Focused Growth Overview

The Focused Growth strategy is based on the simple belief that returns in the equity markets will follow earnings growth over the long-term. As such, we purchase high quality companies in attractive industries that possess long-term growth opportunities greater than that of the broader market. We want to own these businesses as long as these advantages persist, and long-term return projections remain attractive.

Each investment is made with a 3 – 5 year time horizon in mind so that the favorable growth attributes of our portfolio companies are allowed to compound in a tax efficient manner. While the investment philosophy is straightforward, our skills determine exactly which companies fit these criteria. As a general rule, the Focused Growth strategy seeks to invest in companies that are disrupting existing and sometimes sluggish business models, businesses with network characteristics that are very difficult if not impossible to replicate, and businesses with predictable and recurring revenue streams. Many times, companies will have more than one of these characteristics and these favorable business models can be found in a variety of industries. Below, we highlight some of our portfolio companies that fall within each category.

Owning Disruptors

We live in a time in which new technologies are posing threats to entrenched business models across a number of industries. Amazon alone has caused major disruption across the retail, media, consumer staples, and technology sectors and is rumored to be exploring an entry into the health care arena. Entire business models have had to be rethought and, in some cases, reworked as the result of competition from this one company. Some businesses were simply unable to compete in the new world foisted upon them by Amazon while others endured, but at materially lower levels of profitability. While Amazon is the most obvious example of technologically driven disruption, this is a phenomenon occurring across many different industries driven by many different disruptors. Facebook and Google have driven a shift in the global advertising market towards targeted digital advertising. Since 2015, these two companies have combined for well over 100% of the growth in the global advertising market. Intuitive Surgical is driving an ever-greater share of surgical procedures towards robotic surgery. Robotic surgery delivers better patient outcomes and lower long-term costs to the health care system. Alibaba and JD.com are doing in the e-commerce market in China what Amazon has done in the US and much of the rest of the developed world. In fact, it can be argued that e-commerce in China is more developed than it is in the United States and these two companies are a key reason why. The pace of technological disruption is quickening and its effect can be found across all industries. This creates both uncertainty and opportunity and is a strong argument for active, fundamental based investing.

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Enduring Networks

A strong network puts up a competitive moat around a business model that can protect it from technological or any other form of disruption. Visa and Mastercard are two portfolio companies that are a good example of this dynamic. With 60%+ operating margins and high rates of long-term revenue growth driven by a shift from cash towards card-based transactions, there are many seeking to disrupt the Visa and Mastercard franchises. However, the massive number of member bank and retail partners these companies have garnered coupled with the multi-decades long investments made in a reliable and secure payment network makes this a business that is very difficult to disrupt. The same can be said for the cable companies. Both Charter and Comcast have seen their business come under attack in recent years from direct to consumer content products that give consumers the ability to cut the cord and walk away from their cable subscriptions. However, because these companies own the broadband wires over which these new content offerings must travel, they are able to deal with the competition associated with a changing landscape in pay TV and now, broadband cable has become the center of the plate offering around which ancillary services are provided. Because of the hundreds of billions of dollars spent over multiple decades building out the cable plant, Charter and Comcast have unique connectivity with the consumer. These companies own the "last mile" to the consumer. If they cannot keep a consumer on a cable subscription, they will keep them on a broadband plan. Payment processing networks and cable businesses are good examples of defensible network businesses in completely different areas of the economy.

Recurring Revenue Streams

The notion of a predictable, recurring revenue stream as an attractive investment characteristic is pretty straightforward as highly valued by investors. Recurring revenue streams can be found in subscription businesses, businesses with high rates of customer retention, and even consumer staples businesses, provided market shares are stable and brand loyalty rates are high. Adobe is a good example of a company that transformed its business model from one of annual sales of new software products into a recurring subscription business in which over 90% of sales are subscription based and new innovation is rewarded with higher subscription prices. Adobe products are the standard in creative fields and introduction to these products for many occurs during school, which creates a steady stream of new subscribers as creative students leave universities and rise through corporate marketing departments. In the insurance industry, Verisk collects data from the top 100 property and casualty insurers, which it aggregates, analyzes and sells back to these same companies through its analytics service business. Both the data collection and subscriber sales are recurring aspects of this business. Predictable, recurring revenue streams can be found in businesses across a variety of sectors and these businesses have a unique ability to compound earnings growth over an extended period of time.

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Conclusion

Whether it be through owning businesses with disruptive technologies, defensible networks, large and recurring income streams, or all of the above, the Focused Growth strategy seeks to own companies that can deliver steady earnings growth that compounds over time. While the traits discussed in this overview are not a comprehensive checklist that each company must meet in order for inclusion in the portfolio, it provides a sense of our thinking when we say we intend to purchase high quality companies in attractive industries that possess long-term structural growth opportunities.

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