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Memo to: Titan Clients (Confidential) **Date:** May 20, 2022 **Reading time:** 6 minutes

Adjusting the Sails

> *"Though we cannot control the wind, we can adjust our sails so as to profit by it"*

Let's hop right to it. The broader market and related assets have been getting clobbered. Here we aim to answer three of the most common questions we've been hearing from clients:

1. What has changed in the world ("the wind")
2. What are we doing about it ("the sails")
3. What could happen from here (the future)

❶ What has changed in the world?

Over the past decade, investors could get paid playing one note: buy fast-growing, unprofitable tech. Titan's strategies benefitted as well, with our Flagship strategy (consisting of many tech holdings) outperforming the S&P by over 25% in 2020. **But the winds have changed**.

Here's a simplified take: Supply-chain shortages and government COVID stimulus have contributed to rising inflation. In an effort to curb that inflation, the Fed is raising interest rates. Since higher rates can stunt business investment and innovation (weighing particularly hard on businesses with longer-dated cash flows), tech stocks have been hit especially hard and are making headlines.

❷ What have we done to change the sails?

A key lesson here is the importance of being nimble. The strategy of playing just one note no longer makes sense, in our opinion - you should be playing multiple notes - because a range of scenarios might unfold. We'd prefer to sacrifice some of the upside in one scenario in order to position well across all of them. Here are the six things we've already done to best position your wealth, in our view:

A) Reduced exposure to high growth, low profitability businesses. With rising interest rates, these stocks are being held to a higher standard, and we've been reducing our growth exposure for months. For example, we exited Twilio (TWLO) during Q1 with the view that its high sales growth at the expense of low margins wouldn't fare well in this market.

B) Added high-quality cash flow businesses. We expect free-cash-flow generative companies to be great stabilizers to our portfolios. A prime example of this is our position in S&P Global (SPGI) which we initiated in March. SPGI is a dominant player in the debt capital markets ecosystem, with durable competitive advantages and pricing power.

C) Added to investments that stand strong, even in a bear market. We've initiated positions in companies like Alcon (ALC), a predictable global player in the eyecare market. We believe these are the notes to play if the downturn scenario arises. (I.e., even in a downturn, you'll still order new contact lenses).

D) Under-the-radar opportunities. Believe it or not, we still think you should be opportunistic. A prime example you might have heard of is Hasbro (HAS). We see it as an under-the-radar gaming enterprise trading at a historically cheap valuation, with levers that we hope will bring annualized returns to well over 20%. Consider this Titan's version of discount shopping on the "sale rack" for you.

E) Saving some cash (dry powder) for future deals. We know future deals could surface on the market's sale rack, and are selectively deploying cash to our best ideas as those sales become available. Patience is key here.

F) Lastly, maintaining our hedges for rainy days. Weather could remain choppy, and the hedges we implemented in January have come in handy, contributing positively across all equity strategies YTD.

Welcome to adjusting the sails in 2022. All hands on deck. Being diversified and nimble is essential. This year has been rough - we won't sugar-coat it - but we're happy to see these moves soften the blow. Take our Flagship strategy for example - when comparing our current Flagship strategy versus if we had made no changes in 2022, we estimate that our active choices have added about 400bps to performance through April 2022. We think that our ability to be nimble, move away from growth and unprofitable tech, and diversify will continue to be the best path forward. Why? We can't predict the future, but we can be prepared for what can happen from here.

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3) What could happen from here?

Scenario 1 (Good): Equity markets end 2022 in the black. This could happen if inflation eases, the Fed takes a more dovish tone, supply chain issues subside, and geopolitical tensions ease (we'll take any of these). In this scenario, the market could be modestly up by year-end. Our high-growth tech holdings would come in handy here, while our high-quality non-tech compounders may also benefit, but to a lesser extent.

Scenario 2 (Meh): The economy is just "ok." Broader issues of inflation and rising rates still exist, but they are not as bad as what expectations had baked in. In this case, we expect markets to be flat-to-modestly down by year-end. Cash and cash-flowing assets may come in handy here.

Scenario 3 (Not so good): We are unable to control inflation and economic slowdown; real rates rise aggressively, and assets deflate. Markets are broadly down by year-end. Our hedges and cash holdings may come in handy here, while our cash-flowing assets may see mixed performance.

Yes, we just said markets will go up, down, or stay flat, but there's an important takeaway here: In any of the scenarios above, we understand principally how our investments would behave. This enables us to construct diversified strategies for you, and adjust our sails accordingly when needed. Our team continues to be laser focused on deploying capital into best-in-class assets, re-evaluating our positioning, and being nimble where we see fit.

We're all hands on deck for you here. Let us know if we can elaborate on the above at all.

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