

Quarterly Manager Commentary

Q4 2024

The most significant event during the fourth quarter was the election of Donald J. Trump as President of the United States. His election will undoubtedly have an impact on our portfolio companies – but we think it will be a net positive since his push for deregulation and lower corporate taxes will more than offset the relatively minor impact of potential tariffs on our holdings. We'll touch on this in more detail throughout the commentary including our take on tariffs on Canada and Mexico.

The fourth quarter capped off a relatively tepid year for Turtle Creek, at least in terms of the share prices of our companies. While we managed to finish in the black for the year, we lagged the indices by a substantial margin. This was a complete reversal from 2023 when the indices lagged Turtle Creek by a similar substantial margin. However, by one important measure, 2024 was a more successful year than 2023. This may sound odd as the unit price of our flagship fund increased by 30% in 2023 compared with only 2% in 2024. But over shorter periods of time, we measure our success more in terms of growing the intrinsic value of our portfolio (our term is Portfolio Business Value) than we do on unit price results.¹ Of course, over the long run, it is the increase in the unit price rather than our intrinsic value that counts, yet we have seen time and time again that as goes intrinsic, so ultimately goes the unit price. In this regard, 2024 was a stronger year with a 14% increase in the Portfolio Business Value of Turtle Creek Equity Fund ("TCEF") versus a muted 3% increase in 2023. The source of the increase was broad based across the portfolio with 23 of the 26 companies that we owned continuously throughout the year increasing in intrinsic value and only 3 companies decreasing. It is quite normal for us to reduce the value (long term forecast) of a few of our holdings in any given year. We always stress that we are not conservative in our financial forecasts – we are trying to predict the future as best we can. Not surprisingly, from time to time, negative macro factors or company specific events will cause us to temper our assumptions. The conservative part of our approach, and a key component of our risk management process, comes in continuously tilting our portfolio towards the companies with the biggest margin of safety or discount to Business Value.

Moving on to specific companies, the largest positive contributor in our flagship fund, both for the quarter and full year, was our investment in Bread Financial. Bread is a regulated financial services company primarily focused on the issuance of private label and co-branded credit cards. It enjoys a strong return on equity (ROE) in excess of 25% as compared to Canadian banks that are in the low to mid teens. And while nearly 60% of Bread's credit card holders have a prime credit rating, the remaining 40% have credit ratings that are below prime. Despite higher losses from serving these lower credit customers, the higher revenue yield results in higher ROEs. Bread is an excellent example of the power of our long term thinking. It was, in fact, a negative contributor to our performance in 2023 and 2022 before generating a significant positive return for us in 2024. And despite its healthy move this past year, we feel it still holds the potential for significant price appreciation in

the near future and it remains one of our largest holdings. There are a number of potential tailwinds for Bread including an expanding traded price multiple, a shrinking share count due to repurchases and the possible dropping of a proposed rule by the Consumer Financial Protection Bureau (“CFPB”) to cap credit card late fees. Under prior Democrat administrations, the CFPB introduced numerous regulations and restrictions around the financial services industry. The proposed cap on late fees would have made it uneconomic to service lower credit score customers. Not only does the late fee importantly serve as a deterrent to skipping payments, it also adds to the total economic return that allows the provision of credit to these higher risk customers. The CFPB under President Trump is widely expected to be more business friendly and less focused on increasing an already hefty regulatory burden.

Two other companies that contributed positively to the flagship fund's returns during 2024 happened to be the two most disappointing for us in terms of decisions taken by boards: Discover Financial and Berry Global. We wrote about Discover Financial last quarter so we won't rehash things here, but we believe the board suboptimized long term value for shareholders through a variety of actions over the prior year and a half. If you are interested in more detail you can read about it [here](#). Nevertheless, their actions resulted in a higher share price in the short term which we took advantage of to exit the position.

Berry Global, a company we have owned for seven years, was the source of the one notable corporate event the portfolio experienced during the quarter. Berry completed a previously announced spin-off of a part of the business into a separate publicly traded company. Berry then announced a merger with another publicly listed packaging company – Amcor. While combining the two companies makes sense from a synergy standpoint, much like the Discover Financial merger with Capital One, we don't believe Berry's shareholders received their fair share of the combined company. Rather than continue to pursue an independent strategy that would have maximized long term value creation, the Berry board accepted poor merger terms hoping to achieve a higher traded share price in the shorter term.

We know Berry's board has been frustrated with its low share price for some time. When we first added the company to the flagship fund's portfolio seven years ago, it was a classic platform company. Berry was the leading consolidator in the plastics industry, able to make bolt-on acquisitions at very attractive prices once significant cost synergies were realized. In 2019, they made a large strategic acquisition in Europe that provided them the same platform in Europe as they have in the Americas – financing the acquisition with 100% debt. All good up until that point. But since then, the board has gradually altered the company's strategy, over time lowering their senior debt leverage target and backing away from 'inorganic' growth (bolt-on acquisitions) in favour of divestitures and spin-offs designed to improve the company's organic growth profile. This was all with an eye to getting a higher traded share price in the short term. Indeed, the merger with Amcor is in the same vein. Amcor has always traded at a higher price-to-earnings multiple than Berry, despite the fact that their earnings growth has lagged Berry's by a substantial margin. One could speculate that as one of the few large Australian public companies it garners a premium multiple from Australian investors (we see this sometimes in Canada with some Canadian companies). This, combined with the fact that it is in the S&P 500 index, could explain the traded multiple difference. Clearly, Berry's board is hoping that this transaction will result in Berry enjoying a higher traded earnings multiple, and they may be right.

It might strike you as odd that we are criticizing a board for trying to achieve a higher traded price for shareholders. It should go without saying that we are all for higher share prices for our holdings, but not to the detriment of long term shareholder value. We believe that if Berry had continued on its path of a higher (but still prudent) senior debt level, making accretive acquisitions and opportunistic share repurchases, then the share price would be much higher in five to ten years than it will be through merging with Amcor.

Looking back over the full year, we added four companies to the flagship fund and removed three to end December at our target of 30 holdings (we started the year with 29 holdings). Four additions in a year is pretty normal and is in line with our long term average. What is not normal is how attractive they were from a valuation perspective when we added them. In each instance, the companies were trading at a greater than 50% discount to their respective Business Values (intrinsic value). Growing the investment team over the years has allowed us to work on more companies, which has in turn resulted in us identifying more companies that are trading at a discount to our estimate of Business Value. This greater choice has resulted in an increase in the valuation threshold for a company to make it into the flagship fund. Ten years ago, the threshold might have been that a company only needed to trade at a 25% or 30% discount in order to be a candidate for TCEF. Adding companies that are this cheap results in a forward looking 'buy and hold' return that is much better than in the past.

The first company we added was BRP (formerly known as Bombardier Recreational Products). We have owned BRP for five years in Turtle Creek Canadian Equity Fund, but it had never been priced attractively enough during that time to make it into the flagship fund. Early in the year, the share price declined to a point where it merited going into TCEF. Since that time, the share price has fluctuated and ended the year modestly below where we added it.

BRP is the ultimate consumer discretionary company – when consumers are facing headwinds, purchases like Sea-Doos and ATVs often get deferred. Investment opportunities in consumer discretionary companies occur when consumers are pulling back, and we think BRP's intelligent management team is doing all the right things to continue to innovate and take market share in each of their categories. If one is willing to look past the current weak environment, one can see how attractive the stock is today.

The second company we added this year is Ashtead Group, the parent company of Sunbelt Rentals, the second largest equipment rental company in North America. Interestingly, Ashtead is the first European-headquartered and European-listed company we have ever owned. We weren't looking for a European company but as we were doing work on the largest equipment rental company – United Rentals – we concluded we liked Ashtead more. While Ashtead was founded in the United Kingdom many years ago, 95% of their operations are in North America today. Last month, they announced that they are redomiciling their headquarters to the United States and will be moving their primary listing to New York from London. Note that this is not simply a New York listing but fully relocating the company to the United States with an eye to being included in the S&P 500 index. Many of our Canadian companies are cross-listed in New York but are unlikely to be considered by S&P for index inclusion because they are not U.S. domiciled companies.

The third company is Kinsale Capital Group, a specialty insurance company based in the United States. Kinsale operates in the unregulated excess and surplus lines of the

insurance market. This is a good example of how, unlike many value investors, we will sometimes own companies that trade at high price-to-earnings multiples. Since we are willing to give a company credit for substantial growth far into the future (if we think it is merited), we do not miss the opportunity to invest in an outstanding company like Kinsale that may appear expensive to some investors based on its currently high traded multiple.

The final company we added this year is WillScot Holdings. WillScot is the dominant provider of turnkey space solutions in North America: think modular offices, temporary classrooms, portable storage containers, etc. When we established the position, the company was in the midst of a large acquisition – buying a smaller competitor called McGrath Rentcorp. We were sceptical that the acquisition would be approved by the competition authorities and so didn't include this acquisition in our financial forecast. As it turned out, WillScot had to cancel the proposed acquisition and announced a meaningful share repurchase program – right in line with our assumptions.

For the year, the four new positions discussed above contributed, in aggregate, a modestly positive amount to the unit price of TCEF. More importantly, the average discount to intrinsic for the four positions is now greater than 60%, mainly as a result of increasing our long-term forecast on a couple of the companies since we added them. In addition to trading at a remarkably high discount to Business Value, all four of these additions have long tenured management teams that are executing proven business strategies that create long term shareholder value. We expect to continue to own each of them for the long term, unless, of course, the discount to intrinsic value for a particular holding narrows to the point where we feel we need to remove it from the portfolio. This is exactly what happened in the quarter with the one removal – Urban Outfitters. We like the company, but the share price had increased to the point where it was trading at only a 30% discount to intrinsic value. We first added Urban to TCEF over seven years ago and this is the second time since then when we have not owned any shares. As we still like the company, we will continue to follow it closely and it wouldn't be surprising if we added it back to the portfolio at some future point.

As we write this, the United States announced, and then subsequently paused for 30 days, the implementation of 25% duties on Mexican and Canadian imports. If implemented, the tariffs would have a negative impact on the Canadian economy (and also the American one). Monday morning, we tried to make sense of the situation. We quickly concluded that given the amount of economic integration within the North American economy, a blanket tariff was unlikely to be implemented. Auto plants, among other areas, would have shut down in days or weeks and thousands of workers would have been laid off. And there were no details as to how the tariffs were to be implemented. The Trump administration is known for establishing extreme positions in order to bolster its negotiating position. But we are willing to bet that he is not going to plunge the U.S. economy into disarray and induce a spike in inflation. So we did what we always do in these situations after making our assessment – we started buying more of the positions whose share prices had declined the most.

Of course one cannot be certain that some form of tariff may ultimately come to pass. Companies that engage in cross border trade will of course be hit the hardest. But companies that are exposed to the Canadian economy will also see an impact on their businesses in the event of economic weakness and increased unemployment. In thinking about the impact of these potential tariffs on our portfolio companies we would break it down in two ways: first, how much of our portfolio is exposed to the Canadian economy; and,

second, how much of our portfolio ships product across the border. In the first instance, TCEF's portfolio companies overwhelmingly operate in the United States and the rest of the world, not in Canada. In fact, on a look through basis, less than 10% of revenue of our portfolio companies is realized within Canada (to be precise, it is 8.3%). So, if tariffs cause the Canadian economy to slow, it will have an impact on a small portion of the portfolio and we would surmise that the impact will be modest. On the second point of how much of our portfolio ships product across the border, this too is a very small portion. The few companies in our portfolio that ship product across the border can take steps to mitigate the impact of potential tariffs. For example, one of our largest holdings, Premium Brands, has always tried to minimize the amount of food that they ship across the border – shipping food products from one country to the other is accompanied by a higher level of regulatory complexity. Recently, they closed on the acquisition of two U.S. companies that provide them with in-country production capacity (instead of shipping from Canada) to support the growth of a large U.S. customer. Another of our large holdings, ATS Corporation, delivers about 15% of their product from Canada to the United States, but they have sufficient capacity in the United States to shift production over time if tariffs are implemented. The most obvious example of a potential negative impact on our portfolio is BRP, an average size holding, which has the majority of their production in Mexico, so we are paying as close attention to the Mexican situation as we are to the Canadian.

Effective January 1, we are making modest increases to the annual distribution paid by certain funds' D1 or endowment distribution classes of units, and maintaining the amount paid by each fund's D2 or full distribution classes (see the [Communications](#) section of our website for specific dollar amounts per fund and class of units). We review the distribution amounts annually and make a change, if appropriate, at the first of the year. With both classes, the idea is to provide an annual payout such that one's initial invested capital is maintained over time. For D1 classes, the distribution amount is based on the 'endowment spending model', specifically, the Yale Endowment Spending Rule. For D2 classes, the distribution amount is higher, but still sustainable.

Quarterly Results

Unit Price Results

During the quarter, the net asset value of the **Turtle Creek Equity Fund** declined by 2.7%.² This was behind the S&P/TSX Completion index which increased 3.6% and the S&P MidCap 400 index which increased 6.8% (both in Canadian dollars).³ We removed one company, to end the quarter with 30 holdings.⁴ 65% of the portfolio was invested in U.S. companies and 35% in Canadian companies.

Turtle Creek Synthetic PE Fund ("TC SPEF") declined 15.1% during the quarter.² We made two additions to the portfolio, to end the quarter with 27 holdings.⁴ 65% of the portfolio was invested in U.S. companies and 35% in Canadian companies.

Turtle Creek United States Equity Fund ("TCUS") declined 8.4% during the quarter, behind the S&P MidCap 400 index which was essentially flat (increased 0.3%), both in U.S. dollars.^{2,3} We made two additions and one removal to the portfolio, to end the quarter with 28 holdings.⁴

Turtle Creek Canadian Equity Fund ("TCCF") declined 3.5% during the quarter, behind the S&P/TSX Completion index which increased 3.6%.^{2,3} We made no additions or removals to the portfolio, to end the quarter with 22 holdings.⁴

Business Value Results

Changes in Portfolio Business Values during the quarter are shown below.

	TCEF	TC SPEF	TCUS (US\$)	TCCF
Quarterly change in Portfolio Business Value	▲ 6%	▲ 9%	▲ 3%	▲ 5%

Disclosures

Information Sources: Turtle Creek Asset Management Inc. ("TCAM" or "the Manager"), Bloomberg.

Past performance must never be construed as investment advice or a prediction of future performance. We have expressed our own views and opinions in this document and these may change without notice and may differ from others in the industry. All statements, other than statements of historical fact, that address activities, events or developments that we believe, expect or anticipate will or may occur in the future (including, without limitation, statements regarding any objectives and strategies of a fund or outlooks for the portfolio companies) are forward-looking statements. These forward-looking statements reflect our current expectations, assumptions or beliefs based on information currently available. Forward-looking statements are inherently uncertain and subject to a number of risks that may cause the actual results of any of our funds (each a "Fund") to differ materially from those described in the forward-looking statements, and even if such actual results are realized or substantially realized, there can be no assurance that they will have the expected consequences to, or effects on, a Fund. Factors that could cause actual results or events to differ materially from current expectations include, among other things, length and severity of the pandemic, volatility in financial markets, fluctuations in currency exchange rates and interest rates, tax consequences, changes in applicable laws and other risks associated with investing in securities and those factors discussed under the section in the applicable offering memorandum of a Fund entitled "Certain Risk Factors". Any forward-looking statement speaks only as of the date it is made and, except as may be required by applicable securities laws, we disclaim any intention or obligation to update any forward-looking statement, whether as a result of new information, future events or results or otherwise. Although we believe that the assumptions inherent in the forward-looking statements are reasonable, forward-looking statements are not guarantees of future performance and, accordingly, undue reliance should not be placed thereon.

Endnotes

1. A company's intrinsic value or Business Value represents our best estimate of the present value of such company's future cash flows and is necessarily comprised of many assumptions, the use of which includes a number of risks and uncertainties that may cause actual values to differ from our estimate. A Fund's Business Value is calculated using our estimate of Business Value for each company, weighted based on the portfolio's holdings.
2. Based on the change in net asset value of the Fund's Class I Series 1.0 Units.
3. The S&P/TSX Completion and S&P MidCap 400 are total return indices. The S&P/TSX Completion (formerly called the S&P/TSX MidCap) is a Canadian index that is comprised of the constituents of the S&P/TSX Composite Index that are not in the S&P/TSX 60. The S&P/TSX 60 is a Canadian index that is comprised of the largest companies within the S&P/TSX Composite index. Comparisons to certain indices and benchmarks are provided for illustrative purposes only and are intended to indicate broad market performance and characteristics. Comparisons to indices and benchmarks are limited in part because indices and benchmarks are not managed and do not charge fees or expenses. The Fund may underperform or outperform an index or benchmark for many reasons.
4. Holdings that constitute less than 0.25% of the Net Assets of TCEF are not included in the number of holdings. Similarly, holdings that constitute less than 0.1% of the Net Assets of TC SPEF, TCCF and TCUS are not included in the number of holdings.