Adestella
Investment Management

June 10, 2021

Dear Fellow Investors,

Adestella gained 19.6% in the first few months of the new year. Long positions returned 19.8%, while short positions and currency fluctuations were a net drag of 20 basis points. Both domestic and international holdings fared well, finishing at about a 55-45% split in profit contribution. The Fund's net exposure was consistent, staying within the range of 92% to 100%; gross exposure (with short positions weighted heavily toward index ETFs) was around 140%.

Equity markets were broadly higher over the period, driven by optimism over vaccine rollouts and broader economic reopenings, along with a steady dose of accommodative policymaking (or promises thereof). In the end, it was our fourth straight quarter, and fifth of the last six, in which we outperformed the indices. That said, we caution that there is a significant amount of random variance over three-month periods; such streaks are unusual and should not be expected as a baseline going forward.

An updated performance table is provided at the end of this letter.

Dot Plots

Adding value through fundamental active management basically comes down to how well one can connect the dots. This entails finding and synthesizing information from a wide range of sources and then being able to put them together to create the insight necessary to make an investment judgment. Information on stocks is easier to find than ever before, so there are more potential dots than ever as well. But this creates as many pitfalls as opportunities; it is often better to not connect any dots instead of connecting the wrong ones. So how can investors give themselves the best chance of drawing the right picture from the data at hand?

In my view, the ability to draw from a range of disciplines (defined both in terms of investing and beyond) presents a significant benefit to generalists, one not (or less) available to others who focus on a narrow niche or specific industry. Investors work with incomplete information, thus limiting the degree of precision attainable. This makes the stock market what psychologist Robin Hogarth would call a wicked learning environment, where outcomes are non-linear and information feedback is poor, misleading, or missing. Because of this, it is very difficult to use simple rules of thumb, and any assumptions must be defined narrowly and re-checked frequently.

Perhaps because of this wicked environment, the most useful connections are often those that are not immediately apparent and/or require cross-disciplinary knowledge. Such scenarios heighten the odds that your view is a variant one, an important prerequisite for generating outsized returns. One of our most successful investments in recent years, Sea Ltd (SE), was a good example of this – and a particularly apt one, considering its company motto is literally "connecting the dots." Analyzing SE required knowledge ranging from online gaming to eCommerce to FinTech. A gaming analyst covering Activision Blizzard, EA, and Take

Two might have missed the immense growth potential of Shopee, while an eCommerce specialist might not have appreciated the strategic value of also owning a prodigious cash generator like Garena. And of those who did have the requisite industry knowledge, many may have been too focused on home ground to consider a company headquartered in Singapore and doing most of its business in Southeast Asia. Connecting the dots between industries, geographies, and business models requires a range of disciplines, but those who were able to do it in the months following its IPO have been well-rewarded in recent years.

For an investor that only has an inch of knowledge, however many miles deep it may be, there are limited opportunities to make such comparisons and successfully span the gap between details that would otherwise seem unrelated. Meanwhile, a generalist accepts that he may not be able to reach the same level of nuance as a specialist, but he is willing trade it off for the benefits of breadth. His goal is to understand the fundamental underpinnings of the business and industry, knowing that there are usually just a few key factors that ultimately determine whether an investment will be a success or failure. For us, this is the superior approach.

Please, Sir, I Want Some More: On the Merits of Orphan Stocks

In his book *You Can Be a Stock Market Genius*, Joel Greenblatt gives an excellent overview of special investment situations that are often ripe with inefficiencies. While his guide includes a broad range of topics from corporate actions to financial distress, they are connected in the sense that they tend to be off the beaten investment path and thus far off the radar of most investors. Though not included in that book, another type of situation that fits this mold (and that has happened to be a recurring theme in our portfolio lately) is what could be called orphan stocks – companies whose stocks trade in one geography but conduct most of their business in another, and are sometimes even based/headquartered in a third. Such companies often have a smaller natural shareholder base, either from differences in awareness or sentiment between investors in different regions, or from logistical difficulties in purchasing shares for their accounts.

One of our biggest winners last year, Gan plc, was an obvious example of this phenomenon. The great majority of the company's future value creation prospects were based in the United States, yet the firm was based and traded on a small London exchange that many mainstream American brokerages don't support trading access on. Accordingly, many British investors may not have been keyed in to the company's excellent prospects across the pond, while most American investors were either unaware the company existed or unable to purchase shares for their account.

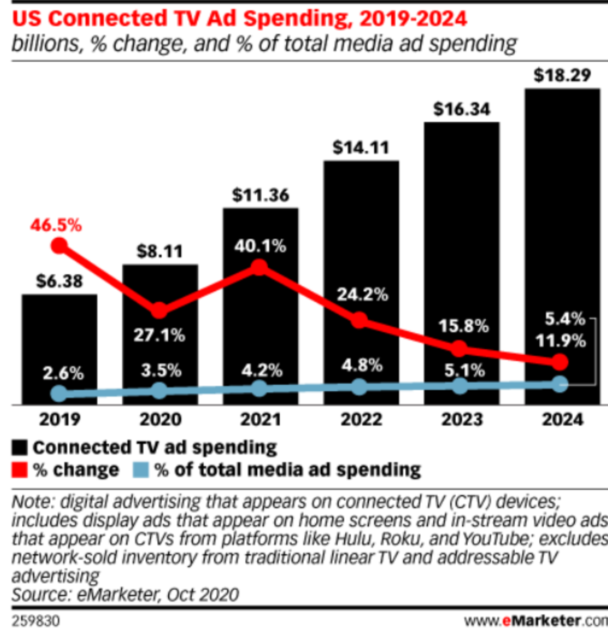
Anyone who was able to, however, was greatly rewarded – when Gan moved its listing to the United States last May, the gap closed and the stock promptly tripled from the high end of its IPO range. This was not a one-off occurrence either; in fact, the two stocks that have probably generated the biggest percentage gains in Adestella's history, Xpel (a US-headquartered company that traded on a small Canadian exchange during our initial purchases) and the aforementioned Sea Ltd, both possessed similar dynamics. While information efficiencies are generally few and far between in today's markets, the combination of an under the radar stock with relatively fewer people willing or able to look at it does occasionally create such situations.

Much like spinoffs became a key part of every value investor's arsenal in the years after *You Can Be a Stock Market Genius* was released, I expect orphan stocks will eventually become a well-scoured hunting ground. But it the meantime, we will continue to pursue these opportunities when they appear, and the well hasn't dried up yet. In my last letter, I mentioned that the Fund had taken new positions in two international stocks. As it happens, both display the same orphan tendencies as our previous winners. An overview of the two companies, Tremor International and Voyager Digital, is provided in the following section.

Discussion on Selection Positions

Tremor International (LON:TRMR): Tremor is an advertising technology company operating solely in the fastest growing medium (video), with a particular focus on the connected TV (CTV) space. Tremor offers both a demand-side platform (DSP) that advertisers use to buy inventory from publishers and a supply-side platform (SSP) that publishers use to find buyers for its available ad impressions, joining them in an automated marketplace that matches bids to publishers. TRMR is a classic orphan story, with an Israeli headquarters and a London exchange listing despite generating nearly 90% of its net revenue in the United States.

While cord-cutting and over-the-top (OTT) adoption has now been a trend for quite some time, advertising breadth has remained limited – only 40% of advertisers reported spending on CTV/OTT advertising, far behind percentages reported for social media and traditional video. Thus, this industry niche has the dual tailwind of a growing CTV base as cable subscribers continue to make the switch combined with CTV taking share of total media ad spend. Putting them together, TRMR's market should expand at a double-digit clip per year for the foreseeable future (see chart below):



Recent results suggest the company is capitalizing on this fully. A few weeks ago, Tremor reported nearly 100% revenue growth in what has historically been a quieter period for it. The particularly strong growth of the company's self-serve ad platform, which carries higher margins, led to significant FCF generation and margin expansion. Yet despite the positive industry tailwinds, clear operating momentum, and strong track record of performance, TRMR's stock trades at around 4x our estimate of sales and 10x our estimate of EBITDA for this year. This is a material discount to closest peers Trade Desk (TTD) and Magnite (MGNI), and is unreasonably large in the context of TRMR's superior growth, profitability, and exposure to the fastest growing segments of the market (see table below):

	Trade Desk	Magnite	Criteo	**Tremor**
EV/CY21 Sales	24.22	13.63	1.90	**3.95**
CY21 Sales Growth	36.2%	78.1%	6.2%	**95.0%**
EV/CY21 Gross Profit	30.3	15.3	2.2	**5.3**
CY21 GP growth	36.8%	70.0%	10.0%	**73.3%**
CY21 GP margin	80.0%	66.6%	34.6%	**75.1%**
EV/CY21 EBITDA	69.5	40.2	6.0	**10.0**
CY21 EBITDA growth	39.8%	746.6%	11.2%	**349.0%**
CY21 EBITDA margin	34.9%	25.3%	28.7%	**39.3%**

This gap should close shortly, however, as Tremor recently filed for an American listing and expects to complete the process by the end of the second quarter. If history is any indication, this is likely to serve as a strong catalyst as the stock becomes available to a far larger number of potential investors. Management seems to agree that the stock is cheap at current levels, as they repurchased shares in the first quarter ahead of the re-listing. We think TRMR hits the trifecta of rapid growth, existing profitability, and potential for further margin expansion – and unlike most other stocks with that trio of characteristics, we aren't paying a premium for it. As a result, Tremor has become one of our larger positions, and we have accumulated shares ahead of its upcoming debut on the NASDAQ.

Voyager Digital (CN-VYGR): Launched in 2018 by a group led by a former E-Trade executive, Voyager Digital operates one of the fastest-growing cryptocurrency brokerages, thanks to a well-regarded app that enjoys favorable reviews for its wide range of tradable assets (nearly half of which pay interest) with zero commissions. Despite this, it trades at a significant discount to peers, in large part because of its orphan status: VYGR is headquartered in NYC and has mostly US-based customers, but its main listing trades on a secondary Canadian exchange.

I have no view on the fair value of any cryptocurrency – but I do have a strong view that there will continue to be growing blockchain interest based on new applications, a wider range of everyday use cases, and greater institutional acceptance as of late. To paraphrase the Peter Lynch quote,[1] most potential digital golds may lose value, but one can make a lot of money selling the digital picks and shovels that customers need to look for them.

Voyager reported $3.3 B USD in AUM for April and has now added over $400 M/month in net deposits for 2021. The company's investor presentation suggests that VYGR generates about $100 per month per funded account; increased volume on smaller "altcoins" that generate more revenue per trade means this number should have upside. The company reached 400k active accounts at the end of April, and from a recent interview, it seems as though the company has already surpassed 600k for May. Putting these metrics together suggests a run-rate of about $720 M in annual revenues, not including any upside from (the highly likely) further account growth, versus a current EV of around $2.7 B. This 3.8x multiple compares very favorably to FinTech peers (even after taking into account Coinbase's recent multiple compression):

[1] "During the Gold Rush, most would-be miners lost money, but people who sold them picks, shovels, tents and blue-jeans made a nice profit." – Peter Lynch

Company Update
March 28, 2021

Figure 4: Private fintech company valuations

Company	Valuation (U$bn)	Sales (U$bn)	EV/Sales
Robinhood	$40.0	$1.35	29.6x
SoFi	$4.8	$0.40	12.0x
Hippo	$1.5	$0.10	15.0x
Acorns	$0.9	$0.07	13.2x
Revolut	$5.5	$0.08	71.6x
Betterment	$0.8	$0.05	16.0x
Wealthfront	$0.5	$0.03	15.2x
Circle	$0.7	n.a.	n.a.
BlockFi	$0.4	$0.02	16.2x
Coinbase	$100.0	$2.30	43.5x
Average (excludes outliers)			**15.8x**

Source: Stifel GMP estimates, various company and industry reports

Looking slightly longer term, the toll road-like business model of a brokerage combined with the stickiness of customer assets produces a long runway for further expansion even after this hypergrowth phase ends. In my original draft of this piece, I wrote that operating leverage would come with scale, and that since mature traditional brokers boast operating margins of 40%+ (and since Coinbase already posted an 32% operating margin for 2020 on $1.3 B in sales), VYGR should eventually be able to reach that mark too. I assumed it would perhaps take until mid-2023, at which point VYGR could generate somewhere in the ballpark of $1.50-1.75 in EPS (after giving effect to SBC dilution), putting it at 12-14x earnings two years out.

A few days later, however, VYGR showed that it was far ahead of my schedule. The company announced in its results for Q1CY21 that it had already achieved a 50% operating margin for the period and even expressed its optimism for further profitability expansion going forward. Even assuming a massive deceleration, the risk-reward is highly asymmetric. Funded account growth could go from the current month-over-month 50% rate to mid-single digits, and the operating margin could contract to 30% for the full year, and the company would still generate almost a dollar per share of free cash flow this year and trade at a market multiple despite having far superior profitability and growth prospects. Assuming a more realistic glide path, in which the deceleration is gradual and operating margins can hold their current level, Voyager could generate over $400 M of FCF in calendar year 2021. This works out to an 8x multiple on today's price, which we think is far too cheap given the current exponential growth within an industry that remains in the relatively early stages of its lifecycle.

A few potential return cases are sketched out below, which show that one can pencil out over 100% upside with assumptions that are not at all heroic, and that very little further growth is underwritten in today's price. Indeed, there are a wide range of outcomes here, but they are highly skewed toward positive ones.

	2021 Low	2021 Mid	2021 High		
Assumptions	No account growth after May; EBIT margin contraction to COIN range	Mid-single digit account growth after May; EBIT margin in line w/ Q1	Gradual deceleration from current 50% MoM; EBIT margin in line w/ Q1		
Sales	581.0	673.9	1,046.9		
x EBIT Margin	*30.0%*	*50.0%*	*50.0%*		
EBIT	174.3	337.0	523.4		
- Interest	5.3	5.3	5.3		
- Tax	35.5	69.7	108.8	21%	tax rate
NI	133.5	262.0	409.3		
÷ Shares	170.0	174.3	178.6		
EPS	0.79	1.50	2.29		
x Multiple	20.0	25.0	30.0		
Value (USD)	15.71	37.59	68.76		
Upside	*-8.0%*	*120.2%*	*302.7%*		

There are plenty of risks with this investment – there could be another multi-year “crypto winter” in which public interest wanes. In terms of business operations, customers have complained about long processing times for withdrawals and intermittent app connectivity issues (though these are not unique to VYGR). And on the stock side, the equity is highly volatile and often sees its daily fluctuations follow that of the underlying tokens’. However, these risks are more than adequately compensated for given the company’s rapid growth, strong execution, and significant valuation discount. The last time we saw a discrepancy this big was Gan plc in 2019, which became a multi-bagger over the next year. Furthermore, the position can easily be structured as a pair trade against recently-public Coinbase to mitigate industry risk if desired. Voyager has lower fees, faster growth, and a much cheaper valuation – COIN’s main selling points are its first mover advantage and name recognition, and we don’t view those as nearly enough to warrant a 100%+ multiple premium.

Outlook & Conclusion

The only constant in the investment world is change, and that has again been the case in the early months of 2021. Many pandemic darlings are down 50%+, while commodity stocks that couldn’t get a bid for years are outperforming the broader indices. Much of this can be attributed to newfound inflation fears after sky-high headline CPI readings in recent reports mixed with anticipated pent-up demand for any activity done out of the house. The current scenario is certainly unusual, both in terms of speed and magnitude of the changes seen. But just as we don’t try to predict the values of stock indices, we won’t try to predict those of

price indices either. All we can do is continue to look for situations where there is a sizable disconnect between a current and fair valuation, and as of now, we are still finding more than enough to keep us busy. Accordingly we will continue along this path, hopefully connecting the right dots and adopting a few more orphans along the way. I look forward to writing you again in a few months' time; in the meantime, I hope everyone enjoys their summer.

"The most important thing in life is to stop saying 'I wish' and start saying 'I will'."

- Charles Dickens

Per Ardua Ad Stella,

Andrew Jakubowski

Performance Summary:

	1Q 2021	Since Inception
S&P 500	6.4%	131.4%
Vanguard Total World Stock ETF	5.4%	82.1%
Russell 2000	12.9%	104.5%
HFRI Equity-Hedge (Total) Index	7.1%	58.9%
Adestella Investment Management	**19.6%**	**298.7%**

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