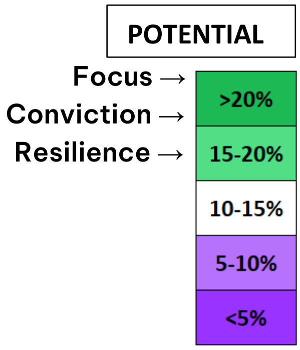
September 24, 2023

"Culture is not the most important thing, it's the only thing." Jim Sinegal, founder of Costco

Friend/Owner,

This was the performance of the funds in the first half of 2023:

Fund	Profitability 1H 23
Conviction	26,56%
Resilience	19,68%
Focus	10,25%
ACWI Index	11,45%



Thermometer and potential

We have added next to the yield a new section with the **average return we expect for each fund over the next 5 years**. We express it in 5 tranches: <5%, 5-10%, 10-15%, 15-20% and >20%.

This potential is based on the difference between today's price and what we estimate our companies will be worth in 5 years. We find it useful for you to have a benchmark of their value versus price.

Our objective is to **beat the ACWI world index over the long term**. The historical return of world indices is around **8-10% per year**. As there are around **50,000 listed companies** in the world, we should always be able to have in the funds a group of 30-40 that, meeting our requirements of **culture, quality and price**, give us a potential of more than 10%.

Recurrently investing the same amount every month is the easiest way to be successful in investing and, if you also make **additional contributions at low prices,** you can boost your profitability even more. At times when prices are expensive and the potential falls below 10%, it may be a time to wait and not make extraordinary contributions. Conversely, if prices are cheap and the potential is above 15-20%, it may be a time to make larger contributions than usual.

Although 2023 has seen upside, the potential for returns over the next few years remains very high as many of our companies continue to trade at **extremely cheap prices**. Several Conviction and Focus growth companies are trading at less than 10 times earnings.

What we are looking for

There are different ways to make money investing. The one we like best is to buy **extraordinary companies at reasonable prices** and own them as long as these two requirements continue to be met. In the short term (less than 5 years), the price can do very different things to the evolution of value, but in the long term it always ends up following the evolution of earnings per share. If our companies increase their profit at a certain rate over many years, the price will have a very similar evolution.

What makes a company extraordinary?

For us two things: its people/culture and its business.

Let's start with the most important thing, your people. A company is nothing more than a group of people using certain resources to solve a problem for society. The quality of those people is what will most affect the future of the company. **Culture is to a company what character is to a person**. We look for 3 qualities: integrity, determination and ability.

The second characteristic is that your business generates **high returns** on the capital you invest, that it is **defensible** against competitors and, ideally, that you can continue to **reinvest** capital at those high returns for **a long time**.

We will use Constellation Software (CSU, all figures in Canadian $) as a guide, which we started investing in 9 years ago and is in all 3 funds. It is a Canadian company that acquires small vertical software companies.

When we studied it in 2014, we saw in **Mark Leonard** a founder who was doing what they call his life's work. We love that the founder of the company is still running it after many years. For a founder, his company is usually more than just a way to make money. It is his creation, almost like a child. The decisions a founder makes are usually more **long-term** than those made by a CEO who knows he won't be at a company for more than 5-7 years. Leonard has most of his personal wealth invested in CSU and doesn't take a salary, so his **incentives are aligned** with ours. And not just his. The employees own 15% of the company (including Leonard's 5%). When you own something, you take better care of it.

CSU has a strong ownership culture. Executives must allocate **75% of their bonus** (always paid in cash) to **buy** company **shares** in the market. In addition, there is a high degree of **decentralization** and each subsidiary is fully independent in making operational decisions, with the parent company retaining only the decision on capital allocation (large acquisitions).

The companies that CSU acquires sell software for specific niches within different sectors such as healthcare, transportation, education or real estate. Because the potential market for these niches is very limited, the large companies in the industry ignore them. Leonard realized that although the potential growth is small in each niche, they are still **software** companies, which is a big business in itself. Software usually has **recurring revenue** with **high margins, needs little capital** and **has captive customers**, (it is difficult to switch vendors once you have learned to use the product and it is integrated into a company's day-to-day business). CSU began to buy these types of companies and bring them together under one umbrella, reducing costs in common functions such as accounting, human resources, legal, etc. The profits generated by the acquired companies are reinvested in making new acquisitions, which are the source of growth.

Since it was founded in 1995 until 2023, it has acquired **more than 750 companies**. In all that time it has only sold one and Leonard still regrets the sale. Not selling gives them a **reputation**. The sellers they acquire companies from tend to be entrepreneurs who generally like to know that their creation has a permanent home at CSU and will not be constantly changing hands as if they sell it to a private equity fund.

When we first invested in CSU in late 2014, its sales were 1,844M and its profit was 362M. We thought they could grow at more than 15% for many years. By 2023 their sales are going to be around 11,300M and their profit at 2,200M, having **multiplied both x6 in 9 years**, 22% annualized. As a result, the stock has gone from $335 to $2,700, an annualized 26%. Over the longer term, Leonard and his team have multiplied their 2006 IPO price of $17 **x159 over 17 years** which, when added to dividends, has resulted in a 36% annualized return.

CSU's long perceived problem is that as it gets bigger, it will need many more small acquisitions each year to keep pace with growth. While the slowdown is inevitable, they have an internal list of over **40,000 potential acquisitions** (and they think it only covers 30% of their total market). The alternative is to **buy larger companies**, for which they will have to pay higher prices as there are more interested parties. This is something they are already starting to do in combination with the IPO of some subsidiaries (Topicus, Lumine).

Although it is unlikely that the next 20 years will be like the previous 20, we think it will continue to be a good investment. The advantage of investing in exceptional people is that the surprises are usually positive.

Save, multiply, wait and enjoy.

Jaime Carrasco Houston
CEO/CIO