

Truffle Portfolio

1Q 2023 Investor Letter

Dear Long Term Investors,

Our portfolio has experienced volatility in recent months. Despite stable market prices in the first two months of the quarter, a weaker September led to a decline in the portfolio's value. We believe that the market has adequately repriced investments in light of rising interest rates and the expectation of a recession in 2023. Going forward, the success of our portfolio will largely depend on the performance of the companies in which we have invested.

For our new Truffle Portfolio investors, our main principle is investing in good businesses at good prices. As Charlie Munger would say, "Don't get too cute." We use straightforward valuation methods, with a focus on earnings and cash flow. We generally avoid anything that has the word "adjusted" in front of it.

Looking ahead to 2023, we expect markets to remain volatile until the macroeconomic picture stabilises. We are still seeing high volatility even in the last few weeks. Some shares have lost more than 30% and then gained it all back within a few days. These types of price movements are not normal and are indicative of a market that is struggling to price shares accurately given the combination of macro and company-specific data. While this presents challenges, it also offers opportunities for investment when prices become favourable.

We understand that these volatile prices may raise questions and concerns among our investors. I have already had several one-on-one conversations with some of you, and if you are an investor and would like to have a conversation, please reach out to me at petetanpy@phillip.com.sg.

One common question we have received is about our recent shift in focus from Tech to Energy, Banks, and Semicon. We made this change in response to the larger macro narrative of inflation and higher interest rates. We believe that these sectors will be more resilient in the face of higher interest rates. Additionally, we choose companies based on their quality, not their industries, and currently seeing good opportunities in these sectors.

Another question we have received is whether our portfolio is too diversified, with 20 companies. We believe that diversification is important to ensure the longevity of our investments.

An example of the risks associated with a highly concentrated portfolio can be seen in the case of a well-known Asia-based portfolio manager (*the identity is not important but the lessons are*). While investing in only 8 companies, the portfolio experienced over 200% growth in 2020, but suffered a decline of more than 82% in 2022. This resulted in a significant loss for investors, many of whom chose to withdraw their investments.

In contrast, we believe in maintaining a well-diversified portfolio to ensure the longevity of our investments. Chasing high risk returns is not worth it if the portfolio is not able to survive the year.

As we move into 2023, you'll notice that we have made some changes to our portfolio while also keeping some existing investments. While it is not possible to discuss all of the changes, I would like to share one example to illustrate our investment thinking and process for choosing a good company.

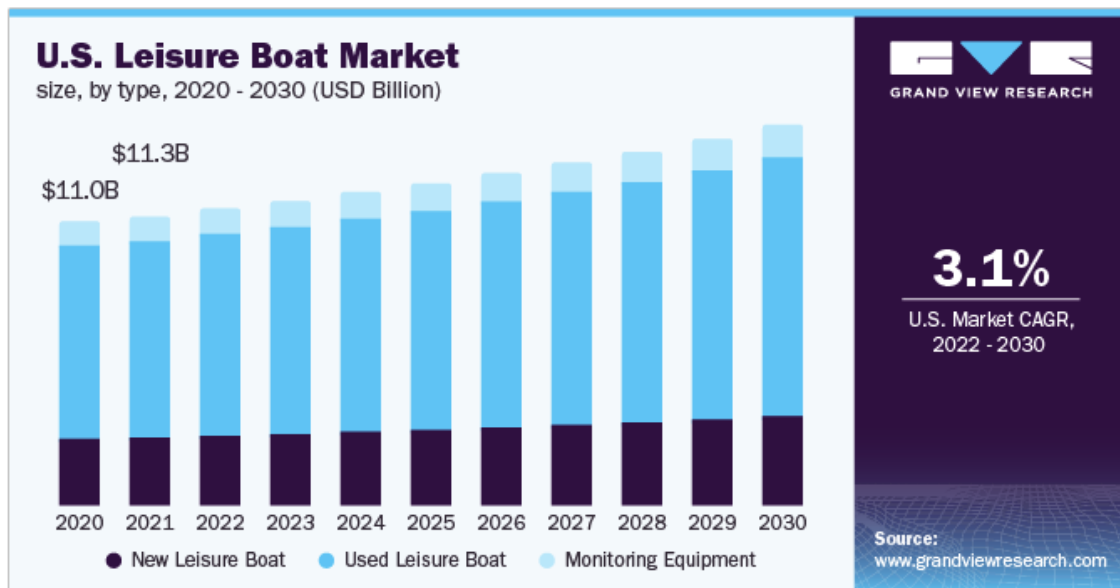
Malibu Boats, Inc. (MBUU)

We are excited to announce the addition of Malibu Boats, Inc. (MBUU) to our portfolio. MBUU is a leading designer, manufacturer, and seller of recreational powerboats. Their product line includes 8 brands, including Malibu, Axis, Pursuit, Maverick, Cobia, Pathfinder, Hewes, and Cobalt. These boats are used for a variety of recreational activities such as water sports, boating, and fishing.



The market for recreational boats has been growing consistently, with a global CAGR of 4.7% and a US CAGR of 3.1% projected through 2030. MBUU sells its boats through a dealer network of over 400 locations worldwide.

The US is particularly important as it was the largest market for recreational boats in 2021, with 46.24% of global revenue. In the US, over 100 million Americans go boating each year, and 11.9% own their own recreational boat. Recreational boat popularity was also elevated during COVID, resulting in the market size expanding to \$13.1 billion in 2022.



In addition, MBUU is able to compete in the recreational boat market through strategic acquisitions.

They acquired a direct competitor, Cobalt Boats, in 2017, which enlarged their dealership network by over 130 locations. In 2018, they bought Pursuit Boats to expand into the luxury market, which came with a large factory to increase production. In 2021, they bought Maverick Boat to enter the center console and bay boat segment, which provided vertical integration with Pursuit Boat's luxury units and also gave them 70 more dealerships and 2 more factories.

Financials

MBUU has strong financials with double-digit revenue growth Y/Y and similar growth in operating cashflow since 2016. They also have a low debt to equity ratio of 0.13 and cashflow yield of 10%. This means they generated over \$164m in free cashflow while only using \$119m in debt, allowing them to easily pay off all the debt and continue to grow without encumbrance. In comparison to competitors, MBUU has the highest margins and return on invested capital.

Year		2022	2021	2020	2019	2018	2017	2016
Revenue	▮▮	1,214.88	926.52	653.16	684.02	497	281.94	252.97
Revenue Growth (YoY)	▮▮	31.12%	41.85%	-4.51%	37.63%	76.28%	11.45%	10.65%
Cost of Revenue	▮▮	904.83	690.03	503.89	517.75	376.66	206.9	186.15
Gross Profit	▮▮	310.05	236.49	149.27	166.27	120.34	75.04	66.82
Selling, General & Admin	▮▮	89.27	79.46	57.83	62.2	45.08	33.4	28.73
Other Operating Expenses	▮▮	6.96	7.26	6.13	12.27	5.2	2.2	2.19
Operating Expenses	▮▮	96.23	86.71	63.96	74.47	50.28	35.6	30.92
Operating Income	▮▮	213.82	149.78	85.31	91.8	70.07	39.44	35.9

Year		2022	2021	2020	2019	2018	2017	2016
Net Income	▮▮	157.63	109.84	61.56	66.07	27.61	28.36	18.04
Depreciation & Amortization	▮▮	26.32	22.89	18.38	15.96	12.85	6.75	5.52
Share-Based Compensation	▮▮	7.4	6.42	3.87	3.4	2.81	2.15	2.7
Other Operating Activities	▮▮	-26.5	-7.83	10.33	-3.92	15.18	-1.4	9.34
Operating Cash Flow	▮▮	164.85	131.31	94.14	81.5	58.46	35.86	35.6
Operating Cash Flow Growth	▮▮	25.54%	39.49%	15.51%	39.42%	63.03%	0.71%	183.64%

Source: Stockanalysis.com

Earnings Quality				
	HZO	BC	MCFT	MBUU
Return on Assets	16.33%	10.98%	18.26%	20.70%
Return on Equity	28.88%	32.66%	39.02%	-
Return on Invested Capital	24.08%	15.23%	25.94%	28.66%

Profitability				
	HZO	BC	MCFT	MBUU
Operating Margin (TTM)	11.49%	13.55%	16.34%	17.86%
Gross Profit Margin	34.91%	28.46%	24.30%	25.71%

Source: Ycharts

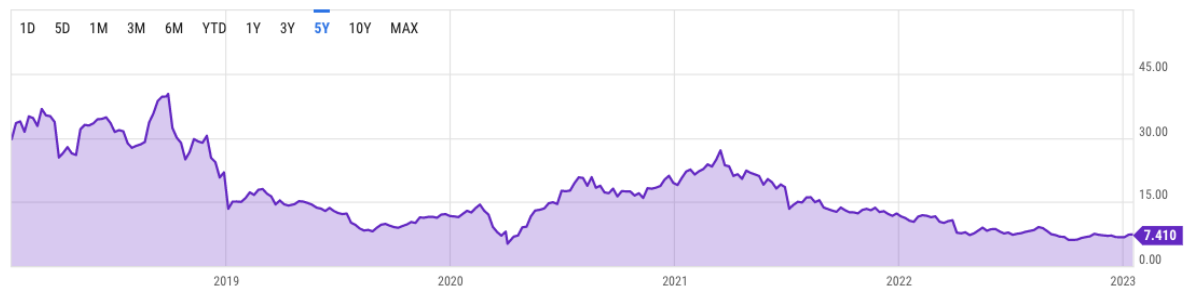
Valuation

Valuation-wise, MBUU is currently at a 7.4x PE ratio, which is better value than Brunswick and Mastercraft, and just behind MarineMax. However, it's important to note that MarineMax is a smaller company. Additionally, the current PE ratio is at the lower end of the past PE ratio range.

	HZO	BC	MCFT	MBUU
Market Cap	735.62M	5.756B	505.47M	1.194B
Enterprise Value	700.59M	7.759B	526.17M	1.242B
Price	33.87	79.38	28.39	58.68
PE Ratio	3.823	9.518	10.14	7.410

PE Ratio Chart

[VIEW FULL CHART](#)



Risk

The main risk for MBUU is the potential impact of a recession on recreational boat demand. They also cited rising inflation as a potential risk as it could make production inputs more expensive. However, they are trying to mitigate this by sourcing a large part of production in-house. The share price of MBUU has been declining since March 2021, reflecting negative market sentiment in the consumer cyclical sector. However, management expects mid-to-high single-digit growth in sales with a slight decrease in EBITDA margin.

METRIC	TARGET
Consolidated Net Sales	Mid-to-high single digit % growth
Adjusted EBITDA Margin	Down slightly

Source: MBUU Annual Report

I hope that this gives you a good idea into the type of companies we are adding to the portfolio and why as the Portfolio Manager, I remain confident and unfazed by the market uncertainty.

New Accounts and Top Ups

Lastly, since the prices have since retreated to more reasonable levels, we are seeking more funds to take advantage of the opportunity.

We are happy to announce that the Truffle Portfolio is opened for new accounts and top-up funding to existing accounts.

For new accounts

1. Apply at <https://investwithpete.co/how-to-apply>
2. Min. investment sum is S\$50,000 or equivalent in other currencies

For top-up funding to existing accounts

1. For SGD funding : <https://www.poems.com.sg/payment/>
2. For other currencies funding:
<https://www.poems.com.sg/helpcentre/PSPLTrustAccounts.pdf>)
3. State their ACCOUNT NUMBER and ACCOUNT NAME clearly in their payment instruction

With that, I will see you in the next letter. Happy Lunar New Year to all who celebrate!

Regards,
Pete