

## Conscious Investor® Fund

### Interim Letter to Members: December 2022

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| <b>Noble Purpose:</b>  | Focussing on growth of wealth with peace of mind for Members and their families.  |
| <b>Mission:</b>        | The Capital Allocation Team does this with consciousness and stewardship, making use of unique and proprietary software and processes to identify the most likely Wealth Winners® while avoiding potential Capital Killers.   |
| <b>Vision:</b>         | That our Members view the Fund as a fundamental part of the growth and preservation of wealth, for themselves and their families, to live the lifestyle they choose while investing in companies that add value to society.   |
| <b>Cultural Values</b> | <ol style="list-style-type: none"> <li>1. We stay true to the philosophies and methodology of Teaminvest and Conscious Investor®—centred around long-term growth of earnings per share—to maximise long-term capital growth for our Members.</li> <li>2. We recognise Members and their families have faith in us, by investing their money in the Fund.</li> <li>3. We support our Members by being responsive to their questions and by providing regular reports explaining the principles of how and where we invest their money.</li> <li>4. We emphasise that we only make money as managers when our Members make money, and not simply by having funds under management irrespective of performance.</li> </ol> |

## Contents

|  |   |
|--|---|
| Technology One .....                                     | 2 |
| MasterCard .....   | 3 |
| Good, Better, Best.....                                  | 4 |
| Conscious Investor® and the Teaminvest Methodology ..... | 5 |
| Appendix: Mastercard: A World Beyond Cash.....           | 6 |

Dear Fellow Fund Member:

Hope you, your family and loved ones are well in these turbulent times.

Despite the turbulence, when we look at the history of our companies, we can see a picture of exceptional companies with sales and earnings that have been consistently growing.

What about their prices? Sometimes they lag the earnings. Other times they bound ahead. Importantly, over time they drive the prices higher.

When prices temporarily slow compared to earnings, we will be waiting in the wings to pounce on more of our—and hopefully, your—favourite companies at bargain prices. (Thank you to our members who regularly keep adding money to their Fund holdings. By the way, Sandy and I added to our holdings during 2022.)

Two of our long-term Wealth Winners are Technology One (TNE) and Master Card (MA). Let’s look at them in more detail to see why I call them perpetual Wealth Winners.

## Technology One

The company states that its purpose is “transforming business, making life simple. We build and deliver truly great products and services that transform business and make life simple for our customers.”

The Fund first bought shares in TNE in June 2015 for \$3.50 each. We bought a parcel of 1,000 shares using all the cash we had available at the time. Today the share price is \$13.20.

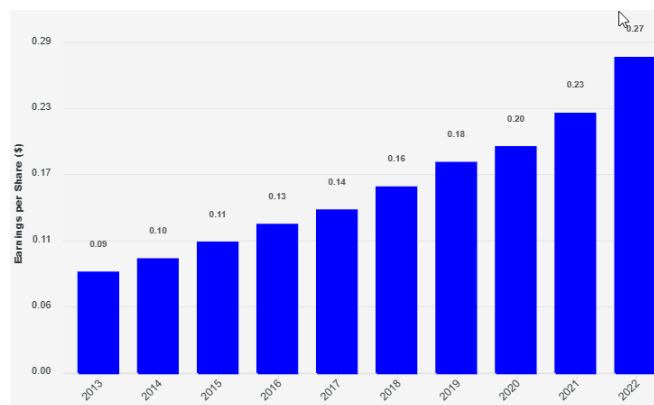
With dividends, this is an attractive return of 20.79% per annum.

But if that was all we did regarding TNE, the Fund would not be as successful as it has been... and continues to be.

This is where Conscious Investor enters the scene. The Capital Allocation Team uses it to monitor all the holdings of the Fund waiting for opportunities to top up. In broad terms, this means waiting until the price lags the earnings of a company. (It is a more complicated than this, but this is the basic idea.)

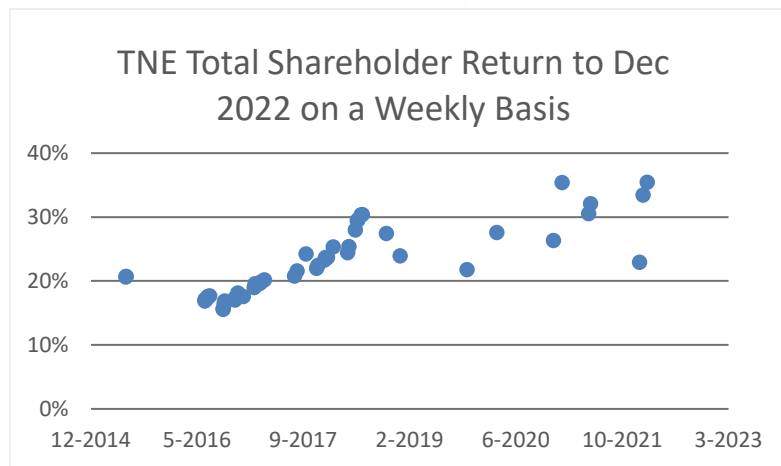
As just stated, the price is now \$13.20. More importantly, by watching for buying opportunities, the initial holding of 1,000 shares is now a holding of 641,000 shares with an overall return of 28.2% per annum.

Here is a chart of the Earnings per Share for TNE. Note how consistently they have been growing year after year. This gives us confidence about the future growth of EPS.



EPS has grown from 9 cents in 2013 to 27.1 cents over the current year, a growth of 300%.

For recording purposes, we bundled the purchases into blocks of length. Since 2015 we have made 49 such purchases. The next chart shows the return for each of these purchase until the end of 2022.



## MasterCard

The company describes itself as: “We reshape the digital economy so everyone — individuals, financial institutions, governments and businesses — can realize their ambitions.” Continuing: “For more than 50 years, Mastercard has pioneered technology to make payments simpler, smarter and safer.”

MasterCard has what they call a “Purpose Manifesto”, what we usually refer to as a noble purpose. It is: connecting everyone to priceless opportunities. They continue:

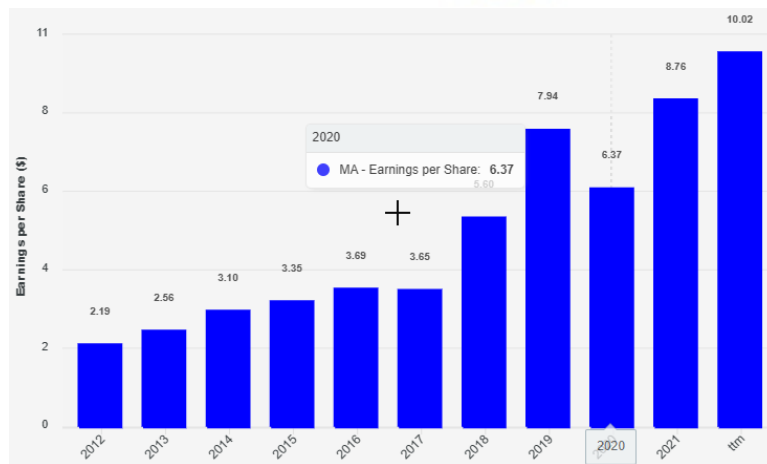
*We see a connected world. Where humanity unites, prosperity is possible and opportunity is open to us all.*

MasterCard rarely appears in the list of our ten largest holdings. The last time it was in the list was August 2020. The reason it doesn’t usually appear is the Fund also holds a large position in a similar company, Visa. So if we add the holdings in Mastercard and Visa, then together they would be in the largest ten.

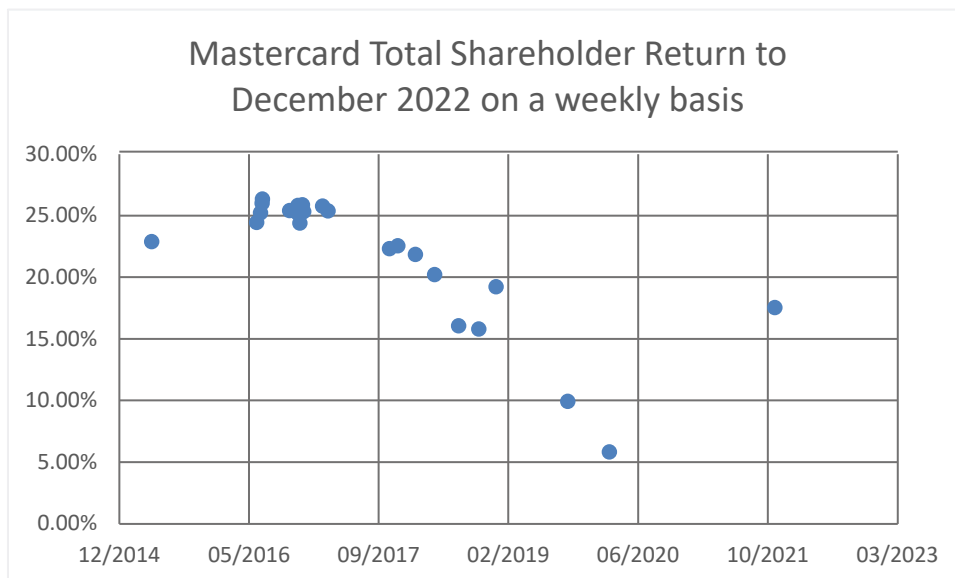
The first purchase of MasterCard was in April 2015: a total of 300 stocks at US\$90 each. Now the Fund has 7,700 shares in Mastercard at the share price of US\$376.28 giving a total holding of US\$2.90m. (The holding for Visa is slightly less.)

The average return for the first purchase alone is 22.46% per annum; the average return for the entire MasterCard holding is 23.99% per annum.

Here is a chart of EPS for MasterCard. EPS has grown from \$2.19 in 2012 to the current level of \$10.02, growth of around 350%.



As we did for Technology One, for recording purposes, we bundled the purchases into blocks of one week. Since 2015 we have made 25 such purchases. The next chart shows the return for each of these purchases until the end of 2022.



Technology One and MasterCard are two examples of the extraordinary companies in the Fund with all the signs that we will want to top up our holdings whenever their prices allow it. What is particularly interesting is that the two of them are at the opposite ends of the size spectrum. Technology One has market cap of approximately AUD\$4.5 billion compared to approximately USD\$376.6 billion (or AUD\$538 billion) for MasterCard, more than 100 times the size.

### Good, Better, Best

Looking back, I had a wide range of extraordinary teachers over my time at primary and secondary school. When I think of their dedication, care and hard work, I feel very humble. They all contributed to my education, some formally, others in terms of behavioural patterns.

In Grade 5 I had Mrs Helgason. She had a saying which sticks with me today: Good, better, best; never let it rest. It was her way of getting her noisy class of ten- and eleven-year olds to do their best. (Let

me know if you had any teachers you still remember who had a particular influence on you. I could collect them together in a later newsletter.)

Apart from my personal life, I thought how this maxim applies to the companies we search for to invest your money.

We want companies that have all the signs that in the ensuing years, they are going to keep improving. We are not interested in turnarounds or startups. Instead, we want companies that have the drive and passion to be better and more successful over the next five, ten or more years.

At the regular meetings of the Capital Allocation Team we scrutinise the companies in the Fund looking for any signs of impending difficulty. Does the management have what it takes to overcome such difficulties? If they can't, what would be the outcome?

On the other side, the companies are scrutinised for qualities indicating they will be able to continue growing at a healthy rate. How have they performed in the past? Do we have confidence that they will continue this growth in the future? What are their products? How confident are we that the demand for them will continue to grow?

A key role in this is the stated purpose and vision of the company. Do they make sense? Does the company use them to provide a basis for decisions at all levels? After all, we want our companies to be passionate believers of "good, better, best" with demonstrated skills to put it into practice.

## **Conscious Investor<sup>®</sup> and the Teaminvest Methodology**

The starting point is our investment software, Conscious Investor<sup>®</sup>. It filters and analyses companies listed in markets around the world in three steps: Filter, Research and Return. The filter stage zeros in on companies with attributes such as strong and stable growth in earnings and sales, high and consistent return on equity and not too much debt. The research stage identifies those companies for which these attributes are likely to continue. Finally, the return stage calculates the maximum price to pay to be confident about getting the required rate of return over the long term. Conscious Investor uses automatic margins-of-safety calculations to stress test the investment assumptions.

Once this is done, the Teaminvest Methodology focuses on the following five areas and the Capital Allocation Team scores these areas to increase the precision of the decision process.

1. How does the company make money? Is the business expected to grow? Are there clear signs it will have a growing customer base?
2. Investments should be like castles with deep moats: What are unique features of the business that separate it from its competitors? These "economic moats" are scored in terms of depth and durability.
3. Risks need to be identified: All businesses face risks that could potentially weaken their operations. These risks are identified and are scored according to the likelihood of their occurring over the next economic cycle and their potential damage if they occur.
4. Does the company have a clear mission statement or noble purpose? Is there strong evidence that the company uses these to guide its direction, decisions and remuneration policy?
5. Is management honest, open and rational? As part of examining the business, evaluation is made of the board and senior management: are there any signs that they are not acting honestly, rationally and in the best interests of shareholders? The Capital Allocation Team

scores the remuneration structures for the CEO and senior management in terms of clarity, alignment and quantum.

The final steps involve calculating buy and sell prices. You can find more details in the Information Memorandum. It also describes our processes to identify Wealth Winners® while making it extremely unlikely we would place any of your capital in potential Capital Killers.

We hope you enjoyed reading this Letter. We chose the topics to help you better understand our philosophy and what motivates us in choosing investments for your money. Please let us know if there are any other topics you would like us to include.

We aim to continue being outstanding stewards of your precious capital you have entrusted with us.

Wishing you the very best of health and well-being.

Kind regards,



(John Price and the rest of the Capital Allocation Team: Howard Coleman, Kevin Robinson and Michael Stewart)

*The Capital Allocation Team prepared this report for members of the Conscious Investor® Fund. It does not take into account anyone's personal circumstances. Remember, what happened in the past is not always what will happen in the future.*

Questions? Contact us: [cifund@consciouscapital.com.au](mailto:cifund@consciouscapital.com.au)

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## **Appendix: Mastercard: A World Beyond Cash**

### **Making Payments Safe, Simple and Smart**

**Background:** Mastercard takes tiny amounts from billions of transactions every year: last year 11.7 billion transactions with a total purchase amount of US\$3.8 trillion using 1.8 billion cards.

Together Visa and Mastercard possess unmatched scale, a powerful barrier to entry for potential competitors.

Mastercard is the second-largest processor with a 26% market share. The brand is accepted by more than 40 million merchants worldwide.

**Strategy** Strives to make payments easier and more efficient. A typical transaction on its core network involves four participants in addition to MA: account holder (a consumer who holds a card or uses another device enabled for payment), merchant, issuer (the account holder's financial institution) and acquirer (the merchant's financial institution).

MA itself does not actually issue cards, extend credit, determine or receive revenue for interest rates or other fees.

**Company Vision** According to its website, the vision of the company is to help create a world beyond cash by using its technology and expertise to make payments safe, simple and smart.

Its goal is to move money from any funding source—cash, card, bank account, mobile money account—to any destination globally, securely, and in real time. It is expanding into payment flows such as business to business (B2B), business to consumer (B2C), person to person (P2P) and government to consumer (G2C), etc., both domestically and across borders—and the channels that can best support these flows safely and seamlessly.

**Success Drivers:** Continually expanding the range of offerings and ease of use.

**Economic Moats:** The strongest moat of Mastercard is the network effect. Its worldwide penetration means that it is extremely difficult for competitors to seriously impinge on its business. The brand itself is well recognized.

**Key Future Risks:** The main risks relate to competition and technology. As the highly competitive global payment industry continues to develop and change, the company faces the challenge of disintermediation. According to company, parties that process Mastercard transactions may try to eliminate its role as an intermediary.

Mastercard has made a number of savvy acquisitions over the past few years, but there is always the risk they overpay for an acquisition or an acquisition moves the company in an unfavourable direction.

**Conclusion:** Mastercard is world leader in payment systems with a very strong moat to continue growing for many years. A welcome investment for the Fund.