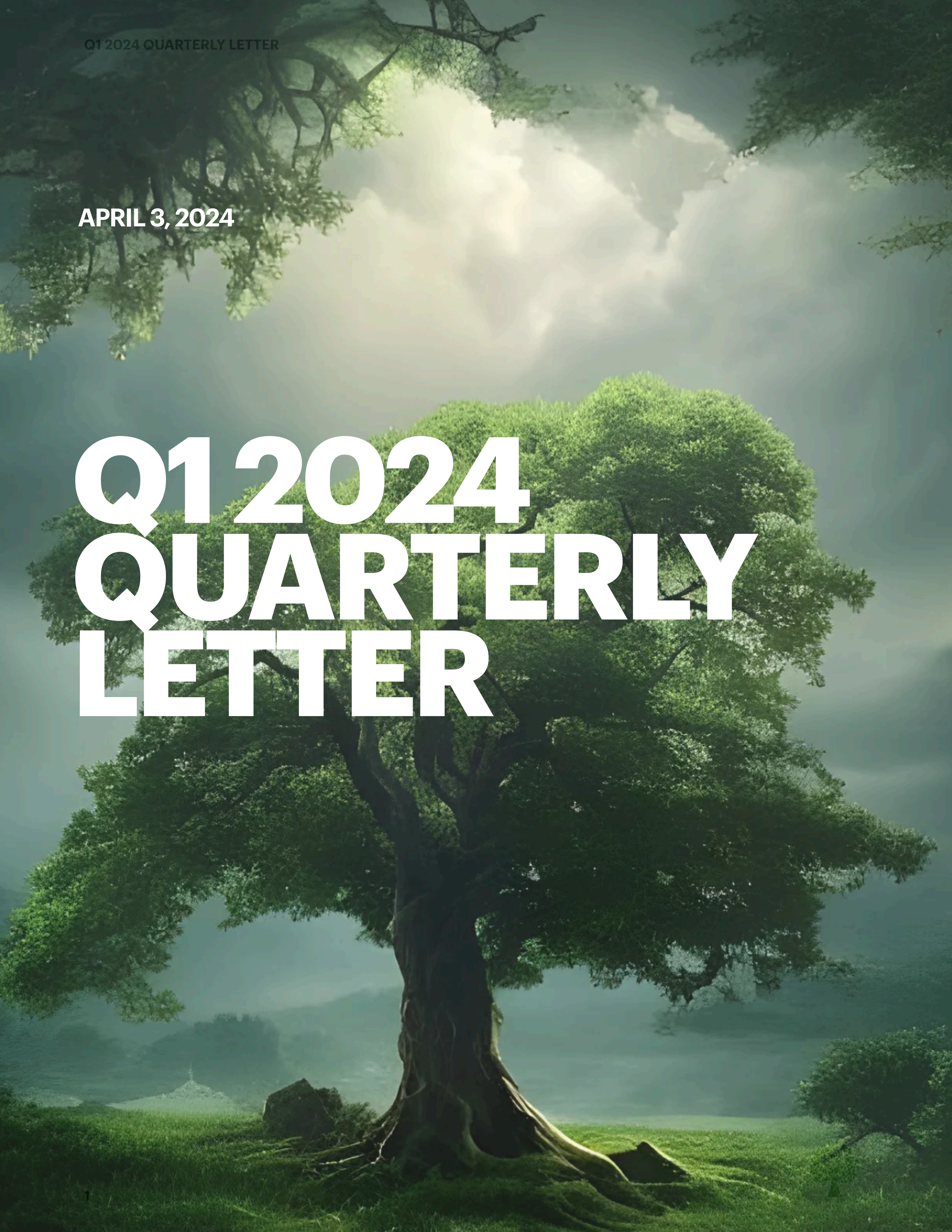

APRIL 3, 2024

Q1 2024 QUARTERLY LETTER

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Seeking Winners

Q1 2024 QUARTERLY LETTER

DEAR FELLOW INVESTORS

INVESTMENT PHILOSOPHY IN ACTION: BUILDING LONG-TERM VALUE

This report offers insights into my investment philosophy and the distinctive themes driving the portfolio construction. I meticulously manage an ultra-long-term, concentrated equity portfolio that targets a select group of publicly traded companies. These companies stand out for their exceptional financial performance and strategic brilliance.

My core philosophy revolves around four key pillars:

Unwavering Focus on Cash Flow: I prioritize companies with a business model I understand and a proven ability to consistently generate high levels of free cash flow. This robust cash generation serves as the lifeblood of future growth and investment opportunities.

Identifying Capital Allocation Masters: Beyond simply generating cash, I seek companies with management teams who excel at allocating that capital effectively. This expertise in making strategic investments fuels long-term shareholder value creation.

Investing Alongside Outstanding Owners: I believe in the power of ownership mentality. I gravitate towards companies led by individuals who are themselves invested in the company's long-term success. This alignment of interests fosters a strong commitment to sustainable growth and value creation.

A Price Conscious Mentality: The starting price you pay does matter. I use a reasonable estimate of future cash flows to arrive at what I consider an acceptable price to pay for an exceptional business.

My Seeking Winners portfolio translates this philosophy into action by specifically targeting companies that align with this approach. I own a number of companies that have established themselves as experts in identifying, negotiating, and integrating smaller, private businesses at compelling valuations, while other businesses in the portfolio have unmatched network effects or limited competition leading to hard to replicate returns on reinvested capital.

By prioritizing these types of companies I aim to unlock the full potential of compounding over a number of years. I'm confident that this approach will allow me to identify and invest in the best-in-class companies poised to deliver substantial and sustainable value over the long term.

Thank you to all the new subscribers to the Substack in Q1 2024 and to the existing subscribers, thanks for the continued reading and support.

SEEKING WINNERS FUND COMMENTARY

The impressive first-quarter performance of my portfolio companies, marked by robust earnings and cash flow growth, did not go unnoticed by the market. The Fund's first quarter 2024 performance was 14.48% compared to the S&P 500 Total Return of 10.56%.

The following table shows performance figures since I began tracking my portfolio publicly:

Performance - Average Annual Total Returns as of 03/31/24

Net Assets	QTD	YTD	1 YR	3 YR	5YR	10YR
Seeking Winners Fund	14.48%	14.48%	38.20%	N/A	N/A	N/A
S&P 500 TR	10.56%	10.56%	29.88%	11.49%	15.05%	12.96%

Outperforming the market or even making a positive return is not something I expect from my portfolio in every year or reporting period. Markets overall were strong in Q1; although we outperformed the S&P 500 total return by roughly 4%, I'm not patting myself on the back as it was hard not to generate returns this quarter.

If you want to compare investing to golf; the analogy would be that I hit a nice drive down the center of the fairway on the first hole in Q1. There is still the approach shot, the putt (or two) and then another 17 holes to go in our investing journey.

Where I am particularly pleased is that I generated the excess return in the quarter without holding any semiconductor stocks, cybersecurity stocks or unprofitable "AI stocks".

For the quarter the contributors and detractors were as follows:

Q1 2024 Attribution as of 03/31/24	
Name	Attribution
Constellation Software	3.49%
Copart Inc.	2.46%
Topicus.com, Inc.	1.80%
Lumine Group	1.58%
Berkshire Hathaway Inc.	1.55%
Microsoft Corporation	1.42%
Amazon.com, Inc.	1.17%
HEICO Corporation	0.72%
Costar Group, Inc.	0.71%
Evolution AB	0.33%
Alphabet Inc.	-0.75%

I made one significant change in the portfolio during the quarter; the sale of Alphabet (Google), which I've held since 2011-2012. The sale was done for three reasons:

- I had other idea's that I thought would provide superior compounded results over time that I wanted to allocate capital to.

- It is my believe that the dominant search business may actually be in trouble for the first time. I've held the stock through plenty of threats over the past decade plus, but never have I thought something could disrupt the search business until now with the introduction of AI search assistants. It remains to be seen if this will be the correct decision or not. Alphabet has plenty of levers they could pull still, such as cutting unnecessary headcount, fixing corporate culture by going back to be a product design company instead of a political institute, copying what Meta did and declaring a dividend, or even finding a way to have the best AI search experience on the market. My fear is that even if they manage the ladder, it won't be with the same monopoly nor the same margins as before.

- Before this sale, my portfolio was weighted roughly 35% to big tech, which isn't that far off from the weighting in the S&P 500 index, meaning the portfolio in my opinion was slightly too similar to this index. My believe is that to outperform this index over

the long-term, you have to do something different that what most investors do (which is become a closet indexer).

The recorded gain was all in tax free & deferred accounts and was subsequently redeployed into **Lumine Group, Topicus & HEICO**.

The other minor change made in the quarter was selling my small stake in **Evolution AB**. The reason for selling this was simply due to simplifying my portfolio by keeping it in CAD and USD. There will be a minor tax expense related to this sale.

The attribution of Topicus, Lumine Group and HEICO was unfortunately impacted negatively due to our sale of Alphabet and reallocation to these three names at substantially higher prices than our previous average cost basis.

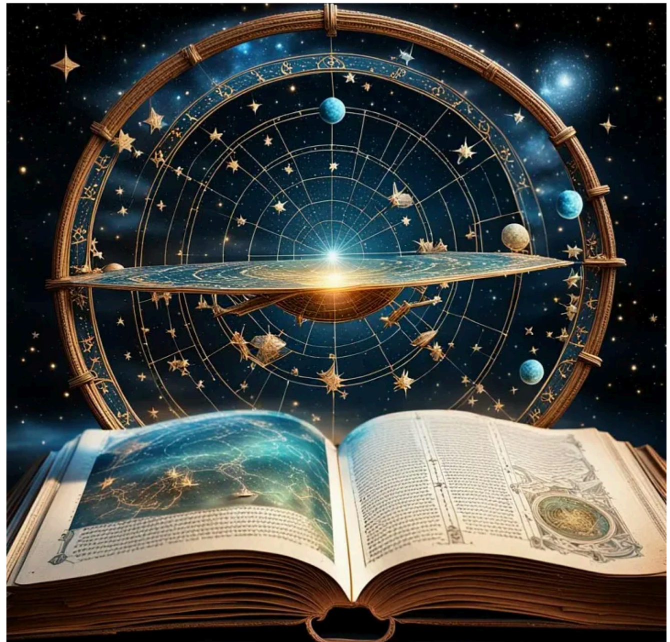
Had the allocation of the portfolio as at March 31, 2024 been held steady since January 1, 2024, the YTD return would have been roughly 18%.

Although this was more activity than I prefer, the end result is a portfolio that is more concentrated in my best ideas.

Holdings as of 03/31/24	
Name	% of net assets
Constellation Software	25.16%
Topicus.com, Inc.	13.01%
Microsoft Corporation	10.58%
Copart Inc.	10.31%
HEICO Corporation	9.76%
Berkshire Hathaway Inc.	9.68%
Lumine Group	9.53%
Amazon.com, Inc.	5.51%
Costar Group, Inc.	5.46%
Cash & Equivalents	1.00%

Sector Weightings as of 03/31/24	
Type	% of net assets
Information Technology	64%
Industrials	20%
Financials	10%
Consumer Discretionary	6%
Cash & Equivalents	1%

CONSTELLATION'S FINANCIAL PERFORMANCE: A DEEPER LOOK



Constellation's 2023 results paint a compelling picture of a company firing on multiple cylinders. Here's a breakdown of the key takeaways, going beyond the headline figures:

Sustainable Growth Engine

Revenue growth continues to be a hallmark of Constellation, with a robust 27% increase in 2023. Notably, even excluding the recent acquisition of Optimal Blue, organic growth is flourishing – a positive sign for the company's long-term health. This shift towards organic growth, which was 6% for the recurring revenue stream, indicates a less volatile and more sustainable business model compared to relying solely on acquisitions.

Beyond the Net Income Dip

A significant year-over-year decline in net income might raise initial concerns. However, a closer look reveals a more nuanced picture. Acquisitions like Altera initially impacted Constellation's overall growth rate. However, recent quarters show promising signs of recovery for Altera, with improvements in revenue, profitability, and cash flow generation.

This highlights Constellation's ability to not only identify promising acquisition targets but also successfully integrate and stabilize them, ultimately unlocking their full potential. Understanding certain accounting adjustments is crucial for a complete financial picture. Foreign exchange fluctuations and a specific liability related to Topicus shares also known as the IRGA/TSS Membership liability revaluation charge, amortization of intangibles and interest related to operating lease payments need to be adjusted for to calculate a more accurate NOPAT. See below for my estimates:

Exhibit 1: Constellation's Net Operating Profit After Taxes, 2022-2023
In ($) Millions of USD

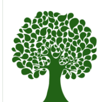
	2022	2023
Operating Income	725	265
Amortization of Intangibles	676	859
IRGA/TSS Membership liability revaluation charge	112	152
Finance Costs	110	192
Redeemable Preferrred Securities Expense	-	597
Earnings before interest, taxes, and amortization (EBITA)	1,623	2,065
Cash Taxes Paid	343	394
Net Operating profit after taxes (NOPAT)	**1,280**	**1,671**
Reinvestment Rate TTM		
CAPEX		42
Acquisitions		1,847
Research & Development*		304
Change in Non-Cash NWC		(266)
Total		1,927
Estimated Reinvestment Rate		**115%**

**25% of R&D included only for reinvestment rate*

Exhibit 2: Constellation's Invested Capital, 2022-2023
Operating Approach
In ($) Millions of USD

Cash	811	1,284		
Accounts Receivable, net	892	1,146		
Deferred income taxes	159	107		
Inventories	48	51		
Other Current Assets	497	538		
Total Current Assets	2,407	3,126		
Non-interest-bearing current liabilities	2,951	4,409		
Net working capital	(544)	(1,283)		
Property & Equipment, net	128	142		
Operating lease right-of-use assets	283	312		
Intangible assets, net & Goodwill	4,662	6,707		
Other long-term assets	174	286		
Total Invested Capital	4,703	6,164		
ROIC	**27%**	**27%**		
Average ROIC	**27%**			
Reinvestment Rate Scenario's	50%	60%	70%	80%
Theoretical Intrinsic CAGR	**14%**	**16%**	**19%**	**22%**

Source: Seeking Winners & Company Filings



Cash Flow: The True Measure of Success

Focusing solely on net income can be misleading. A clearer picture of Constellation's financial health emerges when examining cash flow metrics. Operating cash flow surged by an impressive 39% in 2023, and free cash flow available to shareholders witnessed an even more significant jump of 48%. These strong cash flow metrics demonstrate the company's ability to generate consistent profits that can be reinvested in growth initiatives or returned to shareholders.

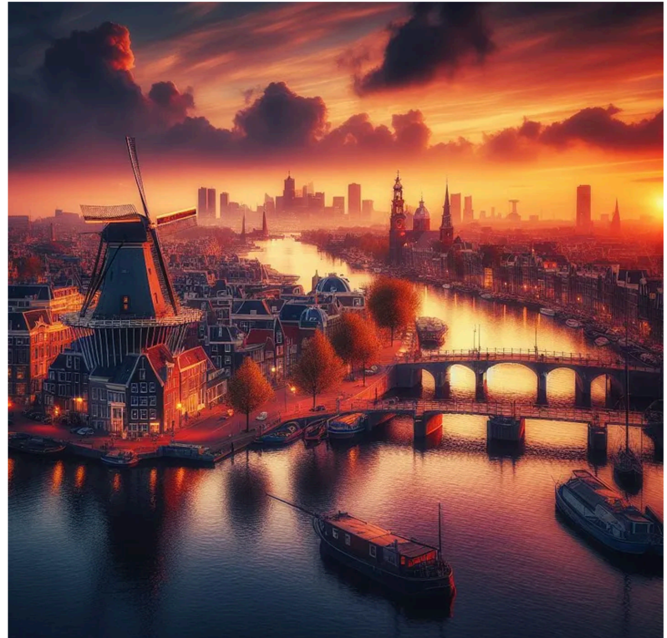
Management's focus on cash flow is another positive indicator for Constellation's long-term health. The company has aggressively deployed capital into acquisitions, exceeding $2.3 billion ($2.17 billion on a standalone basis) in 2023. Notably, they've managed to keep debt levels under control (1.4x leverage) despite this increased investment activity and willingness to lever up the balance sheet a bit. This balance between growth and financial prudence suggests a well-defined strategy that prioritizes sustainable long-term value creation.

A Robust Acquisition Pipeline Fuels the Future

Constellation's future appears bright based on their robust acquisition pipeline. The company has already deployed a significant amount ($654 million) in the first two months of 2024, signifying continued deal flow and growth opportunities. Additionally, if you take into account the upcoming Lumine conversion and Black Knight deals, reported FCFA2S is set to increase by 13-15% alone in FY24 before taking into account acquisition growth.

In summary while Constellation's financial statements might present a complex picture at first glance, a deeper analysis reveals a company with impressive and sustainable growth, a focus on cash flow generation, and a well-defined acquisition strategy. These factors all contribute to a positive outlook for Constellation's future and its ability to deliver long-term value to its stakeholders and I'm happy to hold this as my largest position.

TOPICUS THROWS A CURVE BALL



To the surprise of everyone, Topicus.com announced a €200 million special dividend paid to Topicus shareholders on March 28th, 2024, shaking things up for investors. While it might initially raise concerns about future returns, there's more to the story than meets the eye.

Deja Vu with Acquisitions? Remember how Constellation Software, surprised everyone with special dividends and then went on a buying spree? This move by Topicus could be a similar precursor to exciting M&A activity on the horizon. Additionally, HEICO in late 2012 issued a special dividend of $2.14 per share due to impending tax increases that were to take place in 2013 and has went on to compound at a nice clip since then.

Finding the Right Balance: Topicus is awash in cash, but achieving their ambitious acquisition goals requires careful planning. The true key to growth lies in how effectively they utilize their capital and how much they reinvest back into the business. However, continuously reinvesting everything isn't always the most strategic approach. Although Topicus is still very early in their journey, if we assume Topicus can reinvest 80% of capital at a 25% return over a number of years, the special dividend shouldn’t hurt shareholders in the long-run. Refer to the capital allocation section below for different reinvestment rate scenarios.

Cash Flow Conundrum: The strong start to the year might have left Topicus with more cash than anticipated, making immediate reinvestment of the entire sum challenging. Typically VMS businesses are flush with cash in Q1 as customers renew their annual software subscriptions. They receive the cash up front, but only recognize the revenue evenly over the year due to IFRS rules around revenue recognition.

Cash Flow Optimization: Holding onto a massive cash reserve isn't necessarily beneficial. Topicus recognizes this and is committed to putting their money to work strategically. I've personally seen this at work as the market does not give any multiple premium to companies who hoard cash on their balance sheets, even if it does provide optionality and stability.

Playing Devils Advocate: The other side of the coin is that Topicus couldn't find additional ways to deploy this capital ever or immediately, which could pose a risk on the valuation due to affects on future reinvestment rates. Although, I don't think this is the case, its something to keep on eye on and I'll be approaching this with a trust, but verify mentality.

If I had to critique any of the Constellation family of companies, it would be a bit around communication. I like the fact that they don't do quarterly calls, give guidance or communicate with shareholders unless they feel there is something important to say. However, I do think they could strike a middle ground and provide some additional commentary around events like this or maybe even write a semi annual shareholder letter to address common questions. Maybe in the future.

After my discussion with the CFO of Constellation and speaking with some other investors who hold the name, my conviction remains the same and as discussed above in the portfolio commentary, I added to my position in Q1 and continue to believe this will be long-term out performer.

BE NOT TEMPTED TO SHOOT AT ANYTHING SMALL

"I can't be involved in 30-50 things. That's a Noah's Ark way of investing - you end up with a zoo that way. I like to put meaningful amounts of money behind a few things."

- Warren Buffett

It appears Thomas Phelps, who wrote "be not tempted to shoot at anything small" and Warren were on the same page on this topic, which is portfolio concentration. I want to bet big on my best ideas.

Countless times I've seen investors create a portfolio that is 30-50 names with a 2-3% weighting per holding and claiming that this is a better way to beat a certain benchmark through intelligent stock picking. Although there is no "right" way to construct a portfolio, this approach of having so many names makes no sense to me as all I see is an overly complicated index fund, whereby the investor has no real understanding of the business model of the stocks they hold. I'd rather own the nine names I do and understand the business models well and think this is actually safer than owning an index fund.

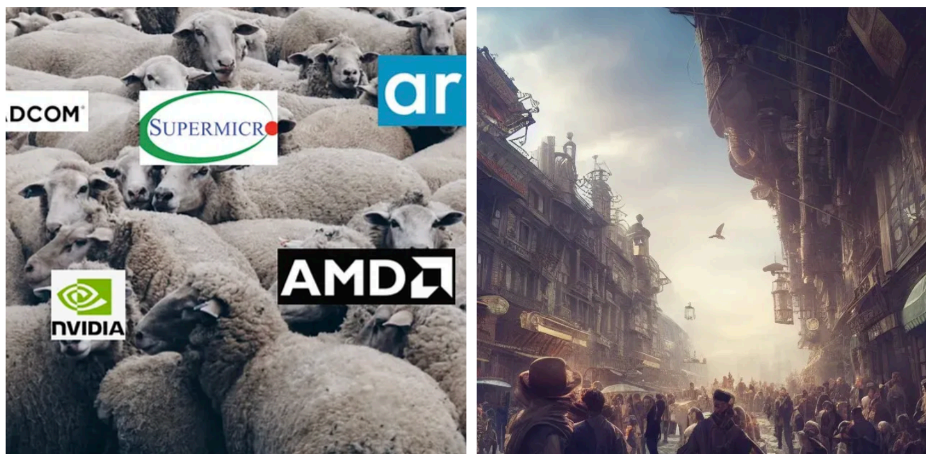
In a 2005 paper titled "Best Ideas," the authors identified which positions in fund managers' portfolios were their best ideas by looking at position weights relative to their benchmark. They found that the best ideas not only generate statistically and economically significant risk-adjusted returns over time, but they also systematically outperform the rest of the positions in managers' portfolios. The level of outperformance varied between 1.6% and 2.6% per quarter depending on what factors were used to risk-adjust the returns.

It seems most investors take the approach of taking a large number of small positions simply so they can say they own the stock if one of them pops in any given year. I don't aim to be that type of person. I want to follow what many great investors do and take concentrated positions and continue to focus and learn about my best ideas. If one of the stocks is going to be a large compounder over time, I want it to matter dollar wise. It's irrelevant if a stock goes up 100% if you allocated 1-2% to it.

UNDERSTANDING THE RISKS OF TRADING LIKE A GAMBLER

"Though the stock market is massively larger than it was in our early years, today's active participants are neither more emotionally stable nor better taught than when I was in school. For whatever reasons, markets now exhibit far more casino-like behavior than they did when I was young. The casino now resides in many homes and daily tempts the occupants. "

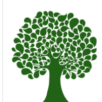
- Warren Buffett 2023 Shareholder Letter



We're seeing a lot of speculative traders jump back into the market in 2024, chasing returns and riding momentum plays, all while justifying the price jumps. The traders currently seem to be crowded around a couple themes right now:

Bitcoin and other crypto currencies - I'm not fully sure what to even say regarding this one; Sam Bankman-Fried was found guilty on all charges for a maximum penalty of 25 years behind bars for stealing money from people who dumped their hard earned cash onto FTX, bought bitcoin all while he was converting it all back to USD for personal use. You would think of all things, this would put an end to folks speculating on these cryptocurrencies. Q1 2024: Bitcoin is up 65%...

Nvidia and other semi-conductor stocks - Artificial intelligence (AI) is everywhere these days, from your smartphone to the stock market. But how are investors approaching this rapidly evolving technology?



Many investors view AI as a transformative force poised to disrupt countless industries. From healthcare diagnostics to automated manufacturing, AI promises to streamline processes, boost efficiency, and unlock entirely new revenue streams. This potential translates to significant growth opportunities for companies at the forefront of AI development.

While the potential is undeniable, I'm a little more cautious. AI development can be expensive, and the path to sustainable profitability for AI-powered companies isn't clear to me yet outside of companies like Microsoft, Nvidia & Amazon. Separating hype from reality can be challenging, making it difficult to assess a company's true AI potential and its impact on future returns.

Investors approach to the above unknown seems to be betting on the semiconductor industry and the chip industry is on fire! The iShares Semiconductor ETF (SOXX) is up a whopping 18% year-to-date, crushing the broader market. It seems anything related to semiconductors is getting a boost.

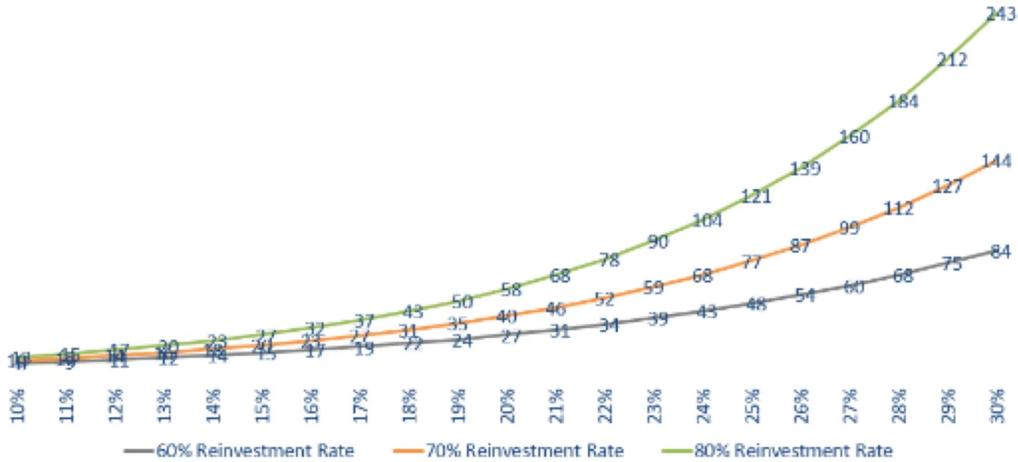
Some investors, like Nate Koppikar and Jim Chanos, are worried about the current AI boom. They see a risky situation where hyped AI startups rely heavily on companies like Nvidia. Here's how it works: Nvidia "invests" in these startups, who then turn around and use the capital to buy Nvidia's H100's. Koppikar calls this a "closed loop" or "round-tripping of revenues." Basically, Nvidia is inflating its sales figures by selling to itself.

Case in point: CoreWeave, an AI startup backed by Nvidia, recently secured a huge loan with Nvidia chips as collateral. Koppikar argues that Nvidia's impressive revenue growth might not reflect a healthy AI market.

If you're rolling your eyes reading Jim Chanos' name and thinking he's wrong the majority of the time, do a bit of research on some of his short thesis'. It may take a while for the market to figure it out, but he's right more than he's wrong.

Investors in Nvidia and other hot stocks might feel comfortable because they have safeguards like stop-loss orders to lock in profits. But constantly chasing the next big thing and having to redeploy capital isn't a winning long-term strategy and we know how this plays out over time.

WHY CAPITAL ALLOCATION MATTERS



Source: REQ Capital

Success in the business world hinges on effective leadership. But beyond generating profits, the true mark of a transformative leader lies in their mastery of capital allocation. These CEOs are not just strong executives; they are astute strategists who understand the art of deploying a company's resources to maximize long-term value for shareholders.

Traditionally, the path to the CEO's office might be paved with expertise in areas like sales, production, or even internal politics. However, once at the helm, a CEO's focus shifts. Capital allocation becomes a critical differentiator, a silent weapon that shapes a company's destiny.

Understanding Why High ROIC Trumps Pure Growth

While a company's growth rate might grab headlines, a metric known as Return on Invested Capital (ROIC) offers a more insightful perspective on its long-term health. A study by McKinsey & Company suggests that ROIC levels tend to exhibit greater stability

over time compared to growth rates. This stability stems from the underlying factors that contribute to high ROIC.

Companies with consistently high ROIC often possess several key strengths. They may boast superior products or services that resonate strongly with customers, translating into consistent demand and pricing power. Additionally, they might have developed efficient business models that optimize resource allocation and minimize waste. Perhaps most importantly, these companies often possess a sustainable competitive advantage, a strategic edge that allows them to consistently outperform competitors and generate superior returns on their investments. This advantage can stem from factors like brand loyalty, intellectual property, or a strong distribution network.

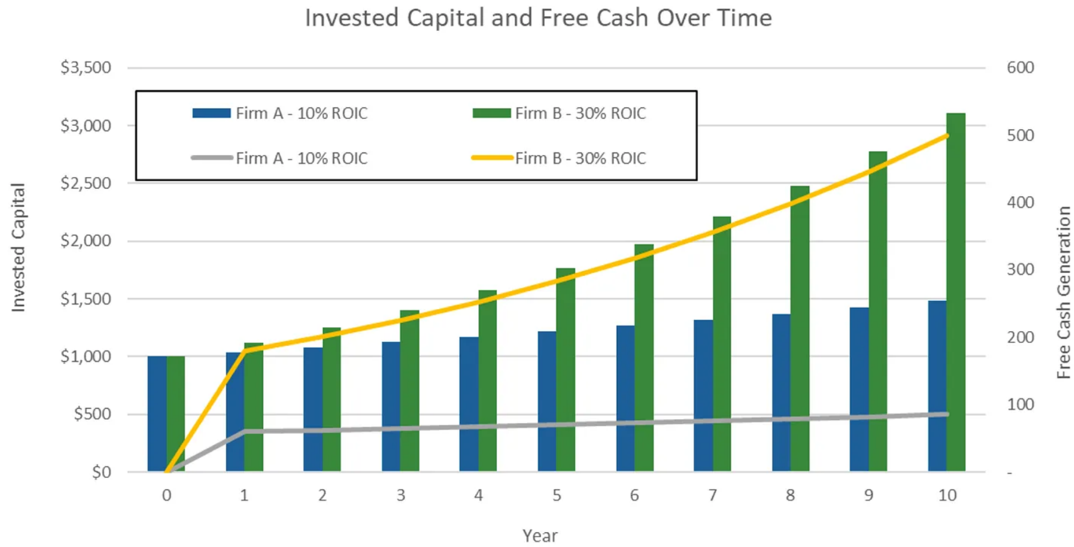
On the other hand, the McKinsey study found that growth rates tend to decelerate over time, eventually converging towards an industry average of around 2%. This is because growth can be heavily influenced by external factors beyond a company's direct control. Factors like market saturation, economic conditions, and intensifying competition can all place limitations on a company's ability to sustain a high growth rate indefinitely. While growth is certainly desirable, focusing solely on a company's current growth spurt can be a misleading evaluation tactic.

The Power of Compounding ROIC

Companies with high ROIC benefit from a powerful financial phenomenon known as compounding. Compounding essentially refers to the process of earning returns on your returns. When a company with a high ROIC reinvests its profits back into the business at similarly high rates of return, the effect is amplified over time. Imagine two companies, A and B:

- Company A: ROIC of 10%, reinvests 40% of earnings, starts with $1,000 capital.
- Company B: ROIC of 30%, reinvests 40% of earnings, starts with $1,000 capital.

Over a ten-year period, Company B will have accumulated significantly more cash and invested capital compared to Company A, solely due to the power of compounding



returns on their higher ROIC. This example highlights the significant long-term advantage that high ROIC can provide.

This is the power of capital allocation. It's the strategic lever CEOs pull to unlock a company's true potential. By prioritizing CEOs who excel in this domain, investors can gain a significant edge in identifying companies positioned for long-term success. After all, a strong balance sheet is just the beginning. It's the CEO's ability to translate those financial resources into strategic investments that ultimately determines how much value reaches shareholders' pockets.

It's important to keep in mind however, what the growth runway looks like for a company and not just looking at ROIC in isolation. ROIC times reinvestment rate is what an investor should focus on and how likely it is that a company can maintain the same reinvestment rate.

Below is an example of one of our portfolio holdings Topicus, with an estimate of NOPAT, ROIC and different reinvestment rate scenario's and how that would impact future returns going forward.

topicus:com

Exhibit 1: Topicus Net Operating Profit After Taxes, 2022-2023
In Thousands of Euros

	2022	2023
Operating Income	104,418	144,766
Amortization of Intangibles	107,078	121,124
Interest expense on debt	11,459	15,207
Interest expense on lease obligations	1,172	1,422
Amortization of debt related transaction costs	2,757	1,101
Share in net (income) loss of equity investee	(584)	(139)
Foreign exchange loss (gain)	286	1,857
Other finance costs (income)	(6,021)	977
Earnings before interest, taxes, and amortization (EBITA)	220,565	286,315
Cash Taxes Paid	45,925	50,281
Net Operating profit after taxes (NOPAT)	**174,640**	**236,034**
Reinvestment Rate TTM		
CAPEX		7,778
Acquisitions		113,846
Research & Development*		79,277
Change in Non-Cash NWC		(20,062)
Total		180,839
Estimated Reinvestment Rate		**77%**

****50% of R&D included only for reinvestment rate***

Exhibit 2: Topicus Invested Capital, 2022-2023
Operating Approach

In Thousands of Euros	2022	2023		
Cash	136,772	179,059		
Accounts Receivable, net	95,790	134,079		
Deferred income taxes	19,978	16,412		
Inventories	1,419	4,517		
Other Current Assets	34,778	55,250		
Non-interest-bearing current liabilities	539,274	566,035		
Net working capital	(250,537)	(176,718)		
Property & Equipment, net	19,579	20,030		
Operating lease right-of-use assets	54,412	61,066		
Intangible assets, net & Goodwill	874,000	906,082		
Other long-term assets	17,030	13,824		
Total Invested Capital	714,484	824,284		
ROIC	**24%**	**29%**		
Average ROIC	**27%**			
Reinvestment Rate Scenario's	50%	60%	70%	80%
Theoretical Intrinsic CAGR	**13%**	**16%**	**19%**	**21%**

Source: Seeking Winners & Company Filings

The above is a somewhat simplistic way of how I think about how much a company could potentially compound over time. Project this over a 5-10 year period, slap a exit multiple on this and then back into your IRR. The way I go about it is as follows:

- Start with calculating your estimate of NOPAT, which is the cash earnings a company would have if it had no debt or excess cash. The reason I do this is because NOPAT is the same whether a company is financed with all equity or if it has a lot of debt. Removing the issue of capital structure allows for effective comparison between businesses.

- I add back amortization of intangibles and not depreciation (even though both are non-cash) because depreciation accurately reflects wear and tear on tangible assets,

but because the company expenses its investment to replenish the intangible assets, we don't want to penalize the company twice, first through amortization and second through investment in intangibles.

- For the reinvestment rate, we want to include the non-cash change in working capital (if the company you're looking at has excess cash on the balance sheet, this will make your ROIC look lower by increasing invested capital, so you have to normalize for the amount of cash the company needs to run the business).

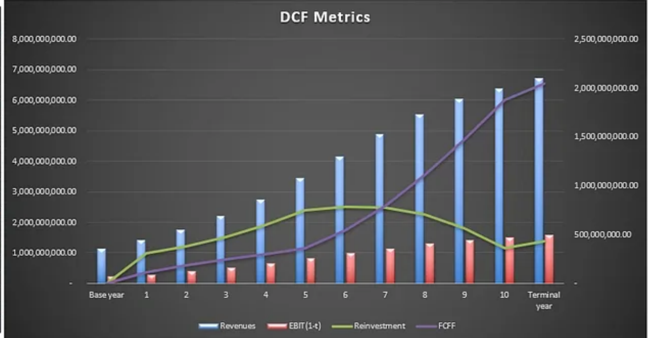
- Included in the reinvestment rate calculation, is research and development costs. The question is, how much should you include into your calculation? The correct answer is any amount that leads directly to commercialization of a product or service. As investors this is hard to know in advance, so I assume 50% of R&D spend for Topicus will generate commercial value. My reasoning behind this is that Topicus is the owner of niche, mission critical vertical market software companies with high switching costs, so any R&D spend to improve the software over time will continue to generate recurring revenue.

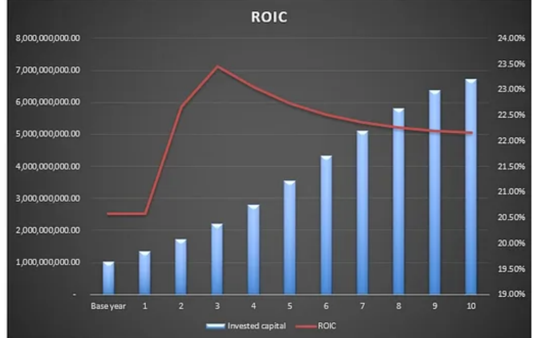
After calculating our ROIC in exhibit two, we can start to think about reasonable reinvestment rates over an extended period of time for Topicus. In exhibit 2, I present what the CAGR would be under 4 different scenarios, leading to a CAGR of 13% - 21%.

From here you have to fact check yourself by building a discounted cash flow model. I've attached a snip below from the most recent one I built for Topicus to give a sense of the assumptions I'm making.

	Base year	1	2	3	4	5	6	7	8	9	10	Terminal year
Revenue growth rate		25.00%	25.00%	25.00%	25.00%	25.00%	21.10%	17.20%	13.30%	9.40%	5.50%	5.50%
Revenues	1,124,973,000	1,406,216,250	1,757,770,313	2,197,212,891	2,746,516,113	3,433,145,142	4,157,538,766	4,872,635,434	5,520,695,947	6,039,641,366	6,371,821,641	6,722,271,832
EBIT (Operating) margin	24.07%	25.00%	28.33%	30.00%	30.00%	30.00%	30.00%	30.00%	30.00%	30.00%	30.00%	30.00%
EBIT (Operating income)	$ 270,760,939	$ 351,554,063	$ 498,034,922	$ 659,163,867	$ 823,954,834	$ 1,029,943,542	$ 1,247,261,630	$ 1,461,790,630	$ 1,656,208,784	$ 1,811,892,410	$ 1,911,546,492	$ 2,016,681,549
Tax rate	22.00%	22.00%	22.00%	22.00%	22.00%	22.00%	22.00%	22.00%	22.00%	22.00%	22.00%	22.00%
EBIT(1-t)	$ 211,193,532	$ 274,212,169	$ 388,467,239	$ 514,147,816	$ 642,684,771	$ 803,355,963	$ 972,864,071	$ 1,140,196,692	$ 1,291,842,852	$ 1,413,276,080	$ 1,491,006,264	$ 1,573,011,609
Intangibles amortization	$ 121,124,000	$ 145,348,800	$ 174,418,560	$ 209,302,272	$ 251,162,726	$ 301,395,272	$ 361,674,326	$ 434,009,191	$ 520,811,029	$ 624,973,235	$ 749,967,882	$ 899,961,459
- Reinvestment		$ 305,699,185	$ 382,123,981	$ 477,654,976	$ 597,068,720	$ 746,335,900	$ 787,384,375	$ 777,278,987	$ 704,413,601	$ 564,071,108	$ 361,065,516	$ 432,578,192
FCFF		$ 113,861,784	$ 180,761,818	$ 245,795,112	$ 296,778,777	$ 358,415,334	$ 547,154,023	$ 796,926,896	$ 1,108,240,280	$ 1,474,178,207	$ 1,879,908,630	$ 2,040,394,875
NOL	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Cost of capital		9.10%	9.10%	9.10%	9.10%	9.10%	9.09%	9.09%	9.08%	9.07%	9.06%	9.06%
Cumulated discount factor		0.9166	0.8401	0.7700	0.7058	0.6469	0.5930	0.5436	0.4984	0.4569	0.4190	
PV(FCFF)		$ 104,362,617	$ 151,859,041	$ 189,266,684	$ 209,459,830	$ 231,857,669	$ 324,447,892	$ 433,199,380	$ 552,294,553	$ 673,577,871	$ 787,606,102	

Terminal cash flow	$ 2,040,394,875
Terminal cost of capital	9.06%
Terminal value	$ 57,314,462,784
PV(Terminal value)	$ 24,012,454,610
PV (CF over next 10 years)	$ 3,657,931,640
Sum of PV	$ 27,670,386,250
Probability of failure =	0.00%
Proceeds if firm fails =	$13,835,193,125
Value of operating assets =	$27,670,386,250
- Debt	$337,873,973
- Minority interests	$253,299,000
+ Cash	$179,059,000
+ Non-operating assets	$0
Value of equity	$27,258,272,278
- Value of options	$0
Value of equity in common stock	$27,258,272,278
Number of shares	129,841,819
Estimated value /share	$ 209.93
Price	$ 121.34
Price as % of value	57.80%
IRR	14%





Implied variables												After year 10
Sales to capital ratio		0.92	0.92	0.92	0.92	0.92	0.92	0.92	0.92	0.92	0.92	
Invested capital	$ 1,026,724,973	$ 1,332,424,157	$ 1,714,548,138	$ 2,192,203,115	$ 2,789,271,835	$ 3,535,607,735	$ 4,322,992,110	$ 5,100,271,097	$ 5,804,684,698	$ 6,368,755,805	$ 6,729,821,322	
ROIC	20.57%	20.58%	22.66%	23.45%	23.04%	22.72%	22.50%	22.36%	22.26%	22.19%	22.16%	20.00%

A couple key points to keep in mind when reviewing this:

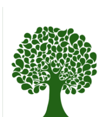
- **The EBITA you have in your DCF model is different than your high level calculation of ROIC, NOPAT and reinvestment rates, what gives?**

In my DCF model above, I'm doing a couple things in more detail than my high level calc. The first is I'm taking the R&D expenses on the income statement and treating them like capital expenditures, which I chose to amortize over three years. So the amortization from R&D I'm adding back to operating income. I think this is necessary in a world we live in now full of intangible assets.

The second change is the off balance sheet liabilities that are present; specifically future lease expenses that are sitting as a liability on the balance sheet of Topicus. The adjustment here has reduced operating income and increased the debt to normalize the future cash outflows for these lease payments.

- **An EBIT margin of 30% really?**

Could debate this one all day long, but a 30% EBIT margin for capital light niche software businesses is not unrealistic, especially when you have 4-6% organic growth annually; most of which accrues to the bottom line.



At the price of the company as of March 29, 2024, the above would give you a IRR of 14%. My cost basis is quite a bit lower than this, but it will be interesting to see how this plays out over time and if my assumption that this will follow in Constellation Software's footsteps is accurate.

The above is a very high level view of how I think about investments and when you put together a concentrated portfolio these, like I have today you end of with a good result. As always, any outperformance I obtain over time relies on estimating the longevity of the ROIC and reinvestment rates of my portfolio companies. This in my opinion is one of the hardest things to do as a investor and it will be a ongoing process of asking myself each year if the companies in the portfolio still have the ability to earn high returns on the capital they deploy and what their future runway will look like.

Once more, thank you for your continued support and hopefully you find some amount of value in my writing. If you found this or any of my other writing useful, please like the article, share with others in your circle and on social media, or feel free to drop a comment with your thoughts on any of my posts and I'll get back to you.

Yours sincerely,

Seeking Winners

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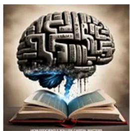

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