February 28, 2021

Value Investor INSIGHT

The Leading Authority on Value Investing

Into the Fray

Contention about a company's prospects increases the likelihood that its shares are mispriced, says David Barr, who has proven quite adept over time at picking sides.

INVESTOR INSIGHT

PenderFund Capital Management
David Barr (*l*), Felix Narhi (*r*)

Investment Focus: Seek companies whose prospects the market is either hotly debating or just overlooking, in both cases resulting in potential share mispricing.

David Barr of Vancouver's PenderFund Capital Management spent the first part of his investing career as a venture capitalist, reflected today in his penchant for small companies with what he considers long growth runways. But he's also a well-read student of Ben Graham, valuing in target companies what he calls "deliberate conservatism" in how they're managed.

This balanced approach to stock picking has paid off nicely for his investors. The Pender Small Cap Opportunities Fund since 2009 has earned a net annualized 19.0%, vs. 8.2% for the BMO Blended Small Cap Index. Today he and colleague Felix Narhi, who invests across a broader market-cap range, see upside in such diverse areas as real-estate services, telecom, beauty products and enterprise communications systems.

Inside this Issue

Investor Insight: David Barr

PenderFund Capital Management's David Barr and Felix Narhi explain why they often gravitate to "battleground" stocks, which companies they consider to be the next-generation "FAANGs", the evolution of their interest in Bitcoin, and why they think Zillow, Liberty Latin America, MAV Beauty Brands and Sangoma Technologies are mispriced.

You characterize your ideas as falling into two general categories: "Compounders – Buy Low, Let Grow," and "Close the Discount – Buy Low, Sell High." Describe how you came to think about ideas in that way.

David Barr: We all grow up reading Ben Graham and Warren Buffett, which is excellent grounding in traditional value investing. You're less focused on the quality of the business and more on what it's worth today relative to the stock price and on why that gap may close over time. The discipline makes sense and has stood the test of time, so we try to capitalize on that in our close-the-discount names.

What we've learned over time from Buffett and how he evolved is that the majority of returns in the market come from select companies that have compounded internal capital at really high rates of return for long periods. That tells us that if we want to build a great long-term track record, we need to find some of those compounders relatively early and hold onto them for dear life – or "let them grow." One qualification to this is that we from early on have been active in the small-cap space, and it's hard to categorize small caps as compounders. There it's more accurate to say we're looking for emerging compounders. It can vary, but overall our portfolios run roughly 70/30, growing compounders versus traditional value.

Felix Narhi: How you manage these two types of holdings obviously differs. For close-the-discount names, we're typically trading around the business cycle or cycles in investor enthusiasm, so when the dollar you bought for 70 cents gets to a dollar, we're usually quick to sell or significantly trim to avoid round-tripping.

With compounders, we're reluctant sellers. We'll trim position sizes for portfolio management purposes, but we typically won't sell outright unless our thesis becomes impaired or the valuation becomes so extreme that decent long-term returns are hard to envision even if our bull-case scenarios come true.

Just as an aside, one of the great things about market meltdowns like we had last March is that they are one of the few times you can find compounders selling at close-the-discount prices. There you're looking at a potential double-barreled return, first when the valuation reverts and then second when the stock follows the growth of the business higher.

ON MISPRICING:

One great thing about meltdowns: You can find compounders selling at close-the-discount prices.

Other than a market meltdown, what tends to make the companies you target potentially mispriced?

DB: I mostly focus on small caps and there often just aren't as many fundamental investors paying attention to these companies, increasing the likelihood of mispricing. As you go up in cap size markets get more efficient, but we often find opportunities in what I call battleground stocks. In these there's both a strong bull thesis as well as a very believable bear case. The tug of war going on in the market can create a lot of volatility and tends to provide various entry points for the value-conscious investor. Amazon was a battleground stock for probably a decade before the bears capitulated. Netflix as well. These aren't for the faint of heart, but if we can build conviction that the bears are wrong, these have been fertile grounds for ideas.

I'll give you an example of a small-cap idea where we didn't think the market was grasping what was going on. We've owned for years a wonderful company in Canada called ProntoForms [Toronto: PFM], which essentially provides software that transforms paper forms into mobile forms. A simple use case would be a gas meter reader, who ten years ago would read your meter in the field, write the numbers down on a piece of paper or maybe enter them into an Excel spreadsheet on a laptop. ProntoForms' software automates that so that the data can be efficiently and securely entered on a mobile device and immediately available for internal use. The company has been growing rapidly and there's a tremendous amount of greenfield ahead as companies with workers in the field slowly come into the 21st century.

The opportunity in the stock came as the company has transitioned from selling through channel partners to its own direct sales force. The share of revenue from each has flipped over the past several years and by next year will be almost 100% direct. It is absolutely the right thing to do – higher margin, more control over messaging, direct feedback on customers' wants and needs – but there has been considerable upfront expense involved in making the transition and some friction with channel partners. If you didn't really understand what was going on as an investor, you'd not see the fundamental change going on at the company for the better. We still think these are the early chapters of a very strong growth story. [*Note*: ProntoForms shares at a recent C$1.25 have more than tripled since the beginning of 2019.]

FN: In the bigger-cap names I focus on, a good example of a battleground stock in recent years has been Baidu [BIDU]. The company was credibly known as the Google of China, but unlike the actual Google it didn't transition its search business well from the desktop to mobile and it ended up left out of mobile apps like WeChat that dominate the market. The bear case, then, has been that while maybe Baidu owned the past, it doesn't own the present.

The alternative view, to which we ascribe, is that the advertising business will continue to generate considerable free cash flow and that the company has a number of assets that are quite well positioned for the future. Baidu owns a majority stake in iQIYI [IQ], which many consider the Netflix of China. It owns 11% of Trip.com [TCOM], the online travel giant in China. It has thriving businesses in fintech and AI cloud services. Maybe most importantly, it's been crowned China's national champion for autonomous driving. The addressable markets for the non-advertising businesses, excluding autonomous driving, is multiple times that of the legacy ad business and growing three times faster. And if Tesla and others are guides, then perhaps the autonomous driving leader of China could be worth a lot as well.

I wouldn't say the battle is over, but the market over the past six months has embraced the more optimistic outlook. Last fall when the ADRs traded in the $130s we could make a sum-of-the-parts case that something like autonomous driving was barely considered a source of value. The upside optionality isn't gone in our opinion, but with the ADRs now near $285, it's not as pronounced as it was. The close-the-discount opportunity may be much less, but we think the company could be at the early stages of reestablishing itself as a compounder again.

In your quest to identify emerging compounders you've identified what you consider a next generation of "FAANG" stocks, which you've dubbed the "ZIPSS". Tell us about those.

DB: I'll give Felix credit for coming up with the catchy acronym, but this is a group of companies that have some similarities to the business models of the most popular technology names, but which we believe have longer runways of growth ahead that have not been as fully appreciated by investors.

There are more than this, but here are the five we highlight as ZIPSS: Zillow [ZG], which is disrupting how property is bought and sold in a world where consumers increasingly demand the same convenient and efficient online experiences they find elsewhere; IAC/InterActiveCorp [IAC], which is transforming a host of areas, from video services to finding a job and home repair; Par Technology [PAR], which is re-platforming and digitizing the restaurant industry; Stitch Fix [SFIX], an online apparel company that wants to "hyper-personalize" the fit and style of clothing for its consumers; and Square [SQ], a leading fintech that is disrupting the payments and banking industries.

The commonalities among these companies are that they have business models that should drive profitable growth as they scale, they benefit from positive feedback loops that amplify their competitive advantages, and they target industries with massive total addressable markets. We owned two of them before – Zillow, which we bought in late 2018, and Par, which we added in May of 2019 – but Stitch Fix and Square we added in the aftermath of the pandemic when their stocks got hammered. IAC we added in August after the spinout of Match Group.

Congratulations on all that – the share price recoveries in these stocks has been rather breathtaking. Are you still as enthusiastic about them?

DB: We have trimmed in cases where position sizes have gotten too big in our view, but as Felix alluded to earlier, the trick for investors in these types of disruptive companies is to be patient and to hold as long as the companies continue to execute on their vision and the share valuations remain reasonable in the context of their potential future value creation. If you sell during the dips because you're more worried about the near-term price action than the long-term value creation, you'll likely miss out on value-compounding opportunities. If you sell during the pops, you may try to get back in at a time when you find it difficult to do so. Our goal is to hold onto such core positions as long as our investment theses are proving out and the valuations don't get totally insane.

ON "ZIPSS":

They have similarities with popular technology names, with growth runways not as appreciated by investors.

Talk in more detail about your broader investment case for Zillow.

FN: The big question we ask with all of our companies is, "What problem are you solving?" The bigger the problem and the better the solution, the greater the opportunity. Buying and selling a home for the most part is an awful experience. The open houses, the repairs, the staging, the inspections, offers fall through, financing falls through. And everything is expensive, from commissions to closing costs. It's a brutal, expensive experience. We think there's a huge need for someone to fix this, and Zillow is front and center in trying.

The company's legacy business is basically a media business, providing information on home prices, markets and the home-buying process in general and then selling advertising to real estate agents and others who want to reach potential home buyers. They've been very successful with that – more people Google "Zillow" than "real estate".

The longer game is more interesting. With Zillow Offers, the company's version of what's called iBuying, it will make a no-obligation offer to directly buy a seller's home, as is, based on a well-developed automated valuation model. There are costs involved and Zillow does pay agent commissions, but as the business scales we and they expect this to eliminate a lot of the friction and at least a material portion of the cost of selling your home. As that business gets larger and they get better at it, they will also continue to add ancillary financing, title, closing and other services on their own or with partners. If they pull it off, they will be solving a big problem and capture an increasing share of the value chain in a massive addressable market.

Can you say yet that Zillow's iBuying model is working?

FN: There is promising data from select markets like Phoenix about the unit economics, but it's fair to say that the track record is too short to arrive at definitive conclusions. That's why there's still somewhat of a battleground element to the story, as bears can make a credible case that the economics won't work and that the legacy ecosystem for buying and selling a home is too tough of a nut to crack. From what we've seen the company accomplish already, we think that's a short-term view that will turn out to be wrong.

To what extent are you betting on the jockey as well as the horse here?

FN: Investing is a probabilistic exercise, so we look at predictive attributes to help stack the probabilities in our favor. One of the most important such attributes for us is when a company is owner-operated, as is the case here with Rich Barton. He co-founded Zillow in 2005, was CEO until becoming executive chairman in 2010, and came back as CEO in early 2019.

He is a remarkable entrepreneur, co-founding in addition to Zillow both the online travel company Expedia and the job-search engine Glassdoor. In each case he's looking to increase the transparency and accessibility of information available to consumers to disrupt industries in a way that creates business opportunity. It meant a lot to us when he took charge again in 2019 and essentially said the company was going to be "all in" in pursuing the iBuying path.

One interesting side aspect here is that because Rich Barton and fellow co-founder Lloyd Frink own super-voting stock and have over 50% of the voting control, Zillow is excluded from most benchmark indexes. We consider that a positive. We've done research on U.S. multi-share-class stocks and, contrary to the conventional view, have found that attribute can be predictive of outperformance. Voting control allows these founders to make long-term bets that might be more difficult in a world obsessed by quarterly results, and where activists are looking to shake things up to turn a short-term profit. Where would Amazon be if Jeff Bezos ran his company to meet Wall Street's quarterly targets?

Wavering a bit of late, the shares at just over $161 are still up 5x from their pre-pandemic price. How are you looking at valuation from today's level?

FN: The current enterprise value is roughly $40 billion. We aspire to earn at least 15% annual returns on our investments, so in this case looking ten years out I'm asking if I can imagine that EV quadrupling to $160 billion. Building from the ground up using estimates of the total addressable market, what we hope is an understanding of scale economics and positive feedback loops, and even details on the actual contribution margin after interest

INVESTMENT SNAPSHOT

Zillow
(Nasdaq: Z)

Business: Provider of online media and transactional services focused on all stages of the home-purchase "lifecycle" in the U.S., including research, buying, selling and financing.

Share Information (@2/26/21):

Price	**161.33**
52-Week Range	20.04 – 208.11
Dividend Yield	0.0%
Market Cap	$39.34 billion

Financials (TTM):

Revenue	$3.34 billion
Operating Profit Margin	1.2%
Net Profit Margin	(-4.8%)

Valuation Metrics
(@2/26/21):

	Z	S&P 500
P/E (TTM)	n/a	43.7
Forward P/E (Est.)	172.4	22.5

Largest Institutional Owners
(@12/31/20 or latest filing):

Company	% Owned
Caledonia Inv	21.9%
Vanguard Group	6.9%
Morgan Stanley Inv Mgmt	5.6%
SRS Inv Mgmt	4.7%
Baillie Gifford	4.7%

Short Interest (as of 2/15/21):

Shares Short/Float	14.6%

Z PRICE HISTORY

THE BOTTOM LINE
The company is what Felix Narhi considers a next-generation "FAANG," capable of solving very big problems for the very large addressable residential home-buying market. While its stock has been on a tear over the past year, he can still envision it generating at least the 15% annual return over the next 10 years that he aspires for his investments.

Sources: Company reports, other publicly available information

earned on Zillow Offers' homes bought in Phoenix, we're very comfortable with the fact that this company can be worth 4x what it is today in ten years. Modeling it to the penny doesn't make a lot of sense for something like this, but we'll be happy to be precisely wrong as long as we're approximately right on the big things.

One of my favorite Peter Lynch quotes says that you should buy companies when they're in the second inning of the game and sell them in the seventh inning – which by the way can last 30 years. Last March companies like Zillow, which we consider in the second inning, were priced like they were in the first inning. Now maybe Zillow is still in the second inning, but it's priced like it's in the third inning. That's not at all a reason to sell.

Switching gears, explain your interest in Liberty Latin America [LILA].

FN: This was part of Liberty Global that was spun out a couple years ago, and is probably the least liked of the John Malone investment vehicles. He still has 25% voting control and management consists largely of his disciples.

The basic business model is familiar. This is a multi-product communications-services provider offering some combination of cable, broadband, wireless and phone service in 20 countries in Latin America and the Caribbean. Free cash flow is invested back into the business to expand the services offered and to consolidate market positions, driving increased profitability and cash-flow generation. Growth drivers include the ever increasing necessity of broadband in their markets and the fact that penetration levels across the product spectrum are generally 30-50% what they are in developed markets.

There's a character on *The Simpsons* named Sideshow Bob who's always stepping on rakes that slam him in the face, and that's sort of how things have been for LILA in recent years. Hurricane Maria slams Puerto Rico. Hurricane Dorian slams the Bahamas. There's civil unrest in Chile, which had been considered one of Latin America's more stable countries. Then the pandemic hits and many tourism-based economies in the region suffer. Progress made in one area gets taken away somewhere else.

The company has managed well through the turmoil and – as you like to see during difficult times – continues to execute on its strategy to strengthen its positions in key markets. Last summer it bought Telefónica's wireless assets in Costa Rica, where it already is the leading cable provider. In November it agreed to buy AT&T's wireless and wireline operations in Puerto Rico, a market where it's already the leading broadband provider. This to us signals the company is still building value that will be unleashed at some point when the rakes eventually stop hitting them in the face.

How do you see that building of value eventually turning into upside for the stock, now trading at around $11?

FN: Pre the two recent acquisitions, the company on a normalized basis earns a little over $200 million in annual free cash flow. Add in the two acquisitions and credit them for some integration synergies, and we believe that number increases signifi-

INVESTMENT SNAPSHOT

Liberty Latin America
(Nasdaq: LILA)

Business: Provides television, broadband, wireless and phone services in 20 countries in Latin America and the Caribbean; key markets include Puerto Rico, Chile and Panama.

Share Information (@2/26/21):

Price	**10.97**
52-Week Range	7.55 – 15.79
Dividend Yield	0.0%
Market Cap	$2.55 billion

Financials (TTM):

Revenue	$3.64 billion
Operating Profit Margin	13.4%
Net Profit Margin	(-16.9%)

Valuation Metrics
(@2/26/21):

	LILA	S&P 500
P/E (TTM)	n/a	43.7
Forward P/E (Est.)	14.9	22.5

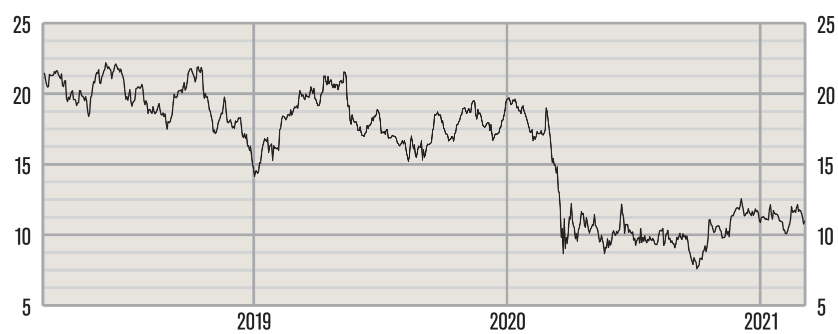
Largest Institutional Owners
(@12/31/20 or latest filing):

Company	% Owned
Ashe Capital Mgmt	9.4%
Genesis Inv Mgmt	9.4%
BlackRock	6.1%
Berkshire Hathaway	5.4%
S & Co.	4.4%

Short Interest (as of 2/15/21):

Shares Short/Float	2.0%

LILA PRICE HISTORY



THE BOTTOM LINE

Through a series of unfortunate events impacting its key markets in recent years, the company has continued to execute on its long-term strategy and strengthened its market positions, says Felix Narhi. On his normalized estimate of annual free cash flow, the shares now trade at what he considers a fire-sale free-cash-flow yield of more than 15%.

Sources: Company reports, other publicly available information

cantly, to $450-500 million. At that level on today's $2.6 billion market cap, that's a 15-20% free-cash-flow yield. That's pretty remarkable for a business like this with a long runway of growth ahead of it.

Looked at another way, the stock today is trading on our 2022 estimates at an EV/EBITDA multiple of around 5x. That also is very inexpensive for a high-quality, recurring-revenue business. John Malone companies usually carry a good amount of leverage, so because of that for every one EV/EBITDA multiple turn, the value of the equity would increase by about 80%.

I think people have just become exhausted with this stock and don't care anymore. Having owned it for the past couple of years, I understand. But if you do the math and believe the bad luck can't go on forever, the upside to sticking with the story is quite high.

Moving to the small end of the cap spectrum, why are you high on the prospects for MAV Beauty Brands [Toronto: MAV]?

DB: MAV Beauty was originally founded by Marc Anthony Venere in 1995 to primarily sell haircare products under the Marc Anthony True Professional Brand. Private equity firm TA Associates bought it in 2006 and after a time implemented a platform strategy focused on acquiring independent personal care brands with let's say, more modern sensibilities, and then helping them scale. The first acquisition was Cake Beauty in January 2018, and in March of that year they also bought Renpure, which produces natural, plant-derived products. The large majority of sales are in North America through the food, drug and mass channels.

The company came public in mid-2018 at C$14 a share, and in classic fashion proceeded to bust as it fell short of the unrealistic expectations used to get a high price in the IPO. Within 12 months it was trading below C$3 and was fully in the market's penalty box.

The business itself, however, has actually done quite well. The focus on young, on-trend brands makes sense in markets where legacy players have a tough time being considered authentic in rolling out their own organic or natural products. At the same time, small founder-owned brands find it difficult to establish distribution channels and get to scale. MAV has relationships throughout the distribution channel, and retailers in particular are eager to support new, credible challengers in order to keep legacy brands honest.

Sales at Cake Beauty have increased seven-fold since MAV bought it. Renpure's revenues have grown at a 30% compound rate since it was acquired. Overall, MAV's revenues over the past three years are up 15% per year and adjusted EBITDA is growing at a comparable rate. They're proving out the model of acquiring small brands and ramping up sales.

How cheap do you consider the shares at a recent C$5.75?

DB: The stock on our forward estimates today trades at about 9.5x EV/EBITDA, which is extremely attractive relative to precedent transactions done at around 15x, or compared to peer multiples closer to 20x. Using private market value, the stock would trade at C$11.50 to C$12. Based on peers, it would be closer to C$14.

INVESTMENT SNAPSHOT

MAV Beauty Brands
(Toronto: MAV)

Business: Producer of personal care and beauty products; strategy is to consolidate newer, founder-owned brands, which today include Marc Anthony, Renpure and Cake.

Share Information
(@2/26/21, Exchange Rate: $1 = C$1.27):

Price	**C$5.73**
52-Week Range	C$1.78 – C$7.34
Dividend Yield	0.0%
Market Cap	C$210.7 million

Financials (TTM):

Revenue	C$123.5 million
Operating Profit Margin	20.3%
Net Profit Margin	4.2%

Valuation Metrics
(@2/26/21):

	MAV	S&P 500
P/E (TTM)	40.3	43.7
Forward P/E (Est.)	11.5	22.5

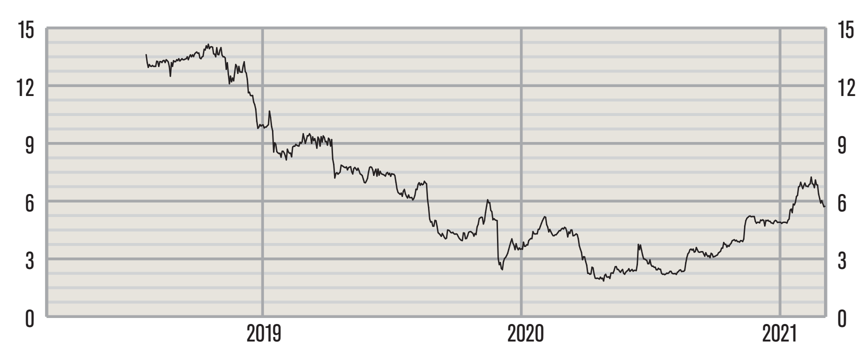
Largest Institutional Owners
(@12/31/20 or latest filing):

Company	% Owned
Marc Anthony Venere	28.2%
TA Associates	25.9%
Burgundy Asset Mgmt	19.9%
PenderFund Capital Mgmt	11.7%
RBC Global Asset Mgmt	2.8%

Short Interest (as of 2/15/21):

Shares Short/Float	n/a

MAV PRICE HISTORY



THE BOTTOM LINE

The company's business is performing much better than its stock since what turned out to be an over-hyped IPO in mid-2018, says David Barr. As it continues to prove out its strategy, he believes the shares will warrant a valuation at least reflecting precedent transactions, which on his forward estimates would lead to a doubling of the stock price.

Sources: Company reports, other publicly available information

Some discount to the market might be reasonable if the company were growing at a below average rate, but that's not the case here. We expect revenues to continue to grow in the low teens over the next few years, including acquisitions, and that the bottom line will likely grow faster than that due to operating leverage.

Two final things I'd mention: The founder, Marc Anthony Venere, still owns 28% of the company and is on the board. TA Associates also still has a large stake of nearly 26% of the outstanding stock. If the market doesn't adequately recognize the value here, we wouldn't be surprised if the company were taken back private or sold, even more so now that it recently announced a strategic review.

Describe your continued optimism around long-time holding Sangoma Technologies [Toronto: STC]

DB: This is a company I've been following for at least 15 years now, and it's fascinating how it has continued to evolve over that time. It provides for business customers cloud-based, on-premise or hybrid communications platforms. The world of course is moving from analog to digital and the unified platforms Sangoma sells ties digital telephony, e-mail and messaging into one seamless digital system. It saves money, is easier to maintain, and is more secure.

The big names people talk about in this market are companies like Twilio [TWLO] and RingCentral [RNG], both of which offer functionality like Sangoma does. The primary difference is that Sangoma targets small to medium sized companies who don't need and/or can't afford the most sophisticated solutions. All the players in the market, however, should benefit from the underlying and ongoing shift from analog to digital, which still has a lot of room to run. Sangoma has been growing organically at 10% annually for several years, and it has augmented that with disciplined acquisitions made specifically to build out the product suite, expand the geographic footprint or build out a vertical customer market.

I mentioned the company's evolution. Just since Bill Wignall took over as CEO in 2011, the company has gone from essentially a one-product hardware vendor, to selling next-generation hardware, to selling integrated hardware and software solutions, to now offering one-stop unified communications platforms. It just announced a further transformative acquisition – of a company called Star2Star – which moves the business even more toward cloud-based solutions and to target somewhat larger customers. In many ways it's been like transitioning a dying textile mill into a dynamic modern enterprise.

The shares, now at C$4.25, have rebounded strongly from a pandemic swoon. We assume you're looking at this more as an emerging compounder than a close-the-discount idea.

DB: The stock trades now at about 3.5x trailing revenue, which doesn't sound cheap, but U.S. peers trade at closer to 10x revenue. That's also not at all an unreasonable valuation for a business with 70% recurring revenue, gross margins of 70%, EBITDA margins of close to 20%, and the potential to increase revenues at least at a low- to mid-teens rate for some time.

INVESTMENT SNAPSHOT

Sangoma Technologies
(Toronto: STC)

Business: Provider of cloud-based, on-premise and hybrid enterprise telecommunications systems targeting small and mid-sized businesses primarily in North America and Europe.

Share Information
(@2/26/21, Exchange Rate: $1 = C$1.27):

Price	**C$4.25**
52-Week Range	C$1.08 – C$5.50
Dividend Yield	0.0%
Market Cap	C$473.3 million

Financials (TTM):

Revenue	C$141.5 million
Operating Profit Margin	9.5%
Net Profit Margin	6.4%

Valuation Metrics
(@2/26/21):

	STC	S&P 500
P/E (TTM)	40.4	43.7
Forward P/E (Est.)	52.6	22.5

Largest Institutional Owners
(@12/31/20 or latest filing):

Company	% Owned
Mawer Inv Mgmt	9.2%
PenderFund Capital Mgmt	5.6%
BMO Asset Mgmt	3.4%
Fiera Capital	1.2%
Principal Global Inv	0.5%

Short Interest (as of 2/15/21):

Shares Short/Float	n/a

STC PRICE HISTORY

THE BOTTOM LINE

The company has been adept in evolving its business as technology enhances what the enterprise communications systems it sells can do, says David Barr. While he believes the valuation gap between its shares and those of peers will narrow, he expects shareholder returns to at least match the firm's strong earnings growth over the next several years.

Sources: Company reports, other publicly available information

Canadian tech companies often trade at a discount to their U.S. peers, but we think there's no reason for the discount to be that high here. Even without a revaluation, if our returns match the company's earnings growth over time, we should be quite well rewarded.

You've written about your interest in cryptocurrencies, particularly Bitcoin. We're curious about the genesis and evolution of that interest.

FN: I started to get interested in the subject three or four years ago, in part because I'm a huge fan of Murray Stahl at Horizon Kinetics, who is both a value investor and very knowledgeable about crypto. The more we've learned about it, the more we believe decentralized finance – which doesn't rely on central financial intermediaries such as brokerages, exchanges or banks – has the potential to have a disruptive impact on several important industries. Bitcoin has emerged as the breakout leader of this nascent digital monetary network and we believe may be in the early stages of growing into a significant asset class, akin to gold. We think that's increasingly relevant when you consider the unintended second- and third-order consequences of the unprecedented central bank and fiscal intervention to fight the economic effects of Covid. I'm summarizing, but all that has led us to conclude we should have some exposure to Bitcoin.

Our approach has been to look for low-risk optionality, call it a "heads I win a lot, tails I don't lose much" strategy. Square, which we own and mentioned earlier, in addition to being a disruptive business is a leading proponent of Bitcoin. We bought shares in MicroStrategy [MSTR], which we also liked for other reasons, but partly because it had moved its very big cash balance into Bitcoin. These investments have paid off very well so far – our average cost in MicroStrategy was around $165 and the shares went above $1,300 earlier this month before a pretty sharp correction – but our eyes are wide open and we're not putting a lot of capital at risk.

You have taken some money off the table in MicroStrategy, no?

FN: We have. We like the company and think the CEO, Michael Saylor, has proven to be an excellent capital allocator. But it became almost a meme stock for Bitcoin and Michael Saylor has been made out to be this Bitcoin Moses. The stock price just went parabolic for reasons we found difficult to understand – in fact, it went up much faster than the price of Bitcoin itself. We're fully ready to sell in those situations, and in this case sold about half our initial stake.

There's one other thing I'd add on this subject. One concept of Warren Buffett's that I used for a long time was the notion of the too-hard pile. If something important isn't clear to you pretty quickly, just put it aside and move on. I've rethought that. In the current day and age I'd argue that many times it's worth doing the work on the too-hard pile. That's where you may be more likely to get real insight before somebody else does. VII