TO: Investment Partners
FROM: Emeth Value Capital | emethvaluecapital.com
DATE: 8/14/2024
RE: 2024 H1 Letter

Annualized Net Returns to June 30, 2024 *(unanualized if < 1 year, inception 12/31/2015)*			
	Emeth Value Capital	MSCI ACWI Index	Delta
6 Months	+6.85	+11.31	-4.46
1 Year	+27.74	+19.21	+8.53
3 Years	+11.39	+5.49	+5.90
5 Years	+20.91	+10.79	+10.12
Since Inception	+19.58	+10.73	+8.85

Calendar Year Net Returns to June 30, 2024			
	Emeth Value Capital	MSCI ACWI Index	Delta
2016	+9.33	+8.39	+0.94
2017	+39.57	+24.35	+15.22
2018	-17.14	-9.12	-8.02
2019	+87.40	+26.59	+60.81
2020	+8.08	+16.33	-8.25
2021	+35.57	+18.67	+16.90
2022	-13.60	-18.37	+4.77
2023	+42.58	+22.30	+20.28
2024 YTD	+6.85	+11.31	-4.46
Cumulative Since Inception	+357.04	+137.86	+219.18

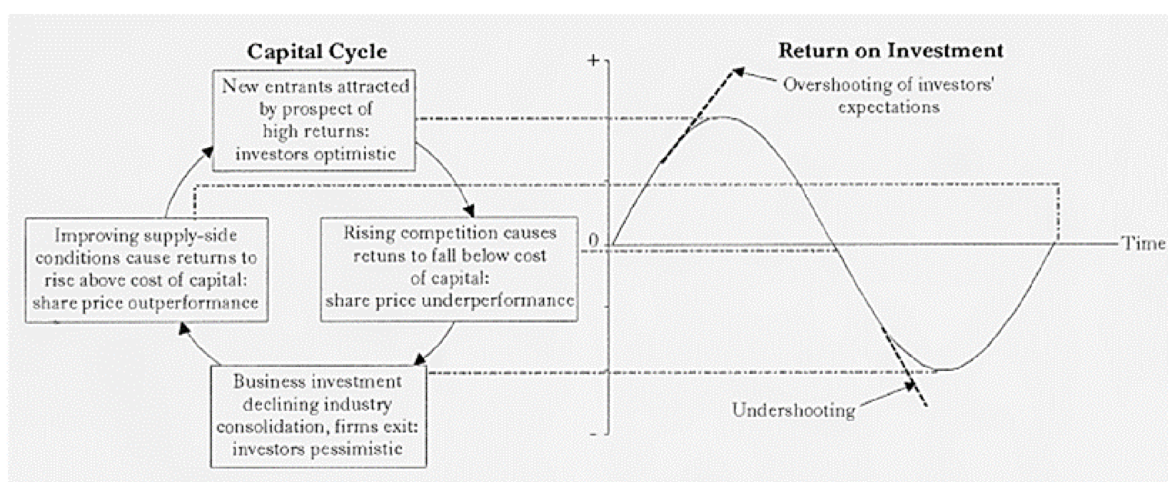
Foreword

I intend to share the updated results at the outset of each letter. It is worth reiterating that I ascribe little significance to short term results. I look out many years when making investments for the partnership and believe our results are best weighed using a similar time horizon.

The Capital Cycle Approach

> *While we invest in growing companies, there are important philosophical differences between growth and quality investing. Growth strategies hinge on demand-side factors, while quality investing is fundamentally rooted in an understanding of supply-side characteristics. (Lei Zhang, Hillhouse)*

Marathon Asset Management was founded in 1986 by Jeremy Hosking, Neil Ostrer, and William Arah. The firm, beyond its claim as the foster ground to the iconic Nomad Investment Partnership, developed an investment approach that produced decades of attractive returns based on a simple insight: that industry profitability and levels of industry investment are inversely correlated. This framework was termed capital cycle analysis and, in essence, looked to invest in companies from sectors where capital was being withdrawn and to avoid companies in sectors where investment was increasing rapidly. This central focus on the supply-side dynamics of an investment stands in contrast to the practice of the broader investment community, which often falls prey to demand-side myopia. To be sure, both sides of the equation are important, but what can go unappreciated is that a general absence of capital and a dull competitive environment can be the ideal context for extraordinary outcomes. Traditionally, Marathon sought inflection points in industry supply-side characteristics, where a once oversupplied industry shows signs of abatement, and as a result the ensuing improvement in return on capital would catalyze share price performance. However, on occasion there are also situations where capital destruction is not the arbiter of supply, but rather, structural forces specific to an industry keep supply low. This setting can produce equally attractive economic outcomes for the right incumbents.



Consider a case study on the extreme end of the spectrum – the tobacco industry. In 1964, the U.S. Office of the Surgeon General issued a landmark authoritative report linking the use of tobacco with the heightened risk of lung cancer and chronic bronchitis. At the time, forty-three percent of adult Americans were smokers, and more than five hundred billion cigarettes were sold per annum. In the years that followed, several regulations were enacted aimed at discouraging tobacco use, including the passage of The Public Health Cigarette Smoking Act of 1969 that banned the advertising of cigarettes and tobacco products on television and radio broadcast. While cigarette consumption continued to rise in aggregate until 1981, the undercurrent of regulation was strong and could be seen in the steady decline in adult smoking rates which declined by a fourth, to thirty-three percent, in the seventeen years following the surgeon general report. Soon, the

structural decline of tobacco was in full onset, and was accelerated by the historic 1998 Tobacco Master Settlement Agreement which not only banned all remaining forms of advertising for tobacco companies, but also forced them to finance a multibillion dollar anti-smoking campaign. Today, less than twelve percent of adult Americans smoke, and the amount of cigarettes sold per annum has declined seventy percent from the 1981 peak. With this backdrop in mind, many would be surprised to learn that one of the highest returning investments over the last sixty years is a tobacco company – Altria Group. One dollar invested in Altria in 1970 has increased by more than six thousand fold today, or approximately a twenty percent annualized return, trouncing any global benchmark. In fact, if one waited until the exact peak of cigarette consumption in 1981, the outcome is still a nearly two thousand fold return, or a seventeen percent per annum return for a half century. While the share price performance has lagged recently, Altria Group has also outperformed global indices for much of the last twenty years; indeed, on a fundamental basis, its earnings per share have compounded at nearly nine percent per annum over the last decade while paying out seventy percent of earnings each year in dividends – equating to an underlying mid-teens total return. So, how can this be? To paraphrase Warren Buffett's remarks circa 1980, it doesn't hurt that it costs a penny to make, you sell it for a dollar, it's addictive, and there's fantastic brand loyalty. All important elements. However, better yet if it is all but illegal for new entrants to start a competing cigarette brand. With the near complete ban on advertising, a startup cigarette company has no way of reaching out to consumers, and per the terms of the 1998 Master Settlement Agreement, that startup would be burdened by annual state settlement payments or would be legally required to escrow funds for future civil litigation. This, in conjunction with an oligopolistic market structure, has led to immense pricing power for tobacco companies. Cigarette prices today are nearly fifty times higher than they were in 1964, compared to the broader CPI index which pegs a broad basket of goods at ten times higher over the same timeframe. Much of this price increase has been driven by increases in state and local cigarette taxes and annual settlement payments, which in some cities amount to as much as seven dollars per cigarette pack. Ironically, while excise taxes have been an effective tobacco control policy for consumption, it has served to exacerbate the pricing power afforded to tobacco companies. Taxes make up a large portion, and manufacturer's net revenue a smaller portion, of the final price consumers pay. As a result, small incremental price increases on the manufacturers part have negligible impact on demand, but equate to a substantial increase in cigarette company operating profits. Indeed, these substantial price increases over time have resulted in operating margins that have expanded from fifteen percent in 1970, to nearly sixty percent today. Taken together, the significantly higher price points and expanded operating margins have dwarfed the decline in cigarette unit volumes. Finally, as Marathon Asset Management recognized, capital cycle analysis can also apply at the meta level to securities themselves. A powerful contradiction has been that the general investor aversion to owning tobacco stocks has itself fueled the compounding of intrinsic value for Altria Group as it allowed the company to repurchase its own stock at attractive prices. Since 1964, Altria has spent tens of billions of dollars to reduce its share count. Below I highlight one of our portfolio companies that has similarly benefited from an industry with structurally low supply – the United Kingdom housebuilding industry. Over the last forty years, Barratt Developments Plc, the largest homebuilder in the United Kingdom, has increased its number of home completions by 1.8x, or a modest 1.5 percent per annum, while its operating profits have increased forty fold over the same timeframe.

Barratt Developments Plc

Overview

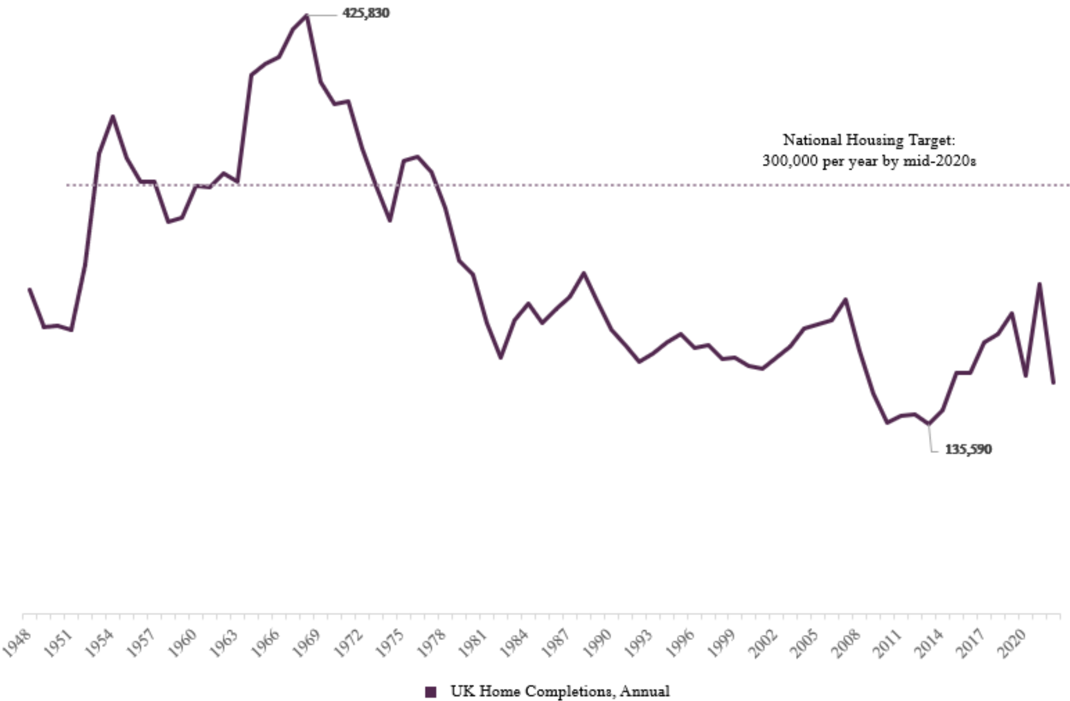
Barratt Developments Plc is the largest homebuilder in the United Kingdom, accounting for approximately eighteen thousand of the country's two hundred thousand annual housing stock additions. The company was founded by Lawrie Barratt and Lewis Greensitt as Greensitt Bros (Contractors) Ltd. in 1958, and expanded rapidly over the subsequent years from its origins as a local Newcastle builder. The group's shares were floated on the London Stock Exchange in 1968 as Greensitt and Barratt Ltd. in a public offering that was more than twenty times oversubscribed, initially targeting five hundred annual completions in its first year as a public company. By 1979, Barratt had attained the status as the nation's largest homebuilder with a record setting ten thousand annual home completions, a success underpinned by its focus on providing a high-quality design and construction at an affordable price point for first-time homebuyers. Today, Barratt has constructed over half a million homes across the United Kingdom, generating billions of pounds in profit and is among the largest owners of greenfield land in the country.

Industry Context

> *I founded Redrow in 1974 originally as a civil engineering contractor and it was only as a result of the squeeze on public spending of the early 80s that I decided to steer the business in a different direction - home building. The transition was easy. Land with outline planning permission was in ready supply and the time to go from a 'red line' permission to a start on site was no more than six weeks, often less. There were four or five conditions to clear – colour of bricks, roof tiles, landscaping, etc, then off you went. With bank finance readily available there were few, if any, barriers to entry. Young entrepreneurs like myself, Tony Pidgley, and Lawrie Barratt before us, were able to start fledgling home building companies from scratch and build them into national builders – something that would be almost inconceivable today. (Steve Morgan)*

The United Kingdom has experienced one of the lowest housebuilding rates of any developed country over the last four decades, which has resulted in a severe structural shortage of homes. Indeed, it is estimated that the shortfall between the country's current housing stock and that of neighboring EU countries stands at approximately four million unbuilt homes, or approximately seventeen years of supply at current build rates. The government, in recognition of this worsening housing crisis, established a target of achieving three hundred thousand new home completions per year by the mid-2020s. However, this goal continues to be missed by a wide margin. At the heart of these ongoing failings is the United Kingdom's deeply flawed land-use planning system. The country's planning system, established by the Town and Country Planning Act 1947, is marked by internationally unusual discretion and restriction on development. While many other countries have land-use regimes that are rules-based zoning systems, in the United Kingdom planning consent is granted on a case-by-case basis by local government councils. In short, instead of land being available for development unless it is prohibited, development is prohibited on all land unless a site is granted a permit at the discretion of a local council. This nationalization of development rights has become problematic as local government councils are often badly under resourced, and are subject to the grandstanding of local citizenry. Over time, this has had profound effects on the composition of the domestic homebuilding industry, as the process of seeing greenfield land through to final planning consent is

complex, unpredictable, expensive, and could last several years on any given site – therefore demanding scale to navigate. Consider that in 1980 there were over ten thousand small and medium-sized (SME) housebuilders active in the United Kingdom, building fifty seven-percent of all new housing. Today, there are less than two thousand SME builders that account for only twelve percent of new housing completions. On the other hand, the ten largest 'volume' housebuilders in the United Kingdom have increased from only eighteen percent of completions in the 1970s to approximately fifty percent of completions today. Moreover, the three largest volume builders – Barratt Developments, Persimmon, and Taylor Wimpey – have remained unchanged in position for the last two decades. Simply put, while these self-imposed regulatory hurdles have created a poor operating environment for housebuilders as a whole to actually deliver new housing units, it has in tandem created an exceptional economic environment for those builders large enough to manage the complexity. Indeed, over the last twenty years, a period that includes both the global financial crisis and the covid pandemic, Barratt Developments has recorded an average return on capital employed of twenty-one percent.



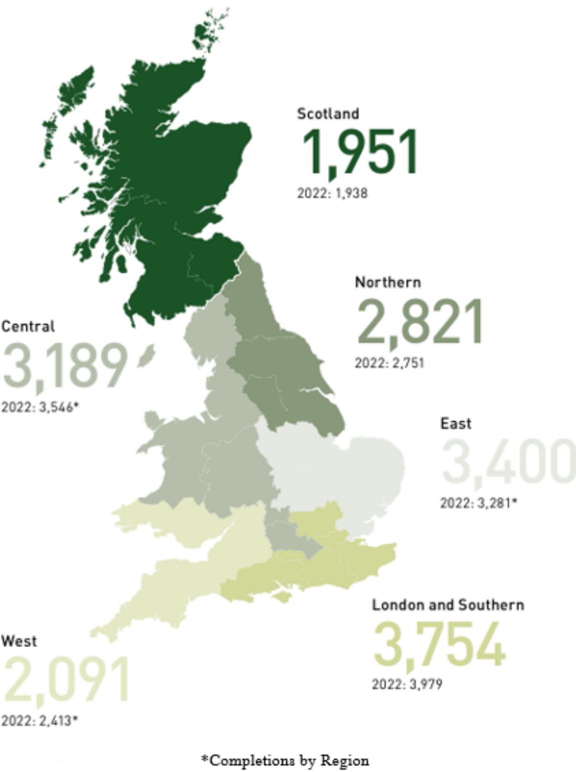
Operations

Housebuilders in the United Kingdom are vertically integrated businesses. They procure land themselves, obtain relevant planning permissions for that land, conduct site development, and ultimately construct new homes for sale. This stands in contrast to many other countries around the world where the land developer and homebuilder are separate entities, and reflects the challenges of obtaining detailed planning permission. Accordingly, land management is a key component of Barrat Developments' business. The group operates across the whole of the United Kingdom and maintains a geographically balanced land portfolio that is among the shortest and most developable in the industry. In number, Barratt targets a supply of owned land pipeline of c.3.5 years and further c.1.0 years of controlled land. When married with the group's operational

model, which ensures a precise match of build and sell rates on each site, this land approach enables Barratt to achieve its goal of a mid-twenties return on capital employed. For example, on a unit basis, to support the sale of a home that cost £350,000 where the group expects to make a nineteen percent margin, or £67,000 in pretax profit, Barratt Developments will on average carry £175,000 in land inventories (c.3.5 plots) and £125,000 in work in progress (c. half a completed home). Furthermore, to complement this pipeline of immediate land, Barratt maintains a substantial pipeline of long-term strategic land controlled under option agreements. These plots are promoted through the planning system to obtaining detailed planning consent, at which point the land is acquired at a pre-negotiated discount, often twenty percent below open market value. Overall, Barratt aims to have thirty percent of completions come on strategic land that has been pulled through to the current land bank, which provides a three percentage point margin uplift on these completions. Including Barratt Developments' wholly owned land promotion division, Gladman Developments, the group has a combined pipeline of strategic and promotional land exceeding two hundred thousand plots, or more than a decade of long-term supply.

BARRATT DEVELOPMENTS - COST STRUCTURE

Category	% of Revenue
Land	c. 16%
Infrastructure and S106	c. 20%
Housebuild - materials	c. 32%
Housebuild - labor	
Site and division based operating costs	c. 9%
Administrative expenses	c. 4%
Total	**c. 81%**



*Completions by Region

Barratt goes to market with three primary consumer brands: Barratt Homes, David Wilson Homes, and Barratt London. Barratt Homes cater to first-time buyers with entry-level price points. These units, often semi-detached homes averaging around one thousand square feet, are priced at approximately £315,000. David Wilson Homes targets those looking to upgrade, offering mid-priced homes finished with premium materials and fixtures. These homes average twelve hundred square feet and are priced at around £430,000. Finally, Barratt London provides a diverse range of London flats, which include luxury mixed-use developments and large-scale regeneration projects. In 2023, Barratt Homes accounted for fifty-five percent of total group completions, David Wilson Homes made up thirty-five percent, and Barratt London

contributed ten percent. Geographically, Barratt segments operations into six regions which are split into twenty-nine divisions. Each division is structured to deliver a capacity of approximately 750 units annually, other than London which can deliver roughly two thousand units. Combined, the divisions have an overall volume capacity for homebuilding of more than 21,500 units per annum. Naturally, Barratt London operates solely in the London division; however, for the remaining divisions the group utilizes a mixture of divisional structures, with some business divisions that are single branded and other divisions that are structured to sell both Barratt and David Wilson homes. This ability to dual brand a given development is a considerable advantage, as the homebuying process is a necessarily localized activity. The more product range and diversity of price points Barratt Developments can bring to a single site, the broader a local audience this appeals to which accelerates absorption and site delivery. Site sizes vary, but typically Barratt will acquire and develop sites that are two hundred plots and will sell about one home per week, which translates to a sales period of four years for an average site. In addition, as part of the planning consent process, each local authority has its own specific Section 106 requirements. These stipulate that builders must allocate a certain proportion of any development to affordable housing, often set at twenty percent of the units. Although the profit margins on these units are lower due to the requirement to sell them at a minimum twenty percent discount to the local market value, often pricing below £200,000, the demand is highly predictable. Indeed, as one measure of demand, consider that there are currently 1.3 million people in the United Kingdom on waiting lists for social housing. Barratt Developments decentralizes its business divisions, allowing site managers the autonomy needed to deliver consistent, on-time, quality builds. However, functions such as design, procurement, and sales are centrally controlled across the brands. This ensures Barratt leverages its scale to the fullest extent where it provides a competitive advantage, while elsewhere allowing the group's highly experienced team members to deliver with a specialized understanding of local markets. This has been a winning combination. Barratt's site managers have won more NHBC Pride in the Job awards than any other builder for twenty consecutive years, widely recognized as the 'Oscars' of the housebuilding industry. In addition, Barratt has been named the NHBC Large Housebuilder of the Year three times in the past five years and has placed second each year it did not win. Finally, Barratt is the only national housebuilder to maintain a five-star HBF rating for fifteen consecutive years, meaning that over ninety percent of customers would recommend their homes to a friend.

A Rational Land Market

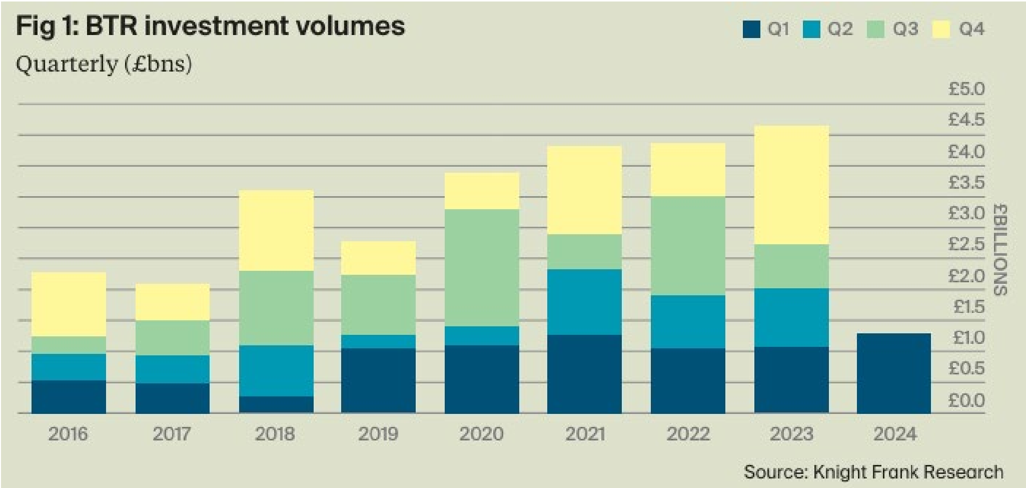
> *A basic industry with few players, rational management, barriers to entry, a lack of exit barriers and non-complex rules of engagement is the perfect setting for companies to engage in cooperative behavior. (Marathon Asset Management)*

One important advantage of being a volume homebuilder in the United Kingdom is the presence of a highly rational land market. There are several reasons for this. One is the simple fact that while it is immensely challenging to bring land through to final planning consent in the United Kingdom, buildable land itself is not in short supply. Consider that over fifty percent of land in England is available for development, while it is estimated that only two percent of additional land is needed to address the housing shortage. Moreover, looking forward, twelve percent of the non-developable land is protected green belt lands which the incoming Labour Party intends to partially allocate toward building more homes. Another reason is that only a limited number of builders can compete for the size of sites Barratt Developments typically acquires - around two hundred plots – and those that can have sophisticated and explicit frameworks for evaluating land purchases based on expected returns. Barratt, for example, applies a strict twenty-three percent gross margin hurdle when considering new land acquisitions. The group determines the purchase price it is willing to pay by factoring in all known variables at the time, such as labor costs, material costs, Section 106 requirements, infrastructure costs, site design, overhead expenses, etc. In other words, in many ways the land price is the residual plug value. Other major builders, who collectively account for a substantial portion of scaled greenfield land acquisition, follow similarly disciplined approaches. For example, Taylor Wimpey, Bellway, and Persimmon each have their own specific margin hurdles for land acquisition in the mid-to-high twenties percent. This cooperative behavior has helped to keep greenfield land affordable, which is evidenced by inflation in greenfield land pricing being roughly three percent per annum over the last quarter century, versus five percent per annum for housing prices.

Finally, there is an unappreciated resiliency that comes as a result of land being the residual in the homebuilders' underwriting process. Consider that while Barratt produced an accounting operating profit in the depths of the global financial crisis, this impressive result nonetheless understated the cash generation of the business. This is because as the downturn unfolded the cost of plots being pulled through on the income statement (i.e., old pricing), and what Barratt could then obtain plots for in the current land market (i.e., new pricing) were quite different figures. Said differently, while the average sales price of a home was falling during the housing crisis, so too was the required replacement capital expenditure. This dynamic alone produced more than £100 million in additional annual free cash flow through the downturn.

Partnerships

A structure growing in relevance in the United Kingdom is what is referred to generally as the partnerships model. In traditional homebuilding, maintaining a viable land pipeline requires significant capital investment, and homebuilders like Barratt, even with careful alignment of build-to-sell rates, remain exposed to the cyclical nature of consumer demand. However, in the partnerships model, homebuilders partner with a diverse range of organizations, such as Homes England, local housing authorities, registered social housing providers, and financial institutions to trade a lower build margin for surety of demand and a lesser capital intensity. These arrangements can take many forms. For example, the build-to-rent (BTR) sector is nascent in the United Kingdom and is growing very quickly. Homebuilders can partner with private rental sector (PRS) landlords, often large financial institutions, who will pre-purchase units from a given development to hold for rent. This allows the PRS provider to obtain units built to specification at a discounted price, while concurrently enabling the homebuilder to decrease the capital intensity and risk profile of a given development. Specific examples include Barratt Developments' partnership with Citra Living, owned by Lloyd's Banking Group, which has delivered over 1,500 homes since 2021, and Vistry Group's partnership with Leaf Living and Sage Homes, owned by Blackstone and Regis Group, which recently announced a landmark agreement for 2,900 PRS units. Today, there are an estimated sixteen thousand BTR units delivered annually in the United Kingdom, which has grown significantly in recent years. However, Savills estimates that there is a need for an additional one million PRS units in the United Kingdom over the next decade, which given lethargic supply growth in the remainder of the PRS market, would require substantial growth still from existing BTR volumes.



Another structure could be partnering with a local authority on a housing development. Local housing authorities in the United Kingdom own 1.3 million acres of land, or enough for more than five million home plots. In these partnership structures, a local authority will often contribute the land to the development, which comes pre-consented, while the homebuilder will execute on the planning, design, and construction. Sometimes there are small upfront cash payments for the land, other times not, and local authorities may elect to either share in the profits of the development or receive housing stock as payment. These developments are often sixty to seventy percent affordable housing, with the balance being private homes for sale. It is worth pausing here to highlight why many investors are enamored by the partnerships model. Consider the graphic below which contrasts the economics of the traditional homebuilding model with the partnerships model.

Traditional Homebuilding	
Land	£175,000
WIP	£125,000
ASP	£350,000
Margin (%)	19%
Margin ($)	£66,500
Invested Capital	£300,000
ROIC	**22.2%**

Local Authority Partnership	
Land	£0
WIP	£75,000
Affordable ASP	£165,000
Magin (%)	10%
Private ASP	£350,000
Margin (%)	19%
Affordable / Private	70% / 30%
Affordable Margin ($)	£11,550.0
Private Margin ($)	£19,950.0
Invested Capital	£75,000
ROIC	**42.0%**

Although the operating margins are lower, often in the range of ten to fifteen percent, the returns on capital invested are significantly higher because of the lower capital intensity. In the example above, a partnership with a local housing authority, not only does the homebuilder avoid the capital requirement of owning land, but because of the presold nature of the development they can also increase the build speed of the site which decreases capital tied up in work in progress. Finally, another form a partnership can take is as a large-scale regeneration project in collaboration with Homes England. This governmental body is responsible for unlocking land and accelerating housing delivery in the United Kingdom. As a major public sector landowner with over twenty thousand acres in its portfolio, Homes England often oversees regeneration sites that need public sector involvement to become viable development opportunities. An example of this would be Barratt Development's Coypool Park development in partnership with Homes England that is slated to deliver 550 homes on the site of a former industrial china clay drying facility. In recent years, Barratt has achieved roughly ten percent of its completions through partnerships. However, it is important to note that Barratt Developments does not share the view held by some homebuilders, like Vistry Group, and investors that the partnerships model is a panacea. One reason for this is that the partnerships model inherently relies on external parties to meet annual delivery targets. Partnerships have been a bright spot in the slow current housing market; however, through cycle there is uncertainty about the security of supply necessary to support large-scale dedicated builders. Consider that there are approximately eighty thousand partnership completions annually in the United Kingdom which are divided between fifteen thousand BTR completions and sixty-five thousand affordable completions. However, of those, section 106 deliveries that are required

of all homebuilders account for thirty thousand completions. Thus, when considering partner funded deliveries from partnership-centric sites, the aggregate market is about one-fourth of the homebuilding industry by completions, and significantly smaller by profit dollars. Perhaps this is large enough to support one or two scaled builders, who then still depend on the efficacy of government agencies, local councils, and financial institutions for their pipeline of work. Next, as can been seen in the illustrative partnerships model economics from above, although a given partnerships development may be up to seventy percent pre-sold, the open market private home sales still account for a significant portion of the site's profit dollars. This is because the private homes have both higher ASPs and higher margins. This dynamic can become problematic as private market buyers can be apprehensive to move into a development with a mix that skews heavily towards renters and subsidized housing. In other words, the private market units in a partnership development are still vital to the economics of a site, but also carry an increased risk of margin degradation versus an equivalent unit on a traditional homebuilding development where the mix is eighty percent private homes and only twenty percent affordable. Finally, in the United Kingdom the long term scarcest resource is labor, which puts the partnerships model, a labor only structure that skews heavily affordable, at a distinct competitive disadvantage. For instance, a traditional homebuilder would generate approximately a dollar of gross profit for every dollar of labor spend, while a partnerships builder would generate only fifty cents of gross profit for the same dollar of labor. When there is slack in the labor market at a trough in the housing cycle, this presents no issue. However, as the market recovers, traditional homebuilders can bid on labor rates in a way that is likely to be disruptive to partnerships developers. All of that said, for Barratt Developments partnerships provide a free option for additional growth. To the extent that the incoming Labour Party properly incentivizes increased affordable building, or to the extent that BTR volumes continue to grow at rapid rates, Barratt is one of the few homebuilders that has the reputation and technical expertise required to take advantage.

Barratt Redrow Plc

On February 7th, 2024, Barratt Developments announced its intention to buy Redrow Plc, the seventh largest homebuilder in the United Kingdom for £2.5 billion in a share for share transaction. Redrow was founded in 1974 in North Wales and over the past fifty years has built more than 120,000 homes, including 5,436 home completions in the most recent period. Redrow offers new build homes with the character and style of traditional homes, aimed at the premium end of the market. These homes average thirteen hundred square feet and are priced at around £480,000 on average. However, the Redrow range includes homes priced at over £1 million and the arts and crafts style architecture of the group's Heritage Collection make the product distinct in the marketplace. The combined group will add the Redrow brand to Barratt Developments' existing brand portfolio to create a broader offering for customers, across a greater range of home types and price points. As has been witnessed in the past, this has the potential to accelerate the utilization of the combined groups extensive land pipeline by introducing Redrow brands on certain appropriate Barratt sites and vice versa. Recall that dual-branded sites have sales volumes that are meaningfully higher than single-branded sites. For example, Grey Towers Village was a David Wilson Homes site that was subsequently dual-branded, adding Barratt Homes and opening a Barratt sales outlet. Absorption at the site increased from the previous four year average of 0.47 units per week, to 0.94 units per week for the three years following

the introduction of the Barratt brand. Framed another way, this site went from trading at thirty percent below the group's average absorption rate during the prior period, to trading at twenty percent above the group's average absorption rate following the dual-branding. Like Barratt, Redrow maintains a strong land pipeline, with four years of owned immediate land, and nearly seven years supply of strategic land. Altogether, the combined group will have 85,000 immediate land plots and nearly 250,000 strategic and promotional land plots, the industry's largest land portfolio by far. Furthermore, in addition to enhancing the utilization of the existing land pipeline, this merger will strategically benefit Barratt Developments by allowing them to bid on very large scale sites – those nearing one thousand plots – knowing they can bring a diverse portfolio of brands to the development. Naturally, there is even less capital competing for these sites which can yield compelling deal values. Finally, Barratt expects to achieve at least £90 million in cost synergies through the optimization of division structures, consolidation of management overhead, and via procurement-related savings.

Valuation

As a traditional homebuilder with a substantial owned land portfolio and a significant net cash balance, Barratt Developments has ample downside protection. While we have previously highlighted the countercyclical nature of maintenance land expenditure, it's worth noting that this excess cash flow dynamic is, of course, most extreme when land purchases are halted altogether. In other words, when the business is being liquidated. For instance, on a typical home sale with an ASP of £350,000, Barratt Development would expect to make approximately £67,000 in pretax profit. However, land is a cost of goods sold that averages roughly sixteen percent of ASP, or £56,000 per plot. Therefore, if Barratt opted to cease its land buying operations and not replace each plot sold, it would pocket more than £120,000 in cash flow per home, resulting in a thirty-five percent cash margin. Let's carry the analysis further to estimate what shareholders of Barratt Redrow Plc might expect if the company were to liquidate. The combined group currently owns 82,595 immediate land plots, which equates to three to four years of build volumes. Recall that an average Barratt site is a development of two hundred plots that has a sales period of roughly four years. Hence, these plots are not open pasture awaiting development. The large majority of these plots are in developments that are established communities and have been selling for years. The underwritten ASP within this land pipeline is approximately £350,000, which includes the impact of section 106 requirements. Assuming Barratt

Redrow Plc constructs and sells these homes at an operating margin of seventeen percent, a figure in-line with the companies' extensive operating history and a discount to recent years' results, this would generate £4.92 billion in pretax profit. In addition, with respect to these volumes, Barratt Redrow would receive a £4.1 billion return of capital from its land investment and a £2.2 billion return of capital from work in progress, resulting in a total pretax cash flow of £11.2 billion. Next, the combined group also has a substantial strategic land bank where at any point in time approximately twenty percent of plots are already included in local draft plans. If we give Barratt Redrow credit for only these plots, this would provide for roughly another year of completions and an additional £2 billion in pretax cash flow. Altogether, including taxes, other liabilities, and the group's nearly £1 billion of net cash, this results in a liquidation value of £11.4 billion or a 1.67x multiple on the combined group's market capitalization and an implied IRR of nearly twenty percent.

Liquidation Scenario	***BDEV***	***RDW***	***Total***
Owned Plots	*57,683.0*	*24,912.0*	*82,595.0*
Owned land bank ASP	*331.0*	*395.0*	*350.3*
Owned Plots x ASP	*19,093.1*	*9,840.2*	*28,933.3*
Operating Profit (@17%)	*3,245.8*	*1,672.8*	*4,918.7*
Strategic Plots in draft	*21,550.0*	*7,500.0*	*29,050.0*
Owned land bank ASP	*331.0*	*395.0*	*347.5*
Stategic Plots x ASP	*7,133.1*	*2,962.5*	*10,095.6*
Operating Profit (@20%)	*1,426.6*	*592.5*	*2,019.1*
+ Net Cash	*865.0*	*125.0*	*990.0*
+ Net Land Bank	*2,680.3*	*1,420.0*	*4,100.3*
+ Net WIP	*1,550.0*	*642.0*	*2,192.0*
+ Gladman WIP	*106.0*		*106.0*
- Fire Safety Liabilites	*(700.0)*	*(180.0)*	*(880.0)*
- Tax	*(1,355.0)*	*(656.9)*	*(2,012.0)*
Liquidation Value	*7,818.8*	*3,615.4*	*11,434.2*
		Capitalization @ £4.75	*6,887.5*
		MoC	1.7x
		5 Yr FCF (Straight Line)	*2,286.8*
		IRR	19.7%

I believe this analysis is conservative in several ways that are worth calling to attention. First, while operating margins are assumed to be in-line with history, if the group did elect to liquidate there would be opportunity to reduce overheads by eliminating roles associated with securing and planning new developments. This could be up to a thousand positions and when combined with the cost synergies already scoped for the Barratt Redrow merger amount to as much as an additional two percentage point uplift in operating margin. Second, there is significant value to Barratt Redrow's strategic land and promotional land portfolio beyond what is accounted for in this analysis. For instance, Barratt purchased Gladman Developments, its wholly owned land promotion division, for £250 million in 2022. Gladman has historically had a seventy percent success rate in securing planning consent on its promotional sites and its current portfolio totals 102,360 promotional plots. Similar to the economics of an option agreement, land promoters generally receive a twenty percent fee on the sale of successfully promoted land. Thus, at current

market rates, Gladman's existing portfolio over time can be expected to realize more than £700 million in revenue and £350 million in pretax operating profit under the business' historic margin structure. When combined with the existing £106 million in work in progress this results in approximately £450 million in pretax cash flow. Now, consider that Barratt Redrow's strategic land bank with more than 140,000 plots carries similar economics. The combined value approaches nearly £1 billion in pretax cash flow. Third, implicit in this analysis is that the value of Barratt Redrow is zero without tangible land holdings when that is far from the case. The extensive track record and know-how of the combined group is immensely valuable, and could be leveraged into becoming a smaller pure partnerships builder. At half the level of completions, Barratt Redrow's partnerships business could add a further £2 billion to £3 billion of terminal value. Finally, consider what must occur to experience a permanent impairment of capital as a shareholder. During the global financial crisis, home prices in the United Kingdom dropped approximately twenty percent from their peak in the summer of 2007 to their lowest point at the end of 2008. They then gradually recovered, surpassing the previous peak by 2014. If we were to experience a housing collapse of a similar magnitude, except this time with no price recovery, Barratt Redrow's operating margins would drop to zero percent. In other words, for each unit sold the group would only recover the cost basis of its land and construction. In this scenario, assuming that Gladman Developments and the strategic land bank are entirely worthless, and that Barratt Redrow has no ability to win contracts as a partnerships builder, then shareholders would recover approximately £6.4 billion, or ninety-two cents on the dollar. Of course, this is all an exercise in theory, as Barratt Redrow Plc is significantly more valuable as an ongoing operating entity. Consider the base case scenario modeled below. This shows the combined group returning to peak levels of activity by 2028, which is achieved predominantly through growth in multi-branded sites. Following its recent return to the land market, Barratt Developments is expected to return to normal site levels in 2026, and thereafter site growth in the combined group is attained from Redrow opening outlets on five percent of Barratt sites, and Barratt opening outlets on twenty percent of Redrow sites. The projected cost synergies from the merger are accounted for, offset by expectations for minimal home price inflation and clearing the backlog of lower return land in 2025 and 2026. The result is a share price of £8.79, or approximately eighty-five percent upside to intrinsic value. Expressed a different way, assuming Barratt Redrow's share price of £4.75 remains unchanged, the combined group would generate enough free cash flow over the coming five years to repurchase two-thirds of the outstanding common stock, at which point shareholders would be left with a growing, high-quality, unlevered business that trades at two times earnings.

BASE CASE SCENARIO					
	FOR THE YEAR ENDED				
	Year +1 (GBP million)	Year +2 (GBP million)	Year +3 (GBP million)	Year +4 (GBP million)	Year +5 (GBP million)
Operating Metrics					
Sites (Barratt)	315	352	370	375	375
Sites (Redrow)	115	120	125	130	135
Absorbption (Barratt)	0.60	0.65	0.68	0.70	0.70
Absorbption (Redrow)	0.62	0.68	0.70	0.70	0.70
Private ASP (Barratt)	350.0	357.0	364.1	371.4	378.9
Priavte ASP (Redrow)	475.0	484.5	494.2	504.1	514.2
Affordable	3,384	4,035	4,408	4,596	4,641
Affordable ASP	180.0	180.0	180.0	180.0	180.0
Private Completions	13,535.6	16,140.8	17,633.2	18,382.0	18,564.0
Total Completions	16,919.5	20,176.0	22,041.5	22,977.5	23,205.0
Financials					
Private Sales	5,200.9	6,303.3	7,012.7	7,455.2	7,697.9
Affordable Sales	609.1	726.3	793.5	827.2	835.4
Total Sales	5,810.0	7,029.6	7,806.2	8,282.4	8,533.3
Land	(1,123.2)	(1,286.4)	(1,322.6)	(1,403.1)	(1,447.8)
%	*-19.3%*	*-18.3%*	*-16.9%*	*-16.9%*	*-17.0%*
Materials, Labor, and Infrastructure	(2,965.6)	(3,579.9)	(3,976.1)	(4,220.9)	(4,348.3)
%	*-51.0%*	*-50.9%*	*-50.9%*	*-51.0%*	*-51.0%*
Contribution after land and build	1,721.2	2,163.4	2,507.4	2,658.4	2,737.2
%	*29.6%*	*30.8%*	*32.1%*	*32.1%*	*32.1%*
Site and division based operating costs	(683.5)	(744.6)	(785.4)	(809.2)	(825.4)
%	*-11.8%*	*-10.6%*	*-10.1%*	*-9.8%*	*-9.7%*
Adjusted gross profit	1,037.7	1,418.8	1,722.1	1,849.2	1,911.8
%	*17.9%*	*20.2%*	*22.1%*	*22.3%*	*22.4%*
Administrative Expenses	(368.5)	(370.4)	(379.2)	(390.5)	(402.3)
%	*-6.3%*	*-5.3%*	*-4.9%*	*-4.7%*	*-4.7%*
Profit before tax	669.2	1,048.5	1,342.9	1,458.6	1,509.5
%	*11.5%*	*14.9%*	*17.2%*	*17.6%*	*17.7%*
Share of Profit from Joint Ventures	37.5	37.5	37.5	37.5	37.5
Gladman Developments Profit	27.5	27.5	27.5	27.5	27.5
Tax Expense	(212.9)	(322.9)	(408.3)	(441.8)	(456.6)
Earnings	521.4	790.7	999.8	1,081.9	1,118.1

VALUATION	
Discount Rate	8%
Terminal Multiple	12x
Net Cash	110.0
CF Value	3,510.5
Terminal Value	9,131.3
IV / Share	8.79
Upside to IV	*85.1%*

Conclusion

I am confident that our partnership owns a collection of businesses that, relative to the price paid, will produce a substantial amount of free cash flow over the coming years. These businesses set for us a demanding hurdle, against which our pipeline of companies that are underappreciated, run by operators with high co-ownership, and available at attractive prices remains robust. As always, I am happy to speak with you at length about any of our companies, and I remain grateful for your trust and partnership.

Appendix A: Realized Investments

Ticker	Company	IRR*	MSCI ACWI	Delta
-	-	94.69%	17.29%	77.39%
-	-	3.19%	13.84%	-10.65%
-	-	46.07%	14.10%	31.96%
-	-	37.70%	17.21%	20.49%
-	-	3.29%	8.86%	-5.57%
-	-	28.08%	14.16%	13.92%
-	-	10.00%	2.09%	7.91%
-	-	38.91%	21.19%	17.72%
-	-	20.01%	14.81%	5.20%
-	-	27.84%	17.45%	10.40%
-	-	29.94%	14.95%	14.99%
-	-	18.71%	16.74%	1.97%
-	-	37.17%	15.28%	21.89%
-	-	42.56%	-2.85%	45.41%
-	-	93.23%	3.95%	89.28%
-	-	25.79%	5.39%	20.40%
-	-	152.89%	8.50%	144.39%
-	-	30.52%	6.80%	23.72%
-	-	-45.74%	6.17%	-51.91%
-	-	-27.90%	8.14%	-36.04%
-	-	52.40%	12.64%	39.75%
-	-	1.79%	-9.64%	11.43%
-	-	-27.62%	0.00%	-27.62%
-	-	-47.93%	0.00%	-47.93%
-	-	-23.85%	-5.67%	-18.18%
-	-	7.17%	-6.36%	13.53%
-	-	-14.32%	27.25%	-41.58%
-	-	67.27%	33.60%	33.67%
-	-	43.42%	9.53%	33.89%
-	-	43.62%	16.98%	26.64%
-	-	-60.75%	-4.47%	-56.28%
-	-	42.27%	9.61%	32.65%
-	-	-15.20%	0.56%	-15.75%
	Average	22.28%	9.34%	12.94%

**Table above reflects the IRR of realized portfolio investments (unannualized if < 1 Year), and the equivalent IRR that would have been achieved had each invested dollar been allocated to MSCI ACWI.*

Appendix B: Unrealized Investments

Ticker	Company	IRR*	MSCI ACWI	Delta
-	-	41.10%	16.06%	25.04%
-	-	30.08%	16.96%	13.12%
-	-	32.38%	12.85%	19.53%
-	-	20.01%	11.46%	8.55%
-	-	-8.65%	7.36%	-16.01%
-	-	8.27%	17.68%	-9.41%
-	-	-8.02%	6.25%	-14.27%
-	-	40.84%	11.93%	28.91%
-	-	-6.84%	2.46%	-9.30%
-	-	7.59%	5.27%	2.32%

**Table above reflects the IRR of unrealized portfolio investments (unannualized if < 1 Year), and the equivalent IRR that would have been achieved to date had each invested dollar been allocated to MSCI ACWI. As of 8/13/2024.*

Disclosures

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Net performance figures are for a typical client under the standard fee arrangement. Returns for clients' capital accounts may vary depending on individual fee arrangements. Net performance figures for Emeth Value Capital, LLC are reported net of all trading expenses, management fees, and performance incentive fees. Reported returns prior to January 1st, 2021 reflect the personal account performance of Emeth Value Capital, LLC's sole managing member, and therefore represent related performance. All performance figures are unaudited and are subject to change.

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