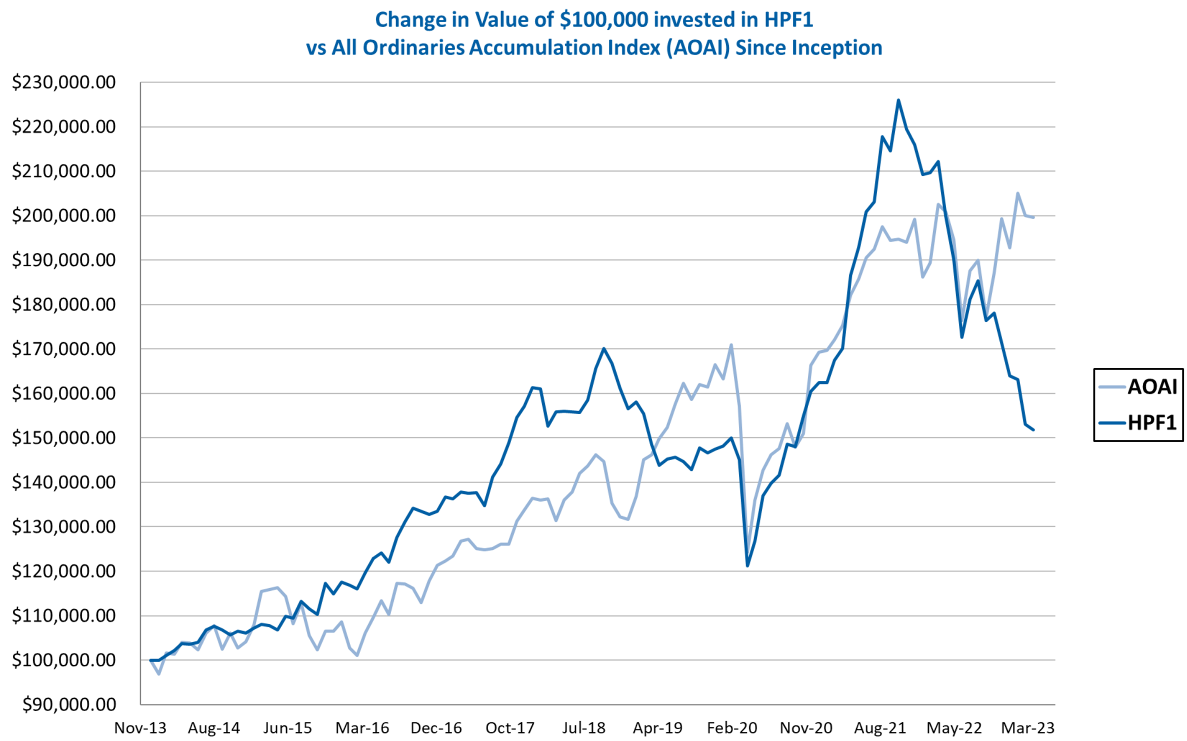
Harrington Partners Fund 1 (HPF1) – 31 March 2023

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, creating 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%
29/06/2022	**-13.91%**	-7.44%	-6.47%
9 Months to 31/03/2023	**-12.05%**	13.60%	-25.65%
Annualised Performance	**4.64%**	7.80%	**-3.16%**
Cumulative Performance	**52.10%**	100.31%	-48.22%

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



The market prices of the Fund's holdings fell by a collective 7.49% over the third quarter of FY23 finishing the 9 months to March 31, 2022, down **12.05%**.

We've previously mentioned that we would no longer routinely write about the Fund's relative returns to that of the AOAI, but considering the recent large performance divergence, we feel some commentary is warranted. Due to the concentrated nature of our portfolio greater volatility is to be expected and we are not concerned with significant short term performance divergence against the broader market. However, the Funds annualised returns, on both an absolute and relative basis, are currently not satisfactory and are well below where we can be objectively convicted that we are adding value for our investors. We believe the quality of the companies that account for the bulk of the portfolio should underpin improved returns, and we will lay out the reasons for this in detail within the full year letter.

The 20% share price decline of our one of our largest holdings, Dicker Data (ASX: DDR) along with a 38% decline from Field Solutions Group (ASX: FSG), contributed the bulk of the period's negative performance. Again, the concentrated nature of the portfolio, particularly in the largest holdings, means that any significant changes in share prices will have considerable impact on the Fund's overall performance. As we've stated many times before, the market price of a business, in and of itself, tells us little about the value of the business. The most important thing to focus on are the value of the underlying economics and whether the per share value is increasing or decreasing. We believe Dicker Data in particular, continues to meaningfully increase their per share value.

The market reacted negatively to DDR announcing that their net profit after tax was essentially flat in the twelve months ending December 2022[1], despite revenue and gross profit increasing by 25% and 23% respectively. The flat profit was largely due to factors outside of managements control which increased operating costs without any offsetting benefit, as outlined in the annual report by the founder and CEO, David Dicker:

> *"Ongoing challenges from factors outside of our control that could not have been predicted, expected, or avoided in any meaningful way, did weigh on our final outcome for FY22. Rising interest rates, inflation and other factors increased our cost of operations with no upside. Despite this, we delivered on our gross margin guidance and finished the year ahead of our competitors yet again. I remain optimistic about business conditions and the company's ability to generate another strong result in 2023."*

David alludes to two key points that are of crucial longer-term importance to DDR, being that they maintained their pricing discipline (gross margins) *and* increased their market share of the information technology sector by 2% in Australia to now be 35%, and by 1% in New Zealand to now be 28%. What isn't mentioned is the fact that DDR also spent a considerable amount of time and money during 2022 integrating two meaningful acquisitions[2], whilst also planning for and giving the go ahead to expand their onsite warehouse capacity by 70%[3]. In particular, the acquisition of Hills Security & Information Technology has propelled DDR to the market leadership position in an entirely new (but skillset aligned) market of physical security product distribution.

Historically DDR has delivered extended periods of strong profit growth following large acquisitions, as they have been able to simultaneously grow revenues and extract significant operating efficiencies. Likewise, they have consistently found ways to develop complimentary adjacent revenue streams such as with the recent expansion into audio visual, security, and electrical. The company has one of the most skilled founder-led and shareholder-aligned management teams on the public markets and

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[1] DDR financial year is January 1st to December 31st.

[2] Exceed Group in New Zealand, and Hills Security and Information Technology in Australia, which collectively added around 300 additional team members.

[3] The most recent warehouse expansion of over 80% was completed in February 2021 and this additional capacity has reached near full utilisation within just over 12 months.

we are confident they will yet again be able to continue their solid revenue growth and translate this into correspondingly higher per share earnings.

At the end of the period, the DDR share price was trading near its 52-week low, and at a point we think is a fair price for an exceptional business that has a high likelihood of strong per-share compounding for several years to come. Although this volatility can feel uncomfortable over the short term, when put in the context of owning such a high-quality business for at least the next decade, we think this should be seen more as potentially being a great opportunity. Indeed, if we did not already have such a large portfolio allocation to DDR, we would likely consider buying more shares at the current prices. Investing more capital into an investment that already accounts for a large proportion of the portfolio requires the discipline of an ever-increasing margin of safety (discount) to our calculation of underlying intrinsic value. To be clear, we would welcome further significant share price declines in DDR that provided a suitable margin of safety and an opportunity to invest more capital in what we believe is one of the most competently managed businesses on the ASX.

The market price decline of FSG was the result of the company's half year FY23 update where they reported meaningful weather-related delays and construction cost increases that have hindered the roll-out of their telecommunications tower infrastructure. The significant flooding that occurred across regional QLD and NSW during 2022 meant that many tower construction sites were inaccessible for extended periods, whilst simultaneous increases in the price of fuel, materials, and labour drove up the overall cost to deliver these projects. FSG is in the process of building 21 fixed wireless networks comprising of 127 towers across rural, regional, and remote parts of Australia and aims to complete this tremendous task over the coming 12 months. The company is set to receive $24m of Federal government grants to help finance this investment, although the scale of the project will require significant additional near-term financing.

The strategic intent behind building these networks is to underpin the competitive advantage that the company's core digital connectivity and managed services division is attempting to build in rural, regional, and remote Australia (including Tassie!). This division generates capital light recurring revenue and has material growth potential as businesses and residents within these geographic areas increasingly demand digital services that are on-par with their urban counterparts.

The primary risks to this strategy are a further blow-out in construction timelines and/or costs, or the inability to secure suitable project financing. These are not immaterial, which would seemingly explain the share price decline, and which at the current level may be a fair appraisal if these known risks do indeed come to full fruition. However, there is substantial upside if FSG can surpass these near-term challenges and continue to consistently expand their core digital connectivity and managed services. We believe the quality of their core cashflows, combined with government grant income, should enable the company to obtain suitable project financing and complete the networks. Longer-term, we think the strength of their core business will become increasingly evident given that their rural, regional, and remote customers continue to increasingly rely on FSG's telecommunications services as mission critical to their business and personal lives.

The portfolio holdings as of March 31, 2023, were as follows:

Rank	Holding	Total Portfolio Weighting
1	Kelly Partners Group (ASX:KPG)	21.40%
2	Dicker Data (ASX:DDR)	13.47%
3	Servcorp Limited (ASX:SRV)	11.79%
4	Ryman Healthcare (NZX:RYM)	8.43%
5	Comms Group Limited (ASX:CCG)	7.61%
6	Blackwall Limited (ASX:BWF)	7.47%
7	Markel Corporation (NYSE:MKL)	5.03%
8	Field Solutions Group (ASX:FSG)	4.26%
9	Berkshire Hathaway Inc (NYSE:BRK-B)	4.04%
10	PPK Group (ASX:PPK)	1.41%
11	Costco Wholesale Corporation (NYSE:COST)	1.28%
	Cash	13.79%

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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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