GATEMORE

11 September 2024

Mr. Ian Carter
Chairman of the Board
Watches of Switzerland PLC
Aurum House,
2 Elland Road,
Leicester, LE3 1TT

Dear Ian,

As you may know, Gatemore Capital Management LLP ("Gatemore" or "we") manages the Gatemore Special Opportunities Fund ("GSOF" or the "Fund"), which currently holds an economic interest of approximately 1.9 million shares in Watches of Switzerland Group PLC ("WOSG" or the "Company").

Founded in 2005 and based in London, Gatemore is a leading activist investor focusing on turnarounds and recoveries. The Fund primarily targets UK small- and mid-cap companies that are often under-penetrated and overlooked by the market. We seek to invest in fundamentally sound businesses that are undervalued and have strong potential for recovery and growth. Our strategy is to influence outcomes and drive outperformance through thought leadership and deep engagement, aiming to effect positive change and unlock value within the companies in which we invest. The Fund has a highly concentrated portfolio, which enables Gatemore to engage effectively with management teams and corporate boards to drive recoveries in share price. Since its launch in November 2018, GSOF has delivered strong returns and significantly outperformed broad market benchmarks.

We believe WOSG is a fundamentally strong business run by a proven management team

WOSG is a best-in-class retailer and a leader in its industry, providing customers with a premium experience. It boasts longstanding partnerships (over 75 years) with the top watch brands such as Rolex, Patek Philippe, and Audemars Piguet — indeed, some of the strongest luxury brands in the world. The Company has a dominant position in the UK (the #1 luxury watch market globally on a per capita basis) and is rapidly expanding its market share in the vast and under-penetrated U.S. market.

The luxury watch market is a compelling industry that has consistently grown ahead of GDP, driven by demand that far outstrips supply for luxury timepieces, supported by price and margin stability provided by brand partners. This insulates the business from economic cycles and underwrites returns on capital investments. Additionally, the industry maintains high barriers to entry through trusted, long-term brand relationships and highly invested store estates.

Financially, WOSG has a compelling profile, with a 19% compound annual revenue growth and 27% compound annual adjusted EBIT growth over the past decade, supported by well-invested assets delivering high returns on capital (20%+) and strong cash flow, and a robust balance sheet. The Company's November 2023 Long-Range Plan (LRP) aims to double the size of the business in the next five years.

WOSG's management team has been together for a decade and has an exceptional track record of delivering on ambitious plans. Importantly, management and the Board are well aligned with shareholders, as demonstrated by the CEO's 3.2% ownership stake and recent share purchases by the Chairman and CFO.

We believe WOSG is significantly undervalued and misunderstood by the market

WOSG is trading at a similar share price to its IPO, despite being a significantly larger business, with revenue more than 2x higher and EPS 4.5x higher. In fact, the Company is trading at EV/EBIT and P/E multiples that are 55 – 70% lower than when it was listed in 2019.

	FY19E[1]	FY25E[2]	Change
Revenue (£m)	773	1,694	+119%
EBIT (£m)	53	162	+206%
EBIT margin (%)	6.9%	9.6%	+395%pts
EPS (p)	9.0	41.8	+364%
ND/EBITDA	1.7x	0.5x	(72%)
Share price (GBp)	270p	374p	+39%
Market cap (£m)	651	901	+39%
Enterprise value (£m)	771	1,001	+30%
EV/EBIT	14.5x	6.2x	(57%)
P/E	30.0x	8.9x	(70%)

We believe there are two common misconceptions in the market that have resulted in the share price not reflecting the company's performance and outlook.

The first misconception is that WOSG is significantly affected by the global slowdown in the luxury sector. While we do not expect growth to be as strong as it was during the pandemic, Swiss watch export data, along with WOSG's own performance, suggests that the US and UK markets remain resilient. Most of the weakness in the luxury sector has been driven by negative growth in China; however, WOSG has no exposure to Asia.

The second misconception is that Rolex's acquisition of Bucherer will jeopardise the WOSG's relationship with Rolex. As part of our deep due diligence, we have explored this topic extensively and held discussions with industry experts familiar with both parties. Consistent with what the Company has stated publicly, we believe the acquisition by Rolex was a defensive manoeuvre to preserve the Swiss heritage of a key partner, rather than an aggressive move into retail. Furthermore, we understand WOSG's partnership with Rolex remains as strong as ever, with WOSG being one of the top two vendors of Rolex watches globally.

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[1] *FY19E as at IPO in May 2019.*
[2] *Source: Bloomberg as at 6-Sept-24.*

WOSG's removal from the Stoxx 600 index, combined with the broader malaise in UK markets, has further detracted from the share price performance. With all these factors at play, WOSG's share price is now significantly dislocated from its intrinsic value. Taking a long-term view, we see this as a near-term opportunity for the Company to accrete permanent value for all shareholders.

A substantial share buyback is in the best interests of shareholders

We believe now is an opportune time for the Company to launch a substantial share buyback program. At current price levels, the return on investment (ROI) for repurchasing shares is highly compelling, in the range of 16–18%[3], providing returns commensurate with other capital allocation opportunities for the business. While we respect the Board's existing capital allocation policy, the unprecedented weakness in the share price creates an immediate opportunity for permanent value accretion for shareholders, free of execution risks.

We note the Company continues to maintain a very strong balance sheet, with approximately £100 million of net debt following the Roberto Coin acquisition (only 0.5x ND/EBITDA) and greater than £200 million in liquidity. We believe WOSG can conservatively support an immediate £25-50 million buyback alongside other planned investments in WOSG's operational business, consistent with the LRP. Such a move would reinforce the Board's confidence in the business and its commitment to maximising shareholder returns.

Please take our suggestions in the spirit in which they are intended — to support the Board and management in their thought process around capital allocation strategy. We would welcome the opportunity to discuss our thoughts with you at any time. Thank you for your consideration.

Sincerely,

Liad Meidar

Liad Meidar
Managing Partner
Gatemore Capital Management LLP

[3] Calculated with share price of 370p, based on counterfactual of investing the capital in the business to achieve the same EPS uplift. Based on inverse of FY25E and FY26E P/E ratios, adjusted for tax. Inverse of P/E multiples is 11-13% post-tax, 16-18% pre-tax.

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