INVESTOR LETTER: CAPCAPITAL Q3 2020

https://kristal.ai/funds/capcapital-ventures-pooled

KRISTAL

+65 8511 9486
support@kristal.ai
8 Shenton Way, #50-03 AXA Tower, S068811

Top 10 Holdings

1 Zoom
2 CrowdStrike
3 Tencent 腾讯
4 amazon
5 sea
6 shopify
7 Microsoft
8 servicenow
9 DATADOG
10 Roku

Performance Summary

	Q3 (Jul-Sep)	May	Jun	Jul	Aug	Sep	YTD
CapCapital Ventures Kristal	22.86%	10.47%	4.96%	6.99%	11.17%	3.30%	42.45%
Vanguard Total World Stock ETF (VT)	7.81%	5.21%	2.58%	5.29%	6.01%	-3.41%	16.36%
SPDR S&P 500 ETF Trust (SPY)	8.60%	4.76%	1.33%	5.89%	6.98%	-4.13%	15.29%
Invesco Technology ETF (QQQ)	12.21%	6.60%	6.10%	7.35%	10.94%	-5.78%	26.92%

Dear Valued Investor,

CapCapital Ventures got off to a flying start in our first full quarter since inception. We had very strong results from our portfolio companies. Many of our holdings benefit from secular tailwinds of the world moving to bits from atoms. The pandemic is lasting longer than I anticipated and we made some changes to our portfolio moving away from a few of our covid epi centre cyclical stocks towards covid beneficiaries during this quarter. I am pleased that market volatility late in the quarter gave us an opportunity to build reasonable positions in some of these beneficiaries. You might notice that three of our five additions this quarter also made it to our top ten holdings. As we are still in our early days as a fund it is easier to be aggressive and build concentrated positions quickly. I anticipate smaller changes in the quarters that will follow this unprecedented year.

"This quarter was a tale of two halves. We had a strong rally in July and in particular August followed by a correction in September. Markets rallied between 13% to 18% in the first two months. The rally in FAANG stocks and especially Apple contributed to most of the gains within different indices. While we matched those gains, our outperformance came in September wherein we managed to add to our gains while indices corrected by 5% to 9%.

The biggest takeaway from this quarter's earnings was that the trends which accelerated during the pandemic continue to persist. In a study published in the European Journal of Social Psychology, researchers concluded that on a average, it takes more than two months before a new behaviour becomes automatic - 66 days to be exact. The widespread global new habits inculcated during live, work and play from home in the last six months are here to stay. I would also like to add that this year is more volatile as the rate of change is greater and more difficult to forecast.

Portfolio Performance & Activity

Performers

Our top performers for the third quarter were **Zoom Communications** up **91.6%**, **Pinterest** up **71.3%** and **Roku** up **42.09%** for the third quarter. Our top three detractors were **Paycomm Software** down **8.4%**, **Shopify** down **3.4%** and **Moody's** down **0.5%**.

ZOOM Communications had a stellar quarter. We first initiated a position in ZOOM after 2nd quarter results wherein the company reported a 169% growth. Zoom was definitely becoming the biggest beneficiary of the pandemic. When we began buying shares around $200, they had already tripled since IPO. If the second quarter results were the biggest enterprise quarter in history, the follow through with a revenue growth of 355% in third quarter left everyone speechless. Zoom shares gapped up 40% and by $132 dollars with 600% increase in volume the next day. Zoom zoomed past other portfolio constituents to become our top holding. I sold some shares late in the quarter to ensure we stay below the 10% portfolio weighting for a single stock name as per our fund mandate. Zoom shares have been volatile in the last one month wherein they retraced back to $350 and then back up to $490. I shall write more on this holding after the fourth quarter results in my mid quarter stock analysis.

In my second quarter letter I had written " The path to profitability for both **Roku** and **Pinterest** is less obvious than all the stocks in our portfolio. If they can find a path to profitable growth there will be tremendous upside." While both companies did not report a profitable third quarter, there were positive catalysts that unlocked some of the tremendous upside. I would also like to highlight that the bigger returns sometimes come from positive surprises that are not priced in and result in a re rating of a stock. These gap up's and move up to a new range only accrue to long term shareholders who ride through the difficult times and volatility. Its not timing the market but time in the market that differentiates remarkable from average returns.

Pinterest like Zoom has been a covid beneficiary with higher levels of engagement from the new cohort users and more engagement with the shopping functionality. Pinterest ingested more catalogs in the quarter (up 350%) than it had previously ingested in its entirety since product launch. Its partnership with Shopify appears to be yielding early results. The management also highlighted that newer ad products appear to be gaining higher traction with over 80% of the cost per click budget moving to autobid and conversion optimisation ads growing faster. Pinterest has been growing faster in international segment with 77% yoy growth. Pinterest also reported a huge ramp up in July up 50% and a 58% improvement from April numbers. Pinterest results have been volatile since IPO, and I would like to see a few quarters of consistent growth to instill more conviction in this name.

Roku is the market leader in TV streaming industry with 43 million accounts. The business has two segments Player (hardware) and Platform (advertising, subscription, and transaction). Roku is going after both the linear TV $70B market and the $130B digital advertising market. The Tv business is moving from linear to connected TV’s and Roku’s platform and collaborations are providing aggregation and discovery to the consumer. They are monetizing this high installed based with advertisers and content providers. The shares gapped up after Comcast - NBC streaming service Peacock signed an exclusive deal with Roku reinforcing it as a must have platform for content providers. Revenue grew 42% in the quarter and revenue growth has been strong and consistent. A path to profitability and better unit economics would unlock further upside.

Detractors

Paycomm software is experiencing strong headwinds from the rise in unemployment due to Covid. It reported a revenue growth of 7% as opposed to the usual high twenties in the past. They are also negatively affected by lower interest rates as they invest the float. However, in spite of short-term pressures management reported the highest recorded quarter for new customer bookings. This is a very strong company with high operating margins with a long runway for growth. I expect shares to consolidate and move higher with employment trends.

Moody’s reported strong third quarter results. Revenue was up 18% and EPS 36%. They raised the full year guidance to $8.80 -$9.20 almost 10% guide up on the back of strong issuance of bonds by many companies due covid. The shares moved up first half of the quarter and then retraced ending flat. The trifecta of rating agencies Moody’s, S&P Global and Fitch have strong fundamentals and will be steady performers in any portfolio.

Shopify pulled back after another stellar quarter giving us an opportunity to start a position.

New Buys & Sells

Caesars Entertainment Inc

We sold our position in **Aristocrat Leisure** - biggest developer and operator of slot machines when a compelling opportunity arose in July 2020 after the completion of the merger between El Dorado Resorts and Caesars Entertainment.

El Dorado Resorts management has an exceptional track record of value enhancing acquisitions in regional casino's in USA. They announced a 8.6 billion bid for Caesars in June 2019 to grow their portfolio to 57 properties from just four in 2014 and became the largest US gaming operator with 10% of the total gaming revenue. Carl Icahn and other activists had been pushing for a sale of Caesars and supported the bid. The share price of both companies rallied and El Dorado made a all time high of $69.47 in February 2020. As Casino's temporarily shut down during Covid. El Dorado share price fell from a high $69.47 to a low of $7.10 in less than one month. With revenue in a free fall, it was uncertain that the deal could close due to high levels of leverage. Both companies were required to divest assets and get approvals from many different state gaming regulators. In May there were too many possible outcomes and I found Aristocrat's sound balance sheet and margins more attractive.

The merger closed on 15th July 2020 with share price at $42.03. I expected the shares to rally on the news. However, the shares retreated to $29.74 within two weeks. There was speculation that Carl Icahn was selling his stake (activists funds usually on a completion of a campaign exit to find newer opportunities). Tom Reeg, CEO of combined company on several earnings calls reiterated meeting synergy, Ebitda and leverage targets inspite of the Covid headwinds. We initiated our first buys at $31.05 on 31st July. There have been positive developments including a sports book deal with ESPN and shares have rallied. The shares are trading around fair value and I am hopeful that they will not have a roller coaster ride again while the management team executes to integrate and drive higher EBITDA margins as well as explore green field opportunities in online gaming.

Adyen

In the land of payment networks there are three big incumbent merchant acquirers Fidelity National Info Services ($90 Billion market cap), Fiserv ($69 billion) and Global Payments ($53 billion). There are also three disruptors Square ($64 billion), Stripe (private valuation $36 billion) and Adyen ($55 billion). These are all incredibly good investments with their own respective merits. We sold **Global Payments** and bought **Adyen** on the prime thesis that online payments were accelerating due Covid and merchants are looking for omni channel solutions which favours the disruptors.

The core mission of Adyen is to make payment choices easy for the merchants. Adyen is a payment gateway, risk management system and acquirer all rolled in one. They also provide an end to end solution, managing the entire payment flow from checkout to final settlement.

Adyen is based in Netherlands and thats a reason for its wide geographic reach to more than 150 currencies and over 200 methods of payments. Adyen went IPO in June 2018 and shares surged 90% in the first day trading. They have more than tripled since in a little over two years. Adyen has always screened well on all metrics except valuation. We have initiated a small position and would add slowly as Adyen grows into its present valuation and hopefully beyond. Pieter van der Does - Adyen co founder writes excellent shareholder letters that explains their business, outcomes and objectives candidly.

DataDog

Datadog is a monitoring and analytics platform for developers and operation teams. Its platform integrates and automates infrastructure monitoring, application monitoring and log management. Datadog dashboard provides real time insight into the full infrastructure - cloud, servers, apps, services, metrics and more - all in one place. Its imperative for IT operations management to ensure optimum performance of the software stack on which everything functions.

Datadog was designed and built by Olivier Pomel for the cloud in 2010 while incumbent competitors like Splunk, New Relic and Dynatrace were all initially built for on premise. The company experienced very strong growth rate as monitoring moved to cloud from on prem. Datadog went public less than a year ago in September 2019 at 27 dollars valuing the company at $10.9 Billion. The company has reported growth north of 80% and always supported higher valuations.

Datadog reported first quarter earnings with a revenue growth of 87% in May 2020 and the share rallied strongly over the next six weeks. I was unable to initiate a position and waited on the sidelines. In August 2020, the company reported a growth of 68% and shares sold off by 25% in two days. I sold Elastic and bought Datadog. This was the hardest decision of this quarter, as Elastic is a very good company. There is some overlap in some products and solutions between Elastic and Datadog and I could only hold one of the two for our portfolio. I have higher conviction in Datadog and also believe it will reach a much higher operating margin at scale.

Amazon & Shopify

E Commerce has been the biggest beneficiary of the Pandemic. The pandemic has pulled forward secular trends in e commerce and permanently inflected demand. Before the pandemic, Amazon commanded approximately 37% of the US e commerce sales, while Shopify was in the second place with a 6% market share ahead of E Bay, Walmart and Apple. These two companies are clearly the best of breed executing at scale and continue to defy gravity and the law of large numbers. We sold **Live Nation** (monopoly on events) and **DIP Corp** (Japan's online staffing company) as the pandemic is lasting longer and revenues for both will remain challenged for an uncertain period of time. In the meantime Amazon grew quarterly revenue by 40% in Q3 to 88.9 Billion and Shopify by 97% to 714 million.

E commerce has an incredibly huge total addressable market. Both companies have taken different approaches. Amazon - everything store is an aggregator with a mission to be the most customer centric company and offer the highest value to the end user. Shopify is a platform with the mission to make commerce better for everyone, so businesses can focus on what they do best : building and selling their products. Shopify is supplying solutions to the merchant to level the playing field. Both of them are building the tools and rails on which commerce of the future will function.

Amazon is seen as the dominant aggregator and Shopify as the platform with the mission to arm the rebels. Its easy to get lost in ideology, debates, forecasting and build an either or bias. However, as an investor our task is to filter the signal from the noise and make decisions based on reason. The slight pullback in both securities has offered a good entry and we have built a reasonably big position in both. I foresee us being shareholders of both businesses for a long time.

Closing Comments

Everyone expects a volatile last quarter as a finale to this unprecedented year. The November US Presidential elections will take center stage for the next two months. We are also closer to final results from various vaccine studies. I believe these two will matter more to market direction than earnings for this quarter. So we may have a roller coaster ride up ahead. While volatility is uncomfortable, some wise words from Warren - " I have been a net buyer of stocks since I was eleven. There have been seven Republican presidents and seven Democrat presidents. And I have bought stocks under every one of them."

I would once again urge you to add excess funds and liquidity to the fund from time to time to participate in this excellent opportunity set we are creating as long term investors in excellent businesses. I would really appreciate any introductions or referrals as it demonstrates conviction in our fund, process and future prospects.

Yours sincerely,

CapCapital Ventures

CAPCAPITAL VENTURES

KRISTAL

Very High Risk	Equity	Unit Price (NAV): **$14,245.2187** *(price as of 30 Sept 2020)*	Min Investment: **50K USD**

Overview

This strategy will invest in public listed equities. The strategy will aim to generate absolute returns through compounding in businesses in the high growth and quality matrix. The portfolio is formed by selecting stocks using bottom up analysis that meet earnings growth, operating margin, return on equity, return on invested capital hurdle rates.

Key Facts

Strategy: **Growth**
Fund Type: **Open Ended**
Class: **Global Equity**
Benchmark: **Vanguard Total World Stock ETF**
Subscription & Redemption Frequency: **Weekly**
Redemption Settlement: **5 Business Days**
Management Fee: **0.5% per annum**
Performance Fee: **20% over 5% Hurdle Rate**

Recommended For

Ideal for investors looking for long term capital appreciation by gaining exposure companies with strong competitive advantages and healthy earnings growth.

Investment Style & Objective

Actively Managed
Capital Appreciation

Investment Strategy

This Kristal aims to invest in companies with strong moats, good management and ability to deliver healthy earnings growth over the next five years.

Portfolio can be divided into 5 buckets:

Central Core - These wide moat equities dominate the market they operate in. Revenue growth is >10% and they have high return on equity. The increase in margin and free cash flow will result in earnings growth of >15%. Expected Return 10 -15%.

Growth at Reasonable Price - These positive moat equities are creating dominant positions. Revenue growth is 15 - 25% and they have good margins. Most of the cashflow is being used for reinvestment in the business that has a growing TAM. Expected Return 15-25%.

Explosive Growth - These are newer companies that have IPO within last two years. Revenue growth is explosive and while margins and earnings are negative presently they are improving. These businesses can have a wider range of outcomes. Expected Return 20-30%.

Undervalued Cyclical - These are cyclical companies that have historically demonstrated high returns on capital. Under the present circumstances the market correctly expects lower earnings and growth potential. Looking further out they will benefit when conditions improve and they gain market share from competitors. Expected Return 20 -25%. Will initiate only when I believe the equity can double in 2-3 years under right catalysts.

Asset Play - These equities are usually conglomerates with various diversified business. In these it can be safely determined that the sum of the parts is greater than the price of the equity. Often this discount can persist for many years. Will initiate only if the discount is greater than 50%.