DAKOTA SUMMIT FUND

Global public equities

- We scour the world for public companies with unusual market power and buy their shares only when they're priced to return 15-20% or more a year.
- Global equity.
- Concentrated: 13-20 positions.
- Strategy: go where the returns are.

FOUNDER

Scott Reardon is an author and value investor. Prior to founding Dakon, he was the head analyst at a holding company pursuing a Berkshire/Leucadia strategy. Prior to that, he worked as a research assistant at Columbia Business School in the Value Investing Program.

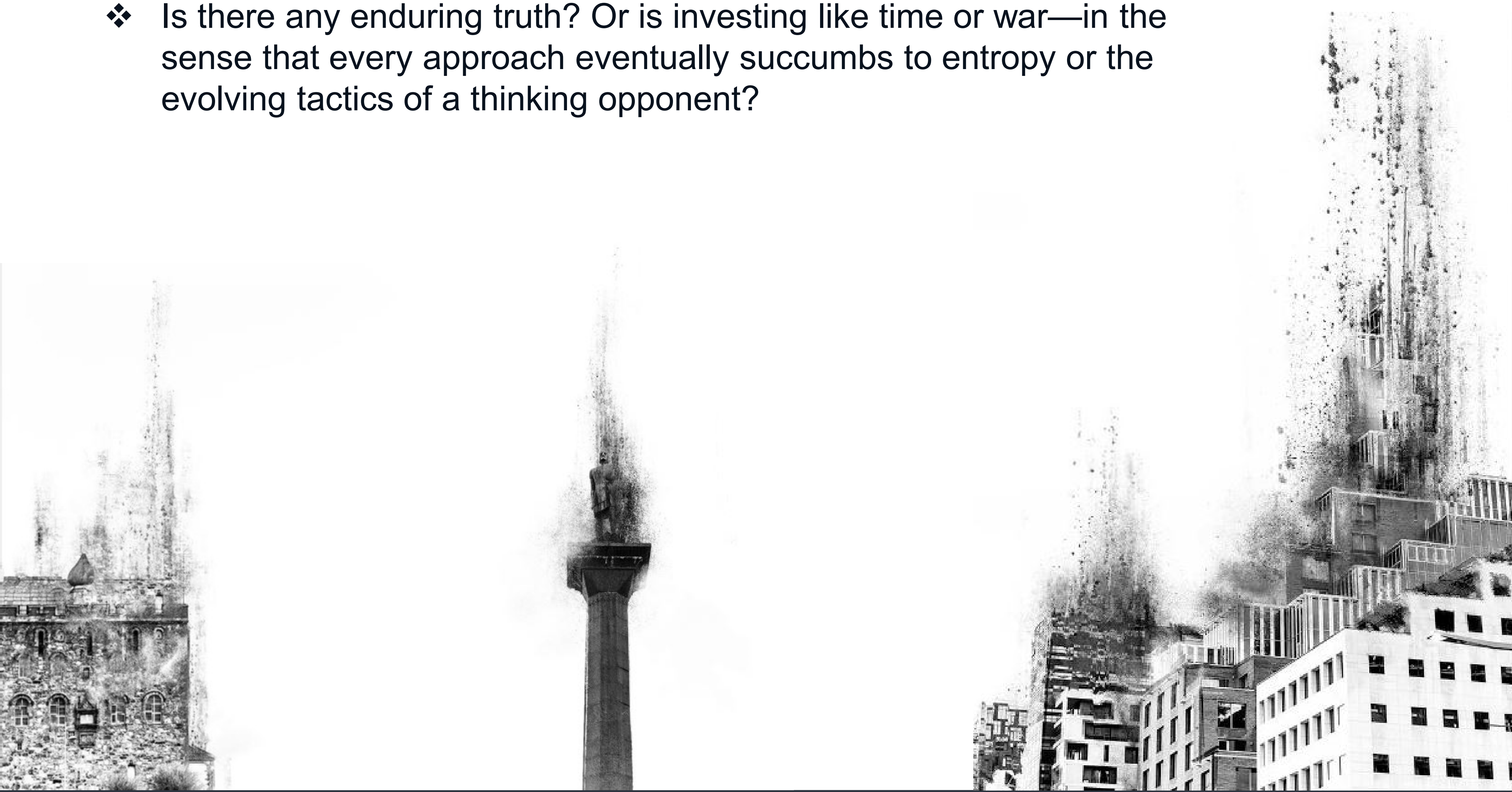
Before turning to investing, Scott was an attorney at Simpson Thacher, a top 5 law firm, and is a cum laude graduate of Northwestern Law.

His first novel, The Prometheus Man, was published by Little Brown in 2017. The second book in the series was published in 2020.

OUR FOUNDING IDEA

❖ What, if anything, has worked in investing across the ages?

❖ Is there any enduring truth? Or is investing like time or war—in the sense that every approach eventually succumbs to entropy or the evolving tactics of a thinking opponent?



OUR FOUNDING IDEA

Investor database

- To answer this question, we did something we don't think has ever been done before. Instead of backtesting historical data, we created a groundbreaking database of the greatest investors in history.
- We systematically studied their strategies and underlying holdings. Significant because most quants study theoretical outcomes. We study what actually happened.
- **The results changed our lives as investors. <u>Because great investors are far more similar than not</u>. Incredibly this holds true across both time and geography.**

#1: PAYOFFS

- The #1 difference between a great investor and a mediocre one is <u>payoffs</u>.
- Great investors focus on investments with <u>massive upside</u>. 50-100% upside. 15-20% IRRs. High absolute value.
- Most professionals, by contrast, buy stocks with less than 30% upside. That’s why even the best mutual funds are mediocre.
- When something hits, you want it to hit big. **<u>Go for the whale</u>.**

#2: ABSOLUTE VALUE

Absolute payoffs

- When we say payoffs, we mean payoffs based on a company's "forever value."
- But how did they know what that forever value was?
- FCF Yield + Growth = Return.
- A "low quality" firm trading at a 20% FCF yield doesn't need to grow at all to return 20% a year. Meanwhile an "expensive" firm trading at a 5% earnings yield could also earn 20% a year if it's growing 15% annually.
- We were shocked at just how many great investors—with seemingly different philosophies—used the Yield + Growth equation as their north star.

#3: SAMENESS

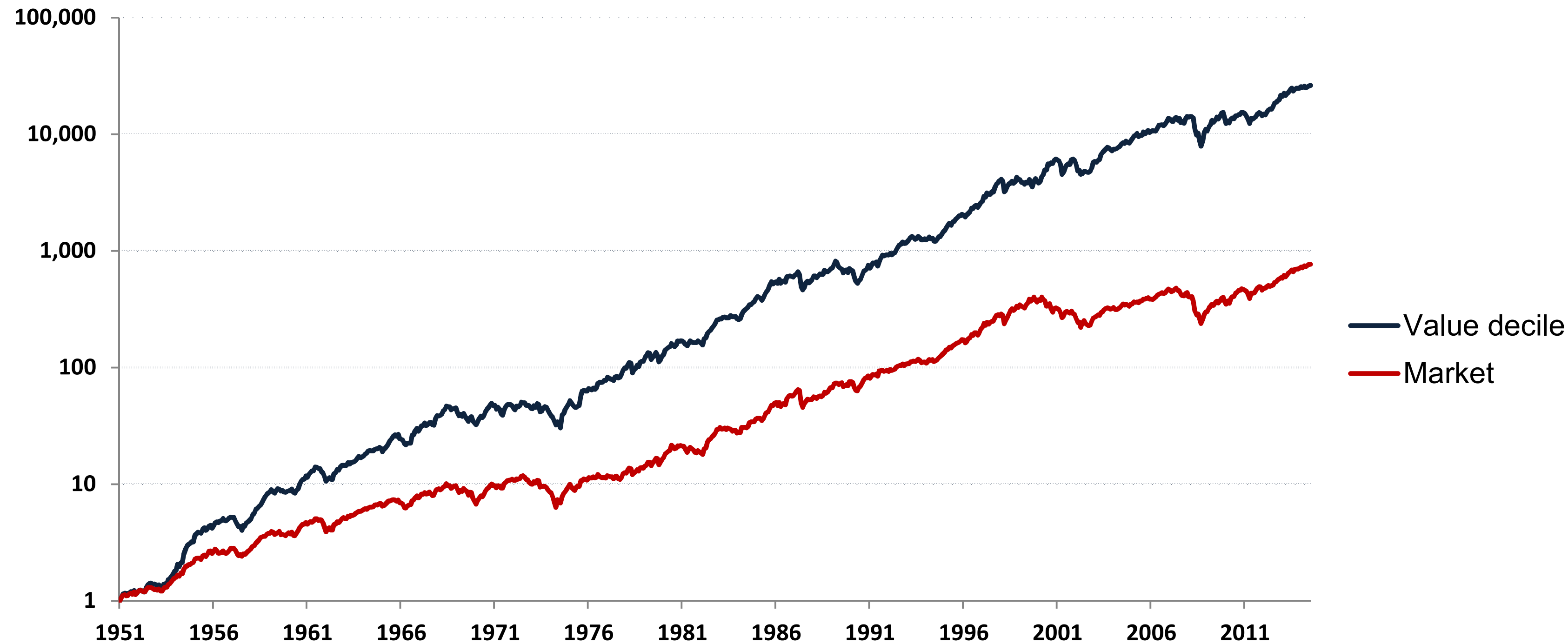
Sameness: the silent strength

- Great investors tended to bet not on change but on sameness (i.e. reversion to the mean or reversion to trend).
- They wanted to buy “inevitables.” These weren’t higher growth or higher quality firms. But they were higher-percentage—in terms of survival and longevity.
- Jeff Bezos: “It’s the things that don’t change that allow you to build great businesses.”
- The greats tended to avoid weak, superfluous businesses in favor of those that supported higher-percentage predictions. They bet on the strength of the tree, not the direction of the wind.

#4: DEEP VALUE

- A shocking 32% of the best investors came from the loneliest school of value investing: deep value.
- "Deep value" = stocks trading at less than 7-10x earnings.
- Deep value is about buying things trading at extremes. Means taking humiliation risk.
- Only 1-2% of assets are managed by deep value investors.

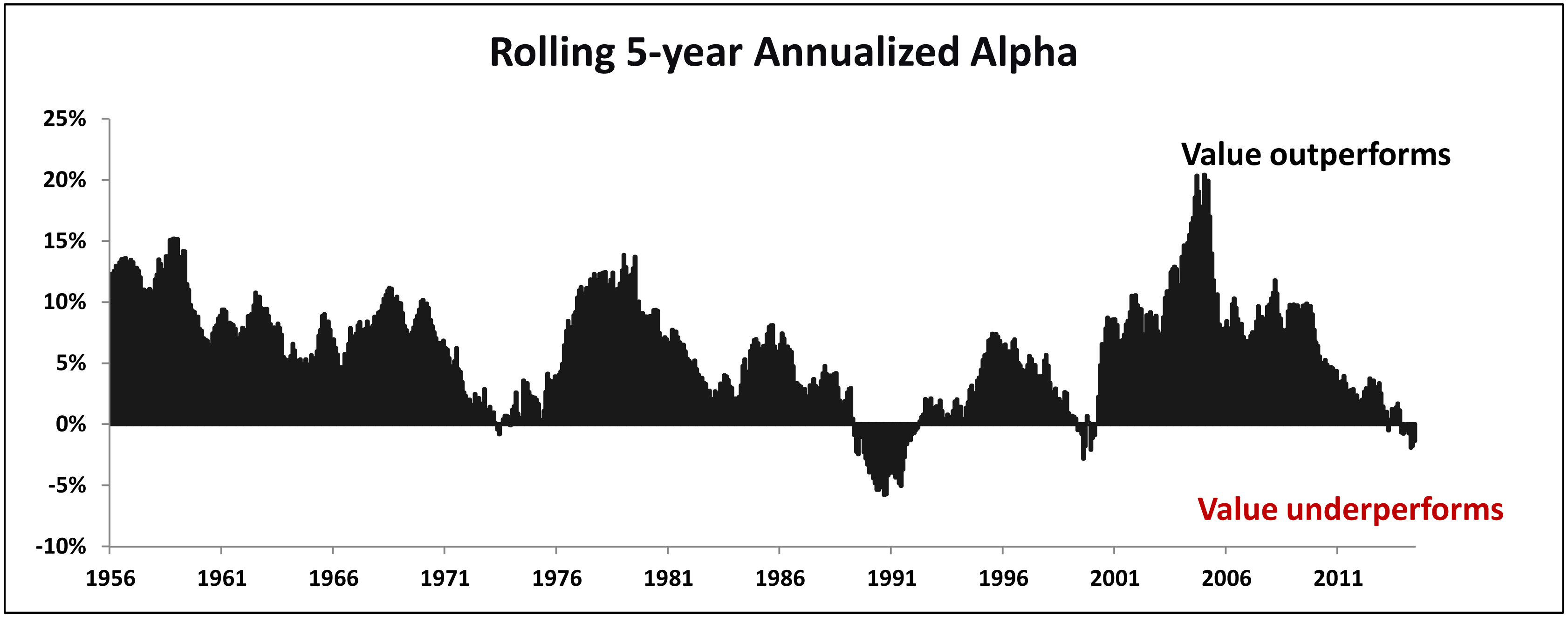
DEEP VALUE LONG-TERM



Source: Ken French data library.

- Value decile is cheapest 10% of stock market (market cap-weighted).
- The market returns 11%. But the value decile returns a whopping 17% a year.
- 6% annual outperformance over six decades.

DEEP VALUE MEDIUM-TERM



Source: Ken French data library.

- This shows alpha for cheapest 10% of the market versus the entire stock market.
- There are few 5-year periods in which deep value doesn't outperform.

OUR STRATEGY

Putting it all together, we created a strategy with historical principles that have withstood the test of time.

1. **Let payoffs be our guide.** If the stakes aren't high, don't play the game.

2. **Hannibal Lecter.** *"Of each thing, ask: What is its nature?"* Time reveals a business's nature. Bet with that nature, not against it.

3. **Market power.** Buy things with privileged place in the ecosystem. Kangaroos have easier lives than lions.

4. **Chinatown.** *"Why are you doing it?" "The future, Mr. Gittes, the future."* Never forget: we are competing for a piece of the future. The only assets worth buying are those that can produce decades of FCF generation.

OUR STRATEGY

- **#1: Focus on oligopolies, duopolies and businesses with market power.**
  - Higher-percentage firms.
  - Research shows they produce significant alpha.*
- **#2: Buy only when there's absolute value: roughly 20%+ annual returns or 100% upside.**
  - Embrace chaos and apathy to buy franchises at once-a-decade valuations.
- **#3: Hang on.**
  - Ignore catalysts, inflection points and other low-percentage "noise."

*"Industry Concentration, Excess Returns and Innovation in Australia." David R. Gallagher, Katja Ignatieva, James McCulloch.

OUR COMPETITIVE ADVANTAGE

- Our competitive advantage is that, unlike most funds, our strategy is time-tested.
- If a manager says that his strategy focuses on firms growing revenues 20% a year, how does he know that's a good thing?
- If historically high-growth stocks have steeply underperformed due overvaluation (which they have), what makes the manager think that this time is different?
- Most investors are forever locked in the present. They don't see a reality far deeper and far broader than the one they witness day-to-day. <u>Our fund is a way to go long this reality.</u>

STRATEGIES THAT INSPIRED OURS


- **#1: Chandler brothers**
  - Achieved 37% returns over 20 years.
  - The two greatest deep value investors in history. They specialized in buying a country's crown jewel assets at fire-sale prices, i.e. 3x earnings or less.
  - Bought UFJ and Japanese megabanks at 1.8x normalized earnings.
  - Bought SK corp, Korean oil refiner, at 1x earnings.


- **#2: Nick sleep and Qais Zakaria**
  - Returned 18.4% after fees for 12 years.
  - Combined ultra deep value investing with Munger-style investing in compounders.
  - The result: a portfolio that combined Costco with…Nigerian cement companies.

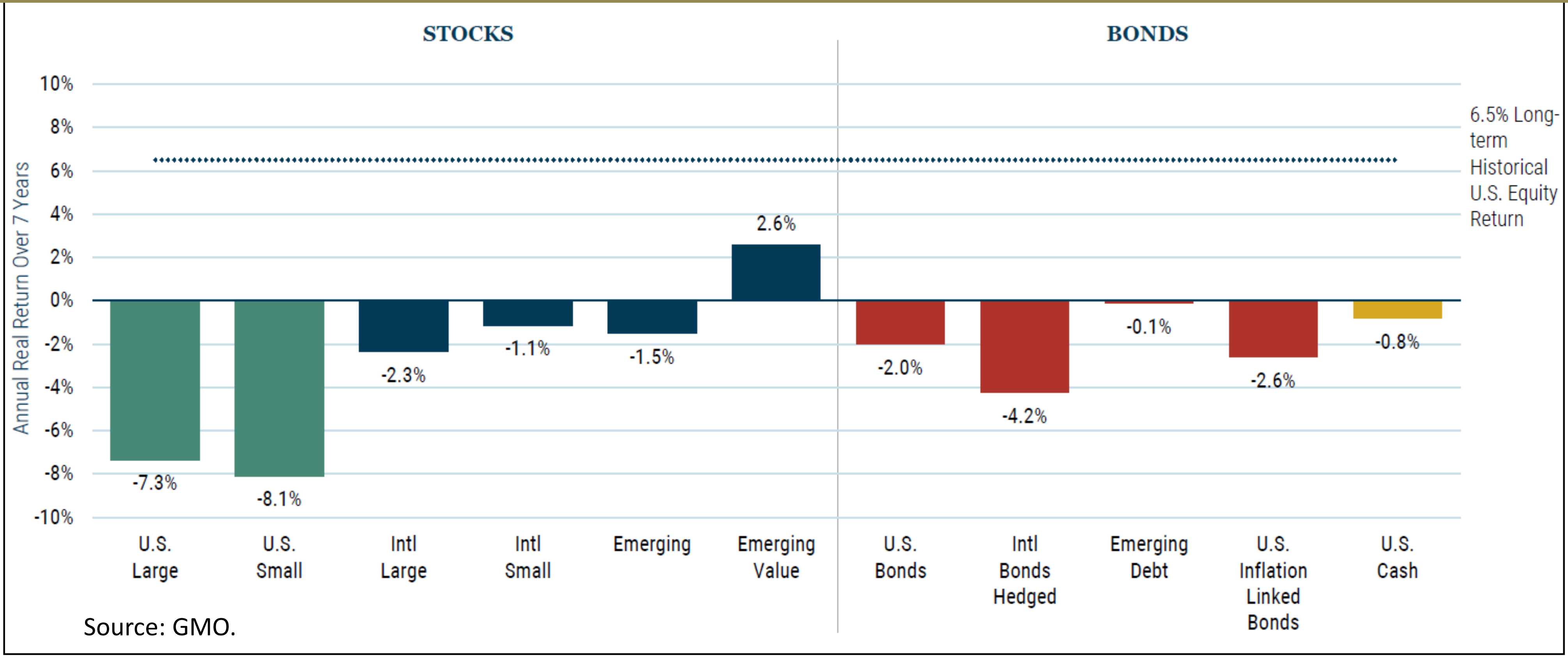
THE WORLD TODAY

"The Deluge" from Genesis.

- We live in a world choking on capital and starved for return.
- Yields can't finance the biggest retirement wave in human history. So the developed world has piled into equities + risk.
- **Nobel-prize winner Reuven Brenner:** when people are doomed, it's rational for them to gamble even though gambling is irrational.
- This is a dangerous time.

FINANCIAL REPRESSION

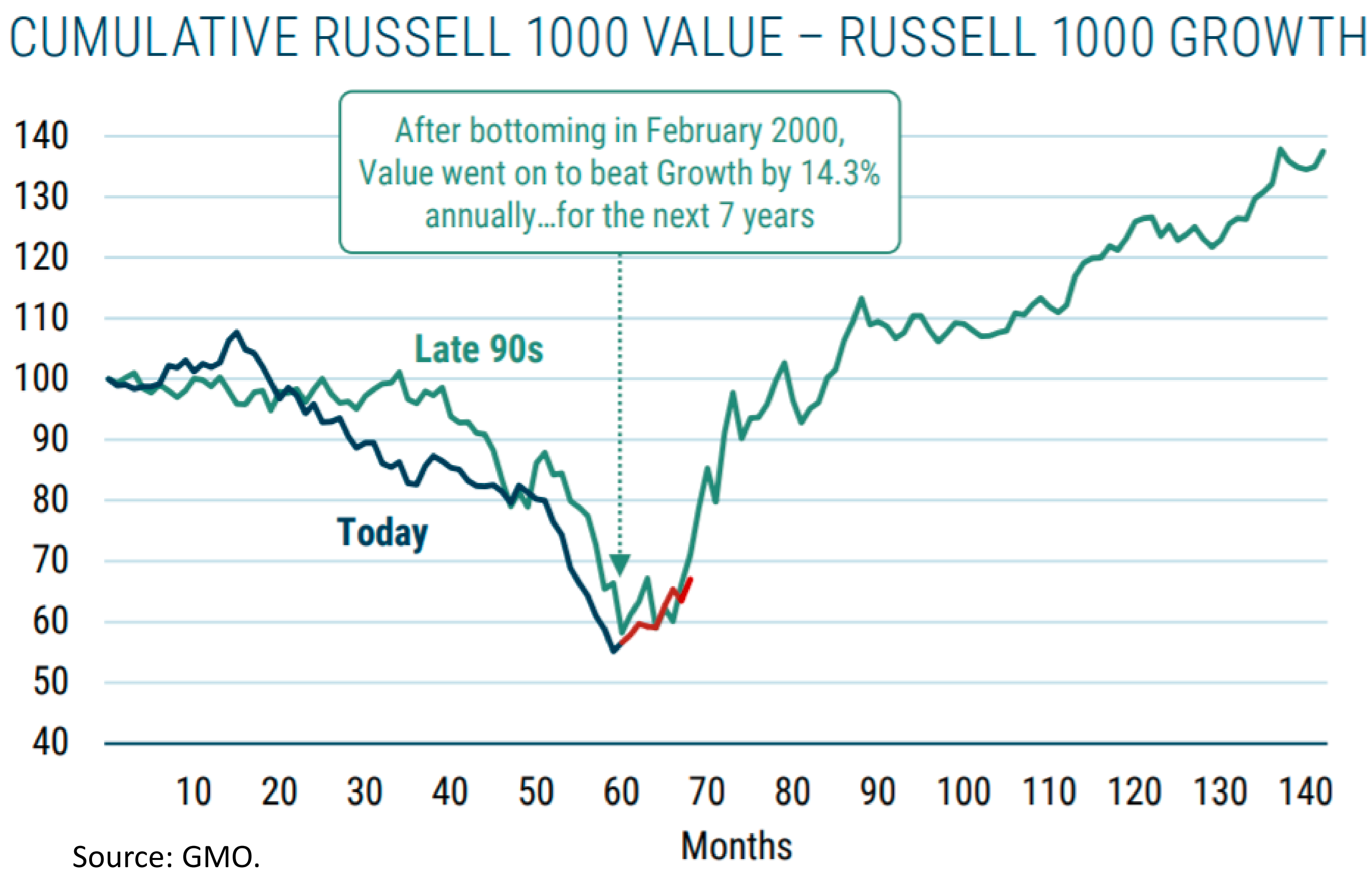
GMO's 7-year Annual Return Forecast by Asset Class



Source: GMO.

- GMO is predicting a 50% cumulative loss in equities over the next 7 years.

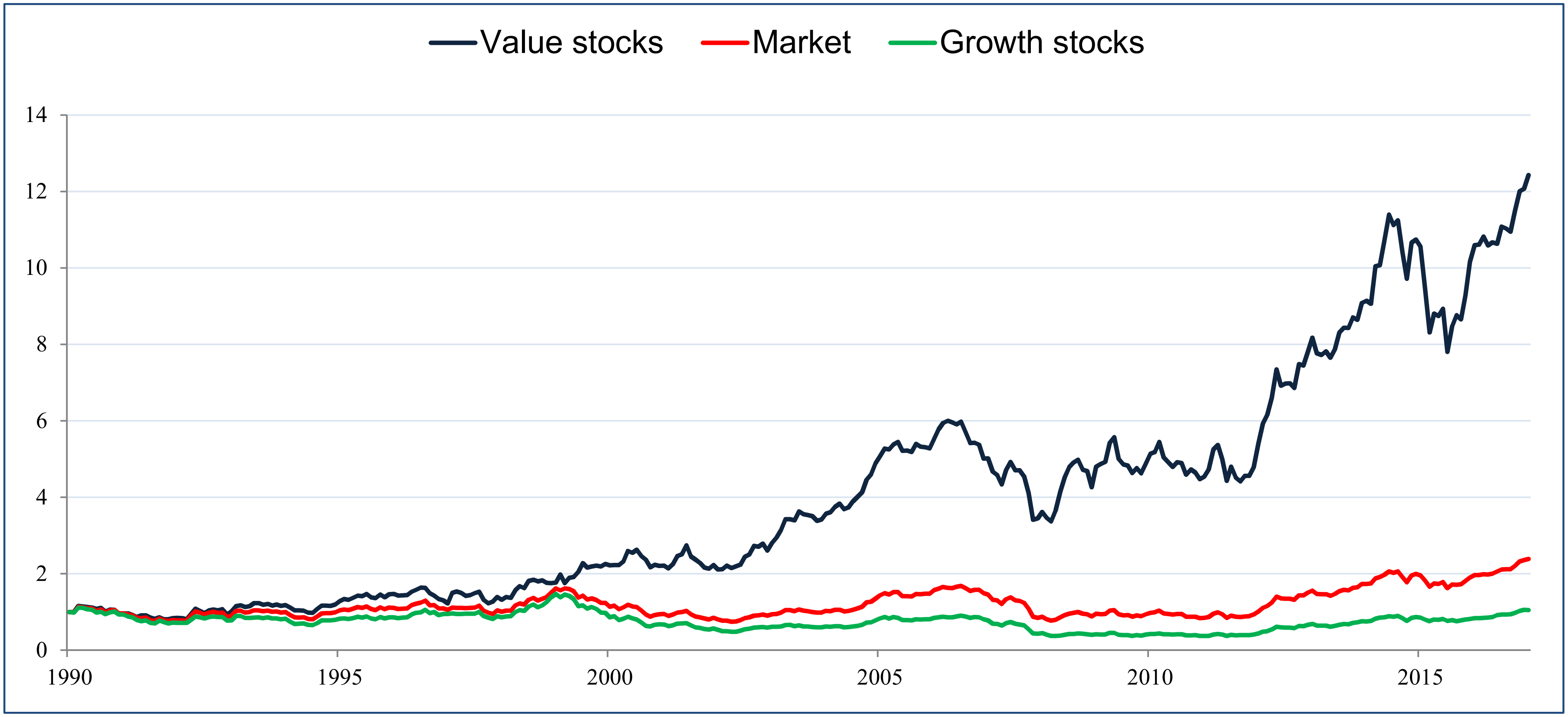
WHAT WORKS IN STAGNANT MARKETS



Source: GMO.

- The US stock market is priced for a "lost decade."
- Last time this happened was in 2000. Back then, value went on to beat growth by 14% annually for 7 years. There's a historic opportunity in value.

VALUE IN STAGNANT MARKETS



- From 1990 to 2018, Japan experienced not just a lost decade but a lost generation. The Japanese market returned just 3% a year for almost 30 years.
- However, Japanese value stocks returned 7% a year (market cap-weighted) versus 0% for growth.

RETURNS BEFORE FEES (unaudited, 6/30/2022)

	2016 (partial)	2017	2018	2019	2020	2021	Since inception
Dakota Summit	8.5%	19.9%	-6.3%	39.5%	20.3%	6.6%	**10.4%**
S&P 500	10.8%	21.8%	-4.4%	31.5%	18.4%	28.7%	**12.8%**
R3000 Value							**8.95%**

- Fee structure: 1% management fee. 10% performance fee.
- After fees, returns would have been roughly 9.4%.

THE MORALITY OF INVESTING

- "Manage your clients' money as though it was your parents' money."
- That statement touches something deep because capital means our lives can be about more than subsistence.
- Our firm's success will depend on how much we can embody that principle.

DISCLAIMER

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