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# Two Centuries Investments

## Warren Buffett's Secret Factor

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# INTANGIBLES INVESTING:

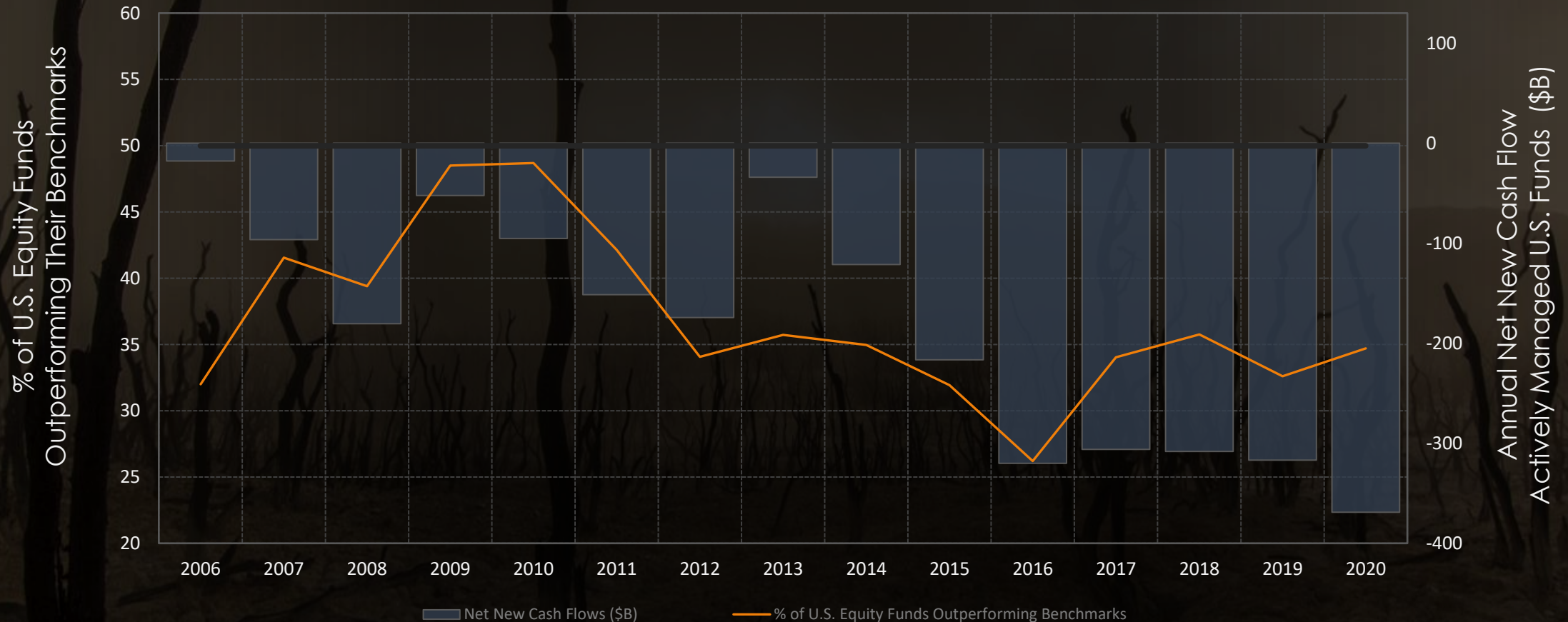
## *Warren Buffett's Secret Factor*

**MAY 2022**

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# ACTIVE ASSET MANAGEMENT IS IN CRISIS

## 15 YEARS of UNDERPERFORMANCE & OUTFLOWS



# INVESTORS HAVE SPOKEN

**From 2010-2020, \$3 Trillion moved from  
active to passive equity**

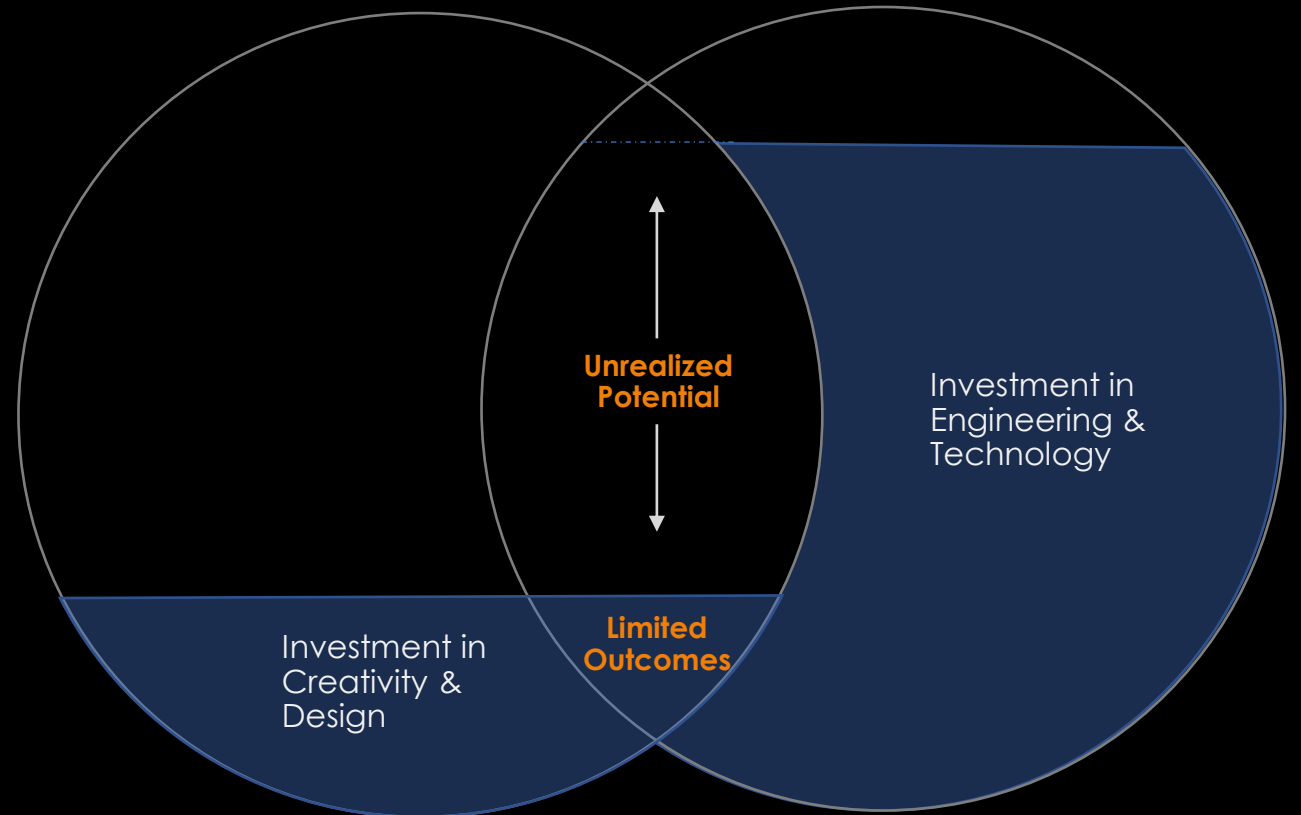
**...the trend is accelerating**

# ROOT CAUSE: Undervalued Creativity

Historically, investment teams have under-appreciated and under-invested in creativity

“Imagination is more important than knowledge. For knowledge is limited, whereas imagination embraces the entire world”

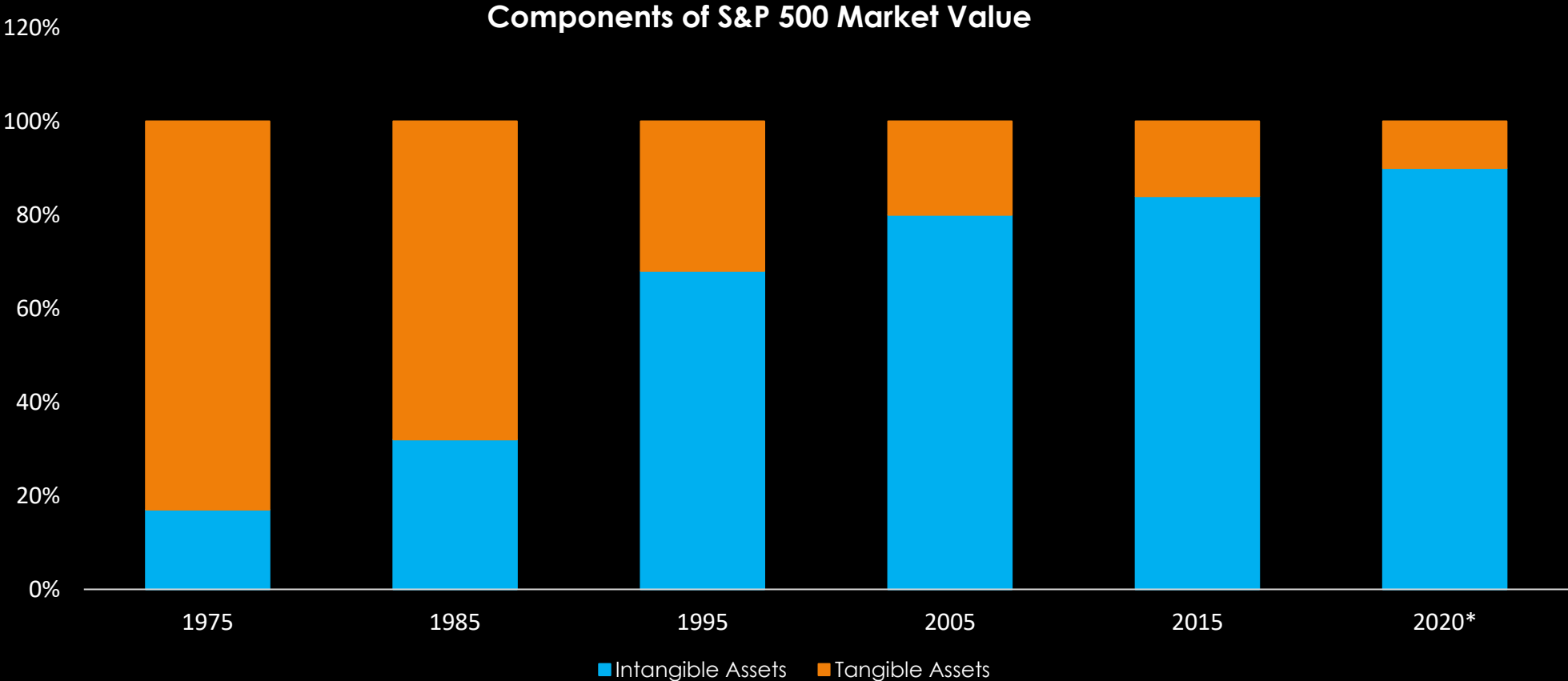
-- Albert Einstein



# OUTPERFORMANCE IS POSSIBLE

**If you know where to look**

# STOCK VALUATIONS HAVE TURNED UPSIDE DOWN: **Less Tangible = More Valuable**





# WHAT ARE INTANGIBLES? **Examples**

Management Team Quality

Brand & Reputation

Innovation & IP

Human Capital & Employee  
Engagement

Customer Satisfaction

Social & Environmental  
Responsibility

- Multiple intangible assets exist, but not all drive significant and consistent performance
- We isolate the most important themes and data sets that create alpha
- Intangible assets enhance implementation of ESG themes

# INTANGIBLES IN ACTION

Lbrands

HubSpot



# HUMAN CAPITAL AND EMPLOYEE ENGAGEMENT: Salesforce dominated CRM market. HubSpot found a way to break in

## Salesforce (2020)

Salesforce is a global leader in customer relationship management technology that brings companies and customers together.

Founded in 1999, Salesforce enables companies of every size and industry to connect with their customers in new ways...

## HubSpot (2020)

We **help** scaling companies deliver a **delightful customer experience** through our cloud-based customer relationship management platform.

Our platform...enables companies to **attract, engage, and delight customers** ...

# SAME GOAL FOR EMPLOYEES AND CUSTOMERS: *Attract, engage, delight*

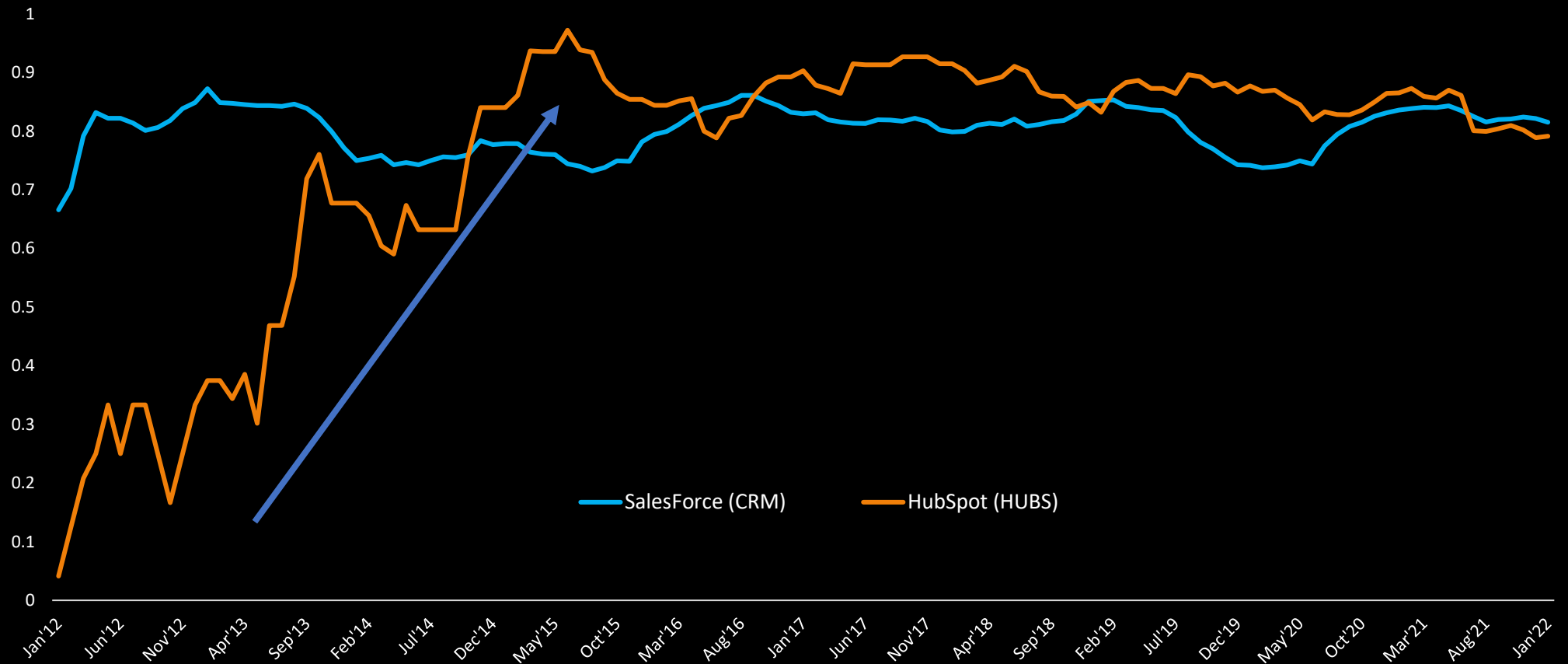


# HubSpot

“We learned long ago that in order for us to achieve our ambitions we needed to build **two products: one for our customers, and the other for our people**. This second product is what we think of as our culture. And, just like any other product development effort, building a great culture is all about getting candid feedback and iterating.”  
---- HubSpot’s co-founder and CTO Dharmesh Shah.

Source: HubSpot

# EMPLOYEE RATINGS VINDICATE THE VISION AND THE STRATEGY: CEO Quality Rating



# THE VALUE OF ENGAGED EMPLOYEES IS...

## ... 1,507% return in less than 7 years!

SALES GROWTH				
From	To	HUBS	CRM	HUBS vs. CRM
2014	2021	1,288%	453%	835%

HUBS - HubSpot  
CRM - Salesforce

TOTAL RETURN				
From	To	HUBS	CRM	HUBS vs. CRM
2014	2021	1,821%	315%	1,507%

Source: Global Financial Data, Two Centuries Investments  
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# INNOVATION AND IP: Upon Steve Jobs' return in 1997, Apple introduces the “creative customer”

## APPLE (1996)

The Company designs, manufactures and markets microprocessor-based personal computers and related personal computing and communicating solutions for sale primarily to **education, home, business and government customers.**

## APPLE (1997)

The Company designs, manufactures and markets microprocessor-based personal computers and related personal computing and communicating solutions for sale primarily to **education, creative, home, business and government customers.**

Source: SEC Edgar, Apple Annual Report, Section 1.

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# INNOVATION AND IP: Steve Jobs leaves in 2011, and so does the phrase “creative customer”

## APPLE (2010)

The Company sells to consumer, small and mid-sized business, education, enterprise, government and **creative markets**.

## APPLE (2011)

The Company sells to consumers, small and mid-sized businesses, education, enterprise and government customers.

Source: SEC Edgar, Apple's 10-K

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# THE VALUE OF APPLIED CREATIVITY IS...

## ... 8,833% return in 13 years!

TOTAL RETURN				
From	To	AAPL	MSFT	AAPL vs. MSFT
1997	2010	8,954%	121%	8,833%

Source: Global Financial Data

*“Innovation distinguishes between a leader and a follower.”*

*- Steve Jobs*

# BUFFETT GETS IT...

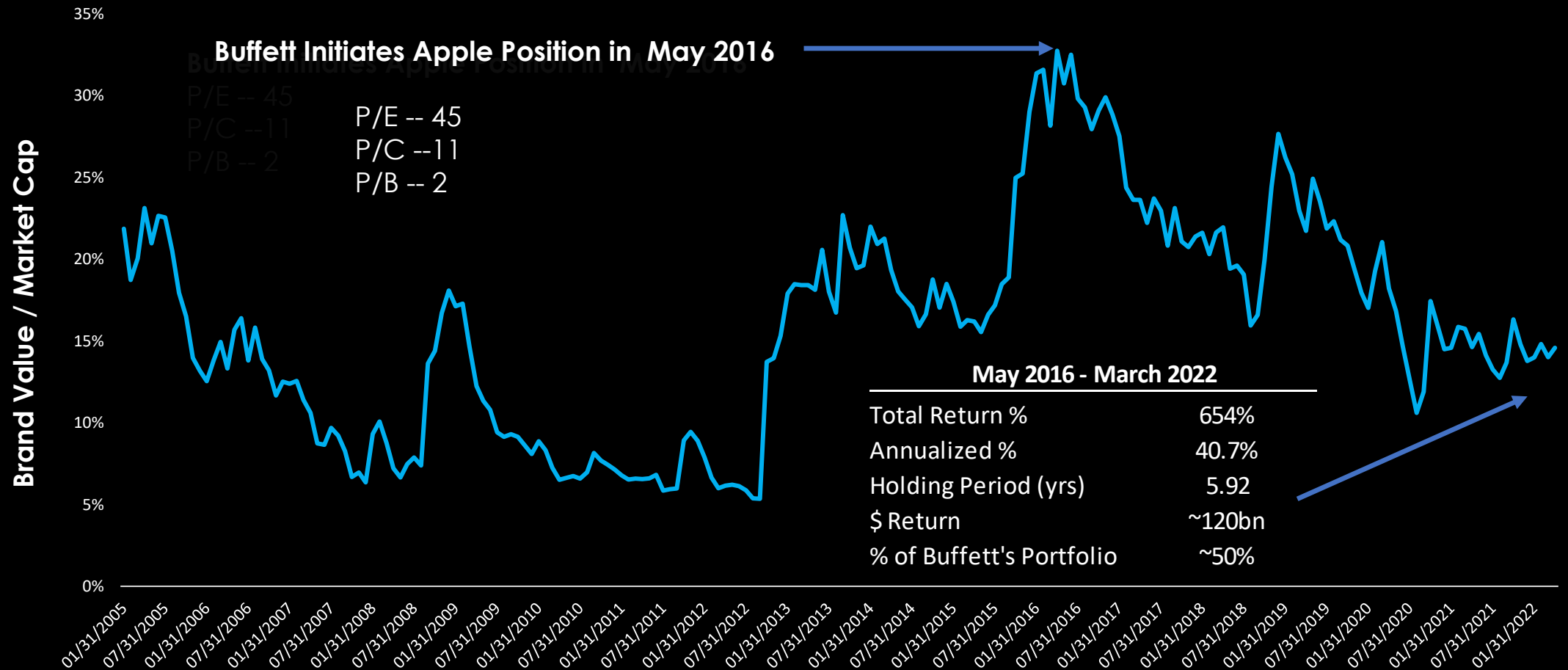
“Business experience ... produced my present strong preference for businesses that possess large amounts of enduring Goodwill and that utilize a minimum of tangible assets.

It was not ... fixed assets that produced the premium rates of return. Rather it was a combination of intangible assets, particularly a pervasive favorable reputation with consumers based upon countless pleasant experiences they have had with both product and personnel.”

**- Warren Buffett, Chairman and CEO of Berkshire Hathaway**

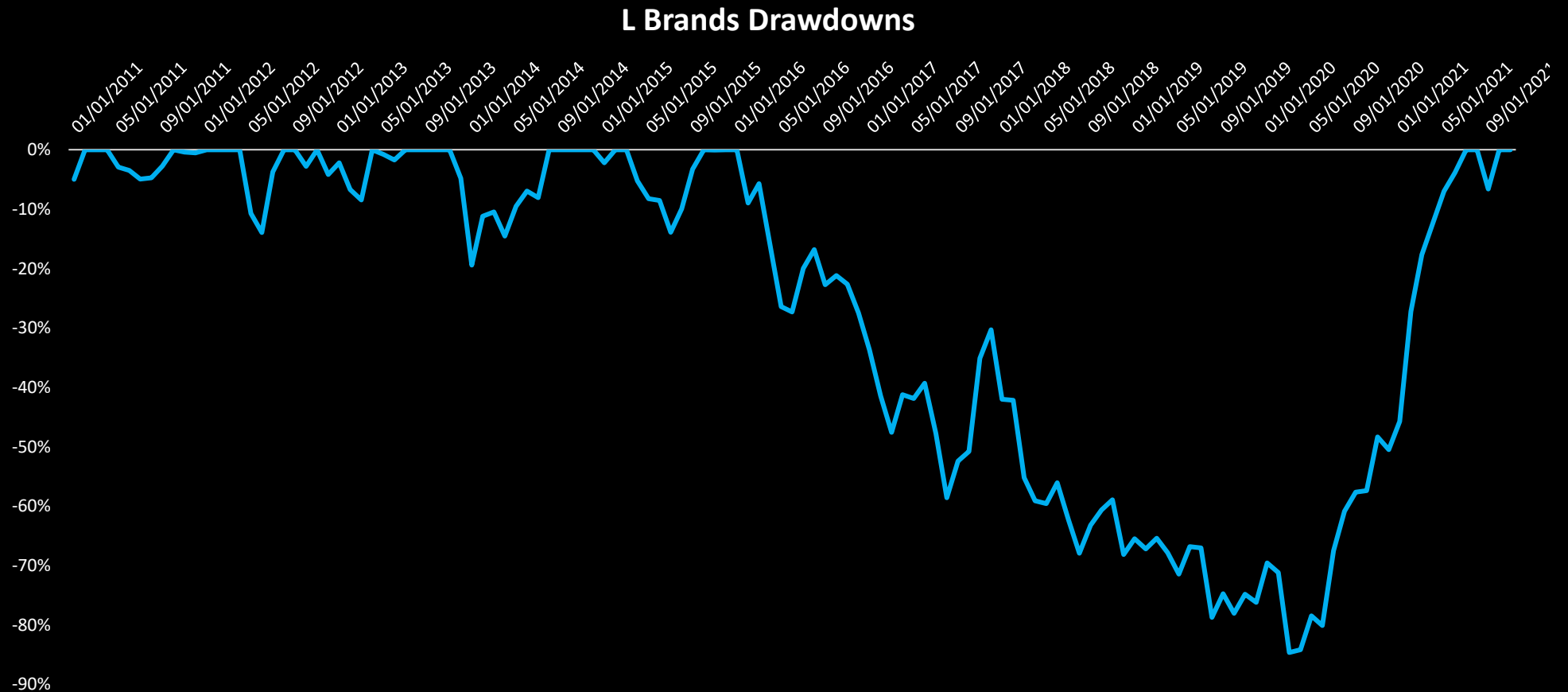
# ONE OF BUFFETT'S BEST PICKS: AAPL

Apple's Brand to Market Cap ("Brand Yield")



Source: Interbrand, Global Financial Data, [CNBCTV](#), [CNBC](#)

# CUSTOMER SATISFACTION: L Brands recovery from CEO change, asset sales, and pandemic



# CUSTOMER SATISFACTION: Change in Ratings

L Brands																														
	Base-line	95	96	97	98	99	00	01	02	03	04	05	06	07	08	09	10	11	12	13	14	15	16	17	18	19	20	21	Previous Year % Change	
L Brands								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	83	81	81	85	82	82	81		-1.2	
Hobby Lobby								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	80		N/A	
Nike								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	80		N/A	
Sephora								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	79	80	80		0.0	
Ulta Beauty								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	80	80	79		-1.3	
Bass Pro Shops								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	82	80	80	79		-1.3	
All Others								72	73	73	75	73	75	76	78	77	76	76	77	79	79	78	80	80	79	79	79		0.0	
Pet Retail Brands								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	79		N/A	
TJX (HomeGoods)								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	79		N/A	
Famous Footwear								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	78		N/A	
PVH								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	78		N/A	
Bed Bath & Beyond								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	81	75	79	80	79	80	78		-2.5
Foot Locker								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	78	78	79	77		-2.5	
Abercrombie & Fitch								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	65	76	79	78	79	77		-2.5	
Menards								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	78	78	79	80	80	77		-3.8	
PetSmart								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	80	77	78	79	79	78	77		-1.3
O'Reilly Auto Parts								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	81	80	78	77		-1.3	
Discount Tire								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	77		N/A	
Gap								NM	NM	NM	NM	NM	NM	75	75	75	74	77	76	77	75	75	79	77	78	79	77		-2.5	
Apple								NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	NM	77		N/A	
Specialty Retail Stores								73	74	74	75	74	75	75	76	77	78	79	78	80	79	77	80	79	78	78	77		-1.3	

Source: <https://www.theacsi.org/industries/retail/specialty-retailers/>,

Scores reflect the American Customer Satisfaction Index that uses customer interviews as input to a multi-equation econometric model developed at the University of Michigan's Ross School of Business.

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**WHY ISN'T EVERYBODY  
DOING THIS?**

# ACCOUNTING STANDARDS Are Behind the Curve

Expenditure for an intangible item is recognized as an expense, unless the item meets the definition of an intangible asset, and:

- it is probable that there will be future economic benefits from the asset; and
- the **cost** of the asset can be **reliably** measured..”

- IAS 38, IFRS.ORG

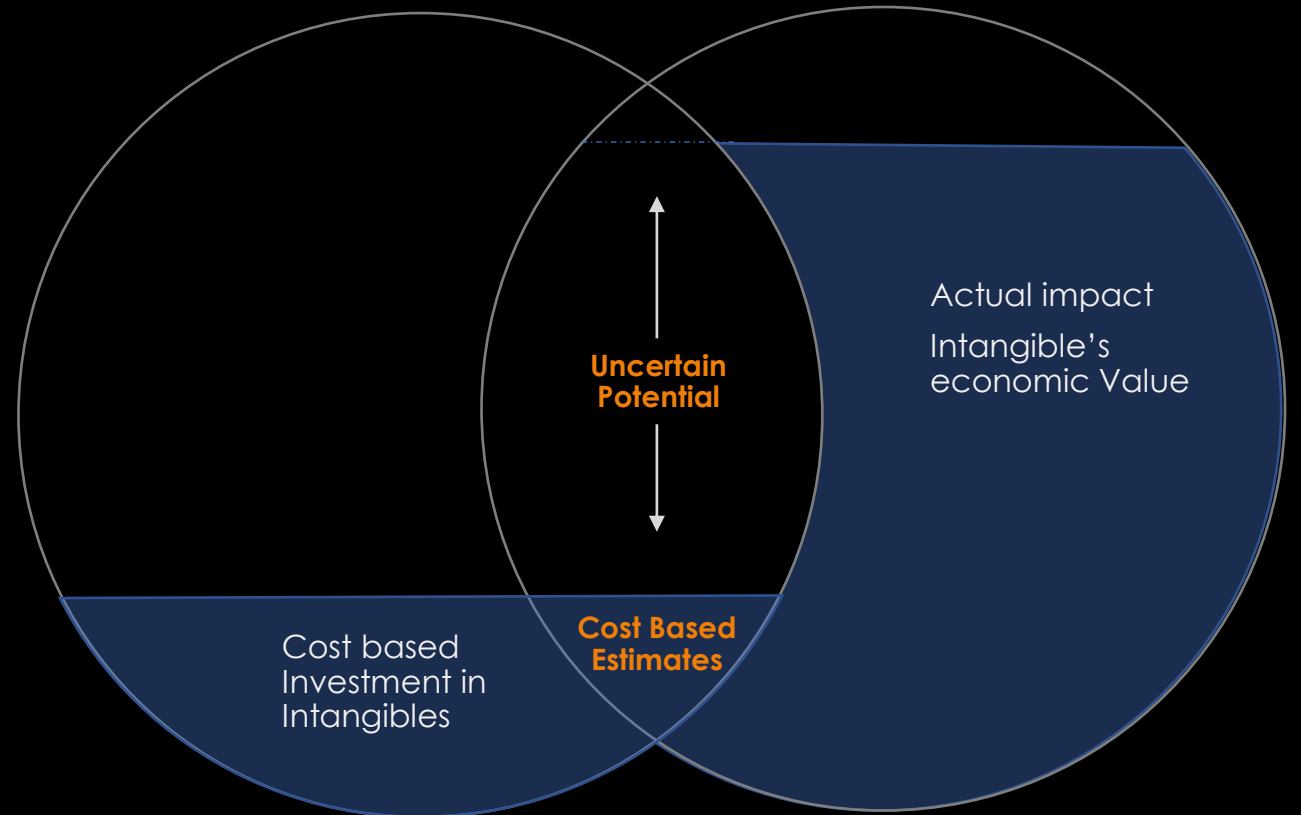


# HOW TO MEASURE

## Cost vs Value

Tangible assets values have a tighter relationship with costs,

Intangibles, however, exhibit a weaker relationship between market value and costs



Online seminar by Professor. Anup Srivastava "Value of Internally Generated Intangible Capital"  
[https://www.youtube.com/watch?v=Bso3\\_SUDjiA](https://www.youtube.com/watch?v=Bso3_SUDjiA)

# CONCLUSION: IT'S ACTUALLY A **GREAT TIME** to be an active investor

## **Access to New Data**

Exciting opportunities to quantify and implement unique ideas

## **Cloud-Based Technologies**

Streamline limitless computational resources to focus on real differentiators

## **Open-Source & 3<sup>rd</sup> Party Frameworks**

Stand on the shoulders of technical giants while adding your own perspective

## **Slow-to-Change Industry**

Opportunities for creative disruption

## **Increasing Management Capability**

Tangible benefits from investing in human capital and creative thinking

**FIND OUT MORE:**

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