

My Investment Thesis on Amerco

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Amerco ticks all the boxes of a reinvestment moat, stewarded by excellent long-term business owners and capital allocators, and trading at a modest multiple of normal earnings power. The DIY moving market was essentially created with the founding by Leonard and Anna Shoen of Amerco in 1945. Today 40% of movers in North America are DIY vs. professional moving companies. Shoen spent decades signing up land-owner franchisees across North America, developing a network across the country which allowed users to collect vehicles in one location and drop off at another, facilitating 'inter-city' house moves.

U-Haul, the brand behind Amerco, has made the most of its first mover advantage by aggressively expanding its network of franchised moving service locations. Each additional location increases the value of existing locations by enabling more convenient pick up and drop off logistics for an increasing number of moving routes. This should increase the steady state asset utilisation of the business. Franchisees are attracted by the number of U-Haul customers; customers are attracted by the convenience of franchise locations. This virtuous circle drives market share and revenue growth, which has been reinvested in more locations and vehicles, making U-Haul's dominance increasingly difficult to replicate. Today U-Haul has eight times as many locations as its nearest competitor, and four times as many trucks. Management has clearly identified the source of the moat for this business and has continually reinvested capital in widening it over time. This network advantage limits the ability to add supply in the 'one-way', inter-city moving market.

Trucks are necessary for moving but people move infrequently; these characteristics lend themselves to a rental business model. Moving depends on idiosyncratic factors such as the need to upsize, downsize, get divorced, get married, move jobs, attend and leave college etc. The need for more affordable housing is a significant reason for moving, likely a countercyclical driver of volumes. If humans live in houses, regardless of how those houses are financed, and if changing life circumstances cause them to move homes several times through their lifetimes, none of these drivers of demand is set to change materially long into the future. It is very possible, however, that Amerco captures an increasing share of the total costs incurred in making these moves.

Another example of management directing capital to widening the business's unfair advantage is the development of MovingHelp.com. Movinghelp.com is a platform bringing together supply of and demand for moving labour. As the number of providers of labour grows, the more users are attracted by greater availability. The accumulation of independent reviews also creates stickier supply and encourages better customer service, increasing demand.

The U-Haul brand is well-recognised and ubiquitous; there are 65% more U-Haul locations in the North American network (20k) than there are Starbucks coffee shops (12k). The orange and white livery and U-Haul logos adorn its 100k trucks, 80k trailers, 20k truck rental nodes and 1,100 storage locations, serving as a free mobile and ubiquitous advertising machine.

Since its inception U-Haul has grown its dominance in DIY moving. Several competitors have tried to enter or grow in the space, but none has succeeded in denting U-Haul's market share. The industry has consolidated down to three main players today: U-Haul, Budget Truck Rental and Penske Truck

Rental. Budget generates 15% of the revenue of U-Haul with a truck fleet one quarter the size and has been retrenching, highlighting the economies of scale in the industry and U-Haul's network advantage.

The other major use of the company's operating cash flow has been the purchase and greenfield development of self-storage facilities. Like truck rental, self-storage is a commodity offering. The site acquisition and build costs are low, lowering barriers to entry. Hence there are many players in a fragmented industry. As fixed costs are high there may also be the temptation to cut prices to fill capacity. However, once tenants are secured, switching costs are high and so rent increases can be imposed.

This, coupled with low maintenance costs and high operating leverage, mean that returns can ramp up quickly. Amerco can use its U-Haul brand and ability to hook truck customers into the sales channel via its website to lower self-storage customer acquisition costs. This potentially lowers Amerco's self-storage breakeven price and occupancy vs. peers.

I think several factors suggest that the company's capital can be deployed at high incremental returns: a wider economic moat, industry consolidation, capital reinvestment into very high margin self-storage services, operating leverage, and declining labour intensity as technology lowers the cost of generating business.

Multiple avenues for earnings' growth suggest that owner earnings' reinvestment rates can continue to remain high for a long time:

- Continued share take in the self-moving market (less than half of the total moving market). Truck rental is subscale for existing players. Budget has been scaling back its fleet and Penske, the nearest competitor, has 10% of the number of locations U-Haul has. The overall moving market is c. \$15bn (U-Haul is less than one quarter of this).
- Encroaching into the professional moving market (>50% of the market), which a fragmented, and therefore largely local, industry. There are 7k companies represented by the American Moving and Storage Association alone, representing 14k locations across the US. Half of these businesses employ fewer than five people. The sustainability of the professional moving segment seems threatened by the scale of U-Haul's network, provision of moving helpers through Moving Help, and the potential introduction of autonomous vehicles. The investments into Moving Help could be a significant enabler of this.
- Finally, the self-storage industry is twice the size of the moving industry, c. \$30bn. This is a fragmented market in which there are synergies with the moving business. Given these two factors, it is possible that certain storage assets are worth more to Amerco than other bidders. Amerco can rebrand the acquired facility with the ubiquitous U-Haul logo and link it to its online reservation system, immediately connecting the assets to Amerco's large customer base. None of Amerco's competitors, either in the self-storage or the moving space, can exploit this synergy to the same extent.

Since we initially acquired shares in February 2017 for \$370 per share, the stock has fallen 9%, materially lagging the market over the last two years. There have been several short-term pressures on Amerco's profitability over this period. There has been some pressure on operating profit margins due to the acceleration of truck and self-storage asset expansion and the tweaks to the company's depreciation policies to front load tax-deductible depreciation ahead of the corporation tax reductions. The fleet increased 10% yoy in 2018 but management expects this to be roughly flat in FY19 as truck acquisition slows and used truck sales pick up. EBITDA margins however continue to improve.

Asset utilisation has been constrained by low occupancy rates on self-storage assets and lower truck

fleet utilisation. However, self-storage square footage has increased 50% over the last three years and the CFO on the call stated that revenue per square foot continues to rise 3-4% yoy and the average occupancy on units older than three years is 84%, vs. 39% for units younger than three years. Given lofty self-storage market prices, UHAL has been focused on a build vs. buy growth strategy, with its associated larger drag on average occupancy. Finally, a collapse in used truck disposal profits was due to an effort to slow down sales and maximise the depreciable asset base ahead of the corporation tax rate change, and poor execution in underwriting the sale of waiver insurance, incurring elevated repair costs in getting vehicles into a sellable condition. The elevated disposal profits are something we highlighted in our original research and normalised for in the owner earnings calculation.

Listening to Amerco's investor conference calls is instructive. Some comments from participants on recent calls reflect a level of frustration at the long-term horizon of management's capital allocation choices, pleading for the installation of a regular dividend and buyback. I disagree. A dividend should be the last thing this company is doing, and despite the stock failing to remotely keep pace with the market's rally over the last few years, a buy back would shrink an already small free float. My sense is that management is making capital allocation decisions that are designed to maximise the total future economic value of the business. I don't care whether this is realised later vs. sooner, if the company's investments are returning more than our opportunity cost of investing. With the company's widening moving and storage network advantage and a CEO who is paid < \$1mn per year but whose family owns most of the business, I think this is likely to be the case.

Over the last 12 reported months of business operations Amerco generated operating cash flow of almost \$1bn. Amerco's enterprise value is less than 9x this number. With capex of over \$1.7bn Amerco is currently generating FCF of c. -\$700mn. Adjusting for c. \$1.1bn of growth capex, maintenance FCF = +\$4-500mn, a 6-8% yield to the market cap for a business with evidence of high cash reinvestment rates and high incremental returns on capital.

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