AIM

Sydney Probus

March 2021

AIM is a global equity investment manager with a single focus: to sustainably compound wealth over time by investing in high-quality businesses.

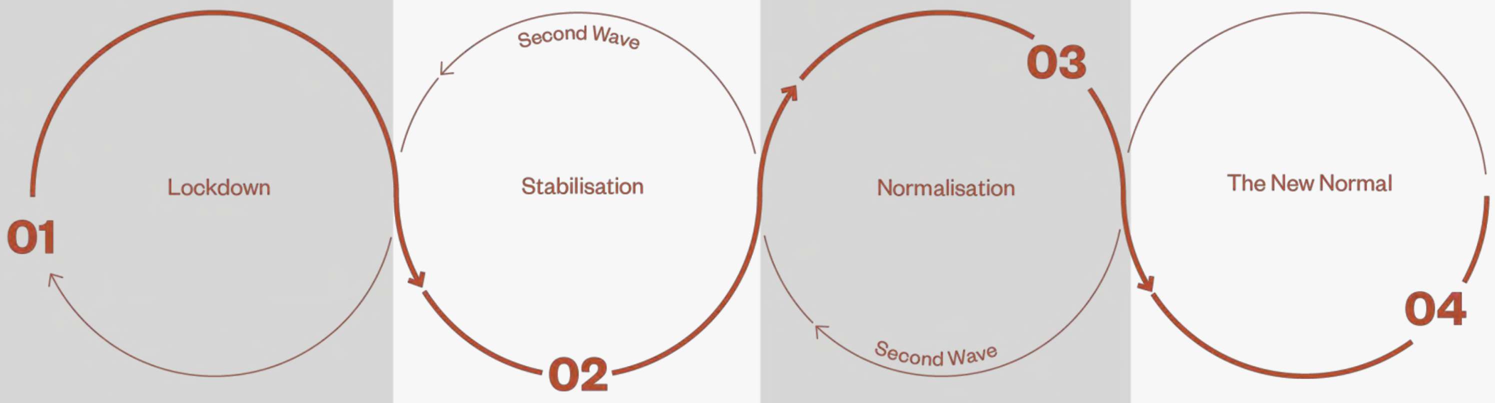
About AIM

- Founded in 2015, an independently owned boutique investment manager based in Sydney.
- All effort is concentrated behind a single investment strategy, managed as the **AIM Global High Conviction Fund**
  - Long-only equity, with a mandate to be between 90% - 100% invested
  - A concentrated portfolio of businesses with strong competitive advantages, robust balance sheets, superior returns on invested capital and long term growth prospects.
  - Removed shorting and moved to currency unhedged position in early 2019.
- Designed to bring global equity investment opportunities to Australian investors

Setting the Stage- A Phased Recovery

Where are we?

- Global roll out of highly efficacious vaccines now underway.
- Approaching "Normalisation Phase", but the recovery will remain bumpy. There are bound to be setbacks in distributing and administering vaccines on a global scale. Look out for air pockets.
- Unprecedented fiscal and monetary support.
- The big unknown that could change everything? Inflation.



- Social distancing, work from home
- Normal out-of-home economic activity substantially impacted
- Buys time for coordinating public health response

- Less severe social distancing
- More mobility leads to pick-up in some economic activity out-of-home, but focused on essentials
- Active public health interventions in place

- Social distancing rules relaxed
- Non-essential out-of-home economic activity recovers, though to lower levels than pre-crisis
- Public health risk has been substantially addressed

- Public health risk successfully managed (vaccine)
- Initially, a recession - length uncertain, but deep
- Longer term questions:
  - What behaviours have changed permanently?
  - What trends are reinforced/broken?
  - Social or geopolitical changes?
- Own businesses that will grow market share or benefit from changes (or both)

Companies that benefit

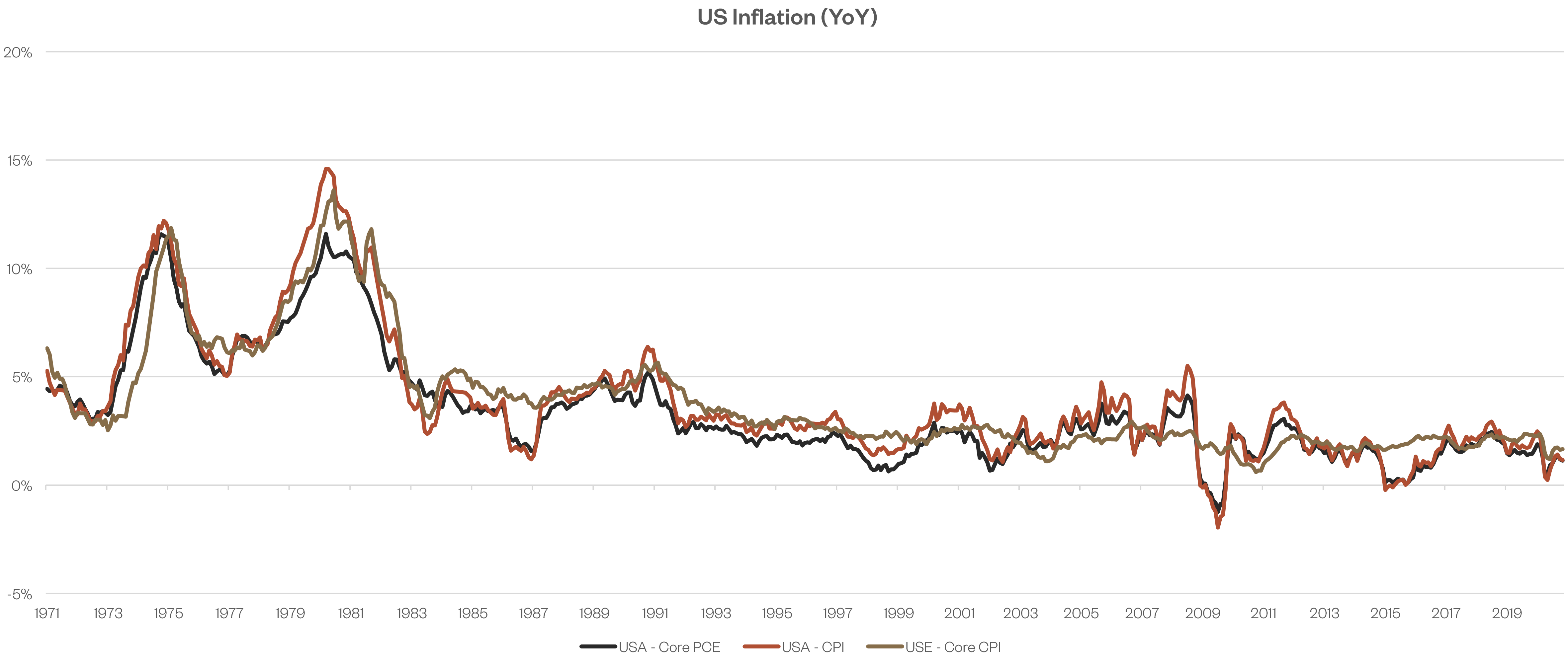
amazon NETFLIX Microsoft

mastercard NIKE ICON

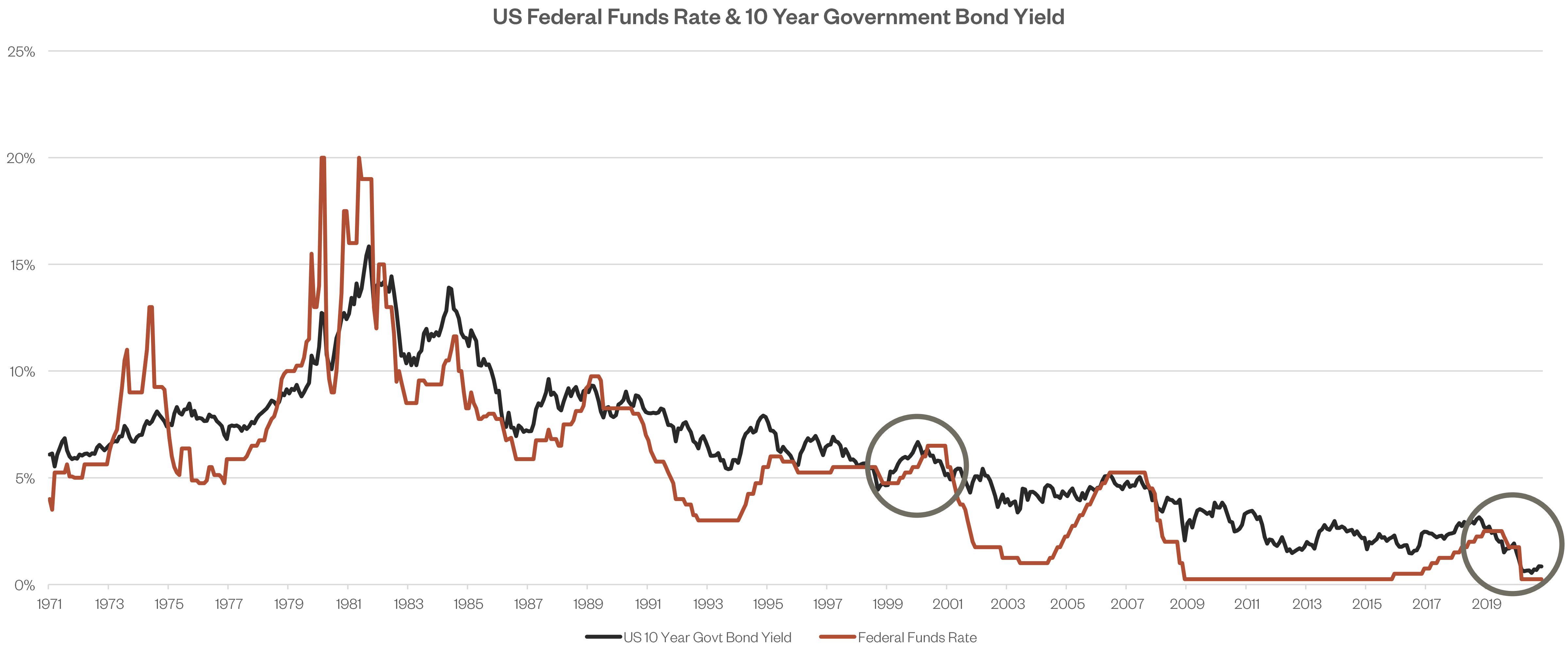
Coca-Cola Berkshire Hathaway Inc. Alphabet

Intuitive Surgical accenture KEYENCE

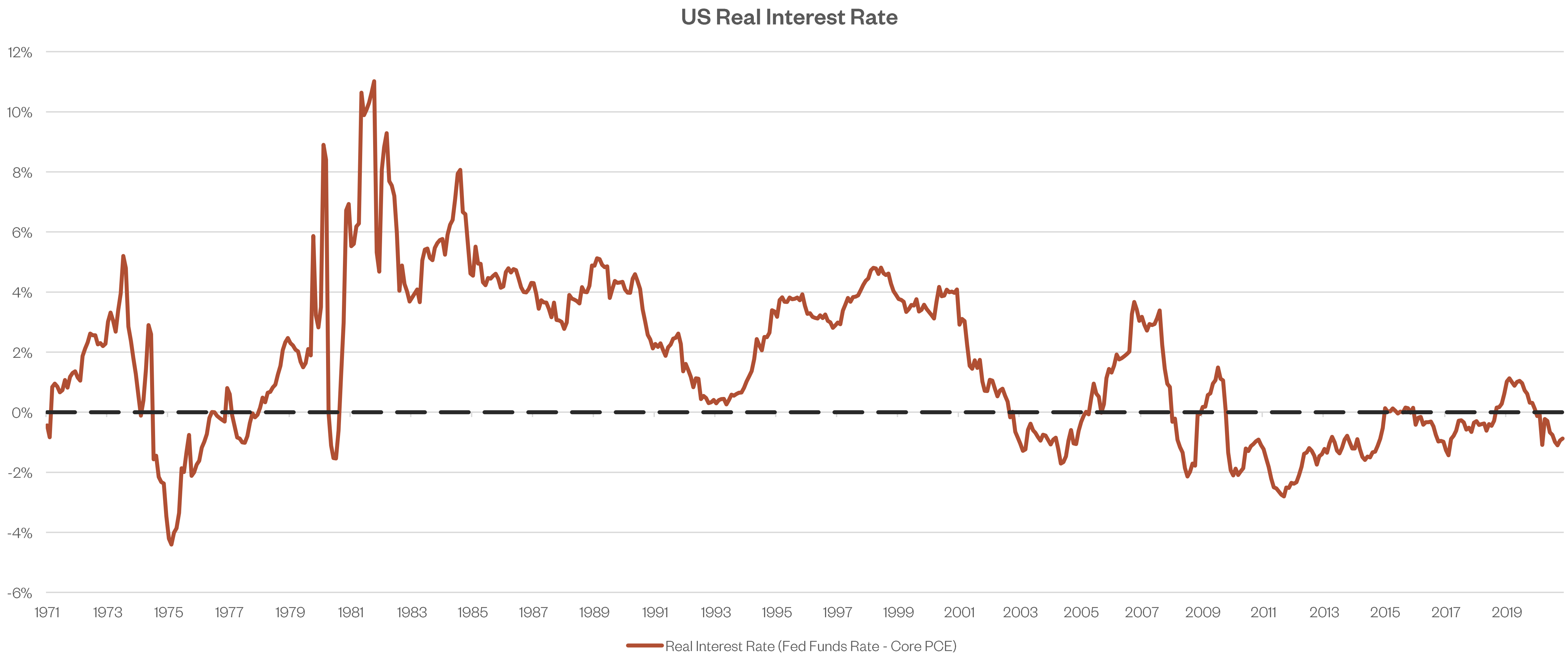
Risks Unexpected Inflation



Risks Unexpected Inflation



Risks Unexpected Inflation

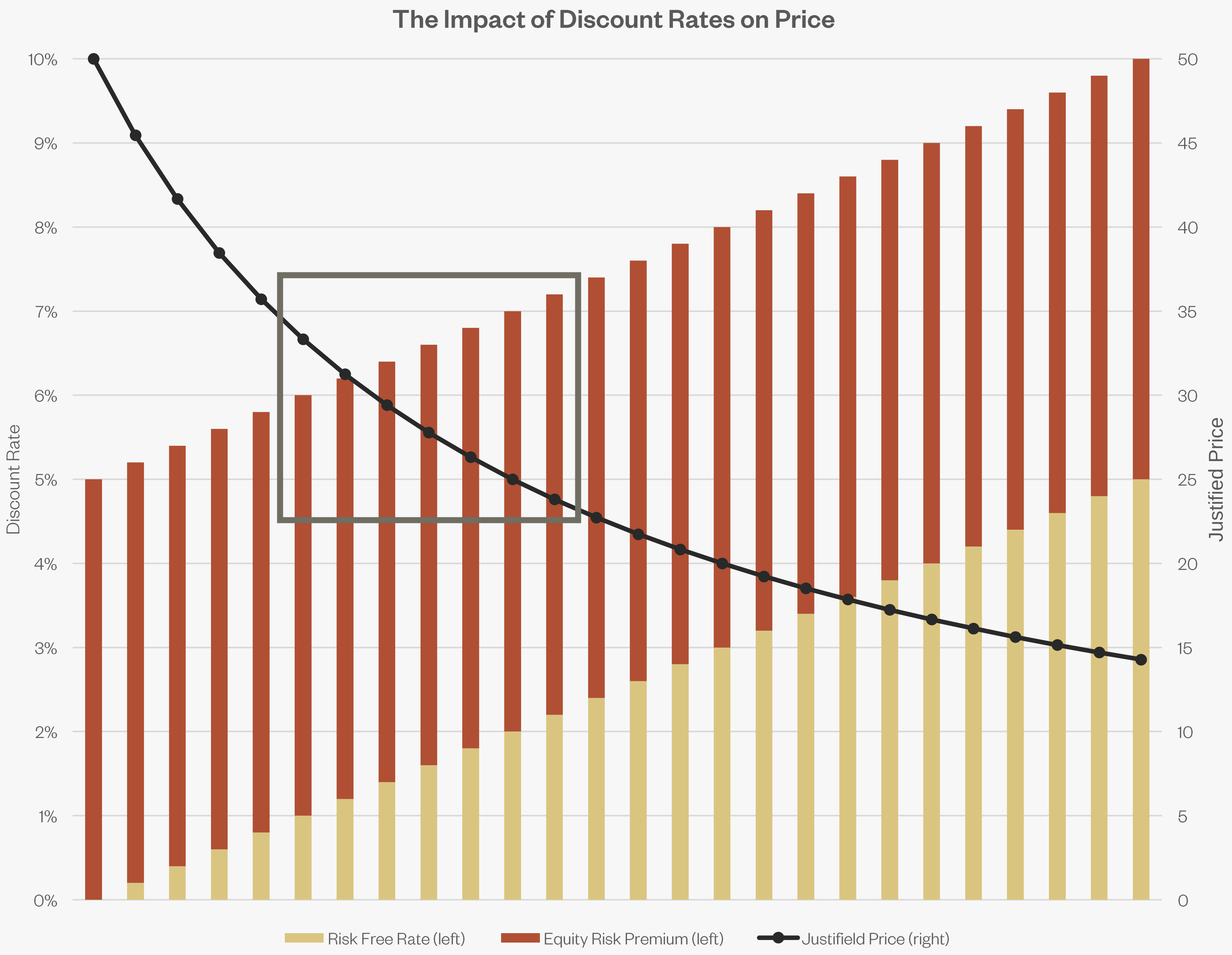


Risks

Unexpected Inflation

Risk #1: market risk

- If inflation moves unexpectedly higher, central banks may be forced to raise rates to get it under control
- This could have a decidedly negative impact on valuation math, particularly for businesses with cash flows in the very distant future
- What would you pay for $1 in cash flow in the future?
  - $Value = \frac{Future\ Cash\ Flow}{Discount\ Rate - Growth\ of\ Cash\ Flow}$
  - $Discount\ Rate = Risk\ Free\ Rate + Equity\ Risk\ Premium$
- The chart on the rights assumes:
  - A constant equity risk premium of 5%
  - A constant terminal growth rate of 3%
  - A risk free rate between 0% to 5%
- Watch for an inflation scare in March – July of 2021 due to base effects



Risks

Unexpected Inflation

Risk #2: business risk

- The primary effect of inflation on a business is an increase in nominal input costs
- Our focus is on answering two critical questions:
  - Does the business need to reinvest a lot of its profits back into tangible assets to grow and maintain its operations? Stated differently, is the business **capital heavy or capital light, reliant on physical or intangible assets?**
  - Does the business offer a service/product that is sufficiently differentiated to increase prices above the rate of cost inflation without impacting sales volumes? In other words, does the business have **pricing power to grow its profits in real terms?**
- The 1970's and 1980's may provide a guide as to how inflation impacts the underlying economics of businesses that the securities investors own represent
  - Few navigated this period better than Buffett and Munger

For years the traditional wisdom – long on tradition, short on wisdom – held that **inflation protection was best provided by businesses laden with natural resources, plants and machinery, or other tangible assets** ("In Goods We Trust"). **It doesn't work that way.**

Asset-heavy businesses generally earn low rates of return – rates that often barely provide enough capital to fund the inflationary needs of the existing business, with nothing left over for real growth, for distribution to owners, or for acquisition of new businesses.

In contrast, a disproportionate number of **the great business fortunes built up during the inflationary years arose from ownership of operations that combined intangibles of lasting value with relatively minor requirements for tangible assets.**

In such cases earnings have bounded upward in nominal dollars, and these dollars have been largely available for the acquisition of additional businesses.

W. Buffett, 1983 Berkshire Hathaway Letter to Shareholders

Risks

Unexpected Inflation

Our approach to mitigate inflationary risks

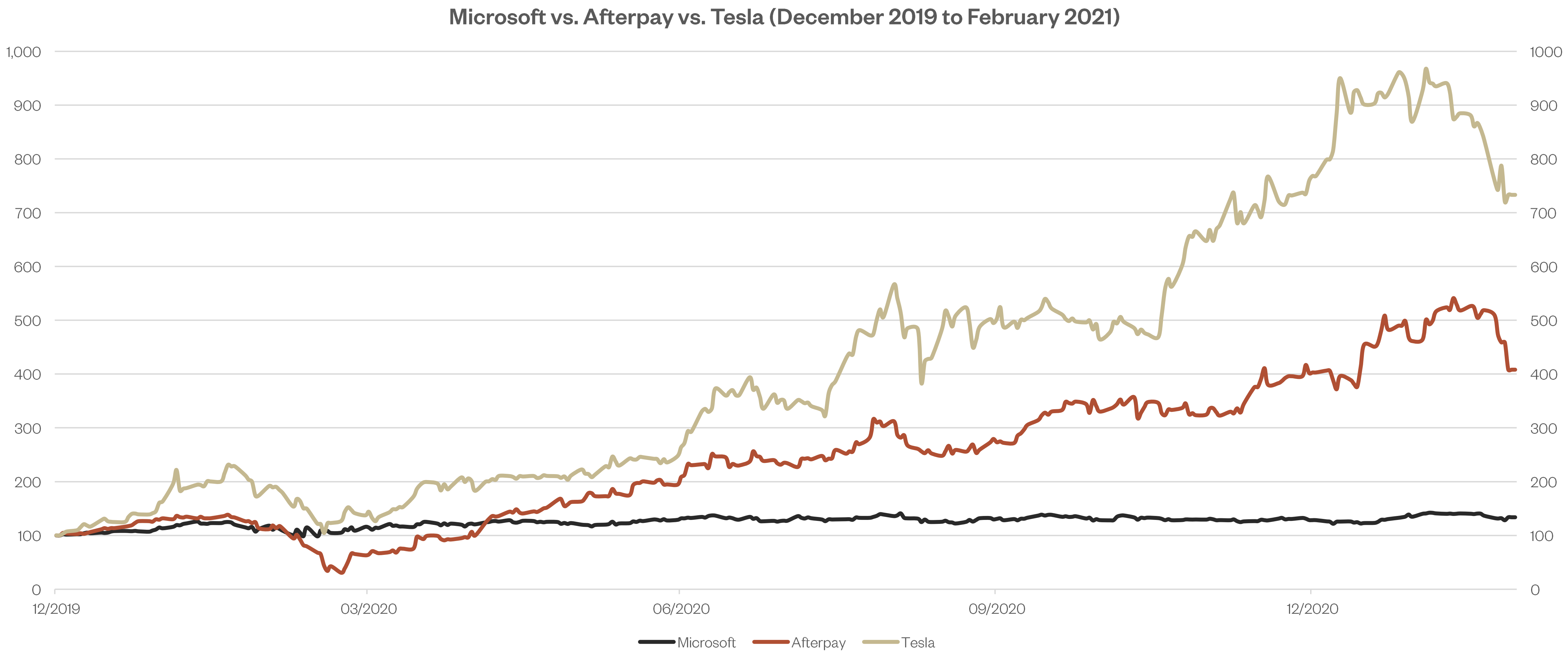
- Own businesses with pricing power
- Own capital-light businesses needing lower tangible reinvestment to maintain/grow their competitive position
- Avoid businesses with poor free cash flow profiles facing material debt maturities
- Ensure the Fund is not a one-way bet on long-duration cash flows
- Own businesses that capture a nominal increase in price levels through their revenue model (MasterCard & PayPal)

Our process generally leads us to three types of businesses

- Dominant consumer brands
- Scalable platforms/software
- Non-core, business-critical goods/services
    - We find these types of businesses generally exhibit the combination of pricing power, high returns on capital, low tangible reinvestment, robust cash generation and strong balance sheets we seek

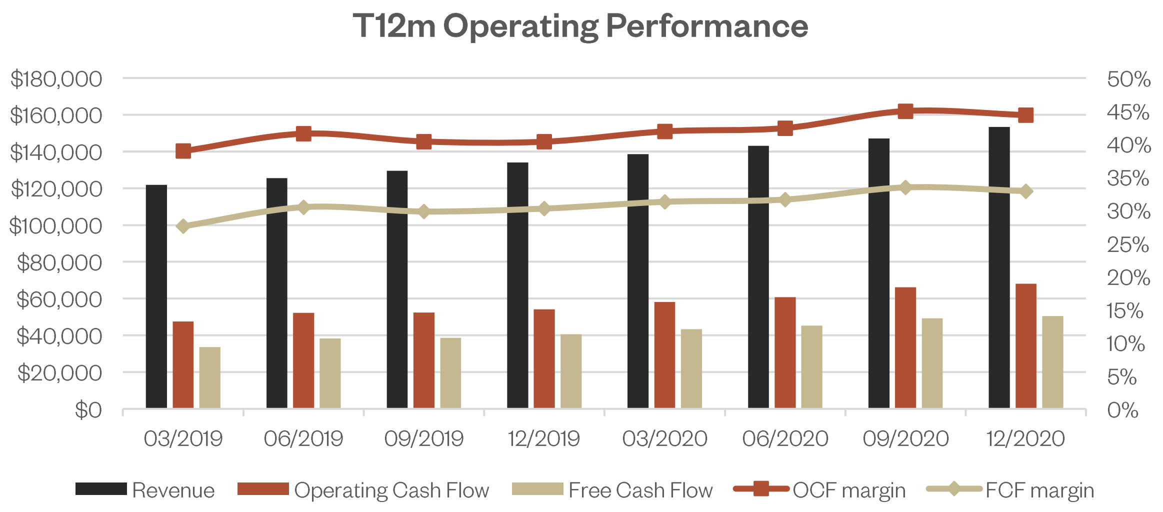
Dominant Consumer Brands	Scalable Platforms/Software	Business Critical Non-Core Goods/ Services
NIKE	Microsoft	ICON
ESTĒE LAUDER	Alphabet	KEYENCE
LVMH	PayPal	FASTENAL

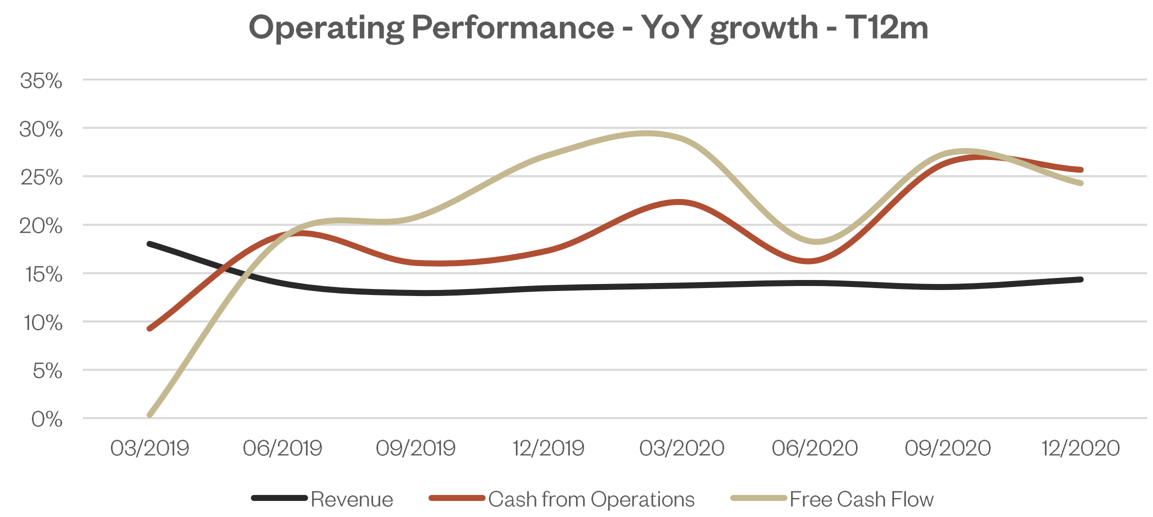
Profitless v. Profitable Tech

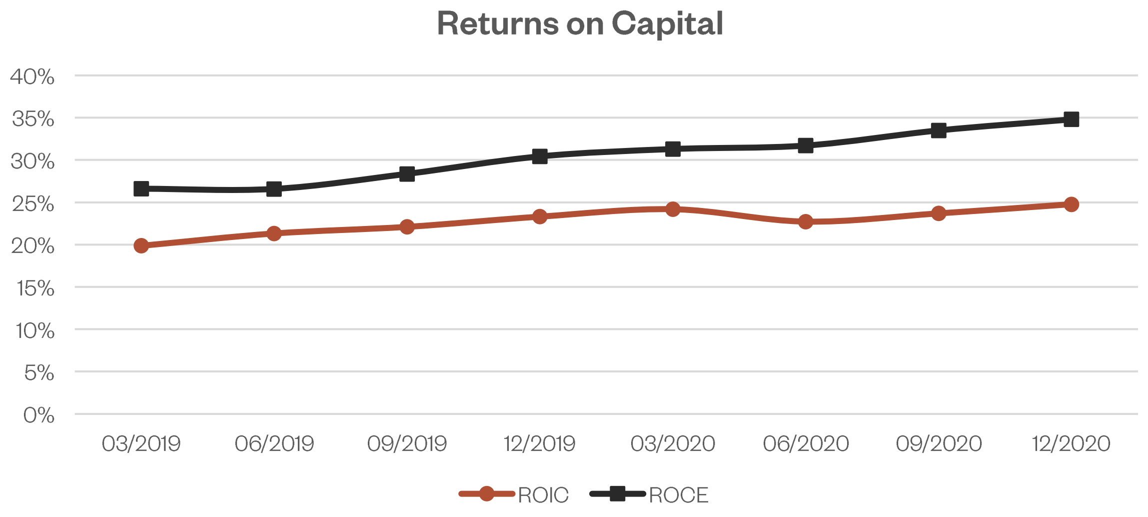


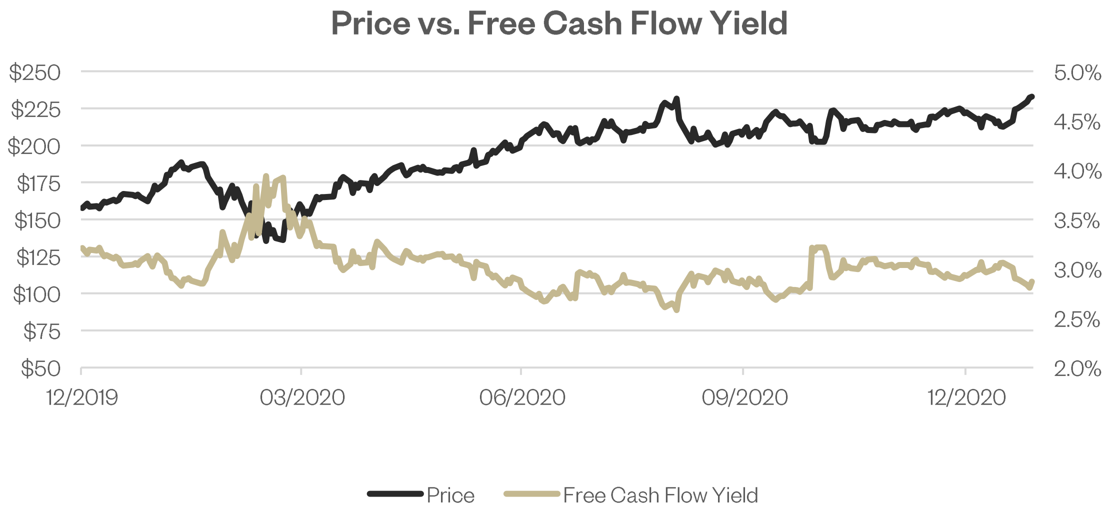
Source: FactSet

Our Focus Returns on Capital / Microsoft









Source: Microsoft company reports, FactSet & AIM estimates

A Simple Investing Framework

Focused on Quality

Four building blocks that seeks to identify resilient businesses with enduring long-term growth prospects

- Sustainably high returns on invested capital most likely the result of an economic moat
- Focused on the cash flow after investing to maintain and grow the business, not earnings
- Ensuring the balance sheet is sound and can withstand unexpected events
- Identifying management team who are good capital allocators and stewards of investors' long term interests

Forecastability is a crucial safety check

- We avoid businesses where the range of future outcomes are too wide to reliably forecast

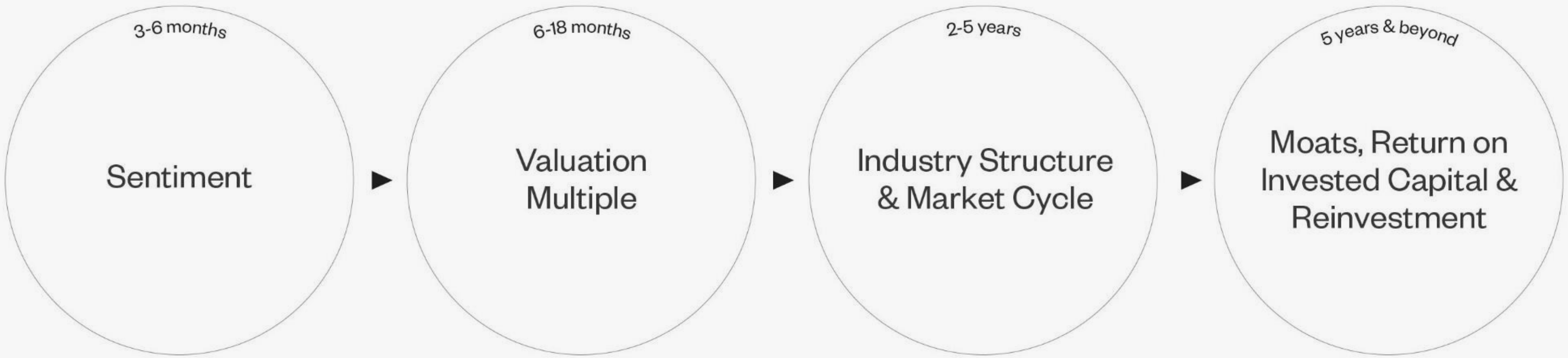
Return on Invested Capital (ROIC)	Focus on Cash Flow	Sensible Capital Structure	Management
Economic Profit (ROIC > WACC)	Intrinsic Value = PV of Future Free Cash Flow, Not Earnings	Debt vs. Equity	Capital Allocation Track Record
Moats Underpinning the Sustainability of Excess ROIC	Earnings Ignore Reinvestment Requirements	Solvency, Liquidity & Coverage	Long-term vs. Short-term Thinking
Industry Competitive Structure	Timing	Maturity Profile	Integrity, Governance & Culture
Runway for Growth	Ownership Mindset	Off-Balance Sheet Liabilities	Dealing with Adversity

Forecastability
Can long-term outcomes be accurately forecast?

What Drives Returns?
Comparing quality to value and growth

A Voting Machine vs. a Weighing Machine

- Over the short term, changes in sentiment and news dominate price moves
- As the investment horizon lengthens, fundamental factors win out
- Different drivers of return
  - Value: mean reversion (“the market is too negative”)
  - Growth: revenue and earnings momentum (“the company will keep on growing at high rates”)
  - Quality: compounding, driven by the sustainability of the high ROIC and lower risk of failure from a weak balance sheet
- The real money is made when a business starts to reinvest its capital base at high incremental rates of return



Why Quality Works

Quality reduces the risk of material and permanent capital loss in a crash

- When controlling for persistently high return on invested capital and low balance sheet risk, quality strategies have a lower probability of a permanent, value-destructive crash.
- The combination of strong competitive positioning and low business risk makes the business more resilient during periods of distress.

Market participants discount the persistence of high ROIC

- Investors are overly optimistic about turn-around stories for low quality businesses (which generally trade on lower valuations) and too pessimistic about the long term profitability of high quality businesses.

Source: Bouchaud, Ciliberti, Landier, Simon & Thesmar (2016). The Excess Returns of "Quality" Stocks: A Behavioural Anomaly, HEC

Portfolio
31 January 2021

Higher returns on capital, materially lower debt levels: wide moats and strong balance sheets for a post-COVID world

- More profitable than the average business by a substantial margin
- Higher returns generated using substantially less debt
- From a valuation standpoint, the Fund is more expensive than the benchmark, but we believe the quality justifies a premium
  - Keep in mind that some of our businesses have been negatively affected by the pandemic (LVMH, Estee Lauder, Coca Cola, Heineken and Nike all had significant lost sales for a period), meaning returns are cyclically depressed
  - For these businesses, current valuations – which are looking through the impact of 2020 and into the future – are optically inflated
- We have reduced exposure to businesses that are richly valued on long-duration cash flows

Portfolio Characteristics	AIM GHCF	MSCI World
Profitability		
Gross Margin	40.3%	31.9%
Operating Margin	15.6%	9.0%
ROE	17.7%	7.8%
ROIC	16.0%	11.1%
Leverage		
Debt/Equity	56.1%	158.0%
Net Debt/Equity	6.4%	60.9%
Valuation		
Free Cash Flow Yield	3.2%	5.4%

Source: AIM, FactSet, Bloomberg, MSCI, S&P.
Index data using most recently reported underlying financials as at 31 January 2021.

Top 10 Holdings
31 January 2021

Recent actions

- After elevated activity levels in March – June, we have been much less active during the 2nd half of 2020
  - Sold Apple (September)
  - Recently sold Netflix and Salesforce.com
  - Currently building a position in a well-known global brand/IP businesses domiciled outside of the US
- Cash at 3.8% at the end of January
- In general, not inclined to pay up for market-anointed winners are present

#	Name	MSCI Sector	AIM Internal Classification	Weight
1	Microsoft Corp	Information Technology	Software	7.6%
2	Berkshire Hathaway	Financials	US Cyclical	7.4%
3	Alphabet Inc.	Communication Services	Internet Platform	6.7%
4	The Coca-Cola Co.	Consumer Staples	Beverages	6.1%
5	ICON PLC	Health Care	Health Care Services	6.0%
6	UnitedHealth Group Inc.	Health Care	Health Care Services	5.6%
7	MasterCard Inc.	Information Technology	Payments	5.3%
8	Accenture PLC	Information Technology	IT Services	5.2%
9	Nike Inc.	Consumer Discretionary	Luxury Goods	5.1%
10	Prosus NV	Consumer Discretionary	Internet Platform	5.1%
	Total			**60.2%**

Performance

Rolling Period Returns	CY2020	Financial YTD	4th Quarter
AIM Global High Conviction Fund	+14.2%	+8.1%	+3.4%
MSCI World Net Total Return (AUD)	+5.6%	+11.1%	+5.9%

Annualised Returns	30 June 2019	31 Dec 2018	Inception
AIM Global High Conviction Fund	+13.3%	+14.9%	+4.6%
Benchmark*	+9.8%	+15.3%	+7.0%

All returns are measured in AUD and are presented after fees as at 31 December 2020. Source: AIM, MSCI, FactSet. Past performance is not indicative of future performance.

** Benchmark changed from MSCI World (USD) to MSCI World Net Total Return (AUD) on 1 July 2019 to reflect to reflect PDS changes (removed shorting and moved to currency unhedged position in early 2019). Inception date: 7 July 2015.*

AIM

Aitken Investment Management Pty Ltd
Level 10, 70 Phillip Street Sydney NSW 2000

Telephone: +61 2 8379 3700
Email: info@aimfunds.com.au
Website: www.aimfunds.com.au