Mutoro Group Partners, LP
Second Quarter 2023 Letter

August 15, 2023

"Often when a young coach comes to see me to ask for advice, I tell them to imprint their vision of the game and not to forget that the game itself is a good coach and that observation is often as effective as talking.

"During a match, there are billions of possible combinations, and that's what makes football the wonderful, rich, surprising sport that it is. A player is constantly adapting his technique to the situation. He cannot act just on reflex. He has to prepare, correct himself, find his place, decide: All this is something he acquires, he works on, he builds on. But he will need to be innovating constantly as he makes his decisions because the situation will never be exactly the same as whatever he experienced in the previous scenario, in the previous match. Our sport depends on three criteria: ball control, decision making, and the quality of execution." – Arséne Wenger[i]

"Rather than being told which tools are available for which ends, it is more useful to invent your own tools." – Richard Serra[ii]

	Annual Percentage Change		
	Mutoro Group Partners, LP (Gross)	Mutoro Group Partners, LP (Net)	HFRI Fund Weighted Composite Index
2015	(3.5%)	(5.0%)	(1.1%)
2016	24.5%	18.9%	5.4%
2017	(3.3%)	(4.7%)	8.6%
2018	(0.9%)	(2.4%)	(4.7%)
2019	30.0%	23.9%	10.4%
2020	34.2%	25.7%	11.8%
2021	8.5%	5.5%	10.2%
2022	(44.8%)	(45.7%)	(4.3%)
H1 2023	13.5%	12.7%	3.4%
Aggregate	36.6%	5.7%	45.5%
Annualized	3.7%	0.7%	4.5%

Dear Partner,

In the first half of 2023, our fund experienced a 13.5% gross increase and, after expenses, a net rise of 12.7%. We finished the quarter with the same 13 portfolio holdings with which we began the year.

On October 1, 1996, the Frenchman Arséne Wenger arrived in London from a stint in Japan to lead the professional football club Arsenal. He was relatively unknown and the club's first foreign manager. He observed something that troubled him. The club's players at halftime of matches would eat chocolate candy bars and drink sodas, and they saw nothing wrong with this. He hired an innovative nutritionist and changed things. In Wenger's words, this "enabled the players to improve the consistency of their performance and made them conscious of good dietary habits." The club's performance rose, and it won the league title the following season because of this and other changes to their "invisible training," i.e., activities outside the field of play, such as nutrition, sleep, and therapy, both mental and physical. I share this anecdote in case you, like me, often wonder what habits professionals today from various fields have that time might regard as unhelpful. I also share this so you, like me, maintain perpetual curiosity in your work and intellectual humility in the face of new ideas that may seem silly but could someday be fundamental. On to the update.

In my first quarter letter, I introduced the concept of the [*Polyhedral View* of industries]. I wanted to emphasize the importance of understanding the multifaceted nature of businesses and the significance of industry selection in our investment decisions. This perspective is instrumental as we construct a long-term, concentrated portfolio through fundamental analysis. Now, at the mid-year mark, it seems apt to shift our focus from industry analysis to portfolio management. So, let's look closer at our portfolio's current structure and some reasons behind its performance this year.

Effective investing extends beyond merely identifying and acquiring undervalued assets. For us, it encompasses four critical stages: Strategy, Planning, Application, and Observation. **Strategy** involves determining the optimal weighting of assets within our portfolio. This strategy is then translated into actionable steps during the **Planning** phase, where we devise methods to limit downside risk while optimizing upside. The **Application** stage sees us implement our strategies through executing these plans. But our process does not stop post-acquisition. Following those three stages is **Observation**. This stage allows us to monitor the operating performance of the assets we acquire, manage risks, and identify new opportunities. We can then reapply these learnings into our strategies so that our investment process becomes a continuous journey of making decisions, applying them, and learning from the outcomes. It's within the lattermost phase that I've observed some aspects of our fund I wanted to share with you that have held back our performance this year. In the short run, only so much of this is within our control. But in the long-run I believe it reveals more upside than downside to our present holdings.

One could aptly describe our portfolio at present as a "tale of two tranches." The first tranche comprises 10 of our 13 holdings, or 77% of our businesses. Let's call this *Tranche A*. On December 31, 2022, these 10 holdings represented 48.7% of our assets under management. Through June 30, 2023, the aggregate market price of *Tranche A* surged 51.5%.

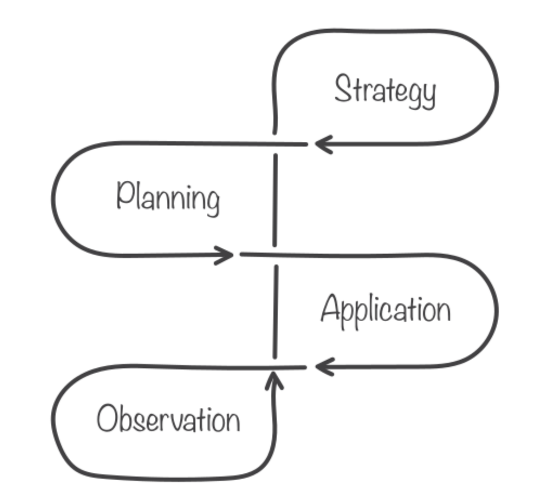

Figure 1: The continuous cycle of portfolio management

The second tranche – let's call it *Tranche B* – consisted of the remaining three holdings, or 23% of our businesses. It represented 40.1% of our assets under management at the end of 2022. (The remaining 11.2% was cash.) I intentionally overweighted my purchases in 2022 toward the business of *Tranche B*, believing them to be the most undervalued companies in our portfolio. They had declined in price more than the businesses in *Tranche A* and, by my judgement, had a more compelling price-to-value ratio. In 2023, they have declined even more. Collectively, through June 30, *Tranche B* declined a further 24.3%. Our results through mid-year were thus tempered by the price underperformance of these three holdings.

Despite their share price declines this year, the underlying businesses of *Tranche B* are competitively strong. Two of these companies operate in a market that is nearly oligopolistic and growing. The third is the only profitable entity in its sector. That's not to say that they face no challenges related to their future earning power. These challenges seem surmountable, though, and overrepresented in their current market pricings. Each company is likely to achieve revenue growth in the mid-teens or higher over the next few years, coupled with increasing returns on capital. However, prevailing market sentiment overshadows their intrinsic value. The typical business in *Tranche A* is 15 years older than the businesses of *Tranche B*, which are in more nascent industries: "Building Meaningful Connections and Relationships" and "Achieving Distinctive Personal Style and Luxury Status." (See Q1 letter.) In the current market environment this invites the skepticism of the marginal investor.

Why am I still optimistic about our portfolio's potential? Consider the current composition. The ten businesses in *Tranche A* today represent 65.0% of our assets under management; the three businesses of *Tranche B* today make up 26.7% of our assets. Barring a broad market downturn, the relative diversification in *Tranche A* somewhat limits the downside to the bulk of our portfolio. While the eventual repricing of *Tranche B* implies significant upside.

While *Tranche A* is diversified across various industries, it's worth noting that a single company represents a third of *Tranche A* and has experienced a remarkable 138.5% increase this year. While the company's stock price has surged, my analysis suggests that it is still underpriced relative to its long-term earning power. Its healthy balance sheet, consistent cash flow generation, and relative strength versus competitors bolster its value.

The table below shows the composition of our portfolio at the end of the quarter.

U.S. Public Equities	79.6%
European Public Equities	11.2%
Cash and Cash Equivalents	8.3%
U.S. Options	0.9%
Total Portfolio	100.0%

Table 1: Portfolio composition at the end of the quarter

Thank you for your ongoing commitment. I welcome your thoughts and questions. I hope this explanation of the state of our portfolio at mid-year and the continuous approach we take to asset management has been helpful. If you would like to add to your investment or know someone who might like to join us, please reach out.

Sincerely,

Godfrey M. Bakuli
Founder & Managing Partner

[i] Wenger, A. (2020). *Wenger: My Life and Lessons in Red & White.* Chronicle Books.
[ii] Serra, R. (2008, June 1). *If Not Now, When?* [Video]. Retrieved from https://www.youtube.com/watch?v=PR01UcgeJts