

A No-Load Mutual Fund Managed by:  
Front Street Capital Management, Inc.



Perhaps the most important holding in the Tarkio Fund since inception is Cognex Corporation (CGNX). Enclosed is a letter on Cognex we wrote in 2016. The unique Cognex culture is alive and well for Cognoids (the internal term used for Cognex employees) around the globe. Since that letter, CEO Dr. Bob Shillman retired and passed the baton to Rob Willett. Rob joined the company in 2008 and has been taking on more of the day-to-day leadership responsibilities ever since. Rob is fully committed to the theatrical Cognex culture, and he recently promoted Sheila De Palma – the company’s head of recruiting, training, and retaining employees – to the executive leadership team. As the company’s “Chief Cultural Officer,” she takes over Dr. Bob’s most cherished role. Over the years we have had the privilege of getting to know Sheila, who shares Dr. Bob’s passion for Cognoids and culture. Of the many management transitions we have witnessed during the past four decades, we believe this transition from Dr. Bob to Rob and Sheila has perhaps been the smoothest.

Cognex continues to be the technology leader in machine vision software. The world’s leading companies rely on Cognex to solve their most challenging machine vision problems in logistics, consumer electronic manufacturing, and automotive manufacturing. Logistics (e.g., moving and keeping track of items for e-commerce) has provided the fastest growth. Starting as a fraction of Cognex’s revenue, it now represents over half in just a few years. Consumer electronics has been the second fastest growing business, as the company’s largest customer (the leader in smart phones) has used Cognex to ramp up manufacturing during a decade of explosive growth. Automotive has also been growing nicely, starting from a modest base a few years ago.

Recently, Cognex’s revenue growth has leveled off as its top two customers have paused expansion during the past several years in order for demand to catch up. As a result, Cognex’s stock price has stagnated during the past two years and, given its large position in the Fund, has been a detractor from the Fund’s performance during that time.

Cognex’s success over the decades has been driven by a culture of engagement that has inspired its engineers to continuously address difficult customer applications. This culture of innovation has consistently enabled the company to enjoy 20% after-tax profit margins over time, the largest of any company we have ever owned in the Fund (the 5-year average for the S&P 500 in 2023 was 11.4%). The extra cash allows Cognex to enjoy one of the largest research and development budgets in its industry. Although Cognex revenues from quarter to quarter are lumpy, the company is committed to spending on innovation regardless of economic conditions. Cognex has been debt free since its IPO in 1989 and has always kept a very large cash position to support this emphasis on R&D.

Until now, Cognex’s revenues have been highly concentrated, coming from a small group of very large companies with complex problems. We believe that is about to change with the roll-out of the next generation of Cognex products. These products bring the power of Cognex technology from only a limited number of sophisticated customers to all manufacturers of all sizes. Cognex claims these products will expand their addressable customer base by over 30X, an estimate we think might be conservative. These products are rolling out as we write this. The company has focused resources on hiring teams of “Sales-noids” to introduce Cognex to this new customer base at an unprecedented pace (again, thanks to its strong cash position). We believe the machine vision/robotics industry is now moving from niche solutions to broad applications aided by artificial intelligence. Cognex is uniquely positioned to lead this trend.

And Cognex's largest logistics customer and largest consumer electronics customer – two of the world's leading technology companies – will both need to expand their capacity once again at some point. We know Cognex is working closely with these industry leaders to develop solutions for their next generation of challenges.

Cognex has been a high teens/low twenty percent compounder since Front Street Capital began accumulating it in 1989. We acknowledge its stock has been a detractor from our performance for the past couple of years but remain optimistic about Cognex's ability to grow well into the future.

As always, please call us at (406)541-0130 if you have any questions.

We thank you for your continued support and confidence.

Handwritten signatures of five individuals: Russ, Michele, Ginger, Jeremy, and Dominic.

Russ, Michele, Ginger, Jeremy, and Dominic

On March 31, 2024, CGNX was 8.22% of the Tarkio Fund Portfolio at a share price of \$42.42 a share.

The mention of any investments in this commentary should not be considered a recommendation to sell or purchase the security(ies) mentioned or similar investments. Please consult an investment professional on how the purchase or sale of such investments can be implemented to meet your particular investment objective or goals. Investments in securities and/or similar investments are subject to risks. It is important to obtain information about and understand these risks prior to investing.

Mutual fund investing involves risk. Such risks associated with the Tarkio Fund (including but not limited to Small/Medium Capitalization Risks, Foreign Securities Risk, Fixed Income Securities Risk, Non-Diversification Risk, and New Fund/Adviser Risk) as well as applicable investment objectives, charges and expenses must be considered carefully before investing.

***An investor should consider the investment objectives, risks, charges and expenses carefully before investing. A prospectus containing this and other information may be obtained by visiting [www.tarkiofund.com](http://www.tarkiofund.com) or by contacting 866-738-3629. We encourage you to read the prospectus before investing.***

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This quarter ending September 30, 2016, we are highlighting another of our important holdings: Cognex Corporation (CGNX). Cognex is the worldwide leader in the development and manufacturing of machine vision systems. Put simply, machine vision enables computers to see.

Our relationship with Cognex dates back to 1989. At that time machine vision was an industry with obvious great promise, but still in its infancy. Like many emerging industries with great promise, there was an over-abundance of venture capital available to fund the hundreds of startups that claimed to have the “right stuff” to address and eventually dominate this exciting industry. Cognex was just one company in a crowded field.

The potential for machine vision was endless, including manufacturing inspection, robotics, pattern recognition (including face recognition), sorting, and (not envisioned then, but now we know) even driverless vehicles. However, the only economically viable products at the time were machines that manufactured semiconductor chips. Other than semiconductor manufacturing all of the other potential uses for the technology could still be performed by humans. As a result, it would take another fifteen to twenty years for these non-semi applications to become profitable businesses.

Cognex was started by a professor at MIT, Dr. Bob Shillman (aka Dr. Bob) and two of his prize students: Bill Silver and Marilyn Matz. Dr. Bob might be one of the most unique CEO’s in the history of capitalism. He has a love of theatrical humor that equals his passion for machine vision engineering. In fact, Dr. Bob could be much more easily identified with Mel Brooks rather than Jack Welch. As a result, Cognex’s culture is, at its core, based upon theatrics and humor.

As a reminder, our criteria for selecting companies for long term investment is based upon the company developing a culture that brings out the best in the human spirit by utilizing the following management principles:

- Integrity - Trust
- Long-Term Focus
- Purpose & Passion
- Teamwork – Cooperation Not Competition
- Employee Empowerment – Drive Fear Out of Organization
- Disciplined Capital Allocation

While we believe Cognex adheres to all of our criteria, the area in which we believe it really excels is in building teamwork by breaking down employee barriers, in this case with theatrics. Check out the annual reports on their investor relations web page for examples. Every year the annual report is a parody of an existing publication. Past reports have been spoofs of the National Enquirer, Machine Vision for Dummies, and Mad Magazine (with a caricature of Dr. Bob on the cover à la Alfred E. Newman). The most important day of the year at Cognex is (you guessed it) Halloween. All employees are required to dress up. In addition, they celebrate all company milestones in elaborate ways, recognize important employee tenure anniversary dates with paid vacations to exotic locations, reserve a movie theater for an all-employee movie of the month outing, and the list goes on. This is probably not what W. Edwards Deming had in mind when he proposed driving out internal competition by breaking down barriers and creating common goals in organizations,

but we have witnessed Dr. Bob's crazy culture do just that. As a result of all this we are thrilled to be associated with such a dynamic and creative organization.

Cognex employees (Cognoids) enjoy a good amount of fun mixed in with hard work, but I can assure you the last twenty years has not been much fun for Cognex's competitors. Out of the hundreds of companies vying for a position in the machine vision market Cognex has emerged as a leading player in the group that we believe boasts margins well above the industry average.

Now Cognex's past is all well and good but let's take a peek at how the company is positioned for the future. As mentioned above, there were limited viable markets for machine vision technology for some time other than semiconductor equipment companies. As a result, Cognex dominated this space, and during the early days this application represented over ninety percent of its revenues. But the company saw its future in the much larger market for industrial applications, including inspection, robotic manufacturing and warehouse logistics. Over the past twenty years these applications have grown on average at over twenty percent per year. That growth has been masked by the fact that the semiconductor business has been commoditized during the same period and, as a result, the company has backed away from low margin contracts. The result of this dynamic transition is that the semi business has been shrinking steadily and now only represents five percent of revenue.

The bottom line to this tale is that although the company has grown during the last twenty years, this growth was accomplished in spite of the fact that a sector that once represented over ninety percent of Cognex's business has actually shrunk to a mere five percent today. As we move forward, the company should be unencumbered by the incredibly shrinking semi business and the growth of the much larger industrial market can now show its full potential. In addition, we believe the uses for computers that can see will only keep expanding for as far as the eye can see into the future and we are confident for as long as its culture keeps breeding new Cognoids, Cognex will be the one to capitalize on it. As the ultimate long-term investors, we believe our equity portfolios and what Dr. Bob has created at the Cognex Corporation is another match made in heaven.

Warm regards,

A handwritten signature in blue ink that reads "Russ Piazza". The signature is fluid and cursive, with the first name "Russ" and last name "Piazza" clearly legible.

On May 31, 2016, the Tarkio Fund Portfolio held shares of Cognex Corporation (CGNX) which represented 8.26% of the portfolio. The mention of any investments in this commentary should not be considered a recommendation to sell or purchase the security(ies) mentioned or similar investments. Please consult an investment professional on how the purchase or sale of such investments can be implemented to meet your particular investment objective or goals. Investments in securities and/or similar investments are subject to risks. It is important to obtain information about and understand these risks prior to investing.

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