Conscious Investor® Fund
Interim Letter to Members: December 2017

The Day Warren Buffett Started Working for the Fund

I remember it clearly. It was 14 March 2016. I got up at 2.00am and logged into Interactive Brokers. The moment had arrived. The Fund had received a number of new investors and the money was there. It was time to buy our first Class A share in Berkshire Hathaway. We paid US$210,090, around $280,000 in Australian dollars, an extraordinary amount of money. But I had done my calculations on the shares and was just waiting for the right time in terms of price and having the available funds

We had bought some parcels of Class B shares in Berkshire Hathaway the year before. But it wasn't until the purchase of the A share that I thought that Warren Buffett had truly started working for the Conscious Investor Fund. After all, originally it wasn't called a Class A share, it was just a share in Berkshire Hathaway. The same shares that Buffett first bought for US$$7.50 back in 1962. So the Class A shares have impeccable lineage.[1]

Most importantly, when we buy shares in Berkshire Hathaway on your behalf, we don't just get the services of Warren Buffett. We also get the services of all the owners, managers and employees of Berkshire Hathaway, at last count around 316,000. By the way, only 25 are at the headquarters of the company. How's that for keeping costs down.

By the way, Class A shares recently crossed US$315,000, representing a growth of 49.9 percent in 22 months, or 24.7 percent on an annualised basis.

One last bit of news regarding Berkshire Hathaway. On January 9, 2018 two new directors were added to the board, Gregory Abel and Ajit Jain. Mr. Abel will be Berkshire Hathaway's Vice Chairman – Non-Insurance Business Operations and Mr. Jain will be its Vice Chairman – Insurance Operations. Mr. Abel joined Berkshire Hathaway Energy Company in 1992 and currently serves as its Chairman and CEO. Mr. Jain joined the Berkshire Hathaway Insurance Group in 1986 and currently serves as Executive Vice President of National Indemnity Company with overall responsibility for leading Berkshire's reinsurance operations.

In an interview on CNBC, Buffett called Abel's and Jain's new roles "part of the movement toward succession" at Berkshire. "They are the two key figures at Berkshire" and "have Berkshire in their blood," he added.

Buffett has also said that roughly half of every board meeting is spent discussing succession of the company. So I think we can be confident that, even after Warren and Charlie Munger depart, it will continue to be very profitable for many years to come.

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[1] Initially there were just Berkshire Hathaway shares. In 1996, Buffett changed the name to Class A shares and introduced the ability to convert a single Class A share to 30 Class B shares. A 50-to-1 stock split in 2010 increased the ratio to one-1,500th. Within a small range, B shares trade at one-1,500th of an A share.

Periodic Despondency and Euphoria in the Market

As you know, the Fund puts its primary focus on finding companies that have had solid growth in earnings with all the hallmarks that this growth will continue in the future.

The secondary focus is using Conscious Investor® to calculate sensible prices to buy shares in these growing companies.

Over time, the continuing growth in earnings will drive the growth in the share prices, and the sensible purchase prices will help ensure that we get maximum benefit from this growth.

But sometimes this gets out of step in both directions. Sometimes the market gets euphoric over a particular company and the share price grows faster than would be justified by the growth in earnings.

Other times the market gets despondent and offers shares at a price way below what the growth in earnings would justify.

As stewards of your investments in the Conscious investor fund, we make two promises during times of market euphoria and market pessimism:

1) We will keep doing what we always do, investing in great businesses at bargain prices. In fact, it doesn't matter whether the market is pessimistic, euphoric or anything in between. We always have a list of companies we will add to our portfolio should the price become suitable, our "bottom-drawer stocks". Similarly, for the companies already in the Fund, we know what prices we would pay to top up the holdings.
2) We will keep you informed through our regular reports (bimonthly eps reports, end-or-year letters, interim letters and company summaries) about what we are doing and why, particularly when there are any major changes in market despondency or euphoria.

Of course, no one can predict if the market is going to become euphoric or despondent at any particular time. The same applies for individual companies.

What we do know is that when we buy a particular company that the market is despondent about, provided that the earnings continue to grow, we will get an even greater profit.

Occasionally the market gets so euphoric about a particular company, we will thank Mr Market for his kindness, and choose to exit the company—provided there is clearly a better opportunity for the money elsewhere.

In the end, the value of a company is dependent on its earnings growth, not on what the market happens to offer for it that day. Often the price gets out of step with the earnings growth, too high or too low, and these provide opportunities to deploy our funds in a way that is most beneficial for our members, either buying or selling.

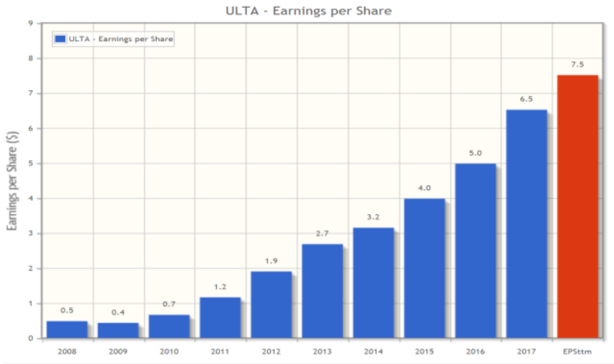
In fact, we welcome unjustifiable big drops in share prices in companies with growing earnings because this enables us to add to our holdings at bargain prices.

Earnings During 2017

During 2017 the weighted average of the growth of earnings per share for the companies in the Fund grew by 14.6%. Over time, provided this growth is maintained, this should translate into healthy growth of dividends and share price.

Two standouts were Ulta Beauty and Domino's Pizza. Their EPS grew by 30.9% and 29.1% during 2017. The adjacent chart shows the growth of EPS for Ulta Beauty for the past ten years.

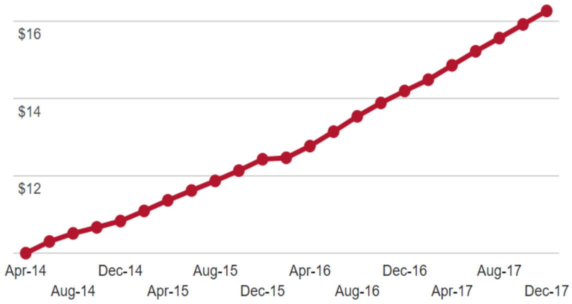
Similarly, the weighted average Return on Equity for companies in the Fund was a robust 25.1%.



In other words, at the end of December 2017, managers of the companies in the portfolio had earned an average of 25.1% on the equity in their companies. Again, overtime, if this ROE is maintained, it will translate into strong growth of share prices.

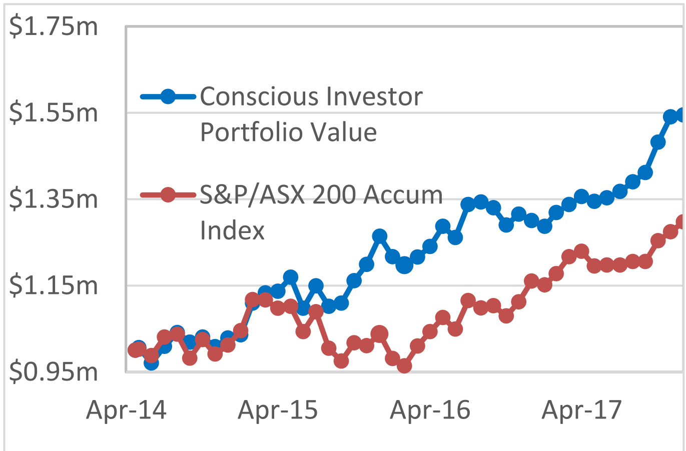
The adjacent chart shows the month-by-month growth of the average earnings per share for companies in the Conscious Investor Fund from April 2014 to December 2017.

This continuing growth of average earnings per share over 2017 translated to a growth of 18.8% in the Fund after expenses as we will see in the next section.



Fund Performance

The adjacent chart shows the dollar performance of the Fund after success fees from April 2014 to November 2017 compared to the S&P/ASX 200 accumulation index. Over this period, an actual investment of $1 million dollars would have grown to $1,545,168 compared to $1,297,388 for the Accumulation Index. In percentages, the average annual growth of the Fund was 12.82% compared to 7.48% for the Accumulation Index.



Conscious Investor® and the Teaminvest Methodology

The investment process used by the Capital Allocation Team for the Fund consists of four steps: Filtering using Conscious Investor®; Applying the Teaminvest investment methodology; Calculating the price to pay and when to sell; and a Final Checklist. Full details of these steps are contained in the Information Memorandum. Here we just give a brief summary of the first two steps.

Conscious Investor® filters and analyses all companies listed on the ASX in three steps: Filter, Research and Return. The main components of the filter stage zero in on companies with attributes such as strong and stable growth in earnings and sales, high and consistent return on equity and not too much debt. The research stage helps to limit the results to companies for which these attributes are likely to continue. Finally, the return stage calculates what maximum price to pay to be confident about getting the required rate of return over the long term. It uses automatic margin-of-safety calculations based on stress testing the investment assumptions.

The Teaminvest Methodology focuses on the following four areas. Wherever possible the Capital Allocation Team scores the areas to increase the precision of the decision process.

- How does the company make money? What is the business of the company? Who are its customers? Are we confident that there will be need for their products and services in five to ten years?
- Investments should be like castles with deep moats: What are unique features of the business that separate it from its competitors? These “economic moats” are scored in terms of depth and durability.
- Risks need to be identified: All businesses face risks that could weaken the continuing success of their operations. These risks are identified and are scored according to the likelihood of their occurring over the next economic cycle and their potential damage if they do.
- Is management honest, open and rational? As part of examining the business, an evaluation is made as to whether we believe that the board and senior management are acting honestly, rationally and in the best interests of shareholders. Specific areas that are looked at include the number and type of related party transactions and the remuneration structure for the CEO and senior management. The Capital Allocation Team scores remuneration in terms of clarity, alignment and quantum.

On behalf of the Capital Allocation Team,

Warm regards,

John Price

The Capital Allocation Team prepared this report for members of the Conscious Investor® Fund. It does not take into account anyone’s personal circumstances. Remember, what happened in the past is not always what will happen in the future.

Questions? Contact us:

Conscious Capital Limited AFSL 427 216 Suite 9, 2 Kochia Lane, Lindfield, NSW 2070, Tel: 02 9416-1941