

# HARRINGTON PARTNERS

Investment Management

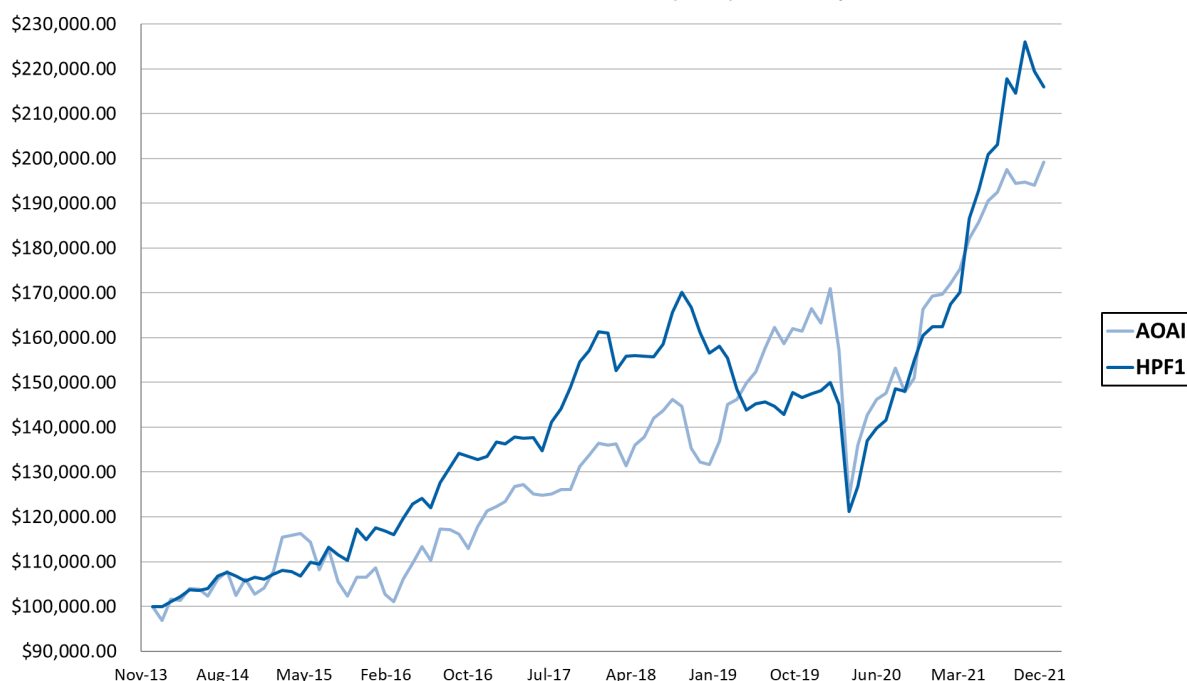
## Harrington Partners Fund 1 (HPF1) – 31 December 2021

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%
6 Months to 31/12/2021	7.10%	4.58%	2.52%
Annualised Performance	10.05%	9.00%	1.05%
Cumulative Performance	115.14%	99.24%	15.90%

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

Change in Value of \$100,000 invested in HPF1  
vs All Ordinaries Accumulation Index (AOAI) Since Inception



The Fund returned **7.10%** net of all fees over the first 6 months of Financial Year 2022 (FY22), this compares to a return of **4.58%** for the All Ordinaries Accumulation Index over the same period.

The Fund has had a great first half of FY22 with all companies performing very well over the period. During the period we increased in our ownership in Comms Group Limited (ASX:CCG) which is now our 6<sup>th</sup> largest position and our investment in 1300 Smiles (previously ASX:ONT, now no longer listed) was sold through a takeover which is detailed further below.

## Portfolio

The top 10 holdings as at December 31, 2021 were:

Rank	Holding	Total Equity Weighting	Total Portfolio Weighting
1	Kelly Partners Group (ASX:KPG)	15.33%	12.96%
2	Field Solutions Group (ASX:FSG)	9.75%	8.25%
3	Dicker Data (ASX:DDR)	9.24%	7.82%
4	Gowing Brothers Limited (ASX:GOW)	7.17%	6.06%
5	Servcorp Limited (ASX:SRV)	6.62%	5.60%
6	Comms Group Limited (ASX:CCG)	6.21%	5.25%
7	PPK Group Limited (ASX:PPK)	6.04%	5.11%
8	United Overseas Australia (ASX:UOS)	5.20%	4.39%
9	Global Data Centre Group (ASX:GDC)	5.08%	4.30%
10	360 Capital REIT (ASX:TOT)	4.95%	4.18%

The top ten holdings made up **63.92%** of the total portfolio and cash allocation was **15.42%** at the end of the period.

## 1300 Smiles (ASX:ONT)

During the period, the Funds' investment in **1300SMILES [ASX: ONT]** was involuntarily sold when ONT was acquired by Abano Healthcare. Abano is owned and managed by BGH Capital (BGH), a local private equity firm, and the Ontario Teachers' Pension Plan (OTPP), a Canadian pension fund. Abano already owns the second largest network of dental surgeries across the ANZ region, through Maven Dental in Australia and Lumino Dental in NZ, and the addition of 1300SMILES fits ideally within their ongoing strategy of dental industry consolidation and corporatisation.

As part of the deal, minority 1300SMILES shareholders received cash consideration of \$7.00 per share along with a \$1.00 fully franked dividend. On face value, the price paid by Abano appears to be a great near-term outcome, and we thank and congratulate the entire 1300SMILES team for shrewdly negotiating on our behalf. However, investors are now faced with the challenge of finding something of comparable quality and value in which to reinvest their *post-tax* transaction windfall. Unfortunately, this is easier said than done given that 1300SMILES possessed a relatively rare combination of above average economics, excellent management, and meaningful longer-term growth potential.

The founding vision of 1300SMILES founder Dr. Daryl Holmes was to build the most trusted and first-rate platform upon which to facilitate an expected wave of industry consolidation. This platform is now in place, and whilst the business's performance has been phenomenal thus far, realistically the best years could still be to come.

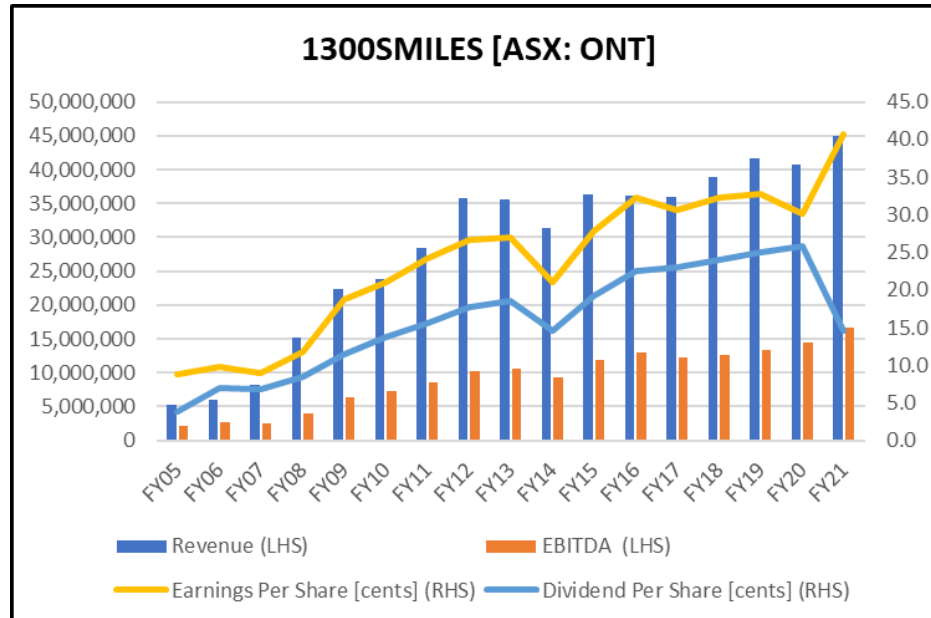
*"One of the Company's core beliefs is that the dental industry is undergoing structural change. Dental services are, in the main, still delivered by individual businesses comprising just one or two*

*dentists. We believe there exists significant scope to consolidate the ownership and management of practices. This creates enormous opportunities to improve the delivery of dental care via coordination and management – not by telling dentists how to do dentistry, but by freeing them of management and administration tasks and allowing them more time to concentrate on what they are good at – dentistry”<sup>1</sup> – 2005 1300SMILES Annual General Meeting.*

In our view, Abano will do very well out of the transaction and more broadly is in a great position to significantly increase their market share over the coming decades. The main contributors to their probability of success are several underlying demographic shifts that are gaining momentum across the dental industry, which combined appear likely to make partnering with a competent corporate provider much more attractive than in past decades. The pace of this generational transition had recently started to appear in 1300SMILES rate of acquisitions, whereby nearly 1/3 of the total network had been added since the start of FY19. Our expectation was that this rate would remain elevated for several years, resulting in a sustained phase of higher earnings per share growth, the benefit of which will now flow directly to Abano.

### Brief Historical Overview of 1300SMILES

1300SMILES was founded 22 years ago by Dr Daryl Holmes and was listed on the Australian Securities Exchange in 2005 as 7-surgery network that today has grown to 34 locations. Daryl was one of the first and most successful pioneers of dental surgery consolidation in Australia. Throughout their nearly 17-year publically listed history, 1300SMILES was one of the most prudently run and consistently high performing businesses on the ASX, as illustrated by the outstanding financial performance shown in the graph below.



Investors who bought into the 2005 IPO, and stayed the course, have seen their original capital compound at roughly 14.81% annually, whilst also receiving a cumulative of \$2.71 in fully franked dividends. Stated another way, if you had invested \$100,000 into the IPO at \$0.80 and held onto your

<sup>1</sup> <https://www.asx.com.au/asxpdf/20051121/pdf/3tcf506nwfjihy.pdf>

125,000 shares, then your proceeds from the Abano takeover would be \$1,000,000 in addition to \$338,750 of fully franked dividends you received along the way!

Just as importantly, Daryl Holmes typifies the exceptional owner-managers with which we seek to partner. He patiently built 1300SMILES as if he owned the whole thing, treating minority shareholders like partners, and communicated with a level of clarity and candour that is rare amongst his peers. We highly recommend reading Daryl's superb [Letters to Shareholders](#), and have included two of our favourite excerpts below.

*"Good things come to those who wait. I have commented in earlier correspondence that there are aspects of our business which are old-fashioned. We endeavour to control costs while delivering the best possible service. We have a simple capital structure and a transparent business. We carry no debt. We make money, pay the tax due, and pass franked dividends to our shareholders. We also make use of the timeless virtue of patience in our business strategy in a particular way: we combine it with impatience. We are impatient for growth in profit and the other financial measures of importance to most shareholders, but patient for growth in practice numbers. I will take one high profit practice any day ahead of 100 stragglers (although owners and receivers of good businesses that have fallen on difficult times should please note that I enjoy a challenge) ... The plans are now playing an important role in the Snowball Effect we observe, wherein more members (or patients) attract more dentists; more dentists bring different skills and special interests, which gives their colleagues the opportunity to further develop their own skills and interests; many dentists like to work alongside the very best, so the deeper the skill base the more that dentists are keen to join 1300SMILES; the depth of high quality dentists attracts more patients; more patients attract more dentists; and so on.*

*Our growth path going forward is both methodical and opportunistic. Our method is a constant recruiting effort aimed at convincing dentists to establish their practices within our facilities or to sell their practices to us and continue working. The harder we work at our methodical approach, however, the more opportunities arise, so we need to stay flexible to deal with the opportunities which arise suddenly. It's impossible to predict exactly how any future period will unfold, but we will work hard to increase the company's revenue and profit through a focused, creative, and flexible campaign to attract more dentists into the 1300SMILES system." – HY14 Letter to Shareholders.*

*"In my capacity as a private investor, I also own shares in companies other than 1300SMILES. In managing my own portfolio, I am increasingly bedevilled by "agency risk," which is the risk that managers of a listed company might operate that company more for their own benefit than for that of shareholders. This risk is greatest where senior managers have more interest in maintaining their salary and benefits packages than they do in increasing Earnings Per Share and enhancing the long-term value of the company's shares. All too often I see companies with otherwise attractive businesses whose managers are paid too much, or where managers have share option packages which far outweigh their personal investment commitments to their companies. Maybe I'm just growing more cynical, but it seems to be getting harder to find companies in which such agency risk is not a major concern. I trust you'll forgive this minor digression. I can assure shareholders that we work very hard to ensure that agency risk does not affect your investment in 1300SMILES. (In past years shareholders have never been shy about telling me about other well-behaved companies. If you know of other good listed companies which have agency risk under control, I would be pleased to hear about them.) ... The second category is that of shares acquired by senior management. I say "acquired" because that is exactly what they do. I believe it is essential for the health of our company that senior managers have a stake in the company, and we encourage our managers to buy shares. In some cases, we need to make new shares available for this purpose, but be assured that we're*

*not giving these shares away. Our managers buy shares at the market price at the time, reflecting their faith in the company going forward and their commitment to it. This leads to minor dilution, but the overall effect is that of strengthening our company.” – FY11 Letter to Shareholders*

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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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