Seeking Alpha α

Invest at a Discount in The Rothschild's Listed Family Office: RIT Capital Partners

2 September 2020

Summary

- RIT Capital trades at a rare discount to its NAV.
- Get exposure to alternative investments that are hard to come by for retail investors.
- The fund has an excellent track record with high returns and below-average risk.
- Morningstar gives RIT its maximum amount of stars.

RIT Capital Partners offers investors to partner up with finance royalty, the Rothschilds. It not only invests in public securities, but also in private companies and commodities. This gives an individual a good way to get exposure to these asset classes. Currently, this investment trust (a closed-end fund) is trading at a discount to its NAV. So, given the discount and the quality, it's a buy.

Fund overview

RIT traces its origins back to the Rothschild family bank, N. M. Rothschild & Sons. Here, in the early seventies, Jacob Rothschild took on the role of chairman of the Rothschild Investment Trust and started growing the asset base. In 1980, it split out of the family bank. The current form originates from 1988 when the company split into two listed entities: St. James's Place and RIT Capital Partners.

Since 1988, the returns have been excellent. If you've had 10,000 GBP invested in RIT at its IPO, it would have grown to 313,000 GBP at the 30th of June of this year with dividends reinvested.

Source: Morningstar

As can be seen at the end of the graph, there currently is a significant discount to the NAV. Which is something that hasn't occurred since 2014, and the current discount of a bit over 6.5% is rather larger.

The experts over at Morningstar also have a high opinion of the fund:

Morningstar Risk & Rating Statistics RCP

07/31/2020	3-Year	5-Year	10-Year
Morningstar Return			
RCP	High	High	Above Average
Morningstar Risk			
RCP	Below Average	Below Average	Average
Morningstar Rating			
RCP	★★★★★	★★★★★	★★★★★
# of Funds in Category	—	—	—

Source: Morningstar

Five stars is the highest category, and it's easy to see why. The fund produces above-average returns at below-average risk. Or a low beta for alpha, if you wish. This is demonstrated by the fact that RIT has participated in the market upside for 73% of the time and only joined in a market decline for 38% of the time.

Something to consider is that buying the OTC-listing is difficult since there is hardly any liquidity. The listing on the London Stock Exchange provides ample liquidity. In London, RIT is also included in the

FTSE 250, the main midcap index, and the broader FTSE 350, which is a combination of the aforementioned FTSE 250 and the more widely known FTSE 100.

In the title, I call RIT a family office. This is because of its origin, but it has other reasons too. First, the Rothschilds still own a sizable chunk of it:

Major Shareholders Information

Shareholder Name	Amount	% Holding
Lord Rothschild*x	19,267,873 #	12.28
Hannah Rothschild*	15,193,064 #	9.69
The Rothschild Foundation*	15,181,204	9.68
Five Arrows Limited+	6,757,835	4.31

The above table does not include Lord Rothschild's or Hannah Rothschild's direct voting rights in shares in the Company which are below the notifiable threshold.

* As Lord Rothschild and Hannah Rothschild are trustees of the Rothschild Foundation, the above notifiable interests include the same 15,181,204 shares held by this charity.

x Part of Lord Rothschild's holdings include entities where Hannah Rothschild is one of the beneficiaries.

+ Lord Rothschild and Hannah Rothschild have an indirect beneficial interest in the shares of the Company held by Five Arrows Limited.

Source: RIT Capital Partners

Personally, I consider this to be a good thing. Aligning interest makes for a beneficial policy for all parties if all can lose or win somewhat equally.

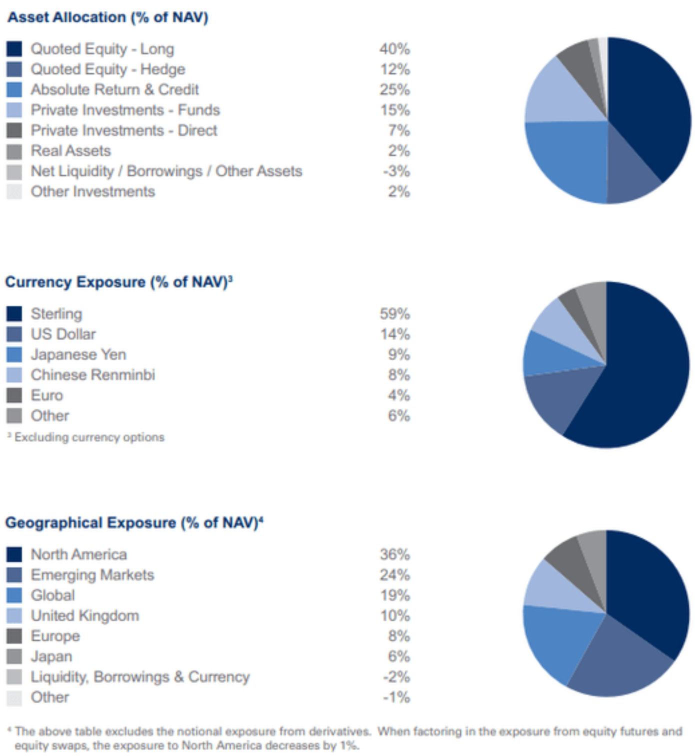
The second reason I call it a family office is that RIT's investment setup makes it so. For most rich families that start a family office, the wealth mostly originates from a specific source such as a business. This is a certain risk element, and the family office is often a low-beta stabilizer. It resembles Warren Buffett saying: "Rule No.1: Never lose money. Rule No.2: Never forget rule No.1." Key is that there is a long investment horizon and that the members are not in need of distributions for their daily needs and can financially handle risk. The last thing is rather different from something like a pension fund. This all is excellently captured in RIT's corporate objective and investment policy.

> Corporate Objective
>
> To deliver long-term capital growth, while preserving shareholders' capital; to invest without the constraints of a formal benchmark, but to deliver for shareholders increases in capital value in excess of the relevant indices over time.
>
> Investment Policy
>
> To invest in a widely diversified, international portfolio across a range of asset classes, both quoted and unquoted; to allocate part of the portfolio to exceptional managers in order to ensure access to the best external talent available.

Source: RIT Capital Partners

Fund Holdings

As stated in the investment policy, the holdings of RIT are across the global and across a variety of asset classes. Currently, it produces the following charts as of the end of July:



Source: RIT Capital Partners

First, to cover the currency exposure. This looks to be heavily reliant on the British pound with 59% of NAV. However, this is not really an issue. This is because it only shows the denomination of the investments, such as at fund unit level. Therefore, the fact that RIT uses primarily the GBP is not much of an issue. The third pie, the geographical exposure, is proof of it.

It doesn't come as a surprise that regarding the geographical exposure North America has the highest percentage. With roughly a quarter invested in emerging markets, RIT should profit from the rise of these new global powerhouses such as China. Something that does stand out is the fact that the exposure to the United Kingdom is higher than the entire markets of continental Europe. This could hint at some form of home equity bias at RIT, especially since the UK equity market represents about 5% of the global financial market. This relatively large exposure could come from the fact that RIT has Spencer House, a large mansion in London, and some other properties in the surrounding St. James area on the books. So, having their HQ included in the calculations does skew the percentages a bit. Another reason could be that the UK scores rather well on several value ratios compared to the rest of Europe.

The first chart shows the asset allocation, but it might be better to take a closer look:

Investment holdings	Country/region	Industry/description	Value of investment £ million	% of NAV
Quoted equity				
Stocks:				
Acorn[1]	Global	Consumer staples	98.3	3.2%
Helios Towers	Africa	Communication services	42.1	1.4%
Alphabet	United States	Information technology	34.4	1.1%
IQVIA Holdings	United States	Healthcare	27.0	0.9%
Booking Holdings	United States	Consumer discretionary	15.0	0.5%
CDK Global	United States	Information technology	14.8	0.5%
3G[2]	United States	Consumer discretionary	14.0	0.5%
Frontdoor	United States	Consumer discretionary	11.1	0.4%
Other stocks	–	–	57.7	1.9%
Total stocks:			314.4	10.4%
Long-only funds:				
HCIF Offshore	United States	All-cap, biotechnology	190.2	6.2%
Morant Wright[3]	Japan	Small/mid-cap, value bias	147.1	4.8%
Springs Opportunities	China	All-cap, diversified	120.5	4.0%
BlackRock Emerging Markets	Emerging Markets	All-cap, value bias	77.0	2.5%
Ward Ferry Asian Smaller Companies	Asia	Small/mid-cap, diversified	74.6	2.4%
Sand Grove UK	United Kingdom	All-cap, diversified	57.4	1.9%
Lansdowne New Energy	Global	All-cap, clean energy	48.5	1.6%
Brown Advisory LATAM[3]	Latin America	All-cap, diversified	45.3	1.5%
Sumi Trust Japan	Japan	Small-cap, diversified	45.1	1.5%
Emerging India Focus	India	All-cap, diversified	40.6	1.3%
Other long-only funds	–	–	49.4	1.7%
Total long-only funds:			895.7	29.4%
Hedge funds:				
BlackRock European Hedge Fund	Europe	All-cap, diversified	130.6	4.2%
Gaoling	China	All-cap, diversified	92.1	3.0%
Springs Global Strategic Partners	China	All-cap, diversified	56.9	1.9%
RIT Discovery[4]	Global	All-cap, diversified	33.8	1.1%
ENA Opportunity	Europe	All-cap, diversified	26.5	0.9%
Tribeca	Global	All-cap, commodities	19.3	0.6%
Other hedge funds	–	–	1.9	0.1%
Total hedge funds:			361.1	11.8%
Derivatives:				
Global Value Basket	Global	Long, 1.0% notional	(1.8)	(0.1%)
iShares NASDAQ Biotech ETF Swap	United States	Short, 0.8% notional	(0.8)	(0.0%)
FTSE China A50 Futures	China	Short, 0.5% notional	(0.1)	(0.0%)
NASDAQ 100 Futures	United States	Short, 0.4% notional	(0.4)	(0.0%)
Other derivatives	–	–	(0.1)	(0.0%)
Total derivatives:			(3.2)	(0.1%)
Total quoted equity			**1,568.0**	**51.5%**

Source: RIT Capital Partners

With over half of the fund invested in quoted equities, it's clearly the most important asset class for RIT. About 20% of this is invested in stocks, mostly on the American exchanges. To highlight a few things: Acorn is not a listed entity itself, but a vehicle of JAB Holding Company. This holding company serves as the investment arm of one of the richest dynasties in the world, Reimann family of Germany. Acorn holds the interests in Keurig Dr Pepper (KDP) and JDE PEET'S, which listed this spring on the Amsterdam Stock Exchange.

The same can be said for 3G, the private equity firm run by billionaire Jorge Paulo Lemann. This PE firm was a driving force in creating Anheuser-Busch InBev (BUD) and also teamed up with Warren Buffett in combining Kraft and Heinz to form The Kraft Heinz Company (KHC).

The other 80% of quoted equities consist of funds. These are either traditional long-only or hedge funds. Both types of funds cover several flavours and provide additional diversification. Exposure to these hedge funds is not always possible as an individual investor, so having these in the mix is nice.

The derivatives are mainly there as additional hedging instruments.

Private investments – direct:				
Coupang	Asia	Information technology	72.9	2.4%
KeepTruckin	United States	Information technology	44.3	1.5%
CSL	United Kingdom	Information technology	31.7	1.0%
Age of Learning	United States	Information technology	11.6	0.4%
Other private investments – direct	–	–	85.2	2.8%
Total private investments – direct			**245.7**	**8.1%**

Investment holdings	Country/region	Industry/description	Value of investment £ million	% of NAV
Private investments – funds:				
Thrive Capital Funds	United States	Venture capital	101.8	3.3%
Iconiq Funds	United States	Venture capital	82.7	2.7%
Hillhouse Funds	China	Private equity	53.4	1.8%
BDT Capital Funds	United States	Private equity	52.0	1.7%
Ribbit Capital Funds	United States	Venture capital	14.7	0.5%
Mithril Funds	United States	Venture capital	11.2	0.4%
Eight Partners Funds	United States	Venture capital	11.8	0.4%
Sandler Capital V	United States	Private equity	10.7	0.4%
Other private investments – funds	–	–	151.0	4.9%
Total private investments – funds			**489.3**	**16.1%**

Source: RIT Capital Partners

The private investments consist of a third direct investments and two-thirds via funds. The direct investments have a heavy focus on the tech sector. Coupang, for example, is South Korea's largest e-commerce company and can count besides RIT also Softbank and Sequoia as its backers.

The fund section is divided between private equity and venture capital funds. This gives a broad exposure into alternatives, even if the focus lies on US-based managers. It is, however, a bit more difficult to value these holdings. Usually, fund managers update the NAVs only once a quarter, and in these times, it's hard to put a price on it as an outsider. Especially since not many private companies have their shares traded on alternative platforms such as SharesPost and EquityZen.

Absolute return and credit:				
Eisler Capital Fund	Global	Macro strategy	164.5	5.4%
Attestor Value Fund	Global	Distressed and special situations	119.5	3.9%
Elliott International	Global	Multi-strategy	114.8	3.8%
Tresidor Credit Opportunities	Global	Distressed and special situations	59.9	2.0%
RIT US Value Partnership	Global	Multi-strategy	57.4	1.9%
Farmstead Fund	United States	Distressed and special situations	50.2	1.6%
Caxton Dynamis	Global	Multi-strategy	47.1	1.5%
Sand Grove Tactical	Global	Multi-strategy	45.7	1.5%
LionTree Advisory Loan Note	Global	Corporate loan	32.5	1.1%
Farmstead AC530	Global	Distressed and special situations	28.3	0.9%
Hein Park Investors	Global	Distressed and special situations	19.9	0.7%
Highbridge	Global	Opportunistic credit	17.8	0.6%
Other absolute return and credit	–	–	35.3	1.1%
Total absolute return and credit			**792.9**	**26.0%**
Real assets:				
Spencer House	United Kingdom	Investment property	31.8	1.0%
St James's properties	United Kingdom	Investment property	27.0	0.9%
Gold futures	United States	Long, 3.6% notional	2.8	0.1%
Other real assets	–	–	6.0	0.2%
Total real assets			**67.6**	**2.2%**
Government bonds and rates:				
Euro 30-year swap	Europe	Short, 4.8% notional[5]	(1.7)	(0.1%)
Other government bonds and rates	–	–	2.8	0.1%
Total government bonds and rates			**1.1**	**0.0%**
Other investments:				
Currency forward contracts	–	Forward currency contracts	(6.0)	(0.2%)
Currency options	–	Premium	1.6	0.1%
Total other investments			**(4.4)**	**(0.1%)**
Total investments			**3,160.2**	**103.8%**
Liquidity:				
Liquidity	–	Cash at bank/margins	385.3	12.6%
Total liquidity			**385.3**	**12.6%**
Borrowings:				
Industrial and Commercial Bank of China loan			(85.0)	(2.8%)
Commonwealth Bank of Australia loan			(145.1)	(4.8%)
National Australia Bank loan			(148.5)	(4.8%)
RIT Senior Notes			(172.9)	(5.7%)
Total borrowings			**(551.5)**	**(18.1%)**
Other assets/(liabilities)			53.3	1.7%
Total net asset value			**3,047.3**	**100.0%**

Source: RIT Capital Partners

The final major group of holdings are funds that focus on credit and absolute returns. So, again, some hedge funds such as Elliott of billionaire Paul Singer. The credit funds mainly shy away from the typical government bonds, but are more aggressive. Given that the safest bonds offer negative returns, the pockets in which alpha can be found fall outside that scope. As said, RIT can take more risk than something like a pension fund, so it's good to see this direction in the credit markets. For most retail investors, this section of the markets is also too hard to operate in, so having it in a CEF such as RIT is a nice to have.

I've already written about the real estate, but the position in gold is worth mentioning. Historically, RIT has made bets on gold. For a large diversified fund, it can be interesting to do so. Primarily because most of the time gold can act counter-cyclical. So, to some extent, it's another hedge.

Finally, the liquidity. This seems to be good enough. With so much illiquid investments, it's important to have a decent buffer. So, that's in place with almost 400m GBP.

Conclusion

RIT Capital Partners is an excellent fund, which behaves like a family office. You get to partner with one of the biggest names in financial history. Not only that, but via the holding you get exposure to big names in the business such as Elliott's Paul Singer. Much of the investments RIT made are not open to the average retail investor, so an investment in RIT is one of the few ways to profit from the upside in these asset classes. The fund is taking on some of the more riskier investments, but these are well managed and hedged. In a similar way in which Michael Milken observed that bundling several risky fallen angels reduces the overall risk and boosts returns, RIT somewhat applies this across its portfolio. Given the excellent historical returns, the financial connections, broad portfolio and rare discount to NAV, I rate RIT a buy.