DKAM DONVILLE | KENT asset management inc.
ROE REPORTER
VOLUME LXVI JANUARY 2024 INVESTMENT ISSUES • STRATEGIES • INSIGHTS FROM DONVILLE KENT

Y-A-R-A-K

The Capital Ideas Fund finished 2023 with our best ever monthly return coming in November followed by a strong December return. 2024 has also started strong and we will explain why we believe this strength and momentum will continue.

We came across the term 'Yarak' while reading *Let My People Go Surfing: The Education of a Reluctant Businessman*. The book focuses on the creation, evolution, and guiding principles of Patagonia. Founder Yvon Chouinard was a well-known rock climber and created the business due to a lack of quality products available to service his passion. The book is well written and provides a unique outlook on how to operate a business and we would recommend you add it to your reading list. A less well-known passion of Yvon's was falconry, the ancient practice of training birds of prey. When trying to train a bird of prey, if they have recently eaten you can't get them to do anything. The opposite is also true. If they are too deprived and weak then they lack the energy and fire necessary to be a killer. The term Yarak refers to "A super alert state where the bird is hungry, but not weak, and ready to hunt."

The state of mind we can all relate to is when times are good and things come easy, there is an urge to get comfortable and relax. You lose your killer instinct. Buffett has said "A fat wallet is the enemy of superior investment results." For this reason, Patagonia tries to keep their business in a state of Yarak every single day.

The last couple years have seen a pandemic, massive supply chain issues, the fastest increase in interest rates, and a lot of stock market pain. If a business was carelessly and continuously relying on an extremely low cost of capital, they either had to adapt or die. If a business was carrying unnecessary expenses, those had to be cut. If the focus was on growth at the expense of profits, that mindset had to change. Companies rationalized, learned to do more with less, and became hyper-alert to their bottom line.

No one felt this harder than smaller companies. The amount of stress applied to these businesses and their stock prices has left the survivors in a super alert state. Many of these businesses are now operating in a much more optimal state. This matters from an investment standpoint because stress either leads to adaptation, growth and strength, or deterioration and fragility.

Our investment thesis for 2024 is profit margin improvement, earnings growth, and multiple expansion. You have margin improvement because of the renewed focus on profitability. Earnings growth because the strong have survived and thrived. The case for multiple expansion because multiples are at historic lows, and now interest rates have peaked, providing the catalyst for renewed momentum.

Company Fundamentals

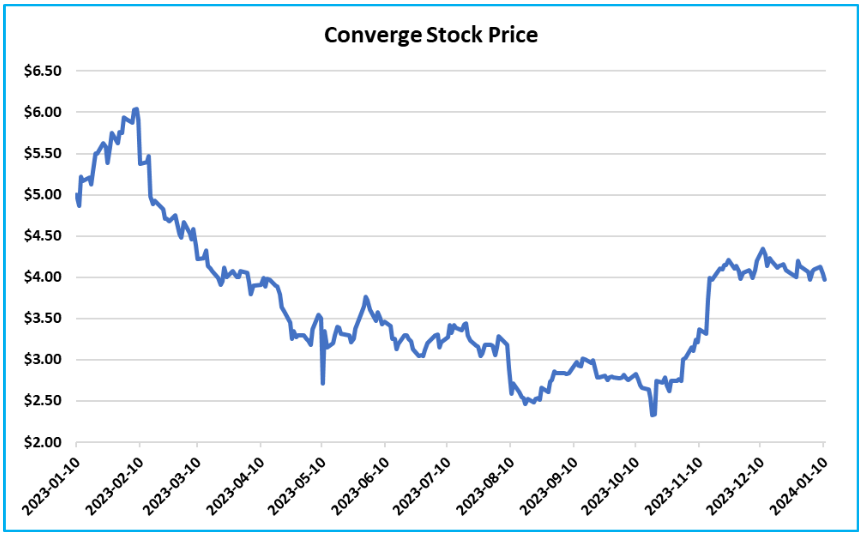
If we were to ask, when is the best time to invest in small and mid cap growth stocks, the answer would be when you have depressed valuations (cheap), improving fundamentals (business strength), and some type of catalyst (like peaking interest rates and large amounts of cash on the sidelines). For these reasons we foresee the recent momentum in our investment returns not only continuing, but accelerating. Our current investments have the most attractive balance of growth + profitability + valuation we have witnessed.

DKAM Investment Fundamentals

Company	Ticker	Market Cap	2024 Revenue Growth	2024 Earnings Growth	2024 P/E
Converge	CTS	$857m	12%	24%	4.6
Propel	PRL	$440m	30%	61%	7.0
Decisive Dividend	DE	$157m	22%	29%	7.5
GoEasy	GSY	$2,615m	22%	24%	8.1
SSC Security	SECU	$50m	17%	69%	8.6
RediShred	KUT	$58m	18%	19%	8.8
Nuvei	NVEI	$3,470m	21%	44%	10.0
Payfare	PAY	$315m	28%	76%	11.7
VitalHub	VHI	$177m	24%	28%	12.0
Constellation	CSU	$71,758m	24%	27%	23.1
Average			22%	40%	10.1

Figure 1 - DKAM Investment Fundamentals[1]

Converge Technology (CTS)

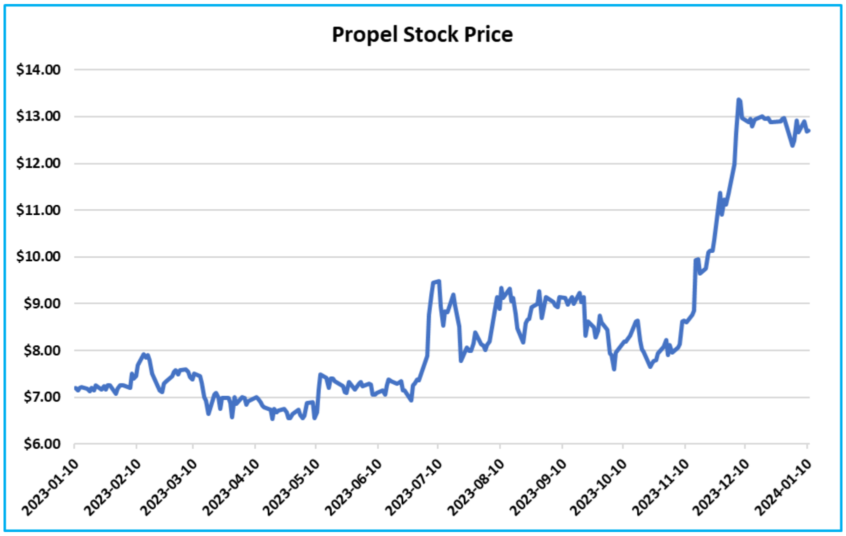


Key Metrics[1]

- Revenue Growth 12%
- Earnings Growth 24%
- Price to Earnings 4.6x

Converge benefits from growth in technology infrastructure investments, specifically AI, which supports steady organic growth. There is currently a bottleneck in compute power and massive increases in technology infrastructure budgets. There have been some generalities made to put this in perspective. As an example, some tech infrastructure budgets may have been $10m in 2022, increased to $100m in 2024 with budgets jumping 10x in 2024. Converge benefits by offering the products and services needed for businesses to implement these investments. Converge management recently noted that their Nvidia gear sales had topped $120m for the first 9 months in 2023, up from $12m in the year prior. Converge is now mainly focused on organic growth and cashflow. Their margins continue to improve, which supports a large stock buyback, and reinforces how cheap the stock is.

Propel Holdings (PRL)

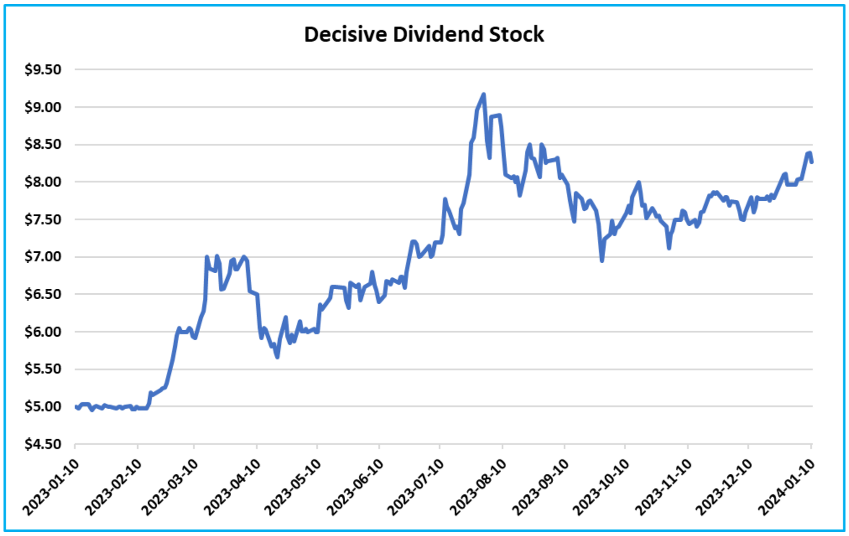


Key Metrics[1]

- Revenue Growth 30%
- Earnings Growth 61%
- Price to Earnings 7.0x

Propel continues to prove their business model and the results since coming public have been impressive. They recently expanded into Canada plus signed important partnerships in the States.

Decisive Dividend (DE)



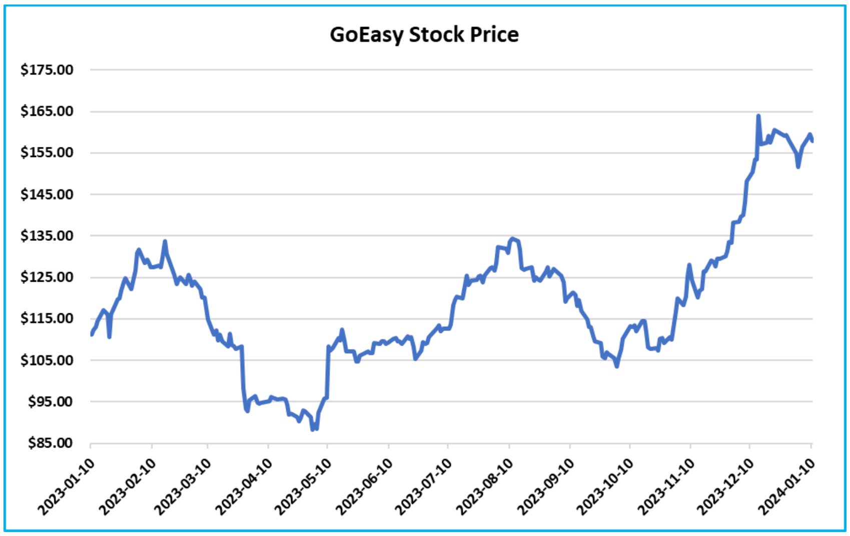
Key Metrics[1]

- Revenue Growth 22%

- Earnings Growth 29%
- Price to Earnings 7.5x

Decisive is run by a growth oriented but conservative management team. They have been doing a great job acquiring & integrating legacy minded industrial & manufacturing businesses. Organic growth after acquiring a business has been impressive. They have grown revenues at 30% on average and margins continue to improve. We expect more accretive acquisitions in 2024.

GoEasy (GSY)

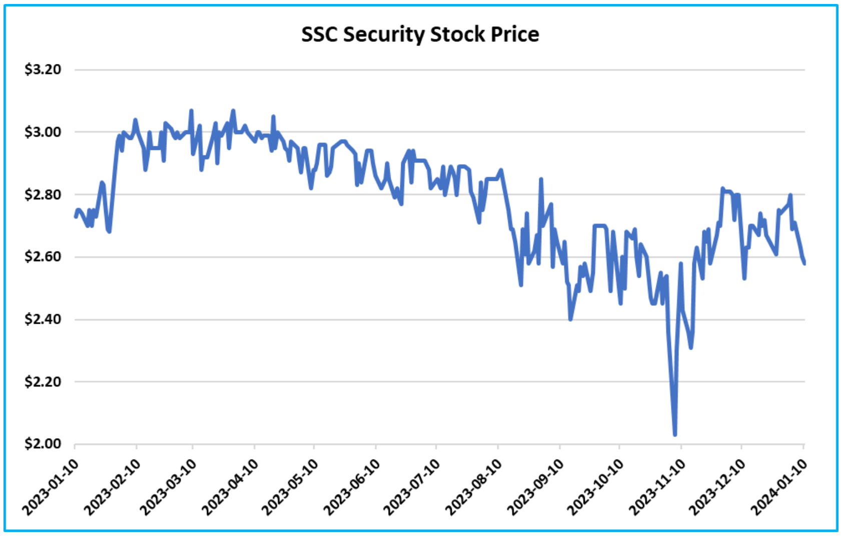


Key Metrics[1]

- Revenue Growth 22%
- Earnings Growth 24%
- Price to Earnings 8.1x

GoEasy continues to be one of the most consistent compounders we can find. They continue to rollout new product lines to support growth as well as increasing their dividend while buying back stock. Their operating leverage is hitting an inflection point and earnings have almost doubled just over the last few years.

SSC Security (SECU)

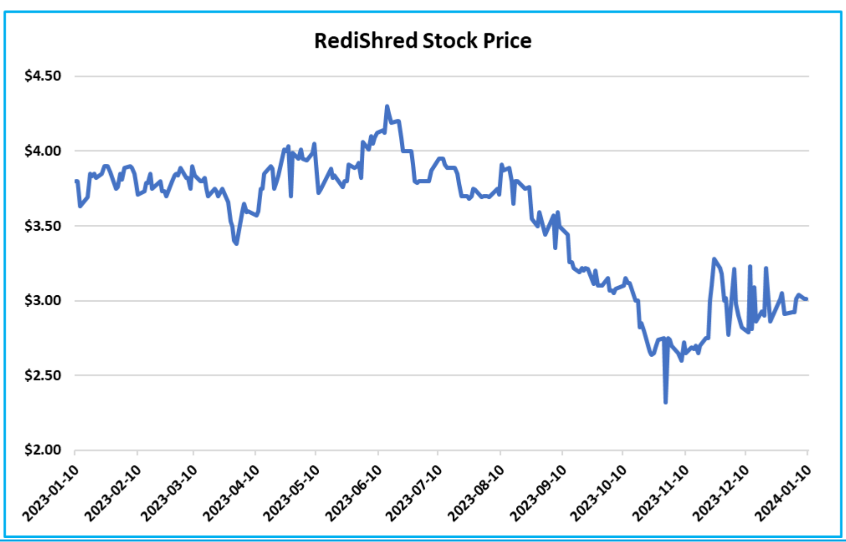


Key Metrics[1]

- Revenue Growth 17%
- Earnings Growth 69%
- Price to Earnings 8.6x

SSC Security offers in person security to clients like the City of Toronto, Suncor, and the Winnipeg Airport. They are growing their high margin cyber security business and the financials should show significant improvement in margins and cash in 2024. They have half their market cap in cash with no debt and we expect them to deploy the cash on dividends, buybacks, and tuck-in M&A.

RediShred (KUT)

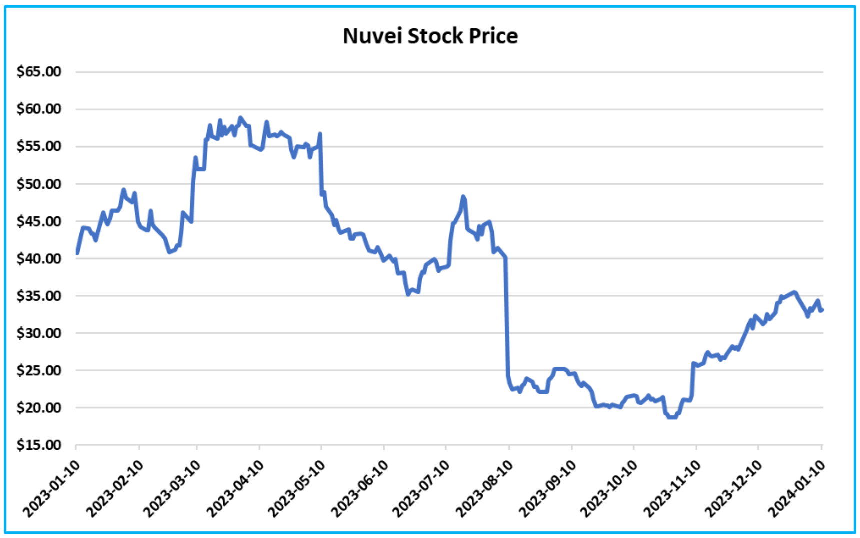


Key Metrics[1]

- Revenue Growth 18%
- Earnings Growth 19%
- Price to Earnings 8.8x

RediShred management continues to execute well on their growth and efficiency plan. Their segment of the paper industry is actually growing year over year and RediShred delivers impressive cash margins. They have a simple and realistic runway for growth and we expect the business to be worth a lot more in a few years than it is today.

Nuvei (NVEI)

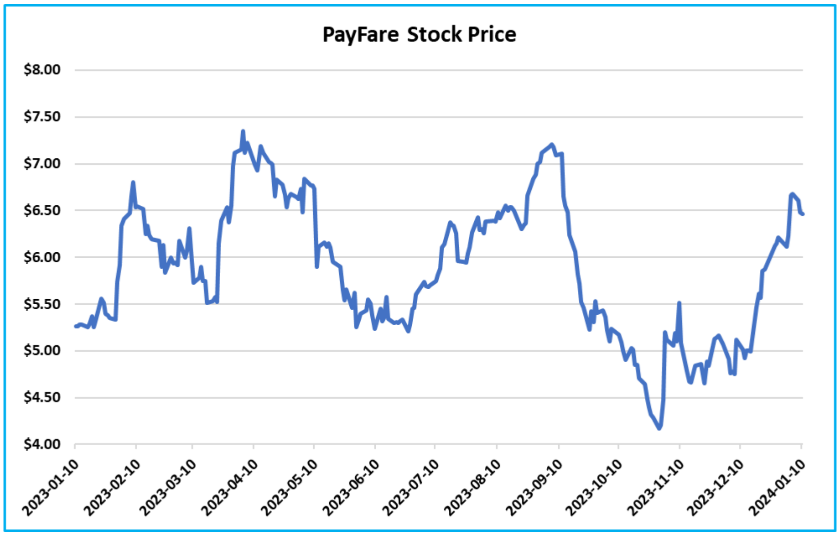


Key Metrics[1]

- Revenue Growth 21%
- Earnings Growth 44%
- Price to Earnings 10.0x

Nuvei provides a back-end payment solution that allows merchants around the world to seamlessly accept hundreds of payment methods. We believe margins will continue to improve as they integrate but also gain more wallet share from current customers. They recently announced impressive partnerships with Microsoft and Adobe. They are growing quickly and have one of the highest cash margins for North American public companies.

PayFare (PAY)

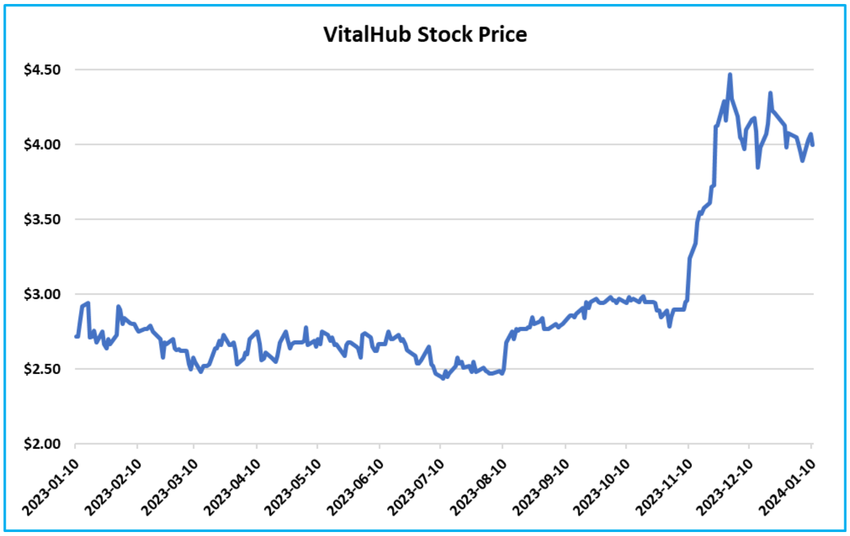


Key Metrics[1]

- Revenue Growth 28%
- Earnings Growth 76%
- Price to Earnings 11.7x

PayFare offers gig workers (Uber, DoorDash, Lyft) the ability to receive the wages they earn in real-time. These companies partner with PayFare because their technology allows them to more cheaply recruit and retain workers. Payfare has breached a certain scale where earnings are now expanding quickly. There is still a lot of room for growth as they gain more users from their existing clients but they have also recently announced new client wins as well as future expansion to W-2 workers.

VitalHub (VHI)

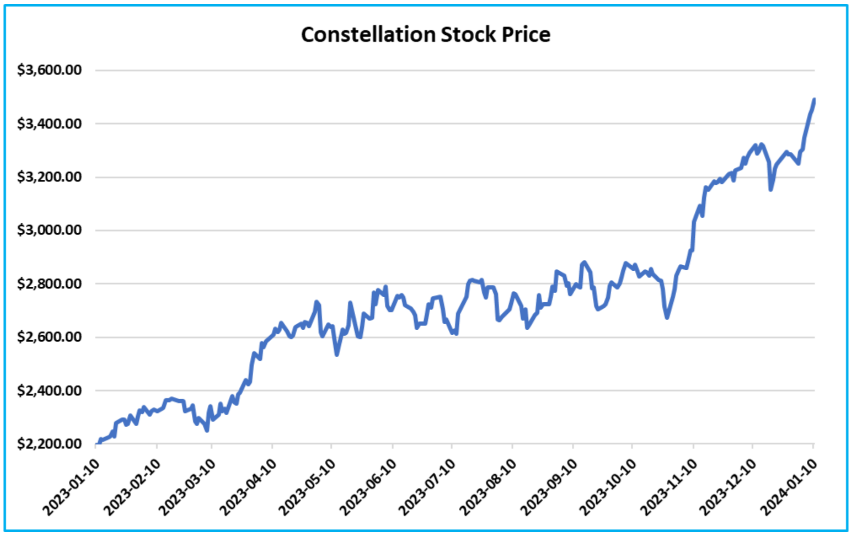


Key Metrics[1]

- Revenue Growth 24%
- Earnings Growth 28%
- Price to Earnings 12.0x

VitalHub has executed extremely well and built an industry leading healthcare SaaS platform. The stock market is starting the realize the importance, resiliency, and profitability of this business. They continue to report +20% organic growth which reinforces the point that their technology stacks up well against their competitors. VitalHub is sitting on a significant amount of cash earmarked for additional acquisitions. We believe we will look back at this moment as the early breakout of a for a long-term compounder.

Constellation Software (CSU)



Key Metrics[1]

- Revenue Growth 24%
- Earnings Growth 27%
- Price to Earnings 23x

Constellation not only continues to execute and compound value, but they have accelerated their pace acquisitions. 2024 should be another record year for M&A plus investors continue to get optionality of future spin-outs. We prefer to own Constellation & Lumine over Topicus.

Final Thoughts

Times of stress can either be seen as an opportunity to adapt and grow, or an excuse for weakness and failure. We believe we are in the early innings of a large rebound for the hungry.

We recently hosted an investor webinar which discussed our market outlook in more detail plus discussions on many companies. You can catch up by watching the replay from our webinar recording HERE. Additionally, feel free to flip through the presentation slides. We value your interest in our portfolio, and we're open to discussing it in more detail. If you wish to meet with us in person or schedule a call, please don't hesitate to reach out.

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All estimates, projections, and calculations have been generated by DKAM. This does not constitute advice for personal investments but rather a breakdown of how Donville Kent approaches stock analysis.

1 – DKAM estimates for Revenue growth, earnings growth & 2024 P/E. Calculated January 4, 2024.