OYAT ADVISORS – QUARTERLY COMMENTARY

2Q 2024

<u>Investment landscape</u>

The second quarter of 2024 was generally positive for equities as investors balanced hopes for lower inflation and central bank rate cuts with resilient economic data. Clearly, market sentiment remains driven by central bank actions and the possibility of rate cuts over the course of the year. Investors started the second quarter concerned that the combination of sticky inflation and relatively strong economic data would prevent central banks from cutting interest rates. The global equity market subsequently weakened in April. As the quarter progressed, inflation prints looked more favorable and weakness in key economic components such as US consumer data gave investors comfort that monetary policy easing was again the most likely outcome, and global equity markets rose once more to all-time highs. In the meantime, fixed income markets remained flat-to-down, perhaps reflecting the underlying nervousness of market participants regarding the imminence of rate cuts, despite early downward adjustments by the Swiss National Bank and the European Central Bank.

The guessing game will likely continue through the second half of the year as investors modulate expectations for rate cuts as fresh data on inflation and economic progress hit the headlines. Weaker economic data may raise hopes for lower rates, but it will also heighten fears of a recession and increasing pressure on fragile government finances. So far, old narratives have continued to hold with strong performances from large U.S. technology companies driving global growth stocks to the top of the heap in terms of performance in the second quarter. Stocks linked to artificial intelligence persisted in their efforts to drag indices up as well. Artificial intelligence darling Nvidia climbed nearly 37% in the quarter, stretching the bounds of market concentration and the relevance of valuation.

We don't need to reinvent the wheel and add yet more text to the flood of commentary on companies like Nvidia, but we do find the situation quite fascinating in the context of history as pointed out by Christopher Bloomstran of Semper Augustus, whose commentary in late June offers valuable perspective on today's markets:

"Stunning. Nvidia passes Microsoft and Apple as largest market cap. Combined, the three are valued at $9.9 trillion, 21.5% of the entire market capitalization of the S&P 500. The three are today LARGER than the capitalization of the ENTIRE S&P in September 2011, not a market low. Including Google, Amazon, Meta and Tesla, the Magnificent 7 have a $16 trillion combined market value, 34% of the S&P 500 and LARGER than the ENTIRE S&P as recently as February 2016, just over 8 years ago and most definitely nowhere near a market bottom. Nvidia is valued at 42x and 78x trailing sales and earnings on an unsustainable 54% net profit margin. Microsoft is valued at 14x trailing sales and 39x earnings on a 36.4% net margin. Apple is valued at 8.6x and 33x trailing sales and earnings on a record 26.3% net margin. These are crazy valuations for very large companies that can grow sales and earnings nowhere near as rapidly as they did over the past one and two decades. Microsoft and Apple traded for less than 10x earnings at various points over the past 20 years.

This is the goofiest and likely most dangerous concentration of overvaluation I've seen in 34 years investing and throughout financial history. Mr. Market is very good at rewarding business success but to a fault. In the short term, stocks can trade at extremes relative to fundamentals, both on the low side and the HIGH side. At 23x 2024 expected earnings, the market-cap weighted S&P 500 is froth with excess and in my judgment uninvestable. Under the hood, the majority of stocks are not overvalued. The bifurcation between the dear and the cheap reminds me of March 2000. From that point the index has returned 7% per year, spending much of the subsequent decade in the red. You can have extremes of over or undervaluation in the short and even intermediate terms. But in the long run, Mr. Market gets it right."

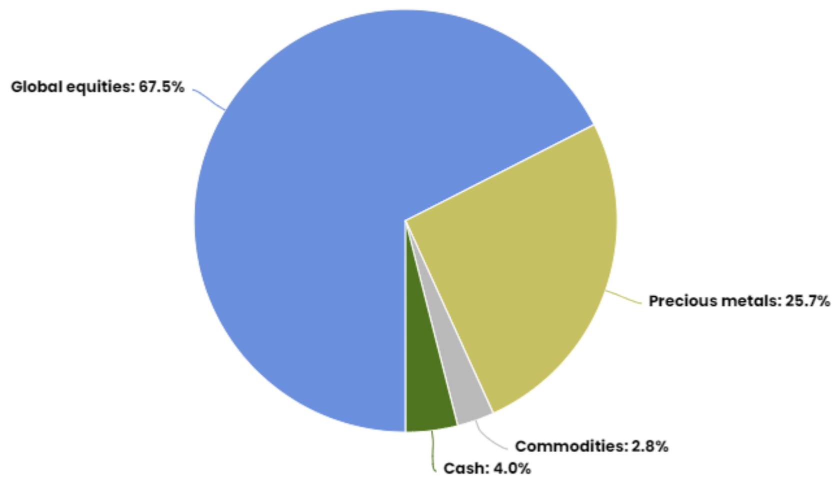
Extreme concentration and valuation metrics should give investors pause and prompt a review of how diversified holdings really are considering the dominance of a handful of companies in the major indices. Timing markets is difficult, and market darlings can drop as precipitously as they rise once achieving such lofty valuation levels while being dependent on what some experienced investors might refer to as goofy expectations. We might also highlight Mr. Bloomstran's mention of a bifurcated market and the observation that many stocks are not overvalued. With investors guessing at the number of rate cuts and riding large capitalization growth stocks to 42x sales and beyond, we prefer to plod along holding a diversity of high-quality companies trading at attractive valuations. And we do continue to find high-caliber firms that the market seemingly forgot to drag up to stretched valuations. Avoiding the dangerous concentration of overvaluation while owning companies with valuations more than supported by their fundamentals may very well be the leading narrative of the next decade of stock market returns.

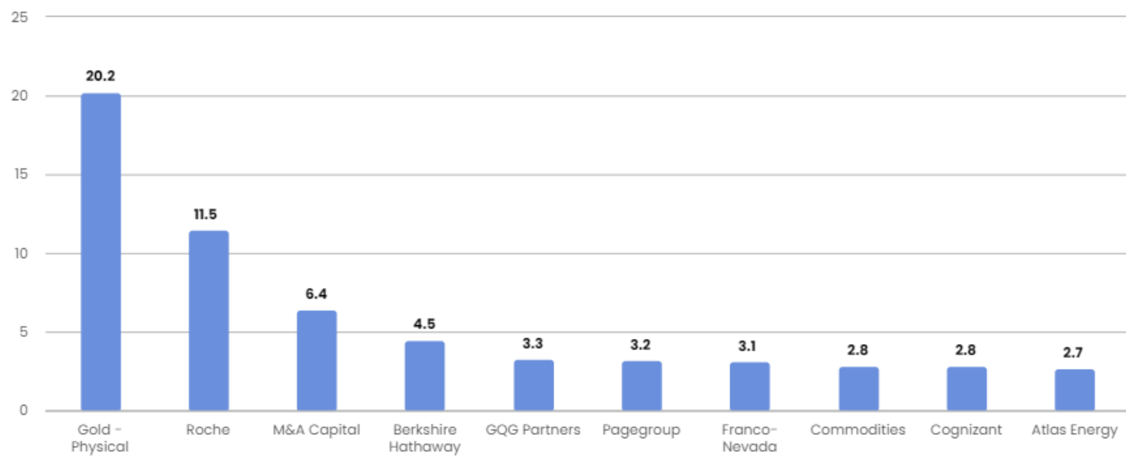
In the meantime, there is another fixture of the second quarter's performance worth mentioning. Gold more than held its own against equities in the period, up nearly 3% in USD. Gold reached new highs in the quarter and ultimately sustained high price levels. Continued geopolitical strife or the political turbulence we see in countries such as France may underpin continued strength in the gold price, but ultimately its status as a portfolio diversifier and proven role as a store of value in relation to ever crumbling fiat currencies offer the real incentive to have a material allocation to the asset class.

Ultimately, the second quarter was a balancing act between hopes of rate cuts intertwining optimally with benign economic conditions and fears that the continuing narratives of artificial intelligence and U.S. big technology growth can't hold up their bubbly track records forever. Predicting interest rates and inflation is often a fool's errand, as is knowing how geopolitical events will play out in these rapidly developing times. We remain humble regarding our ability to predict when 'dangerous concentrations of overvaluation' will reverse themselves or when valuations will once again need to rest upon reasonable fundamentals. But we also remain steadfast in our belief that owning scarce and productive assets with a focus on quality businesses trading at reasonable prices will drive admirable risk-adjusted performance over the long-term. A reasonable level of liquid reserves, predominantly in the form of physical gold, serves to optimize the risk profile while offering option value should the market provide exceptional investment opportunities in the quarters to come.

Asset allocation

The graphs below display the Oyat Investment Fund's allocation of capital across asset classes, as well as the Fund's top-10 positions:





Performance

Performance as of June 30, 2024, in CHF

	3m	1yr	3yrs p.a.	5yrs p.a.	Since inception p.a.
Oyat Investment Fund	1.5%	9.0%	-	-	5.6%
MSCI World	2.5%	21.2%	-	-	16.9%

Annual performance as of June 30, 2024, in CHF

	2022*	2023	YTD	Cumulative
Oyat Investment Fund	-2.4%	3.0%	8.7%	9.2%
MSCI World	-5.0%	13.3%	19.6%	28.7%

**Inception Date: November 10, 2022*

In the second quarter of 2024, the Oyat Investment Fund returned 1.5% in CHF, versus 2.5% for the MSCI World Index. Since inception, the Fund's total return stands at 9.2% vs. 28.7% for the aforementioned reference index.

Physical gold once again contributed positively to the Fund's performance this past quarter. The yellow metal, which we consider as the ultimate reserve asset, given its scarcity, permanence, and the fact that it carries no counterparty risk, rose to new all-time highs in the quarter before settling at an elevated level. The choppiness of central bank buying contributed to some degree of volatility in the gold price, but there are several underlying factors supporting gold's value such as high debt levels and budget deficits, monetary policies that remain far from highly restrictive, growing worries about inflation, and rising geopolitical tensions. Overall, physical gold is continuing to fulfil its function in the portfolio construct admirably, and the time has not yet come to consider exchanging a portion of it for other assets.

Hargreaves Lansdown, Roche and GQG Partners were among the largest positive contributors to performance in the quarter as well. We accumulated Hargreaves shares in late 2023 and early 2024 as the price fell due to some degree of cost mismanagement. We felt that the market was significantly undervaluing the UK's leading investment platform as management sought to get things back on track. Ultimately, a private equity group seemed to agree with us and made an offer to take the company private. We benefitted from the accelerated realization of our view on the company's fair value and trimmed our position later in the quarter. The takeover is not yet complete, and there is some chance for competing bids to materialize.

Roche's share price has been on a downward trajectory for some time, but reversed direction starting in May. Investors are likely starting to see through the top-line pressure from the decline in COVID related sales as well as the easing of currency headwinds. Roche's underlying base business is growing nicely while its leading research and development machine continues to

work away. And 2024 is shaping up to be the biggest launch year in the diagnostic unit's history. We maintain a sizeable position in the Swiss pharmaceutical leader and continue to view shares as materially undervalued.

GQG Partners continued its stellar performance in the quarter. The global asset management firm continued to impress with its very rapid growth in assets under management and its history of outperforming funds. The steady and rapid share price appreciation has chipped away at the upside to fair value, but the company remains a hold as its momentum continues.

Trading activity in the quarter was elevated by our standards and is perhaps more important than performance details. We divested of two positions in the period, Hibbett Sports and Alphabet (Google). Hibbett Sports is a leading sporting goods retailer which we purchased in January at an attractive valuation, just for it to be taken over by JD Sports four months later. We gladly booked a quick gain of well over 30% but find the transaction bittersweet as we feel Hibbett is potentially worth more than the amount offered. Alphabet is a position we held since the launch of the Fund and now sold after a price appreciation of approximately 60% pushed it toward our fair value estimate for the company. Additional funds were created through a number of trims as companies such as Hargreaves Lansdown, Atlas Energy Solutions, Focusrite, Omnicom, Berkshire Hathaway and SGS moved toward our fair value estimates, and we found compelling investment cases elsewhere.

The quarter was certainly unusual for our style of low-turnover fund management as we added five new positions to the Fund in the period, including Ambev, Jeronimo Martins, SHIFT, TechnoPro and JAC Recruitment.

Ambev and Jeronimo add defensive consumer staples companies to the Fund in a deliberate effort to detach part of the Fund from the economic cycle with companies that have an impressive value creation profile and share prices that have overcorrected in relation to their fundamental performance.

Ambev was essentially created by private equity group 3G in 2000 when it merged two Brazilian brewers; Brahma and Antarctic. The company went on to build a Latin American beer empire as it bought up brewers throughout Central and South America and now holds several monopoly-like positions in large markets, including over 60% volume share in countries including Brazil, Argentina, Peru, Bolivia, Uruguay, and El Salvador. Brazil is Ambev's largest market, representing approximately half of the company's business and is also home to its headquarters. Ambev's main business is clearly beer with brands such as Skol, Brahma, Antarctica, Quilmes, Labatt, Presidente and others. But the company also deals in soft drinks and non-alcoholic beverages with top brands such as Guaraná Antarctica and Fusion. Ambev also has a partnership with PepsiCo and currently owns the exclusive rights to bottle and distribute several Pepsi products in Brazil, including brands such as Pepsi, Gatorade, H2OH! and Lipton Iced Tea. Combined with a strong balance sheet and attractive dividend, Ambev ticks several key boxes for investors interested in a high-quality investment option outside the US market. But investors must be wary of the substantial currency risk which may also continue to dampen growth in USD terms as it has over the past decade. Latin American economies are also linked with commodity risk as well as a multitude of political and macroeconomic risks, including proposed changes to Brazilian tax regulation. But the share price has been more than cut in half from pre-COVID pandemic levels, and we feel that the risks to Ambev's investment case are, to a substantial

degree, baked into the current share price, resulting in an attractive valuation that offers skew to the upside in terms of possible outcomes.

Jeronimo Martins provides another interesting investment option in the defensive consumer staples industry with its food retail and distribution businesses and solid track record of execution. Jeronimo Martins was founded in Portugal over 230 years ago but has grown rapidly behind its Biedronka brand of grocery stores in Poland which has carved out a leading position in the country. More recently, the company has penetrated the Columbian market with its Ara branded stores. Its combination of high return on invested capital and reasonable growth offers a ripe opportunity for investors on the lookout for high quality businesses. We particularly like the family ownership and strategic focus on capital allocation while also returning capital to shareholders through a reasonable dividend. The solid balance sheet is a prerequisite from our perspective. The investment case is not without substantial risk, however, as the economic trajectory and political future of emerging markets such as Poland and Columbia are difficult to predict, as is the ultimate profitability potential of the company's ramping Columbian business. Foreign exchange risks are also palpable. But our view on valuation, with what we see as conservative growth and profitability assumptions, provides an adequate margin of safety for such a quality business, despite the risks.

In addition to Ambev and Jeronimo Martins in the consumer staples industry, we added positions in three smaller-cap Japanese companies in the second quarter while also adding to our Japanese holding in M&A Capital.

SHIFT is a Japanese software testing company. Established in 2005 by Masaru Tange (President and CEO), SHIFT has grown at a rapid pace since its founding, with a massively impressive CAGR in sales of 51% between 2015 and 2023. Sales for fiscal 2024 are expected to grow approximately 30% year over year. With its ambitious goal to grow sales to JPY 300 billion by 2030, SHIFT aspires to continue to grow at a CAGR of 15-20% on the back of a structural move from companies to outsource more and more software testing to save precious engineer time for development tasks. SHIFT's success is no accident. The founder successfully identified a market need for better software testing tools and the opportunity to disrupt the multi-layer subcontracting structure of the software development process in Japan. SHIFT built a large database of software bugs and built a system to detect and address all of them. The company also developed a leading educational program for identifying and training qualified personnel which helps keep SHIFT ahead of the competition and assist in client staffing. We expect SHIFT to continue to ride industry tailwinds and dominate market share with its leading solutions in the software testing industry. Our current valuation relies on continued growth but also builds in a margin of safety versus the company's own targets. SHIFT has been a performance detractor since its addition to the Fund, partially due to currency headwinds, but the investment case remains on track.

TechnoPro was also added to the Fund in the second quarter. TechnoPro is a leader in the Japanese engineer staffing market and has an impressive track record of double-digit growth and high teens return on invested capital. The company employs the largest pool of talent in its industry niche with perhaps the most respected training and development program in its segment, busy enriching the careers of over 300,000 individuals a year. The company's history of private equity ownership instilled a culture of disciplined financial control which continues through the company's KPI driven measurement protocols and a keen eye for value creation. The

company's financial profile is supportive with a net cash position and capital allocation split between the dividend and growth initiatives. Historical financial results speak for themselves, and we see little reason why the company can't continue to grow in the mid-single digit range with stable, if not improving profitability levels. If the company can achieve our base case valuation assumptions or even its more aggressive internal growth targets, we'd expect an attractive level of shareholder return for investors aware of this promising Japanese small-cap company.

And finally, we come to another quality example of a Japanese founder owned and operated company, JAC Recruitment. JAC has a long history as a highly effective participant in the recruitment industry, both in Japan and abroad. The company's ability to construct a leading team of recruitment professionals with expertise on the employer and employee sides of their business has helped build a solid reputation in the market and create some degree of competitive advantage. JAC's history and skills regarding foreign markets and what it takes for Japanese companies to move abroad or vice-versa makes the company particularly competitive in that segment of the market. JAC's track record and network in the executive and high-income area of the recruitment industry have also allowed the company to carve out a lucrative market position that should persist for years to come. The company's financial results are testament to its strong execution over the past decade, having achieved a CAGR of over 15% with an average return on invested capital of 30%. We see little reason why the company shouldn't continue to produce double-digit growth while maintaining return levels in the years to come, as is forecast by the company itself, but there are several key risks. The company may prove to be more cyclical than expected should there be a meaningful downturn in its markets. JAC will also need to continue to retain, attract and train talent if it is to meet its growth targets, something that is increasingly challenging in Japan's tightening labor market. But ultimately, the combination of JAC's strong industry positioning, a long runway for growth, respectable capital allocation from the company's founders and a clear ability to turn revenue into cash in admirable fashion, have us convinced that JAC Recruitment is an attractive company to own. Our current valuation assessment shows substantial upside while one might also speculate that the founding Tazaki family will search for a strategic partner over the mid-term. All in all, this small-cap Japanese recruiting company makes a strong case for investment, especially for those valuing a combination of growth and return on invested capital.

Before closing, we will mention a couple additional performance detractors. M&A Capital has continued to trickle down after several quarters of mediocre results and some currency headwinds, but our confidence in the investment case and what we view as substantial undervaluation is confirmed by incremental purchases in the quarter, increasing what was already a sizeable position in the Fund. Thor Industries was also weak in the second quarter as the recreational vehicle market in the US remains challenged on the back of higher interest rates and a cautious consumer. We fully expect the industry leader to recover swiftly as soon as its end markets improve.

Ultimately, the second quarter was a period of continued positive performance. We remain convinced that the Fund's collection of quality companies at attractive valuations, complemented by a healthy dose of precious metals exposure, is the optimal setup to navigate today's complicated markets.

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