



Holland Views – Helios Towers – Price: 138p; American Towers

Money Trees (and what you win IF you win)

Helios Towers has just listed on the London market coming from Private Equity sellers. It has a short track record, plenty of debt, seemingly makes a loss and has no owner manager. Additionally, our work on it below arguably focuses on the upside with relatively less time given to the many risks a company operating in Africa faces. Still reading? We are impressed!

Towers of Strength

Independent Tower businesses are new to the London market, but not new in the US. The compounding characteristics that their business models exhibit is nothing short of sensational (a word we do not believe we have ever used to describe a business model before). They are archetypal of Munger's 'put up more to make more' mental model. With long-runways of secular growth and good access to debt to finance their utility-like cash flows, they can produce compounded returns that are potentially very high. Industry bellwether American Tower (AMT) has compounded its cashflows at c.16% since 2008. To pique your interest, we think Helios, a younger, riskier version of AMT, could compound it's at 24% p.a.!

We have looked at many 'roll-up' businesses in the past (Da Vita, Dollar Tree et al) but not all roll-ups are comparable. Actually, very few offer the certainty of future cashflows that mobile tower networks do, nor indeed the growth prospects. In short: 1) the Tower model is a roll-up of infrastructure *assets*, *not companies* thus minimising integration risks, 2) these assets have perpetual (recurring) revenues streams which in turn allow them to be collateralised and 3) the companies enjoy structural growth as Telco operators divest assets. The leverage that these cash generative assets can support is crucial to this model as it accelerates the compounding of shareholder equity.

As mentioned, all of this is not particularly new to the US stock market where global market leader American Tower (AMT) trades on c.30x Owner Earnings and 25x EV/EBITDA. Rather than just observing that the aforementioned clone, Helios Towers, came to the London market on a lower valuation of c.18x Owner Earnings (today it is on 22x P/OE and 12x EV/EBITDA). Instead want to use this opportunity to educate readers and ourselves as to the compounding power such businesses can have and the drivers that enable them to grow so fast. Towards the end of this note we will look at Helios Towers in more detail. The health warning that this might well be a risky entity due to its assets being based in Tanzania, Congo and Ghana is obvious but not enough to put us off. If Helios shareholders win, we think they win big.

Tower Network Operators – compounding machines

In recent weeks we have done a great deal of work studying Tower company business models. This follows on from a quiet admiration we have long held for them, but in truth without an immediate investment opportunity to focus our minds. The Helios Towers floatation provides the spur to understand these businesses better and to try and explain them to others.

For much of the last few years we have worked hard to find businesses whose compounding power is faster than Mr Market realises (aka great businesses masquerading as OK businesses).

We might lump these great compounders into three buckets:

1. **EDLP**: e.g. JD Wetherspoon, Ryanair, Schwab, Costco. EDLP is a business model we think we know now very well. Crucially, each of these has cash compounding characteristics far better than their headline ROE might suggest.
2. **IP/Content kings**: e.g. WWE, Disney, Games Workshop. These are what we have referred to as ‘rare bird’ businesses which were under-earning – thanks to the hidden pricing power and demand being unleashed by new distribution channels.
3. **Toll bridges**: e.g. Moody’s, American Tower, Mastercard, Visa. We always knew these were great businesses but it is only recently we have spent enough time to truly understand their compounding drivers better – more fool us.

Each of this third category has its own idiosyncrasies in vastly different markets. However all are forms of Toll Bridges on huge traffic volume flows of finance, communication or consumer spending.

Other people’s money

To point out that a company with say, an ROIC of 40% that is growing its sales at a steady 6% pa is a rare and valuable entity is hardly a revelation to today’s investor. But what about another steady grower that makes a seemingly more sedate ROIC of only c.15%, but, and this is key, one that can use ‘other people’s money’ to fund part of its future growth opportunity? Such an approach has made us think harder on companies like Ryanair and JD Wetherspoon and has led to us having far greater conviction on both the quality and the scale of the compounding that can be realised thanks to factors like working capital or prudent debt usage.

In essence, powerful compounding needs **good returns on capital**, but as importantly it needs **growth** and **great capital management** (indeed it’s not just the *allocation* of excess capital from good returns, but often the judicious *sourcing* of externally funded capital too).

1. In high ROIC/ROE companies, often the compounding kicker is more straightforward and comes in the form of equity buybacks as there is limited potential to re-invest significant sums profitably. In other words, per share returns are geared through efficient capital allocation via buybacks (ref: Mastercard and Moody’s).

2. In strong secular growth markets however, there can sometimes be much higher quantum of reinvestment opportunity on offer. Companies in such markets can offer two further drivers to boost compounding. The first is the ability to invest **retained earnings** profitably; the second is using ‘**other people’s money**’ to increase the quantum of investment (and reduce the cost of capital).

Followers of John Malone will recognise this second playbook well.

Source: Helios Towers IPO Prospectus, Oct 2019

To view the remainder of this in-depth report, please contact Andrew Hollingworth, Andrew@hollandadvisors.co.uk for a complete PDF copy.

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