Polen Perspectives

A Business Owner's Mindset: Investing Through a Pandemic

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Key Highlights

- All-season durable growth companies, in our experience, are led by management teams that remain focused on long-term value creation, even in times of economic and financial stress.
- Great management teams, in our view, can often uncover opportunities to invest in future growth and support all their stakeholders, recognizing that these actions can improve the long-term sustainability of their enterprise.
- We believe several companies across Polen Capital's portfolios have demonstrated this mentality of investing for the future throughout the COVID-19 pandemic. In this paper, we highlight some recent examples across our suite of strategies.
- Our 30+ years of seeking to invest in companies and management teams that think and act this way have shown us that these types of businesses often have the potential to generate growth during both prosperous and challenging economic periods.

"All-season durable growth companies, in our experience, are led by management teams that focus on long-term value creation—they operate with a business owner's mindset."

Mark Zuckerberg stated in a recent call to analysts, "Overall, I think during a period like this, there are a lot of new things that need to get built. And I think it's important that rather than slamming on the brakes now, as I think a lot of companies may, that it's important to keep on building and keep on investing in building for the new need that people have and especially to make up for some of the stuff that other companies would pull back on. I think that's, in some ways[...] an opportunity; in other ways, I think it's [a] responsibility to keep on investing in the economic recovery."

Our 30+ years of seeking to invest in companies and management teams that think and act this way have shown us that these types of businesses often have the potential to generate growth during both prosperous and challenging economic periods. At Polen Capital, we invest with a business owner's mindset, looking at a company's long-term growth opportunities over several years, not months.

Enduring Companies Consider All Stakeholders Even During Uncertain Times

True long-term value creation, in our view, is not just defined by a long-term strategic vision. We believe management teams who genuinely think and act like business owners also consider all stakeholders—customers, employees, local communities and equity owners—when deciding how to invest their companies' cash flows. Just as importantly, in our opinion, this mentality does not change, even during challenging market environments. We appreciate corporate managers who play the long game, particularly in times of economic and financial stress, when the path of least resistance is often to prioritize short-term agendas over long-term strategic plans. In fact, great management teams can often uncover opportunities to invest in future growth and support their stakeholders in uncertain times, recognizing that these actions can improve the long-term sustainability of their enterprise.

To that end, we illustrate what we believe it means to have a business owner's mentality in today's global economy by highlighting certain recent initiatives of the management teams of some of our portfolio companies.

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Short-Term Pain in Pursuit of Long-Term Value Creation

In our estimation, few businesses across our Large Company Growth strategies have been more directly affected by the COVID-19 pandemic than **Starbucks**, which we own in both the Focus and Global Growth strategies. During February and March, Starbucks was forced to close most of its owned locations in the U.S. and China, the company's two largest markets.

While many businesses might respond to such circumstances by retrenching—laying off employees, cutting back with suppliers, reducing investments—to preserve cash, Starbucks has done the opposite.

Management has retained employees in its company-owned locations and continued to pay them even while stores were temporarily shut. Frontline employees working during the crisis were also paid a premium. Beyond its employees, Starbucks also accelerated payments to key suppliers and is investing in its international licensees by offering more flexible financial terms. Management also recently decided to accelerate the development of more drive-thru and pick-up only locations in the U.S. to better serve customers who, going forward, may prefer an "on-the-go" transactional experience.

Finally, Starbucks announced a new partnership with Sequoia Capital China. The two companies will co-invest in innovative technologies that can be integrated into Starbuck's retail experience, a key consideration in China where consumers are among the most digitally savvy in the world. We believe these various initiatives will likely weigh on Starbucks' near-term results. Yet, when viewed over a long-term time horizon, we see these investments as potentially strengthening Starbucks' competitive position and ultimately benefiting all stakeholders of the business.

Also within our Focus and Global Growth strategies, **Facebook** continues to make significant investments in their core platform and future growth opportunities despite a deceleration in ad revenue growth. In April, the company finalized a $6 billion investment in India's Reliance Jio, the country's leading provider of mobile telecom services. Reliance Jio recently launched a new e-commerce platform called Jio Mart, which helps to connect consumers with smaller merchants. Facebook's investment includes a commercial partnership with Reliance that will let shoppers use Facebook's WhatsApp platform to transact with small businesses—as of last year, WhatsApp had over 400 million active users in India, more than in any other country. Facebook also launched its Facebook Shops platform, which allows small businesses to set up virtual storefronts, for free, on Facebook and Instagram. At a time when merchants need more options than ever to reach consumers, Facebook Shops now gives them access to its 2+ billion users and a potentially valuable alternative e-commerce platform for merchants to expand their businesses.

We believe medical products manufacturer Medtronic, a holding in our International Growth strategy, exemplifies having a long-term vision and corporate accountability. In an open-source initiative, the company made its ventilator designs publicly available to other manufacturers so that they could ramp up their own production and more rapidly increase overall ventilator supply, even though doing so may have resulted in potential ventilator sales going to competitors. Additionally, the company has supported its employees in several different ways. The company offered bonuses for essential workers required to report to Medtronic facilities and monetary assistance for some employees to cover extenuating costs like childcare. Employees whose roles could not be performed remotely but were nonetheless forced to stay at home for medical or family reasons were offered paid leave. Field personnel with compensation dependent on product sales were also provided financial support.

Small Companies that Exemplify Long-Term Thinking

Companies within our Small Company Growth strategies have also taken action to support their stakeholders. In the U.S. Small Company Growth strategy, **Texas Roadhouse**, a 600-restaurant casual dining chain, was heavily impacted by the COVID-19 pandemic. Still, thanks to a solid financial position, Texas Roadhouse was able to create a "stimulus package" for its frontline employees, providing $17 million in extra pay and benefits. The company and its founder also contributed millions to Andy's Outreach Fund, a program aimed at assisting company employees in times of need. Texas Roadhouse also expanded its menu to include value options to provide its customers, many of whom have been financially impacted by the crisis, with meals at attractive prices. Rather than hunker down, lay people off, conserve cash and wait it out, management chose to address the reality of each day, experiment and learn, and, most importantly, continue to serve its people, its customers, and the community.

Etsy, a newer holding in the U.S. Small Company Growth strategy, offers another shining example of corporate accountability. Etsy is an online marketplace that matches shoppers with small sellers and creators in the $100 billion+ global market for unique and creative goods. Etsy was an early beneficiary of increased online shopping during the pandemic. However, rather than trying to maximize profits in the short-term, Etsy waived fees for sellers as part of a seller relief program. Furthermore, the company encouraged sellers to make desperately needed masks by providing listing credits for mask sellers and donating thousands of face masks to hospitals.

Etsy's "call to action" resulted in 60,000 merchants selling masks on Etsy's platform, and, in April alone, the company sold 12 million masks.

These actions demonstrate to us that management recognizes the value of all stakeholders on the platform, and we believe that mindset will drive better long-term results.

In the International Small Company Growth strategy, we believe **Auto Trader** exemplifies long-term-oriented management behavior. Auto Trader is the U.K.'s largest online automotive marketplace, and COVID-19-related shutdowns have heavily impacted its business. Its business model and positive free cash flow generation have enabled the company to take significant measures to support its dealer customers. Auto Trader extended payment terms and made monthly advertising packages free while dealers were closed. It also provided a 25% discount in June when dealers partially re-opened. Auto Trader offers a critical service for dealers and benefits from stable monthly recurring subscription revenue. In other words, it could have done nothing.

Instead, Auto Trader chose to support its customers, becoming a more trusted and valued partner.

For a network-effect driven marketplace, we believe these actions will pay long-term dividends in terms of retaining customers that have an exceedingly high lifetime value.

Canada-based **Morneau Shepell**, also owned in our International Small Company Growth strategy, is in the business of wellbeing. Its response to the pandemic has been to focus on the welfare of its employees, its clients' employees, and the communities it serves. In April, Morneau Shepell launched WellCan, a website and mobile app that provides a broad range of resources to support mental health and wellbeing to all Canadians free of charge. The company also offered free access to its internet-based cognitive behavioral therapy program to residents in Manitoba and Ontario and opened its crisis hotline to provide emotional support for those affected by traumatic events. We believe these initiatives are not only the right thing to do but also may bolster the long-term strength of the company.

A Unique Approach within Emerging Markets

Within our newly launched Global Emerging Markets Growth strategy, South African apparel retailer **Mr. Price** provides a unique example of savvy and forward-thinking management. Like other retailers in the country, Mr. Price has been hit hard by the pandemic. South Africa has been in a strict lockdown for two months with all non-essential retail stores closed, and even e-commerce sales restricted. Even as the country begins to slowly re-open, immediate business prospects look challenging. Fortunately, Mr. Price entered the crisis with one of the most robust balance sheets in the industry and a net cash position. In normal market conditions, we might have expected Mr. Price to use its balance sheet to take advantage of the equity market drawdown and announce a share buy-back program.

Instead, the company committed to paying employees full salary and benefits during the lockdown period. Furthermore, while buying its own shares at distressed valuations may have been an attractive use of capital, all opportunities are relative. The company's management took the opposite approach and asked shareholders for approval to raise extra capital at low levels—today's distressed market conditions have offered M&A opportunities that have not been seen in years. We believe this strategy can be highly accretive to shareholders, even if financed by raising capital at depressed levels. Thus, a somewhat unorthodox decision by Mr. Price's management team could prove to be an astute use of capital and potentially strengthen the company's competitive advantage going forward.

"We admire management teams who recognize that success is determined not just by meeting the needs of equity owners, but rather, the needs of all stakeholders."

At times, this approach can come at the expense of short-term gains. Still, we believe management teams who emphasize long-term value creation across their corporate ecosystems and who can invest for the future even during times of uncertainty will build even stronger foundations to nurture and expand their companies' competitive positions, foster sustainable growth, and create long-term value for many years.

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Mr. Atkins joined Polen Capital in 2012. Prior to joining Polen Capital, Mr. Atkins spent 12 years as a portfolio manager at Northern Trust Investments, including eight years as a mutual fund co-manager. Before joining Northern Trust, Mr. Atkins spent two years as a portfolio manager at Carl Domino Associates, LP. Mr. Atkins received his B.S. in Business Administration from Georgetown University and a General Course degree from the London School of Economics. Mr. Atkins is a CFA® charterholder and a member of the CFA Institute and the CFA Society of South Florida.

Going Beyond with Polen Capital

For more than three decades, Polen Capital has been dedicated to serving institutional and individual investors by providing concentrated growth portfolios of the highest-quality companies. We adhere to a time-tested process of researching and analyzing sustainable growth—seeking the best companies to build high conviction portfolios. Then, we invest for the long term and with a business owner's mindset—giving these companies time to grow. This singular focus and consistent investment process transcend market capitalizations and borders. We incorporate this approach across three independent investment teams located in Boca Raton, Boston and London, covering large company, small company and emerging markets, currently managing over $35 billion in assets.

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We would be happy to partner with you to understand your needs and discuss the investment capabilities at Polen Capital.

For more information on Polen Capital visit **www.polencapital.com** and connect with us on **LinkedIn.**

Past performance is not indicative of future results. There can be no assurances that any portfolio characteristics depicted herein shall be replicated in the future.