Portfolio Activity Q1 2019

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The following discussion mentions stocks that are widely — but not universally — held by clients of Horan Capital Management. Client portfolios are customized, so this commentary may or may not be directly applicable to any given client or account. Our intention is to provide general insight into portfolio holdings and into our overall approach and to highlight situations of interest, both positive and negative. The mention of any stock is neither advice nor a solicitation to buy or sell any particular investment and our opinions regarding securities are subject to change without notice. Investing involves risk of loss. See the legal disclosures at the end of this publication and on our website for more information.

BUYS

VAIL RESORTS
EXPERIENCE OF A LIFETIME™

Vail Resorts, Inc. (MTN)

Vail Resorts operates mountain resorts and urban ski areas in North America (in addition to one resort in Australia). The company earns money from lift tickets, dining services, ski school, retailing, and lodging.

The company operates four of the six most-visited ski resorts in North America. This dominance is unlikely to change in our opinion due to the high geographic and regulatory barriers to entry in the industry. In addition to the difficulty of finding the right terrain, a prospective entrant into the industry would have to hurdle strict regulations from various governmental institutions (e.g. the Forest Service). This is why the last major ski resort built in the U.S. opened in the early 1980s. The company's valuable licenses to operate its properties run for decades and are likely to be renewed upon expiration.

At the crux of our investment thesis is the company's new business model – namely its "Epic Pass." The Epic Pass is essentially a membership program that offers customers more frequent access to its resorts (usually unlimited access) in exchange for a larger upfront fee. This creates revenue visibility and a short-term float. It also transfers weather risk from the company to the customer while increasing the value proposition to recurring customers. Lastly, it builds an ecosystem and makes future resort acquisitions potentially more rewarding if those resorts are strategically located close enough to an existing resort. This can sway more customers to purchase the pass and create an even stronger ecosystem (i.e. a network effect).

All of this culminates into what we believe to be a business with continuously improving earning power and a defensible economic moat. Vail is one of the few players in its industry with the capital and fixed asset base to generate attractive economic profits. Shares fell during the quarter over concerns about early-season attendance and competition from Alterra Mountain Company. We believe that Vail will continue to be the leader in the space through its high-quality resorts and unique value proposition, which is why we initiated a position during the quarter.

ACTIVISION BLIZZARD

Activision Blizzard, Inc. (ATVI)

Activision Blizzard is a leading global video game developer and publisher. It develops and sells video games under three segments: Activision (console-based franchises such as Call of Duty and Forsaken), Blizzard (PC-based franchises such as World of Warcraft and Diablo) and King Digital (mobile-based franchises such as Candy Crush and Bubble Witch). It also owns Major League Gaming (MLG) – a collection of Esports leagues where city-based teams compete while playing popular video games. Activision largely generates revenues from game sales, downloadable content, in-game micro-transactions, and Esports.

The video game industry as a whole has undergone numerous changes that we believe make it more attractive from an investment standpoint. First, the preferred distribution channel has been shifting to digital downloads as opposed to physical purchases through a retailer. Second, the revenue generation cycle has been re-invented with the introduction of in-game micro-transactions. Third, mobile gaming has become the overall preferred gaming method, which has expanded the total addressable market, increased total screen time/engagement, and introduced lucrative new revenue generation opportunities. Fourth, video games are one of the most cost-effective forms of entertainment and have evolved into a means of social interaction as well. Lastly, the emergence of Esports has been rapidly gaining steam – now selling out live shows and gaining a presence both online and on major TV networks like ESPN.

In our view, Activision is in a unique position to capitalize on all of the aforementioned trends/tailwinds. It has an impressive portfolio of intellectual property which it continues to monetize effectively, in addition to a loyal fan base over many of its franchises. Through its ownership of MLG, it also has an opportunity to build new franchises around professional competition. Activision's share price receded during the quarter, giving us an opportunity to purchase a stake in the business for clients.

BOOKING HOLDINGS

Booking Holdings Inc. (BKNG)

Booking Holdings operates online platforms that facilitate transactions between travelers and hotels/airlines/rental car services. In most cases, Booking acts as a platform and receives a commission for lending its network to travelers and businesses. In other cases, Booking acts as the facilitator of payments, buying hotel rooms in bulk and selling them individually at a profit. The company also generates advertising revenue on select platforms. Most of Booking's revenue is generated in Europe where boutique hotels are commonplace and there is very little consolidation in the hotel industry. This lack of consolidation makes smaller hotels dependent on Booking's services, giving the company a wide economic moat. A majority of the company's gross profit comes from commissions, creating a toll booth-like business model and substantial cash flow. Management has consistently demonstrated the ability to reinvest this cash effectively with extraordinary foresight into growing markets. We added to our existing position during the quarter as the stock fell on a revenue miss and weak guidance. We believe that the long-term prospects of the company far outweigh these short-term concerns.

Apple Inc. (AAPL)

Apple designs, manufactures, and sells consumer electronics, software, and online services. Its primary product is the iPhone, which we believe has pricing power and significant consumer mind share. Apple is an excellent cash generator and a staple in client portfolios. We continue to be a net buyer of the stock and seek to add shares when the market value and our calculation of intrinsic value are materially disjointed. Concerns over iPhone unit sales during the quarter created such a situation and we added to our position.

THOR INDUSTRIES

Thor Industries, Inc. (THO)

Thor Industries is the leading manufacturer of recreational vehicles ("RVs") in North America. More specifically, it is the market leader in Towable and Motorized RVs. Its portfolio of brands includes Airstream, Heartland, Jayco and Keystone. In September 2018, Thor agreed to acquire Erwin Hymer Group – Europe's largest RV manufacturer. The acquisition closed during the first quarter, creating the global leader in the recreational vehicle market. This will give Thor exposure to growing global markets and a diverse procurement, manufacturing, and distribution network. We view Thor as a best-in-breed manufacturer in a growing industry, with a strong competitive position, selling at a discount to fair value. We believe the RV industry stands to benefit from a growing consumer preference for experiential spending, outdoor leisure, and active lifestyles. Share prices have declined recently due to concerns over inflationary pressures from tariffs on steel and aluminum and concerns over a potential economic slowdown. We believe that many of these headwinds are short-term in nature and do not pose a long-term threat to the company's competitive position. Further, we believe the market has more than priced-in these concerns, pushing the valuation to near cycle lows and creating an attractive entry point for long-term investors.

Tencent 腾讯

Tencent Holdings Ltd. (TCEHY)

Tencent is an investment holding company. It invests in numerous businesses in a diverse range of industries. The company's largest revenue source is online gaming. Other sources include (but are not limited to) subscription revenue from music and video streaming, advertising revenue, and fees from payment services. We believe that the company's most valuable asset is WeChat – a smartphone application that offers a broad array of services to its users. The WeChat platform enables messaging, social networking, work groups, mobile payments, online shopping, payments at stores, a ride-hailing service, food ordering, sending money to friends, and buying event tickets. All of this is done on the WeChat app, creating a valuable and convenient ecosystem for the user. This app has over one billion monthly active users who each spend an average of over an hour per day using it. Our underlying thesis on the company is that Tencent has not fully monetized these user hours and has a clear path to do so in the future. We also believe that concerns over the trade war with China have disproportionately punished Tencent's share price. Therefore, we continued to purchase shares during the quarter for client accounts.

Alphabet, Inc. Cl. C (GOOG)

Alphabet (formerly known as "Google") continues to dominate and grow through its wide economic moat. Alphabet is highly profitable, has minimal debt, and holds a stockpile of cash on its balance sheet. These attributes, coupled with an under-appreciation of the company's network effect, an opportunity to further monetize YouTube, and the upside of other subsidiaries like Waymo, continuously incentivize us to add to our long-term position when given the opportunity. With concerns in the market pertaining to data and privacy protection, we were able to acquire more shares of this high-quality company at attractive prices during the quarter. By purchasing shares below our estimate of intrinsic value, we believe that we are being compensated for those potential privacy-related risks.

Facebook, Inc. (FB)

Facebook, Inc. owns multiple social networking platforms – most notably Facebook, Instagram, WhatsApp, and Facebook Messenger. Facebook generates revenue by selling advertising space on these platforms to businesses around the world. In our opinion, Facebook's economic moat is wide due to a lack of competition and a strong network-effect. The market still appears to be concerned with decelerating growth, slimmer margins, and potential regulations/fines. As we stated in last quarter's edition of "Portfolio Activity," Facebook is still growing rapidly and some of the spending that is tightening margins appears to be discretionary. Additional regulations are a possibility, but we believe that they would end up inadvertently strengthening the moat as barriers to entry would rise for potential competitors. Furthermore, we purchased shares throughout the quarter at a discount to our estimated intrinsic value. In our view, this compensates us for unforeseen risks related to regulations and non-discretionary spending requirements.

SELLS

(The positions below were eliminated in most accounts. In some cases, positions were kept in selected client accounts for tax purposes.)

The Proctor & Gamble Company (PG)

We trimmed the position during the quarter for client accounts and used the proceeds to purchase the stocks described in the "Buys" section. We also swapped out of the position entirely for select accounts that did not hold various other core positions. Our decision to sell shares of PG was primarily valuation-related.

Chipotle Mexican Grill, Inc. (CMG)

We trimmed CMG for select accounts during the quarter as it became overweight in client portfolios. We used the proceeds for opportunities described in the "Buys" section.

Union Pacific Corporation (UNP)

We trimmed the position for select accounts during the quarter after significant price appreciation. While we trimmed overweight positions and reallocated the funds, we continue to hold this core position for client accounts as we still like the company's long-term prospects.

Cisco Systems, Inc. (CSCO)

During the quarter, we swapped the position in select accounts for more attractive opportunities. This was portfolio-specific and pertained to accounts that did not hold some of the positions listed in the "Buys" section.

Walmart Inc. (WMT)

We trimmed WMT in select accounts as we felt the proceeds could be used for more attractive opportunities.