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Q1 2021 Portfolio Review

Partners in WMKI's Strategic Opportunities portfolio currently own 19 high quality businesses. A few facts about the portfolio: ~33% of the portfolio is in companies headquartered in Canada or Mexico, 15 of our businesses have leadership (founders, management, board members or shareholders) who have deep "skin in the game," and relative to the S&P 500 we are infinitely underweight Tesla!

Over time, we expect our portfolio to grow more concentrated. One of the key benefits of this commitment to concentration is that businesses must always compete for a share of our highly valuable capital. This mechanism raises the bar for investments and makes our conviction much greater in each individual business that we own.

Our portfolio does not reflect any major indices. We are focused on absolute returns, not benchmarking. However, our portfolio has performed adequately on an absolute and relative basis so far. Quarterly returns mean very little (especially in our first full quarter of performance!) and you should judge our performance on at least a 3-year time horizon.

Total Returns through March 31, 2021	WMKI Strategic Opportunities	MSCI All Country World Index
Since December 31st 2020	9.9%	4.9%
Since Inception (11/5/2020)	18.2%	14.4%
Since Inception (Equity Only)*	25.2%	14.4%

*Highlights the drag associated with pre-discussed lags between accounts being opened and reaching full investment during 2020. Since inception, the average weight of cash has been over 21%.

What are we pondering?

March of 2021 marked the anniversary of global financial markets delving into mayhem as they grasped the gravity of the COVID-19 pandemic. A key lesson ingrained in my head over the last year is the fallacy of people being able to accurately predict the future. Despite a year that should remind us of life's inherent uncertainty, we entered 2021 with bold projections about future stock market returns, interest rate levels, economic reopenings (or closings!), and virus containment.

Rather than make predictions, I am focused on accepting the reality that the future is unknowable. Our job as investors is to make educated decisions while weighing the upside and downside of possible outcomes.

What does this mean to my Partners? I am looking to build a resilient portfolio of businesses that can adapt to a wide range of economic outcomes. First, I want to own businesses that can make money in many environments. Second, I want a margin of safety so that if my expectation of the future is wrong, the downside is limited. Finally, I want stakeholders involved in the business who have deep "skin in the game" and are committed to seeing their business be successful. Things go wrong, but talented people with strong character find a way around inevitable issues.

Portfolio Activity

While we do not make investments with the intention of being short-term, there are times when unique events transpire or material discounts to our view of the intrinsic value of the business close more quickly than expected. There have been two exits worth highlighting in 2021: Lumen Technologies (LUMN) and Canadian

Natural Resources (CNQ). Each position was purchased at a ~50% discount to our estimate of intrinsic value and sold when that discount materially closed.

Lumen was sold after the price increased over 30% in two days of trading. The stock price did not move so dramatically due to a change in the business, but rather it occurred during the first GameStop short squeeze where retail investors caused a raucous throughout the financial markets. Lumen moved from ~50% of our estimate of fair value to ~80%. We took that rapid price improvement and locked in a 43% gain for our investors in anticipation of finding better opportunities down the road.

Canadian Natural Resources – founded by Chairman Murray Edwards – is a best-in-class oil and gas company based in Canada. The competitive advantage is both sustainable and long lasting, with oil reserves that have a useful life of 30+ years vs. US shale producers with much shorter oil well lifespans. This unique asset base enables a self-funding business, which is rare in the energy world and incredibly powerful for equity investors.

After initially purchasing the business for ~$17/share, we sold at ~$30/share. In the meantime, we enjoyed a healthy dividend. The rationale for selling was that oil is no longer "back up the truck" cheap. I do not profess to be the best oil market analyst outside of Texas, but I was astute enough to know that oil will need to settle above the breakeven production rates for much of the world! Our risk reward became skewed in the position from very attractive at time of purchase to quite muted at time of sale.

These sales are indicative of a key point that you should understand about our capital allocation process: Because we are not willing to indefinitely add businesses to our portfolio, we are systematically forced to look at the highest and best use of our collective capital. When businesses have limited ability to reinvest their capital at high returns on investment (both CNQ and LUMN fall into this category), we must closely monitor the discount to intrinsic value. If a business has a very long runway to reinvest capital at high returns, we can be far less precise with the calculation of intrinsic value.

Clearly, owning businesses that can reinvest capital for a long period of time (high quality compounders) is both easier and more lucrative. While we will still purchase businesses that are simply "too cheap," our efforts are focused on owning high quality compounders.

Converge Technology Solutions

I thought it would be useful to highlight a Canadian business, Converge Technology Solutions (CTS.TO), which was introduced to our portfolio as a top five position in Q1. Converge is an IT service provider, helping customers purchase and implement best-in-class hardware, software and managed services solutions. Shaun Maine, the Founder and CEO, astutely realized that mid-sized businesses were underserved from an IT perspective. Converge was recently added to the Toronto Stock Exchange after rapidly growing revenues from C$459MM in 2018 to C$949MM in 2020 and EBITDA from C$20MM to C$60MM during the same time period. Converge remains small and largely ignored by Wall Street, with an enterprise value just above C$1B.

From experience, I can say that running a small-to-mid-sized business can be difficult from an IT perspective. Most leaders know that cybersecurity, cloud infrastructures, and firewalls are important…but we have no idea what to do about these issues! Converge helps fill the IT knowledge void, solving a serious pain point.

Converge is growing both organically and via acquisitions. Since 2017, Converge has successfully acquired and integrated 18 businesses and is on the hunt for more. However, growth only adds value if done in an economically judicious manner. Converge is intelligently utilizing their increasing scale to improve the unit economics of the businesses they acquire and operate.

Let us take an example: A typical single-point business in this industry produces ~3% EBITDA margins. Converge has superior agreements with key vendors, which typically adds ~1.5% to EBITDA margins on day one from volume discounts alone. Cost redundancies with key shared services typically adds another ~2% to EBITDA margins. Therefore, if Converge pays an owner 5.0x EBITDA, it is much more like paying ~2.5x EBITDA. But the "magic" does not end there. Converge can unlock 1-2 years of cash generation by extending working capital terms from 33-66%. It is therefore entirely possible for the cash payback on an acquisition to be just over a year *without* the power of cross selling services across their platform, which is the key long-term organic growth driver.

Converge sits in a structurally growing market (we need *more* technology, not less), works with an underserved piece of this market (their customers *want* their help), and has capital efficient opportunities to grow. However, there are several more ingredients that increase my confidence in the business.

Converge is Founder led and management owns ~10% of the company. Further, they copied a compensation scheme from another Canadian company called Constellation Software (a wonderful business for another day…). Management is required to purchase *actual outstanding shares* of Converge on the open market (not dilutive stock options) and *hold the stock* for an extended period. The alignment with common shareholders is strong and long-term dilution from stock option issuance should be muted. Finally, Mawer is one of the most astute investors in this space and they recently purchased ~10% of Converge. The stakeholders are in place!

An abbreviated checklist: Structurally growing industry, strong market fit, capital efficient growth, founder led, management incentive alignment with common shareholders, strong stakeholders, and a business model that I can personally relate deep experience with. The path is set for wonderful business performance and we were able to purchase this company for less than 10x my estimate of 2021 equity cash flows. Execution risk is high, and there will almost certainly be lots of volatility in the stock price. However, the building blocks to a strong business are in place and we intend to own Converge for many years to come.

Conclusion

As your Partner in all investments, I will remind you that patience is key to winning this endeavor we call investing. I suspect that the road to material outperformance of any reasonable benchmark will be filled with ups and downs. The path to abnormal results *requires* investors to stomach challenges along the way. We intend to be long-term investors and thinkers, focused on the business quality and performance first. Over time, our collective net worth improvement will follow.

We are open to new Partners if they share a long-term mindset and are hungry for sustainable (sometimes slow!) wealth creation rather than focus on short term results. Feel free to share our thoughts with those you believe could fit the bill. In the meantime, we will look for wonderful businesses to buy at a reasonable price.

Appendix: Required Reserves Performance

Several of my Partners as well as myself own what is called a Controlled Foreign Corporation, which functions much like a captive reinsurance business. These entities have a significant portion of their capital in a highly restrictive Investment Policy Statement as mandated by the powers in charge.

With a minimum of 85% of the portfolio required to be held in liquid US based investment grade fixed income, it is not surprising that recent rising interest rates have negatively impacted returns.

Despite this challenge, we put our maximum exposure into preferred and common equity indices as allowed by the IPS, which helped offset some of this pressure. I am not excited to own any source of fixed income today and results are likely to be impaired by the one-sided nature of the fixed income market: rates cannot get much lower but can get much higher. The risk is skewed to the downside.

I still expect that over time we will earn reasonable returns. As more capital builds, more of the funds can be utilized on more lucrative options such as the previously discussed Strategic Opportunities portfolio.

Note that small variations from the benchmark should be expected due to timing of receiving investment funds, which is variable throughout the course of the month and outside of our control. Over time, these should not be material to your investment results.

Total Returns through March 31, 2021	WMKI CFC Required Reserves	Required Reserves Custom Benchmark*
Since December 31st 2020	-2.4%	-2.4%
Since Inception (11/16/2020)	-1.4%	-1.3%

*90% AGG (iSharees Barclays Aggregate Bond ETF)/10% S&P 500 Total Return

Disclosures:

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