31 March 2021) in the information technology sector – an overweight position versus the MSCI AC World Index. 'In the last seven years, the only two calls [to have made] have been the US and technology', says Letchfield. 'We have had a modest bias to growth areas like technology and biotechnology, and while IT stocks may do less well in the near term given the market rotation, we are still in the process of technology changing the way we live, and that story is not over'. However, with Hansa IC's more growth-orientated holdings having done very well over the fund's FY21 (ended 31 March) – technology specialist GAM Star Disruptive Growth was up c 75% – the manager has gently top-sliced some of these positions, and initiated new holdings (c 3% in total) in more cyclical areas such as financials and emerging markets. He has done this using passive exchange traded funds (ETFs), as this enabled new positions to be taken quickly as well as providing flexibility.

Exhibit 1: Portfolio breakdown by silo

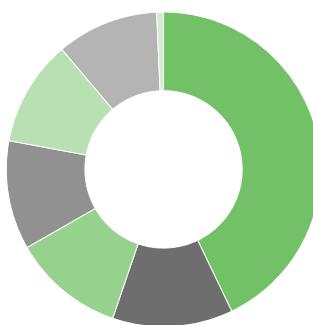
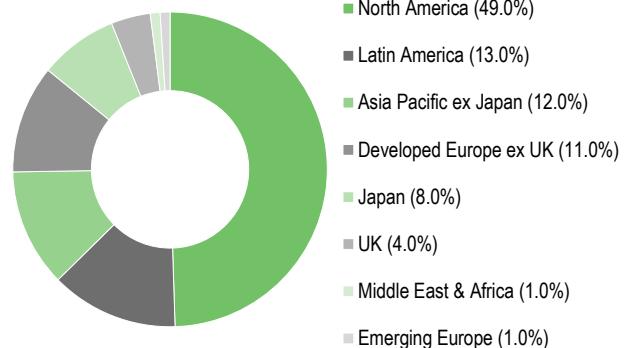


Exhibit 2: Portfolio breakdown by geography



Source: Hansa IC, Edison Investment Research. Note: Data at 31 March 2021. Geographical breakdown excludes diversifying silo.

Letchfield says: 'The question we asked ourselves was do we need to rotate aggressively from growth to cyclicals. We have a long-term quality bias and we are not inclined to chase low-quality cyclical areas. So, while there is a good argument for broadening out, it's a subtle change, not a big rotation – we aren't going to start buying financially distressed cyclicals or companies with large pension deficits.' He notes that he is not the kind of manager who is ever going to join a 'dash for trash', when investors chase low-valued stocks at market inflection points. 'You might buy them well, but you inevitably hold them for too long and end up regretting it', he explains. Letchfield adds that given part of the Hansa IC investment strategy is to invest in fund managers that share a similar philosophy to Hansa Capital Partners, the underlying holdings tend to have a quality bias too. 'These managers tend not to buy commodities, low-quality cyclicals or names that are being disrupted by technology', he says. 'They might invest in companies like Ryanair – good-quality names with robust balance sheets, that should benefit from the reopening of travel – but they wouldn't buy a Lufthansa.'

Looking ahead, the manager argues that a key factor in the sustainability of the global economic recovery and the expected uptick in inflation will be the extent to which these can move past the

'base effect' of comparisons with 2020. 'Oil has gone from \$0 to \$60 over the last 12 months, so this year inflation will pick up, but the big question is whether we are returning to structurally higher inflation', he says, adding that while he is still 'on the fence' about the answer to this question, any evidence of continued inflationary pressure would probably lead him to move further into areas such as Europe, Japan, commodities and financials, which have historically been beneficiaries of higher economic growth and inflation. However, Letchfield warns that an increase in core inflation could eventually force central banks into raising rates, which could lead to 'quite a nasty taper tantrum', as was seen in 2013. 'We may be setting ourselves up for a conventional end-of-cycle bear market', he says, adding that in such a situation, he would consider increasing the allocation to the fund's defensive portfolio of diversifying assets, which proved their worth in the Q120 sell-off.

Performance: Firing on all cylinders in FY21

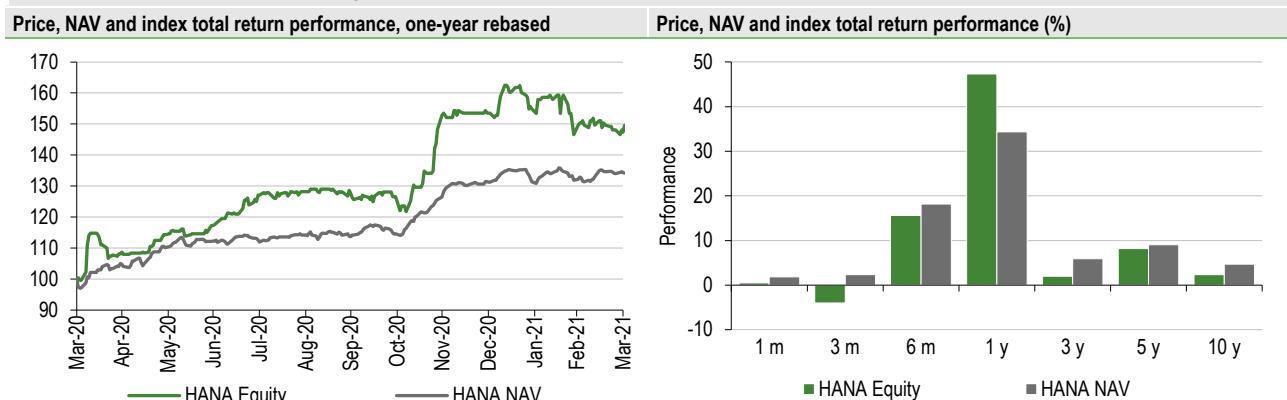
Exhibit 3: Five-year discrete performance data

12 months ending	Total A-share price return (%)	Total NAV return (%)	MSCI AC World (%)	CBOE UK All Companies (%)	UK Gilts TR (%)	UK CPI (%)
31/03/17	19.3	22.0	33.0	22.6	6.6	2.3
31/03/18	17.3	6.3	2.9	1.2	0.5	2.5
31/03/19	1.4	5.6	11.1	6.2	3.7	1.9
31/03/20	(29.0)	(16.9)	(6.2)	(19.1)	9.9	1.5
31/03/21	49.3	34.8	39.6	26.6	(5.5)	1.0

Source: Hansa IC, Refinitiv. Note: All % on a total return basis in pounds sterling.

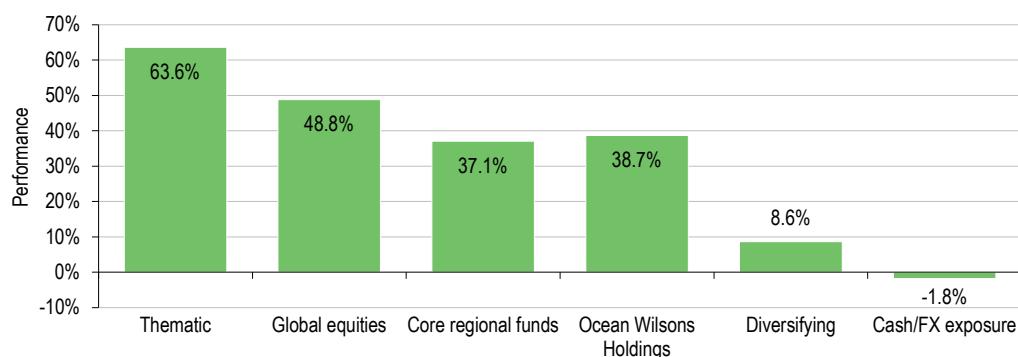
Hansa IC's NAV performance in FY21 (Exhibits 3 and 4) reflects a number of factors. The 34.8% NAV total return for the 12 months to end-March 2021 is only c 5pp behind the MSCI AC World index, a reasonable outcome for a resurgent year in global markets. As shown in Exhibit 5, every part of the portfolio performed positively over the period. However, the underlying drivers of performance differ. The core regional and thematic funds are more exposed to quality and growth factors, and benefited from positive performance from areas such as the US, technology stocks and biotech, which led global stock markets for the majority of 2020, both before and after the COVID-19 driven sell-off in February and March of last year. The global equities portfolio – which contains more value and cyclical-type names – bounced back strongly in the market rotation that followed positive news on COVID vaccines in the latter part of 2020, posting a near-50% return. Part of this very positive outturn is due to the base effect of measuring from 31 March 2020; looking at returns over the 15 months from 1 January 2020 (see front page chart), which captures the full impact of the global market falls in February and March 2020, the return is lower but still respectable, at 13.9% for the period.

Exhibit 4: Investment company performance to 31 March 2021



Source: Refinitiv, Edison Investment Research. Note: Three-, five- and 10-year performance figures annualised.

The strategic position in Ocean Wilsons Holdings (OWHL) is split roughly equally between OWHL's majority (58%) stake in WSON, and the Ocean Wilsons Investments (OWIL) funds portfolio, which largely mirrors Hansa IC's own funds portfolio, with the addition of c 30% in private equity funds. The difference in returns over FY21 (+38.7%) and the 15 months from 1 January 2020 (-7.1%) reflects the performance of WSON more than that of the funds portfolio. WSON's shares sold off heavily in Q120 on fears over the impact of COVID-19 on global trade (around a third of the company's revenues come from its container shipping terminals) as well as the collapse in the oil price (c 15% of revenues are from offshore supply vessels serving the oil & gas industry). The company acted quickly to shore up its balance sheet, cutting costs and cancelling its dividend. This meant it was well positioned for the subsequent recovery in trading conditions, leading to the declaration of a special dividend in November to replace the earlier missed payment.

Exhibit 5: Silo performance in FY21 (ended 31 March 2021)


Source: Hansa IC, Edison Investment Research

The diversifying silo, made up mainly of defensive hedge funds and absolute return-type credit strategies, did its job in difficult market conditions, with all but one of the funds posting a positive return over both FY21 and the 15 months from 1 January 2020. Since inception of the strategy in 2016, the basket has returned 28.4%, markedly outperforming UK and global government bond indices, with a maximum drawdown of 4.5% (in the period February to April 2020) compared with 7.3% for UK gilts and 15.9% for the MSCI AC World index (based on monthly data).

Exhibit 6: Selected peer group performance as at 4 May 2021*

% unless stated	Market cap £m	NAV TR 1 year	NAV TR 3 year	NAV TR 5 year	NAV TR 10 year	Ongoing charge	Perf. fee	Discount (cum-fair)	Net gearing	Dividend yield
Hansa Inv Co Ltd 'A'	168.8	33.5	18.7	55.0	52.2	1.1	No	(34.3)	100	1.5
Hansa Inv Co Ltd Ord	85.6	33.5	18.7	55.0	52.2	1.1	No	(33.4)	100	1.5
AVI Global Trust	1,028.9	57.6	36.5	116.5	129.2	0.9	No	(5.8)	107	1.7
Caledonia Investments	1,634.1	23.7	29.0	53.9	128.0	0.9	No	(25.3)	100	2.1
Capital Gearing	691.7	14.0	24.0	44.0	87.5	0.7	No	2.3	100	0.9
RIT Capital Partners	3,839.2	39.7	45.8	80.0	139.7	0.7	Yes	(3.7)	115	1.8
Ruffer Investment Company	559.3	17.0	26.9	43.0	62.9	1.1	No	1.1	100	0.7
Witan	1,864.9	48.2	27.7	83.3	169.8	0.8	Yes	(6.0)	110	2.3
Simple average (8 funds)	1,234.1	33.4	28.4	66.3	102.7	0.9		(13.1)	104	1.5
HANA rank in sector	7	4=	7=	4=	7=	1=		8	4=	5

Source: Morningstar, Edison Investment Research. Note: *Performance to 3 May 2021 based on cum-fair NAV. TR = total return. Net gearing is total assets less cash and equivalents as a percentage of net assets (100 = ungeared).

In Exhibit 6 we present Hansa IC alongside a peer group drawn from the AIC Global and AIC Flexible Investment sectors. Clearly, the fund's strategic stake in OWHL means it is hard to draw direct comparisons with other funds, but the peers also broadly invest globally in a range of underlying strategies. Despite the negative impact on performance over some periods from the holding in Wilson Sons, NAV total returns are comparable to that of the peer group median over one and five years, while the discount is significantly wider than those of the peers. Ongoing charges (using the AIC calculation basis) are somewhat above average, the dividend yield is in line and, in common with the majority of peers, Hansa IC has no gearing at the fund level. What really

stands out is the wide discount at which both share classes trade (discussed in more detail below). The only other peer at a double-digit discount is Caledonia Investments, another family office-type vehicle, which has a significant allocation to private equity and as such tends to trade on a discount more in line with those of mainstream private equity funds. It is also notable that the two funds currently trading at a premium to NAV (Capital Gearing and Ruffer Investment Company) are the worst performers over one and five years, the periods in which Hansa IC has seen its best relative returns.

Is Brazil the tail that wags the discount dog?

So, is it fair to say that the reason for Hansa IC's persistently wide discount is its exposure to Brazil via WSON? We analysed WSON's performance and that of the Brazilian Bovespa Index versus Hansa IC's discount over the past 10 years and concluded that while the fund's discount tends to widen more when Brazil is out of favour, there is little evidence of a similar narrowing in the discount when Brazil and/or WSON are performing well. This suggests that many investors are content to assume WSON will always be a drag rather than a potential source of opportunity, clearly a mistaken assumption given OWHL's contribution to returns (outperforming the core regional funds portfolio) in FY21. It is perhaps the non-discretionary nature of the stake that causes this poor perception, although at only just over 10% of the portfolio (a similar size to the top holdings of many equity funds), one could argue that the impact of WSON for good or ill is overstated in investors' minds. Furthermore, Letchfield points out that 'you could give away WSON for free' and the fund would still be on a wider-than-average discount compared with its peers of c 26%. Other potential factors affecting the discount may be the high level of ownership by entities associated with the Salomon family, leading to perceptions of illiquidity. In fact, in the non-voting A-shares, the level of trading liquidity (average daily volume of c 0.11% of the share base over the past 12 months) is not dissimilar to that of a core UK equity income fund such as Lowland Investment Company (c 0.15% of shares traded daily), which has a high level of retail investor ownership and trades at a much smaller discount.

Broadening retail ownership may well be one way in which Hansa IC can address its discount. Investment company enthusiasts are often drawn to those funds that are doing something different from the herd, and a quality portfolio of hard-to-access funds with a growth tilt, value-biased global equities, a defensive allocation and an interesting play on Brazilian growth and global trade might prove more attractive in the long term.

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