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Bargain Shares: Primed for new highs

A private equity investment company focused on technology, education and digital consumer market segments is delivering huge valuation gains and is poised to continue doing so

By Simon Thompson

Private equity investment company **Oakley Capital Investments** (OCI:438p) is a prime example of why it pays to run winners. Since I included the shares, at 146.5p, in my **2016 Bargain Shares Portfolio,** the share price has trebled in value and the board has paid out dividends of 27p, too.

The key reason for the outperformance lies in the unerring ability of Oakley's investment team to back the right type of company across three core market segments – technology, education and digital consumer – and then reap handsome gains on exit. A 20 per cent net asset value (NAV) compound annual growth rate in the past five years highlights their success.

A high proportion of investments have defensive characteristics, benefiting from strong structural market growth,asset-light business models and high cash conversion rates. Around 70 per cent of portfolio companies operate a subscription-based model or recurring revenue business model, so are less vulnerable to temporary declines in customer demand; and two-thirds of the portfolio deliver products or services digitally.

A robust start to 2022

- Total NAV return of 35 per cent in 2021
- Record NAV per share of 571p at 31 March 2022 driven by 6 per cent return in latest three-month period.
- £180mn (100p a share) cash accounts for 18 per cent of NAV
- £1bn commitments to be funded from existing balance sheet and proceeds from future realisations

These characteristics help explain why three-quarters of the 2021 portfolio valuation increase was driven by investee companies' profit growth. It also means more bumper exits are highly likely in the coming months.

Oakley's first-quarter trading update delivered more of the same for shareholders. In the three-month period, NAV per share increased 33p to a record high of 571p, and is now 41 per cent higher than at the start of 2021.

Around 75 per cent of the valuation increase was driven by profit growth of investee companies, and 25 per cent by multiple expansion. However, Oakley's portfolio is still only valued on an average multiple of 14 times cash profit to enterprise valuation. That is well below the private sector average even though the group's investee companies have delivered 28 per cent average annual growth in their cash profits over the past five years, a performance at the upper end of the peer group.

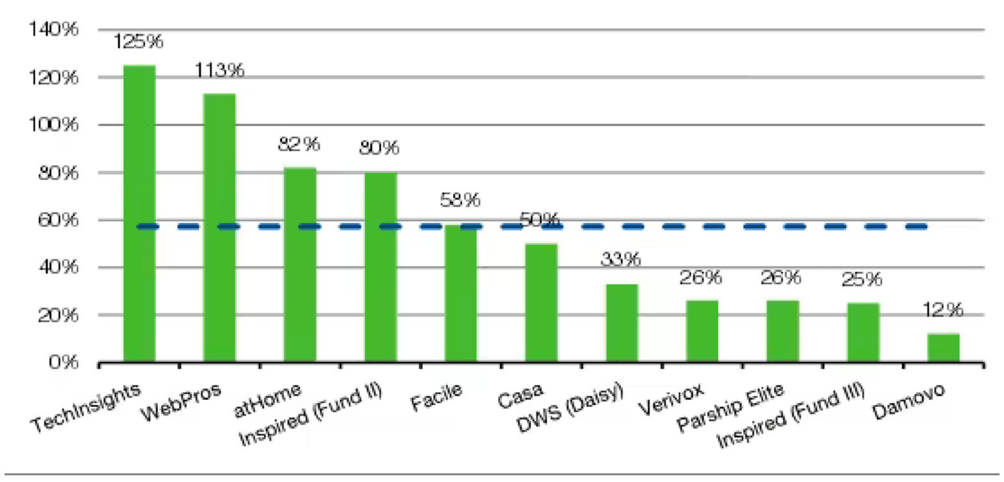
Bearing in mind the modest valuations, and the fact that Oakley's current portfolio is relatively mature – the average holding period is now three years, or six months less than the average for previous exited investments – then it's realistic to expect significant realisation activity this year. Indeed, the directors would not have upped their new fund commitments by £338mn over the next five years unless they had visibility on future realisations.

Since inception, Oakley has booked an average gain of 50 per cent above carrying value on exits, a point worth considering given that the buyout industry is awash with a record $1.4trn (£1.1trn) of 'dry powder' to invest. In other words, the investment backdrop is ideal for Oakley to make portfolio exits to release cash to recycle into new portfolio companies.

It's highly likely they will support further hefty increases in NAV per share, as highlighted by the recent disposal of Oakley's stake in TechInsights, an information services platform for the microelectronics sector, to a fund managed by CVC Capital Partners. The deal was pitched at a 134 per cent premium to Oakley's carrying value, adding 19p a share to NAV. However, despite the potential for further disposals above book value, Oakley's shares trade on an unwarranted 23 per cent discount to NAV, or six percentage points deeper than peers.

Please note that the shares are traded on the Specialist Fund Segment of the main market of the London Stock Exchange and are intended for institutional, professional, professionally advised and knowledgeable investors. This means that your broker may require you to pass a competency test before you can buy the shares. The track record of Oakley's investment team and potential for material uplifts in NAV mean it is a test well worth doing. Buy.

Estimated premium to book value at exit since the start of 2018



Source: Liberum, Company data

■ Simon Thompson's latest book **Successful Stock Picking Strategies** and his previous book **Stock Picking for Profit** can be purchased online at **www.ypdbooks.com**. The books are being sold through no other source and are priced at £16.95 each plus postage and packaging of £4.50 [UK].

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They include case studies of Simon Thompson's market beating Bargain Share Portfolio companies outlining the investment characteristics that made them successful investments. Simon also highlights many other investment approaches and stock screens he uses to identify small-cap companies with investment potential.

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