SINTRA CAPITAL

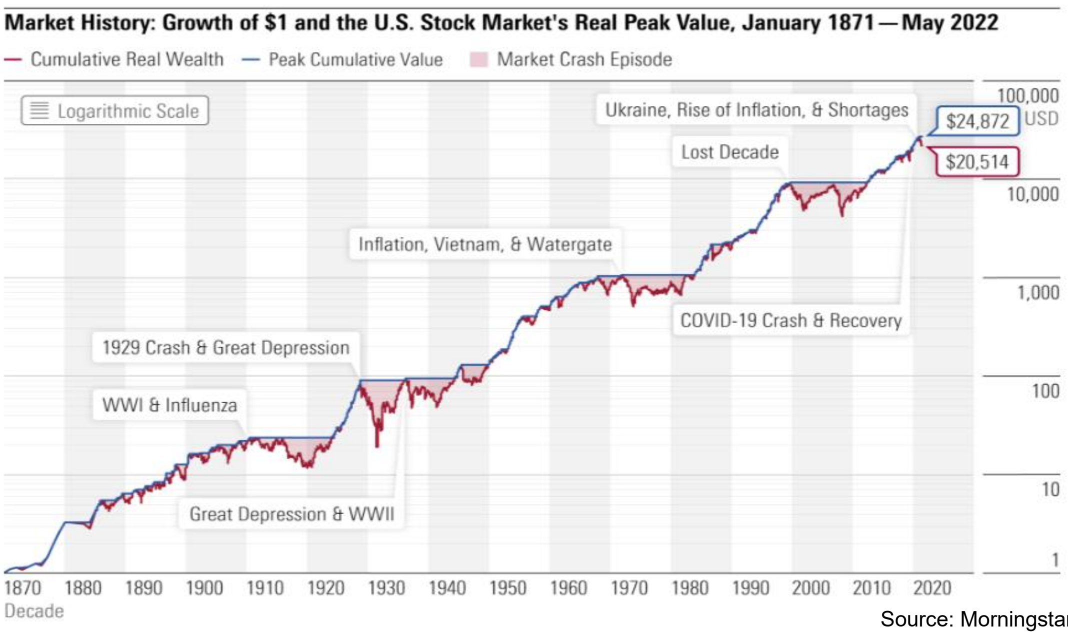
“The journey of a thousand miles begins with one step.”

The Sintra Global Fund launched on 1 July 2022 with a backdrop of rising interest rates, political friction and elevated economic uncertainty.

12 months and a few short steps later, we are pleased to report the Fund returned 13.4% (net of all fees) in its first full year.

The year provided no shortage of challenges, none more so than determining how ‘transitory’ inflation would be and how aggressive central banks would be in tackling it. The over-analysis of inflation and central bank related data points was a dominant theme. Either way, inflation is clearly moderating, and we are likely in the final stages of the rate hiking cycle. The concern now for equity markets is rates stay higher for longer. While bond markets are pricing rate cuts from early 2024, we believe this might be premature. After successfully curtailing inflation, no central banker will risk reigniting it.

This is one of our favourite charts. Over the last 150 years investors have endured wars, depressions, high inflation, pandemics, terrorist attacks and bank collapses amongst other things. Despite all this, equity markets have consistently continued to rise. Experience tells us that attempting to predict macro-economic events (ie. timing the market) is extremely difficult and does not work.



Source: Morningstar

The stock market is not the economy. It is a market of stocks. The good, the bad and the ugly. Our strategy of focusing on stocks with a superior combination of earnings growth, strong management, attractive valuation and leading industry position enables us to construct a high-quality portfolio that provides the first layer of defence during periods of market stress.

Some examples of core portfolio holdings include:

Back in December we highlighted 10 potential surprises for 2023. Number 2 on the list was "Big Tech gets Bigger." While this prediction has proved remarkably accurate (so far), it is for a very different reason. For us it was predominantly about the cloud, but this has been usurped by all things Artificial Intelligence (AI). And yes, the benefits over the next 10+ years do seem realistic. For AI to achieve its much-hyped level of success, it will require enormous amounts of data and data storage. Who is best placed to benefit? Microsoft, Alphabet and Amazon collectively hold 66% market share of the cloud computing industry.

The music industry has come a long way since the dark days of Napster. The rise of streaming services like Spotify and resurgence of vinyl has seen revenues expand significantly. Securing concert tickets to the big-name acts is not easy or cheap. And good luck getting seats at a Taylor Swift show.

The industry is dominated by three main players of which Universal Music Group (UMG) is the largest with almost 40% market share. Recent news about potential negative impacts from AI provided an excellent opportunity to increase our position. You will never be able to fill the MCG for a computer-generated Ed Sheeran or Harry Styles concert. Increased future earnings from streaming services are a major catalyst for the stock. For example, Spotify's standard pricing of US$9.99 per month hasn't changed in 12 years. In addition, negotiations are ongoing regarding a fairer split of streaming revenues for the artists that drive user engagement. Lastly, global streaming penetration is forecast to reach 11% by 2030, almost double the current level of 6%.

We started to build a position in PayPal in December 2022. This has recently started to bear fruit. While PayPal's ultra-high growth rates are in the past, revenue growth of 7% and efficiency improvements are still expected to deliver 10%+ earnings growth over the next 2-years. A recent deal with KKR in Europe to acquire up to EUR 40bn in BNPL loans reduces risk and increases balance sheet flexibility. A new CEO appointment is also imminent, bringing fresh ideas to rejuvenate a market leading business.

In addition, the parallels to Netflix are uncanny – a massive beneficiary of Covid followed by a 70%+ fall in share price as the world returned to normal and subscribers 'surprisingly' declined. Netflix addressed these "normalisation" issues by cutting costs and introducing additional revenue streams. Since bottoming in June last year, Netflix' stock price has more than doubled. PayPal is on a similar trajectory. With a net cash balance sheet and currently trading on an FY24e PE of only 12.8x, we see risk-reward skewed significantly to the upside. 432 million active users can't be wrong.

We thank you for your ongoing support and trust.

Yours sincerely,

Josh Kitchen and Tony Sutton