Global Value and Income Dispatch

Value and income in the food supply chain: a multi-asset approach

An industry in transition

The June 2017 acquisition of Whole Foods Market by Amazon sent shock waves through various segments of the food supply chain impacting valuations of grocery, consumer products and even foodservice distribution businesses.

Over one year later there is still great uncertainty about how new entrants and technological changes will affect how food travels from the farm to our mouths. In the meanwhile, however, the industry landscape continues to look a lot like it did before the Amazon purchase. Grocery incumbents continue to be squeezed by discounters and direct delivery and are trying to pass pricing pressure on to their suppliers.

Some of the other paths through which food can make its way to our stomachs are seeing a bit less disruption. Restaurants and catering businesses, which purchase and prepare food for us, are more insulated by the service component, where know-how and customer captivity can provide some competitive advantage.

Distribution businesses are also somewhat protected by local economies of scale from route density.

Still, the threat of disruption is to varying degrees present everywhere, and with so much uncertainty it can be difficult for investors to know what to do.

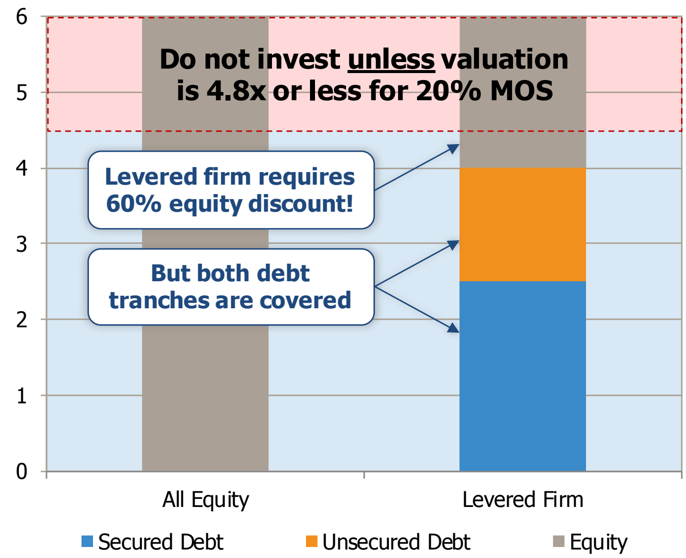
A multi-asset value approach

When industries face disruption and change it can be particularly useful to ***look across asset classes*** for three key reasons:

1. Equity and fixed income securities can offer **different points of attachment** to a business;
2. Fixed income markets can often **spot distress** before equity investors; and
3. Following corporate debt provides **access to information** that equity-only investors can miss.

Different attachment points can be useful when the range of outcomes for an industry is wide. By investing in bonds, which are higher up in a company's capital structure, one can "attach" to a business at a lower valuation and thus have a greater buffer against capital impairment. This can also be useful when equity is expensive and doesn't offer a margin of safety (MOS).

Business value estimated at 6x EBITDA



Spotting distress is critical for fixed income investors. The contractual nature of coupon payments means that bond holders often don't have much upside beyond the interest they receive, and must focus on avoiding impairment. Widening credit spreads can therefore be an early warning sign for companies and industries alike.

Access to information can be more difficult to come by in fixed income versus public equities, since many corporate debt issuers are private. Bondholder conference calls often don't offer a replay option and access even to basic financial information can be controlled by the issuer. Those who are active in corporate debt, however, can use this information to get a more complete picture of an industry or supply chain and to benchmark publicly traded peers.

Bringing it all together

An integrated approach that looks across industries, geographies and capital markets can bring to bear a variety of information and preserve flexibility on where to deploy capital.

For instance, insights gained from looking at the equity of a food catering company could ultimately inform the decision to invest in the debt of a food service distribution business that operates as its supplier.

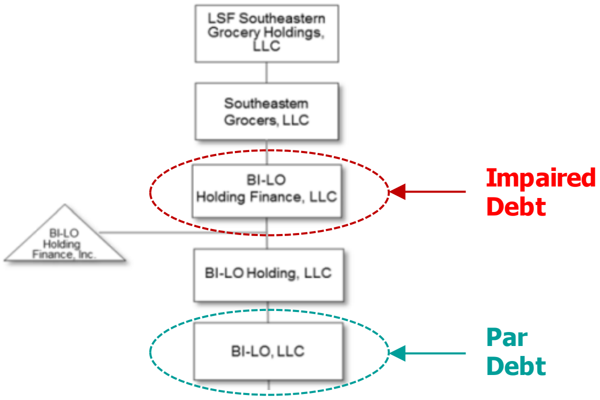
The concept of business persistence brings this all together. Persistence is the likelihood that an enterprise will survive and thrive in the future. Where persistence is low and uncertainty is high, we typically require a larger discount to our estimate of business value.

Our focus is first and foremost on capital preservation, so when persistence is lower, as is the case in grocery, we might be more likely to find margin of safety in the debt securities of an issuer rather than in its equity.

Let the Bi-Lo beware: a case study in attachment

The recent bankruptcy of Southeastern Grocers (the parent company of Bi-Lo and Winn-Dixie) is a cautionary reminder that your attachment point matters even in choosing one debt instrument versus another.

Southeastern was owned by private equity firm Lone Star Funds. In addition to secured debt at the operating company level, in 2013 the company issued unsecured debt at its holding company where the interest could be "paid-in-kind" with additional debt. This "HoldCo" debt was issued so that Lone Star could pay itself a $450 million dividend.



High debt levels, tough competition and questionable execution led the company to file a bankruptcy lanwhere the entire holding company debt issue was to be cancelled in exchange for equity. ***Following the approval of the plan these "HoldCo" notes were quoted at less than 60 cents on the dollar, while the secured operating company debt is to be repaid at par.***

The JOHCM Global Income Builder Fund seeks to generate meaningful monthly income distributions and long term appreciation by employing a bottom-up global value philosophy which prioritizes capital preservation. The fund has the flexibility to invest across equity and fixed income markets and can adapt to the opportunity set.