DivGro

DivGro Pty Ltd
AFSL 238198 (CAR No. 1277044)
ABN 41 633 109 789
Level 10, Hudson House
131 Macquarie Street
Sydney NSW 2000
info@divgro.com.au

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Dear fellow investor

Dividend increases

Our DivGro dividend growth engine is working beautifully. Since we last wrote we continue to capture more meaningful dividend increases from our powerful system:

Lowe's Companies	+9.09%
American Tower	+20.00%[1]
Microsoft	+9.80%
Texas Instruments	+13.33%
Starbucks	+9.76%

Since opening the fund on 15 August 2019 our dividend growth prediction system has achieved 42 consecutive dividend increases at an average increase rate of 13.74%.[2]

Performance summary: 15 August 2019 to 30 September 2020

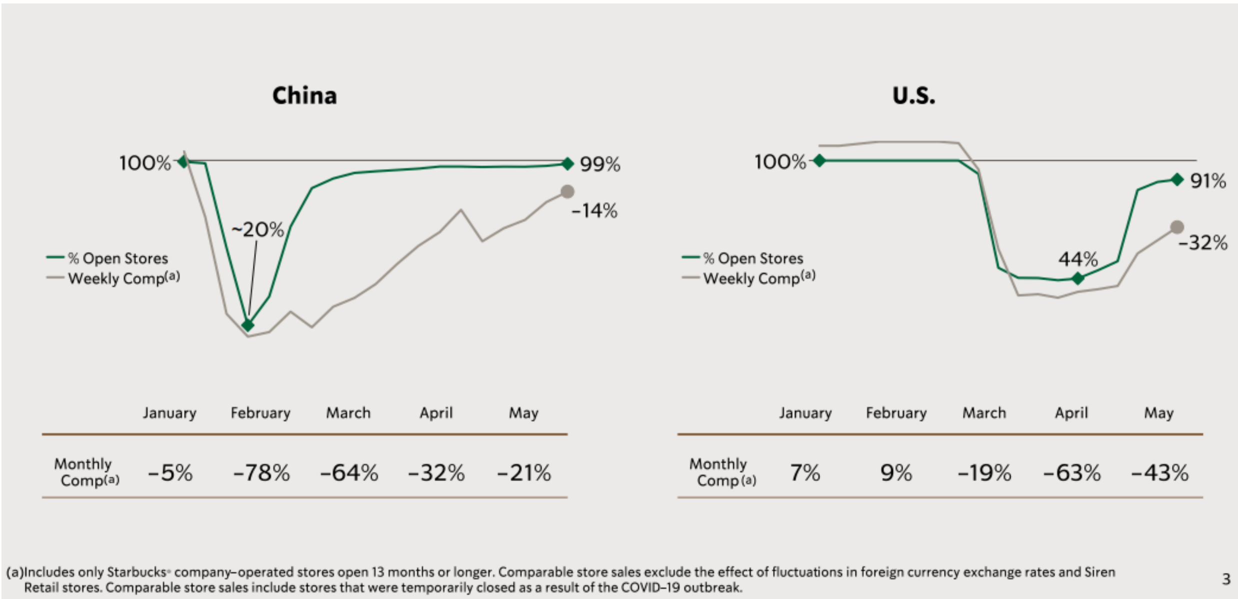
Dividend performance	
Consecutive dividend increases	42
Average increase	13.74%

Unit price performance (net of fees)[3]	
Performance, USD (annualized)	16.08%
Performance, AUD (annualized)	10.70%

[1] Annualized, American Tower raises quarterly.
[2] See dividend track record table attached at the end of this letter.
[3] Inclusive of distributions.

An insight into a dividend star

We are excited to share with you our thoughts regarding the most recent Starbucks (SBUX) dividend increase from $0.41 to $0.45 per quarter (+9.76%).[4] Since initiating its dividend in 2010 Starbucks has been a dividend star with dividend increases exceeding 20% per year annualized. While on the surface a dividend increase of 9.76% appears more pedestrian, this is in the context where the majority of Starbucks' outlets were closed for much of the last six months (see chart below)[5], leading to a loss of sales of approximately $3b in the last quarter alone.[6]



Rather, we believe this dividend increase evidences:

1. That Starbucks has the financial wherewithal to increase its dividend despite an incredibly challenging environment.
2. Starbucks cherishes its pact with investors in terms of maintaining its formidable dividend legacy.
3. Starbucks' "confidence in the strength of its recovery and the robustness of its long-term growth model".[7]

We believe the long-term prospects for Starbucks as the dominant player in specialty coffee have strengthened dramatically. In China – which is Starbucks' primary and most profitable growth engine – the slowdown caused by the COVID-19 shutdown essentially led to the precipitous downfall of Luckin Coffee, which for several years had threatened Starbucks' market dominance by undercutting pricing and expanding rapidly. While Luckin spent aggressively to grow the still nascent but fast-growing specialty coffee market in China, its dramatic demise will almost certainly disincentivize future aspirants from wanting

[4] Starbucks press release, 30 September 2020.
[5] Patrick Grismer - Starbucks CFO presentation at Stifel 2020 Cross Sector Insight Conference, 10 June 2020.
[6] Starbucks Q3 2020 earnings report.
[7] CEO Kevin Johnson comment, dividend announcement press release, 30 September 2020.

to compete with Starbucks on the basis of price, or perhaps even at all. This implies a clearer runway for Starbucks to continue its rapid and extremely profitable growth path in China relatively unencumbered by meaningful competition.

As an aside, Starbucks' China unit economics are remarkable in that the cash payback from a new store is shorter than 18 months, with residual ongoing same-store cash earnings of approximately 87% per year.[8] One would be hard-pressed to find a business with unit economics which even come close to that of Starbucks China.

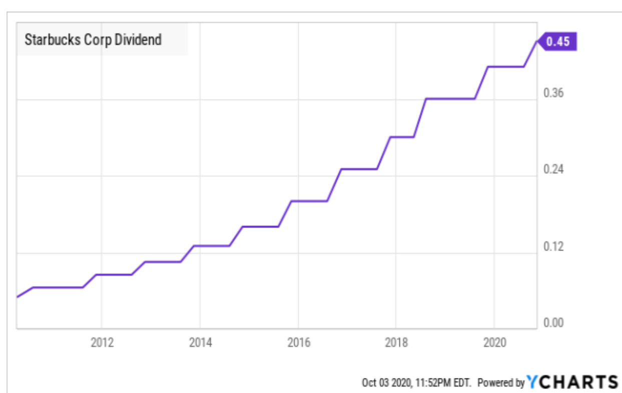
Prior to COVID-19, Starbucks' global growth rate was somewhat constrained by limitations of high-quality new site availability and competition for suitably excellent store-level personnel. Starbucks is renowned for its identification and training of employees – called 'partners' in the Starbucks system – and Starbucks has sent more people to university (at its own expense) than any other company worldwide. Since many weaker coffee outlets, both independents and small chains, have now permanently closed, Starbucks is spoilt for choice both for incremental new sites and suitable personnel.

Indeed, while not to diminish the impact of the shutdown on Starbucks' own recent sales - which are rapidly rebounding[9] - we believe the recent dividend increase underestimates the vastly improved relative competitive positioning and prospects for our core holding Starbucks.

A note on staying power

We have been familiar with the Starbucks story from the day it went public. It has always been a compelling story, a phenomenal business success, and an excellent outperformer. However, while before 2010 we suspect Starbucks may have been hard to hold, since initiating its dividend in 2010 we think that by focusing primarily on its dividend behavior, this should have become psychologically less challenging.

Contrast the two graphs below. The price graph on the left looks pretty much like any other wonderful but *difficult-to-hold* stock. However, **if instead one re-focuses on the dividend graph on the right, we think the ability to hold, and over time actually benefit from long-term value creation, becomes much more feasible.**



This dynamic is typical of stocks in the DivGro system. At its core our system shifts investors' focus from what is random and uncontrollable (price prediction), to something that is real, tangible, and according to our system predictable, and which over time powers commensurate percentage price performance.

As a result of this simple but elegant shift of investor attention, the DivGro system can be defined as a *'+5 system'*.

A *+5 system* is one which is worth an extra 5% per annum to investor returns because it increases the likelihood that an investor will actually benefit from any ultimate underlying positive performance where the path to this positive outcome is volatile, random or psychologically destabilizing. While some may overlook the utility of such a system, we believe it cannot be overstated. This is why Ben Graham – Wall Street's most illustrious teacher of investment wisdom – would begin his courses by stressing that *'to make money in Wall Street one must have the proper psychological attitude'*.[10]

Our objective for DivGro is to be the go-to home for above average returns that are easier to hold. **As the quintessential *+5 system*, our mission is to get our investors *to actually benefit* from the underlying return available from the wonderful companies in our portfolio, rather than being psychologically bluffed out as investors generally are elsewhere.** Our research shows that an important element of successfully shifting investor focus is via frequent, measurable, understandable, and positive feedback. Since, on average, we receive meaningful positive dividend information from one of our investee companies every few days, we will in future broadcast some of these value-adding insights much more frequently.

Concluding remarks

In late August we relocated our team to our new city office. While we have already met with several investors in our new setup, we look forward to catching up with the rest of our growing investor community in the near future. We are encouraged by the growing DivGro community, both in terms of investors and the fortnightly learning seminars that continue to be very well received.

As an administrative update, from 1 February 2021 we will adjust our fees to new investors. To be clear, this will not affect existing investors who have made at least an initial investment in the fund prior to this date, and who may continue to add to their investment under the current preferential fee structure indefinitely. If you have any family or friends interested in accessing these preferential terms, they may wish to invest in advance of this cut-off date.

We are pleased to report that the distribution for the quarter ended 30 September 2020 will be paid out next week. Once again, our research shows that the psychological benefit of receiving this cash feedback is

[10] Please refer to our June 2020 investor letter for more detail.

paramount to increasing the likelihood investors actually capture the long-term value creation inherent in the wonderful businesses that make up the DivGro portfolio.

Thanks again for your continued support.

Sincerely,
Jonathan & Barney

DivGro Fund dividend increases[11]

Increase Number	Declaration Date	Company Ticker	Dividend Increase %
1	14-Sep-19	AMT	20.25%
2	18-Sep-19	MSFT	10.87%
3	19-Sep-19	MCD*	7.76%
4	19-Sep-19	TXN	16.88%
5	22-Oct-19	V	20.00%
6	29-Oct-19	CTAS	24.39%
7	30-Oct-19	SBUX	13.89%
8	31-Oct-19	CDW	28.81%
9	01-Nov-19	ABBV	10.28%
10	07-Nov-19	AL	15.38%
11	14-Nov-19	NKE	11.36%
12	15-Nov-19	ROP	10.81%
13	25-Nov-19	BDX*	2.60%
14	03-Dec-19	MA	21.21%
15	04-Dec-19	SYK	10.58%
16	04-Dec-19	ECL	2.17%
17	11-Dec-19	ZTS	21.95%
18	12-Dec-19	AMT	20.24%
19	13-Dec-19	ABT	12.50%
20	20-Jan-20	MTY.TO*	12.12%
21	24-Jan-20	YUM	11.90%
22	29-Jan-20	MKTX	17.65%
23	29-Jan-20	SPGI	17.54%
24	29-Jan-20	SCHW*	5.88%
25	05-Feb-20	CME	13.33%
26	06-Feb-20	ICE	9.09%
27	10-Feb-20	QSR*	4.00%
28	20-Feb-20	DPZ*	20.00%
29	20-Feb-20	SBAC	25.68%
30	24-Feb-20	HD	10.29%
31	13-Mar-20	AMT	20.00%
32	01-Apr-20	WSO	10.94%
33	15-Apr-20	COST	7.69%
34	23-Apr-20	POOL	5.45%
35	19-May-20	AMT	19.57%
36	21-May-20	MDT	7.41%
37	28-Jul-20	MSCI	14.71%
38	21-Aug-20	LOW	9.09%
39	10-Sep-20	AMT	20.00%
40	15-Sep-20	MSFT	9.80%

[11] Asterisks represent companies no longer in the DivGro Fund portfolio.

41	17-Sep-20	TXN	13.33%
42	30-Sep-20	SBUX	9.76%
		Average	**13.74%**

Important disclaimer

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