Constantia Investment Partners

Interim Letter
2023

Dear Partners

For the financial year ended 30 June 2023, the AIM Global High Conviction Fund delivered a net return of +23.7%, which brings our net return since strategy inception (August 2019) to 12.0% per year.

Performance to 30 June 2023

	GHCF	Benchmark
Financial Year 2023	+23.7%	+22.4%
2023 (Calendar YTD)	+15.8%	+17.3%
2022	-15.6%	-12.2%
2021	+31.1%	+29.3%
2020	+14.2%	+5.6%
2019 (Strategy Inception: 31 Aug. 2019)	+5.3%	+6.3%
Cumulative Since Strategy Inception	+54.2%	+49.3%
Annualised Since Strategy Inception	+12.0%	+11.0%

Total returns shown for the AIM Global High Conviction Fund have been calculated using exit prices after taking into account all the product's ongoing fees and assuming reinvestment of distributions. No allowance has been made for entry fees or taxation. Past performance is not indicative of future performance. The benchmark is a representative index of global equities listed in developed markets and is denominated in AUD, with dividends (net of withholding taxes) reinvested. Refer to our PDS for more detail.

Fund managers are generally credited for investment performance. We believe there are two other contributors often overlooked.

Firstly: Management Teams and Employees

We believe a company's share price ultimately reflects the long-term success of the underlying business. The people who drive and deliver that success, are management teams and employees. Their efforts to successfully meet (and often exceed) the needs and expectations of their customers eventually show up in the numbers. Our understanding of this fact – combined with our ability to identify exceptional management teams – forms part of our edge.

Secondly: Investors

Through their own actions, investors significantly affect their returns. In his 2011 book *The Big Secret for the Small Investor*, famed US investor Joel Greenblatt recounts a Morningstar study of US equity fund returns from 2000 to 2009.

The highest-performing US equity fund during that period delivered over 18% annually, significantly outpacing the S&P 500, which fell roughly 1% per year. Despite this, the average investor in this fund *lost* about 11% per year.

The reason?

'*Pretty much after every period the fund did well, investors piled in. After every period the fund did poorly, investors ran for the exits. The average investor managed to lose money in the best-performing fund purely by buying and selling at just the wrong times*' explains Greenblatt.

Dalbar, a US investment research firm, tracks this disparity between investors' actual returns and the stated net-of-fees track record of the funds they invest in. Their work confirms Greenblatt's observations. Over the past 30 years they found an average equity investor's underperformance was due to behavioural factors, either trying to time the market (i.e., avoiding drawdowns) or chasing performance (i.e., succumbing to the fear of missing out).

We are **exceptionally** fortunate to have investors who take a long-term view when it comes to growing and compounding wealth. Over the past year, we did not receive a single concerned email or phone call during what was a tumultuous period in markets. We did however receive many words of encouragement and support from our approximately 200 investors.

Operating in an environment of calm and trust during periods of market volatility is about as good as it gets in our industry, and we extend our gratitude for your confidence in allowing us to do so.

Markets Have Rallied. Now What?

This brings us to the question we are asked most: '*is now a good time to invest in the stock market?*' Usually, this is where a fund manager would comment on macro-economic conditions, inveigh on central bank action (or lack thereof), and attempt to provide context to what is happening in the world – all to explain their 'positioning'.

Over the past year, we have observed a spirit of competitive 'one-downmanship' (for lack of a better term) that took hold among many market commentators, with each vying to be more bearish than the next.

In contrast, we choose to have no view on 'markets' as a whole, or where they might head next. As we wrote in our 2022 Annual Letter:

> *Whether 2023 sees the world tip into recession (or narrowly avoid doing so) is less relevant to our way of investing. In our opinion, it is far better to focus on the factors creating fundamental value over time, than trying to time markets.*

This does not mean we ignore risks that could negatively impact stock markets, but we do not seek to address these risks through market timing. Instead, our approach is to own exceptional businesses fundamentally resilient to the storms of the world, and hence the Fund will always be 90% to 100% invested in global equities. Annexure C is an important one-page summary of our investment philosophy, which we plan to attach to all future letters.

Returning to the question – *is now a good time to invest in the stock market?* – we can confidently say we have no idea. We can only comment on that which we control, which is the quality of the businesses we own, and the price we pay for them.

We believe the more sensible question to ask would be '*is now a good time to invest in exceptional businesses?*' To that question, we believe the answer is 'yes'. The long-term wealth creation exceptional businesses are capable of delivering does not happen overnight – it takes time.

Internally, we target returns of 8% - 12% per year through the cycle. Though any estimates and forecasts we make are in no way guaranteed, our 5-year forward-looking returns are towards the upper end of that range. To describe why we believe our businesses can deliver on this goal, we are meaningfully expanding our disclosure to you.

Expanded Disclosure

The goal of our interim and annual letters is to provide information to help you make informed investment decisions.

In writing these, we include what we would want to know if our roles were reversed. As of June 30 2023, we are voluntarily disclosing all Fund holdings to investors. We plan to do so in all interim and annual letters going forward.

We will also briefly discuss the underlying business performance of each of our holdings over the most recent 6-month period for which their results are available.

These will not be the usual ‘stock stories’ found in fund manager communications. We will provide a warts-and-all perspective, since we know business performance in the real world is not a smooth, uninterrupted line that goes up and to the right.

We realise not all investors may want this level of detail, which is why we have included it in Annexure A towards the back of the Letter. While we strongly recommend reading the annexure, the letter is structured so investors who do not wish to do so will still be informed of the key drivers of our performance for FY23 by reading through Part One.

The Structure of our Interim Letter

This Letter is divided into several parts. The parts are independent of each other and can be read in any order, though we have presented it in the way we feel is most logical. To help with navigating this document, those reading it digitally can simply click on the underlined text below to jump directly to the relevant part of the letter.

- In Part One, we discuss the drivers of performance for the financial year.
- In Part Two, we contemplate how one might pursue the surprising goal of finding businesses that are sure to deliver abysmal performance to investors.
- There are three **annexures** at the back of the letter:
    - Annexure A contains a snapshot of all holdings as on 30 June 2023, as well as commentaries on the performance of all the businesses for the most recent six-month period for which results are available.
    - Annexure B contains our usual quality scorecard (which includes historical metrics to allow for comparison over time), internal sector allocation and geographic revenue exposure breakdowns.
    - Annexure C is a one-page summary of our investment philosophy, which we intend to attach to all letters in future.

In Closing

We live in, and invest through, uncertain times. (The wise among us might ask ‘when are the times ever certain?’).

Our response to navigating these times is – we believe – rational: own exceptional business, run by exceptional people, and purchase them at the right price. Then be patient and let the wonders of compounding take hold.

As always, we are grateful for your vote of confidence in Constantia and thank you for your ongoing support. Please get in touch if you have any questions.

Kind regards,

Etienne, Les, Dan & Andrew

Part One: FY23 in Review

by Etienne Vlok

The Fund rallied by +23.7% (net of fees) for the financial year ended in June 2023. We estimate that a weaker Australian dollar contributed roughly +3.6% to this absolute return.

In June 2022, the general tone in markets was incredibly bleak. The Russian invasion of Ukraine and related inflationary impact on energy costs was but a few months old, and the outlook for the global economy was for things to get worse before they got better.

This was reflected in prices at the time. As we wrote to you in our 2022 Interim Letter, valuations were looking attractive in May and June 2022. While markets only bottomed around October 2022 – when US inflation peaked and then started trending downwards – the period from July to September proved to be a good time to allocate capital, with the benefit of hindsight.

We do not point this out because we think we are any good at market timing. Instead, we think there are two points worth emphasising:

- To paraphrase a lesson from the 2008 crash: markets don't bottom when the light at the end of the tunnel is obvious; markets bottom when all looks bleak, but just a subtle shade less bleak than the day before.
- Market timing or trying to perfectly buy the bottom rarely works. When one sees value, it makes rational sense to allocate to high quality businesses, and then have the patience to wait.

Contributors & Detractors

We discuss the fundamentals of contributors and detractors in more detail in Annexure A.

Contributors

The top five contributors to our performance for FY 23 are shown in the table below.

	Top 5 Contributors	
Business	**Total Return (AUD)**	**Contribution**
Constellation Software Inc.	48.0%	3.34%
Games Workshop Group PLC	86.1%	2.82%
LVMH Moet Hennessy Louis Vuitton	62.3%	2.81%
HEICO Corp.	38.0%	2.68%
Berkshire Hathaway Inc.	29.0%	2.15%

- **Constellation Software** closed a record number of transactions in the past 12 months, with several notable deals being so-called 'carve-outs' from larger, publicly listed entities that sought to dispose of non-core divisions. Constellation also spun off a media-focused subsidiary division – Lumine – in March. In short, the step-up in acquisition pace at valuations we still consider very reasonable (in many cases, around 1.2x sales, equating to around 9x earnings, by our estimates) has seen sales and cash flow continue to compound.
- **Games Workshop** shrugged off market concerns about the discretionary nature of its products in an inflationary environment as Warhammer fans continued to spend on their hobby. Combined with a peak in capital investment that occurred around the time of our initial purchase (February 2022), the company generated large amounts of excess cash, the majority of which was returned to shareholders in the form of special dividends.
- **LVMH** has seen demand for luxury goods remain resilient. Clearly, the high-end consumer has been less affected by the cost-of-living squeeze caused by inflationary pressures. In addition, LVMH has seen its operating margins move structurally higher from pre-pandemic levels, driven by a combination of internal supply chain efficiencies, pricing power, and a mix shift towards higher margin products. With management

guiding that margins should remain at these levels, the business is significantly more profitable than a few years ago. The excess cash generated has allowed LVMH to work down the debt taken on to finance the Tiffany acquisition much more rapidly than anticipated, meaning that the controlling Arnault family has capacity to look for more value creating acquisitions.

- **HEICO** experienced strong demand for its FAA-approved after-market airplane parts, in large part because of strong end-demand for commercial air-travel post pandemic. A lack of experienced labour and new airframes have in combination seen HEICO act as a key partner to airlines looking to keep their existing fleet in the sky for longer. In addition, HEICO made two extremely complementary acquisitions at very attractive valuations over the past year. We anticipate these newly acquired businesses (Exxelia and Wencor) will position HEICO to expand in Europe and win more market share domestically, both of which bode well for the long term.
- **Berkshire Hathaway's** broad range of underlying businesses provided the firm with internal diversification, with many businesses benefitting from the inflationary period even as others saw their margins compress. Robust cash generation supported ongoing share repurchases and the acquisitions of Alleghany and Pilot Travel Centres.

Detractors

The top five detractors to our performance for FY 23 are shown in the table below.

Business	Top 5 Detractors Total Return (AUD)	Contribution
UnitedHealth Group Inc.	-2.0%	-0.11%
PayPal Holdings, Inc.	-1.3%	-0.05%
Northrop Grumman Corp.	-3.5%	-0.04%
Thermo Fisher Scientific Inc.	-0.6%	-0.04%
Estee Lauder Companies Inc.	-1.3%	-0.01%

Right off the bat, it is worth noting that there were not many names that detracted materially from our absolute return: their negative impact ranges from -0.11% to -0.01%. Rather, these names simply didn't keep up with markets.

- **UnitedHealth** experienced no fundamental slowdown in its business whatsoever: revenues and earnings per share grew at a healthy mid-teens rate. The main concern around UNH seemed to focus on the normalisation of patient behaviours that would lead to a period of above average medical claims after patients – particularly older ones – opted to delay elective surgical procedures during the height of the pandemic.
- **PayPal** has experienced a tough 18 months. eCommerce growth slowed materially over the course of 2022; unsurprisingly, this led to slowing sales at PayPal. Some of PayPal's non-consumer facing businesses (such as payment gateway Braintree) saw a pickup in growth driven by wider adoption by merchants, but this comes at a lower margin. In addition, the company has been looking for a new CEO since February after the current leader announced his intention to retire at the end of 2023. We believe that the lengthy search for a successor has weighed on investor sentiment.
- **Northrop Grumman** has been purchased gradually over the course of the first half of 2023. The marginally negative return is indicative that we have been buying our position while the company is out of favour.
- After several years of rapid growth over the course of the pandemic**, Thermo Fisher Scientific** saw revenue growth slow in FY23 as the last of the sales related to the COVID-19 response was worked down. At the same time, increased interest rates led to venture capital funding to many biotech firms drying up. Whilst having less exposure to early-stage biotech than other life sciences competitors, Thermo Fisher was not immune to the slowdown that ensued because of less funding for novel drug discovery in the short term.
- **Estee Lauder** was sold during the year. Our rationale for exiting the position is discussed in the section below.

Positions Purchased & Sold

The discussion of new purchases and positions sold is reserved for Constantia investors.

Change in Intrinsic Value

We adopt a business ownership mindset when it comes to investing, and therefore place significant emphasis on measuring the growth of the intrinsic value of our businesses over time. We believe this is the best way to assess whether they are fundamentally becoming more valuable.

However, the concept of intrinsic value is generally not widely understood among those who are not directly involved in the fund management industry.

Defining Intrinsic Value

At its most basic, intrinsic value refers to the value derived from the inherent characteristics of an object. In contrast, the opposite – extrinsic value – refers to value that is not derived from an item itself, but rather from external perception. A good example might be a painting by Van Gogh: the canvas, paint and wood are not *intrinsically* valuable, but the fame and skill of the artist means the portrait is worth much more than the sum of the parts.

In an investing context, intrinsic value refers to the estimate of value derived from the underlying fundamentals of a business. Generally, this is taken to mean the present dollar value of all the cash the business will return to its owners from now until the day it is wound up.

The measure of how much cash a business could return to its owners is called 'free cash flow', so called because it is literally the money the business is 'free' to distribute to owners (as dividends or through share buybacks).

Because we own shares in a business – and because management can materially alter our ownership by issuing or repurchasing shares – we believe the best way to measure the growth in intrinsic value for our businesses is by measuring the change in free cash flow per share from period to period.

Our Net Total Return Breakdown

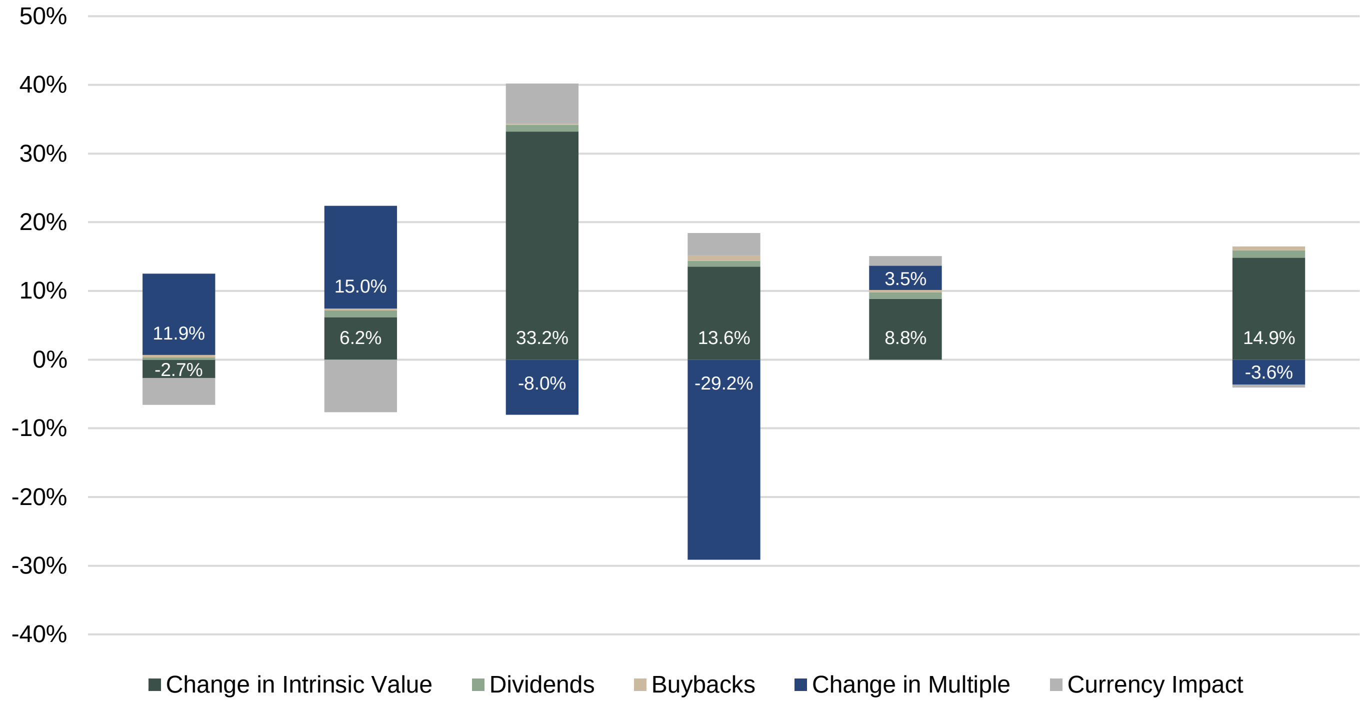
With that in mind, the chart on the following page breaks down our net-of-fees total return since strategy inception (August 2019) into the underlying three sources of return for investors:

- The change in intrinsic value, which we measure as the period-to-period change in free cash flow.
- The cash returned to investors, either in the form of dividends or through share repurchases.
- The change in the valuation multiple the market assigns to a business at the time of initial purchase relative to the time of measurement or eventual sale.

Because we invest globally but report results to you in Australian dollars, the impact of currency fluctuations is an additional driver of return.

Though we derive the change in intrinsic value from observable inputs, we should stress that – as with any calculation of intrinsic value – it is an imperfect estimate. However, we believe it is directionally correct and grounded in sound economics, and in the decidedly unscientific world of capital markets, we'd rather be roughly right than precisely wrong any day of the week.

2019	2020	2021	2022	2023 CYTD	Strategy Inception p.a.
+5.3%	**+14.2%**	**+31.1%**	**-15.6%**	**+15.8%**	**+12.0%**



Figures at the top show net total return for each period. 2019 and strategy inception are measured from 31 August 2019.

Unsurprisingly, the dark blue bar – representing the valuation multiple the market is willing to pay for a dollar of free cash flow – has been the most volatile component of our returns. This makes intuitive sense, as markets are prone to volatility over short periods. For example, the largest driver of our -15.6% return in 2022 was not a decline in free cash flow (which grew by +13.6%), but rather the market placing a lower multiple (-29.2%) on the cash generated by the business. (This phenomenon is known as multiple compression).

Conversely, the dark green bar – representing the change in intrinsic value as represented by the growth in free cash flow from period to period – has been less volatile. Dividends (light green) and buybacks (light brown) have been modest but consistent positive contributors.

The impact of currency has been volatile from year to year but tends to even out over time.

We think the rightmost column – breaking down our 12.0% per year net total return since strategy inception – is likely the most interesting feature of the chart, since it looks through a lot of the volatility from the pandemic period. As you can see, we estimate that our businesses have grown their intrinsic value by +14.9% per year since inception, whilst multiple compression has been a -3.6% per year headwind over the period. Dividends (+1.1%) and share buybacks (+0.5%) have been marginally positive, whilst the currency impact – despite being volatile in any given year – has only detracted -0.4% per year since inception.

Over the long term, we believe the return we deliver to you will roughly reflect the growth in intrinsic value of our underlying businesses. Indeed, it would be fair to say this belief is foundational to our entire investment philosophy.

As such, we plan to update this chart and present it to you in every interim and annual letter we write in future, enabling you to track the fundamental change in value of the businesses we own.

Part Two: Invert, Always Invert

by Andrew Strasser

Long-time readers of our letters know we are unashamed admirers of Charlie Munger. His many essays, articles and speeches are not only filled with advice on how to think rationally when it comes to investing, but also with wisdom that stretches far beyond the realm of markets.

In our opinion, one of Munger's most timeless pieces of advice is to invert the problem-solving process. Instead of working out what to do to reach a desired goal, inverting requires thinking of obstacles that would *stop* one from achieving said goal, and then working backwards to eliminate the causes of failure. All else being equal, one is left with the inputs to success.

In 1986, Munger was invited to give a commencement address at Harvard Business School. Such addresses are mostly dull affairs, filled with clichés about how the graduates might achieve happiness in life. Knowing this, Munger took a different route. Calling his speech *How To Guarantee A Life of Misery*, he delivered a succinct summary of the things to do to make 100% sure one fails in life. (Highlights include: be unreliable; refuse to learn from the experience of others; go down and stay down when you suffer misfortune in life.)

Why take this approach? Quoting Munger:

> *What Carson did was to approach the study of how to create X by turning the question backward, that is, by studying how to create non-X. The great algebraist, Jacobi, had exactly the same approach as Carson and was known for his constant repetition of one phrase: 'Invert, always invert.' It is in the nature of things, as Jacobi knew, that many hard problems are best solved only when they are addressed backward. For instance, when almost everyone else was trying to revise the electromagnetic laws of Maxwell to be consistent with the motion laws of Newton, Einstein discovered special relativity as he made a 180 degree turn and revised Newton's laws to fit Maxwell's.*

Reading the whole speech is well worth your time, if you are so inclined.

A Life of Investing Misery

We think there is a lot of wisdom to be gained in taking Munger seriously and inverting the question we are trying to solve – *how can we invest in a business and earn an attractive return over a long period of time*?

Below, we have identified a list of three steps that an investor should consider if they are seeking to '*earn abysmal long-term returns while pursuing short-term gains*': 1) invest in poor businesses; 2) partner with poor management teams; and 3) be your own worst enemy.

By understanding what not to do, we seek to highlight the path towards rational and intelligent investing. For the sake of clarity: what follows should not even remotely be considered investment advice!

1. Invest in Poor Businesses

If one were to seek poor returns, the following is a non-exhaustive list of characteristics to look for in a business:

Excessive Debt – Gear Today, Gone Tomorrow

> If your intention is to avoid businesses that increase in value every year, you may want to ensure that at some point they go out of business. The most common way businesses fail is by going bankrupt. Owning businesses with excessive amounts of debt – particularly in cyclical industries that have little in the way of differentiation or pricing power – is a great way to increase your chances of earning a poor return… or none at all.

Low Levels of Profitability

> In business, it is widely understood that you need to spend money to make money. Return on invested capital (ROIC) measures how much money you make (the return) relative to the money spent to make it (the invested capital). In many cases, spending more to achieve growth does not necessarily mean value has been created. Frequently, this manifests in a low or negative ROIC.

To ensure a poor outcome, one should focus on owning businesses that consistently generate losses and burn through cash in the pursuit of growth. If you cannot find a cash-incinerator of this sort, you might want to settle for a business merely earning a persistently low ROIC.

By owning either of these types of business, you are well on your way to poor investment returns.

A Product/Service That Won't Endure

Any industry where the market opportunity and future profits are attractive, will likely see new market entrants with competing products.

Businesses whose offerings are easy to copy or whose customers are easily lured away, will find it difficult to maintain their level of profitability over a long period of time and make excellent candidates for investments that deliver poor returns.

The same can be said of a business whose product or service could be easily disrupted by new technologies. Investing in a business whose industry is undergoing a technological shift is also risky, and is fertile ground for opportunities that can destroy value.

A Love of Diluting Shareholders

Growth in cash flow is an excellent indicator of an increase in business value, but only if this is achieved on a per share basis.

If a company's cash flows grow at 12% per year for a decade, but the number of shares in issue doubles over the same period, the increase in business value per share is going to be closer to 4.5% per year. It is like swimming against the current: possible to make headway, but the job is significantly harder.

The most obvious way the share count increases is when a company conducts an equity raise. Less obvious, but in our opinion far more damaging, is egregious issuance of equity as part of stock-based compensation plans.

To ensure low rates of return, look for businesses that perpetually dilute shareholders.

2. Partner with Poor Management Teams

The actions of a business do not occur in a vacuum. A business is a collection of people making decisions on a daily basis. If one *really* wants to turbo-charge the potential for bad investment returns, look no further than a business run by a poor management team.

Below are some things to keep an eye out for when assessing management:

An Attitude of 'If It Moves, Buy It'

The creation of value for shareholders is dependent on management spending money on growth opportunities to generate sufficiently high profits. In short, they need to know how to allocate capital. These additional profits can then be reinvested again and again, providing the compounding effect.

By comparison, paying top dollar for 'strategic' acquisitions with deep wells of 'synergies' – which, research tells us, rarely materialise – is a rich vein to mine for capital misallocation.

Management teams with a track record of poor capital allocation are of great help to the aspiring underperforming investor. Why light your own money on fire when you can have management do it on your behalf?

Poor Management Incentives

Another of Charlie Munger's famous quips: '*show me the incentive and I will show you the outcome*.'

A CEO whose remuneration incentive does not align with shareholder value creation is far more likely to make decisions to maximise their own compensation.

Management incentives and pay are buried in proxy statements, not earnings releases. Completely ignoring the annual proxy – and thereby any chance to determine whether management is incentivised to act for shareholders – is a great way to increase the probability of poor returns.

Similarly, management teams who have very little skin in the game (i.e., equity ownership), or instantly sell any equity awarded to them may act like they have nothing to lose. (This is because – frequently – they don't). These management teams do not think or behave like true long-term owners of a business and are helpful in the journey of wealth minimisation.

Consider a CEO who is paid based on achieving a 3-year target for earnings per share. To reach this goal, the CEO might cut spending on research and development (R&D), take on more debt, and use the money to buy back shares. This leads to higher short-term profits and a reduction in shares outstanding. The combination is an increase in earnings per share. While initially looking like a win for shareholders, cutting R&D can let competitors take the lead. Additionally, the CEO has increased the company's financial risk by taking on more debt. Whilst the CEO has earned a huge payday, the company is left in a much more precarious position.

A History of Disrespecting Minority Shareholders

Management that does not have a strong sense of trusteeship towards minority shareholders may act in a manner that disadvantages investors over the long term. This point covers many management sins, but below we provide a few compelling examples of behaviour that separates the value-destroyers from those who know how to compound wealth:

- Lack of or frequent changing of disclosure to investors, impairing their ability to make decisions.
- Supporting a buyout at a depressed valuation for personal gain, causing minority owners to miss out on future value creation.
- Egregious issuing of stock to staff or to pay for growth via equity-financed acquisitions.

A business run by a management team that thinks little of minority shareholder rights tends to make corporate decisions which benefit themselves. To them, stewardship is something that happens to other people. For the connoisseur of poor investment returns, these people are invaluable companions on the journey.

3. <u>Be Your Own Worst Enemy</u>

Another powerful source of poor returns are investors themselves.

Study after study proves investors do their own returns tremendous harm in various ways that are ingrained in the human psyche. The good news for an investor looking to earn a poor return, is they do not have to go to all that much effort to damage their own fortunes (literally).

Two timeless ways in which investors can impair their own returns include:

Overpaying

What turns any business into a terrible investment is the price at which it is purchased. Buying a stock without any idea of the business fundamentals, is a shortcut to underperformance.

Paying up for a 'story stock' that aligns with the current flavour-of-the-month, or a highly promotional management team talking up the stock to levels divorced from reality, will almost certainly help investors achieve their goal of terrible performance.

Panic-Selling & Interrupting the Compounding Process

Investing in the real world is not a smooth ride. Returns can bounce around from year-to-year, and negative returning years should be expected. Investors who sell out when markets are volatile and every fibre in their body is telling them to rush to safety – always with the goal of buying back into markets when things are a bit more settled – are mathematically proven to destroy returns. The reason is simple: doing so interrupts the compounding process.

The biggest 'up' days in markets tend to follow the biggest 'down' days. If an investor has experienced the 'down' days, but then sells out, they remove the ability to participate in subsequent 'up' days. In this manner, a temporary decline in value can become permanent.

To minimise returns, investors should always be quick to lock in a short-term gain or sell a business they know little about at the first sign of negative price moves.

A Life of Investing Happiness

To state the obvious, all the above points have been written in a deliberately tongue-in-cheek manner. The absurdity of seeking to '*earn absolutely abysmal returns over the long-term*' highlights many of the factors or behaviours we seek to avoid in pursuing our goal of generating attractive returns. By doing so, we are left with the positive drivers of long-term value creation:

'Exceptional businesses, run by exceptional people, at the right price.'

If investors narrow their focus to a few key drivers, they simplify what at first appeared to be a difficult problem of finding great businesses to invest in, while avoiding many of the landmines leading to poor investment outcomes.

In our mind, this leads to a higher probability of compounding wealth over the long term: in other words, a life of investing happiness.

We concede this is not the *only* way to make money investing in public equities. However, we think it represents the most straightforward and low-risk way to grow wealth over the long term, allowing investors to sleep easy at night whilst the businesses they own do the hard work for them.

ANNEXURE A: PORTFOLIO BUSINESSES

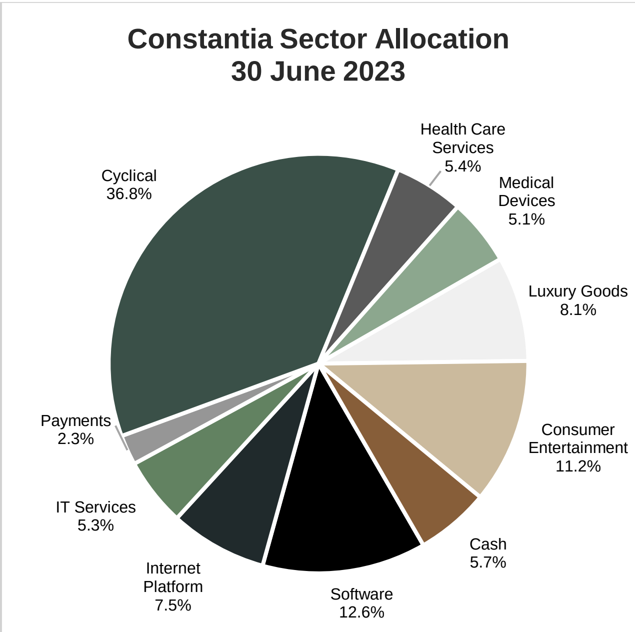
This section of our letter is reserved for Constantia investors.

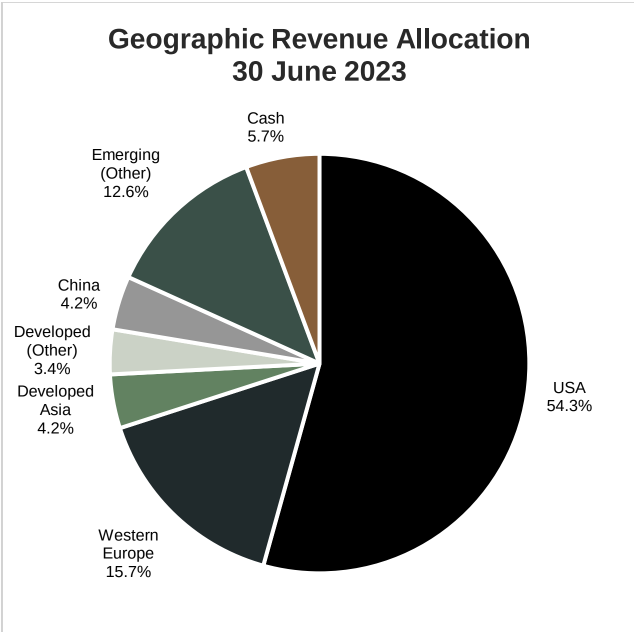
ANNEXURE B: FUND METRICS

Quality Scorecard

Portfolio Characteristic	Dec. 2019	Dec. 2020	Dec. 2021	Dec. 2022	June 2023
Profitability					
Gross Margin	55.7%	49.8%	52.3%	48.1%	42.8%
Operating Margin	23.5%	20.1%	24.3%	22.8%	20.8%
Free Cash Flow Margin	18.9%	17.0%	17.6%	16.8%	15.0%
Returns on Capital					
Return on Assets (ROA)	13.0%	11.9%	13.7%	13.9%	13.2%
Return on Equity (ROE)	28.3%	24.9%	30.4%	29.8%	27.5%
Return on Invested Capital (ROIC)	24.0%	16.5%	20.7%	19.5%	22.1%
Leverage					
Debt/Equity	87.2%	68.6%	78.3%	57.9%	68.7%
Net Debt/Equity	19.3%	22.1%	27.3%	8.6%	32.7%
Valuation					
Free Cash Flow Yield	2.8%	3.2%	2.8%	3.8%	3.6%
12m Forward Free Cash Flow Yield	3.3%	3.6%	3.2%	4.4%	4.0%
24m Forward Free Cash Flow Yield	3.8%	4.0%	3.6%	5.0%	4.4%
Holdings					
Number of positions	19	21	21	24	21
Active Share	86.5%	87.8%	89.0%	89.7%	88.7%

Internal Sector & Geographic Revenue Allocation





Source: FactSet, Constantia analysis.

ANNEXURE C: OUR INVESTMENT PHILOSOPHY

We are ‘business-first’ rather than ‘security-first’ investors, and see ourselves as part owners of the businesses we invest in. Because we subscribe to a business ownership mindset, the quality of the businesses we own matter a great deal to us.

Our investment philosophy can succinctly be summarised as follows:

‘Exceptional businesses, run by exceptional people, at the right price.’

We define the three key terms as follows:

<u>Exceptional Businesses:</u>

- offer a product or service that is hard to disrupt;
- have strong competitive advantages;
- are highly and sustainably profitable;
- convert the majority of their accounting earnings into cash;
- generate more cash than they need to meet the day-to-day needs of operations;
- have a long runway of opportunities to reinvest the excess cash generated;
- have low debt levels to mitigate the risk of failure.

<u>Exceptional People:</u>

- think and behave like owners;
- are appropriately aligned with minority shareholders through share ownership and fair incentives;
- display a degree of trusteeship or moral responsibility to their shareholders;
- have a demonstrable history of value-creating capital allocation.

We look to buy businesses that meet these criteria at prices where we believe we can meet – or exceed – our long-term return targets of 8%- 12% through a cycle.

We do not seek to generate returns by constantly having to trade in and out of businesses. Instead, we believe our long-term return will reflect the fundamentals of the businesses we own. As a result, we tend to own businesses for long periods of time – generally, between three and five years.

We manage a concentrated portfolio and own between 15 and 25 businesses at any given point.

We are bottom-up, fundamental investors. While we are cognisant of macro-economic risks, we do not construct the Fund to take advantage of such events.

We are an equity fund and intend to be between 90% and 100% invested in this asset class. We operate under the belief that if you entrust us with your capital, you want it managed in line with the process and philosophy we follow; you do not expect us to make an asset allocation decision.

We believe in time in the market, rather than timing the market.

We do not engage in shorting, nor do we use leverage to enhance our returns.

Our investable universe is global, and we are agnostic when it comes to market capitalisation size.