

# COOPER INVESTORS FAMILY AND FOUNDER FUND



AFS LICENCE NUMBER 221794  
ABN 26 100 409 890

## QUARTERLY COMMENTARY | DECEMBER 2020

The aim of the Fund is to generate attractive long term returns by applying Cooper Investors' VoF Investment process to build a concentrated portfolio of listed Family and Founder led businesses. These companies must meet our high bar for a Family and Founder company – the unique and rare management teams and boards with extreme levels of financial and emotional skin in the game, or “Soul in the Game”.

Our observations and experience lead us to believe that a portfolio of these companies - those which exhibit the highest quality stewardship combined with operating and capital deployment excellence - will deliver attractive long term returns.

	**Portfolio	#Benchmark	Value Added
Since inception <sup>^</sup>	22.62%	13.56%	9.06%
Since inception <sup>*</sup>	14.53%	8.83%	5.70%
Rolling 3 months	4.20%	6.52%	-2.32%
Rolling 6 months	12.05%	10.65%	1.40%
Rolling 1 year	12.26%	5.90%	6.36%

<sup>^</sup> Cumulative (2 July 2019) <sup>\*</sup> Annualised (2 July 2019)

# MSCI AC World Net Divs in Australian Dollars

\*\* Returns are gross of fees and expenses

Past performance is not necessarily a reliable indicator of future performance

## QUARTERLY PORTFOLIO REVIEW

*For the quarter the fund delivered a 4.2% return. Since inception on 2nd July 2019 the fund is up 22.6%, or 14.5% annualised. For reference the MSCI ACWI AUD delivered 6.5% for the quarter and 13.6% since inception, or 8.8% annualised.*

FX was a significant headwind to returns for the quarter as the AUD increased more than 7% to the USD, the Fund's largest currency exposure. For 2020 and since inception the AUD has increased nearly 10% to the USD, lowering the Fund's returns.

Note all further stock performance commentary is in local currency.

Whilst quarterly performance is not the name of the game there was a unique dynamic this quarter which bears mentioning. Put simply, many of the weaker performing sectors or stocks in the market for the first nine months of 2020 performed strongly in the December quarter, largely buoyed by positive vaccine news. For example, banks and energy companies were up 32% and 27% respectively.

This dynamic extended to portfolio holdings. For example

Paycom, a new addition to the fund in the third quarter, was up 44% for the quarter after underperforming in the first nine months of the year. Based in Oklahoma and led by founder Chad Richison who started the company in 1998, Paycom is one of the leading providers of HR and payroll software for mid-market US companies. It is a fast growing SaaS business but the stock was under pressure in 2020 as growth rates slowed from ~30% to ~10%. Paycom's model is based on charging its customers on a per employee basis and the immediate spike in unemployment from the pandemic directly impacted revenues. However as confidence in the economic outlook grew throughout 2020, Paycom's earnings outlook and share price has followed suit.

On the other hand, a number of strong performing portfolio companies during the first nine months of the year were the weaker stocks during the quarter. Franco Nevada was down 13% despite a flat gold price and an oil price recovery. Veeva Systems was the Fund's best performer for 2020, up over 90% since initiating a position early in the year, but was down 2% for the quarter. Founded in 2007 by CEO Peter Gassner, Veeva provides software to the life sciences sector. We think Veeva is a unique SAAS company. Most of the established SAAS companies are in horizontal markets – marketing, security, etc. Veeva is a vertical market specialist whereby the company specialises in solutions for life sciences and healthcare. We think vertical market specialists typically come with more profitable and enduring franchises.

From a Subset of Value perspective, Bond Like Equities were the main detractor to the portfolio for 2020, with Ferrovia and Equity Lifestyle Properties down 15% and 10% respectively. Ferrovia is an owner of high quality infrastructure assets such as tolls roads and airports, and Equity Lifestyle owns and operates manufactured housing communities, RV resorts and campgrounds in North America. These businesses were impacted by the pandemic but the stocks didn't participate to a great extent in the post vaccine approval rally. In a world where many businesses have been re-rated these typically stable businesses continue to offer attractive opportunities.

## STOCK NEWS

During the quarter, **Fortive** spun out Vontier as a standalone listed entity. Fortive itself was spun out of Danaher (another portfolio holding) over four years ago, as a portfolio of Danaher's legacy industrial assets. The Rales brothers, who founded Danaher, remained on the board of Danaher but also went across to Fortive as directors and continue to be sizeable shareholders. Since separating in 2016 Fortive had already sold a sizeable chunk of lower growth industrial businesses and Vontier was the final step in streamlining its portfolio. The

Vontier portfolio consists of good businesses (Gilbarco Veeder Root in fuel retailing and Matco in tools) but are not the growth area of Fortive. The Rales brothers did not seek directorships at Vontier and hence the Fund sold its Vontier shares.

The new Fortive is a smaller and more focused \$4.5bn revenue company in testing, safety, healthcare and software markets with 20% margins. Fortive has leadership positions in a range of attractive niche markets. For example, their Industrial Scientific business specialises in gas detection equipment and is a pioneer of a new subscription model of gas detection as a service. Another business in Landauer sells products and services that measures radiation levels in energy and healthcare settings. With the spin they have increased their exposure to these faster growing businesses with sizeable margin potential. M&A has been a hallmark of Rales businesses and with Fortive back to a very strong balance sheet the company is in a strong place to capitalise on any investment and acquisition opportunities.

### OBSERVATIONS AND PORTFOLIO POSITIONING

2020 had just about everything. A global pandemic that had not been seen in 100 years and with it a swift fall in markets culminating in a near 35% drop in the space of 6 weeks. The rebound has been just as impressive.

For us there was the added dimension of no travel. The portfolio managers and analysts typically spend two months a year overseas visiting companies and the operations. We made our best efforts to adjust and turned to zoom calls – the team spoke with nearly 500 global companies and industry contacts during the year. Our long term and strong relationships with company management meant we were able to continue the conversations quite naturally over video calls. We have continued to uncover new ideas and are spending our time understanding the businesses, cultures and opportunity sets from afar.

It is taking longer to have the same comfort and conviction with a new company compared to when walking out of the headquarters or sites. It is not an unsurmountable barrier but we know it takes additional meetings to have that same conviction. Regardless, the key to our process for selecting new stocks comes from a watchlist of companies that we have typically been following and meeting with for years. For example Eurofins which was bought in January is a company we had been meeting with and following closely for years. The Fund owns 23 stocks and there are another 35 stocks we are covering closely on the watchlist. This number continues to increase through the power of the Cooper Investors network.

The benefits of the Family & Founder led dynamic were visible

in the most difficult times of the downturn. These companies protected their businesses and core assets as lockdowns were implemented. In order to support cash flows and often due to an abundance of caution, costs were managed appropriately, for example reduced spending on travel and consultants. However employees were protected and supported to maintain the culture and the heart of the organisations. Our companies have kept their balance sheets strong for this exact moment in time. With resilient and well run business models the Fund holdings protected their revenues. For the Fund's holdings as a group, quarterly revenues were flat in Q2 which was the most economically impacted quarter from the shutdowns. Growth has already started to rebound and we expect that to continue. In more normalised environments we expect to see a mid to high single digit organic growth profile for our portfolio.

Many of our companies are leaders in niche, fragmented markets. Examples include insurance brokerage, property services, industrial technology and lab services. This profile provides regular acquisition opportunities to drive further growth and it is a hallmark of many of our companies. The portfolio look through is that less than half of profits are returned to shareholders via dividends and buybacks, and the rest is reinvested back into the business most often through M&A. Most of these acquisitions are small and have largely continued throughout 2020.

In times of stress these companies have previously shown an ability to pounce on unique investment opportunities. There are countless examples of how the fallout from the global financial crisis created opportunities for our holdings and watchlist companies. Danaher acquiring Beckman Coulter, Intercontinental Exchange buying NYSE and Constellation Software buying TSS, to name a few. The portfolio holdings have strong balance sheets and are in a strong position should this occur. The Fund holdings combined have a Net Debt/EBITDA profile of 1x. To put this in context, the S&P 500 has a Net Debt/EBITDA of about 2x and the typical private equity company is over 5x, according to S&P Global Market Intelligence. However, the strong and fast rebound in valuations and the liquidity provided by central banks meant that large opportunities from this crisis have yet to present themselves in a meaningful way. Companies with good businesses but bad balance sheets, which is always a great hunting ground for an acquisition, received financial support during these times. At the same time the good assets were cheap for what felt like all of 24 hours.

The typical acquisition our company makes is of a small unlisted business. The valuations of the FAANGs have little impact on these deals. So despite the elevated markets we expect the typical acquisition opportunities to continue. Should the

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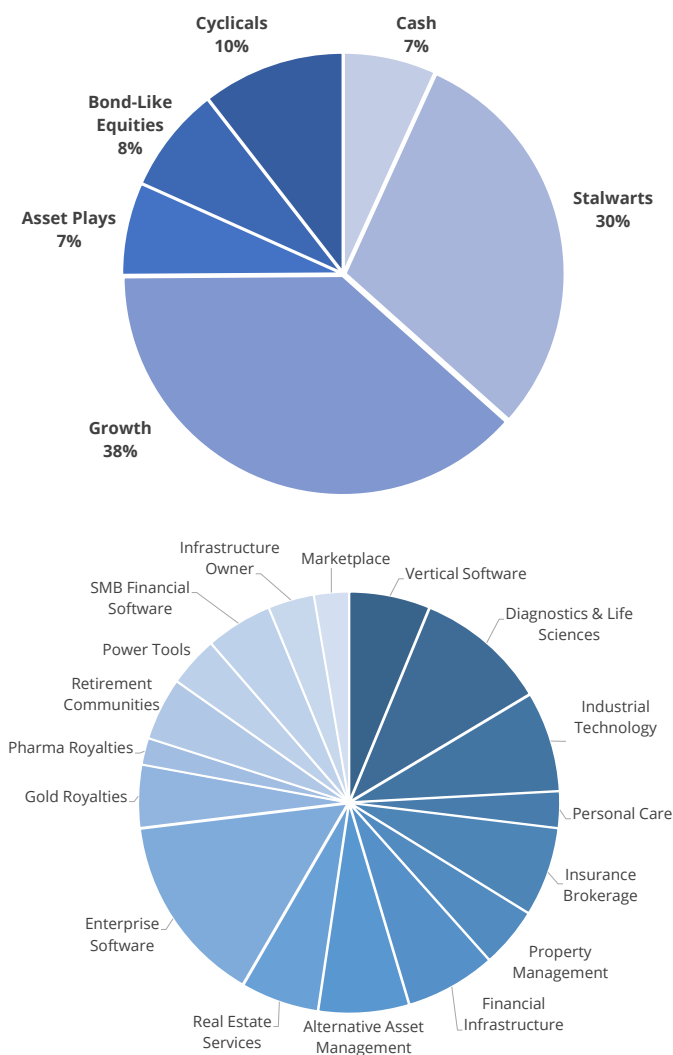
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recovery not prove as fruitful or valuations begin to moderate we would expect to see some of the bigger opportunities start to emerge.

The rapidly changing operating trends and market movements drove some portfolio turnover during the year. Two stocks bought during the year, Estee Lauder and Paycom, were also sold within the year as strong share price performance meant the value latencies we had identified were exhausted. For example Estee Lauder now trades on 45x PE and Paycom on 27x sales. We are cautious on some of the hyper growth names. For example a company on a 20x sales multiple needs to grow at 20% for 10 years to generate a double digit return – very few companies achieve this. We also see a number of cyclical names with valuations which assume a significant and uninterrupted economic recovery. Value latency remains an important part of the process and discipline. We invest across the spectrum of Subsets of Value (stalwart, growth, cyclical, asset plays, and bond like equities) and deploy capital to areas where we see value latency. During the year we added a new component to the portfolio in a range of SAAS founder led businesses. We are currently seeing opportunities emerge in more stalwart and bond like equities areas as they have become quickly forgotten in the recovery phase.

The Fund is quite concentrated, holding 23 stocks. We have seen that in the short term the Fund performance can be quite different from that of the benchmarks. Overall after 18 months we are encouraged by the progress despite a meaningful FX headwind and some own goals, which are a natural part of investing. We continue to see an opportunity and are focused on generating attractive long term returns and are looking forward to the journey.

Breakdown of Portfolio by Subset of Value and Business



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## SENIOR PORTFOLIO MANAGERS



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Allan is the Lead Portfolio Manager for the Family and Founder Fund and joined CI in 2007, having been a foundation member of the CI global equities team. Allan has over 12 years of experience investing in international equities markets.



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Marcus is the Deputy Portfolio Manager for the Family and Founder Fund. Marcus joined CI in 2012 and has 10 years of experience in equities research and investing, primarily in North American companies.

## CLIENT RELATIONS

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