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Quarterly Commentary

December 2024
Fourth Quarter

"A long-term horizon is the closest thing to an investing superpower."

- Cliff Asness

On January 4th, 2010, we set out to do two things, "Make Money and Have Fun." We recently passed the 15-year anniversary for our firm, and we are on the path to achieving both. A seed investor with $1mln on day one now has an account with over $5.7mln net of fees. To use private equity parlance, we achieved a multiple on invested capital (MOIC) of 5.7x. Over this period, numerous macro events and amplified market volatility caused market participants to abandon their processes. Yet, we've never wavered from our strategy to recognize that investor psychology and market volatility create investment opportunities. As we said in our first-ever letter to investors, "our strategy will remain unchanged regardless of economic developments." The same applies today.

Whether observing Small Business Optimism, Consumer Confidence, or the excitement around pro-business policy changes, one can say with certainty that investor psychology is optimistic as stock market indexes continue to hit all-time highs. This does not necessarily portend negative price action; in fact, it can prove to be a tailwind. According to SentimenTrader, similar sentiment readings have occurred 12 times over the past 50 years and only once have stocks been down a year later. Time will prove whether history will rhyme.

It's interesting to note that regardless of how public markets perform, they continue to be the least preferred option for investors. Vanguard estimates that a generational transfer of wealth of $18 trillion will occur across the globe over the next five years. This will be the biggest transfer in the history of the world. The millennials and Gen Z investors that will inherit this wealth are not fond of public equities. A recent Bank of America study highlights that they prefer private-equity, startups, and crypto assets. Almost 75% of respondents under the age of 44 agreed that, "It is no longer possible to achieve above-average investment returns by investing solely in traditional stocks and bonds." This apathy strikes us as extremely ironic given that a family office allocator told us in our first year, "I will never invest in a long-only strategy, ever again." We believe this dogmatic approach to public markets is largely driven by volatility and short-time horizons. We believe that a patient, rational, and opportunistic investment strategy focused on long-term compounding of public equity investments harnesses a superpower that is incredibly rewarding.

A Tribute to an Investing Legend: Shad Rowe

The investment community lost a superstar in 2024. Shad Rowe, a friend and mentor, was an exceptional investor over his career, compounding investor capital over 13% per year for 38 years – that's a MOIC of 100x for the millennials and Gen Zer's doubting that public equity investing works. While the track record speaks for itself, Shad's willingness to evolve as an investor proved the investment process is never fully complete. Shad originally started as a Texas-focused investor, then evolved to short selling, and eventually reverted to more traditional value investing. He ultimately constructed his portfolio using an Americanization theme which was inspired by Sir Martin Sorrell. While he was always refining his investment process, Shad treasured finding companies that did things "better, faster, and cheaper" and focused on products that did things "for the customer, not to the customer." While this proved to be an incredibly lucrative framework, Shad was always tinkering with how he could make it even better.

Shad will be missed dearly, especially his dry wit and fondness for quotes that highlight the humility demanded in this business. One of his favorites was from George Goodman:

"If you don't know who you are, the stock market is an expensive place to find out."

The Next 15 Years – A Premortem

Our mission is to invest opportunistically using a value-oriented strategy to build generational wealth. The simplest way of framing how we plan to achieve this is the 12x30x30 maxim: 12% compounded over 30 years generates a 30x return on the original capital. Execution of the strategy requires a disciplined process and constant anticipation of <u>what could go wrong</u> versus reacting to <u>what just went wrong</u>. We believe our edge is having a long-term time horizon supported by a flexible investment mandate.

Ron Shaich is an entrepreneur and businessman best known for founding Panera Bread and establishing the fast-casual category of restaurants. Shaich wrote a book, "Know What Matters: Lessons from a Lifetime of Transformations" which highlights a practice he developed from Gary Klien: the premortem.

Shaich reveres intentional living and recognizes that reviewing goals/objectives when it is too late results in regret. Instead, he understands that time is the most precious investment you have, and you must use it to come up with a framework to achieve your goals before it's too late: i.e. the premortem.

In contemplating what we hope to achieve over the next 15 years, we performed a similar task. Here are the five key premortems that we believe will prevent regretful decision-making:

1) Process supersedes short-term results and must continuously evolve given markets are always dynamic by nature. Do not overanalyze short term periods of outperformance or underperformance.

2) The balance sheet, the business model, and the competence of management are non-negotiable. Investing in mediocrity results in just that.

3) Self-awareness protects against destructive overconfidence. Conviction is important, but the opportunity cost of continually being wrong can be devastating.

4) Understand the role of ego versus observer. The ego is responsible for excellence and demands perfection, ultimately proving responsible for most of the investment performance. However, it is best counter-balanced by an observer's mindset. There needs to be a neutral, unemotional co-pilot to navigate different environments. This helps protect us from becoming obsessed with the need to always be right and to quickly cease from being wrong.

5) Truly great ideas come along very rarely. Be prepared, invest opportunistically, and size positions to maximize the investment return.

It's been a thrilling 15 years, but we are just getting started. The most amazing aspect of compounding is what happens near the end – from year 25 to year 30 the wealth multiplier increases from 17x to 30x at the 12% rate. Investors can harness a superpower and experience the magnificent wonder of compounding if they are willing to accept the delayed gratification of a long-time horizon.

We are very fortunate and grateful that we get to work alongside the greatest clients we could ever ask for. Thank you for making the start of this journey possible

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and for entrusting us to manage your assets. We are enthusiastic about what the future holds in the next 15 years.

Sincerely,
Ryan, Alex, Ashley and Ray