Intelligent Cloning

The Autumn 2021 Edition

If you have to squeeze out every drop of risk before investing, there won't be any fruit left.
— Tom Gardner.

Great investment results can be achieved simply by copying great investors. Don't try to be the smartest ass around. Start copying the great ones. It's an approach called "cloning". I have practiced it for many years now. Cloning works!

According to Profs. Gerald Martin and John Puthenpurackal's study from 2008, "Imitation Is the Sincerest Form of Flattery," investors would have earned an average annual return of 24.6% for 30 years, simply by buying what Buffett bought. Better yet, this annual rate of return came from buying the stocks after Buffett had disclosed them in regulatory filings.

There are so many great ideas to copy. It's actually hard work to copy just one or two ideas a year! And it is most certainly not easy. A great place to look for compelling ideas is dataroma.com, as is thevalueinvestorsclub.com. And if you've been around long enough in this business, you will find exceptional "under the radar screen investment managers", with outstanding long-term track records. Also, a very compelling hunting ground.

Here is a great list of clone-worthy investors. I got it from a tweet from Brad Kaellner, who runs an entertaining and valuable YouTube channel on investing, cloning, etc.

Investor	Fund	Years	Compounded Annual Gain	AUM
Warren Buffett	Berkshire Hathaway	55	20.0%	$627b
Bill Ruane	Sequoia Fund	51	14.0%	$13.7b
Prem Watsa	Fairfax Financial	35	15.0%	$11.1b
Daniel Loeb	Third Point	25	15.1%	$17.6b
Andrew Brenton	Turtle Creek Asset Mgmt	22	20.6%	$2.8b
Li Lu	Himalaya Capital	19	19.4%	$18.6b
Bill Ackman	Pershing Square Holdings	17	17.1%	$14.5b
Rob Vinall	RV Capital	13	19.8%	$473m
Jason Donville	Donville Kent Asset Mgmt	13	17.8%	$270m
Justin Dopierala	Domo Capital Mgmt	13	23.0%	$47m
Chuck Akre	Akre Capital Mgmt	12	17.0%	$17b
Terry Smith	Fundsmith Equity Fund	11	18.9%	$38.4b
Matt Peterson	Peterson Capital Mgmt	10	19.4%	$10m
Scott Miller	Greenhaven Road Capital	9	21.0%	$595m
Cliff Sosin	CAS Investment Partners	8	37.0%	$2.4b
Fred Liu	Hayden Capital	7	33.6%	$61m

For those of you who have the right mental makeup to handle stock market volatility intelligently, here is your ticket to financial freedom: just copy the best of them. Cloning works!

More so, Brad came up with a list of investors on Twitter with killer returns since fund interception:

- ✓ @Adam_Wyden
- ✓ @AltaFoxCapital
- ✓ @Anrosenblum
- ✓ @bradsling
- ✓ @CliffordSosin
- ✓ @DOMOCAPITAL
- ✓ @GreenhavenRoad
- ✓ @HaydenCapital
- ✓ @LaughingH20Cap
- ✓ @MattPetersonCFA
- ✓ @SagaPartners

Thank you, Brad!

Here is the newest addition to the Intelligent Cloning Portfolio: the **Daily Journal Corporation (DJCO)**. I copied it from Zürich-based investor Guy Spier. At first sight, you might question if the Daily Journal Corporation is indeed this unique outstanding company that has the ability to build a dominant market position in its niche and hold on to that position for many years to come, but after studying an investment thesis on this company, written by Matthew Peterson of Peterson Capital Management, I decided to invest.

Matthew rightfully points out that this investment opportunity is totally misunderstood and makes the case that the Daily Journal Corporation is an undervalued microcap compounder in a huge space for sustainable, long-term growth. You can find his presentation on YouTube. I like the "deferred gratification ethos" part of it. And yes, of course, there are risks to consider. But you know, if you have to squeeze out every drop of risk before investing, there won't be any fruit left.

Another company in the Matt Peterson portfolio is Seritage Growth Properties (SRG). Interestingly enough, during his annual meeting he lays out the returns his fund generates by selling cash secured put options @ 15 USD on SRG. Heads, the stock goes up, and he wins by pocketing the premium, and tails the stock goes down, and he cuts 4.50 USD off the price of the stock he wants to own anyhow. I just might give that a go as well.

Investing Robots

In the Summer 2021 Edition on Intelligent Cloning I introduced "The Wizard Portfolio." It's a fully automated stock picking approach with a set of rules for buying and selling. What you are trying to do is building the ultimate compounding machine, or **investing robot** if you will, that leverages technology, in terms of algorithms and data analysis, as "the great enabler" in long-term compounding & investing.

Up until now, the results are compelling. Let me remind you though, that, although very well back-tested, this remains an experimental approach, or just an attempt if you will, to show that "machines" can outsmart "humans", also in the world of investing and long-term compounding.

Here are the investment returns of the constituents of the "June 2020 basket of stocks" of "The Wizard Portfolio" as per 1 September 2021:

Company	Return
Medifast	107%
Ulta Beauty	55%
XPEL	390%
Domino's Pizza	37%
Nova Ltd	106%
Fortinet	125%

The average return of this June 2020 basket is 102% over the first 14 months. Can't wait to find out if this investing robot ultimately works. We'll know 25 years from now. Surprisingly, I never imagined that when I started my company, I would end up in **The World of Investing Robots**. Pretty cool, actually.

The goal is a consistently high rate of compounding, with more emphasis on "consistently" than on "high". For those of you who are familiar with the power of compounding, it's obvious. But it still surprises me how many are still unfamiliar with it.

There is an often-told story that when Albert Einstein was once asked what mankind's greatest invention was, he replied: "Compound interest". There's even one claim that Einstein called compound interest the "8th Wonder of the World." If you are able to compound your money at 15% over a 50-year period, you will turn 10.000 USD into 10 million USD.

"The Wizard Portfolio", actually the result of an investing robot with a buy-and-hold approach, unfortunately, doesn't have a multi-year real time track record as of today. But there is a completely different breed of investing robots that, by the end of this year, will have a 4 year research track record. In my previous writings, I referred to them as "quants", and to be more specific, the "United States New Year Quants" Q5 to Q11. These are not buy-and-hold robots, but these robots "refresh" their constituents once a year.

I couldn't resist the temptation to have a sneak preview. If by the end of this year the stock prices remain the same as the stock prices per 1 September 2021, then the least performing robot generates a gross **20% CAGR** over 4 years and the best one a gross **32% CAGR** over 4 years.

Unfortunately, there are no "sure things" in investing, but one might be tempted to believe that these investing robots actually work. I will continue pioneering investing robots and I am looking forward to presenting the latest results in the next Edition on Intelligent Cloning.

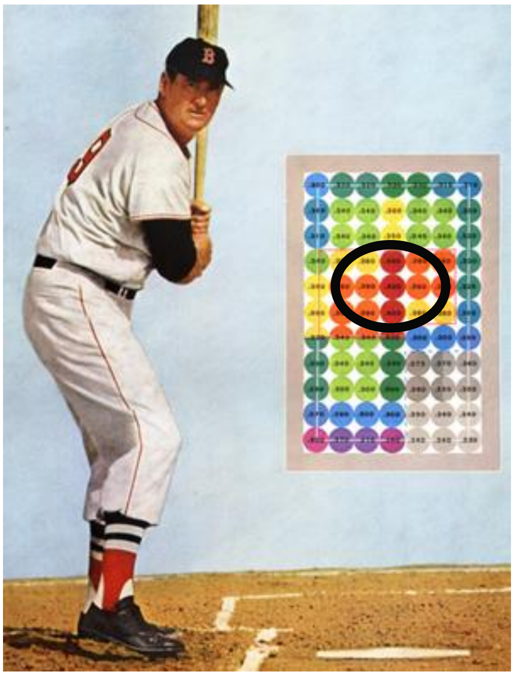
The Multi-Bagger Candy Store

In previous editions on Intelligent Cloning, I wrote a lot about this "algorithm" that identifies **Hyper Value Creators**, regardless of valuation or market cap. What makes this algorithm interesting and unique in comparison with, for instance, typical Buffett-Munger screeners, is that there is lots of additional **multi-bagger back test intelligence** in it.

Let me give an example of what this algorithm can do for you. During the 2021 MOI Global Wide Moat Summit, Ben Beneche of Pictet Asset Management, gave a presentation, entitled "Extreme Returns in International Equities". Looking at the highest performing stocks over the last ten years, the algorithm was able to identify 28% of the multi-baggers from China and Hong Kong upfront, i.e. in 2010.

When you look for multi-bagger stocks, I believe valuation and market cap should come into play. What you preferably look for is the “sweet spot” of substantial, sustainable and profitable revenue growth, e.g. from 50 to 100 million USD in just a few years. And if such a company trades at a reasonable valuation, that’s when you pull the trigger.

This idea of a “sweet spot” reminded me very much of the analogy Warren Buffett uses, when he talks about Ted Williams and his “strike zone”. Ted was, without a doubt, the greatest pure hitter in baseball history. He believed that if he waited for a pitch in his sweet spot, he would hit the ball roughly 40% of the time. However, if he became impatient and swung at pitches that were just a few inches outside of his sweet spot, he would only hit the ball about 23% of the time. His secret? Williams attributed his great success to his rule of “**Waiting for the Right Pitch!”**



Warren Buffett often makes reference to Williams’ “sweet spot” and draws close parallels to decision-making in investing. The trick in investing is just to sit there and watch pitch after pitch go by and wait for the one right in your sweet spot.

This “sweet spot” of decision-making, your **circle of competence**, was first referenced in Buffett’s 1996 Berkshire Hathaway Shareholder Letter where he wrote that, “You don’t have to be an expert on every company, or even many. You only have to be able to evaluate companies within your circle of competence. The size of that circle is not very important; knowing its boundaries, however, is vital.”

What the **Multi-Bagger Search Engine**, which is actually an extension of “the algorithm that generates Hyper Value Creators”, does is look for Hyper Value Creators in the “strike zone”, where the “strike zone” is further defined by a company with revenues of between 30 and 300 million USD, or perhaps even 500 million USD, and a price-to-sales multiple of 4 or less. And that’s exactly the “striking zone” used to identify XPEL as an investment opportunity.

Here is an example, or potential multi-bagger if you will, from the Australian Multi-Bagger Candy Store: Kelly Partners Ltd. (See attachment).

So here we are

Finding tomorrow’s star growth stocks today is not easy. There is, I believe, a sliver of high quality potential multi-bagger stocks, like XPEL, that can be “screened”. And that’s where the **Multi-Bagger Search Engine** comes in handy. Unfortunately, most of the potential multi-baggers can not be screened. The Daily Journal Corporation is such an apt example. As Charlie Munger, the current CEO, pointed out: “You can’t look at our financial statements and make very good judgements about what’s going to happen.”

What you are looking for is the certainty that the company has the ability to grow consistently for many years to come, preferably decades. While most investors think of the Daily Journal Corporation as a dying public notice daily paper, the business carries an impressive high-growth, operating business: their SAAS Justice System Technology, that’s currently being rolled out. The true economic value of these “hidden assets” is, I believe, completely overlooked by investors.

Finally, a note of caution. What goes up, must come down. If you ignore the COVID-19 crash for a moment, you could argue that we are experiencing one of the longest bull markets ever. It will end somewhere. We've reached the 18th month of the COVID-19 pandemic, a somber milestone marked by yet another surge of cases and deaths fueled by the Delta variant. This global crisis has been a health, economic and moral disaster playing out in waves in every geography, sparing none. Jim Rogers believes that the "worst bear market of our lifetime" is nearing fast.

So be careful out there. It makes, I believe, a lot of sense to put some money on the sidelines, to be able to invest when the markets indeed go down.

Thank you for reading my letter. Stay safe!

Peter

Peter Coenen
Founder & CEO
The Value Firm®
30 September 2021
E-mail: peter@thevaluefirm.com

Post scriptum. Here is THE LINK to John Elkann and Elon Musk's debate about the future, when technology and innovation increase human possibilities.

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Everybody makes mistakes now and then. If you find any, let me know: peter@thevaluefirm.com. Always do your own research!

Kelly Partners Ltd

Brett Kelly founded Kelly+Partners in 2006 with a big idea: “to help private business owners be better off”. It’s a simple but powerful concept that underpins the fundamental requirement within small and medium enterprises for a strong and committed financial services partner in order to realise their professional and personal goals.

In the 11 years since formation, Kelly+Partners has grown to become one of the largest accounting networks in the Greater Sydney area, with a primary focus on private SMEs and their owners. Growing from two initial start-up businesses in North Sydney and the Central Coast, Kelly+Partners now has 16 Operating Businesses spread across 12 locations in Greater Sydney and 1 office in Hong Kong. During this period, they have transformed 14 external practices and created 9 greenfield offices, in order to build the existing owner-driver accounting network. This includes 3 specialist Operating Businesses in tax consulting, wealth management and strategy consulting. The Australian accounting industry is a A$20 billion per annum revenue market, and demand for accounting and taxation services is driven by the increasing complexity of the Australian tax system. However, the accounting market is highly fragmented in terms of the number, scope and quality of providers. Services to SMEs comprise approximately 60% of the market, and are typically under-serviced by a myriad of small private practices which are often facing a number of internal & external challenges.

Brett Kelly, Founder, Executive Chair, Chief Executive Officer

Brett is the founder and CEO of Kelly+Partners. He has more than 20 years commercial and professional accountancy experience, specialising in assisting private clients, private business owners and families.

He commenced his career as a Chartered Accountant with 5 years at Price Waterhouse, and then worked at 3 mid-sized accounting firms. In 2006, Brett founded Kelly+Partners with accounting businesses in North Sydney and the Central Coast, before building out the network to 22 businesses over 15 locations to date.

Brett is also the best-selling author of four books on life, business and wisdom.

The Value Creation Engine (VCE) is a for growth adjusted return on capital (ROC) measure. The fine tuning of this measure was done by lots of research and back testing on multi-baggers.

The FCF Margin is the free cash flow margin, where the free cash flow is defined by the operational cash flow minus the capital exenditures (capex).

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