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Letter to Partners #14

Q4 2021 *(10/01/2021 - 12/31/2021)*

January 30th, 2022

Dear Partner,

In the fourth quarter of 2021, **our fund returned +2.8%**. The performance (net of fees) in the twelve months of 2021 amounted to **+35.3%**. The fund volume stood at EUR 31.2 million at the end of the quarter. In 2021, we received EUR 14.8 million in net inflows across all three tranches of the Gehlen Braeutigam Value HI fund.

EUR 100.00 invested at the start of the fund in mid-2018 was worth EUR 177.36 at the end of the quarter. The **overall gain since inception is +77.4%** and the **compounded annual gain is +17.8%** (compared to +42.1% or +10.5% p.a. for our reference index).

Net performance figures (including distributions), after deducting all costs, the -S-, -R- and -I- tranches:

	-S- Tranche	-R- Tranche	-I- Tranche	MSCI Europe S&M Cap
2018	-2.9%*	-2.5%**	-	-17.2%*
2019	+10.3%	+9.2%	+8.3%***	+30.6%
2020	+22.3%	+20.9%	+21.3%	+5.8%
2021	+35.3%	+34.2%	+34.8%	+24.2%
Since inception	**+77.4%**	**+73.1%**	**+77.2%**	**+42.1%***
Annualized return	**+17.8%**	**+18.0%**	**+21.0%**	**+10.5%***

* Since the -S- tranche was launched on July 2nd, 2018 until the end of 2018 (approx. 6 months). ** Since the -R- tranche was launched on September 7th, 2018 until the end of 2018 (approx. 4 months). *** Since the -I- tranche was launched on January 2nd, 2019 until the end of 2019.
Note: Due to the different starting times and fee structures, there may be deviations in the performance of the individual tranches.
Note: MSCI Europe Small & Micro Cap index; net-return (EUR).

All three tranches of our fund are currently open for investment:
The -S- tranche is closed to new investors. Existing investors can order additional fund units with a minimum investment of EUR 10,000. The -R- tranche can be invested in without a minimum investment amount. In the -I- tranche, the minimum investment amount for new investors is EUR 200,000. Existing investors in the -I- tranche can order additional fund shares without a minimum amount. You can find the respective tranche using the following **ISINs** as well as the links below for further information:

-S- Tranche: DE000A2JF8Z7 **-R- Tranche: DE000A2JQHQ2** **-I- Tranche: DE000A2N8119**

Portfolio

In the fourth quarter, and generally in the second half of 2021, many very highly valued shares and excesses in the market – we have written about a few in our Letter a year ago – have faded and experienced strong declines. Covid winners, including e-commerce players, were also not in favour as growth rates have (naturally) slowed when compared to the very good 2020 results.

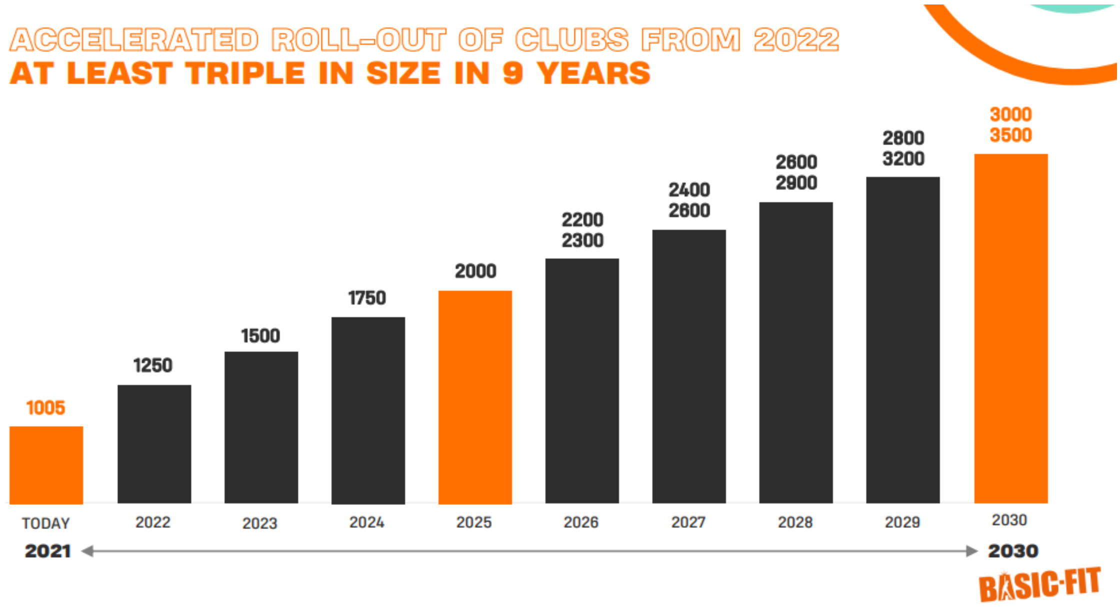
home24 has been no exception and as a result has been the worst performer in our portfolio during 2021. Since we began building the position, we have been aware of, and cautious of, the difficult period that would follow after the COVID e-commerce "boost" would dissipate. We've continued to closely monitor the case as the share price has continued to fall. We still, and even more so, see a company that is materially undervalued at less than 0.3x sales.

At the same time, home24 has continued to deliver results that we find satisfactory and that are in line with our expectations. Additionally, the company has recently announced the acquisition of Butlers, which we are currently analysing in-depth and discussing with management. Finally, home24's impressive progress on own last mile delivery (20%+ share in Q3) allows the company to have more control over their product, which therefore should increase customer satisfaction and lifetime value.

On the other side, we can happily watch the development of our gym investments for which the business is slowly returning to normal. We first invested in **Basic-Fit** right after the outbreak of the pandemic in early 2020. Back then the biggest risk on investors' minds was that people wouldn't be returning to gyms to the same extent they used to. Our investment partly rested on the conviction that people would in fact return to the gyms which was supported by all initial datapoints (we also gave a brief update on this in the LtP #12).

Sentiment has since turned, bolstered by further encouraging datapoints from both Basic-Fit and its competitors. Today, the Dutch company appears to be stronger than ever. Its balance sheet is in great shape while many of its competitors became weaker, giving it a unique opportunity to capture even more market share both in existing and new markets. Its share price reflects this strength and is up almost 150% from our initial purchase price of ~EUR 18.

On November 4th, Basic-Fit held a capital markets day (CMD) in which it provided investors with an update on its strategy and growth prospects. During four hours of presentations the company's senior management delivered a very upbeat message in which it set itself a ***target of more than tripling its current club-base from 1,005 to 3,000-3,500 by 2030***. This figure was ahead of our own expectations (as well as the market's).



Source: Basic-Fit; as of November 4th, 2021.

Management described in detail how Basic-Fit's low-cost base allows them to open clubs in small communities where other operators cannot profitably run a gym, thereby greatly increasing the addressable market for the company. Management also said that it plans to expand to a new European country at the end of 2022 (we suspect it may well be Germany).

The presentation also addressed several exciting innovation initiatives Basic-Fit has been working on, such as an omnichannel strategy that supports at-home workouts as well as new applications that further allow it to reduce the cost of operating clubs. We came away impressed and updated our views and valuation of the company. Despite the near-term complexities from the new COVID-variant, we think Basic-Fit has a very promising future ahead and we bought more shares during the quarter to expand our position. For those interested, the CMD presentation can be accessed here.

In Milan, we met with a group of bankers and investors to join a field-trip to the Barolo region for a site-visit to the Giordano facilities of **Italian Wine Brands** (IWB). So far this has been a very successful investment for us, so it was a good point in time to revisit the case. The CEO and CFO both joined for the full duration of the site-visit, gave a presentation on the business thereafter, and were available for questions.

During the presentation, management highlighted its next focus area for expansion, the US. Shortly after, the company has bought a US distributor at the end of 2021. We are conscious that the US market is very challenging but are also encouraged by the prospects that a stronger position in the largest wine market in the world offers. In the meantime, we have also received further (very) positive feedback from industry experts and customers on the Giordano wine brand.

In the following section, we discuss how we think about acquisitions and in which cases we see a higher chance that acquisitions add value. In particular, we take a deeper look at the recent acquisitions of IWB. Finally, we present the investment case of Sto, which has been one of our largest portfolio positions for quite some time already. As usual, you will find further information on our portfolio on the last pages.

We are thankful that our fund has grown so much last year and are very happy about the quality of the new investors who have joined our fund. In order to make it easier to share our message and beliefs, we recently had the opportunity for our first video interview with Tilman Versch from the Good Investing community. The video has received more than 1,000 views so far. Please enjoy and feel free to share it with whomever you think could be an appropriate addition to our group of like-minded investors.

Last but not least, we would like to highlight that Kory and Tristan have received the *Partner* title. We are strong believers in a meritocratic way of running the fund and this new title adequately reflects that.

We thank you very much for your trust and ongoing support. Please feel free to contact us with questions or comments.

Sincerely yours,

Daniel Gehlen

Marc-Lennart Bräutigam

The value of accretive acquisitions – buy two, get one free

In our recent letters, we have mentioned in a positive light a few of our companies which have made acquisitions. We *don't* generally view acquisitions favorably. In fact, we are quite skeptical about them. Both theoretical as well as empirical evidence support the thesis that acquisitions in most cases don't add but destroy value for the buying party. Nevertheless, the actual merit of a transaction very much depends on the unique conditions and context of the particular situation.

Why one must be careful with acquisitions

An often cited and intuitive reason for the bad performance of acquisitions is the desire of many managers to "build an empire" rather than to optimize company performance. We as investors have to be focused on managers creating value for their stakeholders – shareholders but also employees and customers.

Like many participants in the capital markets, managers are prone to engage in pro-cyclical behavior. In times when business is good and stock prices increase, managers' and their supervisors' confidence increase. During these times, capital to fund acquisitions is also more easily available. Thus, managers become more willing to acquire other companies. However, these are also exactly the times when valuations are usually the highest and competition for targets is elevated (as other companies are in the same situation).

Apart from the risk of buying companies at the worst possible time, acquiring other companies, and integrating them can also be (very) difficult. Different cultures are a key issue – employees can feel connected to a company (brand) and might be less willing and motivated to work for their new employer. Synergies are also rarely as high or easy to achieve as the pre-acquisition estimates imply.

Italian Wine Brands – a value-creating acquirer

We look for managers who think and act like owners, even more so when acquisitions are part of an investment thesis. Next to the direct share ownership, the structuring of management compensation can be crucial as can be the quality and independence of the supervisory board. The long-term (!) alignment of interests with the key decision makers increases the likelihood that acquisitions are done "for the right reasons".

For obvious reasons, we prefer acquisitions which have attractive financial terms and directly add economic value, in addition to a good cultural and business fit. Beyond that, there are other reasons which can make an acquisition compelling, in particular when a takeover can help to manifest a company's moat and market position. However, such rationales are often more difficult to evaluate from the outside.

We like acquisitive companies when they operate in a large but fragmented industry, i.e. an industry with many smaller players. Just like with our own investment approach, this offers a large selection of potential targets. In addition, smaller companies are more often available at more attractive valuations. The valuations ultimately depend on supply and demand. If there is less competition from other acquirers but a large supply of companies willing to sell, prices are naturally lower. These can be great environments for successful "roll-ups". Buying smaller companies comes with another advantage. It can be much easier and especially less risky to integrate or simply add several smaller acquisitions over time than buying a business of the same size.

The most acquisitive company in our portfolio today is the wine producer **Italian Wine Brands** (IWB). We have discussed the investment case in our LtP #9. IWB has taken over three companies since the beginning of 2020. The acquired companies have in total added sales of around EUR 240m. On a stand-alone basis, IWB would have generated around EUR 190m sales in 2020, i.e. the company has doubled its sales in the last 2-3 years just through acquisitions.

We think of Italian Wine Brands as a leading player with superior execution. The industry of wine producers is extremely fragmented. The company has demonstrated that it can buy other firms for attractive valuations. The synergies on the cost side are significant, especially in production and purchasing next to the obvious areas in overhead, which reduces the effectively paid acquisition prices even further.

Target	Date	Acquisition price	Sales	EBIT	Est. synergies	EV/EBIT	EV/EBIT (incl. synergies)
Enovation Brands	Dec-2021	22.9	28.3	2.2	0.8	10.2x	7.5x
Enoitalia	Jun-2021	150.5	200.8	13.6	6.0	11.1x	7.7x
Raphael Dal Bo	Mar-2020	12.6	10.1	1.7	1.0	7.5x	4.7x

Note: Numbers in EURm. Source: Company information, Gehlen Bräutigam Capital (in particular estimates of synergies).

The above table shows that Italian Wine Brands has acquired targets for about 5-7.5x EBIT when accounting for (our own estimate of) synergies. These acquisition prices are very attractive and substantially below the valuation assigned to IWB by the market, which currently trades at ~13x EBIT. It also indicates a (no-growth) return on invested capital – the acquisition price – of 10-15% which is materially higher than the cost of capital of a defensive business model such as IWB's. Importantly, this return is calculated before growth and revenue synergies. The latter are a key consideration for the acquisitions and, given IWB's asset-light business model, growth is highly value-accretive.

Selling to Alessandro Mutinelli (the CEO and a founder of IWB) and his team also strikes us as a very interesting exit route for a business owner. Despite the potential for cost synergies, IWB is primarily looking to growing businesses. This protects a founder's heritage whereas selling to a financial investor or a large corporation could come with risks such as large layoffs of employees.

After having bought a few companies and being recognized for the success of these acquisitions – also very publicly reflected by a strongly increasing share price – IWB's position is only becoming stronger. Its visibility is increasing, qualified employees are actively looking to work for the company and many potential sellers will consider IWB as one of the first options to sell to. Furthermore, the increased valuation of the share gives IWB a strong currency to pay for new acquisitions. In that regard, IWB has managed to create a "flywheel effect".

We also like companies which put an emphasis on culture as well as integration and put a lot of thought into this part of acquisitions. IWB's management team has known the owners of its largest acquisition to date – the Italian wine producer Enoitalia – for a long time before the merger. In addition, the founder family of Enoitalia has reinvested a substantial share of the purchase price into the combined entity which underlines their supportive view of the opportunity.

Sto – refurbishment of a long-term success story

Sto is a great example of an overlooked and underestimated compounder in the German capital market. It's a high-quality business with a very consistent and strong long-term track record. For most of its public market history, shares of Sto have sold for fairly moderate valuations. Sometimes, investors ask us what's going to change this. We don't think a short-term change in the perception of the market is necessary for a long-term oriented investor.

An investment into Sto 20 years ago would have increased nearly 20-fold (incl. dividends). During this time, the company has grown steadily with low volatility and at attractive levels of profitability – the returns on capital ranged between 10% and 25% during most of this time. The revenues have more than tripled from EUR 460m in 2001 to nearly EUR 1.6bn in 2021. In two decades, Sto's revenues have not decreased by more than 3% in a single year, not even during the financial crisis.

Despite this impressive development, Sto's share is only covered by one analyst and, in our view, still trades at a very attractive valuation. Beyond its very successful history, we believe that Sto is at an inflection point today and we will outline later in this case study why today's environment might be more favorable to Sto than it has been at any point in the last 20 years.

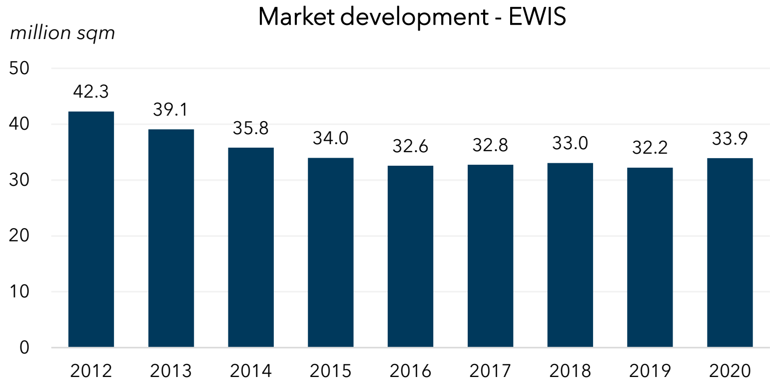
Sto generates about half of its revenues with facade systems (external wall insulation systems (EWIS)). Next to this, the company sells render and paint systems for external applications in its facade coating product group (22% of revenues). Product for interiors, e.g., plaster and paint systems for home and office interiors or decorative coatings, account for another 15% of revenues. Even though revenues have on average grown faster abroad in the last two decades, Sto still generates 45% of its revenues in its home market Germany.

The company operates in a (very) fragmented industry in which many smaller players are still active today. In Germany, Sto is one of the few large players and is very well-positioned thanks to its strong and well-known brand as well as close relationships to its customers. Sto's products are sold at premium prices thanks to their very high-quality level, reliability, and the additional value-add services the company provides. Sto has in particular structured its sales so that it addresses all stakeholders in a building project (incl. homebuilders, investors, planners and architects as well as craftsmen) and their specific concerns separately.

Its strong positioning and competitive advantages have led to consistent market share gains over the past years. Sto has leading market positions in its core markets of France, Germany, Netherlands, and Belgium.

Facing headwinds

As we have mentioned above, we think that Sto is facing an inflection point in its business environment today. In fact, the environment for external wall insulation systems (EWIS) has not been supportive in the last years and market volumes have constantly declined in Germany.



Source: VDPM – Verband für Dämmsysteme, Putz und Mörtel e.V.

This decline was triggered by notable media discussions about thermal insulation systems. Not least the fire in the Grenfell Tower, a large residential building in London, has been very prominent in the media and has unsettled (private) investors as external insulation had been mentioned as one of the facilitators of the fire.

Beyond this negative public attention, politics have considered to provide additional subsidies for thermal insulation in 2011. Since then, subsidy discussions have regularly returned (in particular from 2012-16) but led to no implementations. This led to decision makers postponing investment decisions to renew insulation in the hope and expectation that they might benefit from subsidies later.

This unfortunate environment was also the main reason why Sto has not achieved its growth targets in the last few years (before 2021). Nevertheless, against such a market backdrop Sto's performance can be seen as impressive. Between 2012 and 2020, **market volumes have decreased by 20%**. During the same timeframe, **Sto has still managed to increase revenues by 25%**.

The fight against global warming begins

"Buildings" are responsible for a significant portion of total CO2 emissions. Estimates range from 15-20% of total emissions to even higher percentages (incl. production and delivery of building materials etc.). A better insulation of buildings would without a doubt have a very positive impact.

As anyone can observe, the awareness and the urge to fight emissions has accelerated strongly in recent years. Specific targets have also been set for the building sector. In Germany, greenhouse gas emissions of the sector must fall by 66% by 2030 compared to 1990 levels. To reach these targets, funding and support measures are provided at immense scale.

In its **Sofortprogramm 2022** alone, which is following the Sofortprogramm 2021, the German government intends to provide almost an **additional five billion euros** for energy-efficient building refurbishment and new buildings, including social housing.

In the **EU Green Deal**, of which the first draft was published at the end of 2019, energetic renovation is one of the essential points. A **doubling of annual renovations** is targeted by 2030. For this goal, gigantic subsidy volumes as well as other measures (e.g., strongly improving approval processes) will be provided.

Of course, the ultimate effect and efficiency of these words and good intentions will only be known in the next years. However, it seems almost certain that the market environment in the next decade will be more favorable than in the last decade.

In recent months, another potential tailwind has emerged, namely strongly risen energy prices. With higher energy costs, saving energy through a more efficient insulation becomes economically even more attractive.

Whereas it might be difficult to estimate the exact impact on Sto's financials – one should also consider that there are growth bottlenecks such as craftsmen capacity – we would be surprised if Sto returns to low-single-digit growth rates given the much, much more positive environment. The company has recently published a new mid-term guidance targeting high-single-digit growth rates. We view this as achievable. In 2021, Sto has grown its revenues by ~11%.

Valuation remains favorable

When we first built our position in Sto in 2019, the shares were trading at 6-7x EBIT and a double-digit FCF yield. We looked at a very solid business with an impressive long-term track record. We also viewed it very likely that the environment in the next years would be more favorable than in the last years although it was difficult to estimate how strong the tailwind from this might be.

Back then, we looked with hope at the promising initial effects from first initiatives which started in France. More recently, it seems like the subsidies are indeed finding their place into the real economy in other countries as well. After the share price has increased >150% since our initial investment, Sto's shares still only trade at a 6.5-7% free cash flow yield (excl. growth investments) today. Considering how solid and cash generative the business is that would be an appropriate yield if the company had low growth prospects. However, given the very favorable environment and Sto's strong positioning, we estimate that the company can grow its free cash flow at 10-15% p.a. by growing revenues and improving the margins to its target of >10% (on EBT level).

Overall, these assumptions imply a 15-20% return for shareholders (FCF yield + FCF growth) in the mid-term without any rerating of the shares. We view that as particularly attractive since we see Sto as a (way) below-average risk investment thanks to (1) its very stable business, (2) strong structural drivers and (3) a very conservative financing structure.

In fact, in our view the financing structure is too conservative. As of H1 2021, Sto held a net cash balance of ~EUR 200m according to our calculations. We expect that this cash balance will be another EUR 100m higher at the end of the year. Even considering a EUR 120m pension deficit, this is very conservative for a company as solid and cash generative as Sto. It is also very substantial compared to the current market cap of EUR 1.45bn.

We expect that a change is likely in the not-too-distant future. Either Sto will find good companies which it can acquire at attractive prices, or a special dividend (as in 2015) becomes increasingly likely. This could be on the agenda for the next AGM already, i.e., in a few months, considering how much cash has already piled up on the balance sheet thanks to the strong performance in recent years.

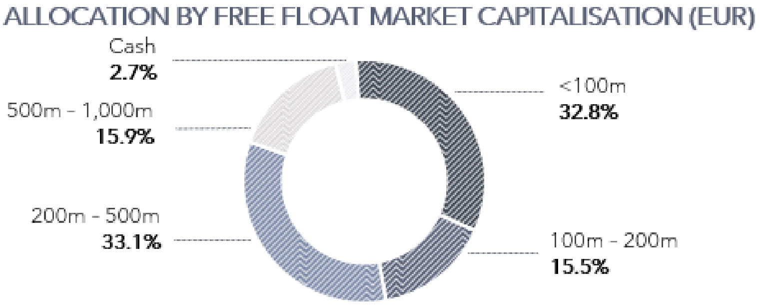
Portfolio overview

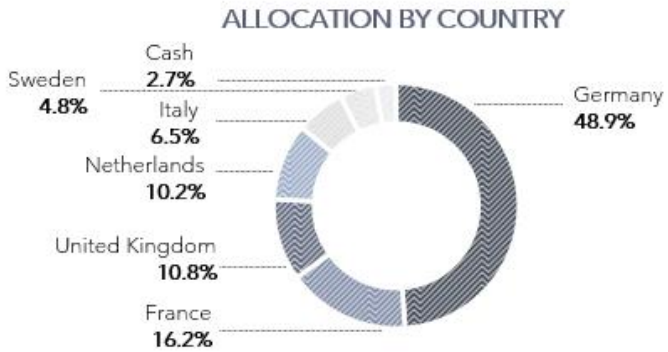
Top 10 positions with respective weightings as of December 31st, 2021:

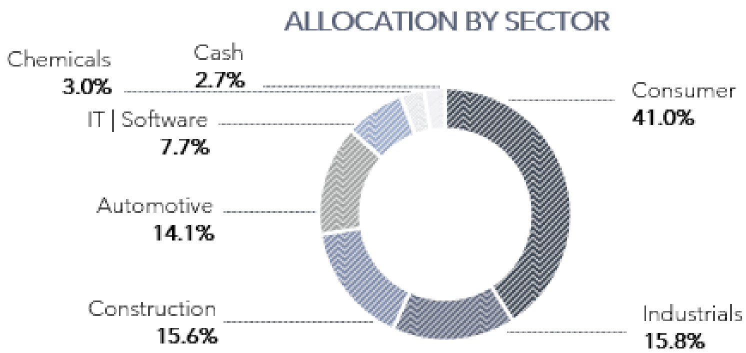
1	Sto	7.4%	6	Catana	5.0%
2	Muehlhan	7.2%	7	Ferronordic	4.8%
3	Akwel	7.0%	8	Naked Wines	4.7%
4	home24	6.6%	9	Basic-Fit	4.6%
5	The Gym Group	6.2%	10	Traumhaus	4.4%

Source: Gehlen Bräutigam Capital; HANSAINVEST.

Allocations as of December 31st, 2021:

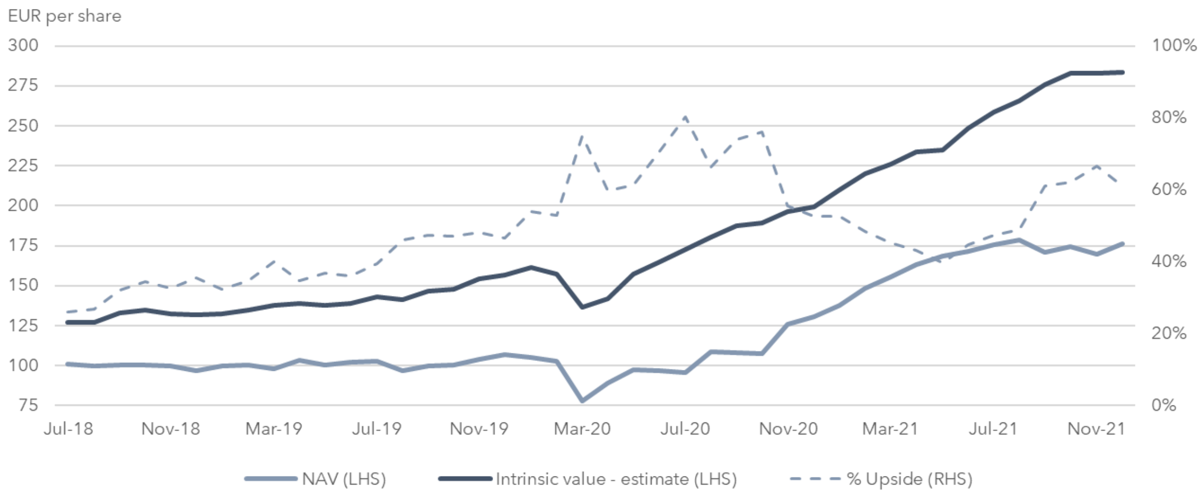






Source: Gehlen Bräutigam Capital; HANSAINVEST.

Development of the intrinsic value estimated by us in comparison to the development of the current price of a unit (NAV) since inception:



Source: Gehlen Bräutigam Capital; HANSAINVEST; as of December 31st, 2021.

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