

March 2022
Fountainhead Partnerships Fund
Quarterly Letter

Patience is bitter but its fruit is (often) sweet – Rousseau

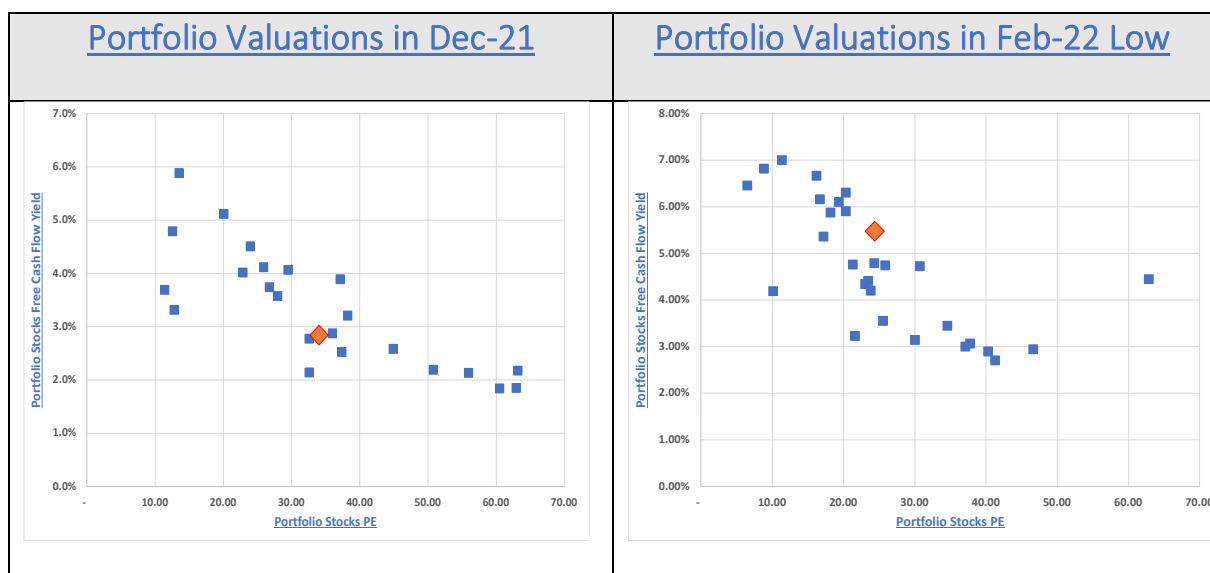
Fountainhead Partnerships Fund (FHPF) was up 3.4% in March with S&P 500 up 3.7% and MSCI World up 1.9%. In 2022 YTD, FHPF was -9% vs S&P 500 return of -5% and MSCI World -6%.

We increased our allocation to equities substantially in this quarter.

In this letter we share our thoughts on:

- [IQVIA](#) - our latest new holding and our rationale for increase equity allocation and hedging
- [Fundamental Attribution Error- An interesting study at Yale and its lessons for us and financial markets.](#)

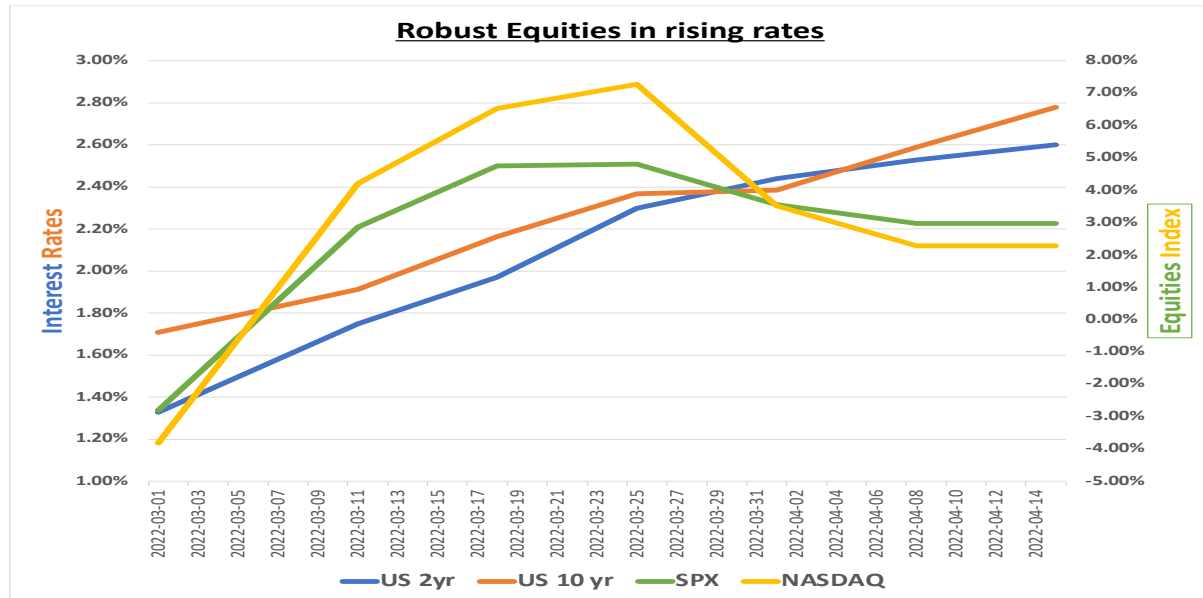
In our [update in mid-February](#) we explained to our clients why we believed it was a good time to increase our allocation to equities. The main reasons we cited were significant declines not only in prices but also in the valuations of our portfolio holdings, pessimistic and elevated volatility. These circumstances have historically been a good starting point for upside in equities.



The average PE and Free Cash Flow yield (orange diamond marker in the charts) of our portfolio in Dec-21 were 30x and 3% respectively.

At the lows in Feb-22 the average portfolio valuations came down 28% to 24x PE and 6% FCF yield which is 4-year low in our portfolio. This encouraged us to increase our equity exposure.

Market anxiety is currently driven by inflation and a significant increase in interest rates. Since 1st March, interest rates have risen ~130bps, a 2-standard deviation move above mean pace.



Interestingly, equities have been quite robust in the face of this move. The strong show from equities is suggesting;

- The rise in rates has already been discounted in January and February
- The market is expecting a much better earnings outcome than what is priced-in
- It is just a typical bear market rally and the correction may restart again soon.

We have no foresight into which one of the above is the most likely rationale for the strength in equities. The correction of 17-25% in the first two months was as bad as we get in a typical recession. The argument can be made that the market has already shaken-out the weakest hands.

It is remarkable the speed in which markets adjust in comparison to prior decades where grinding drawdowns are more typical.

The earnings picture has improved in the last two months; consensus earnings growth expectation for 2022 is 9.8% now vs 7.2% in Dec. Still, both S&P and Nasdaq have given up half of the gains of the rally from the bottom. To make it even more complicated, S&P500 implied volatility has fallen from 35 to below 20, making it much cheaper to hedge.

What are we doing in this scenario? As we have always mentioned in our notes, we are the buyer of valuable assets when they are cheap. We added to our equities holdings significantly in Jan and Feb when they were cheap and now we have been buying cheap hedges through options.

As of Apr14 we are ~40% hedged with SPY and QQQ put spreads.

IQVIA Holdings: A pre-eminent healthcare data company.

Mcap: USD 45bn. 2022- Earnings growth: 13.8%. P.E. 22x FCF yield: 5.6%

IQVIA (\$IQV) is a leading global provider of advanced analytics, technology solutions, and clinical research services to the life sciences industry. In 2016, Quintiles and IMS Health came together to become IQVIA. IQV is now the largest Clinical Research Organisation (CRO) in the world, operating in 100 countries, working with 85% of the largest pharmaceutical, biotech and medtech companies globally.

CROs are essential to the pharmaceutical, biotech and medtech industries - supporting their efforts to test, refine and market the latest drugs and devices. In 2021, the global CRO market was valued at USD70bn in 2021 and expected to grow by 10% in the next 10 years – the type of secular growth we demand.

Over the years we have developed a good understanding of the business model of CROs. We love this industry. There are very few operators in the space. The top 5 players generate 70% of the industry revenue, they have a significant moat of experience and the approvals to run product trials with an irreplaceable data set. They are riding on a significant tailwind of outsourcing from their customers.

CROs are extremely profitable companies and generally have very shareholder friendly management.

IQV operates in three segments – Technology & Analytics (40% of rev, 50% of operating profit) Research and Development/CRO (55% of revenue, 48% of operating profit) and Contract Sales (5% of revenue, 2% of operating profit). In the technology segment, IQV provides an extensive range of cloud-based applications and SaaS solutions. They are number-one in the world in the data and analytics solution providing a wide range of privacy and security safeguards to protect non-identified patient-level medical claims, prescriptions, electronic medical records, genomics, patient reported outcome and social media data. In CRO segment IQV service offerings include protocol design, feasibility and operational planning, site start up, patient recruitment and clinical site monitoring.

One of the key features of IQV and ICON (another portfolio holding) is the seemingly baked-in growth in their future. Their backlog is double their revenue and their net new bookings are rising at a faster pace than their revenues. They generate over 40% FCF return on equity with significant pricing power.

Both stocks were considered COVID beneficiaries as they provided significant support for Covid vaccine trials. Once the market started selling-off the pandemic beneficiaries, these names were sold-off as well. IQV declined over 30% from its high after its earnings announcement in the first quarter.

We considered it a very good buying opportunity in a leading healthcare data company and built our position in it.

Fundamental Attribution Error

[A study at Yale](#) highlighted how most people make a fundamental attribution error by correlating results with their pre-existing notions and ideas. The study finds that when large numbers of people are observed in a wide range of situations, the correlation for trait-related behaviour runs at about 0.20 or less. People think the correlation is around 0.80.

People's knowledge is not always expressed in their judgments and behaviour. For example, the study highlights that providing participants with statistical consensus information does not actually influence their consensus judgments.

Most of us think about the behaviour of objects and people much of the time in purely dispositional terms. Modern scientific psychology insists that explanation for the behaviour of humans always requires reference to the situation the person is in. The failure to make that situational inference sufficiently is known as the Fundamental Attribution Error (FAE).

In financial markets, making FAE is very common while assessing the future performance of a company. Berkshire Hathaway's stock declined more than 50% at least three times in the last 40 years. Although it was evident in hindsight that it was a mistake to sell the stock, a majority of investors still committed it.

The study asks: how can we be so hopelessly miscalibrated, particularly in financial markets? There are many reasons, but one of the most important is that we don't normally get the situational context right that facilitates assessments and calculation.

Thank You.