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FROM DECISIONS TO A WAY OF BEING

MUSINGS ON LONG-TERM INVESTING

Seeking Winners

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Have you ever felt like long-term investing is just a series of decisions you make, hoping for the best? As a young investor that's exactly what I thought. But experience is a great teacher, and in the real world of investing, I soon discovered a crucial truth: a long-term approach demands constant recommitment in the face of internal and external pressures. More than just discipline (which requires effort), but rather a natural state of being – The closer you get to your natural state of being the closer you are to a clearer mind, which creates space for a framework for thinking and making decisions and also coming to the realization there are multiple paths up the mountain.

For many investors, the world of finance revolves around numbers. We pore over balance sheets, scrutinize earnings reports, and build complex models to predict future performance. This data-driven approach is the bedrock of sound investment strategy. But what about the factors that defy quantification? The whispers, the hunches, the intangible aspects that can spell success or failure for a company?

This is where things get interesting. As someone who's primarily focused on the analytical side of investing, I'm venturing into uncharted territory: the realm of the intangible. It's that gut feeling, that spark of recognition when you encounter a company that resonates beyond the numbers.

Here's the challenge: How do we capture these intangibles and translate them into actionable insights? Can we build a positive feedback loop for identifying gems?

GROW YOUR WEALTH STEADILY: THE POWER OF PATIENCE AND CONNECTION

This concept goes beyond simply holding onto investments for a while. It's about rewiring your brain to see the bigger picture, focusing on building wealth over decades, not days. Traditional investing often resembles a frantic chase for the next big thing, fuelled by a relentless stream of financial news and the fear of missing out. But what if there was a way to escape this cycle and invest with peace of mind?

One of the biggest hurdles to achieving long termism is the tyranny of time pressure. Investors constantly feel pressured to unearth the next hot opportunity, leading to rushed decisions and potentially missed opportunities. This relentless pursuit can be detrimental to your investment strategy. The answer I found lies in the evergreen portfolio. A collection of high-caliber investments held with the intention of perpetual ownership. Ideally, this portfolio functions independently, leveraging the power of compounding to accumulate wealth over an extended timeframe.

The beauty of a evergreen portfolio lies in its numerous benefits:

❖ I**nternalized Long-Termism:** By setting an infinite horizon (think forever, not next month!), you naturally adopt a long-term perspective. This ingrained mindset strengthens your resolve and helps you resist the allure of short-term fads.

❖ **A Virtuous Cycle of Quality:** Less pressure to chase the next big thing translates to better decision-making. When you're not constantly on the lookout for new investments, you can dedicate more time and energy to thorough research, prioritizing quality companies with strong long-term potential. This focus on quality, in turn, fosters a stronger portfolio, further reducing the urge to chase fleeting trends. It's a virtuous cycle that promotes a calmer and more strategic approach.

- **Enhanced Decision-Making During Downturns:** When markets inevitably experience turbulence, a evergreen portfolio allows you to remain composed. Freed from the anxieties of short-term fluctuations, you can focus on strategic moves that capitalize on long-term opportunities. Market dips might even present golden buying opportunities for quality stocks at a discount!

- **Sustainable Investing for the Long Haul:** Unlike the high-maintenance approach of traditional investing, an evergreen portfolio is built for the long term. It frees up your valuable time and mental energy, allowing you to focus on other aspects of your life. This hands-off approach is ideal for busy professionals like myself or those who simply don't enjoy the constant market frenzy.

But long-term investing goes beyond just the mechanics of your portfolio. It's about understanding the underlying dynamics that drive sustainable growth. Here, the concept of positive feedback loops comes into play. Imagine a snowball rolling downhill – it gathers momentum as it goes, becoming bigger and more unstoppable. Positive feedback loops function similarly in the world of business. A company with a strong feedback loop enjoys a self-reinforcing cycle where success breeds even greater success. Understanding these loops allows you to identify companies with a solid foundation for long-term growth.

In fact, a closer look at successful long-term investors reveals a crucial, often overlooked factor: a personal connection with their holdings.

For those who achieve exceptional long-term returns, companies transcend mere instruments of financial gain. They become partners in a shared vision, fostering a sense of loyalty and unwavering belief. This emotional connection is surprisingly rare in the investment world, yet demonstrably powerful. This, when combined with an autonomous, decentralized company culture can lead to some impressive returns.

Consider the case of Constellation Software (CSI).

CONSTELLATION SOFTWARE INC.

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	2022	2023		
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

While countless companies have generated exceptional long-term returns, CSI stands out for its ability to cultivate a devoted following among everyday investors. This loyalty extends beyond financial performance; it encompasses a deep appreciation for the company's values, leadership, and overall philosophy. Some investors connect with Mark Leonard personally, while others resonate with the company's way of treating shareholders capital, cultivating trust. From an employee perspective at CSI, Mark calls it Decentralized Human Scale and he has described it as follows:

"We seek out vertical market software businesses where motivated small teams composed of good people, can produce superior results in tiny markets. What we offer our BU Managers is autonomy, an environment that supports them in mastering vertical market software management skills, and the chance to build an enduring and competent team in a 'human-scale' business. While we have developed some techniques and best practices

for fostering organic growth, I think our most powerful tool is using human-scale BU's. When a VMS business is small, its manager usually has five or six functional managers to work with: Marketing & Sales, Research & Development ("R&D"), Professional Services, Maintenance & Support and General & Administration. Each of those functional managers starts off heading a single working group. If the business leader is smart, energetic and has integrity, these tend to be halcyon days. All the employees know each other, and if a team member isn't trusted and pulling his weight, he tends to get weeded-out. If employees are talented, they can be quirky, as long as they are working for the greater good of the business. Priorities are clear, systems haven't had time to metastasize, rules are few, trust and communication are high, and the focus tends to be on how to increase the size of the pie, not how it gets divided. That's how I remember my favourite venture investments when I was a venture capitalist, and it's how I remember many of the early CSI acquisitions."

This deeper emotional connection offers a distinct advantage in navigating the inevitable market turbulence. When faced with volatility, investors and even employees with a personal connection are more likely to maintain composure and trust in the company's long-term vision. They view temporary setbacks as bumps in the road, not reasons to abandon ship. In CSI's case, this will be critically important as they continue to scale into larger deals or a pivot is required. CSI 2.0's success will require a bit of trust and learning from other operating groups because as units get larger life becomes more difficult.

Mark has also stated the following:

"Volaris and TSS regularly divide their larger BU's into smaller BU's that focus on sub-segments of their markets. Volaris feels strongly that splitting larger BU's into smaller ones allows more targeted products and services that differentiate their offerings from their more horizontal competitors. Harris has very successfully acquired multiple BU's in the same industry and run them independently rather than combining them into one BU. Both tactics forego obvious and easily obtainable benefits from economies of scale. We think we get something valuable when we constrain BU headcount, but it isn't a panacea for all of our organic growth challenges"

So, how can you cultivate a deeper connection with your investments and unlock the benefits it offers? I've compiled a few thoughts below:

- **Delve into the Company Narrative:** Uncover the company's story. What is their history? What are their aspirations? Just like any strong partnership, understanding their core values and goals is essential. Explore interviews with founders, delve into their social media presence, and assess whether their company culture aligns with your own. Look for a company that resonates with your personal values. Perhaps you're passionate about environmental sustainability and seek to invest in companies that prioritize eco-friendly practices. Maybe you admire a company's commitment to social responsibility and giving back to the community. Whatever your values may be, finding a company that reflects them can strengthen your connection and fuel your long-term conviction.

- **Leadership Matters:** Many companies host online events or Q&A sessions featuring their leadership team, while some others simply choose to write letters to shareholders. These provide valuable insight into the management's vision, passion, and overall approach. Do they inspire confidence? Do they seem like capable stewards entrusted with guiding the company's future? Look for leaders who exude a sense of authenticity and credibility. Are they transparent in their communication? Do their actions align with their stated values? Trustworthy leadership is a critical factor in building a strong emotional connection with an investment.

- **Find Your Investment Community:** The online world offers a wealth of forums and communities dedicated to specific companies. Engage with other like-minded investors, read books by experts on companies, discuss the company's prospects, and gauge the collective enthusiasm. This virtual space can further solidify your belief in the company's long-term potential. Sharing your investment journey with others who share your enthusiasm can be a powerful source of motivation and support, like what I'm trying to do here at Seeking Winners.

- **Embrace the Long-Term Journey:** Cultivating a connection with your investments is a gradual process that unfolds over time. Don't expect an instant spark. Instead, focus on learning about the company, its leaders, and its place within the larger industry. Look for a company with a strong track record, a clear vision for the future, and a sustainable competitive advantage. By understanding the company's fundamentals and prospects, you'll gain a deeper appreciation for its potential and feel more confident weathering market fluctuations.

THE UNDERRATED QUESTION OF QUALITY FIT

Many investment strategies focus primarily on the characteristics of the investment itself. However, the compatibility between the investor and the investment is often overlooked. There are some companies that have had fantastic long-term performance, but they just don't fit my investing style and investing philosophy, but that's okay. Investing is a no called strikes process, I don't have to swing.

Just like many successful investors, Chris Mayer incorporates seemingly simple yet powerful filters into his strategy. A prime example is his preference for companies with low debt or even net cash (something most readers familiar with his work will recognize). This focus on financial strength has several advantages.

- **Reduced Risk:** With a concentrated portfolio, a single over-leveraged company can cripple the entire fund. Low debt mitigates this risk.

- **Downturn Resilience:** Companies with strong balance sheets are better equipped to weather economic storms.

- **Improved Focus:** This filter significantly narrows down the investment universe, allowing Chris to concentrate his research efforts.

- **Long-Term Mindset:** Financial stability fosters a buy-and-hold approach, encouraging Chris to stick with his convictions.

I recently listened in to the Fundsmith Annual Shareholders' Meeting on Youtube (linked below), which I encourage all my readers to check out when you have free time. There is a section of the presentation where they discuss there "Investable Universe" - the companies where they believe are considered high quality businesses. From the presentation they mentioned there were about 85 for Fundsmith. These 85 businesses are businesses that they have determined are high quality based on many factors, with return on capital employed being the primary one; this is there fishing pool if you will before valuation is taken into account.

What struck me as interesting, was one of the companies that came up in there investable universe was Adyen; an end-to-end payments, data, and financial management company. The interesting discussion was around the stock drop at one point being down 77%. Although the stock is in there investable universe, the 77% drop was so alarming that they did not pull the trigger on buying the stock. Part of the reason is it makes it harder to hold on to and you may make bad irrational decisions based on price movement. It also made them question their conviction in how hard it was to actually switch payment providers given most SMB's are dealing with multiple bank anyway. The focus on risk adjusted returns is what they were getting at for them was the most important, it was a better fit for them not to own it at the current time.

In my opinion, part of their decision was based on intuition kicking in gained from 14 years running Fundsmith and from there time as banking analysts.

Traditional investment approaches often struggle to grasp the true essence of quality. Quality thrives on innovation, on challenging the status quo and forging new paths. It's a dynamic concept that defies rigid categorization and resists being neatly captured in a financial metric. This elusiveness makes it difficult for traditional investment firms to fully embrace.

Conviction in quality is an intangible quality itself, one that's hard to translate across teams and translate into concrete action plans. Imagine trying to explain an innovative company culture or a CEO's visionary leadership through a series of numbers – it simply doesn't translate.

Investors are naturally drawn to what they can readily grasp. Easy to quantify and analyze, creating a comfortable cornerstone of many investment decisions. However, the allure of the measurable can blind investors to the more nuanced power of quality.

Think of it this way: competitive advantages provide a baseline strength, but it's the inherent excellence of a company, its ability to innovate, adapt, and inspire customer loyalty, that propels it towards greatness.

The difference between a good company and a truly great company isn't a marginal improvement; it's a significant leap forward. To understand a truly superlative company, you need to appreciate its unique qualities, its company culture, and its vision for the future. It's about recognizing a company that's not just playing the same game as everyone else, but one that's constantly rewriting the rules.

In his book "The Intuitive Investor: A Radical Guide for Manifesting Wealth," Jason Apollo Voss challenges the traditional, data-driven approach to investing. He argues that exceptional long-term returns come from cultivating a deeper connection with companies, going beyond just analyzing financial metrics.

Quality, in Voss's view, is a dynamic concept encompassing innovation, adaptability, and a strong company culture. These factors are difficult to capture in a spreadsheet but are crucial for identifying companies poised for long-term outperformance.

The book goes on to argue that the very best companies, those with the potential for truly superlative growth, often defy easy analysis. They are constantly evolving, pushing boundaries and rewriting the rules of their industries. These companies consistently surprise investors with their ability to innovate and outperform expectations. Traditional financial models struggle to account for this inherent dynamism.

Voss emphasizes the role of intuition. Data analysis remains important for building a foundational understanding, but it shouldn't overshadow the power of a well-honed "investor's sixth sense." By developing your intuition through experience and a holistic understanding of companies – their stories, their cultures, their visions for the future – you can learn to recognize the often-unquantifiable aspects of quality. This ability to see beyond the numbers is what allows investors to identify companies with the potential to outperform for years to come.

Because quality can't be easily codified and analyzed, truly exceptional companies might fly under the radar for extended periods. This presents a golden opportunity for investors with the foresight to recognize this hidden potential. By looking beyond the standard metrics and seeking out companies that embody true quality, investors can uncover diamonds in the rough, companies poised for long-term outperformance.

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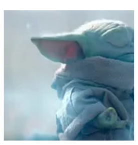

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