HARRINGTON PARTNERS
Investment Management

Harrington Partners Fund 1 (HPF1) – 30 June 2022

Harrington Partners goal is to compound capital over the long term through concentrated investments in undervalued high-quality companies. The Fund managers have the majority of their investable assets in the Fund, this creates a very strong alignment of interests between the managers and investors.

	HPF1 Net Return*	AOAI Return	Relative Performance
6 Months to 30/06/2014	**3.71%**	2.36%	1.35%
30/06/2015	**5.51%**	5.67%	-0.16%
30/06/2016	**11.50%**	2.01%	9.49%
30/06/2017	**10.48%**	13.12%	-2.64%
30/06/2018	**15.49%**	13.73%	1.76%
30/06/2019	**-6.45%**	11.04%	-17.49%
30/06/2020	**-4.06%**	-7.20%	3.14%
30/06/2021	**43.77%**	30.24%	13.53%
30/06/2022	**-13.91%**	-7.44%	-6.47%
Annualised Performance	**6.66%**	6.90%	**-0.24%**
Cumulative Performance	**72.93%**	76.33%	-3.40%

*Net Return to investors which is less fees and charges but includes reinvested distributions.

The Newest Harrington Partner

Before we get into the results, we'd like to introduce you to Hendrix Michael Harrington. Lucinda and Cam welcomed Hendrix to the world on New Year's Eve. Hendrix is now a happy and healthy six-month-old and he couldn't be luckier to have Lucinda who is such an incredible mother.

It's been an amazing journey caring for Hendrix and watching him grow and change over the past 6 months. His energy and curiosity for the world is infectious and his cheekiness keeps us on our toes!

We are so blessed to welcome Hendrix to the family. Having a child has certainly brought into perspective the importance of thinking long-term whilst also remaining present in each moment as they grow so fast!

Back to Business

The June quarter saw a decrease in the market prices of all of portfolio holdings which resulted in the Fund ending the financial year 2022 (FY22) with a return of **-13.91%**. The negative result potentially clouds what has been a very productive and beneficial year for the Fund overall. In fact, in terms of positioning the Fund for future value creation, we think this has been one of our best years yet. We are focused on, and encouraged by, the fact that most of the businesses we own have reported great operating results that were in-line with or exceeded our expectations.

The current market sentiment is heavily influenced by the view that rising interest rates and persistently high inflation will result in much lower or even negative economic growth. The Fund owns well capitalised businesses with strong competitive positions. As a group, we think they will steadily perform through such a period and given that almost all of them have a robust owner-operator culture, are likely to emerge even stronger than their competitors.

The Fund finished the year invested in a total of 13 companies with 81% of the total portfolio now invested in our top ten positions, and 14% in cash. Portfolio concentration has significantly increased over the past two years, as previously mentioned[1] this was out of necessity as it is just not easy finding many very high-quality companies but also as we believe that being concentrated in our best ideas will give us the highest probability of generating above average returns. The consequence to this is that if we are wrong on too many of our investments, we also have a higher probability of getting less than average results and the reason we must be very careful that the businesses we own are actually high quality and durable.

Being highly concentrated means that our portfolio is also likely to be more volatile than and less correlated to the wider market. This volatility may be positive, as it was in financial year 2021, but it may also be negative as it was this year. It should be mentioned that investing in the stock market, no matter how diversified, always has the potential to be extremely volatile over short periods and anyone who tries to tell you otherwise is kidding themselves. Nevertheless, there is now a higher probability of larger short-term swings in the portfolio value as movements in the prices of individual

[1] See the section titled *"The Continual Evolution of an Investment Philosophy"* within our March 2020 Letter.

holdings have a larger impact on the portfolio as a whole. As example of this the Fund has increased in value over the first 23 days of Financial Year 2023 by 6.13%.

As we intend to only hold between 10 to 15 positions going forward, we have decided to include all of our portfolio holdings in the table below. As always, when we feel it would be detrimental to the Fund to disclose a position, then we will just list it as undisclosed (this is usually if we are accumulating a position and we do not want to potentially create increased demand for the stock). We have also included cash as a line item and now only include Total Portfolio Weighting of each holding which creates a simpler table that is easier to understand without losing any of the previous information when total equity weighting was also included.

Our previously unmentioned portfolio investments are Berkshire Hathaway (NYSE: BRK-B), Markel Corporation (NYSE: MKL) and Costco Wholesale Corporation (NYSE: COST)[2]. We regard these businesses as three of the world's best and try hard to adopt the example they set as the standard to which we hold our remaining portfolio companies. Whilst neither of them makes up a meaningful percentage of the portfolio at this stage, we are eager to increase the Funds' ownership across all three when market prices become attractive.

The portfolio holdings as of June 30, 2022 were as follows:

Rank	Holding	Total Portfolio Weighting
1	Kelly Partners Group (ASX:KPG)	18.09%
2	Dicker Data (ASX:DDR)	9.27%
3	Field Solutions Group (ASX:FSG)	8.78%
4	Ryman Healthcare (NZX:RYM)	8.09%
5	Blackwall Limited (ASX:BWF)	8.06%
6	360 Capital Group (ASX:TGP)	7.03%
7	Servcorp Limited (ASX:SRV)	6.78%
8	Global Data Centre Group (ASX:GDC)	6.72%
9	Comms Group Limited (ASX:CCG)	6.24%
10	PPK Group (ASX:PPK)	2.36%
11	Berkshire Hathaway Inc (NYSE:BRK-B)	2.04%
12	Markel Corporation (NYSE:MKL)	1.64%
13	Costco Wholesale Corporation (NYSE:COST)	0.70%
	Cash	14.21%

Portfolio

We welcomed the drop in market prices over the June quarter as it gave us the opportunity to increase our holdings in many portfolio businesses at more attractive valuations. We significantly increased the Funds' holdings in Ryman Healthcare (NZX: RYM), Blackwall Limited (ASX: BWF) and Global Data Centres (ASX: GDC) and made small incremental investments into Dicker Data (ASX: DDR), Kelly Partners Group (ASX: KPG) and Field Solutions Group (ASX: FSG).

[2] All listed on the New York Stock Exchange

Ryman Healthcare (NZX: RYM) is a business we have owned since March 2020 and was the largest increase in position size to the Fund over the period. Due to the relative increase in value of our holdings over the past 2 years Ryman had fallen from our second largest position at time of purchase to outside our top 10 as of 30 December 2021. As we consider Ryman to be one of the best businesses that we have come across, we were eagerly awaiting another opportunity to increase our investment back to a more meaningful level. After patiently waiting over the past two years for another buying opportunity, it finally presented itself and Ryman has now become the Funds' 4th largest position. We welcome any further falls in price as we would be happy to have over 10% of the Funds' capital invested in Ryman at lower prices. Below we have written in detail as to why we own Ryman and why it has the potential to be an exceptional investment for many decades to come.

The only negative news during the period was from Comms Group (ASX: CCG). In February CCG announced a profit upgrade and then subsequently announced a profit downgrade in May, basically down to the previous expected profit levels before the upgrade. The reason for the downgrade, although needing to be monitored closely, does not change our long-term thesis for the business. It was also encouraging to see the CEO, Peter Mcgrath, purchase a meaningful number of shares on market after the fall in price.

One of the Funds' longest held investments in United Overseas Australia (ASX: UOS) was sold during the period (owned since 2016). UOS is a property developer primarily focused on Kuala Lumpur, Malaysia, and is dual listed on the Singapore and Australian Stock Exchanges. Since its founding in 1987 the company has made a significant contribution to what has been a rapid urbanisation and increase in per capita wealth across Malaysia, and in the process has created an exceptional amount of wealth for shareholders. In more recent years the company had expanded to Vietnam where the demographic profile, per capita wealth, and urbanisation rates appear primed for a comparable growth trajectory to what they have experienced in Malaysia over the previous decades. Given the proven operational talent of the management team and the company's substantial financial capacity, we expect shareholders of UOS should do very well over the long term.

Our main reasons for selling the investment are two-fold. Firstly, over the six years the Fund has owned the business the board has strangely persisted in conducting a dilutionary dividend reinvestment plan (i.e. issuing shares at significantly undervalued prices). This is even though the business consistently produces lots of free cash flow and is very conservatively financed with a huge amount of idle cash on the balance sheet. Whilst in general we like conservativeness; we could no longer accept the ongoing and in our view totally unnecessary undermining of shareholder value. The second reason is that, despite their efforts, minority shareholders have had minimal success influencing a change to this frustrating capital allocation policy as over 90% of the company is owned by management and their associates, with very little free-float available to the public. Given this long running division between our views on capital allocation we felt it was no longer rational for us to stay invested and our view is now that the only means for value to fully materialise is if there is a take-over offer for the business. We have learned many valuable lessons from this experience, in particular the upmost importance of controlling and minority shareholders having a strong alignment of interests and congruence between expectations.

Ryman Healthcare (NZX: RYM)

Ryman is New-Zealand's (NZ) largest provider of integrated retirement and aged-care villages with 38 operating locations, a further 2 villages nearing completion, and 9 sites in various stages of development consent. The company also has a meaningful presence in Melbourne with 6 operating villages, 2 villages nearing completion, and a further 6 sites at various stages of development approval. Across the two countries, Ryman has 13,200 residents and 6,700 team members.

We first came across Ryman in 2018 thanks to a memo from Rob Vinall at RV Capital that prompted us to conduct a detailed analysis which ultimately led to the Funds' first investment in March 2020. We were initially sceptical given the tendency for the industry to be riddled with less-than-fantastic operators, and that at the time our Australian centric view was severely clouded by the ongoing Royal Commission into aged-care[3]. To our surprise, in Ryman we found one of the most fascinating businesses in an area where we had least expected it, and we hope the following detail helps to communicate how proud we are to be a part owner of this uniquely great business.

About Ryman

"It's got to be good enough for Mum."

Kevin Hickman and John Ryder founded Ryman in 1984 and Kevin still remains a close consultant to the board and the third largest shareholder. The genesis for the business came about after Kevin, at the time a private detective, was appalled at what he saw when asked to investigate a rest home fire in Christchurch. In Kevin's own words the experience got him asking *"What would I want for my Mum?"* and so the Ryman ethos was born that *"Everything we do must be good enough for Mum or Dad"*.

Since the beginning the company has always aimed to build communities with a purpose, where older people can live in beautiful homes and have access to superb amenities surrounded by supportive friends and neighbours, and where they can receive the best of care if and when required. Well over three decades later Ryman has become NZ's largest and most trusted brand in the industry and serves as the model for best practice to which competitors aspire.

Our experience strongly confirms that the founding ethos remains deeply woven into the cultural fabric at every level of Ryman, and this view is supported by several objective assessments of their performance against the industry standards and competitors. For example, Ryman has achieved the NZ 'Gold Standard' 4-Year Certification of Care[4] at 91% of their villages compared to the competitor average of just above 50%, and was recently voted as the NZ Reader's Digest Most Trusted Brand in the retirement villages and aged-care sector for the eighth time in 9 years.

In Victoria, Ryman was the winner of the COVIDSafe Innovation Award from the Victorian Chamber of Commerce for their *"fabulous response that was ahead of the curve in preparedness."*. Perhaps the most telling, is both the level of their available resales stock, which generally hovers between 1-2%, or stated another way only about six weeks of annualised sales volume, and the rolling occupancy rates at their care centres, which generally hovers between 95-98% compared to 85-90% for relevant competitors.

[3] In retrospect, Ryman already met or far exceeded all of the Royal Commission recommendations.

[4] This process involves an unannounced government department audit which, if the facility passes, then results in certification for anywhere from 1 to the maximum of 4 years until the next audit is required.

A final, and extremely vital component of Ryman's culture of care, is the fairness and transparency of the underlying financial agreement they make with residents as outlined in more detail in the 'Economic Model' section below. Ryman's Peace of Mind Guarantee includes by far the lowest deferred management fee (DMF) in the industry which they cap at 20% and accrue at 4% annually, compared to the majority of competitor's who charge 30% and accrue at 10% annually, and their nearest competitor, Summerset Group, who charges 25% and accrues at 5% annually[5].

Continuum of Care

At a strategic level, Ryman is unique in that it only builds fully integrated villages in which independent living units (ILU's) and serviced apartments (SA's) surround a centralised care centre that provides rest home, dementia, and hospital level care. Each village features extensive landscaping and has a wide range of communal amenities including a bowling green, indoor pool/spa/gym, library, hair salon, café, and a movie theatre. Specialising in this type of village has resulted in Ryman becoming a world leading pioneer in the 'continuum of care' (COC) model which provides residents and their families the peace of mind that they can age in place without the need to relocate as their care needs develop.

For example, ILU and SA residents have priority access to available places in the care centre which is a significant attraction for potential residents because it ensures they can remain closely connected with their family, friends, and broader community for the remainder of their lives[6]. With the ANZ aged care industry facing a severe economic and staffing crisis, this optional access to high quality care is becoming an increasingly important priority in the purchasing decision of prospective independent residents. We think the implicit premium that is paid for this optionality will expand over time and ultimately this will help to underpin the value of Ryman's property. In NZ, multiple competitors have begun copying the COC model, but Ryman remains the only operator who is entirely committed to this model and whom has it present at all of their operating villages. Meanwhile, the COC model is particularly rare in Australia, and this is proving to be a very strong selling point for Ryman.

Vertical Integration

Ryman is really the combination of four large businesses that span property design and development, property construction and maintenance[7], property sales and management, and of course nursing and care[8]. The competitive benefits of this model should not be underestimated, particularly the differentiation that results from alignment between these disparate functions. For example, each team member, whilst a professional in their own discipline, is at heart a "Rymanian" working for the common mission of delivering all aspects of the built environment and personal care experience that are "good enough for Mum and Dad".

Economic Model

Ryman's economic model is driven by four income streams. The first of these are management fees which are charged to the residents of ILU's and SA's. Essentially this is a type of rent paid for their period of occupancy that contributes toward the unit refurbishment and village management costs. Secondly are regulated care fees which are primarily paid by care centre residents with a small

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[5] Having the lowest DMF by a wide margin and having the fairest terms in the industry also gives Ryman the ability to increase prices (in a fair manner) if their margins were put under severe pressure.

[6] On average, around 30% of care facility residents were previous ILU/SA residents. This dynamic is also beneficial for Ryman as it provides much higher certainty around ongoing care centre occupancy.

[7] Ryman has a significant internal construction management and trade team; however, they also partner with external contractors for large parts of the construction process.

[8] Ryman is also building a sizable technology division that conducts extensive R&D on the myriad of ways Ryman can improve the way it operates through adoption of innovative technologies and the analysis of data.

contribution also coming from ILU and SA residents who opt for additional services[9]. During most years the combination of these first two forms of income comfortably cover all operating costs despite the fact that the business has almost always been expanding rapidly.

This leaves the remaining income streams of development and resales margins, as the primary contributors to overall profitability. Development margins are earned from the sale of occupancy rights to ILU's and SA's at new villages, whilst resales margins are generated from the subsequent resale of these occupancy rights when one resident vacates and another moves in.

Occupancy rights confer to residents the right to occupancy of an ILU or SA for life or until the resident decides to terminate the agreement. Rymans' ILU's and SA's are priced significantly below the median house price within each village location providing great affordability for prospective residents as they tend to already own property close to the village. For example, across their Melbourne locations the average price of a Ryman ILU is approximately 47% less than the comparable area's median house price and 27% less in Auckland. This affordability gap has been expanding, particularly over the last couple of years, because the company has not raised their prices comparable to the rates of growth in the broader market. As such, we believe there is a high likelihood that the broader property market could depreciate 10-15% before Ryman comes under noticeable pricing pressure.

As mentioned above, Ryman charges management fees, which accrue at 4% per year on the face value of each occupancy right and are capped at 20% which means residents will not pay a management fee beyond the fifth year of living in their unit. When the resident vacates their unit, the occupancy right is repaid in full less any accrued management fees. Ryman records the net amount of occupancy right that are repayable to residents as a liability known as an occupancy advance, which today stand at just over $4.86 billion. This interest free source of capital has enabled Ryman to rapidly grow their number of villages whilst remaining conservatively financed and without the need for additional equity since listing in 1999.

In the past the sale of occupancy right has been sufficient to fund their growth with only a relatively small amount of debt capital required. However, In the last several years Ryman has been focused on meeting the oncoming wave of demand by building more villages each year that are much larger and in significantly higher value locations (over the previous four years the number of villages under construction has increased from 4 to 16). As a result, the company has required a lot more upfront debt funding which will be progressively repaid by incoming occupancy right income as completed villages are sold down. In essence, the financing from the interest-bearing bank debt will be replaced by interest-free occupancy right financing and Ryman can then recycle a large proportion of the capital into further growth. Given rapidly expanding demand and Rymans industry leading reputation, we think the likelihood of being left with a significant amount of unsold stock is highly unlikely, and hence the risks posed by the debt and occupancy advance liabilities are relatively low.

There is the potential for meaningful risk with this business model in terms of capital deflation if property prices decline significantly and stay low for a long time, along with possible liquidity pressure if Ryman is unable to resell a large number of vacated units. Fortunately, the company has a number of inherent characteristics that should help to meaningfully offset these risks. The first of these is the consistently stable tenure of residents, which currently stands at 7 years for ILU's and 3 to 4 years for SA's, resulting in a very manageable amount of annual occupancy right resales as a percentage of their total portfolio, which helps to ease the capital depreciation and liquidity pressure within any one year.

[9] Most residents utilise their government aged pension allocation to pay a large proportion of their care fees.

For example, over the last ten years the average annual number of occupancy right resales as a percentage of the total retirement unit portfolio have been approximately 13.6%.

There are a substantial proportion of residents who make the decision to move into a Ryman village based on their current needs and/or their desire to confidently age in place and receive top quality care when required, rather than a purely lifestyle decision. In the past Ryman has benefited from a consistent stream of new residents despite prevailing property market dynamics, and given the demand, we think this is likely to continue. The material discount that exists between the price of Ryman's ILU's and SA's and their comparable suburb median house prices also provides considerable protection from pressure on the broader property market. We believe the combination of these characteristics should see Ryman comfortably navigate both tough economic periods and challenging property markets.

In aggregate, the Ryman economic model has been brilliant for residents, their families, team members, and local communities, it has also worked phenomenally well for shareholders. In 1999, at a time when the company had just over 1,000 residents, Ryman publically listed raising $25m resulting in total assets of just $103m. Nearly twenty-three years on, the company has grown to over 13,200 residents supported by total assets of $10.97 billion, and has paid out approximately $1.14 billion of dividends to shareholders *without ever raising another dollar of equity*.

Ryman's Investment Potential

During the previous 23 years as a publically listed company Ryman has proven to be a truly outstanding long-term investment. High quality aged care provided across a beautiful communal setting - which is at the core of what they do - is a base human need which is almost certain to witness a rapid and sustainable increase in demand for many decades to come and has a low probability of disruption risk. It must be acknowledged that the near 35-year bull run in property prices across the two continents has been a significant contributor to Ryman's financial performance, and the price dynamic over the coming 35 years is unlikely to be as favourable. **In the near-term, we do expect downward pressure on property markets and therefore pressure (but to a lower extent) on Rymans development and resales margins**. Fortunately, this pricing pressure is likely to be offset by a meaningful increase in resales volume as the portfolio continues to mature[10] along with an increase in the annual build rate to well over 900 units. Additional support will come from the fact that the current development pipeline is concentrated in higher value locations with more affluent populations wherein affordability is in general less of an issue. More broadly, the generation that is increasingly seeking out high quality operators like Ryman is the wealthiest in history and the average current or prospective resident tends to have significant property and/or superannuation wealth with little to no debt. As a result, we think that price sensitivity is likely to be much lower within Rymans' target cohort than it is across the broader property market.

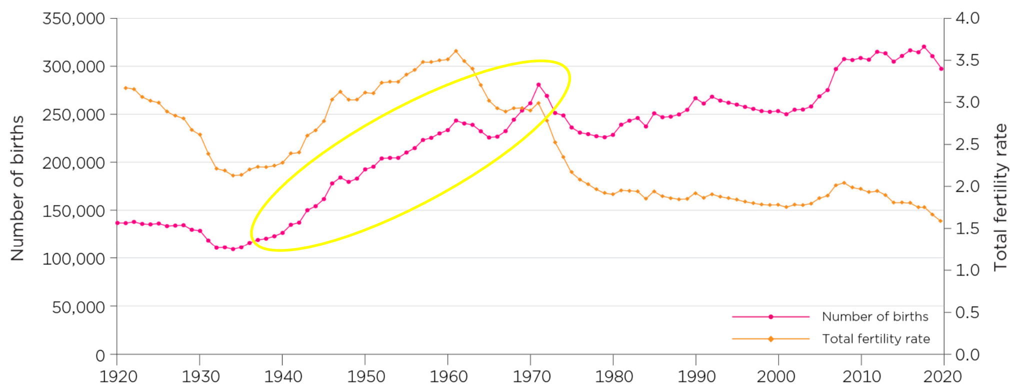
Growth

As at the end of March 2022, the average age of new residents moving to a Ryman village was 79.3 for independent living units, and for 85.7 serviced apartments, whilst the average age of *current* care centre residents was 86.8. We can see from the graph below, which shows Australian birth rates over the last 100 years[11], that there was a profound acceleration beginning in the late 1930's that saw more

[10] Around 50% of Ryman's villages are yet to reach maturity which occurs after 6-7 years.
[11] We are using the historical Australian birth-rate as a proxy for all of ANZ as they are similar.

than a doubling of the birth rate from around 125,000 to a peak of around 275,000 by the early 1970's[12] (as highlighted in yellow).

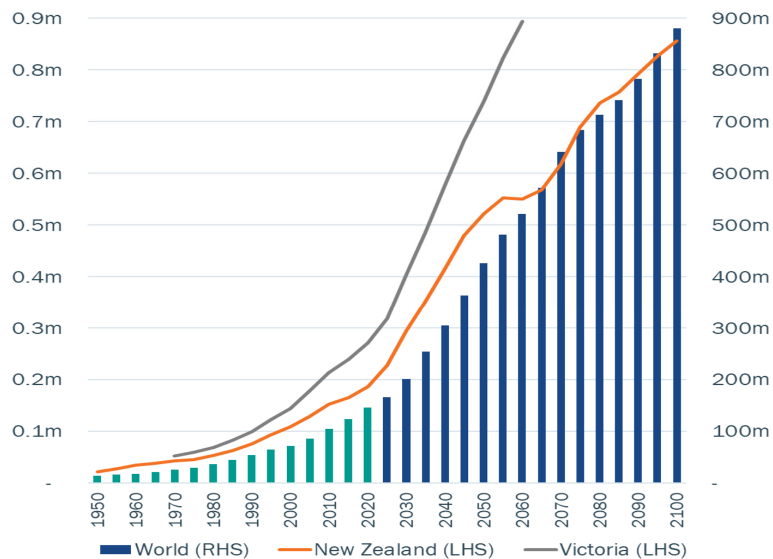
Figure 1: Number of births and total fertility rate, 1921–2020



Source: https://aifs.gov.au/research/facts-and-figures/births-australia

The first generation of this cohort is today in their early to mid-eighties, directly in line with Rymans target market, and the absolute and population relative size of this cohort is set to continue expanding rapidly for at least another 30 years before stabilising to a somewhat more manageable incremental growth rate from 2050 onwards. Figure 2 below illustrates Ryman's own internal growth expectation for the 80 years + cohort across their operating locations of NZ and in Victoria (LHS) and the rest of the world (RHS).

Figure 2: World Population Growth 80+



Source: United Nations World Population Prospects 2019, Australian Bureau of Statistics (Series A). Victoria data projections end 2060.

[12] The first of the Baby Boom generation is considered to have been born in 1946, as this aligns with the end of World War II, however the graph clearly illustrates that the birth rate was on a sharp rise several years earlier.

These graphs help to illustrate the sheer significance of the impending challenge most developed societies face in providing high quality infrastructure and care at scale for this rapidly expanding cohort. Unfortunately, there are few societies across the world that appear comprehensively prepared for this challenge. Within the ANZ region, we are already seeing wide-spread industry consolidation as escalating clinical, administrative, compliance, and staffing costs and shortages are giving many smaller providers no other choice than to merge or shut down. This is particularly true of standalone care providers who do not have the benefit of recurrent capital proceeds from the sale of ILU's and SA's to bolster their cash flow. If there is any company suitably equipped to step-up to this challenge and thrive in doing so it is Ryman as a pioneer of large integrated villages.

Competitive Advantage

Culture

We pay utmost attention to how a company behaves during a crisis because during these times the authenticity of their stated values will be revealed. The aged-care industry across the globe has been at the epicentre of the COVID-19 pandemic and the performance across the industry has uncovered widespread lack of preparation with the attendant devastating outcomes for residents and their families. Ryman has risen to this challenge and excelled every step of the way, and in doing so has comprehensively met their stated values of prioritising care and kindness in everything they do.

Since January 2020 Ryman has directly invested over NZD$70 million[13] protecting their residents and team members from COVID-19 and because of their efforts all of the care centres remained Covid free whilst only a very small number of their independent residents contracted the virus. To provide context, this investment equates to around 15% of the total underlying profits Ryman has generated over the previous two financials years. We think it is in the best interest of long-term shareholders when a company is willing to sacrifice short-term outcomes to stay true to their values, stakeholder commitments, and longer-term objectives. Below we have listed some of the initiatives Ryman has taken since the onset of COVID-19 to care and protect their most important stakeholders, residents & their families, and Ryman village team members.

> For Residents and their Families:

- Ryman's clinical governance committee, which includes a microbiologist/infectious infection control specialist, alerted the board to the COVID-19 risk in early January 2020, well ahead of the relevant government authorities. The company immediately stocked up on personal protective equipment (PPE), implemented a comprehensive visitor check-in and screening process, and restricted village travel from anyone who had been to a hotspot region. As a result, Ryman experienced minimal impact from subsequent PPE shortages and has been able to keep their villages essentially COVID-19 free.
- Project Safe Haven was launched in early 2020 that was designed to provide peace of mind for residents and their families that Ryman villages were safe havens. This included the provision of essential services to all independent residents, so they did not have to leave their home. Initiatives included tens of thousands of deliveries of both groceries and 'happy hours in a bag', the establishment of dedicated wellbeing website and internal well-being team who made regular check-in calls to residents, deployment of video calling across care centres so residents

[13] The company also voluntarily opted to repay the NZ government's $19.8 million wage subsidy received as a temporary measure to support businesses such as Ryman, so the $70m is a true net investment.

could stay connected to their friends and family, and the scheduling of regular social and entertainment (virtually).

> For Ryman village team members:

- Increase the hourly pay by $2 and provided uncapped paid special leave for people with or recovering from COVID-19 with a total 110,000 hours of this leave being provided thus far, whilst also provided remuneration for anyone who had to cease working at another facility to comply with Ryman's one village requirements during the height of the pandemic. In addition, team members recovering from the virus were sent 'recovery packs' and received 'wellness calls' from Ryman's People and Culture team to make sure they were ok and if any assistance was required. In Victoria, the company applied for the healthcare retention bonus which was approved and paid to all team members.
- Provided over 3,000 meals every day along with 'hydration stations' that were equipped with electrolytes and nibbles to ensure team members wearing face masks and shields were taking micro breaks every hour to stay hydrated and nourished.
- Allowing team members to move-in to villages as a means to avoid close contact with their family members or housemates who had the virus or were in mandatory isolation.

Reputation

Ryman has long been the most respected provider of aged care in the NZ market and is fast building a similar reputation in Australia. This is vitally important to their competitive advantage because one of the biggest drivers of development and resales are the delighted recommendations current residents and their families give to their friends, who are often potential residents themselves, and their families alike. This recommendation effect is strong at both a national and regional level (primarily in the case of NZ) and particularly powerful at a local level given that potential residents in any given area have been part of that community for a long time. The tangible value of Rymans reputation was illustrated by the take up of their first village in Melbourne which sold much faster than expected, with less marketing and at higher prices than budgeted.

Economies of Scale

Ryman benefits from several scale efficiencies that meaningfully lower their cost of doing business. Of particular importance is the reputational and capital backing that their internal development team can leverage to secure some of the best sites within traditionally tightly held and scarce metropolitan infill locations. These sites offer the most attractive proximity to dense and affluent populations generally resulting in a faster upfront sales process, and, in theory, less capital risk as resales progress over time. Their ability to support a dedicated design and construction team has resulted in a high level of expertise when it comes to optimising building layouts and construction techniques[14]. The sheer size of their operating portfolio along with the breadth of the development pipeline means they have a strong volume purchasing power across healthcare related consumables, construction materials, and external contractor rates. The internal People and Culture team provides significant advantage in the company's ability to attract, train, and retain great people, which, in combination with the skills of their IT team, has helped to significantly reduce the overall staffing and rostering challenges that is a serious issue faced by the broader industry.

A great example of what Ryman can achieve when they leverage their scale and vertical integration was the development of the proprietary technology app known as *MyRyman Care* which took NZD$40m to develop and implement across their village network. Each resident has their own tablet

[14] This is important given most projects require multiple amendments as part of the development consenting/approval.

which is securely linked to *MyRyman Care* and provides nurses and carers with resident specific details such as up-to-date clinical data, critical medical alerts, detailed care tasks, and personal preferences. Management estimates that MyRyman has enabled nurse's and carers to spend an extra 20% of their time being face-to-face with residents because they no longer have to spend considerable time scribing hand-written notes into a centralised computer network, whilst also significantly reducing the time required for shift handover, internal communication, and training of new team members. The readily accessible and interactive tablet interface also enables residents and their families to be more involved and informed about their care[15] further improving trust and peace of mind.

Most important is Ryman's ability to cumulatively leverage each individual scale and vertical integration advantage to provide some of the highest quality infrastructure and care whilst also being strongly profitable[16]. Ryman's structural advantage of being one team driven by aligned values, that collaborate across complimentary skillsets, and all work toward a common goal will be of crucial importance in meeting the monumental task of developing new aged-care infrastructure and the care teams necessary to meet escalating demand. We think Ryman has an exceedingly difficult to replicate cultural, reputational, and structural flywheel that will result in increasing competitive strength as the industry continues to consolidate. Further, it appears almost inevitable that financially and operationally stretched federal and state governments will have no choice but to rely on the likes of Ryman for the provision of this critical infrastructure and service delivery.

Management

At the time of our first investment Ryman was capably led by CEO Gordon Macleod who had been with the company for 15 years, along with chair and meaningful shareholder Dr. David Kerr who had served on the board for over 25 years. David had overseen Gordy's development along with Simon Challies before him, and founder Kevin Hickman before that. Each of these gentlemen were absolutely brilliant leaders who had the love for Ryman running through their veins. Unfortunately, Gordy recently retired, and David has stepped back from the board but remains a close advisor to the clinical governance committee. The new group CEO is Richard Umbers, with newly created dedicated CEO roles in both NZ and Australia, respectively filled by Cheyne Chalmers and Cameron Holland.

Whilst we think Richard, Cheyne, and Cameron are all very capable leaders that appear to fully embrace the Ryman way, they all have relatively short tenures at the company, and Richard is the first external hire of a group CEO. In general, our preference at successful businesses is always for the board to prepare well in advance for, and to only make, internal promotions especially for the important leadership positions. In our experience, this tends to correlate with a continuation of the thriving culture and also signifies that the company is likely to be developing high quality talent right throughout the organisation. The fact that Ryman have not been able to promote sufficient internal talent for these positions is somewhat of a concern for us, and we are closely watching how the new members of the management team develop. We are on alert for any meaningful shifts away from honouring the fundamentals of Ryman's purpose driven culture of care and kindness.

The current board has a comparatively long tenure and a good amount of skin in the game, especially non-executive director Geoffrey Cummings who is Ryman's largest shareholder and has been involved with the business for well over 30 years. We are also encouraged by the unique rationale provided to shareholders from more recent board appointments such as Andrew Leighs (2018) and Paula Jeffs

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[15] Residents also reportedly love the ability to read, game, surf the web, and communicate via video with their friends and family all through the tablet upon which MyRyman is enabled.

[16] Ryman is one of a few companies' that legitimately excels at what business researcher and author Jim Collins calls the "Genius of the AND", whereby a business embraces (as opposed to trading off) two generally accepted extremes across a given dimension – in Rymans case, very high-quality resident care + team member fulfillment *AND* very strong profitability.

(2019) who both spoke at length about their eagerness to join Ryman because of its values, importance of its mission, record of success, reputation, and the scale of the challenge ahead. Overall, we believe that responsibility for nurturing the Ryman culture is in great hands and there is a first-class team of leaders who will steward the company through many more periods of great success.

Intrinsic Value

At the time of writing the company's market capitalisation was approximately NZD$4.4 billion, resulting in an earnings yield of a touch under 6% based on the FY22 underlying earnings of NZD$254 million. We think this is an attractive starting point given the resilience of Ryman's long-term growth profile and proven ability to compound at high rates without the need for fresh equity, hence the reason it already accounts for 8.09% of the HPF1 portfolio.

In the near-term, we expect Ryman can offset a meaningful amount of the headwinds posed by declining property markets[17] and ongoing inflationary pressures through a sustained increase in the number of development and resales, and the continuation of rising care & management fee earnings. However, the likely pressure on development and resale margins, along with a much higher cost of debt, is likely to result in subdued profit growth as the headwinds work through the system over the coming 2-3 years. In theory, Ryman has several levers it could pull to quickly improve profitability, such as raising DMF's and care fee premiums, but we think these actions should and would be a last resort. In this regard, we are encouraged by managements contention that they are focused on further operational improvement and innovation as the primary means to sustain and improve operating margins.

When we consider the near-term challenges as just one chapter of an investment in Ryman over the coming decades, they fade into somewhat inconsequential. Ultimately, we think profits will march up strongly over the long-term and as a result shareholders are likely to earn a great return on investment from current levels.

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We are privileged that you have chosen to partner with us on this journey. As always, we welcome any feedback and if you have any questions, comments or investment ideas please do not hesitate to contact us.

Yours Sincerely,

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[17] Our view is that price declines across Ryman's property portfolio will be much less than the broader property markets given their portfolio's needs-based characteristics, low relative price points, and wealth of their target market.

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