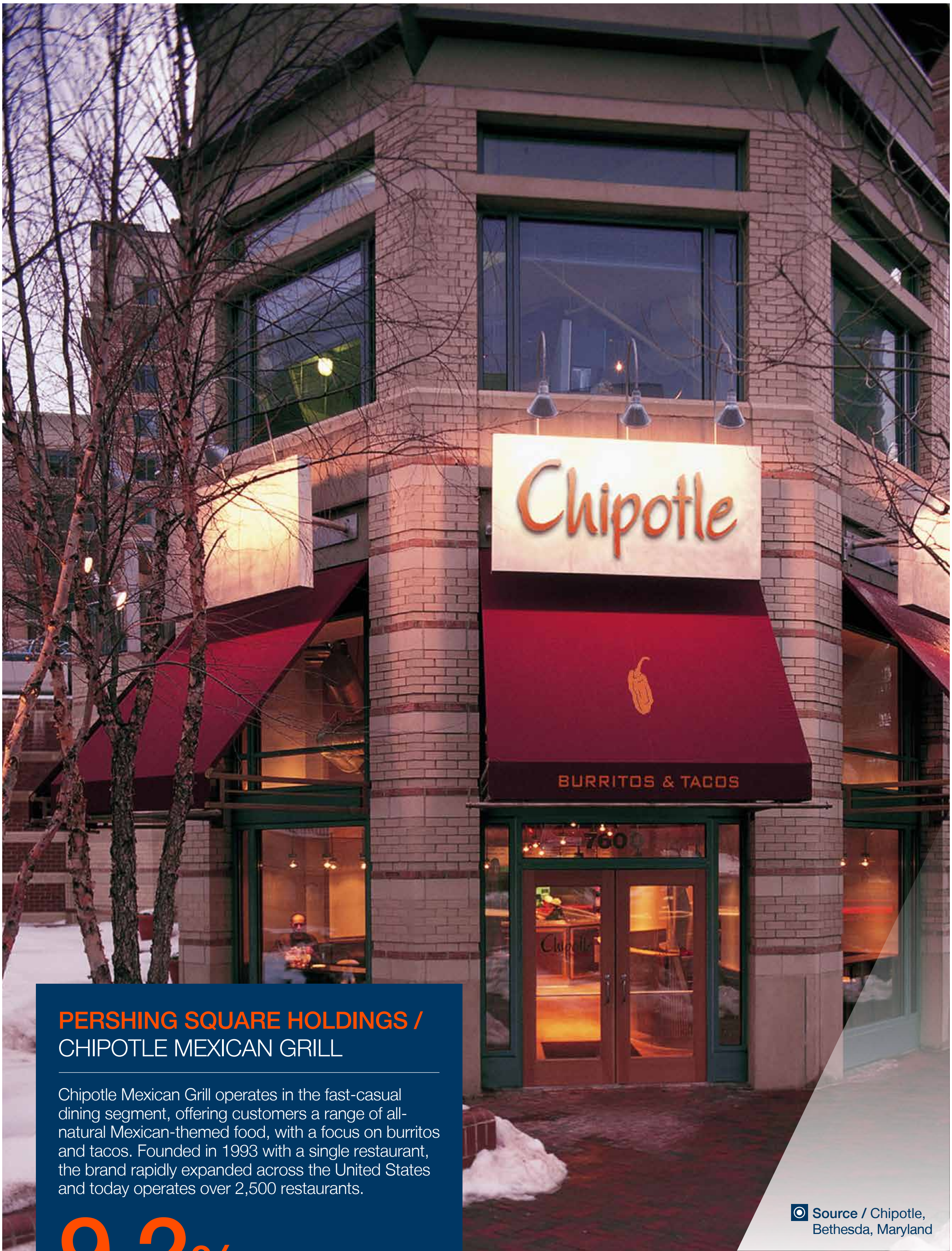

Source / Chipotle, Bethesda, Maryland

PERSHING SQUARE HOLDINGS / CHIPOTLE MEXICAN GRILL

Chipotle Mexican Grill operates in the fast-casual dining segment, offering customers a range of all-natural Mexican-themed food, with a focus on burritos and tacos. Founded in 1993 with a single restaurant, the brand rapidly expanded across the United States and today operates over 2,500 restaurants.

9.2%

% of portfolio

CONTRIBUTORS

PERSHING SQUARE HOLDINGS

Description Closed-end Fund	**Total return on position FY19 (local)**[2] 20.6%
% of portfolio[1] 9.2%	**Total return on position FY19 (GBP)** 24.2%
Discount -27.3%	**Contribution (GBP)**[3] 1.31%
% of investee company 2.7%	**ROI since date of initial purchase**[4] 37.8%

Pershing Square Holdings ('PSH') was the third-largest contributor to your Company's returns over the period, adding 131bps, driven by NAV growth of +33%. As a reminder, 40% of the PSH position is hedged (as at the financial year end) by shorting a pro rata amount of the underlying holdings; this provides the potential for equity-like returns from discount tightening (albeit this did not prove to be the case over the period) while not taking on equity market risk. The outright long position added 186bps to returns, and the hedged position reduced returns by -55bps as a result of the discount widening.

The majority of PSH's holdings produced strong returns, with positions in Chipotle (+85% total share price return), Starbucks (+60%), Restaurant Brands (+23%) and Hilton Worldwide (+16%) all being significant contributors. Only one stock, Lowe's Inc, produced negative returns (-2%).

PSH also holds stakes in Fannie Mae and Freddie Mac, option-style plays on housing market reform in the US. Over the year, those positions increased by +164% and +156% respectively as the US Treasury inched ever closer to overhauling the businesses and ending the government's claim over the companies' excess capital. (Note: these positions are not hedged given their non-equity-market risk profiles).

Despite the strong progress over the year, the share price discount to NAV widened out from 24% to 27%, which reduced share price returns slightly. PSH introduced some measures to combat the extraordinarily wide discount, including a quarterly dividend payment and a buyback programme for 3% of outstanding shares. While both of these measures are helpful at the margin, we believe that deeper structural solutions are needed to resolve the issue.

The discount, however, was not helped by the issuance of USD400m in debt with a 20-year maturity in August – a view which we made known to the Chairman of PSH by means of a public letter.

Our view, expressed in detail in the letter, was that the issue of such long-dated debt would act as a poison pill in constraining the ability of the company to tackle its very wide discount to NAV. While the eventual terms of the debt showed some concessions (e.g. caps after ten years on the make-whole premium due in the event of early repayment, offering some protection against further falls in interest rates), and hinted at a portion of the proceeds being used to refinance existing debt, these do not change our fundamentally negative view of the issue.

Taking a step back, it is highly debatable whether PSH should be refinancing its debt at all, let alone using very long-dated debt to do so. Given that the existing debt has been cited frequently in the past by the board and by the manager as an impediment to more aggressive share buybacks and/or tender offers, or other more structural solutions, there is a strong argument that it should be repaid in full at its maturity in 2022 and that the company should either be run on an unleveraged basis or levered using more flexible debt.

Aside from limiting the company's ability to manage its discount, the additional gearing increases the option value of the manager's performance fee (as performance fees can be viewed as a call option on NAV growth with the strike set at the high watermark, the more leveraged the company is, the more volatile its NAV will be, and the more valuable is that option). We have grave concerns that the board of PSH seems to have been blind to the consequences of, and conflicts surrounding, the recent debt issue.

We invested in PSH over two years ago, having conducted extensive due diligence on its portfolio and the manager's investment strategy, and have benefited from the strong NAV returns as performance has turned around. We continue to have a favourable view of the prospects for further share price appreciation from PSH's portfolio of high-quality, free cash flow-generative companies with limited capital expenditure requirements, high returns on invested capital and clear idiosyncratic drivers for earnings growth. We now await a similar "turnaround" from the board, which bears responsibility for the discount suffered by shareholders.

1 For definitions, see Glossary on pages 89 to 92.
2 Weighted returns adjusted for buys and sells over the year.
3 Figure is an estimate by the managers and sum of contributions will not equal quoted total return over the financial year.
4 Figure quoted in GBP terms. Refer to Glossary on pages 89 to 92 for further details.