

Quality Compounders

FY24 Investor Update



You can have a great strategy but execution, of course, is everything.

– Mark Leonard – CSU 2024 Annual Meeting.

The above quote really resonated with us as there has been much speculation about ‘copycats’ replicating Constellation Software’s business model of acquiring niche software businesses, Mark is arguably the most believable and humble software investor in the world and is subtly highlighting how hard it is to get it right.

Quarterly Commentary

The Quality Compounders team (Sam, Alex, Lachlan, and Shaun) are all personally invested in the stocks we recommend, and we are more passionate than ever to find and learn about new businesses and meet with passionate founders. We love doing what we do. **Thank you for trusting us to manage some of your capital**, we will continue working as hard as we can to get you the best results over the long term and treat your money as it is our own.

The portfolio **returns for the period ended 30th June 2024 was +39.1% vs the All-Ordinaries index of +12.1%**, The annualized return since inception (Mar-2020) is now 23.9% vs 8.46% for XJAOAI. The top portfolio contributor for the month and year was ProMedicus +118% (year) and +33% (month), it was also the largest holding in the portfolio starting the year at ~17% and closing the year at 26%. The other meaningful contributors for the year were **Lovisa +70%** and **Netwealth +47%**.

Current Portfolio – Top 5 holdings

Top Holdings	% Fund
Pro Medicus Ltd	26%
Lovisa Holdings Ltd	14%
Lumine Group Inc.	11%
WiseTech Global Ltd	10%
Constellation Software Inc.	7%

Quality Compounders Performance FY24

To summarise, the Quality Compounders portfolio is focused on investing in the highest quality businesses and management teams in the world and attempts to outperform your zero-cost alternative, the ASX All Ordinaries Accumulated index. So far it has achieved this **producing an annualized performance of 23.9% vs 8.46%** over a ~4-year period. We have been more active with the portfolio in the past 6 months than we would have liked however we believe it is critical to be focusing on our best ideas to continue compounding the returns achieved.

Pro Medicus

Given PME is a quarter of the portfolio we thought it would be worth a quick update. At a share price of \$143 where it finished FY24 the valuation was \$14B AUD market cap and 73x EBIT FY26 multiple.

Our assumptions are that the radiology business (no AI or other ologies products) continues to grow revenue at 14% (half volume half price) + \$20M annual contract value added per annum and is worth \$17B in FY29. On top of this we believe that the AI and other ologies products could be contributing \$3B of value by FY29 (some products will be commercialized imminently).

In total our forecasts for valuing PME are \$490M of revenue in FY29 at ~75% EBITDA margins. We believe if this occurs the stock could be worth ~\$200 per share or an 8% IRR at \$143.

We believe the upside opportunity appears worth holding given the quality business model and outstanding management. We believe that Visage could become the core operating system for clinicians in the workflow of medical imaging. There are 650M medical scans conducted every year in the USA (\$2B USD @ \$3 per scan) however, the Diagnostic imaging industry is \$122B USD in size and if ProMedicus continues to penetrate other workflows as they have done with Workflow and Open Archive products, we could be underestimating the long-term potential by focusing just on today's products.

Recent Ideas

We added 4 new companies to the portfolio during the quarter (Brunello Cucinelli, Hemnet, Lifco and F&P Healthcare, we also sold 3 holdings (Macquarie Telecom, Netwealth and Nanosonics). We have outlined below some brief commentary on some of these.

Brunello Cucinelli Purchase

We admire the luxury brands business; they appear to us to be one of very few businesses that have maintained pricing power over nearly a century. The USD price of a Chanel medium flap bag in 1955 was \$220 and is close to \$10,500 today a CAGR of 5.8% per annum and close to double the annual inflation rate in the USA. Majority of leading companies in 1955 have lost virtually all pricing power while arguably the pricing power of Chanel, Louis Vuitton and Hermes has increased. Our view is that Brunello Cucinelli is a luxury brand that is early in this journey (€1B of revenue and €6M revenue per store while carefully balancing growth with scarcity and quality). At today's valuation of €6.3B market cap and 25x EV/EBIT FY26 we believe that BC can produce a 16% IRR. Since 2014 Cucinelli has retained €265M of earnings to increase EBIT by €152M per annum and added ~€5B of market value with no new shares.

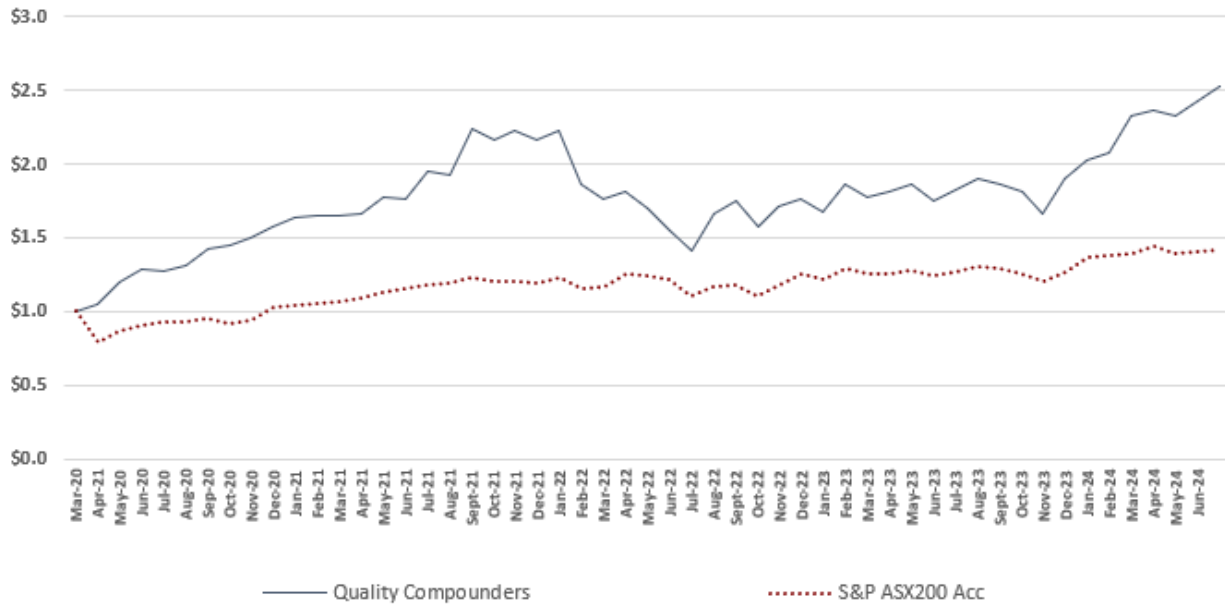
Fisher & Paykel Healthcare Purchase

F&P is a niche monopoly medical device business that provides mission critical respiratory devices to ICU departments around the world. As Mark Miller said in the 2024 CSU AGM "*...The more mission critical the product, the deeper the moat to build from*". This has been a key learning for us. F&P humidifiers breathe for patients and keep them alive in an intensive care environment (life or death) hence very mission critical. The F&P business is growing outside this department now. The performance of the business is very reliable via 85% recurring revenue from consumables plus pricing growth, the business also carries zero debt and owns its land and buildings. F&P has retained \$900M of earnings since 2014 to increase annual EBIT by \$200M pa and added \$13B of market value with no new shares.

Macquarie Telecom Sale

We struggle to understand the recent capital allocation decisions of raising capital twice to acquire land and buildings underneath the MAQ data centers, increasing equity capital by 23%. These two recent decisions highlight our lack of understanding in the business economics. It appears that MAQ require more capital to remain competitive than we thought. Capital allocation decisions are pronounced in situations like this where the company is retaining all earnings and seemingly operating a capital light business. This has changed our view on MAQ until we understand it further.

\$1 Invested in Quality Compounders vs ASX200 Acc.



	FY20	FY21	FY22	FY23	FY24
Quality Compounders	27.1%	54.0%	-27.9%	29.1%	39.1%
All Ords Acc. Reinvested	-7.6%	27.8%	-6.5%	14.8%	12.1%
Outperformance	34.6%	26.2%	-21.5%	14.3%	27.0%

ANNUALISED		30.06.24
Class/Security	Inception Date	Since Inception (1)
Morgans Scone Quality Compounders Portfolio	2020-03-01	23.91
S&P ASX200 Accumulation Index		8.46
NON annualised		
Class/Security	Inception Date	
Morgans Scone Quality Compounders Portfolio	2020-03-01	153.16
S&P ASX200 Accumulation Index		42.16

Things we have been working on

We have been spending considerable time over the past month collating our thoughts and notes from our recent research trip to the USA. We have previously communicated our thoughts on the key ideas being Lumine and Heico.

At the end of July, we are traveling to the Mainfreight Annual meeting in Auckland and are also visiting the Fisher & Paykel manufacturing facility and head office. We are looking forward to seeing the Mainfreight team and hearing how trading has started for the year which we expect to be a better year than FY24. We remain confident in their global opportunity and quality of the team.

We are also preparing for a research trip to Europe to visit several companies that we are researching and within the portfolio including Lifco, Hemnet, Brunello Cucinelli and several other high performing companies.

Summary and Outlook

Thank you for trusting us to manage some of your precious capital, we are as passionate as ever to keep compounding learning and capital and think we have some great ideas to further improve performance of this portfolio over the coming 12 months. We are particularly excited by the new holdings introduced to the portfolio and believe they will provide a good base for growth in the coming several years.

Regards,

Quality Compounders Team

This publication is provided for general information purposes only and is not intended as an offer to enter into any transaction. This information contained in it is not necessarily complete and its accuracy can not be guaranteed. We have prepared this presentation without consideration of the investment objectives, financial situation or particular needs of any individual investor. Before a client makes an investment decision, a client should, with or without Morgans' assistance, consider whether any advice contained in the presentation is appropriate in light of their particular investment needs, objectives and financial circumstances. It is unreasonable to rely on any recommendation without first having spoken to your adviser for a personal recommendation. The information contained in this presentation has been taken from sources believed to be reliable. Morgans Financial Limited does not represent that the information is accurate or complete and it should not be relied on as such. Any opinions expressed reflect Morgans' judgment at this date and are subject to change. Morgans and/or its affiliated companies may make markets in the securities discussed. Further Morgans and/or its affiliated companies and/or their employees from time to time may hold shares, options, rights and/or warrants on any issue included in this presentation and may, as principal or agent, sell such securities. The Directors of Morgans advise that they and persons associated with them may have an interest in the above securities and that they may earn brokerage, commissions, fees and other benefits and advantages, whether pecuniary or not and whether direct or indirect, in connection with the making of a recommendation or a dealing by a client in these securities, and which may reasonably be expected to be capable of having an influence in the making of any recommendation, and that some or all of our representatives may be remunerated wholly or partly by way of commission. The presentation is proprietary to Morgans Financial Limited and may not be disclosed to any third party or used for any other purpose without the prior written consent of Morgans. Morgans Financial Limited (ABN 49 010 669 726 AFSL 235410)
A Participant of ASX Group Principal Office: Level 29, Riverside Centre, 123 Eagle Street, Brisbane QLD 4000
This document has been prepared by Morgans Financial Limited in accordance with its Australian Financial Services License (AFSL no. 235410). The views expressed herein are solely the views of Morgans Financial Limited.