Quarterly Update

For the quarter ending June 2025, the portfolio returned 2.28%, compared to the benchmark, S&P 500 (VFV), which returned 4.85%:

Date	Portfolio[1]	VFV[2]	Relative
Q3 2024	5.22%	4.56%	0.66%
Q4 2024	7.95%	8.81%	(0.86%)
Q1 2025	0.98%	(4.24)%	5.22%
Q2 2025	2.28%	4.85%	(2.57%)

The portfolio holdings as of the market close on June 30, 2025, are as follows:

#	Symbol	Cost/Share[3]	Market Price	Return	% of Portfolio
1	BRK.B	$436.68	$485.16	11.10%	22.55%
2	AMZN	$193.52	$219.36	13.35%	16.75%
3	GOOGL	$149.07	$176.19	18.19%	14.62%
4	VFV	$134.86	$149.64	10.96%	13.14%
5	CSU	$3646.75	$4993.20	36.92%	12.18%
6	GE	$243.96	$257.22	5.43%	6.83%
7	TVK	$160.02	$168.41	5.24%	3.70%
8	APO	$133.29	$141.86	6.43%	3.77%
9	Cash	$-	$-	-%	6.46%
					100%

[1] Portfolio returns are money-weighted and net of fees, including exchange and trading costs. It also accounts for currency fluctuations.
[2] VFV returns are sourced from the official Vanguard website: https://www.vanguard.ca/en/product/etf/equity/9563/vanguard-sp-500-index-etf.
[3] Per-share costs are calculated on a net basis.

Review

The portfolio underperformed the VFV by 2.57% in the second quarter of 2025. There were four major trades during this period:

1. Exited Constellation Energy after a sharp rally triggered by the May 23rd announcement. While the long-term thesis remains intact, the valuation appeared stretched relative to the intrinsic economics typical of a utility company.
2. Exited Alibaba after further evaluating the intense competition within China's internet retail sector, as well as having a clearer perspective on the political risks inherent in China. These factors have significantly narrowed the margin of safety, making the investment less attractive.
3. Exited Apple after a sustained period of compounded growth that has resulted in a valuation considered to be on the richer side. While the company continues to produce some of the highest-quality consumer electronic products, it is increasingly difficult to justify the current valuation relative to other opportunities in the market. Additionally, the portfolio maintains indirect exposure to Apple through its holdings in Berkshire Hathaway.
4. Entered a meaningful position in the S&P 500 following a recent politically-driven decline.

As a result of the above four, and other minor trades, the portfolio's cash position has decreased from ~30% to ~6.5%.

Reasons of underperformance during this quarter can be explained in two:

1. Depreciation in all insurance related businesses, including Berkshire Hathaway.
2. Large allocations of cash (~30%) that protected the portfolio earlier in the year, were not deployed rapidly enough to catch the upward trend of the general market.

Neither of these fundamentally changed the portfolio's investment strategy.

Two Pillars

Berkshire Hathaway has outlined four key goals for both good and challenging years. My slightly adapted version focuses on two:

1. Maintaining a substantial amount of excess liquidity at all times to meet all near-term personal obligations.
2. Widening the collective "moats" of the holdings, making them as close to time-invariant as possible.

With these two pillars, the portfolio can perhaps be operated in the simplest way possible.

GE Aerospace

GE Aerospace presents a compelling investment opportunity due to its strong competitive advantages and recent corporate restructuring:

- GE Aerospace holds a dominant market share (around 75%) in both wide-body and narrow-body commercial jet engines, operating in a duopolistic environment with high capital requirements for new entrants.
- Decades of consistent investment in R&D have resulted in fuel-efficient engines and a self-reinforcing cycle where higher margins enable greater reinvestment.
- Airlines face prohibitive financial and operational costs to switch engine providers once an aircraft is configured.
- The 20+ year lifespan of jet engines and the need for sustained R&D investment create a hurdle for new competitors to gain market share.
- GE Aerospace's long-standing, impeccable safety record is a crucial factor for airlines, creating an incredibly high switching cost.
- Growing average age of the global commercial fleet from ~12 to ~15 years, for which "locks-in" the customers for longer periods of time.
- GE Aerospace was previously an undervalued asset within the "damaged goods" conglomerate of General Electric. The spin-off of GE Aerospace allowed it to focus on its core business and capitalize on its strong market position.

On Warren Buffett

On March 3rd, Warren Buffett announced his retirement, marking the end of a remarkable 60-year career. Greg Abel has been named his successor as CEO of Berkshire Hathaway. This prompted me to revisit my notes on Mr. Buffett and share a few lesser-known insights and stories that may not be as familiar to casual followers of investment matters:

- Buffett's early investment strategy closely resembled what we now refer to as activist investing. He focused on purchasing large positions in companies trading below their net asset value—so-called "net-nets"—but limited his selections to businesses he could potentially acquire outright with his existing capital. If the market eventually recognized the value, he would sell for a profit. If not, he would often acquire a controlling stake and liquidate the company, effectively locking in the profit whether or not stock appreciated.
    - Buffett categorized these investments into two buckets: "Generals", which involved passive positions in undervalued companies, and "Controls", where he pursued majority ownership to unlock value directly.
    - In addition to these, Buffett engaged in arbitrage, leveraged investments, and short selling—grouping these activities under the label of "Workouts".

- Prior to acquiring Berkshire Hathaway, Buffett favored textile companies, many of which at the time traded below their book value. He had already broken apart several such businesses for profit after gaining a controlling stake.
    - Initially, Berkshire appeared to be another candidate for 'Control'.
    - However, Berkshire was a little different: the company was actively buying back its own shares, an uncommon practice at the time. Buffett recognized an opportunity to potentially sell his shares during these buybacks. He initially entered at $7 per share, eventually becoming the second-largest shareholder. When Berkshire's board sought his exit and requested an offer, Buffett proposed $11.50 per share - which the board had accepted. However, two weeks later, Berkshire announced a buyback at $11.375 per share. Feeling slighted, Buffett then persuaded the third-largest shareholder to take over the company together.

- Prior to Berkshire's acquisition of Blue Chip Stamps, Charlie Munger held a 5% stake. Buffett recognized the company's significant free cash flow and was inspired to use it as investment capital, a concept now known as "float." Buffett then invested in Blue Chip through both the Partnership and a separate entity he co-founded with Munger, Diversified Retailing Company.
    - Despite the significant float generated by Blue Chip Stamps, the company itself lacked growth prospects. Recognizing this, Buffett looked for businesses that generated float and grew at the same time. This led him to insurance.
    - Buffett then identified National Indemnity as a company he wished to acquire. The owner was generally not inclined to sell, but was amenable at certain times of the year. Knowing this, Buffett had an associate monitor the CEO and inform him when the owner's disposition changed. Using these periods, Buffett was able to sign a deal.
    - One of the biggest mistakes (or can be seen as risk control) of Buffett comes from how he bought National Indemnity. Instead of buying it from Buffett Partnership outright, he used a bank loan from Berkshire to buy the company. It was likely because insurance operations involved a lot of debt and Buffett was uncomfortable taking it to Buffett Partnership's balance sheet.
    - Buffett Partnership had a 30% stake in Berkshire. So National Indemnity became less of an acquisition than buying outright. National Indemnity was then used to acquire many of the companies that led to the current Berkshire Hathaway.

- See's Candy and Blue Chip Stamp are both from LA California. Charlie Munger sourced these deals which have built the bedrock of Berkshire.

- The Buffett Partnership had a stake in Omaha Sun and it offered more than just financial returns—it gave Buffett insight into the inner workings of the newspaper industry. What stood out to him was the peculiar economics of the business: newspapers leaned heavily on advertising dollars, and to attract those

advertisers, they had to produce content. But content creation isn’t cheap; it demands capex, which ironically depends on the very ad revenue it seeks to generate. In smaller towns, Buffett noticed, this cycle made it incredibly hard for more than one newspaper to thrive. Any runner-up publication would be hard-pressed to fund quality content, making it tough to compete for ads. The result? The dominant local paper would typically scoop up most of the profits. Only in larger cities, he concluded, could the market sustain two or more competing companies without squeezing them into financial distress.
    - This analysis led to the acquisition of The Buffalo News and The Washington Post.

- The ownership structure between Blue Chip Stamps, Berkshire Hathaway, and Diversified Retailing Company was complicated. This complexity led to ongoing investigations by the SEC, which ultimately found no evidence of wrongdoing. Frustrated by the scrutiny, Buffett and Munger elected to merge the three entities into a single organization, retaining the Berkshire Hathaway name, with Warren Buffett appointed as Chairman and Charlie Munger as Vice Chairman.

- At one of Berkshire Hathaway’s more recent Annual Meetings, Munger remarked that Buffett became a better investor after turning 60. This becomes evident when we examine how Berkshire’s investment strategy evolved during that period.

- Early on, Berkshire focused on acquiring low-cost producers of strong consumer products—companies like See’s Candies, Gillette, Coca-Cola, and American Express. However, over time, their approach shifted toward investing in capital-intensive businesses, where large upfront investments themselves serve as a competitive moat. For example, firms in the energy and railroad sectors—such as Burlington Northern and MidAmerican Energy—benefit from both deep capital reserves and exceptionally high barriers to entry.

- One key advantage of owning capital-heavy or "essential to society" businesses is their durability. These enterprises often have longer lifespans and greater resilience compared to product-oriented, low-cost competitors. Today, Berkshire owns companies across insurance, energy, oil, transportation, manufacturing, and other sectors characterized by significant entry barriers. This diversified, moat-rich portfolio positions Berkshire as a holding company built to endure for generations.

- The most important lesson from See’s Candy was the understanding of consumer behavior. This is why Buffett mentions See’s Candy, Coca-Cola and Apple as a group. And it is also why he bought into Kraft-Heinz although he admittedly said he has paid too much for it.
    - During the 2024 annual meeting, Warren Buffett extensively discussed consumer behavior. He candidly admitted his investment in Paramount was a mistake, then shared insights into his unique "gut" feeling about consumer habits. Buffett explained that his deep understanding of how consumers behave allows him to instinctively sense when a product has a rare, unmatched "stickiness." He also detailed his thoughts on how people spend their leisure time and the crucial variables at play that helps him decide if a product is worth his capital.

Market Inefficiency
In my 2024 annual write-up, I outlined my perspective on risk. However, as the S&P 500 inches towards richer valuations—with the largest market-cap company boasting a price-to-earnings (P/E) ratio exceeding 40, and even stalwart companies like Walmart and Costco trading at P/E ratios of 40 and 50 respectively—it becomes imperative for a rational investor to revisit the concepts of market inefficiency and risk premium.

Market inefficiency occurs when asset prices don't fully reflect all available information, creating opportunities for abnormal profits. This can stem from factors like information asymmetry, investor behavioral biases, or simply a lack of participants willing to capitalize on these discrepancies. Essentially, an inefficiency signals a "free lunch" or a mispricing that exists because it hasn't been widely noticed or acted upon.

In contrast, a risk premium is the additional return an investor expects or demands for undertaking a specific level of risk above a risk-free investment. It's not about exploiting mispricing, but rather about being compensated for assuming a calculated risk that others may be unwilling or unable to bear. This premium reflects the inherent uncertainty of an investment, incentivizing investors to venture beyond safe assets.

Consider the analogy of a specialized construction project to differentiate these concepts:

- *Inefficiency*: Imagine a complex engineering blueprint for a new bridge, promising substantial long-term economic benefits for a city. The plans are publicly available, but their intricate nature requires highly specialized knowledge to interpret. Few construction companies initially grasp the immense profitability embedded within this design. A savvy engineering firm, possessing this rare expertise, reviews the blueprints. They identify a more efficient and cost-effective method to build a critical component that no one else has noticed. Their bid, based on this overlooked efficiency, secures a significant profit margin. This profit stems not from taking on extra risk, but from possessing unique insight that the broader market of bidders lacked. It's akin to finding a "hidden gem" due to an information gap or a specialized knowledge barrier preventing wider recognition.

- *Risk Premium*: Now, picture building a similar bridge in an extremely remote, mountainous region prone to severe, unpredictable weather. The construction firm undertaking this project knows it will be exceptionally challenging and dangerous. There's a high probability of delays from storms, difficulties in transporting materials, and significant safety hazards for workers. Because of these inherent and unavoidable risks, the firm demands a significantly higher payment—a risk premium—compared to constructing a bridge in a safe, accessible urban area. This additional compensation is explicitly for enduring the heightened uncertainty and potential for adverse outcomes associated with the project's demanding environment. Other firms might recognize the potential profit, but their aversion to the high physical and logistical risks means they won't bid unless this premium is substantial.

In essence, an inefficiency represents a fleeting opportunity to profit from a market's temporary oversight or incomplete information. A risk premium, however, is continuous compensation for bearing inherent, persistent uncertainty. The former tends to disappear as information spreads and market participants react; the latter endures as long as the underlying risk remains.

Returning to the current market, the high valuations we're observing in the S&P 500, particularly in high-growth and even some stable companies, compel us to reconsider the interplay between these concepts. While some might argue that elevated prices reflect a market that has efficiently priced in future growth, it's also possible that certain areas are experiencing behavioral biases or an overestimation of growth prospects, leading to temporary inefficiencies.

More significantly, current valuations imply a considerable degree of risk tolerance among investors. When P/E ratios climb to such levels, it suggests that investors are demanding a lower earnings yield for the risk they're taking, or perhaps that they anticipate exceptionally high future growth to justify today's prices. This is where the concept of risk premium becomes central: are investors being adequately compensated for the risks associated with these elevated valuations?

It is highly probable that the risk tolerance of the general investing public has not genuinely shifted. Human psychology often behaves differently in a herd dynamic compared to individual decision-making. We appear to be in a "herd stage," where the collective sense of danger diminishes, and high confidence further draws individuals into the crowd, creating a self-reinforcing cycle that further lowers the perception of risk. However, as the herd gradually approaches a tipping point—where individuals begin to feel less part of a unified group and more like a collection of separate entities, eventually reverting to individual behavior—this herd-initiated momentum will slow and ultimately dissipate. In the market, this transition will likely translate into an eventual re-valuation, echoing two of my favorite quotes on this topic:

- J.P. Morgan: "In the bear market, companies get the investors they deserve."
- Warren Buffett: “Naturally, investors will be feeling disappointed - but only because they started out expecting too much.”