

Investmentaktiengesellschaft für langfristige Investoren TGV

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Dear Investors

We are enclosing the shareholder letter for our Teilgesellschaftsvermögen “Intrinsic” for the year 2019 written by our sub-advisor CL Capital GmbH.

Yours sincerely

Investmentaktiengesellschaft für langfristige Investoren TGV

Vorstand: Jens Große-Allermann, Waldemar Lokotsch
Aufsichtsrat: Dr. Maximilian Zimmerer (Vors.), Wolfgang Fritz Driese (stv. Vors.), Alexander Pichler (stv. Vors.)
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Investmentvermögen mit veränderlichem Gesellschaftskapital

Sub-Fund Intrinsic

Annual report 2019 of the sub-advisor CL Capital GmbH

Dear Co-investors,

In the nine months after its launch on March 29, 2019, the performance of the TGV Intrinsic was + 9.2%. As of December 30, 2019, the NAV was EUR 109.16. During the same period, the Dax achieved a return of + 15.0% and the MSCI World a return of + 11.9%.

In the following, you will find an overview of the TGV Intrinsic, and I will describe my considerations as to why crises can have a positive impact on the companies in the TGV. I will also elaborate on the reason why TomTom is one of the largest positions in the TGV.

Portfolio structure and performance overview as of December 30, 2019

Portfolio structure

NAV	109.16€
Number of investments	11
Weighting biggest investment	17.5%
Weighting five largest investments	64.1%
Weighting cash	4.4%

Alphabetical listing of the five largest single positions within the TGV Intrinsic

Alphabet

Microsoft

TomTom

Tucows

Wabtec

Performance overview

Period	TGV Intrinsic (1)	Dax (2)	Delta (1)-(2)
2019 (9 months)	9.2%	15.0%	-5.8%

All companies have operationally met or exceeded my expectations since the first half of 2019. Most companies in the TGV Intrinsic were able to significantly increase their sales and profits. The Argentinian company MercadoLibre, about which I reported in detail in my previous investors' letter, continues to be the leader. In the third quarter of 2019, the company increased its sales by

70% compared to the same quarter of the previous year. This means that the sales growth has accelerated again.

In the coming years, there will also be times during which the companies in the TGV will not meet operational expectations. Every industry must experience shorter or longer-lasting crises. Such crises generate several opportunities for the companies in the TGV to develop operationally and emerge stronger. Nassim Taleb describes this phenomenon in his book “Antifragile”. According to his deliberations, systems can assume three states: fragility, resilience and anti-fragility. This concept can be applied to the corporate world. A fragile company faces significant problems during a crisis and may have to abandon its business operations. A robust company, on the other hand, can withstand a crisis much longer before it gets into serious trouble.

Antifragility, on the other hand, means that a company uses a crisis to strengthen itself. Vaccination of a human being is an example of anti-fragility taken from nature: As part of the vaccination process, humans are injected with a small dose of bacteria or viruses against which they are to be immunised. The body produces antibodies to fight these pathogens. If the body is exposed to a major attack by these pathogens in the next few years, it can fight them off due to this vaccination. There are consequently situations in nature in which a crisis means strengthening in the long term. In a similar form, in my opinion, this also applies to many companies in the TGV Intrinsic.

The following three examples show possibilities that arise for companies in the TGV Intrinsic in a crisis:

1. Organic investments – market share gains: All companies in the TGV Intrinsic are solidly financed, and some have a high net cash position. Should the level of profitability within an industry temporarily deteriorate, competitors will encounter financing difficulties, while companies in TGV Intrinsic can expand their competitive advantages by investing in innovations or marketing and increase their own market share in the long term.
2. Inorganic investments – company acquisitions: Wabtec acquires companies from the railway sector every year. Many smaller companies could get into trouble in a crisis. I expect that Wabtec will then buy at reasonable prices and provide these companies with the resources they need.
3. Investing in share buybacks: Microsoft buys back several billion US dollars' worth of own shares per quarter. Should the share price drop sharply during the next crisis, Microsoft can buy back significantly more shares for the same amount and future profits will be distributed among fewer shareholders.

Nobody knows precisely when the next crisis will hit, but one thing is certain: it will come. The companies in the TGV Intrinsic are positioned in such a way that they should emerge stronger from the next crisis. This also applies to TomTom, one of the largest positions in TGV Intrinsic. It

seems to me that many investors believe that the company is already past its prime. However, I think those times are just ahead and that is why I recommended an investment in TomTom.

TomTom – an investment in expanding network effects

For TomTom, the future began in 2008. The company had just reached a new sales peak, and in 2007, it sold 10 million mobile navigation devices. Then TomTom took over the digital map provider Tele Atlas for 2.9 billion euros and significantly expanded its own product portfolio. The company was now able to sell map data directly to automobile manufacturers.

Skipping the next 12 years, it is 2020. Self-driving automobiles will eventually hit our roads – but how are these cars going to navigate? There are two potential solutions: Every car is equipped with sensors, cameras, and software that are as intelligent as possible and can manoeuvre through all driving situations. Or the car uses a map that is accurate down to the smallest detail to locate and navigate.

There are good arguments that neither of these two solutions will dominate in the long term, but rather a mix of both technologies. The car must notice when a child is running across the street and needs cameras and sensors for this. At the same time, the map material is vital to allow for a smoother journey. For example, the data from the map will be used to reduce speed in time ahead of a curve. The map is also a safeguard in case sensors and cameras do not provide precise signals or fail.

For a car to be able to localise itself with high accuracy, it needs a high-definition map (HD map, HD = High Definition). HD maps contain significantly more information than the SD maps (SD = Standard Definition) used in navigation devices today. In addition to the higher accuracy, one of the technical advantages of an HD map is the ability to update the smallest details on the map at any time. This ability becomes necessary with higher automation of mobility because changes of streets, speed limits or new construction sites have to be kept up to date on the map at all times.

A few years ago, TomTom realised that the market leadership of HERE¹ in SD maps cannot be broken. That is why TomTom started investing early in the development of HD maps. The company's strategy paid off: in 2019, the major automobile manufacturers awarded the first contracts for HD maps. TomTom was able to secure a market share of 60%, well ahead of HERE.

Changes in the Business Model of TomTom due to HD Maps

The higher demands on the map material which I described above will lead to changes in the business model of TomTom. Today, TomTom receives a one-off payment of around 30 euros for every car sold with its map material. As soon as maps have to be updated continuously, the

¹ Was bought in 2015 from Audi, BMW and Daimler for 2,6 billion Euros from Nokia

remuneration will be converted into a subscription model and thus lead to recurring revenue (for example in the form of an annual fee per car for the use of the map material). As a result, TomTom should generate higher earnings over the operating life of a car than in the past.

Why do I define TomTom as an investment in expanding network effects? Today, the company can access more than 600 million data sources, from which map information is updated daily. In the past, anonymised movement data from mobile phone manufacturers, information from the built-in navigation systems from car manufacturers, and data from TomTom mobile navigation devices were used. TomTom has gradually expanded this data network over the years. Now, automotive suppliers supply TomTom with their sensor and camera data for creating and updating the HD maps. Road authorities enter new construction sites on the map in good time and cities provide information about street markets and other upcoming events. In the long term, the map provider with the most real-time information has a permanent competitive advantage. TomTom is well on the way to becoming this map provider.

The competitive position of TomTom has further improved in recent years: HERE was bought by Audi, BMW, and Daimler, who are in competition with the other car manufacturers. These other car manufacturers are more likely to avoid HERE as a supplier. Alphabet, with the divisions Android and Google Maps, will be represented in some operating systems by automobile manufacturers in the next few years. However, a large number of automobile manufacturers are wary of a partnership with Google, as they fear to lose a central area of value creation – in the form of contact with the end customer – to Google. As a result, TomTom is well-positioned to expand its market share. This can be seen in the successful awards of the first orders for HD maps.

A risk for TomTom is the fact that many HD map startups are currently receiving high levels of funding and could develop into new competitors. Regardless of when HD maps become commercially available, TomTom has an advantage over these potential new competitors. If HD maps achieved significant sales within a few years, an attractive market would quickly develop for the startups and TomTom. However, these startups do not currently have the financial or human resources to create a global high-resolution map. TomTom would, therefore, benefit more from the rapid marketability of HD maps. If, on the other hand, it took longer for HD maps to reach mass use, startups would only generate low sales until then and could hardly finance the necessary investments. TomTom does not have this problem. The company has been generating positive free cash flows for many years and has over 400 million euros in net liquidity on its balance sheet.

Evaluation of the HD map Opportunity

Every year, almost 100 million cars are sold worldwide, including around 40 million cars in Europe and North America – the two main markets of TomTom. A navigation device is installed for 30% of these 40 million cars. This percentage will continue to increase and will eventually reach 100% for mass production of self-driving cars because each self-driving car requires an HD

map. Due to mobility sharing in Europe and North America, it is likely that fewer cars will be sold in the long term, but in the coming years, more cars sold in Asia, Latin America, and Africa will be equipped with a navigation system. This should keep the addressable market for TomTom at least stable.

What could a valuation of the HD map field look like? With 40 million cars as an addressable market and a 40% market share², TomTom would deliver HD maps to 16 million cars. I assume an annual fee of 30 euros per car and consider a profitability of 20% at free cash flow level to be achievable. That would lead to an annual free cash flow of 96 million euros. I multiply the result by a free cash flow multiple of 15 and assume that TomTom will achieve this result in 10 years. Therefore, I discount the value over 10 years with a discount rate of 10% and get to a value of the HD map segment of 560 million euros.

The added value of a subscription model compared to a one-time transaction model is that customers from the first year do not have to be acquired again the following year. If the assumptions remain the same, the annual profit will double in the second year. Because the cars sold in the first year continue to pay their annual fee, but in addition, the cars sold in the second year also pay the annual fee. If a car were to be driven for 3 years in the future (the useful life will decrease from today's level because of the higher utilisation due to mobility sharing), this would lead to recurring free cash flow of 288 million euros³ for TomTom under the assumptions described above. This value of the future opportunity is not sufficiently reflected in today's enterprise value.⁴

In addition to the positive growth prospects, the visionary founding team at TomTom also stands out. Harold Goddijn, Corinne Goddijn-Vigreux (both executive board members), Peter-Frans Pauwels, and Pieter Geelen have demonstrated strategic foresight several times in the past and run the company with great passion. Together they hold 45% of the company's shares. Tele Atlas founder Alain de Taeye is responsible for map innovation and initiated TomTom's early focus on HD maps. It will take a few years before HD map profits are made. However, TomTom is already profitable with sales from SD cards and other services such as traffic information and is only valued at 13 times the free cash flow.⁵ TomTom thus fulfils exactly the criteria that I am looking for for the TGV Intrinsic: an intrinsically motivated founding team, excellent long-term growth prospects, and a stock market valuation that is below the intrinsic value of the company. That's why I recommended an investment in TomTom.

² Roughly TomTom's marketshare today in SD maps

³ Corresponds to the 96 million Euros free cash flow multiplied with the useful life of 3 years

⁴ Enterprise value = market capitalization – net liquidity

⁵ Based on TomTom's enterprise value

Only the long-term investor benefits from Antifragility

At the beginning of the letter, I spoke about the Antifragility of companies in the TGV Intrinsic – in other words: the possible positive consequences of a crisis for these companies. TomTom could use all of the previously mentioned possibilities to create value:

1. Organic Investments: As previously described, a crisis could make financing difficult for other companies. TomTom has enough capital to take advantage of it. By investing in sales or product innovations, TomTom could gain additional market share.
2. Inorganic Investments: In a crisis, TomTom could also use competitors' potential financing problems to acquire these competitors. Either to complement their own technology or to add more intelligent minds to the team.
3. Stock buybacks: In the next downturn, the valuation of TomTom would probably decrease. On the Investor Day in September 2019, TomTom CFO Taco Titulaer announced that the company was intensively considering the possibility of share buybacks in the near future. Since we first met in 2013, I have known Taco Titulaer as an exceptionally level-headed and rational capital allocator who is acutely aware of the potential added value from share buybacks. In that case, a lower share price would even be desirable, since TomTom could buy back more shares and future profits would be distributed among fewer shareholders.

Many investors are worried about the next crisis. I hope I have succeeded in emphasising the fact that with a long-term investment approach, crises always offer opportunities for companies. Thank you as an investor in the TGV Intrinsic for allowing me to take this long-term perspective.

On June 6, 2020, the annual investor meeting of the Investmentaktiengesellschaft für langfristige Investoren TGV will take place in Bonn. You are cordially invited, and I look forward to welcoming you there.

I wish you all a healthy and prosperous 2020.

Clemens Lotz

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