



**DEAR FELLOW PARTNERS & FRIENDS,**

*“Long ago, Ben Graham taught me that price is what you pay, value is what you get. Whether we’re talking about socks or stocks, I like buying quality merchandise when it is marked down.” - Warren Buffett.*

Years like 2022 should be viewed as a gift for stock pickers, as the investment options available at attractive prices include more high-quality companies. In most economic environments, “value” investments tend to come with a lot of baggage. However, in weak economic environments, investors can be indiscriminate in their selling and high-quality companies may also trade for “value” prices. To put it another way, in some environments we are buying the best among mass-market vehicles, while in others we can buy Porsches at mass-market prices. This year was more like the latter, even if not as extreme as the Global Financial Crisis. We invested in over a dozen companies and sold about half a dozen holdings in 2022. Most of the new investments were in higher-quality franchises, while most of the holdings sold were on the cigar-butt side of the value spectrum. Consequently, the Centerstone Investors Fund (CENTX) and the Centerstone International Fund (CINTX) are currently more balanced between franchise and cigar-butt companies than during the previous few years.

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The big factors at play recently are top-down issues, but they also affect the bottom-up analysis. First, is the extreme policy behavior by both monetary and fiscal agents. Second, are the supply and demand shocks. Third, and perhaps most important for the future, are changing trade policies.

In a nutshell, the seeds of our recent bout with inflation were planted during the chaos of the economy-wide shutdowns

and the various shortages that ensued. The resulting fiscal and monetary extravagance created excess demand well before the labor market was ready to recover. Prices rose across the board. Analysis of 150 years of data by the Fed found that the effects of supply shocks, such as the one we had, have proven more temporary than those from demand shocks. Whether the current situation proves longer lasting depends on the labor market and, ultimately, wage inflation. The rapid reversal of monetary policy this year could cause an abrupt economic slowdown, which could nip any wage inflation spiral in the bud. The next question is, as always in economics, “and then what?” Maintaining tight monetary policies could cause a severe recession. Returning to easier monetary policies too quickly could risk a repeat of the stagflation experienced in the 1970s. It seems obvious, to me, that inflation hurts a lot more people than modestly higher unemployment. But you never know how the “authorities” will act. I take some comfort that 2023 is the third year of the Presidential cycle, meaning the authorities can probably tolerate higher unemployment, for a while, to bring inflation under control.

So how do we incorporate this into our process? Although I still find little overlap between the day-to-day work of business evaluation and macro considerations, it does inform our views on currency hedging and our gold exposure. Continued tight monetary policy in the US should lead to less pressure on foreign currencies and by extension gold. In the case of the Funds, the supplemental information is that, within equities, they are now exposed to an interesting basket of newly purchased franchise-like companies.

## High Quality Franchises in Structural Growth

The high-quality companies we invested in during 2022 include Logista<sup>1</sup>, Ryanair<sup>2</sup>, IAA<sup>3</sup>, Porsche<sup>4</sup>, Ross Stores<sup>5</sup>, Tencent<sup>6</sup> and Worldline<sup>7</sup>. The common element among these investments was a strong core business and an attractive valuation. An improving valuation was not always due to issues at the company. For example, Logista's share price declined sharply after the Ukraine War began, before investors realized it would not be affected by these events. Additionally, certain industries saw broad share price declines throughout the year, regardless of company-specific performance. In some situations, though, disappointing short-term results motivated investors to sell, creating an attractive opportunity for long-term investors. Ross Stores is a good example of this situation, which is discussed below.

Ross Stores is the second largest off-price retailer in the US. In retail, the best business model allows the retailer to offer the lowest prices. Off-price retailers buy excess merchandise from vendors and other retailers at a significant discount to market prices and then sell it at a 20-60% discount to full-price retailers. By definition, off-price retailers offer the lowest prices. Consistent growth in store traffic at both TJX and Ross Stores over the last three decades validates the model. Off-price retailers grow in good times and even faster in economic downturns as more people bargain shop. Ross is a franchise investment: strong business model, solid balance sheet and exceptional management team, both operationally and regarding capital allocation.

Ross' share price fell to an attractive level in May 2022, when we built our position. The issues Ross Stores was facing were affecting the entire retail landscape: higher

fuel prices, higher transportation costs, higher wages and a tough comparison with the last two years when stimulus checks were being distributed and consumers went on a shopping spree. Ross is better positioned to handle an inflationary environment than most retailers because of its low-price business model. As consumers see their wallets stretched, many will begin bargain shopping to maximize items purchased. This should lead to greater store traffic for Ross, allowing it to slowly offset rising costs. In the second half of 2022, Ross' results trended better than expectations as it maintained low prices to attract customers. This drove a sharp recovery in the share price from earlier this year.

Tencent is another example of a high-quality company we bought this past year. Several factors collectively turned investor sentiment toward Tencent, and most other Chinese companies, negative over the last two years. These factors include a changing regulatory landscape in China, a slowdown in China's economy and increasing geopolitical tension between China and the West. Tencent, through its super-app Weixin (WeChat outside of China) and its dominant position in video games, is one of the largest technology companies in both China and the world. Its operations and investments touch many aspects of China's digital/technology ecosystem (cloud, payments, news services, video, etc.). When we first invested, Tencent was trading for less than 12x normal operating income. Investors were valuing Tencent as just another mass-market vehicle. However, Tencent has an extremely strong competitive position in many categories of China's digital/technology ecosystem. While the near-term outlook is uncertain, the strength of the competitive position is not in doubt. As long-term investors, we took advantage of the bumpy roads to add another Porsche to our investment collection at a value price.

1 0.46% position in the Centerstone Investors Fund and 0.64% position in the Centerstone International Fund as of September 30, 2022

2 0.68% position in the Centerstone Investors Fund and 0.69% position in the Centerstone International Fund as of September 30, 2022

3 0.96% position in the Centerstone Investors Fund as of September 30, 2022

4 1.33% position in the Centerstone Investors Fund and 1.35% position in the Centerstone International Fund as of September 30, 2022

5 0.84% position in the Centerstone Investors Fund as of September 30, 2022

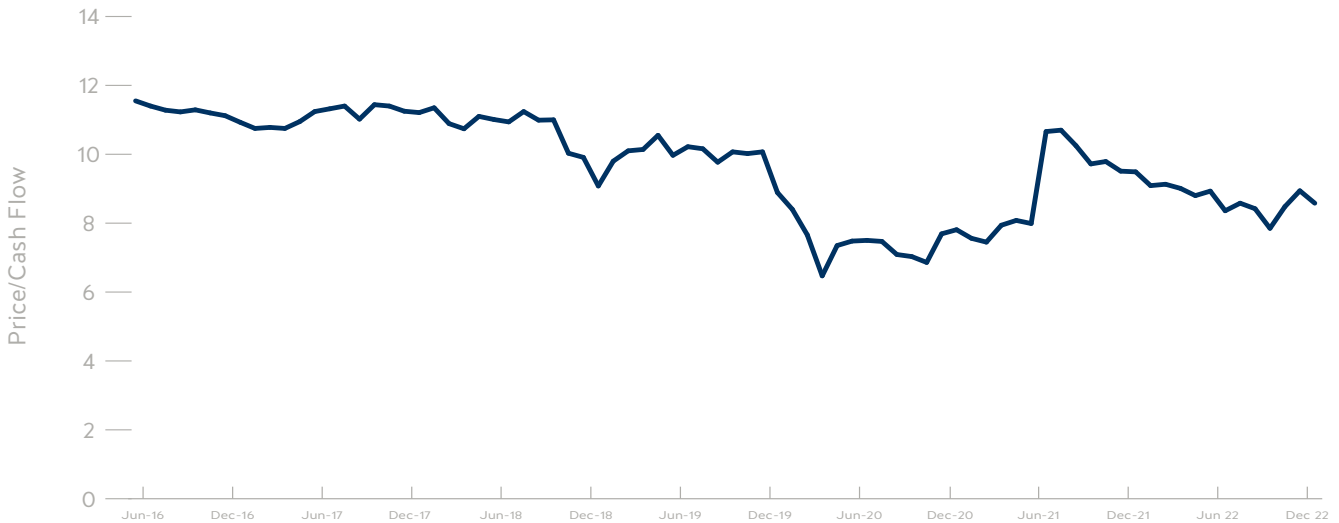
6 0.96% position in the Centerstone Investors Fund and 0.94% position in the Centerstone International Fund as of September 30, 2022

7 0.69% position in the Centerstone Investors Fund and 0.64% position in the Centerstone International Fund as of September 30, 2022



CONSISTENT VALUE STYLE THROUGH CYCLES

CENTERSTONE INVESTORS FUND



Source: FactSet

Price/Cash Flow: A stock valuation indicator or multiple that measures the value of a stock’s price relative to its operating cash flow per share. The ratio uses operating cash flow which adds back non-cash expenses such as depreciation and amortization to net income.

Portfolio Valuation & Holding Quality

From a valuation perspective, the Funds are approaching their “cheapest” levels since inception. The previous “cheapest” point was during the COVID-panic in early 2020. A key difference, however, is that the quality of the companies in the portfolio is significantly higher today. Subjectively, I believe the portfolio quality is near its highest point since the Funds’ inception. Therefore, the attractiveness of the Funds, considering valuation and investment quality, is probably at an all-time high. And as more stocks (or socks) go on sale in the coming months, we plan to keep adding Porsches to our collection.

Thank you for your continued support and trust. We wish you a happy and healthy New Year!

Sincerely,

Abhay Deshpande, CFA  
CHIEF INVESTMENT OFFICER

*“...the attractiveness of the Funds, considering valuation and investment quality, is probably at an all-time high.”*

**Important Risk Information and Disclosure:**

**Investors should carefully consider the investment objectives, risks, charges and expenses of the Centerstone Funds. This and other important information about the Funds are contained in the prospectus, which can be obtained by calling 877.314.9006. The prospectus should be read carefully before investing. For further information about the Centerstone Funds, please call 877.314.9006. The Centerstone Funds are distributed by Northern Lights Distributors, LLC, Member FINRA/SIPC. Centerstone Investors, LLC is not affiliated with Northern Lights Distributors, LLC.**

The commentary represents the opinion of Centerstone Investors as of December 2022 and is subject to change based on market and other conditions. These opinions are not intended to be a forecast of future events, a guarantee of future results or investment advice. Any statistics contained here have been obtained from sources believed to be reliable, but the accuracy of this information cannot be guaranteed. The views expressed herein may change at any time subsequent to the date of issue hereof. The information provided is not to be construed as a recommendation or an offer to buy or sell or the solicitation of an offer to buy or sell any fund or security.

An investment in the Funds entails risk including possible loss of principal. There can be no assurance that the Funds will achieve their investment objective.

Past performance is no guarantee of future results.

The value of the Funds portfolio holdings may fluctuate in response to events specific to the companies or markets in which the Funds invest, as well as economic, political, or social events in the United States or abroad. The impact of the coronavirus (COVID-19), and other epidemics and pandemics that may arise in the future, could affect the economies of many nations, individual companies and the market in general in ways that cannot necessarily be foreseen at the present time.

Value investing involves buying stocks that are out of favor and/or undervalued in comparison to their peers or their prospects for growth. Our value strategy may not meet its investment objective and you could lose money by investing in the Centerstone Funds. Value investing involves the risk that such securities may not reach their expected market value, causing the Funds to underperform other equity funds that use different investing styles.

Investments in foreign securities could subject the Funds to greater risks including currency fluctuation, economic conditions, and different governmental and accounting standards. Foreign common stocks and currency strategies will subject the Funds to currency trading risks that include market risk, credit risk and country risk. There can be no assurance that the Funds' hedging strategy will reduce risk or that hedging transactions will be either available or cost effective. The Funds use of derivative instruments involves risks different from, or possibly greater than, the risks associated with investing directly in securities and other traditional investments.

Domestic economic growth and market conditions, interest rate levels, and political events are among the factors affecting the securities markets in which the Funds invest.

Large-cap company risk is the risk that established companies may be unable to respond quickly to new competitive challenges such as changes in consumer tastes or innovative smaller competitors. Investments in lesser-known, small and medium capitalization companies may be more vulnerable than larger, more established organizations. Securities in small and mid-cap companies may be more volatile and less liquid than the securities of companies with larger market capitalizations.