Newsletter 3

July 2025

For external use

Compound Equity Group – Investment Newsletter – July 2025

Dear Fundholders,

A Further Update on Our Start

Compound Equity Group continues to evolve. By way of reminder, we now manage two funds, which both follow an identical approach, investing globally through a concentrated portfolio of currently 23 stocks across a broad spectrum of market capitalisations. The custodian for both funds is now State Street. We refer to the funds internally as the Irish fund and the UK fund, and the holdings are identical.

Our results to date are frankly unremarkable, neither good nor bad, and are summarised in a table at the end. The Irish fund, denominated in € and US$, is now called RGI Compound Global IE Equity Fund. When we started managing this fund at the end of August 2024 the new shares were conveniently repriced at 1.00. Today, on 17 July the € price is 1.065 (+6%) and the $ price 1.114 (+11%). The strengthening of the € from 1.03 to the US$ on January 1 to 1.16 to the US$ today has been a headwind for the Euro denominated shares.

The UK fund, denominated in GBP, is called SVM World Equity Fund. Our intention by now was to have this fund renamed RGI Compound Global Equity Fund, however the renaming is taking longer than anticipated. On July 17 SVM World Equity B shares are priced at 479p versus 425p when we started on August 5, so up 13% in £. For context the latest UK 12-month CPI inflation, was 3.6%.

As I said last time, I would encourage shareholders to pay little attention to results so far. Please judge us on what we achieve over a rolling 4–5 year period. Compound's strategy and approach is one for the long term. If you do not have a time span of 4-5 years, I would courteously suggest these funds are not appropriate for you. My expectation is that investing in these funds will be a prolonged grind with returns eked out. By way of reminder our aspiration is to deliver returns after fees that are well ahead of inflation, thereby increasing the purchasing power of the Compound Global Fund shareholders. Month-by-month results are summarised through to the end of June in Appendix 1.

On the housekeeping front, Compound Equity Group is now approved in its own right by the Financial Conduct Authority. Previously we were working under the regulatory umbrella of River Global Investments. And we now also have a website, compoundequitygroup.com, and we would welcome feedback on it.

Thoughts on Owner Free Cash Flow and Portfolio Revenue Growth:

As I will reiterate many, many times we are searching for businesses that can redeploy capital at medium to high returns with a degree of certainty and generate both growth in revenues and growth in owner free cash flow. The financial press is generally fixated with earnings, often also called net income or earnings per share (EPS). I have much more faith in owner free cash flow than earnings.

Why the fixation with owner free cash? Simply put, cash is a fact whereas earnings are generally an opinion. You can spend cash; you cannot necessarily spend earnings. I would encourage any budding investment nerds to study Terry Smith's outstanding book, "Accounting for Growth", an exposé of the shenanigans management indulges in to overstate their profitability and earnings. My recollection is the first edition of this book back in 1992 got Mr. Smith fired from his role of Head of Research at UBS Philips and Drew, testimony to the insight, accuracy, and wisdom of Mr. Smith's analysis.

I define owner free cash flow (owner FCF) as the cash available after funding all growth, so cash after deducting the cash costs of operating the business, including working capital and marketing, maintaining and adding to equipment, and acquiring other companies. Owner FCF can either be stored on the balance sheet for future use, for example an acquisition, or returned to shareholders via dividends and buybacks. Another perspective is imagine you were a billionaire and owned the business 100%, owner FCF is money you could spend on frivolities and philanthropy, after making all the investment required to safeguard and grow your business. I have a penchant for businesses that generate oodles of owner free cash. Think of owner FCF as a comfort blanket providing managers and owners with options. A company with owner FCF can take advantage of a recession by investing against the grain; they can buy an adjacent business the moment that business decides to sell; they can buy back their shares if their share price is down, or they can pay special dividends.

Moving onto revenue growth, the recent revenue growth of the stocks in the portfolio is summarised by quarter or half in the table below, the figures are in local currency:

Portfolio Revenue Growth Rates

Stock	3Q 2024	4Q/2H 2024	1Q 2025	2Q/1H 2025	Stock	3Q 2024	4Q/2H 2024	1Q 2025	2Q/1H 2025
1	21	22	17	18	13	11	-4	-5	15
2	25	28	31	23	14	11	10	8	
3	51	25	20		15	-3	5	6	6
4		9	7		16	16	14	8	
5	7	14	7		17	19	16	15	
6	17		14		18		29		
7	37	15	15		19	36	37	35	39
8		11	9		20		20		21
9	19	24	30		21	39	27	17	
10		13			22	19		12	
11	13	15	17		23	9	11	12	11
12	16	12	15		**Average**	**19**	**17**	**15**	**14**

The overriding point is the stocks in the portfolio are pumping out robust rates of revenue growth, the portfolio averaged 15% revenue growth in Q1 2025.

Wrapping owner free cash flow and revenue growth together, Compound is trying to identify businesses that can grow revenues and earnings with reasonable certainty, all the while sending their owners a growing stream of cash. This is easily said, harder to deliver. Layered on top of this is a judgement on valuation. If a business is generating vast owner FCF in relation to its valuation, we are less demanding on the growth rate.

Some Thoughts on Private Equity

One niggle I have is that trouble may be brewing in the world of Private Equity (PE). PE has been a prodigious force for the last 20-30 years and has grown to over $8 trillion of assets. Grossly simplified, PE buys businesses, generally puts them in a fund, then 4-5 years later tries to sell each business for substantially more than they paid. Whilst PE owns the business they seek to optimise it's profitability through measures such as improving the management, opening up new markets, and improving cost control. PE will likely also try to improve capital efficiency by taking cash out of the business and replacing it with debt, probably from Private Credit (see below). The understanding PE has had with investors was PE would deliver higher returns than the stock market and, in return, PE would command higher fees. A typical PE fund might charge a fee of 1-2% of assets plus carried interested ("carry"). Carry is a percentage of the fund profits, say 20%, after investors have received a pre-agreed hurdle rate.

I have multiple concerns about PE:

Poor liquidity: PE seems to be increasingly illiquid – in other words investors cannot exit. One dataset I recently looked at demonstrated the five-year distributions from the 2018 and 2020 vintages were substantially lower than the 2010 – 2016 vintages. The number of PE exits is predicted to be down sharply in 2025. Investors in the 2020 vintage have only recovered 10% of their original investment.

Lacklustre returns: Average returns look poor. Average three-year returns appear to be around 3%/year, well below the stock market. One of the large, listed PE firms recently disclosed the returns on their Evergreen funds had slipped to 7-8% short term, this maybe the thin end of the wedge.

Untested valuations: If a PE fund rolls over a businesses or businesses that it cannot exit how can one be confident the valuation is correct? It is analogous to asking an overconfident teenager to mark their own homework, the grading is liable to be generous. The PE firm is surely conflicted as the carry is contingent on the exit valuation?

Lack of funding: In Q3 2024 unrealised values were around $4.4 trillion, whereas dry power was around $1.7 trillion. The PE industry is short of $2.7 trillion to exit the $4.4 trillion. To give context the French economy is around $3 trillion, PE has a shortfall almost the size of France's economy. The proceeds from fresh fundraising are also down.

High and widening ownership: PE is widely held by professional investors and endowments stretching for return (yield). For example, the Harvard Endowment has 39% of assets under management in PE and 11% in public market equities. Presumably tempted by assets and fees, the big active fund managers are now plunging in and forming joint ventures with PE firms thereby making PE investments available to retail investors. These joint ventures will offer "combo" products where liquid assets from the active manager, so equities and bonds, are blended with illiquid private assets from the PE firm. The active manager gets to enjoy a higher fee, the PE firm gets to realise an exit. The investor pays higher fees, sacrifices liquidity and may or may not get a higher return (see above).

An area of high growth, that is aligned with PE is Private Credit. My understanding of the Private Credit industry is somewhat rudimentary, so take this analysis with a pinch of salt. Private Credit basically does what banks did 20 years ago. They lend, so they provide capital, to small and mid-sized businesses. Typically, these loans are wrapped in a closed end Business Development Corporation (BDC) which issues shares. The borrower will pay a base lending rate of say 500 basis points, a further illiquidity premium of another 500 basis and an annual fee of 20 basis points, for an all-in rate of say 1020 basis points. The growth in Private credit has been phenomenal, around 18% compound for the last two decades. The Private Credit industry now has around $1.8 trillion under management, mostly in the USA. Around 40% of lending is direct lending, this is where PE lends to a business owned by PE. An important new avenue of growth for Private Credit will be Asset Backed lending, which is potentially massive ($30 trillion?). A factor behind the strong growth has been the robust regulation of banks post the Great Financial Crisis (GFC), so banks have retrenched, and Private Credit has stepped in. Meanwhile returns in Private Credit have been good, approximately 500 basis points more than global high yield funds, around 900 basis points a year for the last decade. New providers of Private Credit, non-bank lenders such as the Alternative Investment Managers ("Alts"), have ballooned. My concern with Private Credit would be the exponential growth. Industries and businesses where lending has grown explosively can be a minefield. And in the push for growth, flattered by good returns, the industry may be taking on more risk. Further concerns are the industry has not been tested by a severe economic downturn combined with high interest rates and also the loans might be illiquid in a downturn. The regulatory scrutiny on Private Credit is much lighter than on the banks. My level of uncertainty ranges from moderate to high when investing in unsecured debt and banks, and I would note some of the great investors are very judicious when it comes to investing in this area.

That said "people who live in glass houses should not throw stones". Most open-ended unit trusts and mutual funds have also not covered themselves in glory over the last 20 - 30 years, we will perhaps discuss some of the reasons in a later newsletter. Here at Compound we are very mindful that many of our fundholders are in there golden years, they have 20-30 years left to go. Our fundholders remind us of the importance of liquidity, they want to be able to access their savings, not to be cautioned by their private banker that they need to wait until 2030. Should the need arise, we believe we could entirely liquidate both Compound funds in a few days. Our fundholders also beseech Compound to invest wisely and to preserve and ideally grow their purchasing power, this is their reward for investing in listed equities. On this front, our intent is clear, see the portfolio revenue growth metrics detailed earlier in this newsletter.

Some Latest Thoughts on the Current Investment World – The "Litany of Grimness"

My mantra remains that the current investment world is a "Litany of Grimness". I remind the Compound team daily that the economic and political environment is as challenging as any I have experienced.

France remains the posterchild for a large, developed nation with an unconscionable and fractious fiscal set-up. The budget deficit is now 5.8% of GDP and national debt is circa €3.3 trillion. By 2027 the debt to GDP ratio will be circa 120%. The Prime Minister, M. Bayrou, who has an invidious job, recently unveiled a new budget which included €40bn of proposed savings including abolishing two bank holidays. Bayrou's changes are mostly tactical rather than structural. The response from the other political parties has predictably been strident belligerence. My favourite line was from the ultra-left wing La France Insoumise (LFI) who declared Bayrou's programme "a long tunnel of untruths, a museum of neolithic horrors". One personal observation is terrible sovereign governance and sluggish economic growth does not necessarily equate with bad company results and bad stock returns. Poor sovereign governance tends to force the domestic companies to be better. The companies know they cannot rely on their government, so they improve governance, focus on productivity, they innovate, and they accelerate going global. Some of the corporate gems in France include L'Oréal, Pernod Ricard, LVMH, L'Air Liquide, Airbus, Dassault and Virbac.

Meanwhile the UK is trying to emulate Frances tragic fiscal performance as fast as possible. The March Economic and Fiscal Outlook published by the Office of Budget Responsibility (OBR), despite being over-optimistic, is a dour read and I recommend a stiff Negroni before embarking on this tome (https://obr.uk/efo/economic-and-fiscal-outlook-march-2025/). Mrs Reeves' policies have so far largely backfired. In March the OBR had bought down growth forecasts for 2025 from 2% to 1%. Further tax increases seem inevitable and will no doubt curtail economic growth further. UK debt to GDP is 100%. The dilemma facing Reeves is evident in the June tax figures where the raised National Insurance contributions brought in an additional £3.1bn but this more than offset by an £8.4bn jump in the cost of government debt, as rising inflation is pushing up the cost of index linked gilts. Meanwhile even though the tax rate applied to Capital Gains Tax is up, proceeds are down from £13.5bn in the first 6 months of 2024 to £11.8bn in 2025. Mrs. Reeves should not be surprised as 15,000 -16,000 millionaires have left the UK in the last year. Winston Churchill put it eloquently when he said: "For a nation to try to tax itself into prosperity is like a man standing in a bucket and trying to lift himself up by the handle".

On US tariffs I resonate with Stanley Druckenmiller's position, namely that 10% tariffs were probably the least "evil" option on offer. In the US entitlements and interest devour the entirety of tax revenues. The US fiscal deficit is 6-7% of GDP. The DOGE effort seems to have plateaued at $190bn. Trump's Big Beautiful Bill reduces tax rates and possibly tax take. Hence tariffs are all that remains to raise money for government. Tariffs are effectively a consumption tax and inevitably regressive. US debt is $37 trillion, about 120% of GDP. For context US tax receipts are circa $5 trillion. Just like the UK the US is vulnerable to interest rates, a 1% rise in rates would add $370bn to the interest bill, just over 7% of tax receipts. President Trump is acutely aware of this vulnerability and relentlessly harangues Chairman Powell at the Federal Reserve to drop rates.

In the case of the UK and the USA it seems that some debasement of the respective currencies is inevitable. The rising price of gold supports the debasement thesis. The implication for owners of stocks is interest rates will likely stay higher and for longer, curtailing stock valuation multiples. However, over the very long run, stocks provide a hedge against debasement because they represent ownership in real assets and productive enterprises. Regrettably, debasement will impact the poorer in our societies the most.

A Business We Like – Wise WISE.LN – 1033p - £10.6bn market cap

Wise is a business we are interested in. Wise is a UK listed company that moves money around the world, quickly, easily and cheaply. Wise aspires to be the world's lowest cost, highest quality, money mover. If you are not a Wise customer, I recommend you load the app on your phone and see for yourself. If nothing else I am confident that on your next vacation you will discover much more competitive exchange rates than the rates offered by your old school commercial bank, for example Barclays, Lloyds, BNP, Bank of America etc. One of the grubby secrets of commercial banks is the profitability of their foreign exchange business, their fees are obscure but probably 200-250 basis points. Put another way when you use your debit card to spend €100 on a meal in Spain, your bank at home pockets €2.00 to €2.50. The commercial bank will charge a transaction fee and a spread on the exchange rate. This €2.00 to €2.50 is Wise's opportunity.

Here are some elements of Wise we like:

- Wise delights customers, both individuals and businesses, with value for money, service and ease
- Wise is growing fast. Between 2021 and 2025 active customers are up 2.6x to 15.6m. Cross border volumes are up 2.7x to £145bn. Customer holdings, funds left on Wise platform, are up 5.8x to £4.5bn.
- Wise's provides terrific speed of payment. 65% of all payments are instant, 86% are within one hour. Their engineering core is their single stack technology which is created and run by 850 engineers globally. This stack bypasses the clunky traditional correspondent networks used by banks.
- Wise has unique infrastructure. Wise has 70+ global licenses, direct connections in 8 countries and a further 90 or so integrations into domestic banks. Wise covers 160 countries and handles 40 currencies. Wise partners include Standard Chartered, Morgan Stanley, Itau Unibanco, Nubank. Wise is now directly integrated into 8 local payments

systems, the recent additions include Instapay in the Philippines, Zengin in Japan and PIX in Brazil.

- Wise prices competitively and passes on the benefits of scale with lower prices to customers. The cross border take in Q4 FY 2025 was 53 basis points down from 69 basis points in FY 2020. In 2025 Wise dropped the take rate 9 basis points. I personally received an unsolicited rebate on my Wise fees this last quarter.
- Profitability is high. The gross margin for FY 2025 was 75%, up from 73%. The pre-tax margin for FY 2025 was 21%, up 17%, after increasing administrative expenses 25%.
- Earnings quality is high. For the last five years the cumulative ratio of owner FCF/net income is 114%
- The runway is long. Around £32 trillion is moved cross border each year. Wise moved a fraction of this, £145bn, in 2025. Wise believes they can grow profits 13-16% a year.
- The valuation is tolerable. For one year out the price earnings multiple on reported net income is 26x and the owner FCF yield is 3.7%.
- The management are conservative and favour adjusted net income rather than reported net income. The main difference is in the adjusted figure is a notional figure where management exclude interest income in excess of 1% earned on customer deposits. The reason for this is one day in future, when Wise has the relevant banking licences, management intend to return interest income above 1% to the customer. The valuation 12 months out on adjusted net income is 47x.
- The balance sheet is strong with £1.3bn of net cash. Net cash is 13% of the market capitalization today rising to 32% by 2029.

I think of Wise as the Costco of global money movement. A scale business that is constantly enhancing their competitive moat through better service and better price. And the runway is very long.

Wishing you all an enjoyable finish to the Summer.

Yours Sincerely,

Jonathan Knowles

Jonathan Knowles, Investor

Fund Returns, Net of Fees*

UK Fund: SVM World Equity Fund (to be renamed RGI Compound Global Equity Fund) – GBP

%	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug**	Sep	Oct	Nov	Dec	**YTD**	**ITD**
2024								0.6	-0.4	-1.3	3.0	2.2	**4.2**	**4.2**
2025	4.9	-7.1	-8.7	1.9	8.9	4.0							**2.7**	**7.0**

Irish Fund: RGI Compound Global IE Equity Fund – EUR

%	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	**YTD**	**ITD**
2024									0.5	-1.6	3.7	2.5	**5.2**	**5.2**
2025	4.2	-5.9	-9.9	0.2	10.2	2.2							**-0.2**	**4.9**

Irish Fund: RGI Compound Global Equity Fund – USD

%	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	**YTD**	**ITD**
2024									1.5	-4.5	0.8	1.0	**-1.2**	**-1.2**
2025	3.8	-5.7	-6.2	5.2	9.9	5.8							**12.3**	**11.0**

YTD = Year-to-Date, ITD = Initiation-to-Date

* Since Compound took over management of the funds

** Since 26th August 2024

Compound Equity Group

Disclaimer

The content of this newsletter is provided for informational purposes only and does not constitute, nor should it be considered as, financial advice, a recommendation, or an offer to buy or sell any financial instruments. All opinions expressed herein are those of the presenter and do not necessarily reflect the views of Compound Equity Group Limited ('CEG')

No Financial Advice. This newsletter is not intended to serve as a basis for any investment decision. You should obtain independent financial advice tailored to your personal circumstances before making any investment or financial decisions. Reliance on the information presented herein is at your individual risk.

Accuracy and Completeness. While every effort has been made to ensure that the information contained in this presentation is accurate and up-to-date, CEG makes no warranties, express or implied, regarding its accuracy, completeness, or suitability for any purpose. Past performance is not indicative of future results, and all investments carry risk, including the potential loss of principal.

Regulatory Oversight. Compound Equity Group Limited is authorised and regulated by the Financial Conduct Authority (FCA), Firm Reference Number (FRN) 1023836. This newsletter is provided solely within the parameters of our FCA authorisation and is not intended as a substitute for full regulatory disclosures or documentation.

Risk Warning. Investments in financial instruments and strategies discussed in this presentation carry inherent risks. You should be aware that under current market conditions, the value of your investments may fluctuate, and there is a possibility of losing some or all of your initial investment. You should, where appropriate, seek independent professional advice regarding the risks involved.

Limitation of Liability. Under no circumstances shall CEG, its affiliates, employees, or agents be liable for any direct, indirect, special, consequential, or any other type of damages arising out of, from, or in connection with this newsletter or any actions you may take based on its content.

You acknowledge that you fully understand and accept these terms. If you require further clarification or additional details regarding our regulatory obligations, please consult our Compliance team.