Exor SpA (EXOR.MI)

Priced for failure, run for success; initiating as Conviction Buy

Real sustained change is driven from the top

Under Agnelli heir Mr Elkann, together with executives and Fiat CEO Mr Marchionne, there have been several recent positive steps taken to unlock shareholder value. The share price appears to imply that efforts to execute change will fail, but we believe upside potential is high and likely.

Exor is a way to play Fiat's restructuring and execution of the business plan…

The next steps in the Fiat story are: (1) demerger of Fiat Industrial, which we believe may unwind the implied current 40% Fiat conglomerate discount; (2) a potential merger between Fiat Auto and Chrysler, which should help execution of the business plan and may in time lead to a re-rating of the auto business to European peer multiples; and (3) transformational deals in Fiat Ind.

…at a 44% discount that's likely to tighten

Exor's NAV discount remains among the widest in our European coverage despite simplification of the structure with the merger of IFI/IFIL into Exor. We believe Exor's discount will tighten materially.

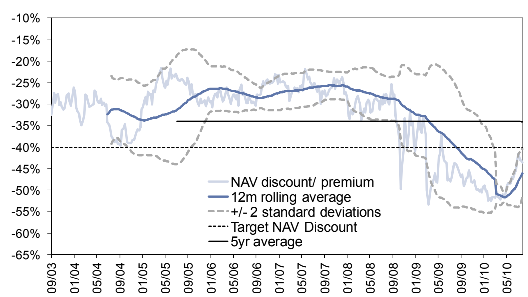
Initiating as Buy; onto Conviction List

We initiate on Exor with a Buy rating and add the shares to the Pan-Europe Conviction List. Our 12-month risk-weighted NAV-based price target is €23.7, implying 59% potential upside.

Risks

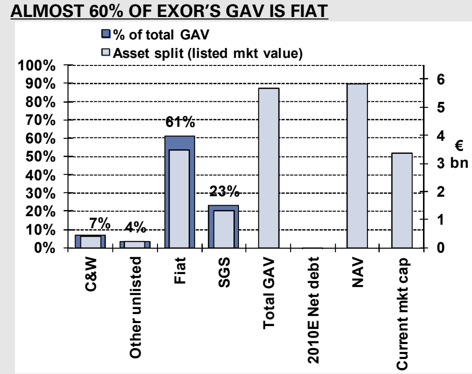
Risks to our view and price target include our analysts' price targets on underlying listed assets, prolonged market volatility and risk aversion.

We expect Exor's wide NAV discount to tighten



Source: Company data, Bloomberg, Goldman Sachs Research est.

ALMOST 60% OF EXOR'S GAV IS FIAT



Source: Company data, Bloomberg, Goldman Sachs Research estimates.

RECENT RESEARCH

NAV discounts dislocated and close to trough boundaries; Eurazeo and Exor top picks; July 28, 2010

Triple boost for holding companies if market confidence returns; April 27, 2010

Priced at the close of July 26, 2010 (€14.92)

Coverage view Neutral

See the Financial Advisory Disclosure section of this document for important disclosures about transactions in which The Goldman Sachs Group, Inc. or an affiliate is acting as financial advisor

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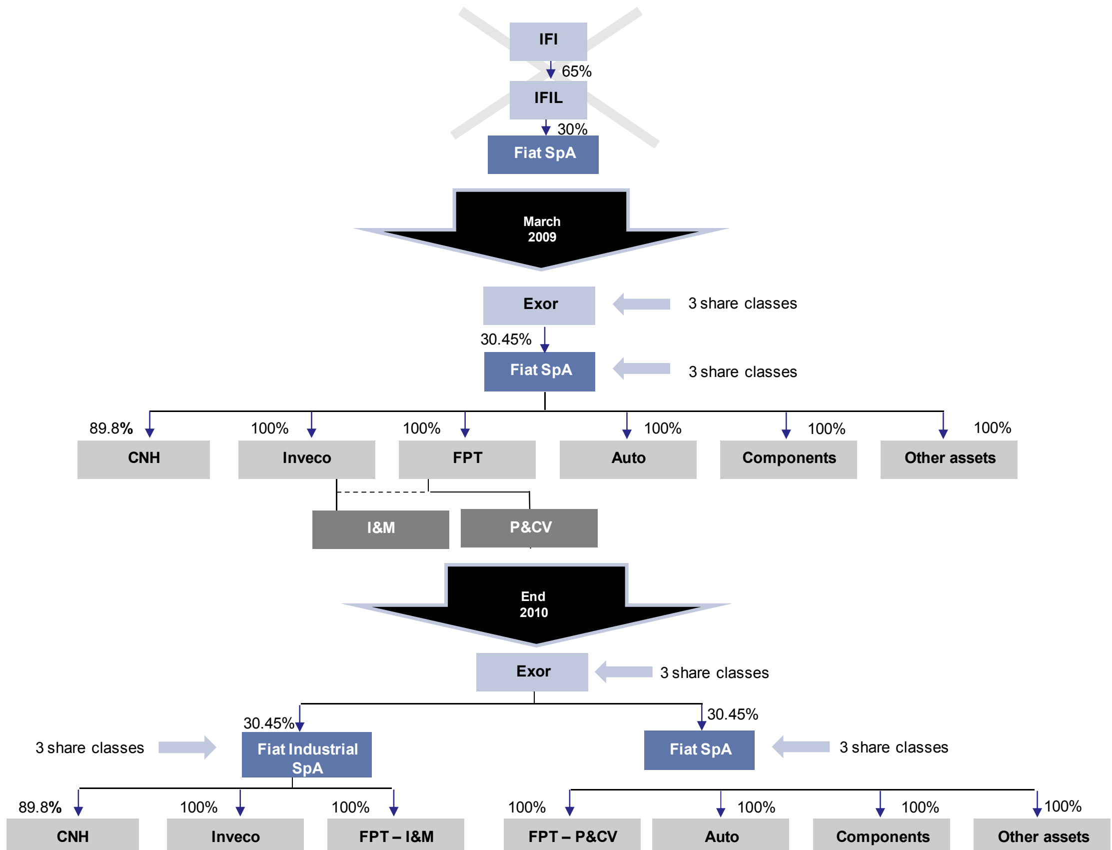
The prices in the body of this report are based on the market close of July 26, 2010.

Accretive steps have been substantial but yet to fully materialise

Under Agnelli heir Mr Elkann, together with other executives and Fiat CEO Mr Marchionne, there have been several accretive steps taken to unlock value for shareholders. First, in March 2009, IFI and IFIL merged into Exor, removing one of the layers in the holding structure. In the months after the Exor IPO, the initial discount (IFI + IFIL) narrowed materially, before widening again to above 50% as market volatility resumed. We believe the current Exor NAV discount (44%) will tighten towards the average European level of 33%. Second, Fiat has announced plans to demerge its industrial and auto businesses. Our analysis suggests Fiat has historically traded at a material conglomerate discount (35%); we expect the spin-off of Fiat Industrial to reduce (if not full unwind) this discount. We further believe that a combined Fiat/Chrysler would be well positioned to improve profitability over the next 3-5 years, which could potentially lead to a considerable re-rating in Fiat's auto shares. In our view, Exor offers investors an attractive way to gain exposure to these structural changes. We initiate on Exor as Conviction Buy; our 12-month price target of €23.7 indicates 59% upside.

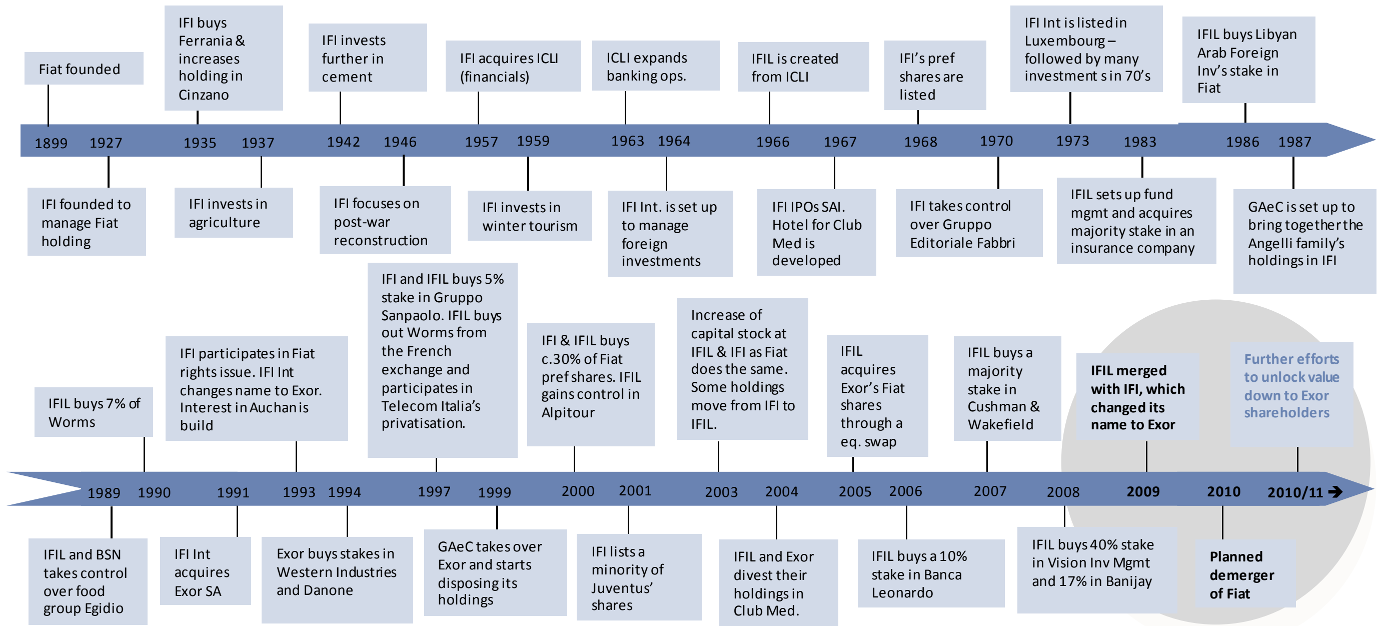
Exhibit 1: IFI and IFIL became Exor, next step is a simplification on the Fiat level



Source: Company data, Goldman Sachs Research.

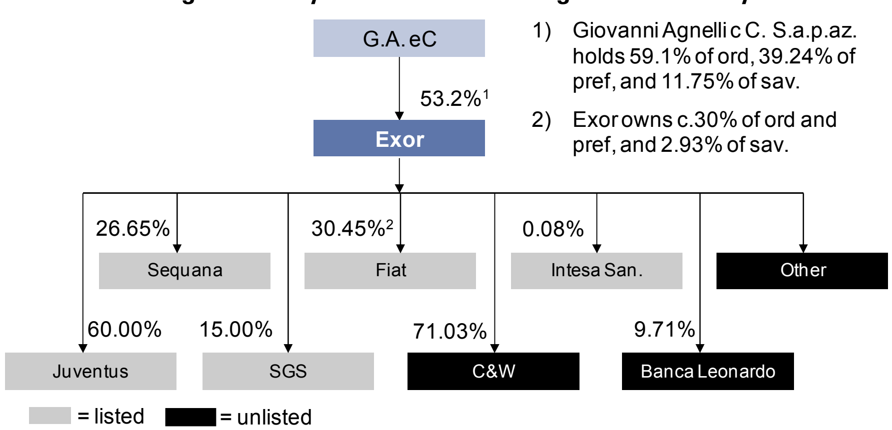
Exor's 100-year history and current form

Exhibit 2: Exor has a long history with several investments and divestments; the recent steps taken are substantial



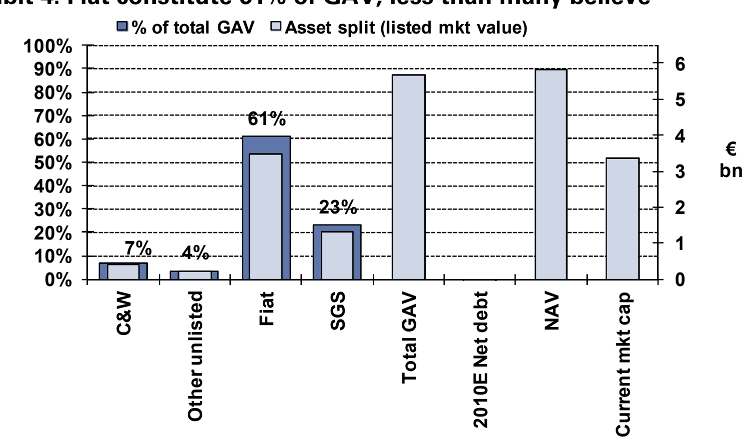
Source: Company data, Goldman Sachs Research.

Exhibit 3: The Agnelli family are still in the driving seat after 100 years



Source: Company data, Goldman Sachs Research.

Exhibit 4: Fiat constitute 61% of GAV; less than many believe

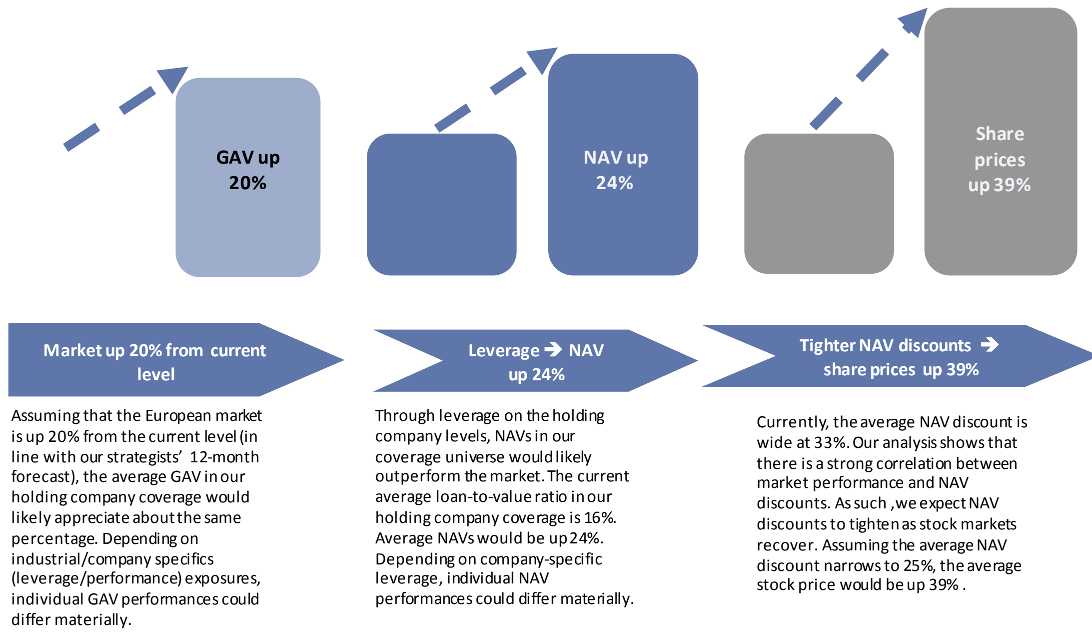


Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Holding co's context: Potential triple boost from higher GAV + leverage + tighter discounts

We see potential for holding companies to outperform if market confidence improves. Our European holding company universe has an average LTV ratio of 16%, which means NAVs would appreciate 24% if GAVs were to appreciate 20% (assuming static net debt), as detailed in our scenario analysis below. Additionally holding companies' NAV discounts tend to be wide in times of uncertainty (market troughs) and tighten significantly when markets regain confidence. As illustrated in Exhibits 6-7, the peak average NAV discount is 15%, trough 35% and current 33%. In a scenario (Exhibit 5) of regained market confidence (+20%, in line with our strategists' forecast for the overall European market over the next 12 months), we estimate average share prices of European holding companies would increase 39%, outperforming the overall market materially. In a market correction, the effects in Exhibit 5 would work in the other direction, leading to significant potential downside.

Exhibit 5: Potential triple boost to holding companies if market regains confidence
Scenario analysis



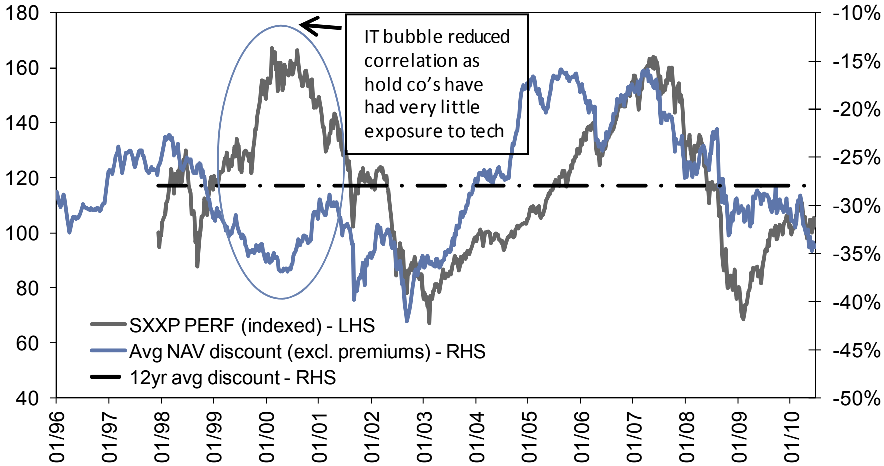
The simple maths

	Before	After	Change
GAV	100	120	**20%**
Net debt	16	16	
NAV	84	104	**24%**
NAV discount	-33%	-25%	
Share price	56	78	**39%**

Source: Goldman Sachs Research.

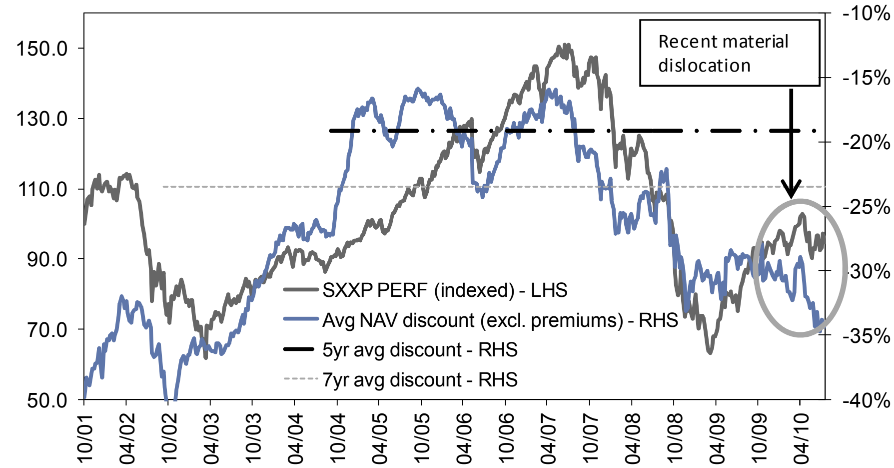
We observe there is a strong relationship between overall market performance and NAV discounts (correlation is 0.73 from 2001), as illustrated in Exhibit 7. The TMT bubble around 2000 caused a lower correlation between market performance and NAV discount (0.62) when measured from the mid-1990s, since holding companies have had relatively low exposure to TMT (Exhibit 6). See *NAV discounts dislocated and close to trough boundaries; Eurazeo and Exor top picks,* July 28, 2010 and *Triple boost for holding companies if market confidence returns: Eurazeo remains top pick,* April 27, 2010, for more details on European holding companies.

Exhibit 6: Correlation between market performance and average NAV discounts since 1996 is significant (0.62) ...



Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Exhibit 7: ... and increases to 0.73 starting in 2001 (after TMT bubble period)



Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Exor has one of the widest NAV discounts in our coverage

NAV discounts remain wider than historical norms, as seen in Exhibit 8, which highlights current NAV discounts vs. historical averages. As a result of a reduction in borrowing costs, which have remained high for a considerable amount of time, we believe mean reversion strategies around NAV discounts will play out quicker than in the past. This would help NAV discounts to gradually normalise if the economy continues to rebound, in our view. On our estimates, NAV discounts for Eurazeo and Exor currently appear among the most dislocated.

Exhibit 8: NAV discounts remain wider than history; Exor has one of the widest discount in our coverage
(as of close 26 July, 2010)

Company	Current	-1w	-1m	-3m	-1y	1yr avg	3yr avg	5yr avg	Max	Min	Dif. Current vs. 3yr avg
Aker ASA	-54%	-53%	-50%	-40%	-43%	-39%	-19%	-23%	5%	-55%	-35%
Christian Dior SA	-24%	-24%	-24%	-19%	-21%	-21%	-19%	-21%	-9%	-38%	-5%
CIR SpA	-44%	-42%	-43%	-39%	-38%	-43%	-39%	-33%	-13%	-70%	-5%
Corp Financiera Alba	-50%	-48%	-47%	-43%	-46%	-46%	-35%	-31%	-18%	-55%	-15%
Criteria Caixacorp SA	-25%	-25%	-28%	-21%	-25%	-28%	-31%	NA	-16%	-41%	NA
Eurazeo	-44%	-43%	-42%	-47%	-51%	-47%	-21%	-22%	3%	-57%	-22%
Exor SpA	-44%	-43%	-45%	-52%	-45%	-47%	NA	NA	-41%	-53%	NA
GBL SA	-27%	-28%	-30%	-29%	-29%	-27%	-24%	-15%	12%	-33%	-3%
Industrivarden AB	-24%	-25%	-26%	-21%	-16%	-14%	-14%	-14%	3%	-28%	-10%
Investor AB	-34%	-34%	-34%	-33%	-32%	-31%	-28%	-28%	-19%	-38%	-6%
Italmobiliare SpA	-54%	-56%	-55%	-48%	-57%	-51%	-26%	-29%	0%	-59%	-28%
KBC Ancora	-45%	-46%	-43%	-39%	13%	1%	-9%	-14%	NA	-46%	-36%
Kinnevik Investment AB	-32%	-38%	-36%	-35%	-36%	-33%	-30%	-26%	-9%	-47%	-2%
Lundbergforetagen AB	-14%	-15%	-18%	-18%	-22%	-20%	-19%	-16%	-8%	-34%	4%
Nationale a Portefeuille	-28%	-29%	-30%	-26%	-15%	-13%	-10%	-5%	17%	-32%	-18%
Orkla ASA	-17%	-23%	-24%	-7%	3%	4%	-9%	NA	22%	-29%	-8%
Pargesa Holding SA	1%	4%	8%	9%	2%	3%	0%	-7%	25%	-17%	1%
Rallye SA	-33%	-31%	-30%	-26%	19%	-6%	-20%	-13%	42%	-47%	-13%
Ratos AB	-16%	-16%	-17%	-8%	-12%	-11%	-5%	-14%	24%	-34%	-11%
Sacyr Vallehermoso SA	-26%	-29%	-21%	-22%	2%	-4%	-19%	NA	19%	-37%	-7%
Semapa	-31%	-31%	-32%	-20%	-11%	-14%	-20%	-17%	25%	-34%	-10%
Societe FFP	-46%	-45%	-44%	-39%	-39%	-42%	-30%	-28%	-15%	-49%	-16%
Sonae SGPS SA	-49%	-48%	-47%	-47%	-56%	-52%	-29%	-32%	7%	-61%	-20%
Wendel	-31%	-39%	-39%	-37%	13%	-10%	-21%	-19%	57%	-41%	-9%
Average	-33%	-34%	-33%	-29%	-23%	-25%	-21%	-20%	5%	-43%	-12%
Median	-31%	-33%	-33%	-31%	-24%	-24%	-20%	-20%	3%	-41%	-10%
Top quartile	-25%	-25%	-25%	-21%	-8%	-11%	-16%	-14%	20%	-34%	-6%
Bottom quartile	-44%	-44%	-43%	-39%	-40%	-42%	-28%	-28%	-11%	-53%	-18%

Source: Company Data, Bloomberg, Goldman Sachs Research estimates.

The Italian holding company regime is favourable

Italy has a relatively favourable holding company regime. Since January 1, 2008, only 5% of capital gains on stakes owned for at least 12 months are taxed at the Italian corporate income tax rate (IRES), currently 27.5%, making the effective tax rate 1.375%. If the asset is held for less than 12 months, than the full IRES applies, plus a regional tax rate (IRAP), currently at 5%. Only 5% of dividends are taxed at IRES irrespective of the holding period, making the effective tax rate 1.375%. Under the EU Parent-Subsidiary Directive, there will be no withholding tax on cross-border distributions of dividends if the parent holds at least 10%. Of note, Exor has almost €400 mn in tax losses carried forward that may be utilised to minimise tax on future profits.

Fiat roadmap includes several catalysts over the next few years – some imminent

Our Fiat analysts have a positive view on Fiat's shares, which are on the Pan-European Conviction Buy List. For more details on their thesis and view see: *Fiat (FIA.MI): Attractive risk/reward; Conviction Buy, €16 price target*, March 8, 2010 and *Europe: Automobiles: Focusing on our core ideas in times of volatility; reiterating Conviction Buys on VW and Fiat*, May 20, 2010. The optimistic view on Fiat's shares is summarised by a belief that the following events are likely to have a positive outcome and that the optionality these events offer in terms of delivering a beneficial outcome does not appear to be priced into Fiat's shares:

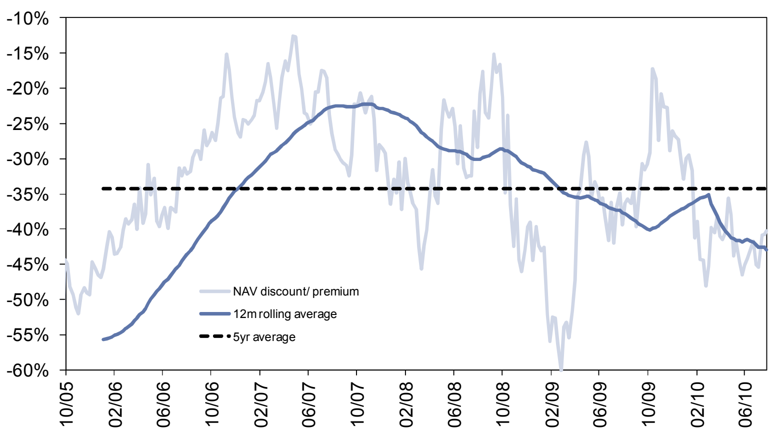
- **Mid 2010:** (1) Constructive settlement with unions; and (2) EGM to decide split of debt between Fiat Auto and Fiat Industrial.
- **Dec 2010/Jan 2011:** Demerger of Fiat ➔ two listed Fiat entities ➔ potentially fully unwind the conglomerate discount over time
- **Mid-2011:** Potential Chrysler IPO
- **2H 2011/12:** Potential merger between Fiat and Chrysler
- **2011/12:** Potential transformational deals in Fiat Industrials
- **2012 onwards:** Fiat + Chrysler = economies of scale ➔ best case scenario: F+C profitability = average industry ➔ re-rating of Fiat Auto shares to average sector EV/Sales multiple (10%-20% ➔ 45%-60%)

Key risks include a double-dip recession, leading to a broad industrial downturn plus failure to deliver on the new Turin targets.

First major catalyst: demerger may unwind conglomerate discount

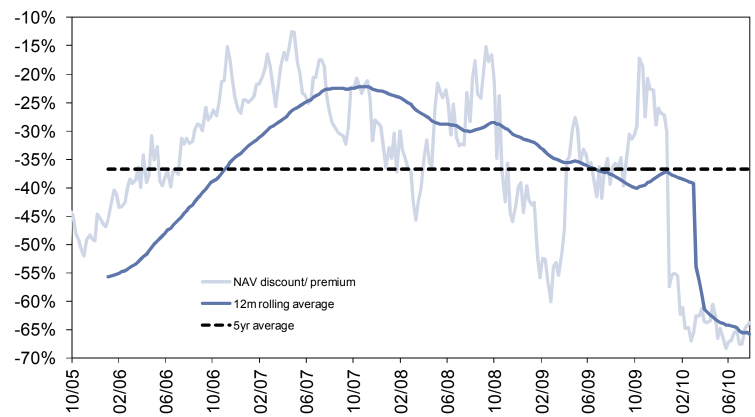
Our analysis shows that Fiat's shares have traded at a substantial conglomerate discount historically. When computing the relative valuation, we have used: (1) Peugeot EV/Sales multiple for the auto business (10%-30%); (2) its stake in CNH at market value; (3) average EV/Sales multiple of Volvo, MAN, Navistar and Paccar for the other industrial businesses (avg. 45%-100%); (4) industrial net debt less CNH's net debt. We believe the demerger of Fiat Auto and Fiat Industrial will unwind the conglomerate discount over time.

Exhibit 9: Fiat's conglomerate discount has averaged 35% in the last 5 years



Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Exhibit 10: NAV discount assuming fully re-rated Fiat auto is >65%

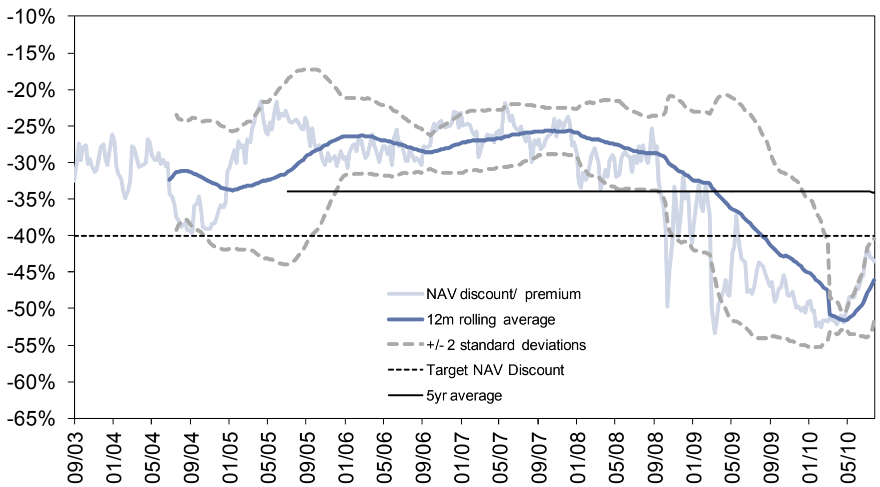


Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Investors get exposure to the Fiat story at a 44% discount via Exor

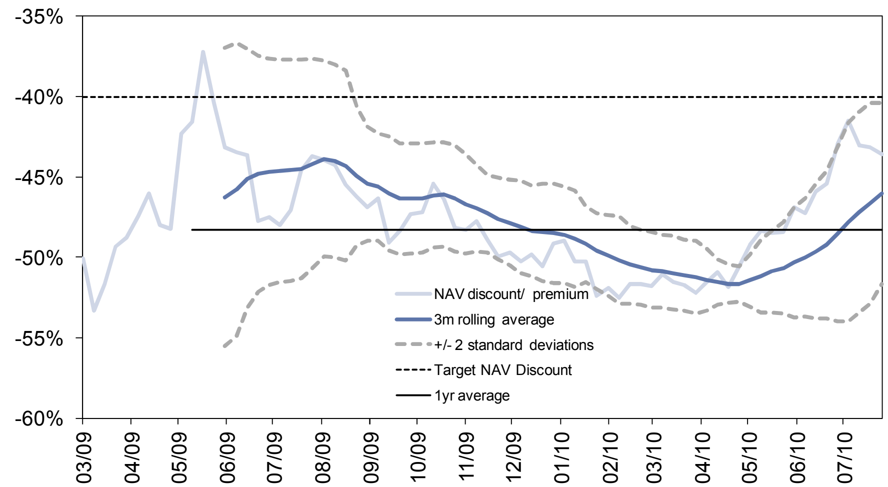
Exor's NAV discount is one of the widest in our European coverage universe (see Exhibit 8), on our estimates. Currently, Exor's NAV discount is 44% compared with a 5-year average of 34% (Exhibit 11). As illustrated in Exhibit 12, Exor's NAV discount has varied between 37%-55% since its IPO in March 2009. We see few reasons why its NAV discount should be substantially wider than comparable European holding companies; hence, we expect it to narrow.

Exhibit 11: Flow-through discount is near trough levels



Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Exhibit 12: Exor discount has widened over the last year

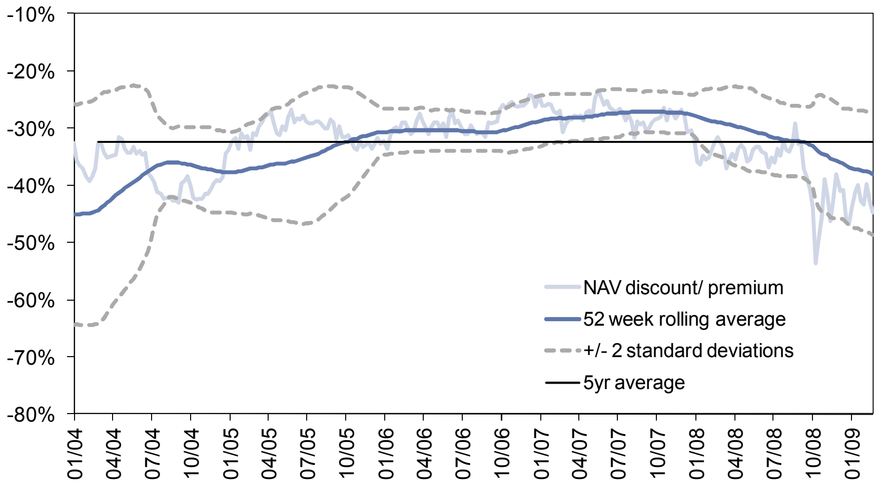


Source: Company data, Bloomberg, Goldman Sachs Research estimates.

One of the main reasons for the merger between IFI and IFIL in 2009 was to eliminate one of the layers in the holding company chain, and as such increase transparency and reduce complexity (see Exhibit 1). Usually collapsing, or minimizing, a holding company chain is viewed positively by the market. The "New Co" would as a rule reduce overall overhead costs and increase overall minority protection (mainly through less complexity and better transparency). As a result, the NAV discount often narrows materially for the "New Co" which has one NAV vs. several NAVs in the previous set up, each with a discount.

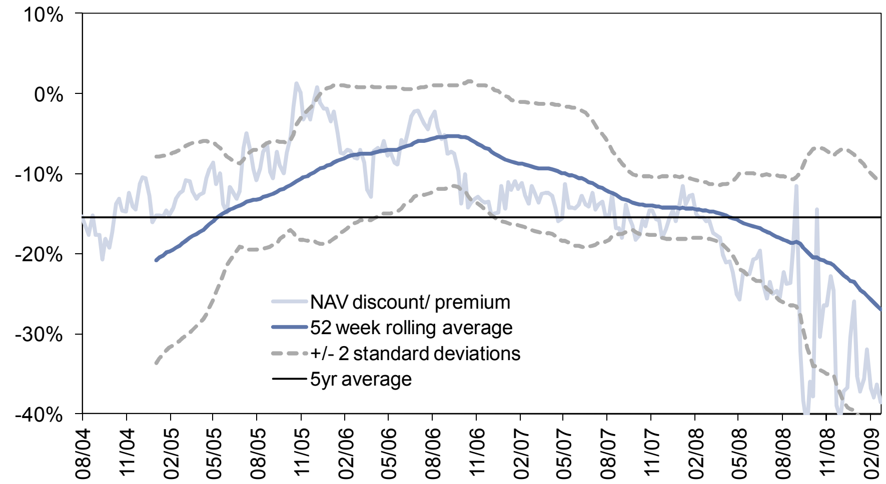
Surprisingly, Exor's NAV discount is the sum of IFIL's (c.30%) and IFI's (c.15%) 5-year average NAV discount (see Exhibit 11-14). We believe the considerable market turbulence over the last two years may explain this anomaly, especially since the merger into Exor was made at the peak of market uncertainty. Our analysis shows there is high correlation between NAV discounts and implied market ERP, which has increased during the spring as concerns towards sovereign debt magnified. As the economic recovery continues and market volatility is reduced, we believe Exor's NAV discount will trend towards the European average of 33%.

Exhibit 13: IFIL's NAV discount ranged between 30% and 40%



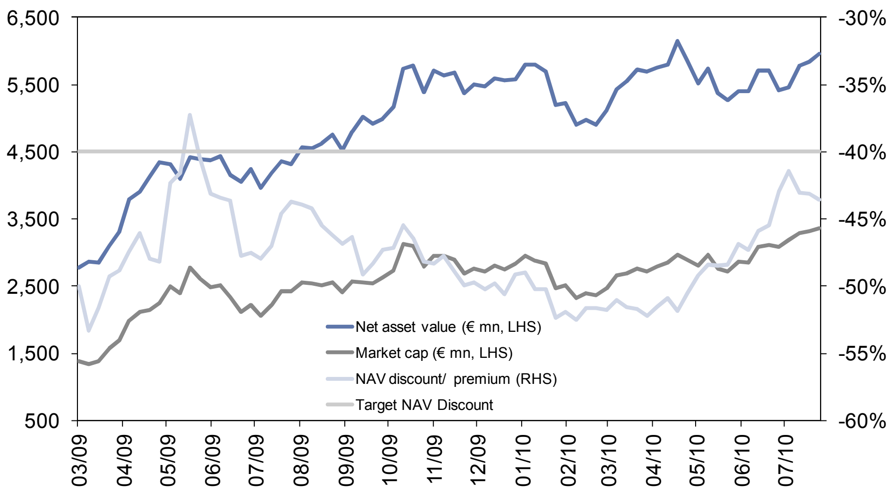
Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Exhibit 14: IFI's 5-year average NAV discount was 15%



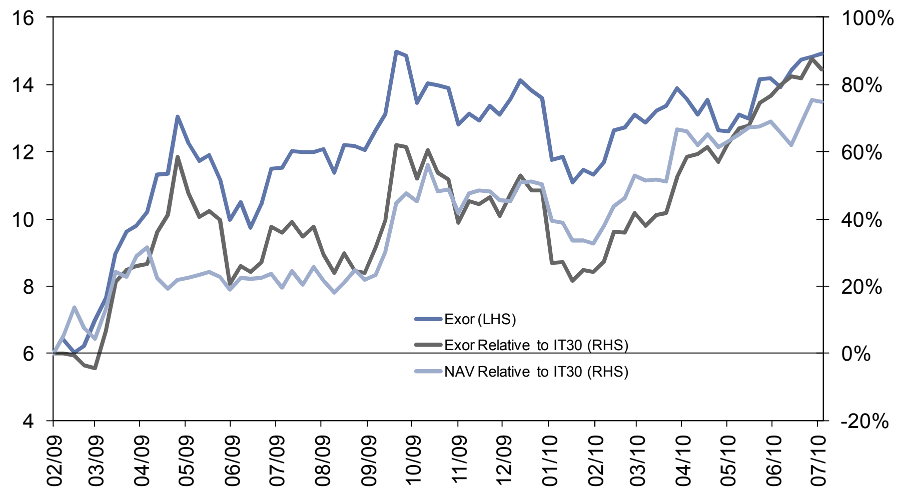
Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Exhibit 15: Exor's NAV has more than doubled from trough in 2009



Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Exhibit 16: Exor's shares have performed well vs. Italian index



Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Liquidity seems adequate; in fact financial risk at the Exor level is limited, in our view

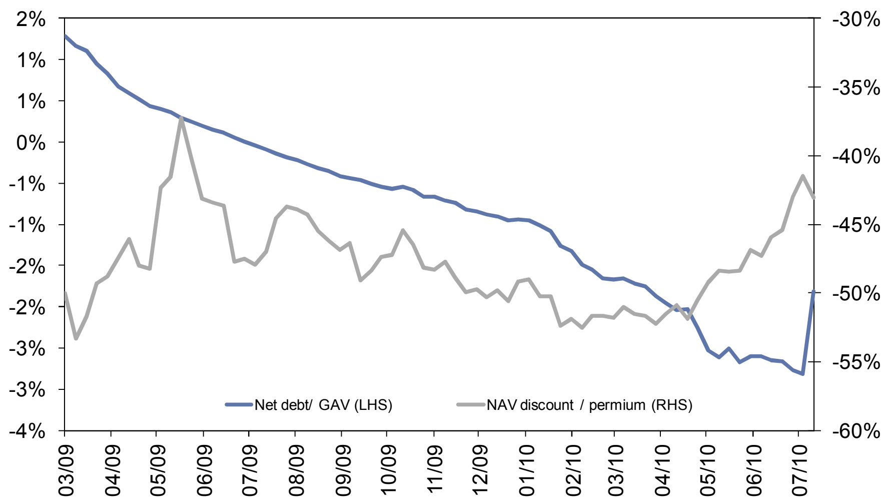
The Exor holding system currently has a small net cash position. Current liquidity (excluding stakes in liquid listed assets, which together have a value of over €5 bn) is €1.4 bn. Exor is actively looking to invest excess capital (c.€1.6 bn). The company wants to retain a minimum of €200 mn in cash and keep its LTV ratio below 20%. The current excess capital is unlikely to be invested in one new larger asset, but more likely in around three separate investments, according to management. These investments would be larger and different in nature than the recent committed €100 mn in the partnership with Jardine Matheson and Rothschild partnership, which will invest in private equity in India and China.

Exhibit 17: The Exor holding system sits on net cash and has almost €1.4 bn in liquid funds

Net financial position - € mn (parent)	2009	Net financial position - € mn (Exor holding system)	2009	Non current
Financial assets	353	Financial assets	692	87.2
Financial receivables	28	Financial receivables	28	
Cash and eq.	337	Cash and eq.	463	
Total financial assets	719	Total financial assets	1,182	
Exor bond 2007-17	768	Exor bond 2007-17	768	
Exor bond 2006-11	200	Exor bond 2006-11	200	
Bank debt	163	Bank debt	163	
Total financial liabilities	1,131	Total financial liabilities	1,131	
Net debt (Exor SpA)	412	**Net debt (Exor holding system)**	**-52**	
Undrawn credit line	760	**Total liquidity**	**1,365**	

Source: Company Data.

Exhibit 18: Exor sits on net cash; future LTV ratio to stay below 20%



Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Exhibit 19: Expenses vs. NAV is low, coverage ratio is solid

Exor	2008	2009	2010E	2011E
Operating costs as % of NAV	**0.69%**	**0.39%**	**0.42%**	**0.42%**
Dividend from listed assets - € mn	206	65	129	125
Operting expenses (overheads) € mn	23	22	22	22
Net interest expenses - € mn	66	19	19	22
Interest/overhead cost coverage from dividends	**234%**	**159%**	**314%**	**288%**

Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Our NAV model suggests 59% potential upside; add to Conviction Buy List

Fiat is Exor's main listed holding and our 12-month price target suggests 51% potential upside for Fiat shares. Fiat is included in our Conviction Buy List. We further believe Exor's NAV discount will narrow from the current elevated level of near 44%. We note that the current average NAV discount in Europe is 33% (which is materially wider than historical levels). In our view, Exor is not more complex or less transparent vs. European peers, especially after the merger between IFI and IFIL in March 2009. We believe Exor offers investors an attractive route into Fiat's restructuring. Our NAV model suggests there is 35% upside to the value of the Exor's listed holdings and our Exor price target of €23.7 indicates total potential upside of 59% on a 12-month view. We initiate on Exor with a Buy rating and add the shares to our Conviction Buy List.

Exhibit 20: We see 59% potential upside to our 12-month price target, current NAV discount wide at 44%

Listed	SEDOL	BBG	Name	% stake	Curr.	Conv. factor	Price (EUR)	Market value (mn, EUR)	% NAV	Rating	Tgt / mkt (EUR)	Up/down	Analyst	Tgt / mkt value (mn, EUR)	% NAV	% GAV (mkt)
Holding 1:	5748521	F IM	Fiat SpA	26.53%	EUR	1.0000	9.9	**3,304**	*55%*	Buy*	15.0	51%	Stefan Burgstaller	**4,989**	*65%*	*57%*
Holding 2:	5748554	FP IM	Fiat SpA	2.48%	EUR	1.0000	5.7	**178**	*3%*	NC	8.6	49%		**267**	*3%*	*3%*
Holding 3:	5748532	FR IM	Fiat SpA	0.19%	EUR	1.0000	6.2	**14**	*0%*	NC	9.0	46%		**21**	*0%*	*0%*
Holding 4:	4824778	SGSN VX	SGS SA	15.00%	CHF	0.7339	1,116.3	**1,310**	*22%*	Neutral	1,089.8	-2%	Charles Wilson	**1,279**	*17%*	*23%*
Holding 5:	5469242	VOR FP	Sequana	26.42%	EUR	1.0000	11.2	**147**	*2%*	NC	11.2	0%		**147**	*2%*	*3%*
Holding 6:	7264809	JUVE IM	Juventus Football Club	60.00%	EUR	1.0000	0.8	**99**	*2%*	NC	0.8	0%		**99**	*1%*	*2%*
Holding 7:	4076836	ISP IM	Intesa Sanpaolo SpA	0.08%	EUR	1.0000	2.5	**25**	*0%*	Neutral	3.0	20%	Domenico Vinci	**30**	*0%*	*0%*
Holding 8:															*0%*	*0%*
Others:								**0**	*0%*	NC				**0**	*0%*	*0%*
							Value of listed holdings:	**5,077**	*85%*				**Value of listed holdings:**	**6,831**	*89%*	*87%*
							per share	***20.6***					***per share***	***27.7***		
													Upside / Downside:	**34.54%**		

Unlisted	Sector	GSSB/ peers	Name	% stake	Valuation method	Target value (mn, EUR)	% NAV		2011E (mn, EUR)	Multiple	Net debt 2010E (mn, EUR)	Target value (mn, EUR)	% NAV	% GAV (mkt)
Holding 1:	Financial services	CBG	Cushman & Wakefield	71.81%	12m forward EV/EBITDA	**411**	*7%*	EBITDA:	89	8.2x	(152)	**411**	*5%*	*7%*
Holding 3:	Banks	EUBANKS_	Banca Leonardo	9.74%	12m forward P/B	**117**	*2%*	Book value:	870	1.4x	na	**117**	*2%*	*2%*
Holding 2:	Fin. services	GSSBBKBR	Vision hedge fund	40.00%	Book value	**58**	*1%*					**58**	*1%*	*1%*
Holding 4:	Travel	GSSBHOLR	Alpitour/N.H.T.	100.00%	Book value	**50**	*1%*					**50**	*1%*	*1%*
Others:						**91**	*2%*					**91**	*1%*	*2%*
					Value of unlisted holdings:	**727**	*12%*				**Value of unlisted holdings:**	**727**	*9%*	*13%*
					per share:	***3.0***					***per share:***	***3.0***		

Net debt (parent company level)		2010E (mn, EUR)	% NAV		2010E (mn, EUR)	% NAV
Cash & Equiv.:		**358**	*6%*		**358**	*5%*
ST Debt:		**(25)**	*0%*		**(25)**	*0%*
LT Debt:		**(1,070)**	*-18%*		**(1,070)**	*-14%*
Pensions&Other Prov.:		**(3)**	*0%*		**(3)**	*0%*
Other assets:		**789**	*13%*		**789**	*10%*
Treasury shares:		**104**	*2%*		**104**	*1%*
	Value of net debt:	**153**	*3%*		**153**	*2%*
	per share:	***0.6***			***0.6***	
	NAV:	**5,957**		**Target NAV**	**7,711**	
	per share:	***24.19***		***per share:***	***31.31***	
	Market cap. (mn):	**3,363**		**Market cap. (mn):**	**3,363**	
	NAV discount:	**-43.6%**		**NAV discount:**	**-56.4%**	
				Assumed NAV discount:	-41%	
				Implied per share:	***23.7***	
				Upside / Downside to price target:	**58.6%**	
	LTV:	**-2.63%**				

* = also on the Conviction List, NC = not covered.

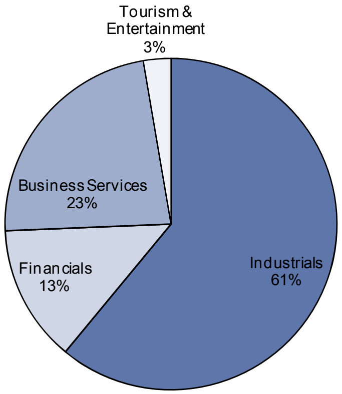
** Banca Leonardo 2009A book value

Price targets for Fiat, SGS, and Intesa Sanpaolo are based on a 12-month timeframe. For important disclosures please go to http://www.gs.com/research/hedge.html. For methodology and risks associated with our price targets, please see our previously published research,

Source: Company data, Bloomberg, Goldman Sachs Research estimates.

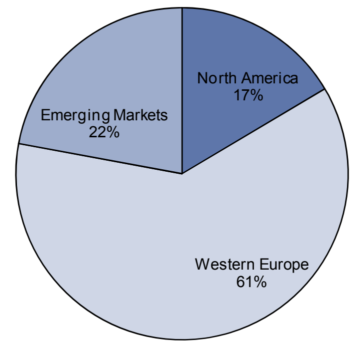
Exor's exposure to Industrials exceeds 60% in terms of GAV (Exhibit 21), of which Fiat constitutes the vast majority. Correlation between Fiat and Exor shares is substantial at 0.83 over the past year (Exhibit 23). Of note, Exor's flow-through exposure to emerging markets, which we expect to outperform the development world all else equal, is relatively high at 22%.

Exhibit 21: Industrials (mainly Fiat) constitutes over 60% of Exor's GAV
% of current GAV



Source: Company data, Bloomberg, Goldman Sachs Research.

Exhibit 22: Flow-through emerging market exposure is relatively high
% of current GAV



Source: Company data, Bloomberg, Goldman Sachs Research.

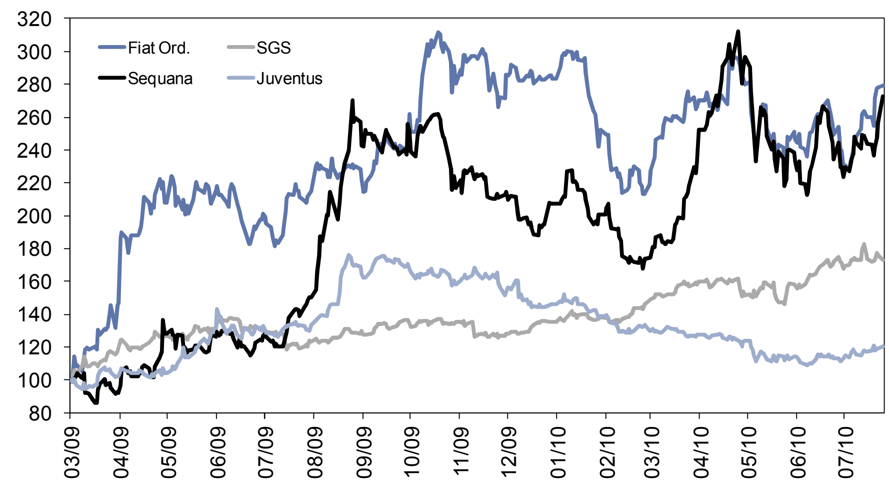
Fiat's share price performance has been the major driver of Exor's NAV over the last 15 months (Exhibit 24). We believe Fiat shares will continue to outperform the market over the next few years (see page 8 for details on our thesis).

Exhibit 23: Exor's 1-yr correlation to Fiat is very strong

	Exor	IT30	Fiat	SGS	SXFP
Exor	1.00				
IT30	0.77	1.00			
Fiat	**0.83**	0.75	1.00		
SGS	0.28	0.36	0.27	1.00	
SXFP	0.71	0.87	0.70	0.38	1.00
Average	**0.65**	**0.69**	**0.64**	**0.32**	**0.67**

Source: Company data, Bloomberg, Goldman Sachs Research.

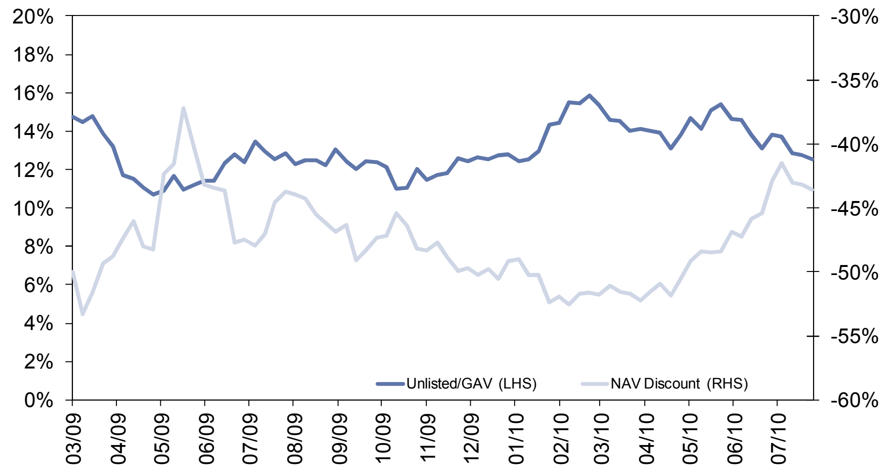
Exhibit 24: Performance of listed assets



Source: Company data, Bloomberg, Goldman Sachs Research.

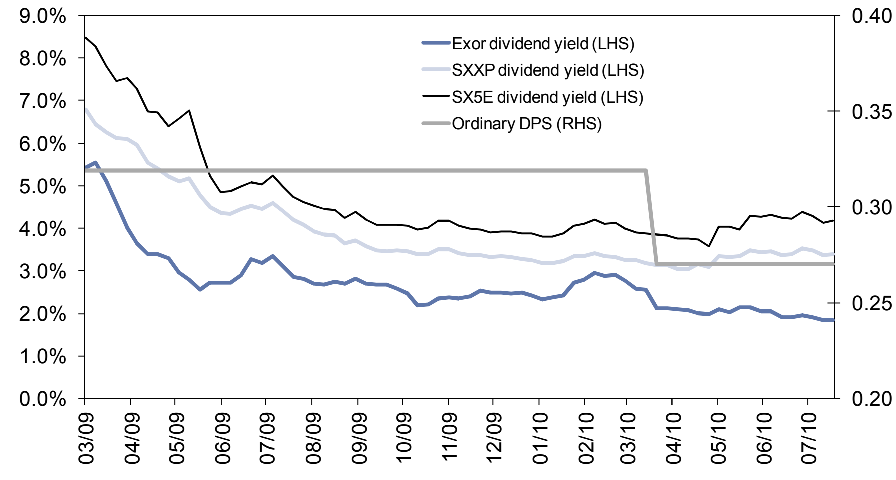
Exor has less than 15% of its GAV in unlisted assets. Were Exor to invest its €1.6 bn excess liquidity in unlisted assets, scarce assets would increase to 26% of total GAV. Our analysis suggests attractive scarce assets help narrow NAV discounts for holding companies, as the only way investors can gain exposure to these assets would be via the holding company, whereas investors can "free-ride" any positive influence holding companies have on listed assets.

Exhibit 25: Asset scarcity (unlisted assets) is limited to c.15% of total GAV



Source: Company data, Bloomberg, Goldman Sachs Research.

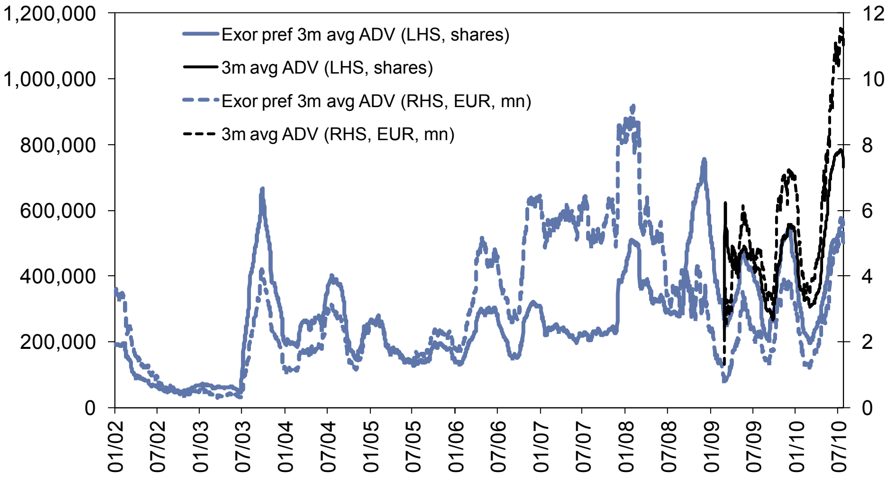
Exhibit 26: Exor's dividend yield is lower than the European market average



Source: Company data, Bloomberg, Goldman Sachs Research.

Liquidity in Exor shares has increased recently, but we argue that multiple share classes unnecessarily add complexity and reduce liquidity. The latter is especially true for companies whose shares already have relatively low liquidity; we include Exor here. For a more comprehensive discussion on share classes and dividend yields, see pages 19-20.

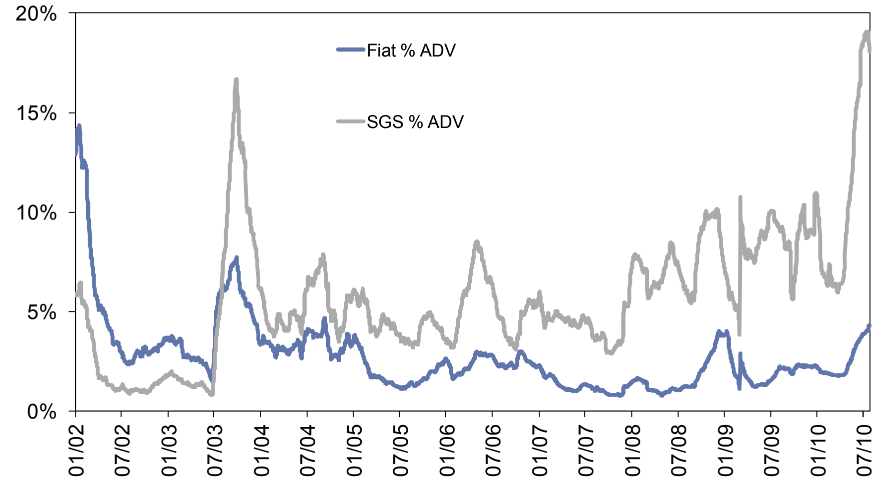
Exhibit 27: Exor liquidity has increased, total 3m ADV over €15 mn



Source: Company data, Bloomberg, Goldman Sachs Research.

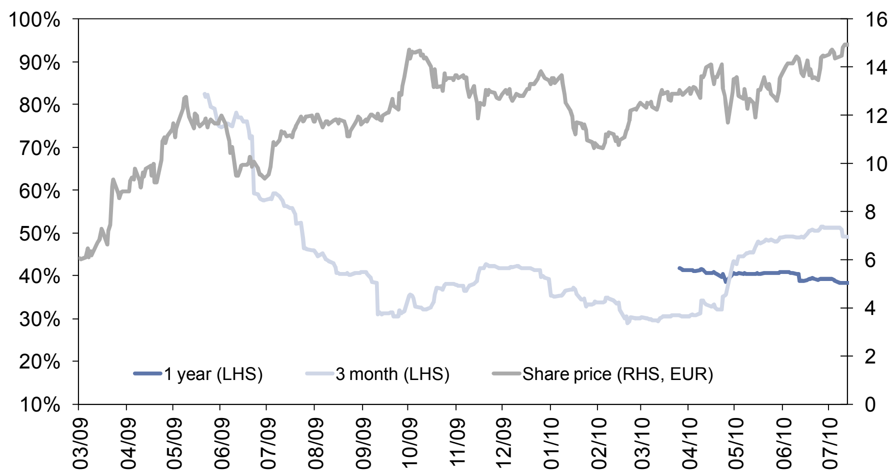
Exhibit 28: Relative liquidity vs. holdings is relatively low but has increased

Exor pref before Mar-09, thereafter Exor ord



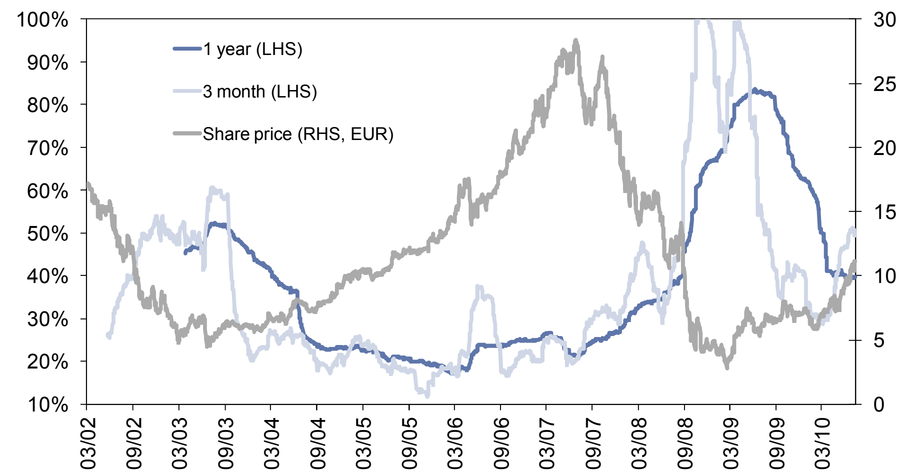
Source: Company data, Bloomberg, Goldman Sachs Research.

Exhibit 29: Volatility was near peak at IPO in Mar-2009



Source: Company data, Bloomberg, Goldman Sachs Research.

Exhibit 30: Volatility on pref showed extreme volatility 18m ago – now back to norm



Source: Company data, Bloomberg, Goldman Sachs Research.

Cushman & Wakefield looks well placed for market recovery

Cushman & Wakefield (C&W) is the largest unlisted holding of Exor. It is also the largest private real estate service in its field globally. Exor bought a 71.5% stake in C&W in 2007 for US$625 mn from the Rockefeller Group. C&W management and employees own the remaining 28.5%. C&W offers several services for the real estate sector including: Transaction Services, Client Solutions, Capital Markets and Consulting Services. We believe C&W is well placed to benefit from a recovering real estate market place.

Exhibit 31: We expect C&W and its two main listed peers to grow EBITDA and reduce debt levels substantially to 2012

CBG (US$ mn)	2006	2007	2008	2009	2010E	2011E	2012E	2009-2012E CAGR
EBITDA	612	842	455	334	569	792	959	**42.1%**
% change yoy		37.7%	-46.0%	-26.5%	70.3%	39.2%	21.0%	
Net debt to EBITDA		2.7x	4.8x	6.0x	3.1x	1.7x	0.9x	
Net debt	153	2,250	2,165	2,013	1,744	1,354	828	
JLL (US$ mn)	**2006**	**2007**	**2008**	**2009**	**2010E**	**2011E**	**2012E**	**2009-2012E CAGR**
EBITDA	292	404	272	247	304	349	394	**16.9%**
% change yoy		38.4%	-32.5%	-9.3%	23.0%	14.7%	13.1%	
Net debt to EBITDA		-0.1x	1.7x	0.5x	1.0x	0.6x	0.1x	
Net debt	0	-35	463	129	319	207	53	
C&W (US$ mn)	**2006**	**2007**	**2008**	**2009**	**2010E**	**2011E**	**2012E**	**2009-2012E CAGR**
EBITDA	118	148	67	56	81	111	138	**35.0%**
% change yoy		25.0%	-54.7%	-16.4%	44.3%	37.2%	24.4%	
Net debt to EBITDA			2.2x	3.2x	2.1x	1.2x	0.5x	
Net debt			150	179	171	134	69	

Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Our US Real Estate Research team estimates C&W's two main public competitors CB Richard Ellis (CBG) and Jones Lang LaSalle (JLL) will grow EBITDA substantially after a very tough 2008/09; 2009-2012E CAGR of 42.1% and 16.9% respectively. On our forecasts C&W will deliver EBITDA of US$111 mn in 2011 and US$138 mn in 2012. C&W is executing on its announced cost-cutting programme that targets operational expense savings of US$300 mn.

Exhibit 32 and 33 illustrate sensitivities around our valuation of C&W depending on cost cutting achieved and the multiple ascribed. Assuming C&W transfers one-third of the targeted US$300 mn cost savings initiative to the EBIT line, we calculate Exor's stake would be worth €874 mn if using the entry multiple. This implies an IRR of only 5.7%, which is not surprising considering the vintage year was 2007. That said, we believe it is important to note C&W's main listed peers have recovered significantly since the trough in early 2009 (Exhibit 34), and we see little evidence why C&W should not have experience a similar re-rating.

Exhibit 32: Potential value if cost measures are efficiently executed
US$ mn (unless otherwise stated € mn)

2008 EBIT	67
33% of reduced opex (US$300 mn) drops to EBIT	166
Net debt	189
EV/EBIT	7.3x
EV/EBITDA	6.9x
Implied EV	1,712
Implied Equity	1,522
Exor's stake	**1,093**
Implied IRR (Exit 2011)	**5.7%**
Exor's stake € mn	**874**

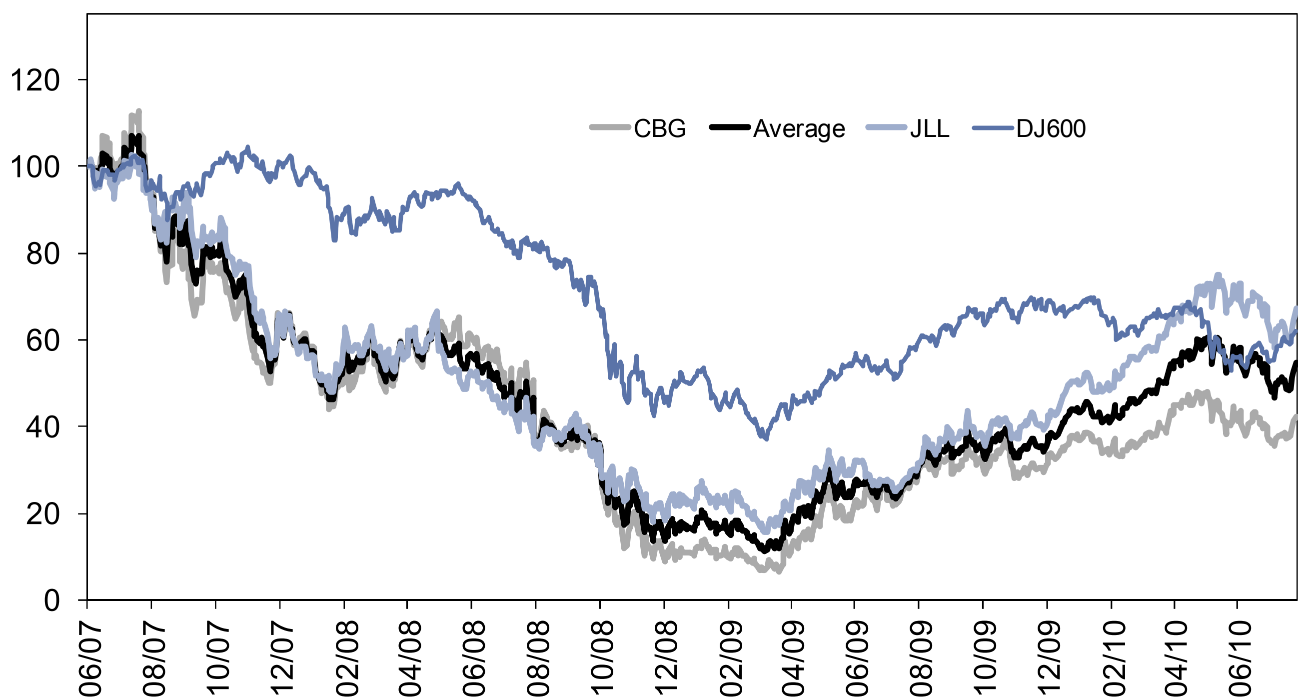
Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Exhibit 33: Sensitivity on C&W valuation
US$ mn

		EBIT post cost savings (US$ mn)				
		$134	$149	$166	$183	$201
E	8.5x	$1,094	$1,185	$1,287	$1,388	$1,500
V	8.1x	$1,036	$1,122	$1,219	$1,316	$1,422
/	7.7x	$980	$1,063	$1,155	$1,246	$1,348
E	7.3x	$927	$1,005	**$1,093**	$1,181	$1,277
B	7.0x	$874	$948	$1,032	$1,115	$1,206
I	6.6x	$823	$894	$973	$1,052	$1,139
T	6.3x	$775	$843	$918	$993	$1,075

Source: *Goldman Sachs Research estimates.*

Exhibit 34: Listed peers' share prices have recovered substantially from the trough in early 2009



Source: Bloomberg, Goldman Sachs Research.

Our valuation of C&W (Exor's stake US$514 mn or €411 mn) is based on a risk-weighted sensitivity analysis as per Exhibit 35. It translates to 8.2x our 2011E EBITDA of US$111 mn (€89 mn).

Exhibit 35: Sensitivity analysis on C&W valuation, earnings and implied multiples

US$ mn (unless otherwise stated € mn)

C&W 2011E (US$ mn)

Optimistic scenario	
Revenues (12% CAGR 2009-2011E)	1,507
EBITDA (avg hist. margin)	8.5%
EBITDA (strong recovery)	128
10% premium to peer history	8.9x
Implied EV	1,136
Net debt	189
Implied Equity	946
Value Exor's stake	**679**
weighting	15%

Premium scenario	
Revenues (GS forecast)	1,446
EBITDA margin (GS forecast)	7.7%
EBITDA (GS forecast)	111
10% premium to peer history	8.9x
Implied EV	983
Net debt	189
Implied Equity	793
Value Exor's stake	**570**
weighting	25%

Mid multiple on GS est.	
Revenues (GS forecast)	1,446
EBITDA margin (GS forecast)	7.7%
EBITDA (GS forecast)	111
EV/EBITDA (10yr avg - disc.)	8.1x
Implied EV	894
Net debt	189
Implied Equity	704
Value Exor's stake	**506**
weighting	25%

Discount multiple on GS ests.	
Revenues (GS forecast)	1,507
EBITDA margin (GS forecast)	7.7%
EBITDA (GS forecast)	111
10% discount to peer history	7.3x
Implied EV	804
Net debt	189
Implied Equity	615
Value Exor's stake	**441**
weighting	25%

Discount multiple on weak recovery	
Revenues (GS forecast)	1,446
EBITDA margin (GS forecast)	6.1%
EBITDA (GS forecast)	89
10% discount to peer history	7.3x
Implied EV	643
Net debt	189
Implied Equity	454
Value Exor's stake	**326**
weighting	10%

Risk weighted value	
EBITDA (GS forecast)	111
Implied multiple	8.2x
Implied 1yr fwd multiple	8.5x
Implied EV	952
Net debt	189
Implied Equity	715
Value Exor's stake (€ mn)	**411**

Historicals

Purchase multiple (2007 EBITDA)	6.9x
Purchase multiple (2007 EBIT)	7.3x
Initial investment	2007
Initial equity (US$)	874
2008 Net Debt (US$)	150
Initial EV (US$)	1,024

GS EBIT est.		Implied EV/EBIT
148.0	2007A	6.4x
67.0	2008A	14.2x
56.0	2009E	17.0x
80.8	2010E	11.8x
110.8	2011E	8.6x
137.8	2012E	6.9x

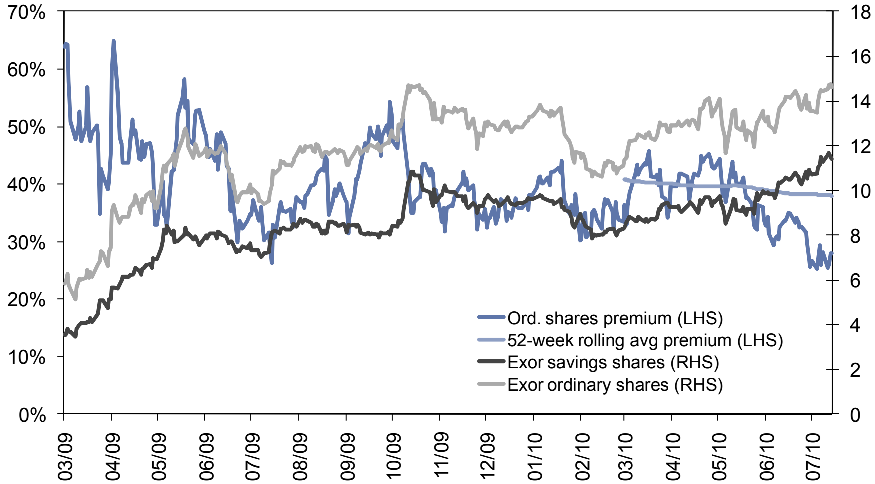
Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Multiple shares increase complexity but offers different ways to play the situation

For both Fiat and Exor, there are three share classes (ordinary, preferred and savings). Non-voting shares act as a control multiplier and lower the minimum economic ownership while maximizing control and can further restrict the protection of minorities. The shares with preferential voting rights are mostly held by the controlling family (in this case the Agnelli family through G.A. eC in Exor and indirectly in Fiat). The voting-disadvantaged shares have some other advantages such as a higher dividend.

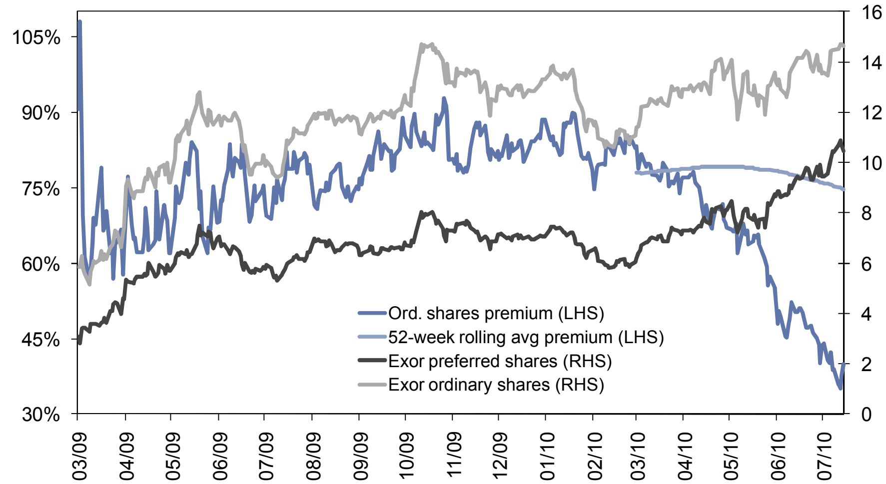
Savings and preference shares pay a higher dividend as a percentage of the par value – this introduces an additional cost. However, additional dividend payments are usually not adjusted for inflation and as a result the additional benefit is relatively small. Exor savings shares also have a cumulative feature – if the dividend is omitted, the minimum amount has to be added to the dividend which is paid in the following year.

Exhibit 36: Exor ord vs. sav



Source: Goldman Sachs Research, Bloomberg.

Exhibit 37: Exor ord vs. pref



Source: Goldman Sachs Research, Bloomberg.

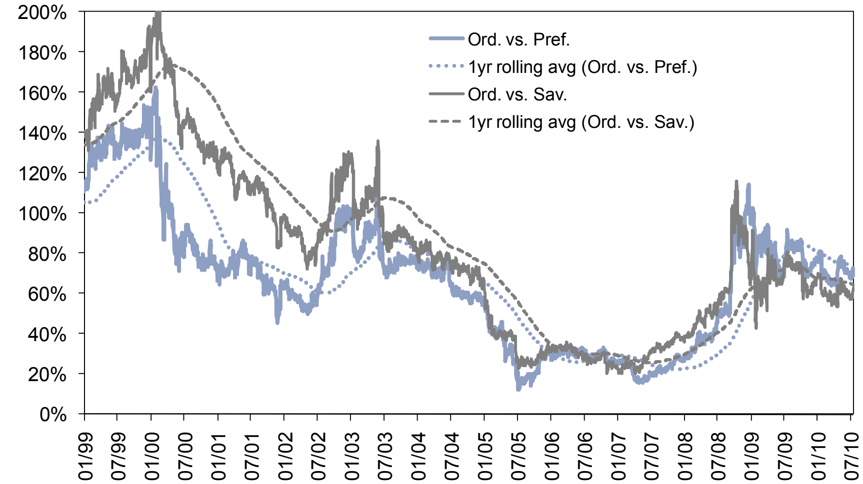
Savings shares often trade at discounts to ordinary shares. This is because they carry no votes, are often less liquid and not part of benchmarks (and thus mandates), their higher dividends might lead to higher taxation (income or withholding tax) for investors and there are limits to arbitrage such as restrictions on foreign ownership or borrowability of either share class. Exhibits 39-41 show that the savings share discounts vary over time, often with investor sentiment (discounts tend to widen in “bear” markets). From 2000 to 2005, most savings share discounts narrowed considerably; since 2007, discounts have widened on average. This has to be incorporated when deriving price targets and might lead to trading opportunities based on mean reversion. Events such as takeovers or proposals to convert savings to ordinary shares tend to result in a sharp narrowing of the discount. As earnings and cash flows appear at risk in the current macroeconomic slowdown, the additional cost of paying higher dividends on savings shares has been questioned, leading to more speculation over the conversion of dual shares. We note that the conversion of dual shares is not a current priority at either Fiat or Exor.

Exhibit 38: Exor does not offer dividend yield enhancement

Div yield	2008	2009	2010	2011E
Fiat Ord	2.37%	0.00%	1.69%	1.71%
Fiat Pref	2.99%	0.00%	5.44%	5.40%
Fiat Sav	4.48%	11.47%	5.43%	5.26%
Div yield	**2008**	**2009**	**2010**	**2011E**
Exor Ord	0.00%	0.00%	2.03%	1.81%
Exor Pref	1.06%	8.42%	4.56%	2.88%
Exor Sav	0.00%	0.00%	3.61%	2.81%
Div premium	**2008**	**2009**	**2010**	**2011E**
Exor Pref vs. Ord	30%	16%	19%	19%
Exor Sav vs. Ord	80%	44%	29%	29%
Fiat Pref vs. Ord	0%	na	82%	82%
Fiat Sav vs. Ord	39%	na	91%	91%

Source: Goldman Sachs Research, Bloomberg.

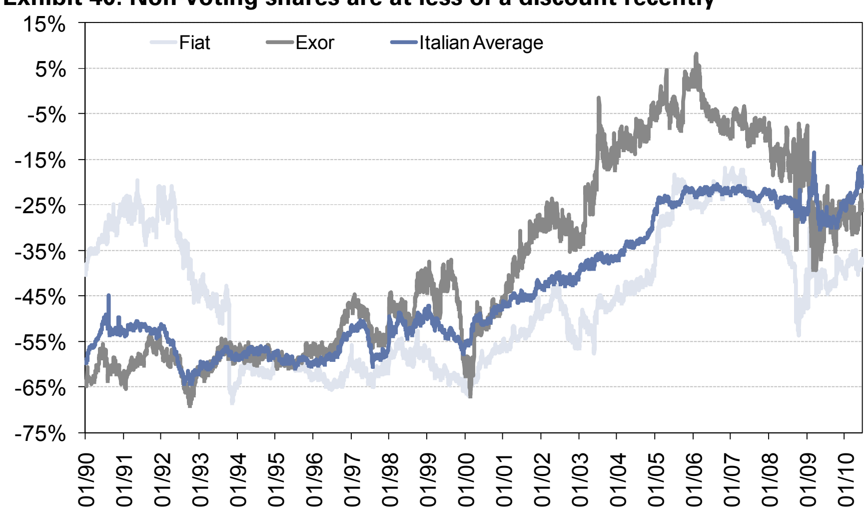
Exhibit 39: Fiat ord premium vs. pref and sav



Source: Goldman Sachs Research, Bloomberg.

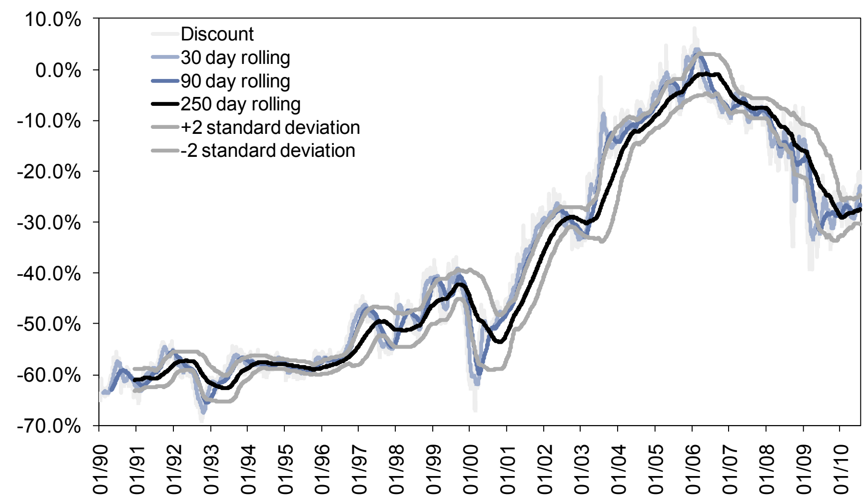
A strong catalyst for the conversion of dual shares could come from changes in regulation and shareholder rights. The EU started proceedings with the aim of streamlining corporate governance within the EU, but decided in December 2007 not to take action on the question of proportionality between capital and control, after much lobbying from the holding companies and the Swedish government. For further details on the EU study see *Proportionality between ownership and control in EU listed companies*: External Study Commissioned by the European Commission, May 18, 2007.

Exhibit 40: Non-voting shares are at less of a discount recently



Source: Goldman Sachs Research, Bloomberg.

Exhibit 41: Exor saving shares discount over time



Source: Goldman Sachs Research, Bloomberg.

Exor stub offers 31% ROCE if the NAV discount narrows to the old IFIL average

An Exor stub can be constructed by purchasing Exor shares and selling short a combination of shares in its listed holdings. Exhibit 42 shows an implementation for Exor where only the more liquid of dual share classes are shorted, given liquidity and borrowing constraints. A minor risk of this strategy is that the spreads between different share classes may change materially over time and result in a different return on the trade. Below, the Exor stub isolates exposure to Exor's €0.7 bn unlisted holdings (major holding is C&W), less liquid listed assets, net cash of €153 mn and changes in the NAV discount.

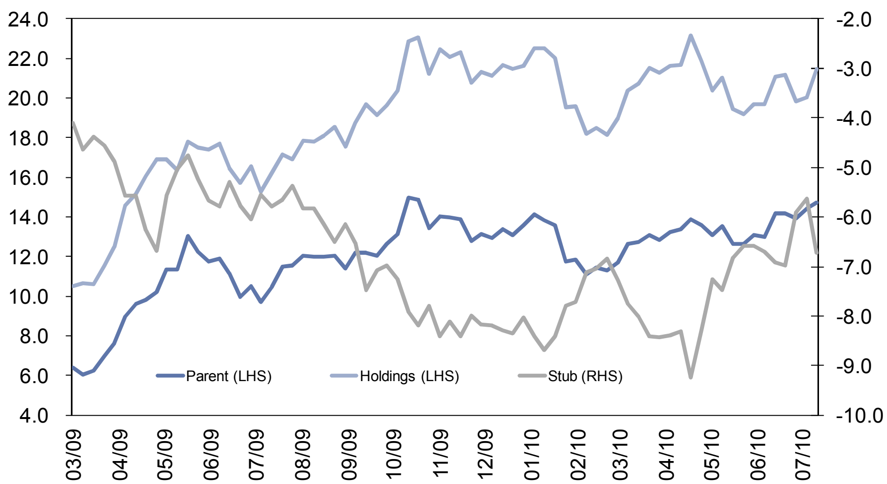
Exhibit 42: 31% potential ROCE if Exor NAV discount narrows to 30%

Shorts	SEDOL	BBG	Name	% stake	Curr.	Stub ratio	3m ADV (mln, USD)	Value per share (EUR)	% share	NAV discount	Stub value (EUR)	ROCE [1] (50%, 50%)	ROCE [1] (20%, 20%)
Short 1:	5748521	F IM	Fiat SpA	29.20%	EUR	1.5297	335	**15.20**	*102%*	***-40%***	-6.00	-1%	-3%
Short 2:	4824778	SGSN VX	SGS SA	15.00%	CHF	0.0049	27	**5.49**	*37%*	***-35%***	-4.78	6%	14%
Short 3:										***-30%***	-3.55	12%	31%
Short 4:										***-25%***	-2.33	19%	48%
Short 5:										***-20%***	-1.10	26%	65%
Short 6:										***-15%***	0.12	33%	83%
Short 7:										***-10%***	1.34	40%	100%
Short 8:										***-5%***	2.57	47%	117%
Short 9:										***0%***	3.79	54%	134%
Short 10:										***5%***	5.01	61%	151%
							Stub value:	**-5.76**		***10%***	6.24	67%	169%
							Stub NAV:	**3.79**		***15%***	7.46	74%	186%
							Up/down to target stub value:	**31%**		***20%***	8.68	81%	203%

[1] ROCE = Return on capital employed, with assumed margin requirements on long and short legs respectively.

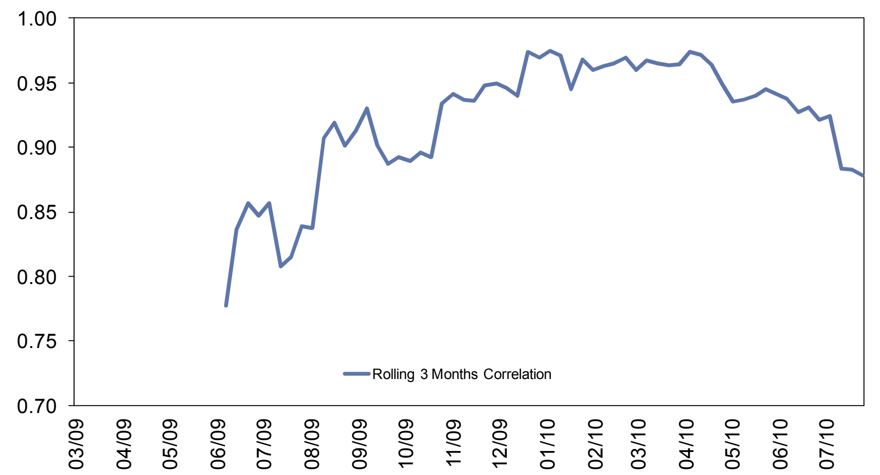
Source: Company data, Bloomberg, Goldman Sachs Research estimates.

Exhibit 43: Stub value, parent company price & value of listed portfolio



Source: Goldman Sachs Research estimates, Company data, Bloomberg.

Exhibit 44: Correlation between parent and the listed portfolio



Source: Goldman Sachs Research estimates, Company data, Bloomberg.

Risks related to buying or selling stubs

Purchasing a stub involves purchasing a parent company's shares and simultaneously selling short a combination of shares in proportion to the parent company's holdings.

Selling a stub involves the reverse – purchasing the combination of shares of the holdings and selling short the parent company's shares. For the long side of the trade, investors can lose the entire gross amount invested. For the short side of the trade, the risk of loss is potentially unlimited and investors may be required to cover positions at an unfavourable price. We also acknowledge the risk of regulatory changes which restrict selling short specific stocks given the current market environment.

When undertaking a stub trade, investors should bear in mind both the fundamental risks associated with any directional views that they are seeking to exploit, as well as the transactional or arbitrage risks that may not be immediately apparent. Holding company NAV discounts are driven by multiple interrelated factors, including market risk aversion, borrowing stability, minority protection and regulatory risks.

Summary financials

Exhibit 45: Consolidated summary financials

Exor (€ mn)							
Profit model (group, € mn)	**2007**	**2008**	**2009**	**2010E**	**2011E**	**2012E**	**2013E**
Revenue	**2,661**	**2,681**	**2,427**	**2,461**	**2,640**	**2,829**	**2,975**
Growth	*NA*	*1%*	*-9%*	*1%*	*7%*	*7%*	*5%*
EBITDA	158	85	87	268	293	320	345
Margin	*6%*	*3%*	*4%*	*11%*	*11%*	*11%*	*12%*
EBIT	66	(0)	(7)	172	195	220	243
Margin	*2%*	*0%*	*0%*	*7%*	*7%*	*8%*	*8%*
Net Income (recurring)	**480**	**327**	**(287)**	**189**	**453**	**831**	**843**
Margin	*18%*	*12%*	*-12%*	*8%*	*17%*	*29%*	*28%*
EPS (€)	**3.04**	**1.39**	**-1.20**	**0.77**	**1.84**	**3.38**	**3.42**
Dividend (€)	157.89	235.29	238.56	246.23	246.23	246.23	246.23
Payout ratio	*33%*	*72%*	*-83%*	*130%*	*54%*	*30%*	*29%*
Balance Sheet (group, € mn)	**2007**	**2008**	**2009**	**2010E**	**2011E**	**2012E**	**2013E**
Cash	919	975	630	680	739	811	893
Total Current Asset	1,734	1,843	1,698	1,785	1,871	1,971	2,075
Total Assets	**9,059**	**7,749**	**7,595**	**7,792**	**8,211**	**9,013**	**9,821**
Debt	1,557	1,405	1,355	1,371	1,371	1,371	1,371
Total Liabilities	2,657	2,323	2,205	2,271	2,293	2,317	2,334
Equity	6,402	5,426	5,390	5,521	5,919	6,697	7,487
Total Liabilities & Equity	**9,059**	**7,749**	**7,595**	**7,792**	**8,211**	**9,013**	**9,821**

Source: Company Data, Goldman Sachs Research estimates.

Appendix: Refresher on stub trading and European holding company discounts

A stub gives focused exposure to unlisted businesses within a listed company

Stub situations emerge if a listed company owns substantial stakes in other listed companies. If certain liquidity and borrowing requirements are met, investors are able to trade the stub, which is the collection of unlisted businesses of the parent company, by going long the parent company and selling short its stakes in listed subsidiaries or cross-holdings. By trading stubs, investors isolate exposure to the valuation of residual unlisted businesses and/or the valuation of the parent company relative to its holdings.

Stub situations arise mostly in three situations:

- **holding companies** that have a portfolio of listed shareholdings
- companies that have carried out an **equity carve-out** (or partial spin-off), potentially with the intention to complete it later
- companies with substantial **strategic investments** in other listed companies that are usually unrelated to core businesses.

Stub opportunities emerge from intra-group relative value anomalies

Trading opportunities emerge if the market value of the parent company is materially different from its sum-of-the-parts valuation after adjusting for net debt, also called net asset value (NAV). In the NAV, listed parts are usually marked to market, while unlisted parts can be valued using common techniques such as DCF or relative valuation. This approach highlights discounts or premiums assigned by the market to the company's holdings. These may be anomalies with a clear case for relative value convergence – but, more often, multiple factors cause such discounts or premiums to persist for longer periods until a catalyst occurs.

The stub ratio indicates how many shares to sell short for each share long of the parent company

The stub ratio indicates how many shares to sell short for each share long of the parent company. It can be calculated by **dividing the number of shares in a company held by the number of shares outstanding of the parent company.** The number of shares outstanding should include all share classes (ordinary and preferred, A, B, C, etc.). When a company buys back shares, they are usually kept as treasury shares and can become material in the valuation. We decide whether or not to adjust the stub ratio depending on which case they fall under:

- If the treasury shares are intended to be cancelled, we decrease the number of shares outstanding and therefore increase the stub ratio (number of shares owned in a listed holding/ number of shares outstanding).
- If they are used to match liabilities/employee stock options or for subsequent sale, the number of shares outstanding is left unchanged.

For example, Hochtief owns 163,844,626 shares (54.49%) of Leighton. Hochtief has 70,000,000 ordinary shares outstanding and no other share classes. The stub ratio for Leighton is 150,650,410/ 70,000,000 = 2.3406. Based on company filings, Hochtief currently has 4,312,000 treasury shares. Assuming those are to be deleted, the stub ratio is 150,650,410/ (70,000,000-3,455,685) = 2.4622.

Stub trades can be implemented physically or synthetically

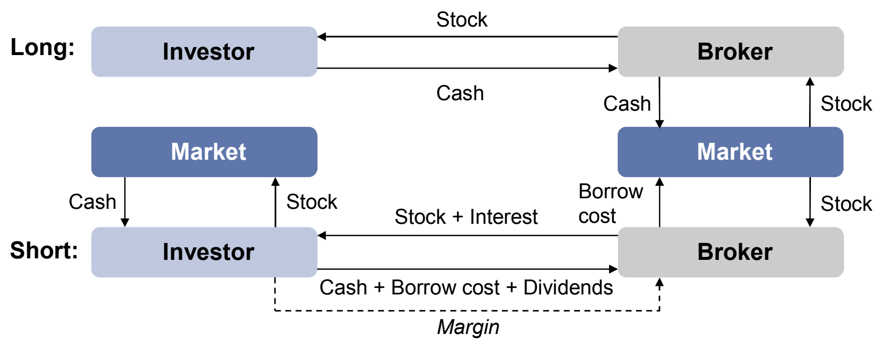
There are different ways to implement stub trades. The optimal implementation will depend on the investor's desire to leverage and on trading constraints. We differentiate broadly between physical and synthetic implementation:

- **Physical implementation** involves buying and selling short shares with different levels of funding. Exhibit 46 shows the mechanics – investors will usually buy shares partially financed by debt and sell short shares only with the margin requirement as equity. Minimum margin requirements are usually set by market regulators and stock exchanges.

- **Synthetic implementation** is a combination of OTC swaps as shown in Exhibit 47. In addition, it is possible to trade stubs as one swap. A major difference from physical implementation is that margin requirements are set by the broker. Depending on the credit risk of the investor, this can allow for higher leverage.

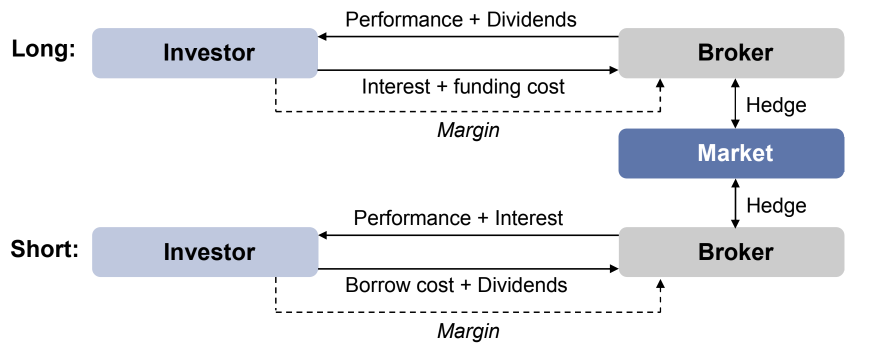
- For long-only investors, it may also be possible to buy structured certificates, and on more liquid situations to trade options on stubs.

Exhibit 46: Implementation with physical long and short positions



Source: Goldman Sachs Research.

Exhibit 47: Synthetic implementation with swaps



Source: Goldman Sachs Research.

Main determinants of cost are holding period, margin requirements, ease of execution, and tax

Entry and exit costs such as market-impact-related costs and brokerage fees are usually similar. However, holding period costs such as financing and borrow costs can vary, as can costs due to differences in dividend income between long and short positions. When investors physically sell stocks short, they leave collateral which is invested in risk-free bonds and pay borrow cost embedded in the "rebate" rate, which is usually 25-50 bp lower than the interest on the collateral. Initial margin requirements on the short can be partially offset by pledging long positions.

For long positions via swaps, investors pay funding costs on top of interest incorporating a balance sheet charge and the cost of hedging the position. For short positions via swaps, investors receive the interest less the borrow cost. Investors can also trade a swap directly on the stub. Advantages of synthetic implementations are ease of execution and currency hedging, tax considerations and potentially lower capital employed. A disadvantage of OTC swaps is that trades have to be closed out with the broker they were entered with.

Margin requirements and capital employed drive returns on stub trades

Investors should consider capital employed rather than return on the stub when trading stubs. As shown in Exhibit 48, the return on capital employed can vary considerably for the same expected return. This is because a stub trade is a combination of a long and a short trade, potentially with different notionals. The capital employed against which changes in the stub value should be compared will be determined by margin requirements; the return on capital employed will increase with lower margin requirements (and thus higher leverage).

Exhibit 48: Returns on stub are identical, return on capital differs …

Capital employed example		Stub A		Stub B
Parent company price		120		500
Value of holding (using stub ratio)		20		400
Stub value		100		100
Expected change stub value (+10%)		10		10
Margin (50% on both legs)		50%		50%
Capital employed		**50% x (120+20)**		**50% x (500+400)**
	=	70	=	450
Return on Capital		**14.29%**		**2.22%**

Source: Goldman Sachs Research.

Exhibit 49: … which also is a function of margin requirements

Leverage example		Stub A		Stub B
Parent company price		120		120
Value of holding (using stub ratio)		20		20
Stub value		100		100
Expected change stub value (+10%)		10		10
Margin (different requirements)		**20%**		**50%**
Capital Employed		20% x (120+20)		50% x (500+400)
	=	28	=	70
Return on Capital		**35.71%**		**14.29%**

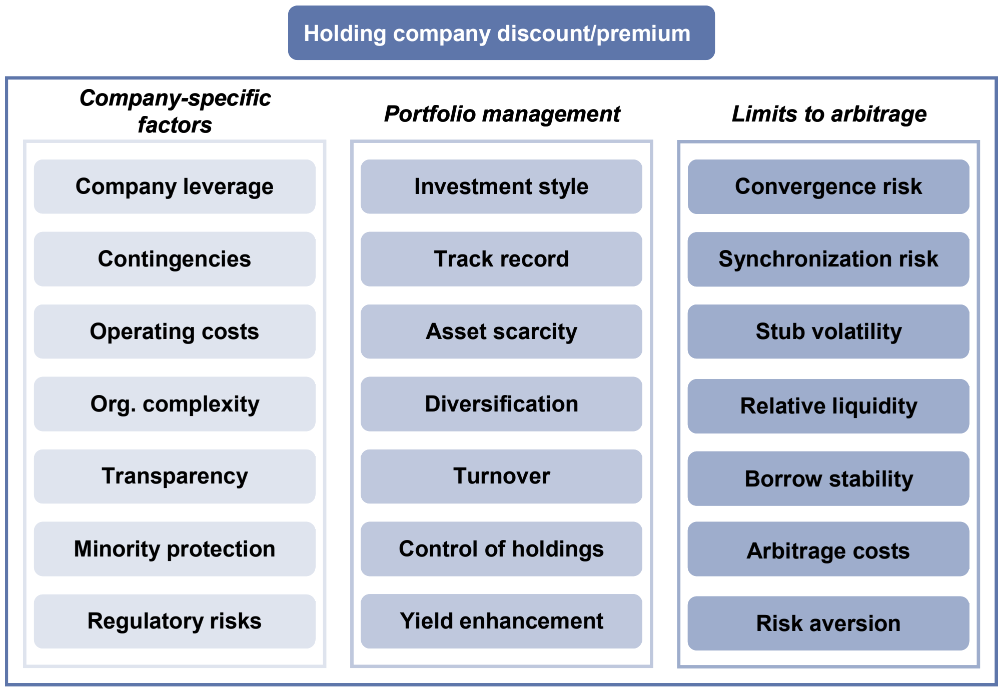
Source: Goldman Sachs Research.

Holding companies tend to trade at discounts to their NAVs

There is strong evidence that the market values holding companies at a persistent discount to their NAV, often called holding company, conglomerate or diversification discount. NAV discounts tend to vary over time but are mean-reverting and there are often significant differences between companies. As a result, holding companies tend to attract arbitrageurs such as proprietary trading desks or hedge funds, but also activist investors who see the opportunity of a collapse eliminating the NAV discount.

We find that factors such as regulatory risk, corporate governance, different approaches to portfolio management and principal-agent risks play an important role in explaining the variation in discounts over time and between different holding companies. However, limits to arbitrage can also cause consistently high NAV discounts. Exhibit 50 summarises these factors.

Exhibit 50: We identify 21 interrelated factors driving holding company NAV discounts



Source: Goldman Sachs Research.

Discounts to NAV can result from company-specific factors

- **Company leverage (and excess cash):** If a holding company uses leverage efficiently and has an appropriate capital structure, it offers investors a leveraged return on its holdings. However, as the leverage increases so does the sensitivity to the underlying holdings and the risk carried. Thus whether higher leverage increases or decreases the NAV discount will largely depend on equity market conditions or risk aversion and the sentiment for the holdings.

- Some holding companies have significant non-operating cash balances relative to their market value – for example after the sale of investments (e.g. Groupe Bruxelles Lambert after it sold Bertelsmann). Excess cash has to be valued by the market incorporating reinvestment risk. Reinvestment risk can be higher if a controlling shareholder influences investment decisions. As a result, cash can be valued at a discount by the market, reflecting dilution risk until the investment is made or excess cash is distributed as dividend. A good investment track record and availability of investments prevents high NAV discounts.

- **Contingencies:** Contingent assets or liabilities can introduce fundamental risks that result in higher NAV discounts. In the published accounts, they are usually not disclosed in the balance sheet but discussed separately in the notes to the financial statements. As a result, they are more difficult to capture. Examples are possible liabilities from pending litigation, loan guarantees or pensions and possible value appreciation of assets if real estate is accounted for at cost. Also yield enhancement strategies with options bought or sold around listed holdings or convertible bonds can increase uncertainty if they are not properly disclosed. To account for these in the NAV it is necessary to assess the probability of such cash flows materialising – this increases the overall risk to the NAV estimate.

- **Operating costs:** While holding companies can create benefits for their shareholders by effective portfolio management, there are usually costs involved in running the company (e.g. taxes and management costs). If these costs are substantial and not outweighed by benefits, the market may incorporate the negative NPV of these future costs in its valuation, which can in part explain the discount. Taxes on dividends and on realised (and unrealised) gains play an important role. Countries with more favourable holding company regimes are Sweden, Belgium, Luxembourg, the Netherlands and France – Italy and Germany appear less favourable. Management costs tend to be low in absolute terms.

- **Organisational complexity:** Holding companies are often characterised by complex organisational structures for two reasons: (1) they may be part of pyramidal structures that aim to maximise control while minimising capital employed, and (2) holding companies often seek to minimise taxation by creating separate entities in countries with favourable holding company taxation. However, increasing organisational complexity is valued negatively by the market because of higher operating costs and lower transparency. As a result, restructuring aimed at reducing organisational complexity through demergers or buyouts usually lowers NAV discounts.

- **Transparency:** As holding companies are often characterised by complex organisational structures, high portfolio turnover, contingent assets or liabilities and yield enhancement transactions, they are not easy to analyse. The more layers in the corporate chain the less visible the group is. If the holding company does not provide detailed and timely disclosure of its current holdings and voting rights, operating costs and tax situation, the market may assign an uncertainty discount.

- **Minority protection:** From the perspective of investors, highly concentrated ownership limits accountability to minority shareholders and is often viewed negatively by the market, leading to a higher discount. The principal-agent problem here is between the controlling shareholder and its minorities – which arguably is more prevalent in cases of dual share classes (one share class having preferential voting rights – most common in Italy and Sweden). Dispersed ownership, in contrast, protects the rights of minority shareholders, prevents abuses of power, and increases free float and liquidity.

- **Regulatory risks:** Holding companies are often subject to specific regulation, either on taxation, their control of companies or corporate governance. As a result, changes in regulation can lead to changes in the market's perception of the value of holdings. Double taxation of dividends will have an impact from a going-concern perspective and capital gains taxation from a break-up or exit perspective. Similarly, as holding companies can profit from control premiums resulting from unequal distribution of voting rights on their holdings, a regulatory change can lead to a loss of control.

Portfolio assets, the investment approach and track record can lead to NAV premiums

- **Investment style**: There are several dimensions along which the "investment styles" of a holding company can be compared: active vs. passive, minority stakes vs. controlling stakes, listed vs. unlisted companies, short vs. long investment horizon, regional vs. global, etc. However, while differences in investment styles can warrant a discount or premium to the NAV, it is often questionable whether a holding company actually follows a professional approach to portfolio management focused on creating value for its shareholders. A clearly communicated investment strategy aimed at generating a net operating profit in excess of the weighted average cost of capital indicates such value creation. If a company is merely a rigid control structure, the market will assign a higher discount.

- **Track record:** By investing in a holding company, investors give up discretion they could retain by replicating the portfolio. Investors may assign a higher discount to NAV to reflect uncertainty about how much value the holding company management will add relative to long-term costs (i.e. previous president of misused funds or inefficient allocation of resources). Conversely, a good track record would help to mitigate information asymmetry and agency costs. One indicator is the relative performance of a holding company versus the market.

- **Asset scarcity:** If the holding company invests in attractive, undervalued assets that are not accessible to investors (e.g. Bertelsmann before it was sold by GBL, CIR's stake in Sorgenia), the market might assign a NAV premium. This is one reason why some holding companies are increasingly focusing on private equity transactions (e.g. Eurazeo and Ratos). Scarce investments must be material in the portfolio context – in an optimal case, all other investments are listed so that exposure to the valuation of an unlisted asset can be isolated with a stub trade. In addition, the value the market assigns to the holding will depend on the anticipated exit route.

- **Diversification (or conglomeration):** Provided the portfolio has no sector or country concentrations (e.g. Investor and Industrivarden focus on Swedish stocks), as well as low correlation across the assets, an investor can get a diversified equity portfolio through an investment in a holding company at potentially lower transaction and management costs. However, there is also evidence that diversified firms destroy value by subsidising subsidiaries that are inefficient. Generally, the market tends to view conglomeration negatively because of the potential agency costs and the additional complexity. However, there are successful examples of conglomerates that have been able to increase shareholder value (e.g. General Electric).

- **Turnover:** Usually, holding companies are characterised by a long investment horizon, also because of the size and control of their holdings. However, if holding companies have too rigid an approach to their holdings, it is questionable whether the holding company is really aiming at value creation for all its shareholders or if it is merely a control structure for a group of shareholders, which would warrant a higher discount.

- **Control of holdings:** A positive influence by the holding company will not only create benefits for the shareholders of the holding company but in part also for the shareholders of the holdings – as a result, the value of control is questionable. Also, a holding company can create additional value for its shareholders by granting services to the companies in which it has a stake (e.g. Pirelli via Pirelli Labs). This will create additional revenues for the holding company but may raise corporate governance concerns.

- **Yield enhancement strategies:** Many holding companies follow yield enhancement strategies in order to mitigate operating costs and other frictions caused by the holding company structure. Through option strategies, the holding company management can express short- to medium-term views around its holdings. Covered call selling is a popular strategy. The holding company exploits a view that the stock price of one of the holdings has limited short-term upside and receives an up-front premium. Similarly, if a holding company has a positive long-term view on one of its holdings and would be willing to increase its position at a lower price, it can sell put options with the respective strike price. A related strategy, which is followed by holding companies with active portfolio management, is stock lending for which a borrow fee is received.

Limits to arbitrage play a central role in assessing the risk/return trade-off of stub trades

- **Convergence risks:** The prevalent arbitrage risk of stub trading is convergence risk, i.e. the risk that the relative value anomaly does not resolve or worsens during the duration of the investor's trade. For instance, NAV discounts can widen if noise traders favour investing in a subsidiary because it is a popular stock (e.g. a recent IPO) and/or if institutional investors neglect holding companies because they prefer a "pure play". Convergence is mostly idiosyncratic and often depends on corporate catalysts changing the relationship between parent company and subsidiaries. Examples of corporate catalysts include the completion of a spin-off, the sale of (unlisted) equity stakes, tax and regulation changes or restructuring.

- **Synchronization risks:** As single investors are unable to influence prices alone there is synchronisation risk between arbitrage investors. Lack of communication between investors makes the entry decision difficult and adds to convergence risk during the trade. There is also synchronisation risk related to the exit of a stub trade. If the convergence is dependent on a corporate catalyst and several arbitrage investors have positions in the stub before the catalyst occurs, then in order not to lose performance at convergence, the timing of the exit decision has to incorporate the market impact of the group exiting the trade. Otherwise, if the parent company is not sufficiently liquid, the exit of the group of arbitrageurs might lead to a new liquidity-related valuation anomaly.

- **Stub volatility:** The relationship between parent company and subsidiaries will determine the volatility or holding period risk of the stub trade. Uncertainty during the duration of the trade can be large and relative value divergence may lead to higher margin requirements affecting risk-adjusted returns and employing additional capital. We believe three factors determine holding period risks: the leverage of the stub trade, the co-movement of long and short positions and the respective volatilities.

- **Relative liquidity:** Differences in liquidity and liquidity risk can lead to a discount on equity stakes held or the holding company itself. Liquidity risk occurs with non-large cap stocks when a lack of sufficient market depth and liquidity limits the maximum position that can be taken (long/short) or closed, especially if the parent company owns the majority of a company.

Lack of liquidity limits price discovery and impedes short selling. It increases the market impact of entering or exiting positions and thus the influence of noise trading. If the holding company has significantly lower liquidity than its holdings, the relative value anomaly might be liquidity-driven and persist as the holding company valuation does not immediately reflect the value of its holdings. Similarly, if liquidity of the holdings is low relative to the holding company, the market might assign a discount as management might not be able to sell its holdings at current market prices.

- **Borrow stability:** A stub trade is implemented via a combination of long and short positions – thus holdings have to be borrowable at reasonable cost and are subject to recall risk. Short-selling constraints prevent arbitrageurs from correcting an anomaly and NAV discounts persist. Risks are particularly prevalent in the event of corporate activity. Short squeeze risk usually decreases with higher liquidity of the underlying stock, as in the event of a recall it would be possible to close out of the short position by repurchasing the stock in the market.

- **Arbitrage costs:** The fixed costs of identifying and evaluating stub opportunities can be high. And there are transaction costs such as market-impact-related costs and brokerage fees, as well as holding period costs, which are mainly financing, borrow and dividend-related. The majority of European medium to large cap stocks can be borrowed at reasonable cost. The exceptions are some special cases where borrow availability is limited, notably recent IPOs, highly popular and volatile stocks, stocks involved in corporate activity or highly illiquid stocks.

- **Risk aversion:** In addition to idiosyncratic risks to convergence, worsening market conditions and increasing risk aversion are notable risks to relative value convergence within holding companies. Holding companies are often out of favour in difficult market conditions – potentially because they are perceived as more risky and are usually less liquid. As a result, they can exhibit greater market sensitivity during market corrections than their listed holdings, leading to a widening discount.

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Reg AC

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