

Management report

For the period from January 1 to June 30 2026, the S&P/TSX index posted a return of 11.10% (including dividends), the S&P 500 14.05% (in Canadian dollars and including dividends), while the MSCI World generated 13.48%. The Barrage Fund's return for the same period was -7.44% before fees and -7.97% after fees.

Market commentary

While headlines bombard us with Trump's numerous tariff changes, the US debt reached a new milestone on August 18th, surpassing \$40 trillion. While this doesn't seem to be causing significant alarm among investors, it remains a factor to consider in security selection. A bit of historical context should help us grasp the magnitude of the debt.

In 1835, Andrew Jackson, president of the United States from 1829 to 1837, had paid off the entire national debt. This was the only time in American history. In 1866, the Civil War caused it to surge to \$2.7 billion. Then came World War II, during which the debt reached \$258 billion.

In 1981, the first trillion dollars of debt was reached. It's important to remember that at the time, there was a recession. Then came the financial crisis in 2008, pushing the debt to 10 trillion dollars. It's worth noting that this was the last real recession, if we disregard the brief two-month recession caused by COVID-19. Despite the generally strong performance of the American economy, creating large, chronic deficits has become the norm. During the pandemic, the debt skyrocketed to 27 trillion dollars. Given all the spending incurred to support the economy when many businesses had to cease operations, the reason is understandable. But even though things are going relatively well, the debt continues its upward trajectory, surpassing 40 trillion dollars today, equivalent to 125% of GDP. What will happen in the next recession?

As investors, we are not trying to sound the alarm. Our confidence in our securities remains unwavering. However, we must pay close attention to any company that is overly dependent on the strength of the bond market. The financial sector is a prime example. Outside of financials, however, we assign a higher risk than before to companies that rely on refinancing their own debt to survive. Refinancing debt at 5% or 7% when the market is healthy is relatively easy. Doing so in the midst of a crisis can be fatal if interest rates suddenly rise to 10%, 15%, or even 20%. It is with this in mind that we seek to act cautiously in our stock selections.

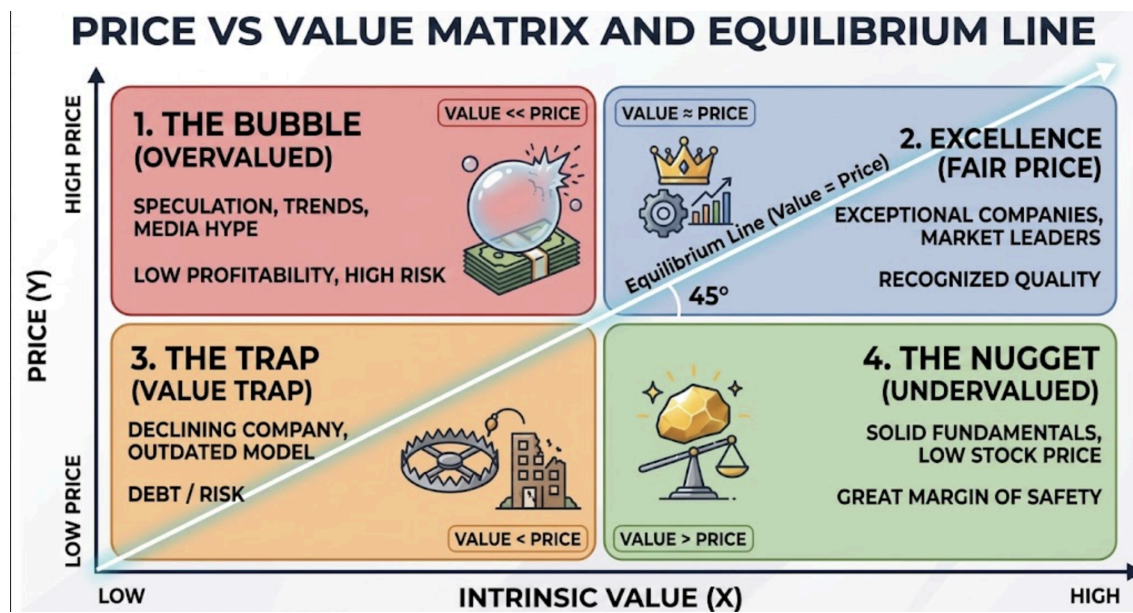
It's never too late to do the right thing

In our 2022 annual letter, we recounted a transaction involving Bill Ackman of the New York firm Pershing Square. At the beginning of that year, he acquired Netflix shares for \$375, justifying the purchase by highlighting the merits of this exceptional company at a time when investors were pessimistic. Indeed, at the time, the stock had lost considerable ground following a decline in subscribers, and Mr. Ackman saw this as a golden opportunity to buy shares at an attractive price. However, he sold them shortly afterward for \$225.

Note that with the subsequent 10-for-1 stock split, this equates to a price of \$22.50. His reaction seemed unusual to us, especially since he considered it a long-term investment at the time of purchase and was himself profiting from the negative market reaction.

He then bought more shares, at a price roughly three times higher than when he sold them. We're mentioning this because we believe it's a smart move. It highlights his ability to change his mind without being swayed by his past actions with the stock. This capacity for constant self-reflection is, in our opinion, crucial for success in the stock market. Some investors would likely let pride or past experiences influence their decisions. Why buy back a stock at nearly \$70 when you sold it at \$22.50 previously?

The business world is dynamic, and with the advent of artificial intelligence, this is even more true! It may have been a mistake to sell it at the time, but the company is constantly evolving, and the risk/return equation changes according to this evolution as well as the stock price. We could represent this risk/return or price/value equation using a line and four quadrants:

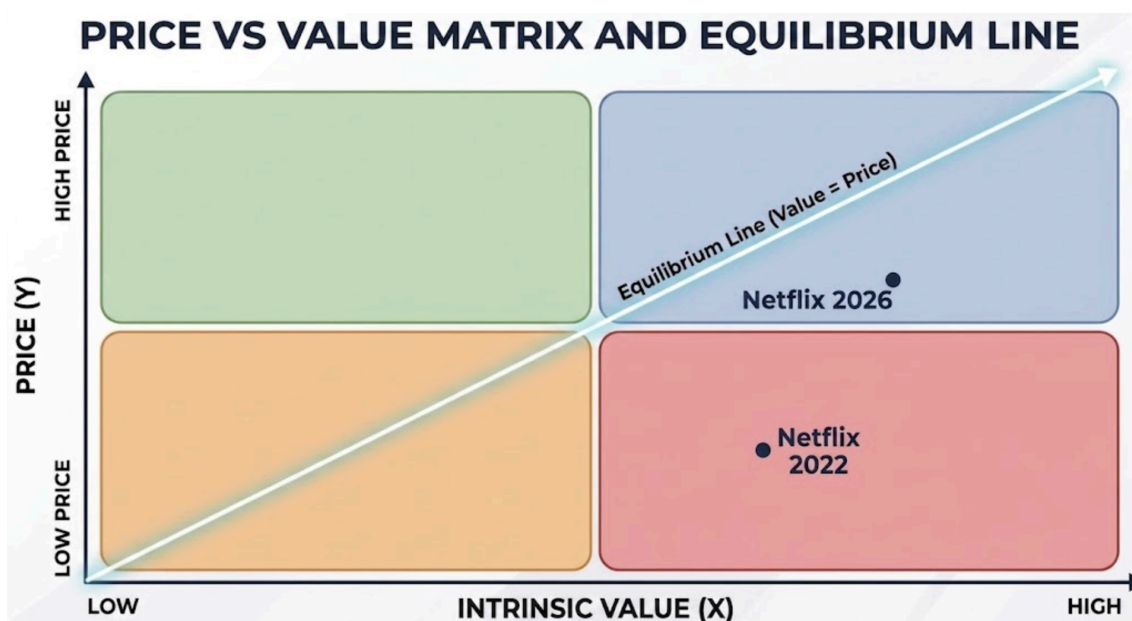


AI-generated image

The further to the right a stock's value is, the more attractive it is. This value is calculated based on profit and sales growth, as well as the strength of the business model. As for the price, the higher the stock's value, the greater the market demand. The equilibrium line divides the rectangle into overvalued and undervalued areas. So, ideally, we want a security that is as far to the right as possible (intrinsic value), but as low as possible (price).

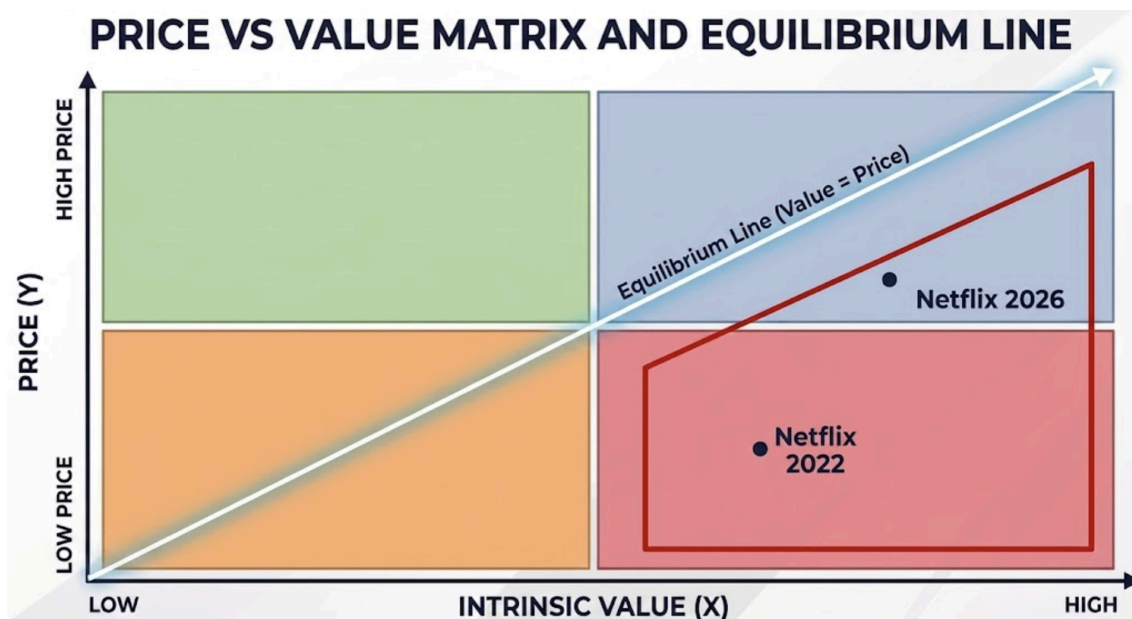
We invested in the stock twice in the last five years. After our 2022 purchases, we significantly reduced our position three years later, as the market price had appreciated faster than the intrinsic value. From a low of \$19 (adjusted for stock splits), the stock price nearly septupled to reach \$130. However, while the intrinsic value had indeed improved, it hadn't increased by a factor of 7. The stock was therefore becoming less attractive.

With the stock having corrected by 50%, we obviously bought back in, we can compare our 2026 and 2022 purchases as follows:



AI-generated image

At Netflix's 2022 low, developments at the company raised doubts about its future growth. The slowdown in subscribers was accompanied by a shift in its business model. The company had decided to embrace advertising, something its founder, Reed Hastings, had firmly stated he would never do. This uncertainty normally leads us to reduce the intrinsic value, although in many cases, it remains temporary. However, the stock had lost so much ground that it became even more attractive, which is why we added shares at the 2022 low. The lower the price falls, the greater the margin of safety. As seen in the chart below, our buy and hold zone is represented by a right-angled trapezoid:



AI-generated image

We tend to avoid venturing into the lower left quadrant. Too often, even by paying a very low price, we have to accept the risk of being significantly wrong about intrinsic value. In times of recession, however, these situations become much more apparent, since economic difficulties often highlight the strengths and weaknesses of companies. This is why we might be interested in acquiring shares of a bank, to name just one example, during a recession. As Warren Buffett so aptly put it, "Only when the tide goes out do you discover who's been swimming naked." Recessions separate the good loans from the bad. At the same time,

even the most solid banks see their share prices battered in the stock market when pessimism reaches its peak, creating golden opportunities. We have taken the example of a bank here, because the sector has characteristics and risks that will rarely arouse our interest in holding them in the long term (leverage, regulation, and homogeneity of loans which make it a commodity).

Returning to Netflix, Bill Ackman justified his purchase by declaring a victory for the company in the streaming wars. "Netflix is the dominant global streaming platform with over 325 million subscribers, nearly double the combined base of its two closest competitors, Disney+ and HBO Max....Netflix's ability to amortize content investment across the largest user base in the industry remains a highly valuable competitive advantage....with cash content growing at a 2% annual rate since 2021 and EBIT margins expanding from around 21% to over 31.5%," he stated.

While he seemed worried about the new advertising model at the time, he is now delighted with it. This new revenue stream now brings in nearly \$3 billion and is proving very promising.

Results of our companies

Alphabet and Meta

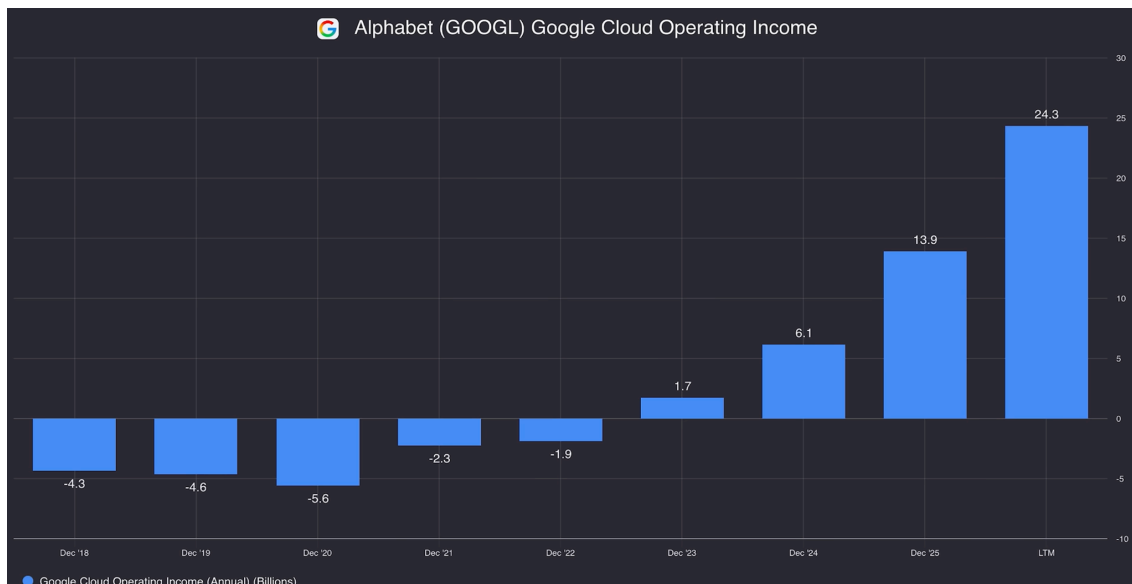
"I think it will feel like the next six months is like maybe equivalent to the last two years of model progress, something like that." – Sam Altman, CEO of OpenAI

We have held these securities for nearly a decade, at various weightings depending on the valuation. In the early days, our investment thesis differed significantly from our current one. Back then, we focused on the online migration of advertising, whereas the thesis now rests on artificial intelligence. If even the slightest of Mr. Altman's observation proves true, we will witness numerous developments very soon.

In the shorter term, Alphabet and Meta continued to show strong revenue growth in the second quarter, with increases of 24% and 28% respectively. Despite this, their stock market performance was mixed. As expected, the substantial budgets required for artificial intelligence development have increased again, further fueling investor anxiety.

In response to this reaction, Mark Zuckerberg insisted that AI "is already accelerating our core activities today." He specifically argued that AI-powered Advantage+ advertising tools have surpassed \$75 billion in annualized revenue.

At Alphabet, its cloud computing division, Google Cloud, exceeded our expectations with an 82% increase in sales. The chart below illustrates the impressive rise in profitability for this segment:



Such results lead us to be optimistic about future growth. Alphabet has begun deploying its 8th generation chips. These serve as a very powerful internal alternative to Nvidia's graphics processing units (GPUs). They have been optimized for production deployment, real-time query processing, and the "era of AI agents." They therefore bring significant benefits to the Google Cloud offering.

Returning to Meta, the company is currently facing several legal challenges. Most recently, a New Mexico judge ordered Meta to pay \$567 million for harm to the safety and mental health of young people. Meta obviously intends to appeal. In California, a jury found the company liable for damages to the mental health of a young woman who developed an addiction to the platform as a child. Consequently, the plaintiff was awarded \$6 million in damages. While the amount may seem modest for Meta, this trial sets a legal precedent, paving the way for thousands of other similar lawsuits. It's worth noting that this lawsuit also involved YouTube (Alphabet).

All this bad news has weighed on the share price, leading to a modest valuation of 17 times forward earnings. This is obviously not the first time we have seen legal challenges involving Meta since we first acquired our shares, and the company has only just settled one such case. We believe that the long-term impact on the company's intrinsic value remains mixed.

Amazon

Amazon's sales grew by 20% in the last quarter, and those of AWS (Amazon Web Services) by 36.7%. Their chip sales and artificial intelligence segment are both growing by triple-digit percentages, according to management, and each reached \$25 billion in revenue. Unlike Meta and Alphabet, the disclosure of their ambitious \$220 billion spending plan did not cause the stock to fall; instead, it climbed 15% the following day, reaching a valuation of \$3 trillion for the first time.

Currently, Amazon is our largest holding, and we remain optimistic about its prospects. The planned capital expenditures will primarily be used for AI infrastructure and data centers. It's worth noting that despite investor enthusiasm for anything related to artificial intelligence, our holdings haven't experienced the frenzy seen in some other stocks. A striking example that comes to mind is Smartbird (symbol: BIRD), which announced on April 15th that it was taking a completely new direction, shifting from shoes to data centers. That day, the stock price surged by nearly 600% at the close of trading, and even by almost 1000% if we consider the highest price reached during the trading session.



This is why many investors fear a speculative bubble linked to AI. Conversely, it seems that so far, our stocks are being punished when management announces significant investments in this promising future. We are very far from a bubble among large tech companies. On the contrary, we see them more as value stocks!

Teekay Tankers

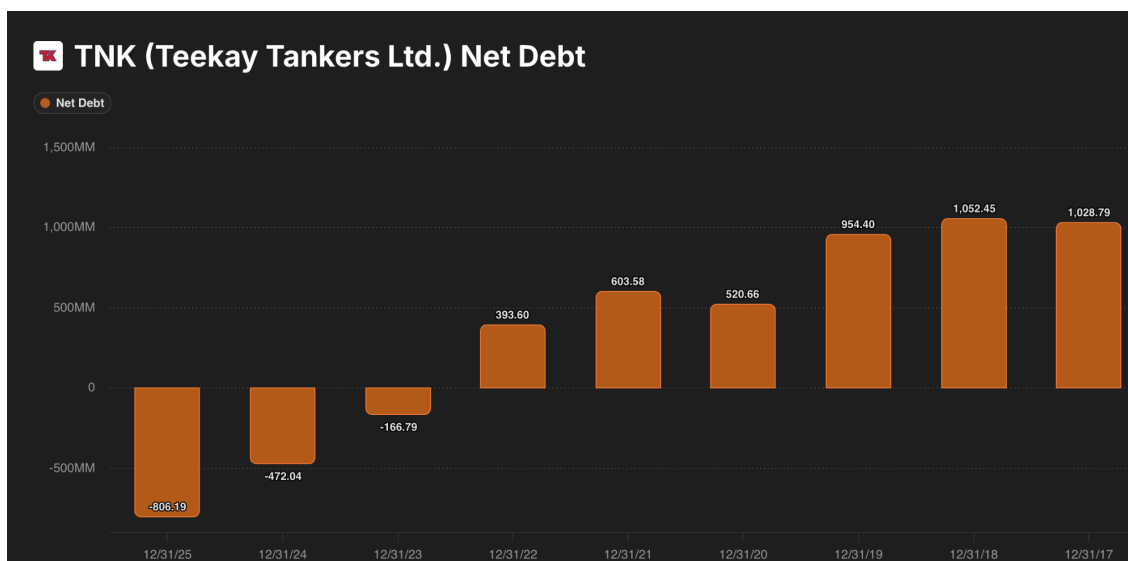
We decided to end this letter by discussing one of our oversights, regarding a stock we didn't buy in the past. During COVID-19, Teekay was trading between \$10 and \$12 when we first noticed it.



We weren't experts in the shipping industry, and we were cautious about such a cyclical sector. Nevertheless, the stock met many of our criteria. At the time, before the pandemic, management observed that whenever the daily charter rate (the amount customers pay per day for a given vessel) reaches a peak, shipping company executives order more ships en masse to expand further. Two or three years later, the market becomes flooded with new vessels, causing prices (the charter rate) to plummet. Faced with market overcapacity, executives then react by cutting their generous dividends and suddenly focusing on debt (which they had used to quickly purchase numerous ships).

When the market improves, the cycle begins again. Therefore, the only way to survive in difficult times is to have the lowest possible daily cost.

Recognizing the unsustainability of this model, management undertook a significant shift between 2017 and 2019. They decided to consistently prioritize the health of the balance sheet: they cut the dividend and sold off their oldest ships, in order to use the money to repay their debt. The graph below shows the debt minus cash:



source: TIKR

Management wanted to ensure they could easily weather downturns in order to fully capitalize on upturns. By maintaining this discipline over time, the company was building a structural margin of safety. At the time we were looking at the stock, the company was still undergoing its transformation, but the sector had become challenging, creating a golden opportunity for the stock price. Management was clearly explaining that they saw several reasons to expect a thriving market in the years to come:

- 1) Order books were at a historic low. When the market is down, fewer ships are ordered.
- 2) The global fleet was aging (in their category of ships), approaching 15 to 20 years old. Management anticipated a massive wave of decommissioning due to their age.
- 3) The shipyards were already saturated with orders in other categories of carriers, which would prevent the rapid return of new ships to compete with them.
- 4) The new environmental rules would force older ships to reduce their speed or be scrapped, further reducing market capacity.

All these factors would eventually support a high charter price. We really liked their plan to strengthen the balance sheet, even when everything was going well. Five years ago, the debt had already decreased, and the company had been working to reduce its costs for some time. We hesitated to buy the stock at \$10, but we also turned a blind eye later on as management pursued its plan with an iron fist, even when profits climbed significantly. Even though the stock had appreciated, we had several opportunities to buy it at a good price. Such discipline from management is rare, and it proved to be a mistake to simply watch the ship sail by! In 2022, the stock performed very well, unlike the rest of our portfolio, which at the time experienced its worst performance since Barrage Capital's inception.

Sincerely,



Patrick Thénier



Rémy Morel



Mathieu Beaudry



Maxime Lauzière

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