Investmentaktiengesellschaft für langfristige Investoren TGV

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Dear investors

Attached, you will find the semi-annual report for the year 2019 provided by our sub-advisor JMX Capital GmbH for the sub-fund „Truffle“.

Yours sincerely

Investmentaktiengesellschaft für langfristige Investoren TGV

Semi-Annual Report 2019 of the Sub-Advisor

Dear investors,

in the annual letter 2018 I wrote:

"Over the past six months, the price development of the TGV Truffle was slightly negative at -1.9%. In the context of declines of 20% and more in many equity indices worldwide, the price development of TGV Truffle in 2018 may paint a calm picture. However, nothing is further from the truth. Over the last 12 months, the performance of the shares in the TGV Truffle has clearly diverged: one portfolio position has halved in price since the beginning of 2018 while another quotes one-and-a-half times higher. It is pure coincidence that the aggregate result across all positions was minus 1.9 per cent."

In the first half of 2019, the TGV Truffle has come out in its true colours: After a swift increase until the end of April, in recent weeks, the price has returned to the level of December 2018. My goal at this point is not to interpret these fluctuations. I would much rather like to raise awareness that significant fluctuations in equities are part of the game and do not necessarily have anything to do with the development of the underlying companies. As the TGV Truffle is invested in a small number of stocks, there will always be periods during which – coincidentally – some stocks in the portfolio will have a good while some will have a bad run at the same time. I urge you for not attach too much importance to these short-term fluctuations.

In fact, the evaluation focus must be on the development of the underlying companies, where there was little surprise in the first half of 2019. The only noteworthy news is a capital increase at amaysim (which the TGV Truffle has subscribed for). The Australian provider of customer-friendly mobile and electricity products currently sees a good opportunity to acquire new customers at attractive customer acquisition costs. It seems sensible to grow the subscriber base because, within the next few years, important supply contracts will be up for renegotiations. With increasing size, amaysim's negotiating power will also grow, and it is safe to assume that significant renegotiations of the subcontracting agreement for mobile communications in 2022 will lead to considerable cost reductions. For example, the mobile phone brand Ting of the portfolio company Tucows currently generates around 60% gross margin with a product that is almost identical to amaysim – with less than 200,000 customers in the vast US mobile communications market. Amaysim merely earns 30% gross margin in Australia with more than 1,000,000 customers (although the Australian population is 92% smaller than the US population!). The support of amaysim by shareholders like the TGV Truffle appears effort well spent and the right place to invest capital.

Measuring and Weighing

As always, please find the most important portfolio and performance data of TGV Truffle in the following table.

NAV as of 06/28/2019 in EUR	120.01
Total number of investments	13
Weighting largest investment	21.3%
Weighting Top-5 investments	62.7%
Weighting cash / fixed deposit	0.7%

Alphabetical Listing of Top-5 Investments:

Alphabet

Amaysim

Rolls-Royce

Scout24

Tucows

Period	TGV Truffle	Berkshire[1]	*(Difference)*[2]	6% p.a. Benchmark	*(Difference)*[2]
2015[3]	-12.5%	-10.0%	*(-2.5%)*	+4.5%	*(-17.0%)*
2016	+18.1%	+27.5%	*(-9.4%)*	+6.0%	*(+12.1%)*
2017	+17.0%	+6.9%	*(+10.1%)*	+6.0%	*(+11.0%)*
2018	-1.9%	+7.5%	*(-9.4%)*	+6.0%	*(-7.9%)*
2019	+1.1%	+4.9%	*(-3.8%)*	+2.9%	*(-1.8%)*
Since inception[4]	+20.0%	+38.3%	*(-18.3%)*	+28.1%	*(-8.1%)*

[1] in EUR

[2] Rounding can lead to minor deviations in the differences.

[3] 03/31/2015 – 12/31/2015

[4] Since 03/31/2015

Portfolio changes

After virtually no changes in the second half of 2018, the first half of 2019 was more busy. Especially the attractive prices of many shares around the turn of the year in connection with some inflows into the TGV led to comparatively high trading activity.

In particular, the position in Scout24 is a new and important addition to the portfolio. The company operates the advertising portals Immoscout24 and Autoscout24 in Germany and some European countries. Advertising portals (be it on the internet today or previously in newspapers) are very strong business models by nature. All providers want to be present in the advertising space where most interested parties are looking. All interested parties are looking where the most extensive range of providers is available. This creates a so-called network effect, making it hard for competitors to break into the market. Unlike other competitors in Europe and also compared to advertising budgets previously paid in newspaper advertisements, the prices of Scout24 products, despite price increases in the past, are still at a moderate level. Continuous price increases seem to be possible for many years to come. With a current free cash flow yield of around 4% and a plausible earnings growth of 10-15% per year for the foreseeable future, the investment in Scout24 looks very attractive. Add to this is the possibility of the company bidding on individual parts of the eBay Group that are for sale. Some of these parts are highly complementary to Scout24's products and should, therefore, be a very attractive reinvestment opportunity for free cash flow.

Other major changes included the sale of the TripAdvisor position and the reduction of the Rolls-Royce position.

Letting ideas burst

An outperformance on the stock market is only possible if you have a correct opinion at the time of purchase or sale that varies from the respective seller's or buyer's opinion. However, a differentiated view alone is as insufficient as making the right assumptions. The idea is to be right where it pays well – especially if the consensus contradicts your own assessment. Only then is the market price of a security inefficient and active positioning can generate excess return. Being right where your own (albeit correct) opinion is already consensus, creates no excess return. As a result, an active investor must bring along a peculiar mix of humility and arrogance.

Humility, since one must always question one's own opinion and, in reality, rarely can see things more clearly than other market participants.

Arrogance, because one must also have the courage to stand up for a different opinion to deliberately take a position against the view of the majority.

Such behaviour, however, goes against human nature. There are sound evolutionary reasons to move with the herd, not against it. Psychologically, it is far easier to be loved by all than to be the quirky non-conformist who is laughed at for their unique alternative view. The psychological pressure would be even worse if one were once so arrogant to hold and defend a different opinion but then had to abandon this point of view (driven by reasonable humility). In real life, such people are often treated with malice and ridicule. Bearing this prospect in mind, in social situations, only a few people dare to represent nonconformist theses and then hardly change them. People want to hear clear statements from their leaders and not a deliberate “on the one hand yes, on the other hand no”. We worship heroes who act decisively and boldly. Men in particular are credited with determination as a positive trait.

The stock market is shaped by the human psyche, and here, too, the same patterns as at a cocktail party apply. It is therefore extremely hard to change a decision that has been made, especially if it has been declared publicly. Among investor colleagues, one can sometimes experience highly emotional debates (or rather: polemics) about individual stocks. People *defend* their ideas instead of *questioning* them. Upon the inception of the TGV Truffle, a prominent investor who has been generating outperformance for many years gave me the advice that I should never "put my paranoia to sleep". He spoke of the paranoia of falling in love with an investment case. However, that is easier said than done, as it is extremely difficult to discard one’s former good ideas in the investment business.

In the first half of the year, there were two such ideas revisions. First, I recommended selling TripAdvisor. This was not easy for me, because I was right in 2017 with my arrogant assessment that the market misjudged TripAdvisor. Exercising humility and selling a position is not easy after making such a statement. Some new insights have emerged in recent months: the functionality of Google Maps is improving very quickly, and at the same time, TripAdvisor has put short-term monetisation over the long-term value of the customer. Though from the long-term investor’s point of view, sustainable customer satisfaction is much more important than short-term sales growth per customer. Ironically, it is comforting to know that the competitive pressure on TripAdvisor comes from another company in the TGV Truffle portfolio – in fact, portions of the amount realised from the sale of TripAdvisor were redeployed to the Google parent Alphabet.

I also had to revise my assessment of Rolls-Royce. One new finding was that over the coming years, Rolls-Royce would have to keep a significant portion of its free cash flow as cash on the balance sheet. This is perfectly legitimate to handle crises, product recalls, or to give increased security to airline customers - who in some cases conclude maintenance contracts spanning more than ten years. Previosuly, I underestimated the influence of rating agencies: Rolls-Royce will not pay any money to shareholders until the rating 'A' has been awarded. As less money goes to shareholders, my view on valuation has changed. Nevertheless, there has been no change in the qualitative assessment of the investment, and I assume that Rolls-Royce will be an integral part of TGV Truffle for years to come. Only a 10% position size based on the adjusted risk/reward profile seems more appropriate than the previous 20%.

Revisions of decisions, as shown above, appear comprehensible ex-post – but they also have a dark side. Stoic sticking to it is often the right choice, especially for high-quality companies. Most of my rebalancing recommendations are driven by price changes. A company is bought, the price goes up, and the position is trimmed to give weight to other, apparently cheaper, companies. Oftentimes, such adjustments are a waste of love, because the only crucial question is whether the stock price will be significantly higher five or ten years down the road than it is today. My last major blunder in this area was the sell recommendation for Microsoft in early 2018, at just under $ 100 per share. At the time, TGV Truffle had gained about 70% with this investment, and I saw opportunities for reallocation. Sadly, not the first time I underestimated the positive momentum of a well-developing company: today the price is at USD 130 – driven not by speculation, but by a continued decent company development. Especially if growth drivers in the business persist for a long time, selling shares due to temporarily higher prices at such companies tends to be too short-sighted.

The key to keeping great companies in the portfolio is to research a company's culture in detail to create the necessary confidence. Especially with fast-growing companies, a qualitative understanding of the "substructure" and the long-term strategy of an organization is of paramount importance. This is the only possible way to understand how long growth can be supported organizationally. A qualitative understanding of corporate culture also allows for an assessment of how a firm can cope with emerging crises. There are a number of companies for which I believe I can say something about the culture "in the depths of the organization".

The mathematician Benoît Mandelbrot coined the term “fractal”. The idea is that there are figures, each part of which has the same geometrical character as the whole. A snowflake, for example: An individual flake has the same shape as part of the flake viewed under the microscope. The best companies are like snowflakes: they have a clear pattern, a unique and consistent corporate culture. However, it is crucial for this structure to not only exist on the PowerPoint slides for investors but that the company lives and breathes this culture even in the smallest organizational units self-sufficiently. This can be discovered only by visits to different units of the company, usually over several years. Sometimes, a penny drops at a company and you know it has a particularly strong culture. In such a case, the struggle between arrogance and humility is the hardest, as it is often worthwhile to arrogantly believe in the success of the company for years.

Recommended reading

Bill and Melinda Gates are known as the largest donors in world history. With their foundation, they shape the way people return capital to society. Melinda has written an over large passages autographic book about the role of women in the world and their unused potential. "Moment of Lift" provides insights into the reality of the life of women in developing countries and offers eye-opening data. I was especially fascinated by the complex personality of Melinda Gates, who clearly has tremendously evolved as a person and shares this transformation intimately. Excellent summer reading!

Outlook

I wish you a lovely restful summer. Until the annual report in January, I'm sending greetings from Hamburg and thank you for your continued trust!

Kind regards

Jan-Hendrik Mohr