

July 2020

Dear Fellow Investors,

Greenhaven's estimated returns for the second quarter exceeded +50%, more than markets have returned over many five-year periods. This quarter included three of the best months we have ever had in the eight-year history of the partnership. However, this return was also earned on the heels of the pandemic-driven March sell-off, when the partnership experienced its most challenging month by a factor of two. The net result is that both funds are up single digits for the year, comparing favorably to the Russell 2000, which ended June down -13% year to date. We continue to own zero businesses in the S&P 500. Your final statements from SS&C should be sent next week.

Investing during a pandemic presents an unusual set of challenges. If there is a rule book on how to invest at times such as these, nobody has forwarded it to me. Several managers I respect shared short descriptions of their approaches in the Q1 letter of the Partners Fund, our fund of funds ([linked here](#)). For me, investing in this period reminds me of when I began to learn to kite surf. I say "began" because I never got much beyond beginner level. Kite surfing is the sport where you strap a board to your feet, try to fly an enormous inflated kite 40 feet above your head, and harness the wind's updraft to lift your body out of the water, all while keeping balanced so that the momentum can pull you across the water. A proficient kite surfer makes frequent adjustments while managing the direction of the board and the position of the kite in order to optimize conditions. When you try to go from sitting in the water to skimming over it at 20 miles per hour, there are any number of things that can go wrong, such as having the kite too high or too low, not moving it enough, moving it too quickly or at the wrong angle, positioning your board poorly, and, of course, losing your balance, to name a few. If you only focus on your kite, you can risk dangerous crashes with others on the water. If you only focus on your board, you risk losing all momentum. Kite surfing is glorious when it's going well, but I was always hyperaware of the risks and, as a result, proceeded with fits and starts. My desire to fly on the water was tempered by my fear of crashing, which left me sitting in the water with the kite over my head as I tried to understand my shifting surroundings and pick my opportune spots.

I feel similarly about investing in the markets in the current environment. Companies are navigating an infectious virus, government policies, and customer reactions, all against an uncertain economic and logistical backdrop. We have high unemployment and unprecedented government response. We have changing policy responses and varying levels of compliance by citizens. These factors continue interacting and influencing each other – and evolving – with significant cross currents. There is both a reasonable case for falling interest rates and a reasonable case for rising interest rates. Price multiples are high but bond yields are also stunningly low. The range of potential outcomes is incredibly wide right now. So, what to do going forward?

I think the first step is to continue acknowledging how unusual the landscape is and that there will be short-term gyrations caused by factors that I am ill-equipped to predict or interpret, such as clinical trial results for experimental drugs. While pandemic developments such as infection rates, death rates, and drug status fill every news cycle, it is unlikely that the impacts of Covid-19 will permanently impair the prospects for our larger holdings. In fact, I continue to believe that in 10 years, when we look back at the price charts for many of our holdings, the first quarter of 2020 will be a pronounced dip on a generally upward-rising chart. As such, four of our current top five holdings were also significant holdings at the beginning of the year: PAR Technology (PAR), Digital Turbine (APPS), KKR (KKR), and SharpSpring (SHSP). Ultimately, I think we will be well-rewarded over time for holding on tight to these companies despite any interim volatility. Our major

holdings were the significant driver of returns in the quarter as both PAR and Digital Turbine more than doubled in value, recapturing losses from the first quarter.

In addition to holding on to our larger holdings, I made several new investments that are smaller in size but could have upside of 3-5X over time. These are attempts to take advantage of the extreme volatility in the markets and express my current view on the economy and the course of the pandemic. This opinion is, of course, subject to change on a moment's notice with the introduction of additional data. I believe that the most likely path is that a combination of improved treatments, progress on vaccines, modifications in behavior, lack of political will, and more stringent protections for the most vulnerable will result in our economy largely remaining open for the next year. Coupled with unprecedented stimulus for consumers, small businesses, and affected industries, this will lessen the pain of the virus and job losses. The drumbeat of economic news is likely to be progressively positive off the low base. So yes, earnings will be horrible and there will be waves of unfortunate new Covid cases, but investors are likely to look past them to an improving future. In my opinion, this does not mean investors should blindly buy the entire market. Rather, we should seek out pockets where the risk-reward may be more favorable.

One of these investments – certainly non-consensus, but consistent with a view that the world will largely remain open – is Gogo, Inc. (GOGO), an internet provider for airplanes. Understandably, as passenger traffic declined 90%+ and planes were largely flying empty, the share price was decimated by almost 80%, resulting in a sub-\$200M market capitalization at the time of our share purchases. To compound the risk, Gogo is highly indebted. This investment is not predicated on an immediate rebound in air travel, but, rather, the number of ways that the investment can “work out” and the potential payoff if it does. At cost, this is an approximately 1.5% position, so our partnership will survive in the case of a company bankruptcy. There are a few factors in our favor. The first, and perhaps most important, is that Gogo's CEO owns 30% of the equity and is highly incentivized to find a path that avoids bankruptcy and preserves the value of his largest personal holding. The second is that there are two components to the business: commercial and private. The commercial segment provides internet for passengers on commercial carriers like Delta and is closely tied to passenger traffic, and therefore was impacted severely by declines in airline passengers. The private/corporate jet segment is a net beneficiary of the pandemic as those individuals and companies with the means are using the lower risk private jets. These two businesses could easily be separated, and, in fact, there are scenarios where the private business is worth significantly more than the current value of the company.

If businesses were static, fossilized enterprises unable to change and adapt, Gogo would be a horrible investment. However, companies *can* change and adapt. To preserve resources in this environment, Gogo has furloughed 60% of its workforce and implemented salary cuts for remaining workers. They are renegotiating with suppliers and delaying equipment installs to preserve cash, and management has applied for government assistance under the CARES program, which could be very substantial. If air passenger travel remains depressed for five years and we are in a prolonged recession/depression, Gogo is unlikely to be a profitable investment. However, with \$200M in cash, a valuable private aviation division, and a highly incentivized CEO, there are several paths to a positive outcome, many of which likely would lead to multiples of our original investment.

Clothing retailer Lands' End (LE) is a less aggressive new investment that also seeks to take advantage of severe price dislocation. The partnership was actually short Lands' End a few years ago when the company embarked on an ill-conceived transformation from a casual to high-end retailer while also rolling out shops within the struggling Sears department stores. The Board had hired their new CEO from fashion house Dolce & Gabbana to run the pragmatic Lands' End

brand. The CEO did not move to Wisconsin, but rather opened an office in New York City and had the company participating in Fashion Week at great expense. I know almost nothing about Fashion Week, but I am highly confident there are better ways to spend marketing dollars for a catalog company that has the names, emails, and addresses of its long-tenured and loyal customer base. The strategy made no sense and did not work, and we closed out the short position after the “fashion” CEO was fired and they began to return to their brand heritage.

I took a new look at Lands’ End as an investment during the past quarter when Matthew Goodman of adoY Capital sent me a brief write-up noting that the share price was down more than 70%, yet more than 90% of the company’s revenues were from the online business and not directly impacted by Covid. Moreover, the brunt of the economic shutdown was occurring in a seasonally slow quarter for Lands’ End. Historical financials were negatively impacted by the company’s withdrawal from Sears stores and investments in online infrastructure, and were thus not necessarily indicative of their future profitability. The last Sears store closed in January, winding down almost \$200M of unprofitable sales from a few years prior. With just 25 physical stores compared to +\$1b in sales, Lands’ End is well-positioned versus peers who are battling much higher fixed costs and aged inventory collecting dust on the shelves. The market may be overestimating the impact of Covid on many companies, making them moderately interesting investment prospects. However, given that nobody really knows the path of the virus, that is not sufficient reason to invest.

What I find most attractive about Lands’ End is the current CEO, Jerome Griffith, who led the turnaround, IPO, and sale of the sleek, durable luggage brand Tumi. Despite cashing out \$50M+ when Tumi was sold to Samsonite, he passed on early retirement and moved his family to Dodgeville, WI to run Lands’ End starting in March 2017. He has aligned his interests by buying \$1M of stock and taking a significant portion of his performance pay in shares. More importantly, he is a very pragmatic leader who appears to be making logical, data-driven decisions, many of which have not shown up in the income statement yet. For example, he has begun to increase distribution through Amazon and is launching a partnership with Kohl’s that will see the full catalog on their website and a seasonal selection in 150 stores by September. There were more green shoots when the company reported May global e-commerce sales accelerated to double-digit growth year-over-year.

In 2017, the company laid out a five-year plan that implied cash generation in the range of \$100M per year. They reaffirmed this projection earlier this year (pre-Covid). Given the current state of the economy and consumer habits, Lands’ End may not reach its five-year plan on time, but given the quality of the management, the longevity of the brand, and the earnings potential, buying shares at an implied market capitalization of a bit over \$200M could work out quite well over time.

Other smaller “Covid-related” investments include a restaurant chain that should resume buying back copious amounts of stock as locations reopen, a building supply company that should benefit from the anemic interest rates, and a very complicated asset manager. These are not “bet the farm” situations, but are small investments that may yield high returns.

As the quarter progressed, like kite surfing, I invested in fits and starts. One larger investment made during the quarter was APi Group, which we purchased ahead of the company joining the Russell 2000 index at the end of June, and the forced buying of 20+ days of volume that would accompany that event. This was opportunistic and I felt attractive on a risk-reward over a very short timeframe. The situation had the added benefits of company operating in stable end markets and trading at a discount to peers. With APi Group, I could be wrong about the direction of the virus and still generate returns. However, the point of asking for long-term-oriented capital is to find situations where Greenhaven can grow our collective capital over long periods of time. In the world of kite surfing, APi was the equivalent of catching our breath and trying not to get creamed by any of the obstacles. However, to stretch the kite-surfing metaphor to the point of breaking, we want to



catch the wind of great management teams and just hold on. People who can build businesses with aligned incentives can navigate pandemics. If we can exit the pandemic owning one or two new durable companies or backing one or two great management teams, I will feel very fortunate.

## **NEW INVESTMENT: IAC HOLDINGS (IAC)**

IAC Holdings (IAC) could be the first great company/management team that we invested in during the pandemic. If such monuments existed, Chairman Barry Diller would be on both the Mount Rushmore of business builders and the Mount Rushmore of capital allocators. Since 1995 he has compounded capital at higher rates than Berkshire. To be fair, Warren Buffett has the burden of large numbers; growing a \$400B enterprise like Berkshire Hathaway by 30% means generating an incremental \$120B of value, which is the approximate combined market capitalization of the bottom 30 companies of the S&P 500 – no small feat in any year, let alone every year.

Media and internet conglomerate IAC has a long history of acquiring and nurturing companies. Past IAC spinoffs include Expedia, Ticketmaster (now part of Live Nation), LendingTree, Interval Travel (acquired), HSN, and Tripadvisor. IAC's market capitalization is still hovering around \$10B because the company keeps spinning off their valuable assets. Thus, the company is still sufficiently small that high rates of compounding are possible.

On July 1, IAC shrunk again by spinning off Match.com (which also owns Tinder) to shareholders. Prior to that date, the Match.com shares represented approximately two-thirds of the value of IAC, so investing in IAC required a positive view on Match/Tinder. Now IAC is a much smaller company and therefore much more of an investment in Barry Diller and IAC's brands, including an ownership stake the ANGI Homeservices (ANGI) platform, which matching property owners with home improvement contractors. We began buying before the spin-off and grew IAC into a top five position on July 1.

Our cost basis is approximately \$103/share, which was less than the value of IAC's ANGI shares, cash, and exposure to Care.com on July 1st.

<b>Holding</b>	<b>Per Share</b>
ANGI (4.98 shares at \$13.09 July 1 <sup>st</sup> Close Price)	\$65.19
Cash	\$44.81
Care.com (at cost)	\$5.90
	<b>\$115.90</b>

But wait, there is more. By investing in IAC, we also receive Vimeo – a global video sharing platform with ~1.3mm paid subscribers, Dotdash – an online publisher with 90mm+ monthly users, and Applications, which is comprised of 40 mobile applications and 155 browser extensions. The Applications basket includes Apalon (mobile development company with 25M monthly users), Ask Applications (distributor of desktop applications with 60M monthly users), Daily Burn (membership-based fitness platform with 1.7K curated videos), iTranslate (more than 100M app downloads), Mosaic Group (3.8M paying subscribers), and RoboKiller (blocks over 1.1M telemarketers).<sup>1</sup> IAC also owns a \$250M investment in car-

<sup>1</sup> Source: UBS

renting platform Turo in 2019. This currently may be worth less than the original investment because of reduced demand for travel, but Hertz is in bankruptcy and we have effectively paid zero for this lottery ticket. Various sell side firms put IAC's "sum of the parts" value at \$150+. Unlike many "sum of the parts" situations where cash is largely static, given the disruptions in the economy and funding markets, now is an interesting time to ride shotgun with Barry Diller and billions of dollars in cash, especially given his history of turning cash into enterprises that are valued on multiples of sales. The smaller company size, level of talent, and large cash balance provide a lot of optionality, while the cash and valuation provide downside protection.

## TOP 5 HOLDINGS

**Digital Turbine (APPS)** – This has been a top five holding for well over a year. In the last quarterly letter, I wrote, "New phone activations will be impacted in the short term, but I am not ready to bet against humanity's love of having a device in their hand, or advertisers' desire to reach those consumers. Digital Turbine is positioned for revenue growth, margin expansion, and multiple expansion, despite what the share price said on March 31st." The price has more than doubled since the end of March, making APPS a very positive contributor to Q2 performance. Digital Turbine's primary business has been brokering "app slots" on smart phones. Demand continues to rise for the limited number of slots, so revenue per device rises, which is hugely beneficial to the company. To management's credit, execution has been superb. They have signed up the largest carriers (Verizon, AT&T, Telefonica) and the largest advertisers (Amazon, Netflix, Disney+), they have introduced new products and new pricing models, and they have allocated capital very well with the recent acquisition of Mobile Posse, which was accretive and dramatically increased their recurring revenue base. This management team may lack some of the fancy pedigrees and reputation of some of today's "high flyers," but if you step back, their execution has been phenomenal.

**KKR (KKR)** – If there were ever a business that could survive a global pandemic, KKR is it. They have a fortress-like balance sheet with almost half the share price covered by cash and investments, a capital base of more than \$200 billion that is locked up well beyond when a vaccine should be available, and a highly variable cost structure. The management team has been very aggressive investing during the pandemic, putting in excess of \$12B to work with large investments like their purchase of the commercial beauty business from publicly traded Coty, their carve-out of a waste business from the British firm Pennon, and a €3 billion takeover of Spanish phone carrier MasMovil Ibercom. The transactions are notable because they are large and took place in three different countries and three different industries. On July 8, KKR announced the agreement to purchase insurance company Global Atlantic. This is a meaningful strategic move that will increase their permanent capital base dramatically over time, making the foundation even more rock solid.

These are A-players playing a game where the odds are tilted in their favor. Heads they make some money; tails they make a lot of money. With endowments and others trying to generate high single-digit returns in a world of negative interest rates and volatility in the public markets, the siren song of private equity sings loudly. Even during the pandemic, KKR has been actively raising more than \$10B. The company has scale, expertise, and secular tailwinds. Over time, the balance sheet will compound, while management fees and incentive fees should continue marching higher – driving earnings higher along the way.

**Elastic (ESTC)** – I wrote about Elastic software in detail in the Q4 2019 letter, and the holding has since appreciated its way into the top five position. As a refresher, Elastic is an open source software company that enables users to search

through structured and unstructured data for a range of consumer and enterprise applications. Quantitatively, it is the most expensive company that we own at more than 14X revenue, but it is also the most impressive on a variety of metrics, including net revenue retention above 130%. Further, in a quarter that included two of the most economically challenging months of the last 50 years (March and April), Elastic grew sales an astounding 57% year-over-year. In eight years and with minimal capital, the company has grown from an open source project to over \$500M in sales.

When I graduated from business school, I worked for John Doerr's New Schools Venture Fund. John's day job was a venture capitalist at Kleiner Perkins, where he used a "mercenary or missionary" framework for evaluating CEOs. He spoke about the differences in this video ([Link](#)). To be clear, both types can be successful, but he had a strong preference for missionary CEOs. I realize that some may roll their eyes at the potential fluffiness of the concept, so it may have more gravitas when you consider that the person he held out as the prototypical missionary CEO in the early 2000s was none other than Jeff Bezos, who is now the richest person in the world (even after his divorce).

At New Schools, my job was to source and diligence potential investments in the education sector. I believe that Shay Banon, Elastic's CEO, is a missionary CEO trying to advance the open source software movement and the power of search. There have been dozens of difficult decisions to further these ends, many of which have negative short-term economic impacts but have resulted in a very large and supportive user base. Shay has repeatedly delayed short-term gratification, making key features available to the free users. He is also investing very heavily in R&D, devoting more than 35% of revenue to development alone. These investments have allowed the company to expand into security, monitoring, and now enterprise search.

The company has a substantial asset that does not appear on the balance sheet: a large base of non-paying users. Since Elastic is an open source software company that offers free versions of the software, there are very likely more than 50X non-paying customers for each paying customer. Now, many of the non-paying customers will never convert, but over time, Elastic is adding features to the paid versions that should nudge non-paying over to paying, especially given the loyalty that the company has inspired. A missionary CEO, a mission-critical product, a history of under-monetizing and significantly investing in future products is a very attractive set-up for investment.

**PAR Technology (PAR)** – We have owned PAR for well over a year and I have written about it extensively. Their "jewel" business is the restaurant Point of Sale (POS) software for QSR (quick service restaurants). As the pandemic unfolded and shutdowns spread, PAR's share price was decimated, falling as low as \$9.62 in March after starting the year around \$31. One might assume that with a 70% decline in share price, PAR's restaurant software and customers were on their way to extinction. However, QSRs that primarily do drive-thru and take-out business have held up quite well. In fact, PAR's churn (customers who cancelled the software) went DOWN year over year. The pandemic has highlighted the value of a modern POS system that integrates with delivery systems like Uber Eats and enables mobile app ordering. Restaurants with a modern POS actually have a revenue advantage. PAR's pipeline has a shadow backlog of restaurants to sell into/install that is almost as big as their current installed base. In addition, because the POS is the spine of the restaurant operations, they have the opportunity to integrate with other functionality such as inventory management and scheduling. PAR should continue to grow locations and revenue per location as they add additional functionality. It is a matter of time before PAR sells off its ancillary government business and gets further scale and becomes a cleaner SAAS story, likely concurrent with another software acquisition, and likely multiple expansion (higher share price).

I believe that PAR will exit this traumatic period as a net beneficiary. CEO Savneet Singh struck a bullish tone in his annual shareholder letter where he wrote, “So much of success is driven by being in the right market at the right time, we believe we’ve focused PAR into the right market. Said differently, our focus towards restaurant software at PAR is choosing to fish in a very shallow pond with a very large net. While we believe Brink POS is a special product, there is an industry tidal wave of fish flowing right into our little pond.” I believe that he is correct.

### **SharpSpring (SHSP)**

As a board member, I am limited in what I can say; however, I would point out that quantitatively, SharpSpring is one of the least expensive SAAS stocks at sub 4X EV/Sales for a company that has guided to growth in excess of 30% this year. If you have other companies that are cheaper with a similar profile that you are excited by, please send them my way.

### **SHORTS**

We ended the quarter short the ETFs of major indices, a hotel chain, a no-growth business with a nosebleed valuation, and a company in the process of being acquired.

### **ADMINISTRATIVE/ANNUAL MEETING**

At this point, it seems premature to put a date on the calendar for the annual meeting. The most likely scenario is we delay until early 2022 and go virtual if absolutely necessary. In any and all circumstances, we will record the event for limited partners, since that was effective and appreciated last year. At the end of last year’s meeting, one LP remarked how smart and engaged the LPs were as a group. He also said that he was an investor in another much larger fund that had a tradition of asking annual meeting attendees to write down their best investment idea for the next year. The ideas were collected and the person who submitted the best-performing idea got a nice, if somewhat silly, trophy at the following year’s meeting. I was hearing about this as folks were trickling out of the room, so it was impossible to implement at the time. but the idea stuck with me. We may be waiting for the annual meeting, but I do not want to wait to try this concept. Feel free to submit an idea to [investorrelations@greenhavenroad.com](mailto:investorrelations@greenhavenroad.com) – please limit your summary to 100 words and put “2 BAGGER” in the subject line. Ally will track the submissions and I will look at them for investment purposes. When we meet, the winner will be announced, a quirky trophy presented, and glory shall be conferred.

### **OUTLOOK**

It has been a very unusual period. On the days record job losses are announced, the market rallies. On the days of riots in the streets, the market rallies. China retaking Hong Kong has not registered with equity investors. No matter how you measure it, the unemployment rate in the United States is up multiples from a year ago. There is an enormous gap between the “real” economy and the stock market. In the long term, there should be a relationship, however, in the short term there can be significant divergences, which also can be exacerbated by very low interest rates. Is buying a company at 40X earnings with a 2% dividend yield so much crazier than buying government bonds that yield just over one-half of 1%? The divergence between the economy and the market can also be partly explained by the five trillion dollars



(\$5,000,000,000,000) in stimulus that has been provided so far. This equates to roughly \$40,000 per U.S. household. I realize it is not distributed evenly, but it is the two-thirds of annual household income. It would be out of character for our president to turn off this spigot right before the election, or, to put it another way, more stimulus is coming. I believe the market marches higher, but we really are just looking for a couple of great opportunities per year.

Just as I have ended many of our letters... as volatility arises, I will attempt to take advantage of the opportunities it creates. We will continue to invest with a long-time horizon, and we will continue to invest like it is our own money – because it is. Thank you for the opportunity to grow your family capital alongside mine.

Sincerely,

Scott Miller





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