MOI Global *presents*

The Process of Intelligent Investing

Building a Great Investment Firm

June 2017

Scott Miller: The Genesis and Approach of an Investment Partnership That Invests "Off the Beaten Path"

We recently had the pleasure of interviewing New York-based value investor Scott Miller. Scott is the founder of Greenhaven Road Capital, an investment partnership that looks for investments "off the beaten path". Scott participated in this year's Zurich Project and shared his thoughts on the topic, "how to build a base of aligned LPs while spending less than 5% of time on marketing".

The Manual of Ideas: Please tell us about the genesis of your firm and the principles that have guided you since then.

Scott Miller: Some people like to fish; I like to invest. It doesn't feel like work for me. I spent ten years working in a non-investment job while beating the market by thousands of basis points per year as a private investor. Finally I decided to leave my "real" job at Acelero Learning, a company I had co-founded, to begin work at Litmus Capital, a hedge fund founded by two of my classmates from Stanford Business School. I thought I was a good investor before I got there, but Litmus really opened my eyes to the Joel Greenblatt-style of special situations investing. Keith Fleischmann had worked for Eddie Lampert at ESL and Dan Carroll had worked for Dan Loeb at Third Point. Litmus had assembled a talented team and was running approximately $200 million at the beginning of 2008. Unfortunately, 90% of the assets were from two investors who could redeem with 60 days' notice, and they were forced to take advantage of any liquidity and pull their funds when the financial crisis hit. This experience drove home the importance of a stable LP base, and I gained a real appreciation for the importance of the terms on which money is accepted. I also walked away a more complete investor.

2009 was a great time to be an investor, but a horrible time to find an investing job after Litmus. I went back to the company I had helped found, while exploring roles at other funds. For the stock pitch component of the interview process, I pitched a company called Gevity, which I knew well because my company was a customer. I predicted Gevity would be bought out by General Atlantic at a large premium because of some off-balance sheet assets. I got literally everything right about the situation and had timing on my side – in the two months of interviewing, Gevity doubled and was indeed bought out by General Atlantic. When I didn't get hired, I thought, "It's time to do this yourself". You love the work, you have the skills, and you have enough money saved to open the doors – why wait for somebody else to validate you?" I then laid the foundation for my own fund—Greenhaven Road.

Starting a hedge fund is a very asymmetric opportunity (limited downside / great upside). I was able to put myself in business for less than $20,000. My initial investors were my retirement fund, my wife's retirement fund, my parents, my in-laws, a portfolio manager and an analyst from Litmus, my college roommate, and a few more friends and family. You cannot manage other people's money without a few brave and generous people stepping up first. They were invested in part out of self-interest (who doesn't like the potential for big returns), but also to help me out, for which I am very grateful. We launched with $2 million in January 2011.

While the cost to start a fund can be quite low, the economics on a $2 million fund are probably even worse than you think. To that end, I decided to continue in the operating role with Acelero and work on Greenhaven Road on nights and weekends. Given my concentrated, low turnover style of investing, I was able to strike an appropriate balance. Importantly, having outside income removed the pressure to generate short-term returns and allowed me to be selective with my early limited partners rather than needing to accept capital from anybody on any terms. I was a tortoise on the AUM front. One year, I was up over 60% and did not add a single LP. In 2015, I finally decided to leave the operating world and focus full-time on the fund. To grow meaningfully beyond the core friends and family I was going to have to give up the security of the operating role and remove the barrier. With 10,000 funds in existence, most incoming LPs don't want to pick one with a part-time manager.

I invest Greenhaven Road's money like it is my own because it is my own. The fund began as friends and family and has grown over time to include investors from as far away as Uruguay and South Africa. I view myself as incredibly lucky. Investing was a passion that I pursued on the side, and I was able to turn it into a career.

My only real guiding principle is that I want the fund to retain its nimbleness by remaining relatively small with an investment committee of one. This model worked to great success for Warren Buffett in his partnership, and it worked for Chris Sacca at Lowercase Capital. I am not saying that I can generate returns like they did, I am just saying the model of a boutique can work quite well. You don't need a portfolio manager, three or more analysts, a CFO, and a marketer to compound capital. My goal is to keep the partnership small and simple, and see if we can do something special over time. I don't understand the fascination with size, other than it provides guaranteed wealth from management fees, but after a certain point… come on! I am happy to let others have the biggest because I am trying for the best. I don't think you can have both investing in public equities.

MOI: How did you get to know Chuck Royce?

Miller: Over Fourth of July weekend 2015, I got an alert on my cell phone that somebody had requested more information through Greenhaven's website. Fortunately, this happens pretty frequently, but this one caught my eye: Chuck Royce. Normally I would wait to respond when back in the office, but in this case it made sense to send information now, when the gatekeepers were off duty and he was on his iPad. I excused myself from the family gathering and sent Chuck the fund's information. There was a very short back-and-forth before he said, "I am in, let's meet." It was the quickest "yes" I have ever gotten. Shortly thereafter, we met in his family office in Greenwich, Connecticut, in a great room that just has two couches and a view of the water. We went really deep on my background and eventually on a company that I had written about. It was two stock enthusiasts just "geeking out" on operating details like customer retention and incremental margins. After doing this a few times, Chuck offered that I work out of his family offices where we could run into each other more often. The relationship has grown over time, and his family has become a partner/seed investor and friend. I believe the investment committee of one (me) is the perfect size, but it is certainly wonderful to have Chuck as a sounding board and resource. He is an example that nice guys can finish first. I hear random Chuck Royce stories all the time as I circulate in the investment world, and they are always positive. He is one of the good guys, and I am happy to be in his orbit.

MOI: In choosing your investors and communicating with them, what considerations have you found most important?

Miller: My goal is to have a very broad base of patient and stable capital that will allow me to invest with a multi-year time frame in off-the-beaten-path ideas of all sizes. To facilitate that, Greenhaven has a relatively low minimum investment of $200,000 and both onshore and offshore vehicles (so we can also accept capital from IRAs and non-US citizens). Our fee structures are also much more investor-friendly than the traditional 2/20. These choices are designed to minimize the barriers or "yes—but's" for potential investors. Still, I only want philosophically aligned limited partners, and I only want patient capital. The power of compounding doesn't work if an investor redeems at the first sign of volatility.

Given Greenhaven Road's size and concentrated strategy investing in more esoteric ideas, the people and groups that are going to come into and stay in the fund are a very small subset of the allocator population – independent thinkers looking for a small, unique, entrepreneurial fund. Thus, I have made the decision to not actively seek potential investors because the return on my time would be too low, and my real interests are on the investing side.

The result is that Greenhaven Road is bought, not sold. Outside of the initial friends-and-family capital I raised, every investor—including Chuck Royce and Stride Capital Group—has filled out a form on *greenhavenroad.com* inquiring about further details. My investors were not cold-called; there was no third-party marketer; there was not extensive networking. Each of my limited partners read an investor letter or saw an investment presentation and was moved enough to actively reach out. My investors have self-selected into the fund. They share my long-term orientation, and they share my view that volatility creates opportunity. They understand that having down quarters and years is an inevitable part of the process. In essence, my investors have chosen me, and I think that is the perfect setup.

In terms of communication, I try to be very transparent with my investors—my goal is to make them comfortable. I write long and detailed letters every quarter because I think it is important that they know what we own and why we own it. My investors are not looking to me to help them understand the Federal Reserve or money supply. I focus on the specifics of each company and keep the macro "gobbledy gook" to a minimum. I try to just be me in the letters by sharing each step of my analysis and any external factors impacting the timing of my buy and sell decisions. I don't try to please everybody or actively sell them on the fund. I

want a small group of people to invest alongside my family for decades. I want somebody to read my letters and say, "I know who Scott Miller is and what he thinks." As long as .000001% of the population says, "he is my guy," I will continue to have a great partnership. My goal is to be authentic and let people opt in or out.

The one investor I have chosen is Stride Capital Group as seed investors along with the Royce family. In addition to stable, long-term capital, Stride is a valuable strategic partner with experience building successful asset management firms. Stride appreciated what makes Greenhaven unique, and unlike most seeders who prioritize size and scale, Stride felt the competitive advantages of staying small and simple were a source of producing sustainably high returns over the long term. They felt we could avoid the pitfalls many other firms experience by growing too big to sustain the strategy they built the firm on. The fact that they fully embraced my style and approach were very meaningful for me. Their institutional scale and abilities open up opportunities that would have been hard for me to access on my own. Stride also provides Greenhaven Road with business support, particularly related to investor onboarding, fund administration, and the annual audit. Our relationship is structured to allow Greenhaven Road to continue as a small, independent boutique, and having a partner to handle the non-investment portion of the business allows me to focus on where I add the most value.

MOI: How do you define your investable universe and how do you generate ideas?

Miller: I view Greenhaven Road as a forty-year vehicle. I have the vast majority of my investable assets in the fund, and our fee structure rewards generating returns. So within the context of a highly aligned long-term vehicle, I want as large an investable universe as possible. My documents are incredibly broad; I can basically invest in any public company on the planet earth. However, the reality is it is my money in fund, and I don't know anything about Azerbaijan or Mongolia or any of the fringe markets, so to date we have only invested in the U.S., Canada, and Western Europe. Greenhaven invests across the market cap spectrum with particular emphasis on small- and micro-cap names where my owner-operator experience can inform my analysis of management decisions and incentives, and my contrarian streak can help me figure out what the market is missing. I have a natural preference for overlooked, misunderstood, or esoteric names with limited analyst coverage, high insider ownership, and high growth potential.

The vast majority of our investments are straight equity investments, although in certain situations we have owned TARP warrants and SPAC warrants. For both the TARP warrants and SPAC warrants, they are tied to a company I am intimately familiar with and have 4+ years of duration. They are not quite equity, but the long duration nature of these instruments tilts them toward the equity side of the spectrum and away from the options side, and they can have very attractive return profiles. In most cases, if you like the SPAC you should love the warrants.

In terms of idea generation, my challenge is to weed out ideas, not to generate them. I see thousands of pitches a year, yet my goal is to invest in four to six new companies. I find Value Investors Club to be an incredible place to learn, I read every investor letter that I can get my hands on, and I follow some interesting people on Twitter. I am also a paying member of MOI Global. I have a pretty robust network of friends / talented investors, including Adam Wyden at ADW capital, Eric Gomberg at Dane Capital, Brad Hathaway at Far View, and Matt Sweeney at Laughing Water. These peers invest in similar companies and are another great source of ideas. I also have an incredibly sharp group of limited partners, more than a quarter of whom are current or former portfolio managers. Among all of these sources, the challenge for me is culling, not generating.

MOI: What are your key stock selection criteria, and what types of businesses have you favored historically?

Miller: Product, markets, team, and degree of difficulty (execution risk) are the four elements I think about in every situation. I first learned and executed this Kleiner Perkins framework when I worked for KP's John Doerr and Brook Byers at their venture philanthropy effort, the New Schools Venture Fund, after graduating from business school. I will also layer in stakeholder incentives, which are not always aligned in public companies. I have a strong preference for asset-light businesses with recurring revenue, as these businesses tend to be easier to manage and have high returns on invested capital. Software companies, asset managers, and business service businesses are all in the sweet spot for me. I want to understand the business and "how the sausage is made." Often, I will invest in businesses I know from being a purchaser in my operating days, creating a competitive advantage in understanding the value proposition. I shy away from commodity and biotech companies.

MOI: What sources of competitive advantage have you found to be most durable?

Miller: Fortunately, over the last fifteen plus years I have been able to outperform the market pretty dramatically on both a gross and net basis and not using Bloomberg, consultants, or a team of analysts. I have thought about this a fair amount, wondering how one person, working alone,

could do better than funds with hundreds of people and infinite resources. The fight almost seems unfair. I cannot out-resource or outwork organizations who receive $100+ million per year in management fees and have infinite resources. Ultimately, I think the three primary advantages that I have are size, temperament, and operating experience.

While large capital allocators and gate keepers often like large funds (nobody gets fired for allocating to a $5 billion manager), if you're focused on generating returns, it's ideal to be small. The investable universe is simply larger. Greenhaven Road can go into the cracks of the markets that large funds either ignore or have to skip over since the position size would be too small to move their performance needle. Through the power of compounding and asset flows, this advantage erodes over time as a fund grows. We are not at the point of closing the fund, but we have said that we will do a soft close at $80 million. We will take a long pause from adding additional capital, because I want to preserve size as an advantage for as long as possible.

In addition to size, I think temperament and personality are a real source of durable advantage. Mark Sellers (not the ponzi scheme operator) gave a speech at Harvard Business School where he outlined what he thought it takes to be a great investor. I send a PDF of the speech to people when they ask me how to become a better investor. Let's start with the traits he lists and then I will give you my spin on it.

The first trait he lists is "the ability to buy stocks while others are panicking and sell stocks while others are euphoric." I certainly have the buy-while-others-are-panicking ability; for example, I went fully invested in March 2009. It was lonely. Will I be able to do it again? I don't know, but during the maximum panic of my investing life, I effectively went all in.

Being obsessive…: Some people fish; some people paint; some people do crossword puzzles. I think about my portfolio when I walk the dog or go to the supermarket. I am a quiet guy, in part because my mind is constantly picking over the companies we own and the companies I am researching. The party is in my head.

A *willingness to learn from past mistakes*: In addition to emphasizing transparency with Greenhaven Road's LPs, another reason I write such long letters is so my investment theses are preserved on paper. I go back and compare what I thought would happen to what actually happened.

An inherent sense of risk based on common sense: I call my models "scratch sheets" as they can typically fit on a napkin. My thesis never hinges on the discount rate in a model. I want to make six investments a year or fewer. I am trying to move slowly and just invest in the "no brainers" others often miss.

Confidence in [your] own convictions… even when facing criticism: I am comfortable holding a highly divergent opinion. I may not be the easiest guy in the world to be married to, but I sleep well at night because I don't need others to validate my beliefs.

Have both sides of your brain working: Sellers reminds listeners that it is important to also be a good writer. I may not be Steinbeck, but a small subset of the internet seems to appreciate my quarterly letters.

The ability to live through volatility without changing your investment thought process: Sellers believed this is the most important trait. For me, with an operating background it comes back to the frameworks of product, market, team, and execution risk.

Ultimately, I think I am wired to be an investor. I am not the best analyst in the world—others make better Excel models and PowerPoint decks than I do—but the actual buy-and-sell decisions, and the portfolio construction process come rather naturally to me.

One trait that Mark Sellers did not list is the ability to change your mind when the facts change. This "flip flopping" behavior is derided in politics. In my house, it is celebrated as "flexible thinking." My portfolio is low turnover and I like to hold investments for several years, but there have been times where a sell decision is made very quickly when new facts come to light to challenge my basic thesis.

In terms of operating experience, the template for most fund managers is a two-year analyst program at Goldman Sachs or Morgan Stanley, business school, and then a stint at a Tiger cub. When I graduated from college, I managed a paper bag factory. In Porter's "five forces", a bag factory would be deemed a terrible business with no barriers to entry, low margins, little product differentiation, and cyclical characteristics—but the meaningful operating experience has been valuable for me. Later in my career I helped start a business, Acelero Learning, which has grown to over 1,200 employees. I was Acelero's CFO for years and also ran an effort to develop, sell, and support software used by Acelero, customers, and competitors. I draw on these experiences when evaluating management with my, *"What would Scott Miller do?"* test. The best teams are the ones that come up with solutions even better than those that I would have thought of.

MOI: When it comes to equity analysis, how do you assess the quality and incentives of management? Which CEOs do you admire most?

Miller: As mentioned before, I run management through a, *"What would Scott Miller do?"* screen, where I apply my

operating experience to the company I am analyzing. Often the industries and particular problems are different, but I look at how management communicates and the solutions they choose. I strongly prefer companies with high insider ownership. Owner-operators are far and away my favorite when they have retained a significant stake in a public company, are highly aligned, and know a thing or two about capital allocation. The CEO I admire most is Thomas Peterffy of Interactive Brokers. He came to the U.S. penniless and built a massive fortune and, more importantly, a great company. His is a story of innovation; he was one of the first to use computers for market making. Peterffy was smart enough to see the applications of technology to online brokerage, and brave enough to pursue what could effectively kill the market-making business—and he is a great executor. The business has profitably and steadily grown the account base, growing brokerage accounts by 15%+ per year like clockwork. Peterffy still personally owns over 70% of the company, and all but ten of the company's approximately 1,400 employees own shares. He has built a company with the lowest costs and highest margins, a very long runway for growth, a history of execution, and a highly aligned team. The stock has largely been dead money, but from an operating perspective, Peterffy is a *maestro*.

The other CEO for whom I have great admiration is Sergio Marchionne of Fiat Chrysler. He is another straight shooter who has executed year in and year out. Both Peterffy and Marchionne never *"do what Scott Miller would do"*. Their answers are always far better.

MOI: Would you outline the summary thesis behind one or two of your investments at this time?

Miller: One of our more recent investments has been Limbach. I discussed it in some detail at MOI Global's Best Ideas 2017 conference [slides | video]. The share price has not moved since I presented it and I think the thesis still holds. This is a really boring company, but I mean that in a good way. It is not sexy, but it is essential. The company installs and maintains HVAC systems for large commercial projects. They emphasize hospitals, educational institutions, and entertainment venues. It turns out that air conditioning systems for hospitals are complicated. For example, you do not want air flowing from outside an operating room, into an operating room, so there are different target air pressures in different portions of the hospital. One of Limbach's competitive advantages is a design center in Orlando where 30 employees spec out systems and look for savings and optimizations. They often suggest alternative configurations to initial specs that are more cost effective, thus making their bids more attractive. I actually went to the design center in Orlando, because I was curious how complicated these systems are and how big of an advantage is the design center. I also wanted to go a layer below the CEO and get a sense of the quality of the team and the culture. I walked away thinking, these are "A" players in a really boring business. They actually love air conditioning. But obviously that is not enough to merit a significant investment.

Like many businesses we invest in, there is a quality team with aligned incentives. The CEO, Charlie Bacon, grew his last company to over $4 billion in sales. He has been at the company for 13 years and owns over 5% of the company. Kingsway Financial which is on the board, owns another 40%. Limbach as a company has a complicated history that included private equity ownership. Charlie says all of the right things about culture, prudent growth, and capital allocation and so far has delivered.

Limbach came public via a SPAC (special-purpose acquisition company) and initially traded OTC for technical reasons—they did not have enough shareholders. It is fair to say this was a thinly held company. In addition, initially Limbach had no sell side coverage. So, there are some external factors that make it difficult for folks to invest—$100 million market cap, was OTC, limited history as a public company. But what about the core business?

Limbach is pursuing a strategy with limited execution risk. They are building their maintenance business by expanding into buildings where they were not an initial installer, which is obviously a much larger market than just the buildings they have been the installer. Maintenance contracts are higher margin than installs and are recurring in nature.

Limbach is also expanding geographically into parts of the country where they are not currently operating, such as Texas and the Pacific Northwest, as well as adding complimentary products such as fire protection and electrical. The net effect is that there is a very long runway for growth with a strategy that is very logical. Their margins will expand as the mix of business shifts to include more service. In addition, they are growing backlog and have indicated they are not bidding in certain geographies because of capacity constraints. I also expect to see margins improve modestly on the non-service portion of the business as they bid more selectively.

This is a management team that is quite aware that SPACs that have traded OTC that miss guidance head straight for the penalty box. I believe that they are conservative in their guidance that calls for revenue growth of 10%+ and adjusted EBITDA of $20 million. This is an asset-light business that is growing revenue, growing recurring revenue, and expanding margins—selling for 5x adjusted EBITDA—to be fair, there are some warrants and preferreds that increase

the fully diluted share count – but you have an above average company and growth rate selling below peer multiples with a long runway for growth pursuing a strategy that is executable and logical. Over the next five years we should get revenue growth, multiple expansion, and margin expansion from a quality team providing a non-discretionary service. Boring is beautiful. Sign me up.

My largest position is Fiat Chrysler. I have been involved for several years, when it only traded in Italy, before the spinoff of Ferrari and the Chrysler purchase was completed. Fiat Chrysler, also has high insider ownership. The CEO, Sergio Marchionne and the Agnelli family are major shareholders, but it also lacks some of the attributes I like most in a business. There is effectively no recurring revenue, it is highly cyclical, it is capital intensive, and it is very competitive.

The reasons for owning Fiat Chrysler have changed over time. Throughout, there has been a very effective CEO, but initially it was a sum-of-the-parts story and a post-merger/complicated accounting situation where the company was getting little credit for the valuable Chrysler asset they had purchased. Those reasons are behind us now, and Fiat is still my largest holding. I effectively own it for a very simple reason, real companies don't trade at 2x earnings. The company put out an ambitious five-year plan in 2013 and they have executed against it. They are ahead of plan on every major metric. If they hit their plan, they will have zero net debt and generate $5 per share in earnings. In effect, the company can be bought for less than 2x forward earnings—something has to give as we get closer to 2018.

The press focuses on car volumes, peak SAAR, a weakening consumer. For Fiat Chrysler, it is a mix shift and margin expansion story. They do not need to increase volumes to improve earnings meaningfully. The incremental margin on a *Maserati* or *Alfa Romeo* or even a Jeep is multiples of the low margin fleet sedan business they are exiting. An incremental *Maserati* in Q4 sold for $100,000 euros and generated 25% EBIT margins. One incremental *Maserati Levante* is worth several dozen fleet sedans in terms of contribution. The same story will play out with *Alpha Romeo* in terms of high-margin incremental volumes. Pay less attention to total volumes and more attention to the luxury brands and SUVs and margin expansion.

MOI: How do you think about the art of valuing a business? To what extent do industry-specific considerations or industry comparables play a role, and to what extent do you focus on "shareholder earnings" or free cash flow?

Miller: My favorite metric, by far, is free cash flow yield—the higher, the better. When a stock has a 20% plus FCF yield, there are a lot of ways to make money and a lot can go right. That being said, attractive, growing, sustainable high FCF-yielding companies are almost non-existent right now. I spend most of my time looking at companies that do not screen well. Murray Stahl of Horizon Kinetics refers to them as "invisible companies." Given my operating background and long time horizon, I am comfortable investing in businesses in transition, effectively before the FCF yield is reflected in the quarterly statements. In these situations, the valuation on traditional metrics is much less important than the products, markets, and teams, and the execution risks they face. The exercise is about understanding the event path, what has to happen for us to be successful, and thinking about timeframes and ultimate payoffs. It is not an exercise in finding a company trading at 9x when comps are trading at 11x – it is more an exercise of finding a quality business that has a reasonable chance of being a double or a triple in a few years if we are right, and limited downside if we are wrong.

MOI: How do you strike the right balance between being concentrated in your best ideas while remaining sufficiently diversified to keep downside risks under control? How does short selling fit into your portfolio management approach?

Miller: Charlie Munger had a recent quote to the effect of, "diversification is for people who do not know what they are doing." My family group is Greenhaven Road's largest investor and I personally have the vast majority of my investable assets in the fund. I want to be able to sleep at night and I don't want to look at my three children and say, "I bet the farm on the wrong stock." As a result, we typically own 15 companies in the fund. When we get down to eleven or twelve holdings, I seek greater diversification. When we get to around 18 companies I typically want to put more money into my top couple of ideas vs. adding a 19th or 20th position. Besides the number of positions, Greenhaven Road is diversified in other ways. I don't feel comfortable having the vast majority of my investable assets only in small caps or only in software companies. So, the portfolio will skew towards smaller companies but will own names of all sizes and in multiple industries. The portfolio is also typically divided evenly between high quality companies that can grow and compound earnings over decades, and special situations. Buffett actually had this framework in his partnership. He called the good companies, "Generals" and the special situations "workouts." The benefit of the special situations – which include spinoffs, rights offerings, and post-merger situations – is that the outcomes tend to be less correlated to the overall market, and the catalysts are very company-specific.

I short modestly – the fund has a very long bias. I will use index shorts occasionally as a way to reduce exposure to the

market, and will often have small 1-2% short positions in individual companies. I wanted to preserve the option to short in the fund because I view it as a very long-term vehicle and environments change.

MOI: In your Q4 letter, you wrote that, "The investment business can be brutal on the psyche." Please tell us about a difficult period in terms of performance or "the mental game". How did you handle it, and what lessons did you draw from it?

Miller: A number of years ago, I took a personality test, and one of the conclusions was that I was "comfortable holding a highly divergent opinion." I think this trait benefits me in a rough patch, as I do not constantly need market prices to confirm my thesis. As prices decrease, I am far more likely to buy more shares if the long-term thesis holds than to "puke out" of an investment. As discussed above, I also believe that temperament is incredibly important. I am a pretty even-keeled optimist. During rough periods, I return to fundamentals such as the quality of the team, the cash flows of the business, and the length of the runway. My mantra is, "fundamentals matter." Based on my framework, if holdings continue to have strong products, are well positioned in their markets, have a team I believe in, and a clear and reasonable path to success, I sleep well at night.

I think my past operating experience is beneficial in rough patches as well. Markets tend to panic when GDP growth is stalling. The multiple compression and magnitude of worry triggered by growth shrinking to 1% or even going negative 1% is disproportionate to the havoc it will cause on underlying companies. Shrewd managers in an operating business can easily deal with a 1-2% headwind. In my experience, there are always dials to turn such as suppliers to squeeze, headcount that should really be cut anyways, places where prices can be raised or service levels lowered. The point is the potential of a 1% decline in GDP – what CNBC would call a dreaded recession – can lead to a 10% plus share price selloff. In reality, the actual impact to earnings for most companies and industries is nominal. Appreciating the latitude of company management gives some comfort in buying and holding during challenging times.

Fortunately, the rough patches to date have been macro-driven, not company-specific. When markets were selling off last year because oil was getting too cheap, I just shook my head and thought, "this is ultimately good for the consumer and the majority of companies that we own." I just try to tune out the noise, focus on the fundamentals, and keep my eyes open for the opportunities created by the volatility while accepting that others' styles and approaches are temporarily in vogue, but ultimately fundamentals will matter. For me, the rough patches are a period to look to upgrade the portfolio. When everything sells off indiscriminately, opportunity is created. Volatility is our friend. This means I am typically nearly fully invested and capture much of the downside, but dramatically outperform on the upside.

MOI: You have said that "investors are bad at math." What do you mean by that?

Miller: Well, I am sure your readers are better at math than most, but the average investor significantly underestimates the power of compounding and the impact of differences in return rates over a long period of time. If I ask most people, "how much more money would you have if you were able to grow $100,000 by 20% for 30 years vs. 10% for 30 years?" I get a stutter. I didn't know the answer off the top of my head either, but I know the difference in returns really matters over time. The answer is that the difference between the aforementioned scenarios is over $21 million: the 10% pile grows to $1.7 million while the 20% pile grows to $23 million. That extra 10% of returns per year really adds up.

When investors underestimate the power of compounding, they also underestimate how profitable boring businesses with long runways can be. There is a boring business, Watsco (WSO), which acquired and improved hundreds of HVAC (air conditioning) companies. I want to yawn just talking about it. How good could it be? Well, the historical returns are so astounding I had to double check the numbers. The company trades at over 12x EBITDA and buys companies at 4-6x using debt, cash, and stock. They have had margin expansion with scale and multiple expansion. When you add it all up over 30 years, they have grown revenue 35x, free cash flow 50x, and share price by 60x.

The CEO of one of our portfolio companies, EnviroStar (EVI), worked at Watsco for eight years. He is using the Watsco "buy and build" playbook in commercial laundry distributors which is perhaps even more boring than HVAC. We have gotten in early and if EnviroStar is even half as successful as Watsco has been, we will be thrilled. I know the math works, now the CEO and his team have to do deals and execute.

MOI: Which one or two recent books have given you new insights into the art of investing?

Miller: Joel Greenblatt's *You Can be a Stock Market Genius: Uncover the Secret Hiding Places of Stock Market Profits* was completely eye opening for me. I just had not understood all of the dynamics of spinoffs before reading the book. Joel compounded at 50% per year for over a decade. I really put him up on a pedestal, not only for his returns, but he also because he started the Value Investors Club, which I think is

a great resource for investors, and – even more importantly – he started a group of charter schools, which are making a real difference in New York City. He is a guy who recognizes there is more to life than money. All of his books are solid, but *You Can be a Stock Market Genius* is a must read.

I know your question is about books, but there are some incredible YouTube videos that can be engaging and timely: a *Talks at Google* series that has some fantastic investors, and the Chuck Akre Google talk is well worth the hour.

In a similar vein, I am an admirer of Mohnish Pabrai, who I know is well known to the Manual of Ideas readers. In my almost 20 years of marriage, I have never woken my wife up from a deep sleep except for one time. Early in the life of the fund, I got an email from Mohnish saying he liked what I was doing. It was 1am, but it did not matter, I had to tell somebody. Mohnish is a guy who has given back to his country in such a thoughtful way with his Dakshana Foundation providing resources for poor students. I find he also consistently gives back to the investing community by allowing talks he gives to be published and freely accessible on YouTube. I have a Pabrai alert setup through Google, and whenever a new talk comes out, I sit down for an hour or two and soak it in. His book *Dhandho Investor* is really solid as well, but I think the talks on YouTube are even better.

MOI: You recently presented at the Zurich Project. It was very well received—can you tell our readers the gist of the presentation?

Miller: John, first let me say, you all put on an incredible event, rarely are two days of travel worth it, but in the case of the Zurich Project, it would have been worth it if it was held at the North Pole. You are a great convener, I got to meet investors I had admired for years and interact with capital allocators in a much different setting than the typical one-hour office meeting. So, thank you for holding the event, it was fantastic.

In terms of my presentation, I only did it because I had to. I am not a professional presenter, all I want to do is invest in companies, but the cost of admission to the Zurich Project included a presentation to peers that was not about a particular investment idea, so I thought my value add would be to explain how I have attracted a highly aligned group of limited partners while spending less than 5% of my time on "marketing".

In essence, I use a fairly simple website, my investor letters, which I write anyway, and some automation. The website greenhavenroad.com makes it easy for people to sign up for more letters and to indicate if they want more information. It is all automated, so it is low touch for me. I also make old letters available. The result is, an interested party can read hundreds of pages of letters spanning multiple years. I am not right for 99+% of the world, and that is okay. The beauty of the Internet is the reach and always-on nature. I was trying to push managers away from relying on capital introduction to a series of gate keepers, which leads to a series of meetings that are all very time consuming.

What I have learned is that if your returns are good and you are willing to share the rationale for your investments, there are people out there who will invest. There is a path towards building an investor base only through inbound inquiries. You end up with a stronger and more aligned investor base, and it allows you to spend almost all of your time on investing, which is what drives returns and why most of the attendees got into the business anyway. There are some resources about this approach at HubSpot's website.

Could my fund be bigger if I was actively trying to meet with anybody who has money—of course, but my life would be full of meetings and rejection. When I meet with somebody or do a call, they already have a very good sense of who I am and what the fund is about. It is a better use of everybody's time. I was trying to say, don't spend your time figuring out how to woo the large endowments that have a two-year plus process—I would have starved. With a decent website, useful content, and infrastructure that allow for low-touch inbound inquiries, you can reach a broad audience and not have to compromise investing time. There are wealthy individuals, family offices, and funds of funds that will self-select in.