Qualivian Investment Partners Q1 2024 Investment Letter

July 2024

> *"The goal of investment is to find situations where it is safe not to diversify."*
>
> *– Charlie Munger*

Overview

Qualivian Investment Partners is an **investment partnership focused on long-only public equities**. We own a concentrated portfolio of 15–25 understandable companies with **wide moats**, long **reinvestment runways**, and **outstanding capital allocation**. Since we expect them to **compound capital at a mid-teens rate, we hold them** for an extended period. **We are seeking investors who are aligned with our long-term investment time horizon.** We **do not short securities.** We **do not use leverage**. We **do not use derivatives**. We are **not macro investors**. We believe that only a relatively small number of exceptional companies are worth investing in over the long term.

Our Formula

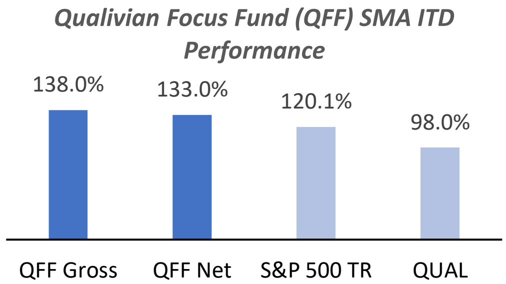
Long-Term Orientation + Long-Term Investors + Focused Portfolio + Quality Compounders = Maximizing Chance for Outperformance

Our investors should understand how we invest so they make the right decision. We encourage investors who agree with our long-term horizon and philosophy to contact Aamer Khan (aamer.khan@qualivian.com) at 617-970-9583 or Cyril Malak (cyril.malak@qualivian.com) at 917-742-2039.

Preface

We are issuing our Q1 2024 investor letter a bit later than usual. As a result, in this abbreviated letter, we are going to simply review the portfolio's performance, changes to the portfolio we made in the quarter, as well as provide a snapshot of the portfolio's characteristics as compared to the broader market to remind investors of the key attributes of the portfolio. We will also have detailed performance metrics and our top and bottom performing stocks in the quarter in the Appendix as usual. We will resume our regular programming with insights into our investment thinking as well as a deep dive Quality Compounder stock review in our upcoming Q2 2024 investor letter, as we normally do.

Cumulative Performance Since Inception[1] Through March 31, 2024



Qualivian Investment Partners introduced a Separately Managed Account (SMA) product for investors managed in the same manner as the Qualivian Focus Fund in the first quarter of 2024. The terms reflect a lower management fee than in our Founders Class shares. As explained further in Appendix 1, the performance above represents the actual performance of the Qualivian Focus Fund adjusted by removing fund expenses and the management fee charged to fund investors and applying the lower management fee for SMA investors (the "SMA Performance"). As a general matter, all performance numbers herein represent the SMA Performance as adjusted.[2]

SMA Performance Inception-to-Date and Q1 2024

Since inception through March 31, 2024, we have **outperformed the iShares MSCI USA Quality Factor ETF (QUAL) by 40.0% and 35.0% on a gross and net basis. Similarly, we have outperformed the S&P 500 by 17.9% and 12.9% on a gross and net basis, respectively, with a Beta of 1.0.**

During Q1 2024, we outperformed the iShares MSCI USA Quality Factor ETF (QUAL) by 0.9% and 0.8% on a gross and net basis. Similarly, we outperformed the S&P 500 by 2.0% and 1.9% on a gross and net basis, respectively.

Our detailed performance summary is presented in Appendix 1 for both our Founders Class shares in our pooled vehicle, as well as the performance reflecting our SMA terms.

Portfolio Highlights

Portfolio Changes in Q1 2024

We sold our positions in Johnson & Johnson (JNJ) and Northrop Grumman (NOC) and trimmed our Google (GOOGL) position. We used the proceeds to initiate a new position in Brown and Brown (BRO), as well as added to our positions in Arthur J. Gallagher (AJG), Amazon (AMZN), Danaher (DHR), and S&P Global (SPGI).

[1] Qualivian Focus Fund inception date is December 14, 2017.

[2] Note the higher gross performance compared to Founders Class shares in the Qualivian Focus Fund (QFF). This reflects that we do not flow fund management expenses (capped in our commingled fund, QFF, at 50 bps to cover expenses such as Fund Administration for example) through the SMA product. In addition, the lower management fee (35 bps annualized) is reflected in the Net performance fee.

Exits and New Positions

We exited our position in JNJ after owning it for a little over a year. The overhang from the Talc powder ovarian cancer and mesothelioma lawsuits against JNJ reduced our confidence in how to ring fence the potential liability from the thousands of lawsuits against JNJ in all 50 states. We decided we had better opportunities to redeploy the proceeds into higher returning alternatives.

We exited our NOC position after owning it almost exactly one year as key strategic programs, such as the Sentinel Program among other EMD[3] programs. In the case of the Sentinel Program, NOC experienced significant cost overruns, requiring the US Air Force to review & restructure the program. This resulted in Northrop Grumman having to take charges against this program but also delaying the more profitable and cashflow generating Production & Deployment phase of this contract out into the future.

It became increasingly hard for us to determine whether we had adequate visibility and more importantly confidence into Northrop's forward earnings and cashflow growth given these unanticipated charges and development program delays.

Finally, we initiated a new position in BRO, a Quality Compounder that we think can continue to grow organically and through consolidating the middle market insurance distribution sector and deliver above market returns. We think BRO, much like our position in AJG, can generate strong revenue, earnings and cashflow growth for the foreseeable future both organically and via tuck-in acquisitions of the highly fragmented insurance brokerage industry.

For our top 3 and bottom 3 contributors in the quarter, please refer to Appendix 2.

Fundamentals of Our Portfolio vs. the S&P 500

As we kick off a new year, we thought it would make sense to review our portfolio's characteristics vs. the S&P 500. As can be seen from the tables below, the Qualivian Focus Fund (QFF) continues to have superior gross, operating, and free cashflow (FCF) margins as compared to the S&P 500. Furthermore, QFF's forward consensus revenue and EPS growth estimates continue to outpace that of the S&P 500. Our portfolio trades at a premium to the S&P 500 but considering the superior margin, growth, and return characteristics, that makes sense.

	2023 Gross Margin	2023 EBITDA Margin	2023 EBIT Margin	2023 FCF Margins	2018-2023 FCF/Sh CAGR
QFF	57.5%	33.9%	28.8%	18.3%	15.7%
S&P 500	33.0%	20.2%	14.5%	10.9%	7.4%

	LT Rev Growth [(1)]	LT EPS Growth [(1)]
QFF	9.2%	15.7%
S&P 500	5.4%	12.4%

[(1)] *Long-term Revenue and EPS growth estimates are based on 2026 consensus estimates vs. 2023 actuals.*

3 EMD = Engineering & Manufacturing Development (EMD) Phase, which is pre-Production & Deployment phase when programs scale up and come down the cost curve due to economies of scale and manufacturing learnings.

	2025 EV/Sales [2]	2025 P/E [2]	2025 P/FCF [2]	LTM FCF Yield [2]
QFF	7.1x	26.9x	26.3x	2.9%
S&P 500	2.8x	20.2x	23.1x	3.7%

[2] *As of 7/12/2024.*

We believe QFF's superior fundamentals as compared to the overall market will generate S&P 500-beating returns over an investment cycle as the market appreciates the higher growth, margin, and return on capital characteristics in the stocks we own.

Ending Thoughts

We look forward to sharing our thoughts on our investment approach and to keeping you abreast of our performance and changes to the portfolio. If you would like additional information about Qualivian, please refer to Appendix 3 for links to prior Investor Letters, our investor presentation, and an interview that Aamer did with Insider Monkey. In the meantime, if you have any questions, please feel free to reach out to us at the links below.

With best wishes,

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Appendix 1: Quarterly Performance Tables

Performance for Qualivian Focus Fund Founders Class Share Terms

	A QFF Gross Returns	B QFF Net Returns [1]	C QUAL [2]	D S&P 500 TR Index [3]	Difference with QUAL A-C Gross	B-C Net	Difference with S&P 500 Index A-D Gross	B-D Net
Dec. 2017 [4]	**-2.9%**	**-2.9%**	**-0.1%**	**0.5%**	**-2.7%**	**-2.8%**	**-3.4%**	**-3.4%**
Q1 2018	5.4%	5.3%	-0.2%	-0.8%	5.7%	5.5%	6.2%	6.0%
Q2 2018	4.2%	4.1%	0.9%	3.4%	3.3%	3.2%	0.8%	0.6%
Q3 2018	5.6%	5.5%	8.3%	7.7%	-2.7%	-2.8%	-2.1%	-2.2%
Q4 2018	-14.6%	-14.8%	-15.1%	-13.5%	0.4%	0.3%	-1.1%	-1.3%
2018	**-0.9%**	**-1.5%**	**-7.4%**	**-4.4%**	**6.5%**	**5.9%**	**3.5%**	**2.9%**
Q1 2019	17.7%	17.5%	15.4%	13.6%	2.3%	2.1%	4.0%	3.9%
Q2 2019	5.3%	5.2%	3.3%	4.3%	2.0%	1.9%	1.0%	0.9%
Q3 2019	2.4%	2.2%	1.0%	1.7%	1.3%	1.2%	0.7%	0.5%
Q4 2019	10.5%	10.3%	9.3%	9.1%	1.2%	1.0%	1.4%	1.3%
2019	**40.2%**	**39.4%**	**31.6%**	**31.5%**	**8.6%**	**7.8%**	**8.7%**	**7.9%**
Q1 2020	-14.8%	-14.9%	-19.8%	-19.6%	5.0%	4.9%	4.8%	4.7%
Q2 2020	30.2%	30.0%	18.4%	20.5%	11.8%	11.6%	9.6%	9.5%
Q3 2020	9.3%	9.1%	8.2%	8.9%	1.1%	0.9%	0.3%	0.2%
Q4 2020	7.6%	7.4%	12.0%	12.1%	-4.4%	-4.6%	-4.6%	-4.7%
2020	**30.4%**	**29.6%**	**15.1%**	**18.4%**	**15.3%**	**14.6%**	**12.0%**	**11.2%**
Q1 2021	2.5%	2.3%	4.8%	6.2%	-2.3%	-2.5%	-3.7%	-3.9%
Q2 2021	12.5%	12.3%	9.1%	8.5%	3.4%	3.2%	3.9%	3.8%
Q3 2021	-1.2%	-1.4%	-0.9%	0.6%	-0.4%	-0.5%	-1.8%	-2.0%
Q4 2021	4.4%	4.3%	10.5%	11.0%	-6.1%	-6.2%	-6.6%	-6.8%
2021	**18.8%**	**18.2%**	**25.3%**	**28.7%**	**-6.4%**	**-7.1%**	**-9.9%**	**-10.5%**
Q1 2022	-11.0%	-11.1%	-7.5%	-4.6%	-3.5%	-3.6%	-6.4%	-6.5%
Q2 2022	-17.6%	-17.8%	-17.0%	-16.1%	-0.6%	-0.8%	-1.5%	-1.7%
Q3 2022	-4.8%	-5.0%	-7.0%	-4.9%	2.1%	2.0%	0.0%	-0.1%
Q4 2022	6.4%	6.2%	9.6%	7.6%	-3.3%	-3.4%	-1.2%	-1.3%
2022	**-25.8%**	**-26.2%**	**-21.7%**	**-18.1%**	**-4.0%**	**-4.5%**	**-7.6%**	**-8.1%**
Q1 2023	8.4%	8.3%	8.9%	7.5%	-0.4%	-0.6%	0.9%	0.8%
Q2 2023	11.9%	11.7%	8.7%	8.7%	3.2%	3.0%	3.1%	3.0%
Q3 2023	-1.6%	-1.8%	-2.3%	-3.3%	0.6%	0.5%	1.6%	1.5%
Q4 2023	10.7%	10.6%	11.6%	11.7%	-0.9%	-1.1%	-1.0%	-1.1%
2023	**32.1%**	**31.3%**	**29.1%**	**26.3%**	**3.0%**	**2.2%**	**5.8%**	**5.1%**
Q1 2024	12.5%	12.3%	11.7%	10.6%	0.8%	0.6%	1.9%	1.7%
ITD [5]	**130.7%**	**122.2%**	**98.0%**	**120.1%**	**32.7%**	**24.2%**	**10.6%**	**2.1%**

(1) As of November 2019, we began calculating Fund net performance reflecting new proposed Founders Class share terms of gross performance less a tiered management fee (75bps for first $20M, 65bps for next $20M, and 50bps for anything above $40M) and no performance fee. The scenario above reflects a $50M Founders Class investment. We have recast all the historical net performance data to reflect these new assumptions. Prior to November 2019, our net performance numbers reflected the terms of our Class A Shares, which have different terms (1% management fee and 15% performance fee over the spread to the S&P 500 returns), resulting in different net performance than shown above.

(2) QUAL represents iShares MSCI USA Quality ETF which replicates the MSCI USA Quality Index.

(3) S&P 500 Total Return Index which includes reinvested dividends.

(4) Dec. 2017 period represemts Dec. 14 (Fund launch) through Dec. 31, 2017.

(5) ITD = Inception-to-date and represents the time period from Dec. 14, 2017 through March 31, 2024.

Performance for Qualivian Focus Fund with SMA Terms

	A QFF Gross Returns	B QFF Net Returns [1]	C QUAL [2]	D S&P 500 TR Index [3]	Difference with QUAL A-C Gross	Difference with QUAL B-C Net	Difference with S&P 500 Index A-D Gross	Difference with S&P 500 Index B-D Net
Dec. 2017 [4]	**-2.8%**	**-2.8%**	**-0.1%**	**0.5%**	**-2.7%**	**-2.7%**	**-3.3%**	**-3.3%**
Q1 2018	5.6%	5.5%	-0.2%	-0.8%	5.8%	5.7%	6.3%	6.2%
Q2 2018	4.4%	4.3%	0.9%	3.4%	3.5%	3.4%	0.9%	0.8%
Q3 2018	5.8%	5.7%	8.3%	7.7%	-2.5%	-2.6%	-2.0%	-2.0%
Q4 2018	-14.5%	-14.6%	-15.1%	-13.5%	0.5%	0.5%	-1.0%	-1.1%
2018	**-0.4%**	**-0.7%**	**-7.4%**	**-4.4%**	**7.0%**	**6.7%**	**4.0%**	**3.7%**
Q1 2019	17.8%	17.7%	15.4%	13.6%	2.5%	2.4%	4.2%	4.1%
Q2 2019	5.5%	5.4%	3.3%	4.3%	2.2%	2.1%	1.2%	1.1%
Q3 2019	2.5%	2.4%	1.0%	1.7%	1.5%	1.4%	0.8%	0.7%
Q4 2019	10.6%	10.6%	9.3%	9.1%	1.3%	1.2%	1.6%	1.5%
2019	**40.9%**	**40.4%**	**31.6%**	**31.5%**	**9.3%**	**8.9%**	**9.4%**	**9.0%**
Q1 2020	-14.7%	-14.7%	-19.8%	-19.6%	5.1%	5.0%	4.9%	4.9%
Q2 2020	30.3%	30.2%	18.4%	20.5%	12.0%	11.9%	9.8%	9.7%
Q3 2020	9.4%	9.3%	8.2%	8.9%	1.2%	1.1%	0.5%	0.4%
Q4 2020	7.7%	7.6%	12.0%	12.1%	-4.3%	-4.4%	-4.4%	-4.5%
2020	**31.0%**	**30.6%**	**15.1%**	**18.4%**	**16.0%**	**15.5%**	**12.6%**	**12.2%**
Q1 2021	2.6%	2.5%	4.8%	6.2%	-2.2%	-2.3%	-3.6%	-3.7%
Q2 2021	12.6%	12.5%	9.1%	8.5%	3.5%	3.4%	4.1%	4.0%
Q3 2021	-1.1%	-1.2%	-0.9%	0.6%	-0.3%	-0.3%	-1.7%	-1.8%
Q4 2021	4.5%	4.5%	10.5%	11.0%	-6.0%	-6.0%	-6.5%	-6.6%
2021	**19.4%**	**19.0%**	**25.3%**	**28.7%**	**-5.8%**	**-6.2%**	**-9.3%**	**-9.7%**
Q1 2022	-10.8%	-10.9%	-7.5%	-4.6%	-3.3%	-3.4%	-6.2%	-6.3%
Q2 2022	-17.5%	-17.6%	-17.0%	-16.1%	-0.5%	-0.6%	-1.4%	-1.5%
Q3 2022	-4.7%	-4.8%	-7.0%	-4.9%	2.3%	2.2%	0.2%	0.1%
Q4 2022	6.5%	6.4%	9.6%	7.6%	-3.1%	-3.2%	-1.1%	-1.1%
2022	**-25.4%**	**-25.6%**	**-21.7%**	**-18.1%**	**-3.7%**	**-3.9%**	**-7.3%**	**-7.5%**
Q1 2023	8.6%	8.5%	8.9%	7.5%	-0.3%	-0.4%	1.1%	1.0%
Q2 2023	12.0%	11.9%	8.7%	8.7%	3.3%	3.2%	3.3%	3.2%
Q3 2023	-1.5%	-1.6%	-2.3%	-3.3%	0.8%	0.7%	1.8%	1.7%
Q4 2023	10.8%	10.8%	11.6%	11.7%	-0.8%	-0.9%	-0.8%	-0.9%
2023	**32.7%**	**32.3%**	**29.1%**	**26.3%**	**3.6%**	**3.2%**	**6.5%**	**6.0%**
Q1 2024	12.6%	12.5%	11.7%	10.6%	0.9%	0.8%	2.0%	1.9%
ITD [5]	**138.0%**	**133.0%**	**98.0%**	**120.1%**	**40.0%**	**35.0%**	**17.9%**	**12.9%**

(1) *As of January 2024, we introduced a Separately Managed Account product based on our core Qualivian Focus Fund (QFF) strategy. We have recast QFF's gross and net performance above reflecting new SMA terms which do not include 50bps of fund management expenses (e.g., Fund Administration and tax filing fees) in our gross performance numbers less a flat 35bp management fee which is reflected in our Net Returns. This compares to the performance in our pooled vehicle, Qualivian Focus Fund, which does incur 50bps fund management expenses that is included in our calculation of its Gross performance (hence the 620bp differential in ITD Gross returns as of 12/31/2023), and which has higher tiered management fee (see Founders Class shares performance table for the management fee detail) which further explains the 930bp Net return differential in ITD Net returns as of 12/31/2023.*

(2) *QUAL represents iShares MSCI USA Quality ETF which replicates the MSCI USA Quality Index.*

(3) *S&P 500 Total Return Index which includes reinvested dividends.*

(4) *Dec. 2017 period represemts Dec. 14 (Fund launch) through Dec. 31, 2017.*

(5) *ITD = Inception-to-date and represents the time period from Dec. 14, 2017 through March 31, 2024.*

In January of 2024, we introduced a Separately Managed Account (SMA) product which replicates our core pooled vehicle product (Qualivian Focus Fund — QFF) for interested investors. The key difference is that the SMA product will not incur the typical fund management expenses, such as fund administration, tax filing and audit fees, which we cap at 50 bps in QFF. Furthermore, the SMA product will incur a lower management fee of 35 bps annually, as compared to the tiered management fee in QFF (75 bps for the first $20 million, 65 bps for the next $20 million, and 50 bps for anything above).

Appendix 2: Top 3 and Bottom 3 Contributors for Q1 2024

Our top three contributors in Q4 2023 were Meta Platforms (META), O'Reilly Automotive (ORLY) and Amazon (AMZN). Our bottom three contributors were Watsco (WSO), Northrop Grumman (NOC), and S&P Global (SPGI).

Top 3 Contributors

Meta Platforms Inc. (META): Q1 2024 revenues grew 27% and EPS grew 114% against depressed levels a year ago, beating expectations and continuing momentum from Q4 2023 as ad revenues grew double digits across all geographies coming in better than expected with ad impressions growing 20% and price/ad growing by 6% in the quarter. User/engagement trends continued to show stability with DAPs[4] growing 7%. The company continued to deliver on CEO Zuckerberg's year of "Efficiency" focus at Meta, with operating margins coming in 110 bps[5] ahead of expectations. Furthermore, FCF, at $12.5Bn came in 16% ahead of expectations, highlighting the operational improvement in cost efficiencies and earnings rebound, as well as more discipline with capital expenditure. Management did revise their capex guidance upward to meet the investment requirements behind their push into Generative AI applications, like the announcements made by their peers such as Microsoft, Alphabet, as well as Amazon, among others. We will be keeping a watchful eye on the heightened investment spending going forward.

O'Reilly Automotive (ORLY): The company reported Q1 2024 revenue growth of 7% on a same store sales comp of 3.4%, while EPS grew 11%, both of which missed expectations slightly. Management as well as competitor commentary suggested a moderating demand picture industry-wide, especially in the Professional or DIFM (Do-It-For-Me) segment. Operating cost leverage from a growing topline was offset by wage inflationary pressures, resulting in operating margins coming down by 40bps year-on-year. The company reaffirmed full-year guidance despite the slight miss in the quarter.

ORLY is the leader in the automotive retail parts marketplace and has out-executed the competition, especially the smaller mom and pop auto parts stores that cater to the retail and auto mechanic shops in the US. Furthermore, its historical deployment of its excess cash to repurchase its shares continues to be a key linchpin of its ability to generate shareholder returns more than the market. While we are maintaining a watchful eye on slowing market trends, we continue to see ORLY as a long-term core holding in the fund.

Amazon (AMZN): Amazon's Q1 2024 results beat top- and bottom-line expectations, continuing its top-line reacceleration with growth of 13.0%, including continued reacceleration in AWS (Amazon Web Services) which grew 17%. Advertising revenues grew 24%, which we consider an area of further opportunity for AMZN.

Encouragingly, the company continued its streak of delivering impressive cost efficiencies in Q1 with operating margins jumping 700bps vs. Q1 2024 and 280bps ahead of consensus expectations. We remain comfortable with our long-term outlook for Amazon's eCommerce and AWS businesses, and expect they have new avenues of growth to exploit in scaling their advertising and generative AI business in the years ahead.

[4] DAP: Daily Active People.
[5] Bps: basis points.

Bottom 3 Contributors

Watsco (WSO): In what is traditionally the seasonally weakest quarter in the year, WSO reported a slight miss on topline with revenue growth of 1% and a more noticeable miss on EPS which declined 23% vs. the much tougher comparison to year-ago levels. In large part, the EPS miss was driven by higher SG&A expenses, reflecting a one-time jump in expenses which should not reoccur as well as actions taken to streamline branches at outset of the year. We should see reductions in SG&A vs. year-ago levels for rest of year. Furthermore, heading into the seasonally stronger portion of the year, management indicated seeing April sales activity pick up at high single-digit levels in the month.
We believe WSO's growth rates should revert to more normalized mid-to high single digits on revenue and low- to mid-teens on EPS basis over the coming years, after much higher levels during the product-constrained inflationary COVID period when the company grew revenues and earnings at much higher clips. We remain constructive on WSO's long-term fundamentals and returns versus the broader market.

Northrop Grumman (NOC): The company reported beats on top and bottom-line results, with revenues growing 9% and EPS growing 15% in the quarter. Operating margins came in line, while FCF disappointed, declining by almost a $1Bn in the quarter due to heightened inventory & Capex levels required by setbacks in Sentinel and other key programs. While company management reaffirmed full year guidance, the setbacks the company has been experiencing for the last couple of years with key development programs (like Sentinel) drove us to reevaluate our position in NOC, resulting in our exit from the position earlier in the quarter.

S&P Global (SPGI): SPGI delivered strong revenue and EPS growth of 14% and 28% (adjusting for sale of its Engineering Solutions business), or 10% and 27% on a GAAP reported basis. Management was able to deliver strong operating margin improvement of 350bps on a reported (as well as adjusted) basis in the quarter. Furthermore, management upped their FY2024 revenue guide for the Ratings and Index businesses, while reaffirming their revenue guide for the remaining segments.
We believe SPGI is well positioned to continue delivering at least mid-teens earnings and cashflow growth for the foreseeable future leveraging their oligopolistic position in their Ratings and Index businesses, as well as their unique collection of data assets in their Market Intelligence and Commodity Insights businesses.

Appendix 3: Links to Additional Information

Investor Presentation	QIP Focus Fund Final December 2023
Insider Monkey Interview	https://www.insidermonkey.com/blog/exclusive-interview-with-aamer-khan-of-qualivian-investment-partners-886994/
Last 4 Investor Letters	QIP Q4 2023 Final.PDF QIP Q3 2023 Final.PDF QIP Q2 2023 Final.PDF QIP Q1 2023 Final.PDF

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