FORAGER

CHIEF INVESTMENT OFFICER LETTER

QUARTERLY LETTER DECEMBER 2021

www.foragerfunds.com

FORAGER FUNDS PERFORMANCE SUMMARY (as at 31 December 2021. Net of all fees and expenses)

	1 month return	3 month return	6 month return	1 year return	3 year return (p.a.)	5 year return (p.a.)	10 year return (p.a.)	Since inception* (p.a.)
Forager Australian Shares Fund	2.81%	3.02%	11.47%	31.31%	18.15%	10.68%	16.17%	12.55%
Forager International Shares Fund	-4.61%	-5.13%	-12.43%	14.92%	25.22%	14.22%	-	16.13%

*8 February 2013 for FISF and 30 October 2009 for FASF

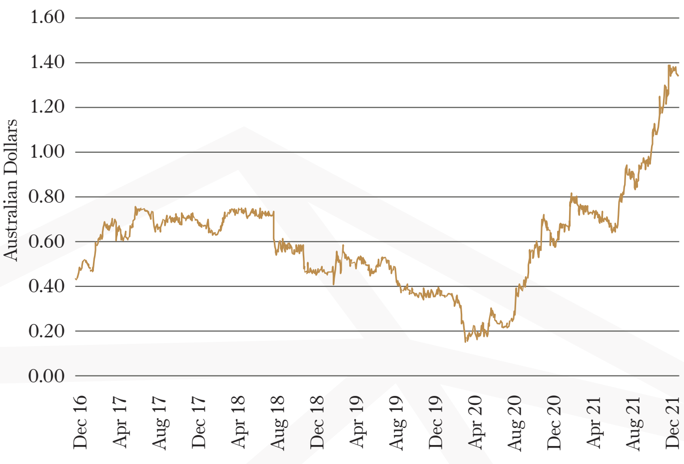
Past performance is not indicative of future performance and the value of your investments can rise or fall. Performance in FASF is calculated using Net Asset Value (NAV), not the market price.

LESSONS FROM THE LAST WAR WON'T WIN THE NEXT ONE

Forager's first investment in Kiwi media company NZME was made in June 2016. The research piece I wrote for the investment was concise and simple: I added up the worth of its radio and newspaper assets to reach a per-share value of $1.25. Given a $0.77 share price at the time, that looked like an attractive investment.

A brief glance at today's share price would show that we got it mostly right.

NZME 5-YEAR SHARE PRICE



Source: Bloomberg

NZME last traded at $1.34 a share and has paid a touch over $0.20 in dividends over the ensuing five years, making for an annualised return of roughly 14% per annum. Far from the greatest investment ever, but roughly in line with expectations at the time. However, as anyone invested in our Forager Australian Shares Fund over the period will know, it hasn't been anywhere near that straightforward. The share-price path from $0.77 to $1.34 went via $0.20. It traded well below that first purchase price for most of the time the Fund owned it.

NZME wasn't on its own. The period 2016-2019 was a horrible bear market in "value" stocks (for simplicity, let's define them as businesses that are seen as having lower-than-average future prospects). What started as a proportionate response to overly optimistic stock prices and concerns about industry obsolescence soon became indiscriminate and self-fulfilling extreme selling. Super funds withdrew mandates, value-based fund managers were forced to close and those that remained were asking serious questions of themselves. Including us.

I learned a great deal through that period and my CIO letters over the past few years contain plenty of investing lessons. The thing about 2021, though, is that most of our Australian Fund's outperformance came from the businesses that were doing all of the teaching. The lessons are still applicable—it's just that 2021 was a time to ignore them.

Lesson number one, for example, was that it is hard to pay a low enough price for a business in decline—but that doesn't mean it's impossible.

NZME announced a NZ$30 million buyback of its own shares with excess cash, which is just shy of the company's entire market capitalisation at the share price low in March 2020. Tyre distributor National Tyre's profit in 2021 was 70% of the whole company valuation less than two years ago. That's a price-earnings ratio of 1.5 times.

It's an important lesson (and perhaps we *should* wait for these businesses to trade at three times earnings rather than six), but you can make an awful lot of money where the future is far from exciting if you pay an absurdly low price.

Lesson number two: portfolio liquidity and diversity are important.

I don't ever want to be back in a position where it is nigh on impossible to sell half the stocks in the portfolio. Our ability to capitalise on the turmoil of March 2020 was constrained by the lack of liquidity at the time (in the Forager Australian Shares Fund, that is). But stocks are often illiquid because no-one else is interested in them. In 2020, it wasn't uncommon for NZME shares to not trade at all for days on end.

That can be a trap, but it's also where the best opportunities are likely to be found. Now that the company is paying dividends and buying back shares, hundreds of thousands of dollars worth trade every day. Once again, it's important to be wary. But swearing off illiquidity altogether in March of 2020 was the worst thing an investor could have done.

None of this is to suggest that the lessons of 2018 and 2019 should be forgotten. The scar tissue is thick enough to last a lifetime, I can assure you. But the biggest lesson of 2021?

Generalisations can be right at one price and wrong at another.

The vast majority of our Australian Fund's 31% return in 2021 came from stocks we've owned for many years. They were mostly illiquid and perceived as mediocre businesses. Most of the big contributors (with the notable exception of RPMGlobal) were trading at fractions of Forager's purchase prices in March 2020. Had we been hell-bent on improving portfolio liquidity and exiting underperforming businesses, 2021's returns would have been severely diminished. As it was, we left a lot of money on the table by selling some of those long-held stocks far too early.

As if to prove the point that there are very few hard and fast rules in investing, our other Fund has suffered from exactly the opposite problem. The Forager International Shares Fund experienced a difficult second half in 2021 as a number of our previous high-flyers (perceived as high-growth and relatively liquid) came crashing back to earth.

Great businesses can justify extremely high share prices. When you find a successful investment, selling it too early can be a huge mistake. But share prices, on the upside, can still incorporate all of that and more. Many new investors are learning that lesson as I write. By the time they decide to implement it, it is likely time to be buying those growth stocks.

One of my Twitter followers likened the problem to "learning how to fight the last war". Because when it comes to investing, you're often taught the most important lessons at the worst possible time to implement them.

Kind regards,

Steven Johnson
Chief Investment Officer