Higher Ground SICAV plc
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Valletta,
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Malta.

14th October 2022

Dear Investors,

After an 11% fall in the value of our units in the Core Wealth Fund during September, it's good to restate the thinking. Since I wrote to you soon after the start of the war in Ukraine, we have only made small changes to the portfolio. The businesses of the companies we own continue to do well even as their stock prices have been punished. Equity prices have been far more volatile than the earning power of the underlying businesses. I propose that it's that earning power of the underlying businesses that we care about.

We are interested in receiving a long-term flow of income from our investments that will put food on our tables for many years. The more direct and conventional way to do this would be to own equities and bonds that pay those dividends and coupons to us directly. The Core Wealth Fund is just a selector mechanism and a roll up of those cash flows.

But why do we have to tolerate such large swings in value in pursuit of stable and growing long term underlying cash flows? One year, those future cash flows might be discounted back to the present at an interest rate of 1%. Another year at 5%. The difference between the market values resulting from those two interest rates is very large although the future cash flows…. those that put food on the table…. haven't changed at all. Add to that fear and greed, which act on market values and not so much on the underlying prospects of the businesses, and we can suffer big swings in market value without any change in the underlying cash flows coming from the portfolio. For a deeper dive on this, my former colleague Victor Hagani recently published this excellent paper entitled, 'A Sheep in wolf's clothing'.

So, what is that underlying earning power of our portfolio? The equities we own produce a weighted average 6.93% dividend yield. So, for every 100 we have in equities, we received 6.93 in gross dividends last year. But our holdings taken together, paid out less than a third of their last year's net earnings. They made net profits of 20% of their current market price…again a weighted average. If you're more comfortable with Price/Earnings ratios, that means our portfolio is only on a P/E ratio of 5, (the inverse of 20%)…. amazingly cheap for good and growing companies. This is partly the market saying that it doesn't believe last year's earnings and dividends will be repeated, and partly the discounting and fear factors I mention above. Shame we're not better at forecasting those.

We are invested in close proximity to a major war. Volatility can be expected. There are great risks. Patience is required.

However, the countries where we invest will benefit from the eventual peace. We are invested in good companies which currently trade at very inexpensive prices.

Yours sincerely,

Richard Wood
Director