



Jean Pierre Verster

Portfolio Manager, Fairtree Capital





Best Ideas 2019, Hosted by MOI Global

Jean Pierre Verster
Portfolio Manager
Protea hedge funds

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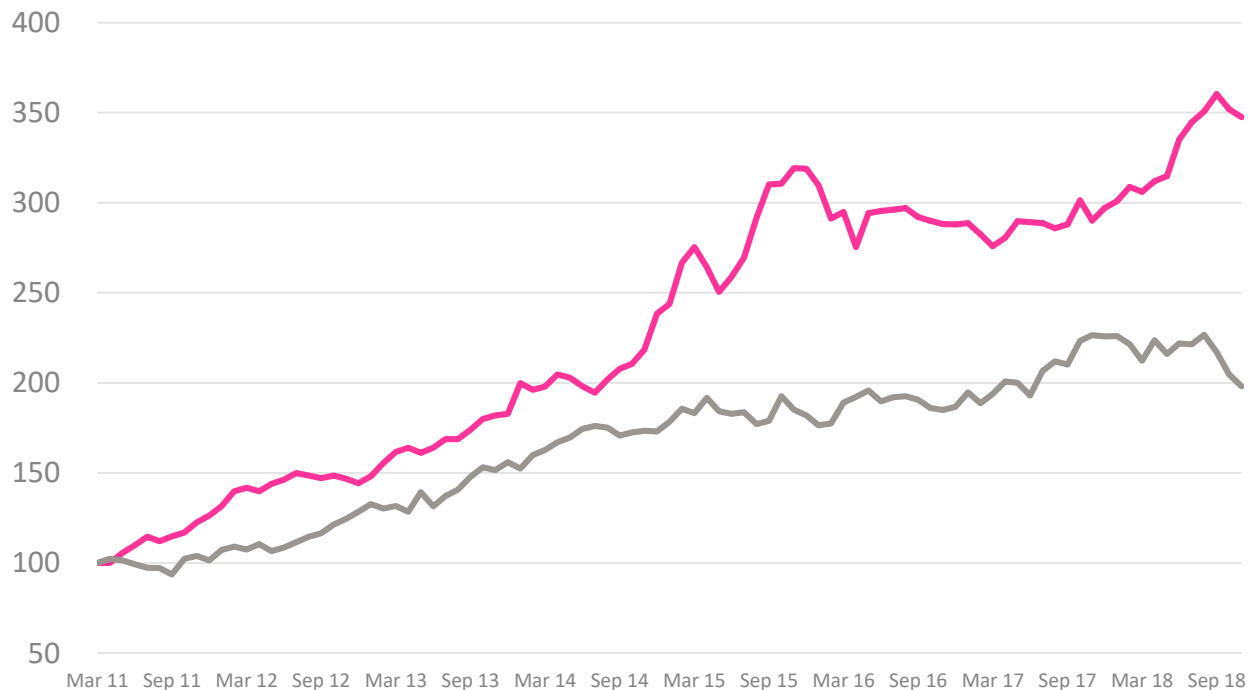
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The performance of the portfolio is dependent on the making of correct assessments of the price movements of individual securities and other investments. Financial markets have historically exhibited high levels of volatility and negative movements that have affected the price of all assets within a specific class. The portfolio's investments will thus be subject to market risk. Through financial gearing via the long/short process, the portfolio may be leveraged. This will mean enhanced positive gains but conversely can mean magnified losses. No taxation has been deducted in the computation of returns. The taxation treatment of returns is the investor's responsibility. All returns are disclosed net of performance fees.

Long-term track record

Jean Pierre 248% (17.4% p.a. net) vs JSE All-Share 98% (9.2% p.a. gross)



Investment vehicles:

- Mar '11 to May '16 = Friends & Family Partnership
- Jun '16 to Aug '16 = Protea segregated mandates
- Sep '16 to Nov '18 = Protea Worldwide Fund

Assumed fees pre Protea Worldwide Fund:

- base fee of 1%
- performance fee of 20%
- other fees of 0.4% (admin, middle office, audit)

Qualitative Fundamental Analysis



Quantitative Analysis Techniques

- **Read, read & read** – Newspapers, business magazines, trade publications, sell-side analyst reports, buy-side analysis, annual reports, investigative websites, regulatory releases
- **Assess the Management team** – Consider the people involved: their aptitude, attitude, shareholder-orientation, logic, reason, drive, strategic thinking, capital allocation skills, risk appetite, incentives, ambition and authenticity
- **Know the product/service and where it fits in the economic ecology** – Analyse competitors, suppliers, customers, threats, opportunities....classic Porter 5-forces
- **Scuttlebutt & mosaic theory** – Seek opinions far and wide and connect the dots / fill the gaps through abductive reasoning
- **Be aware of psychological biases** – Use common sense and don't fool yourself, know you don't know
- **Think** – Have time and space that is conducive for thinking deeply and clearly, get in the 'flow'

- **Financial Data** – Use Bloomberg to pull in full historical financial statements automatically into excel master model. Adjust data if necessary
- **Use algorithms** – Forecast each line item of the financials for the next 4 years, using proprietary statistical techniques (reversion to the mean, momentum & linked accounting items). Automatic base case
- **Du Pont / Gordon Growth model** – 'Translate' future full financials into fair value using robust valuation principles, discounting future cashflows at the appropriate discount rate
- **Assess outcome/fit** – Graph the Price vs Value, evaluate past 'fit' and projections for reasonability
- **Toggle variables** – Adjust inputs (model allows for multiple input toggles), see what is implied by the current price
- **Rank** – Rank the various valuation metrics of companies to compare expected returns in real-time
- **Second-level thinking** – Know what you don't know & what can hurt

Introduction

Give a Man a Fish, and You Feed Him for a Day.

Teach a Man To Fish, and You Feed Him for a Lifetime.

Best Idea

Salmar (Oslo: SALM)



One of the world's largest producers of farmed salmon

Fully integrated, highly efficient operator

US\$6.2bn Market cap, December year-end

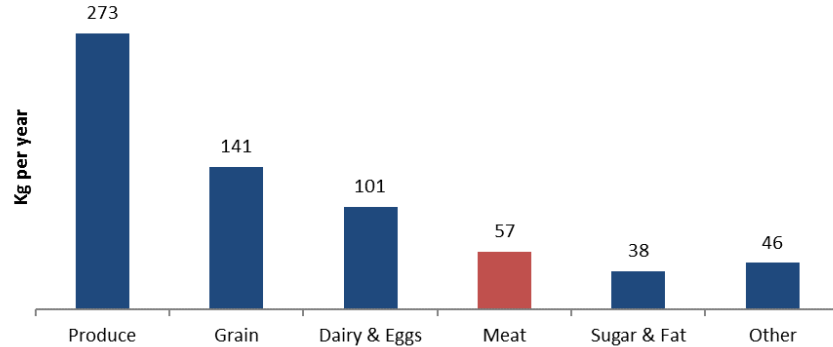
18.5x PE (17x 1-year forward)

Also see 'Best Ideas 2018' presentation by Robert Leitz on Bakkafrost

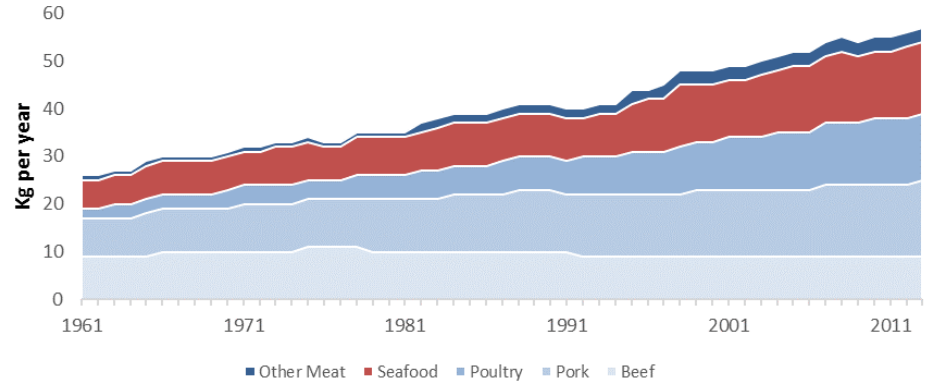
Salmar shares have doubled over the past year – can it still be a 'Best Idea'?

Global salmon industry – demand/supply overview

Per capita Food Consumption (2013)



Per capita Meat Consumption (2013)

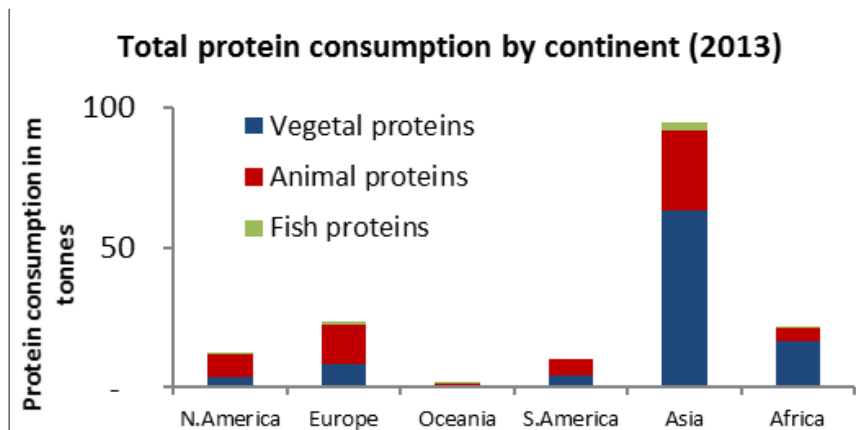


Source: Salmon Farming Industry Handbook 2018

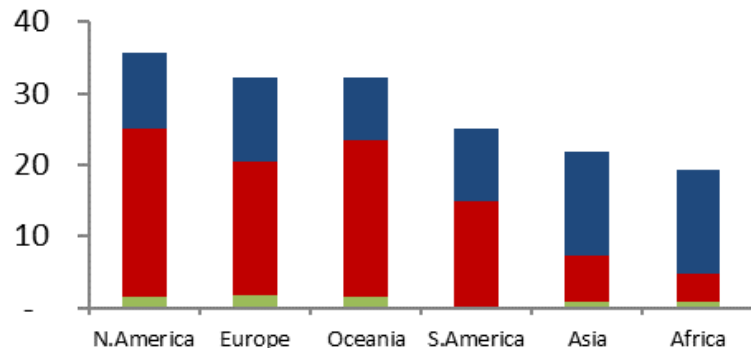
Average human eats 650kg of food each year

Global per capita meat consumption has more than doubled since 1961

Global salmon industry – demand/supply overview



Protein consumption in kg per capita (2013)

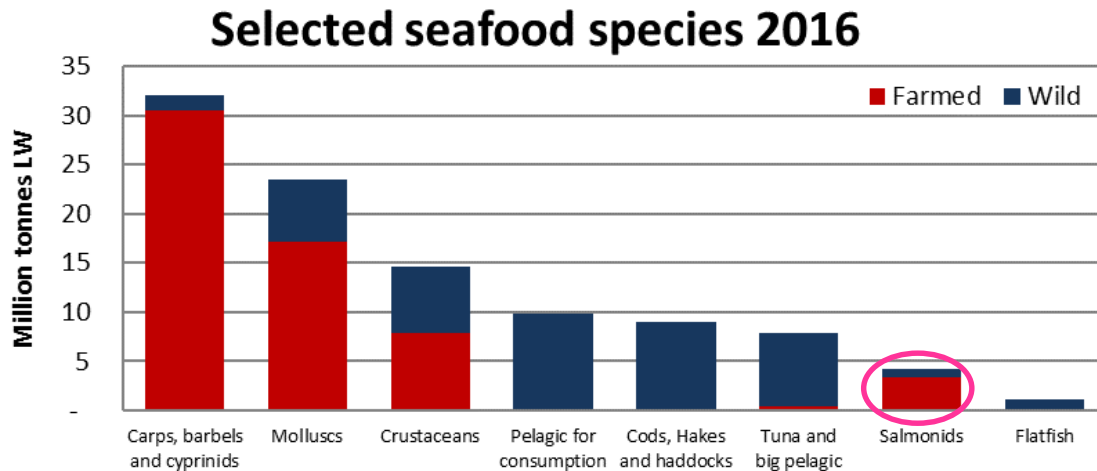


Source: Salmon Farming Industry Handbook 2018

Potential for significant increase in fish protein demand

Health & environmental benefits of fish protein versus other animal proteins

Global salmon industry – demand/supply overview



Source: Salmon Farming Industry Handbook 2018

Potential for significant increase in salmon demand *and* supply
White fish demand/supply 10x larger than salmonids

Global salmon industry – demand/supply overview

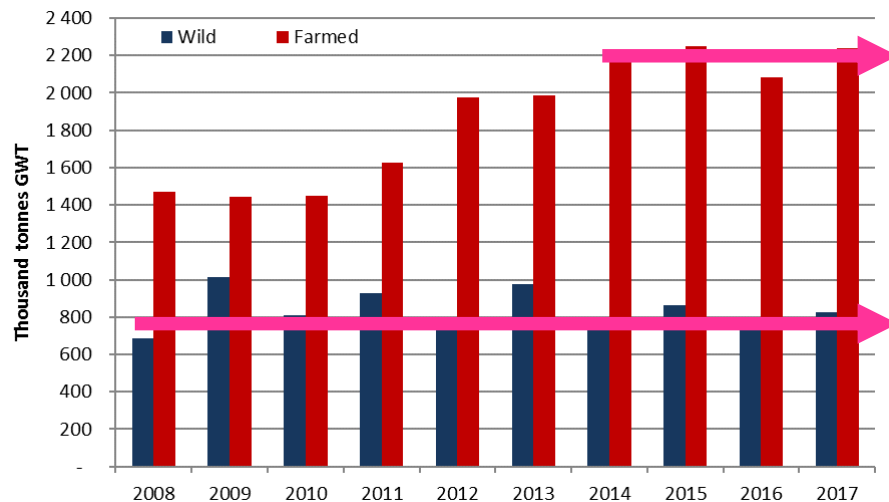


Protein Retention	31 %	21 %	18 %	15 %
Energy Retention	23 %	10 %	14 %	27 %
Edible Yield	68 %	46 %	52 %	41 %
Feed Conversion Ratio (FCR)	1.1	2.2	3.0	4-10
Edible Meat pr 100 kg fed	61 kg	21 kg	17 kg	4-10 kg

Source: Salmon Farming Industry Handbook 2018

Salmon resource production is very efficient
Feed represents around 40% of cost of production

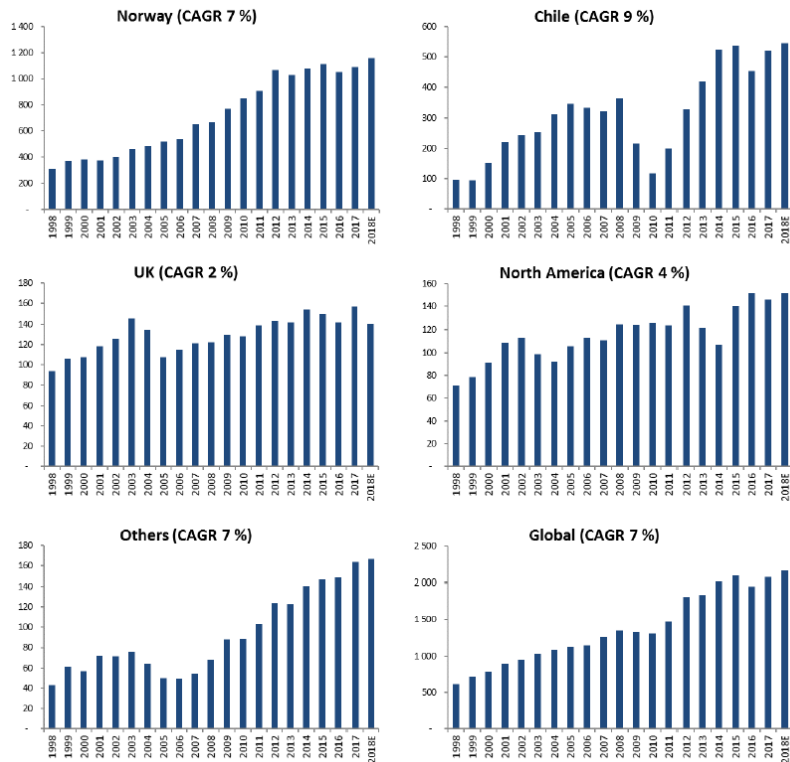
Global salmon industry – demand/supply overview



Source: Salmon Farming Industry Handbook 2018

Farmed supply has been static since 2014, wild supply for 10+ years
Current fisheries almost fully exploited

Global salmon industry – demand/supply overview



Source: Salmon Farming Industry Handbook 2018

Norway accounts for roughly 50% (1.1m tonnes) of supply

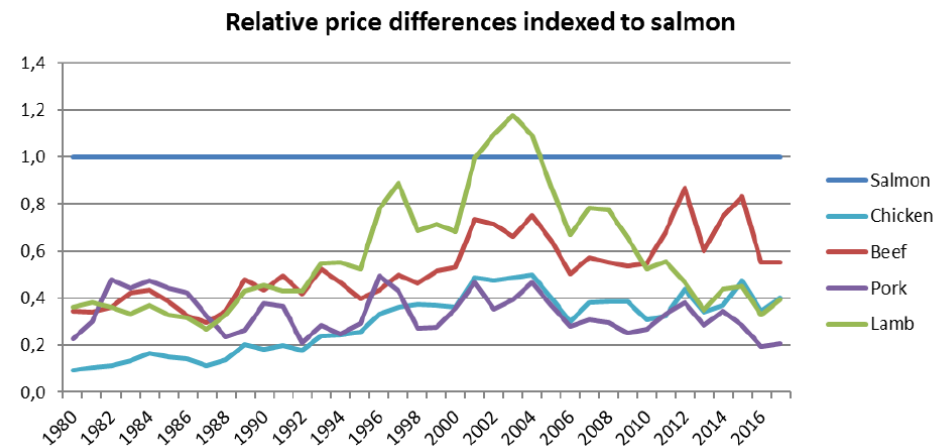
Chile 25% (500k tonnes)

Others 25% (e.g. Faroe Islands, Iceland)

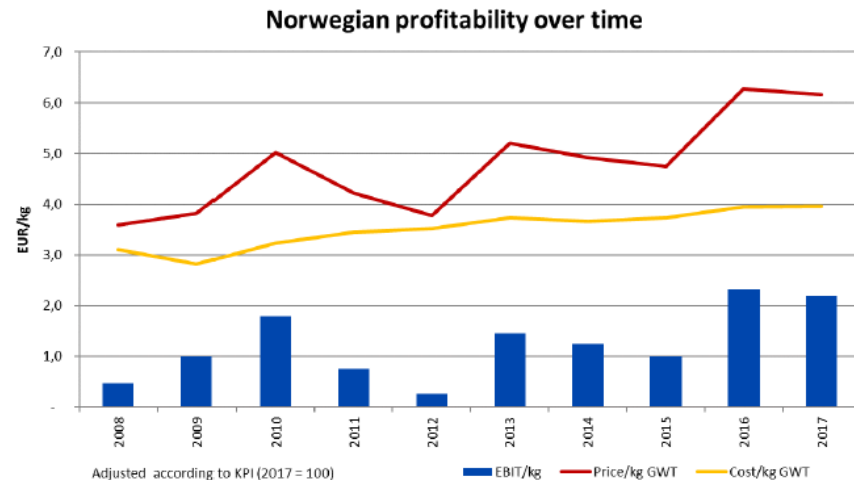
Salmon farming very temperature sensitive

CAGR	Norway	Chile	UK	North America	Others	Total
1998-2018E	7 %	9 %	2 %	4 %	7 %	7 %
2008-2018E	6 %	4 %	1 %	2 %	9 %	5 %
2018-2021E	4 %	1 %	7 %	1 %	6 %	3 %

Global salmon industry – demand/supply overview



Source: Salmon Farming Industry Handbook 2018

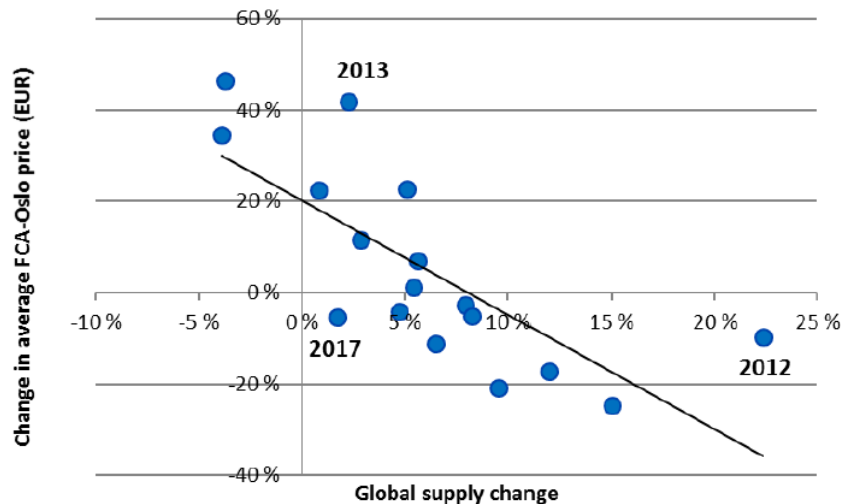


Salmon has always been a premium protein product

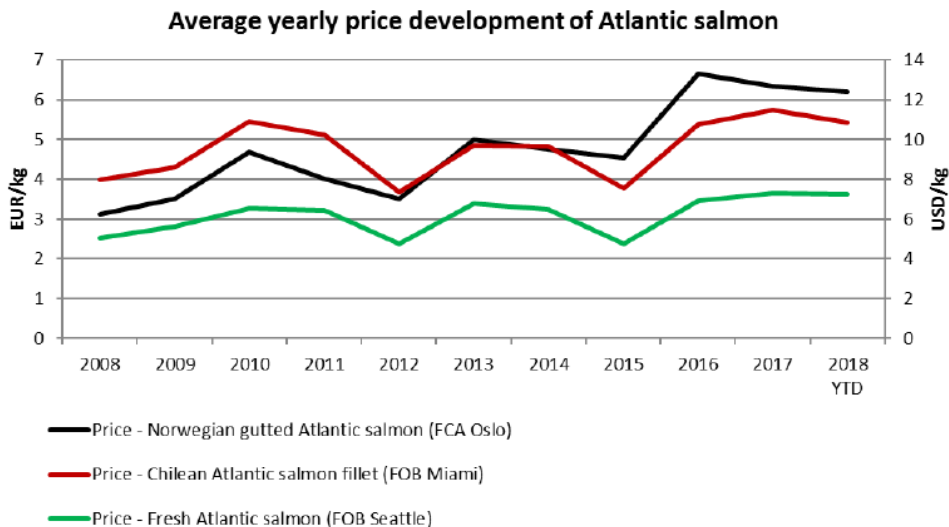
Premium to other meats have been relatively stable, except for lamb

Profitability of industry has fluctuated between EUR 0.5-2 EBIT/kg (NOK5-20 EBIT/kg)

Global salmon industry – demand/supply overview



Source: Salmon Farming Industry Handbook 2018



Salmon prices like a commodity, lower supply years associated with higher prices

NB: Constrained supply creates favourable dynamics for a consistent, low-cost producer

Consistent, low-cost producer characteristics

1. Scale to benefit from fixed cost allocation efficiencies
2. Vertical integration to control input costs
3. Widespread geographical footprint to negate concentration risk
4. High operational standards & innovation / R&D
5. Good & aligned management with a long-term mindset

1. Scale

	Top 10 - Norway	H.Q.	Top 5 - United Kingdom	H.Q.	Top 5 - North America	H.Q.	Top 10 - Chile	H.Q.
1	Marine Harvest	210 200	Marine Harvest	60 200	Cooke Aquaculture	57 000	Salmones Multiexport	58 700
2	Salmar	135 200	Scottish Seafarms	31 000	Marine Harvest	39 400	Cermaq**	54 000
3	Lerøy Seafood	132 000	The Scottish Salmon Co.	25 300	Cermaq**	21 000	Marine Harvest	44 900
4	Cermaq**	48 000	Cooke Aquaculture	20 000	Northern Harvest	12 500	Empresas Aquachile	43 300
5	Grieg Seafood	40 900	Grieg Seafood	12 100	Grieg Seafood	9 600	Pesquera Los Fiordos	41 000
6	Nova Sea	40 700					Australis Seafood	39 100
7	Nordlaks	40 000					Camanchaca	30 800
8	Norway Royal Salmon	31 900					Blumar	27 000
9	Alsaker Fjordbruk	25 000					Nova Austral	24 500
10	Bremnes Seashore	24 000					Invermar	23 200
	Top 10	727 900	Top 5	148 600	Top 5	139 500	Top 10	386 500
	Total	1 087 000	Total	156 900	Total	145 500	Total	521 200
	Share of total	67 %	Share of total	95 %	Share of total	96 %	Share of total	74 %

Note: All figures in tonnes GWT for 2017

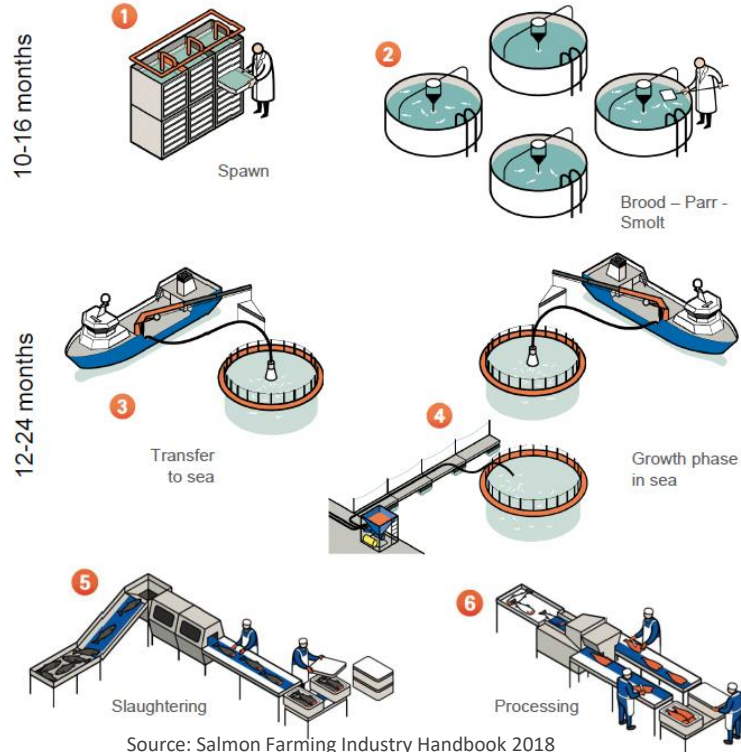
* UK and North American industry are best described by top 5 producers.

** Cermaq is a fully owned subsidiary of Mitsubishi Corporation

Source: Salmon Farming Industry Handbook 2018

Salmar owns 50% of Scottish Seafarms & 34% of Amarlax (Iceland, 3 300 eq. tonnes)
 Total equivalent production for 2017: 154 000 tonnes (7% global share). **2018: 160 000**

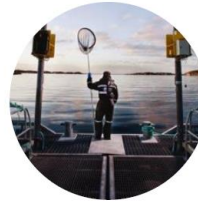
2. Integration



Genetics



Smolt



Farming



Harvesting & VAP



Sales

Source: Salmar 2017 Annual Report

Salmar is integrated from broodstock, roe and smolt to value added products and sales

Large single processing facility (InnoVar) supported by smaller processing facilities

Direct sales to over 40 countries: spot/contract

3. Footprint

Salmar farms in central & northern Norway as well as in Scotland and Iceland

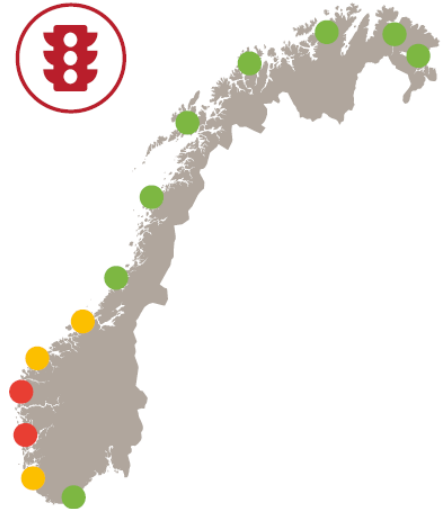
Spread is important given environmental risks, especially occurrence of sea lice

Norwegian fish licences regulated according to 'traffic light' system

Sea lice costs estimated to be up to 10% of revenue(!)

New 'development' licences have been issued

Norway's goal is to increase production to 5m tonnes by 2050 (4x)



4. Standards / Innovation

2017 mortality rate below 6% (good)

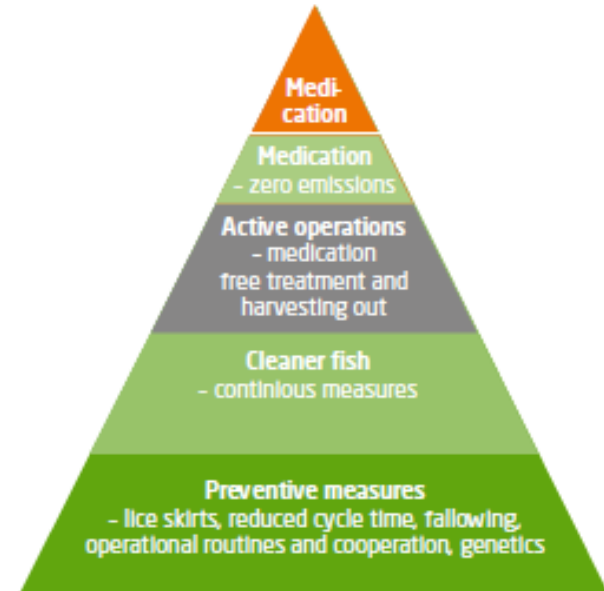
Zero antibacterials usage (from 50 tonnes in 1987)

Use of cleaner fish (lumpfish) to counter sea lice

Greater use of vegetables in feed mix (40% vs marine +-25%)

Growing larger smolts before release

Offshore fish farming developments – 2 concepts



4. Standards / Innovation: Offshore fish farming

PILOT PHASE

OCEAN FARM 1 – ENABLING OCEAN FARMING

- Successful test harvest completed at end of Q3 2018
- Remaining volume for 1st generation to reach market in Q4 2018
- Plan to release 2nd generation of smolt in 2019



UNDER DEVELOPMENT

SMART FISH FARM - ENABLING DEEP OCEAN FARMING

- Partnering with MariCulture for the development of a semi submersible production unit enabling offshore fish farming at high seas
- Applied for 16 licenses within “development license scheme”, awaiting approval from authorities
- Will largely resolve current space challenges for the industry



Significant effort lead by Salmar's founder

5. Management

Salmar was founded in 1991 by Gustav Witzøe, now 65 & Director: Strategic Projects

He restructured his shareholding but still controls around 53% of the company via Kverva AS

Has spent the last few years focused on the offshore fish farming project

Current President & CEO is Olav-Andreas Ervik, 42, previously Farming division head

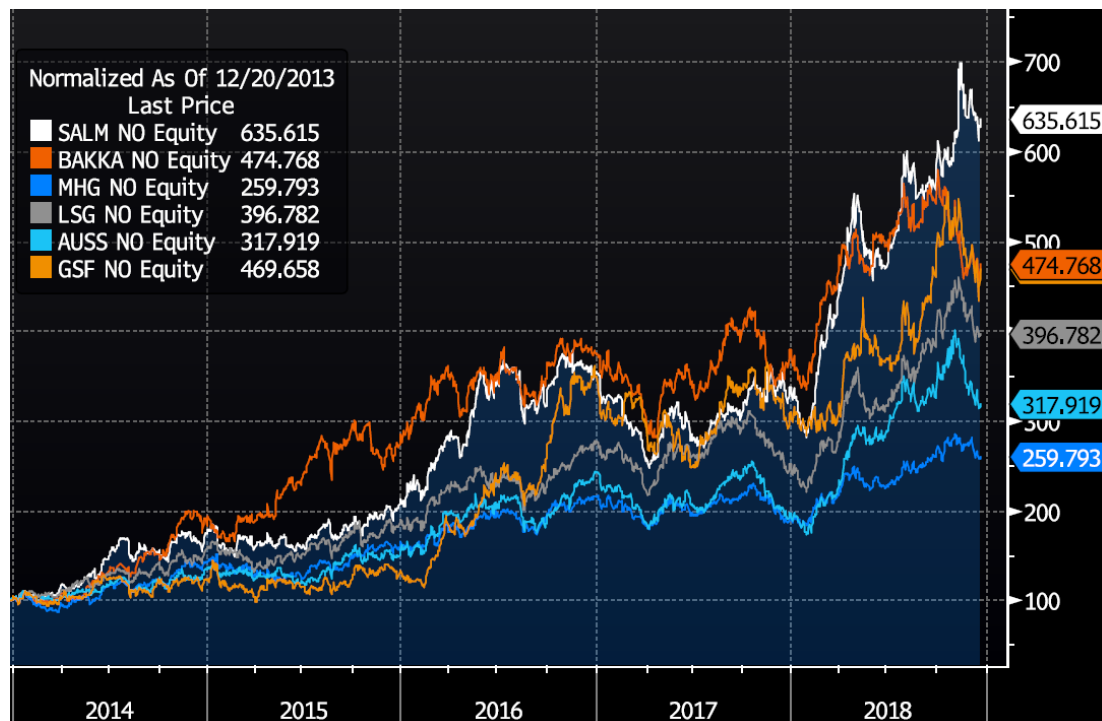
Authentic tone in annual reports, compares favourably to competitors

Consistent, low-cost producer characteristics

1. Scale to benefit from fixed cost allocation efficiencies ✓
2. Vertical integration to control input costs ✓
3. Widespread geographical footprint to negate concentration risk ✓
4. High operational standards & innovation / R&D ✓
5. Good & aligned management with a long-term mindset ✓

EBITDA margin >30%; net profit margin >20%; ROE >30%

Past performance against peers



Source: Bloomberg

SALM total shareholder return
(reinvested dividends):
Past year **113%**
Past 5 years **807% (55% p.a.)**
Past 10 years **2370% (38% p.a.)**

Great company....but is the
price still **reasonable?**

High-level revenue & cost per kg forecast

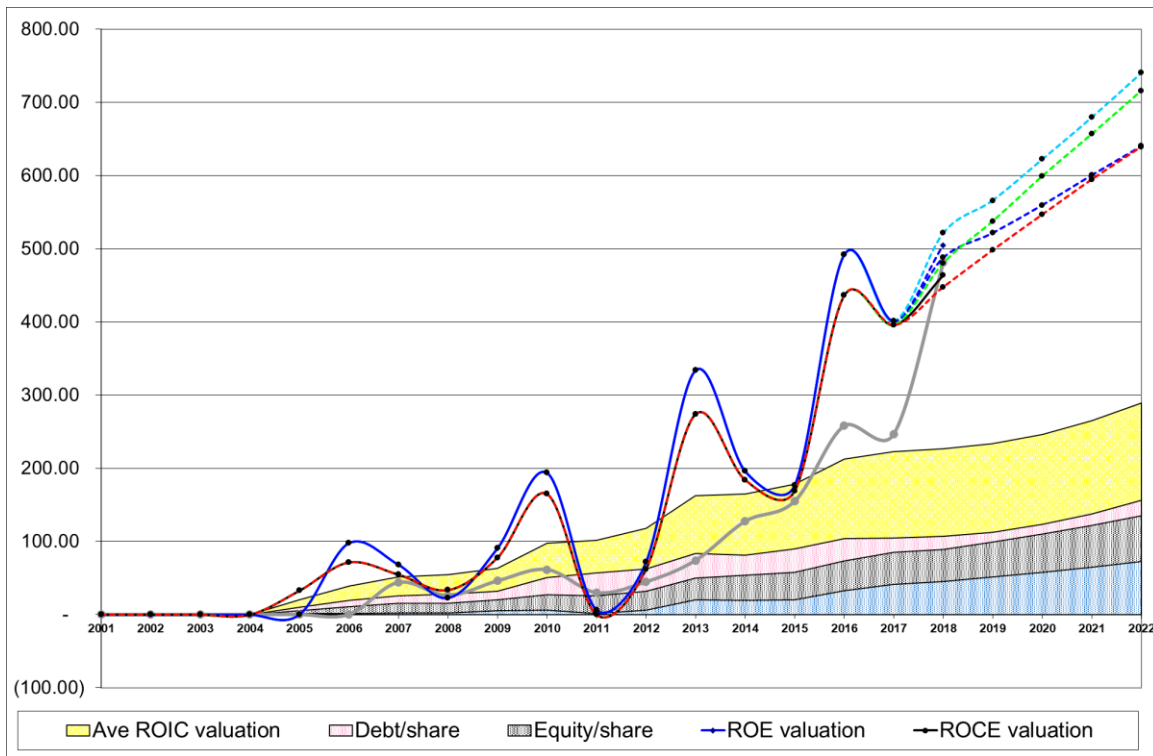
	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>2019</u>	<u>2020</u>	<u>2021</u>	<u>2022</u>
Harvest (tonnes)	102,600	114,900	141,000	145,400	115,700	135,200	143,000	145,000	150,000	160,000	175,000
Price (NOK/kg)	30	42	40	42	60	60	62	64	67	71	75
EBIT/kg	6.2	17.0	11.7	9.9	26.7	20.7	23.8	24.0	25.0	27.0	28.0
Cost/kg	23.8	25.0	28.3	32.1	33.3	39.3	38.2	40	42	44	47
EBIT (NOK '000)	639	1,949	1,647	1,444	3,086	2,792	3,400	3,480	3,750	4,320	4,900

Excluding fair value adjustments (fish work-in-progress stock marked-to-market annually)

Only exceeding 2016's peak EBIT/kg in 2021

Note interplay between harvested tonnes & price – structural real revenue growth

Valuation – graphical output of automated process



- Decelerate Revenue growth
- Fade EBITDA margin to <30%
- Net profit margin to 18%
- Keep ROE static (↓ div pay-out)
- Smooth fair value adjustments

Conservative expected return:
50% over 4 years (15% p.a.)

Upside from R&D + efficiencies

What can go wrong?

Extensive disease outbreak

Regulatory disruption

Technological breakthroughs by competitors

Costly offshore fish farming failure

Norwegian salmon pricing pressure

Other management missteps



Best Idea - recap

Salmar (Oslo: SALM)

One of the world's largest producers of farmed salmon

Fully integrated, highly efficient operator

US\$6.2bn Market cap

18.5x PE (17x 1-year forward)

Compounding intrinsic value at 15-20% p.a.



Still a 'Best Idea'!

End

“The most expensive mistake in investing is selling too soon, or thinking it is too late to buy a great company compounding intrinsic value at an above-average rate, for a reasonable price.”

Questions?

Jean Pierre Verster

Portfolio Manager

Protea range of hedge funds

verster@vodamail.co.za