EDISON

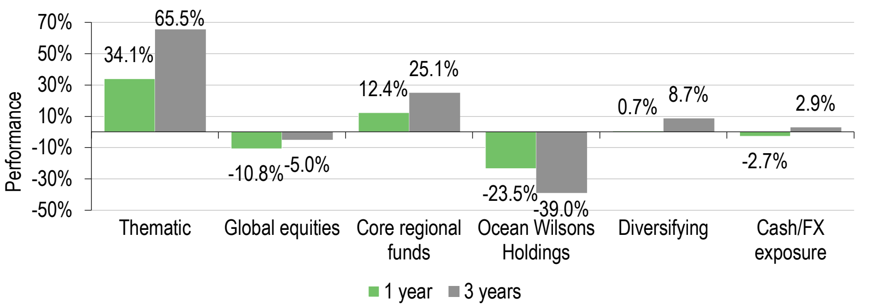
Hansa Investment Company

Overdue a reappraisal?

Investment trusts
Global multi-asset

Investors looking at Hansa Investment Company (Hansa IC; HAN/HANA) may have been perplexed in the past as to why its strongly performing multi-asset fund portfolio sits alongside a large strategic holding in a Brazilian maritime services company, Wilson Sons (WSON) and a value-oriented selection of direct equities. In this short update, we seek to address this question and argue that Hansa IC's deep 'double discount' (c 45%) to net asset value and near-2% dividend yield could mean long-term investors can effectively afford to wait for an exit from or reappraisal of the WSON holding, and/or a rerating of the equity portfolio.

Fund selections performing well over one and three years to end-October



Source: Refinitiv, Edison Investment Research. Total returns in sterling.

Why consider Hansa IC now?

Manager Alec Letchfield's overhaul of the portfolio since 2014's strategic review has largely worked well, with strong performance coming from the regional and thematic funds silos and the diversifying exposure performing as it should, limiting downside in volatile market conditions and adding to incremental returns. The Ocean Wilsons Investments (OWIL) part of the strategic stake in Ocean Wilsons Holdings (OWHL) has significant overlap with these fund selections. However, the portfolio of direct equities, chosen by Rob Royle with a value tilt, has underperformed and OWHL's holding in WSON has suffered a perfect storm of low oil prices, falling global trade and a declining Brazilian real. With some of these headwinds abating as the world begins to look beyond COVID-19, Hansa IC therefore offers recovery potential as well as access to structural growth themes such as tech and healthcare. This may be more than fully reflected in the fund's current c 35% discount to NAV.

The analyst's view

- Discussion over the WSON holding has dominated the discourse around Hansa IC, but is arguably less relevant given it is now only c 10% of the fund.
- Letchfield deserves credit for his fund selections, which have allowed investors to access global growth themes such as technology and healthcare while retaining a degree of downside protection via the 'diversifying' silo.
- While the value-oriented direct equity portfolio has detracted from recent returns, it acts as a foil to the more growth-focused fund selections and could be beneficial if there is a change in market leadership from growth to value.
- Although Hansa IC's discount to NAV is to some extent understandable, it remains wider than we believe is justified by the underlying holdings.

20 November 2020

Price Ord.	**180.0p**
Price A-share	**178.5p**
Market cap	**£215.4m**
AUM	**£336.2m**
NAV*	278.7p
A-share discount to NAV	35.4%
Ordinary share discount	36.0%

*Including income. At 17 November 2020.

Yield (A-shares)	1.8%
Shares in issue	120.0m
Code Ord/A-share	HAN/HANA
Primary exchange	LSE
AIC sector	Flexible Investment

52-week high/low*	197.5p	128.5p
NAV** high/low	296.4p	224.6p

*A-shares. **Including income.

Gearing

Net cash at 31 October 2020	1.7%

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

- Lead manager Alec Letchfield's fund selections (c 75% of the portfolio) have performed well.
- Flexible silo structure is supportive of future gains and can offer downside protection.
- Significant rerating potential given wide discount.

Bear points

- No clear catalyst for Brazil to return to favour, albeit the market may be at a cyclical low point.
- Given the persistence of wide discounts on both Hansa IC and OWHL, and value remaining unloved, timing of a rerating is uncertain.
- Fund NAV has lagged global stock markets over one and three years.

Analysts

Sarah Godfrey	+44 (0)20 3681 2519
Mel Jenner	+44 (0)20 3077 5720

investmenttrusts@edisongroup.com

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Hansa IC: What's the story?

Hansa Investment Company (previously Hansa Trust until its redomiciliation to Bermuda in 2019) has long offered a differentiated investment proposition to investors, with a family office approach to preserving and growing capital. It has been transformed since the arrival of lead manager Alec Letchfield, a multi-asset specialist, from HSBC in 2013. What was once effectively a UK equity fund with a large (c 40% of NAV) strategic stake in holding company OWHL – which owns a portfolio of funds (OWIL) alongside 58% of WSON – is now a diversified, multi-asset portfolio of funds (c 75% of NAV including OWIL) and global equities (c 13% of NAV), with WSON accounting for just 9.6% of assets at end-October 2020 (a little over half of the 18.4% holding in OWHL). Letchfield has organised the fund portfolio (excluding OWIL) into core regional funds (43.2% of NAV at 31 October), thematic funds (11.0% of NAV), and 'diversifying' funds (12.4% of NAV), a category that includes credit and hedge funds and aims to offer downside protection in volatile markets. As shown in the chart on page 1, these three 'silos' produced creditable performance in the three years to end-October (+25.1%, +65.5% and +8.7% respectively for core, thematic and diversifying funds), including over the difficult past 12 months, in which period the core regional funds returned 12.4% and the thematic funds 34.1%, while the diversifying funds were up 0.7%. (The drag from OWHL/WSON has reduced the fund's total NAV returns to -1.2% and -2.8% over 12 months and three years respectively to 31 October 2020.) This compares with total returns of 5.5% and 22.6% from global equities (as measured by the MSCI AC World index) over one and three years. However, the market seems to have overlooked the positive developments since 2014, with the fund's discount to NAV widening from c 20% to nearer 40% over the period.

Altering perceptions on a 'complicated' structure

It seems likely that Hansa IC suffers from a perception of being structurally 'complicated'. On one level this is understandable: it is a listed company with two classes of share (HAN/HANA) that owns 26% of another listed company (OWHL, whose ticker on the London Stock Exchange is OCN), which in turn owns 58% of Brazil-listed WSON. Both Hansa's own shares and those of OWHL trade at significant discount to the value of their underlying assets (respectively 35–36% and c 45%), to the extent that the look-through discount is c 46%. However, we would argue that it is possible to take an alternative view by focusing on the elements that are not complicated and looking at the wide discount as an opportunity rather than a threat. As mentioned above, including the funds in the OWIL portfolio, around 75% of Hansa IC's total assets are invested in third-party funds, the majority of which are open ended and therefore trade at NAV. In the main, these are successful funds run by specialist managers, giving access to some of the most popular current investment themes, such as US equities, global technology stocks and innovative healthcare names. If these themes should go off the boil then Letchfield, who has managed funds of funds for many years, could rotate the portfolio with relative ease given the underlying funds are largely liquid and tradable. Then a little over 13% of the fund is invested directly in a portfolio of global equities selected by Letchfield's colleague at Hansa Capital Partners, Rob Royle. The 19 equity holdings include well-known names such as Alphabet (parent of Google), Samsung Electronics and the Warren Buffett vehicle Berkshire Hathaway. However, Royle's value tilt has meant some of the names in the portfolio have underperformed in the growth-driven market recovery this year, while others, such as TripAdvisor and Irish drinks firm C&C, have suffered as a direct result of coronavirus-driven lockdowns. It is worth noting that the extent to which value has underperformed growth has been at historically stretched levels this year, and it would be reasonable to expect this to reverse at some point in the future. This is particularly so given recent positive news on COVID-19 vaccine candidates, which has led to swift gains in travel and leisure-related names as the market begins to believe in an eventual return to 'normal' ways of living.

If WSON is the 'elephant in the room', it is a much smaller elephant than it used to be, making up only 9.6% of Hansa IC's NAV at 31 October 2020. Letchfield points out that the only reason OWHL was ever such a large part of the portfolio was because of WSON's strong historical performance. Clearly performance has not been strong over recent years, but despite the headwinds WSON has faced from the pandemic-induced decline in global trade, a collapsing oil price and a slump in the Brazilian currency (its shares were down 9.0% in local currency terms from 1 January to 31 October 2020, but fell 35.5% in sterling terms), it has actually performed well in recent months, up c 49% in BRL terms from the low point in March to the end of September, and rising another c 3% since then (as at 18 November). Indeed, Letchfield points out that WSON came out strongly from the global financial crisis and could do so again as the world recovers from the COVID-19 shock. The company has already reinstated its H220 dividend. Brazil's stock market has tended to be highly cyclical, given its large exposure to natural resources and a shifting political backdrop, but with much of the recent global fiscal stimulus focused on supporting infrastructure investment, there is significant scope for recovery from what could prove a cyclical low point. Both the currency and the main Brazilian stock market index have already strengthened markedly since the positive vaccine news in early November.

Conclusion: Time for a reassessment?

Even if the WSON stake were completely disregarded, we argue that Hansa IC's discount would still look unreasonably wide for a diversified portfolio of quality global equities and funds (including the OWIL portfolio), chosen with an eye towards capital preservation. To put this in numerical terms, excluding the 9.6% of Hansa IC's NAV accounted for by WSON at 31 October 2020 would reduce the cum-income NAV per share from 262.7p to 237.5p, with the 169.0p closing price of the A-shares at that date equating to a 28.8% discount to the ex-WSON NAV. This compares with an 8.3% average discount for Hansa IC's chosen peer group (excluding the three UK-focused funds and Henderson Alternative Strategies, which is winding down) at the same date, within a range of a 1.3% premium to a 23.2% discount to NAV. While there can be no guarantee that Hansa IC's discount will narrow in the near future (given the long-term level and the 12-month average of 36.3%), the c 20pp differential versus the peer group average means it would be easy to argue that either or both of WSON (9.6% of NAV) and OWIL (8.8% of NAV) are effectively 'in for free'. Furthermore, with OWHL also standing on a c 46% discount to NAV, the valuation anomaly appears even greater. This may give investors some comfort that underlying value in the portfolio could be realised, particularly given the much-improved outlook for WSON and emerging signs of a move away from the 'growth at any price' mindset that has dominated global equity markets in recent years. We will publish a full review note in the coming weeks.

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Frankfurt +49 (0)69 78 8076 960
Schumannstrasse 34b
60325 Frankfurt
Germany

London +44 (0)20 3077 5700
280 High Holborn
London, WC1V 7EE
United Kingdom

New York +1 646 653 7026
1185 Avenue of the Americas
3rd Floor, New York, NY 10036
United States of America

Sydney +61 (0)2 8249 8342
Level 4, Office 1205
95 Pitt Street, Sydney
NSW 2000, Australia