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# FRAZIS

## • CAPITAL PARTNERS •

### December Investment Update

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Dear investors and well wishers,

The fund had a tough December down 12.4%, which also knocked our calendar 2021 number to -12% and net return since inception to 17% per annum. Our two-year return is +83% and our three-year return is +127%.

I'll host an update next Tuesday morning at 11am Sydney time, please [register here](#).

We are in the middle of one of those extraordinary periods where valuations collapse and investor time frames have shortened from years to days. Long term plans are forgotten and the whole market is focusing on where prices will land tomorrow.

At periods like this extraordinary transfers of wealth take place. As with similar shocks in March 2020, Dec 2018, and 2008/2009, those liquidating shares will realize sharp short term losses, while the immense long term wealth created by fast-growing technology companies over the coming years will flow to those who hold or buy.

A number of indications suggest things have reached the kinds of extremes that lead to buying opportunities.

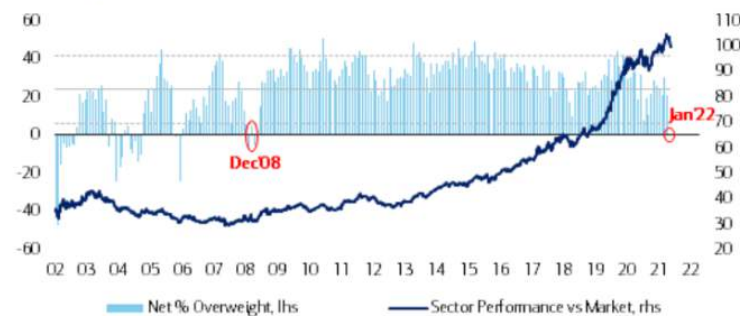
Over 40% of the Nasdaq is now down more than 50% from one-year highs, which includes many of the best companies in the world, and many of those likely to generate the highest returns over the coming years.

The rolling quarterly new lows in technology is now as high as it has been since Lehman collapsed in 2008, a generational buying opportunity.

The performance of technology over the following decade was phenomenal, painful though it was for everyone holding tech shares at the time. Tech bottomed several months before the rest of the market, and then pushed to significant new highs. We saw this dynamic in March 2020, when our fund sold off well before the market - and much harder too - only to recover long before the indices and push to major new highs.

**Chart 2: Tech net allocation fell to the lowest level since Dec'08**

Net % OW Technology



Source: BofA Global Fund Manager Survey

BofA GLOBAL RESEARCH

Life sciences saw the worst of it, with a number of companies selling down to below cash levels. Multi-year projects are out of favour right now, to put it mildly. Some of this was deserved - but multiples are now at extremes that marked or exceed previous lows.

Fortunately many of these companies raised money or IPOd recently, so we can all

be grateful that scientific progress will continue.

There's a narrative around rates and quantitative tightening causing the sell-off. There is some truth to this, but a better explanation is that institutions, as they did in March 2020 and 2008/2009, have rushed to the exit, swinging from max overweight to max underweight technology (as measured by data above).

Goldman Sachs reported the heaviest tech selling in over five years and that was earlier on in the sell-off.

This institutional shift, combined with rising short selling and no doubt some level of retail panic (data on that is harder to come by) is both causing the current volatility and creating opportunity for longer term investors to take the other side.

Ofcourse, the most important thing is not to participate in mass selling, and where possible, take advantage.

All the gains from the growth in life sciences, software, fintech, and e-commerce will flow to those who end up with the shares being dumped on the market now.

The most important thing to know is that our companies are still performing exceptionally well.

Many of them are internet-based so we can track real-time data, and they have made substantial progress since the sell-off began, and most certainly since the highs of early 2021. Strikingly, this sell-off has not been triggered by any operational issues. For example:

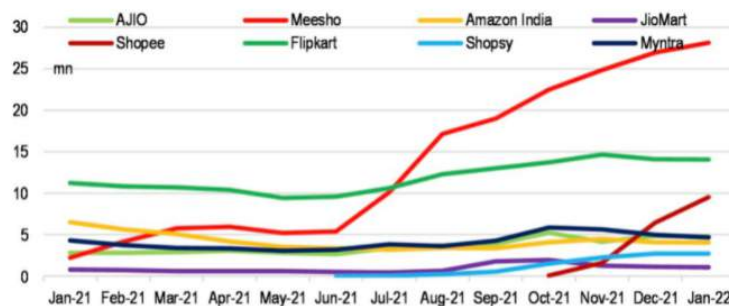
### Sea

In November only two long months ago, Sea reported:

- 122% year-on-year organic revenue growth
- 148% growth in gross profit
- GMV at a \$67 billion run-rate, a 1.3x Sea's enterprise value
- A \$2.9 billion EBITDA run rate for gaming, though growth here has moderated to 29% year-on-year
- 120% growth in users of Sea's payment app, up to 39 million mostly young emerging market users,
- And in addition, Sea entered India, and was the most downloaded app in South America, and entered Europe through Poland, Portugal, France, and Spain.

So far, indicators suggest Sea's e-commerce app Shopee is doing even better in India than it was in Brazil, where it quickly became the most downloaded app and already accounts for ~8% of Sea's GMV.

After their October launch, Shopee is already the third largest shopping app in India by daily active users.



Source: Apptopia

Despite these results, the stock dropped 55% since November, which is why we see this as a positioning/valuation unwind rather than any fundamental issue.

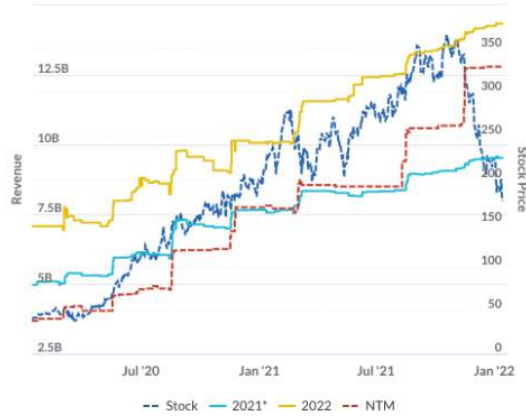
The main negative news was that Tencent, a major shareholder, sold a small portion of its holding below 10%. But even this has a silver lining - as it allows Sea to avoid foreign ownership restrictions in India.

In September, Sea raised \$6 billion of capital at \$318/share (currently \$167) leaving the business with \$11 billion of cash and a current enterprise value of \$88 billion.

If you separate the two businesses, and value payments at zero, this is one of the cheapest e-commerce companies around, as well as the fastest growing and most

cheapest e-commerce companies around, as well as the fastest growing and most dominant at this scale. As with many of our companies, Sea is truly an apex predator, entering new markets and rapidly taking share, forcing competitors to react.

Throughout the sell-off, estimates have been consistently revised upwards:



This mix of expanding TAM, >100% organic growth, market dominance, upgraded guidance, and a >50% sell-off is a compelling recipe and we have added to the position over recent weeks.

### MercadoLibre

Similarly to Sea, fundamentals remain extraordinarily robust.

In MercadoLibre's 3Q21 result, net revenues grew 73% and their net take-rate reached an unprecedented level of 16.7% as they offer additional services to their immense and rapidly growing userbase.

Both MercadoLibre and Sea have vast, barely monetized audiences, and have barely started offering advertising, a high margin business that could add up to 3% to their take rates.

MercadoLibre is now at 10 year valuation lows.

It has sold off to these levels multiple times, and no doubt each time investors were thinking, 'why on earth am I in this stock, it's down 50%! What an awful company, and what a mistake.'

And each time, the difference between realising a substantial loss and extraordinary long-term profits was steadiness, consistency, and following the fundamentals.



Despite excellent progress and a substantially derisked business from years past, MELI fell 47% to valuation lows.





MercadoLibre share price over 10 years. In the past those that panic sold at valuation lows - precisely where we are today - realised painful short term losses and missed out on exceptional long term gains

### Twitter

As with most of our universe, Twitter is now down well over 50% from all time highs, just as revenue is accelerating under new management.

This was our largest new position and we have continued to add over recent days.

The stock trades at 4.3x 2022 sales, with revenue growing at ~40%, and 17x EV/EBITDA, with EBITDA forecast to grow at 125% this year.

On an EV/Sales basis, Twitter is now approaching COVID panic lows.

Their semi-addicted userbase of 211 million daily active users (which for better or worse I count amongst) grew at 11% year-on-year. From these levels we expect this to be one of our best performers over time.



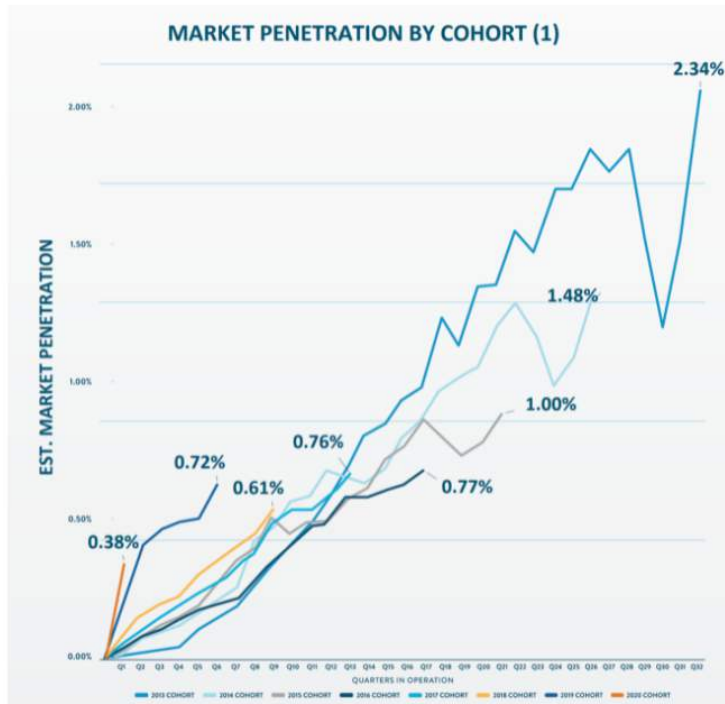
### Carvana

We purchased Carvana at \$36 and it's now trading at \$156 - but this doesn't feel like a win as the stock is now down 60% from its high only a few months ago. This has brought its EV/Sales below its long term average, right as the company has posted its first two consecutive quarters of profit.



The second hand car market is substantial, larger than luxury goods, fashion and electronics, and Carvana still has 41% share.

electronics, and Carvana still has 11.7% share.



Carvana remains such a small part of the market that it could grow even if the second hand auto market declines.

In recessions second hand autos are less cyclical and more resilient than new cars as cash-strapped consumers trade down, softening the blow from reduced overall demand.



This was one of our original customer love and explosive growth plays, and they continue to execute on both.

## DELIVERING SUPERIOR CUSTOMER EXPERIENCES

**4.7** ★★★★★ Rating <sup>(1)</sup>

**122,000+** Customer Reviews on Carvana.com <sup>(1)</sup>

**96%** Would Recommend To A Friend <sup>(2)</sup>

**84** Net Promoter Score (NPS) <sup>(3)</sup>

“Carvana will change the way you buy cars so...”

“Carvana is the bomb!”

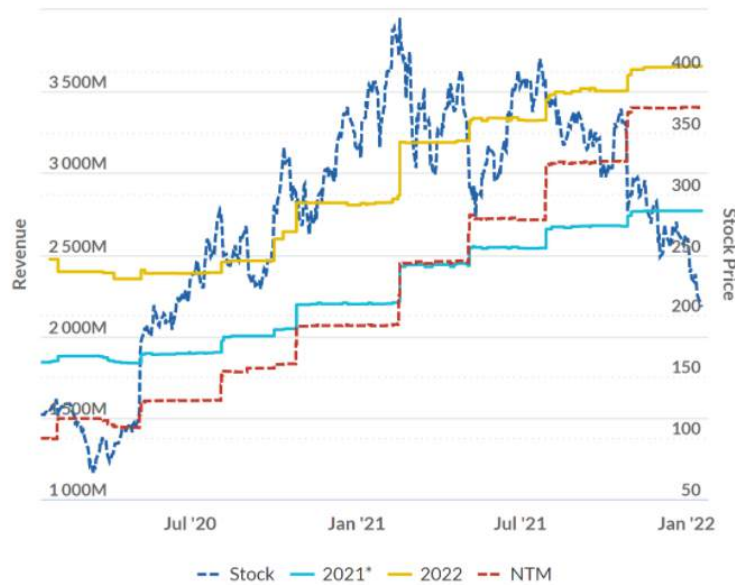
“Never thought car buying could be enjoyable.”

**GROWING UNITS & REVENUE**

### RAPID SECULAR GROWTH

CARVANA





*Consistent improvement in revenue and KPIs*

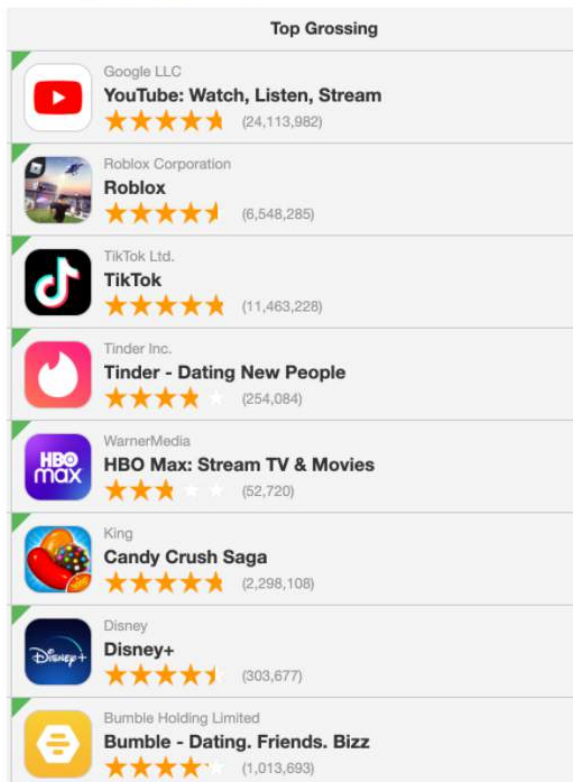
Ofcourse, those that sold in the long 54% drawdown in 2019-2020 realised a heavy loss. The difference between a 100% gain and losing more than half your money depended simply on patience and following the fundamentals.

We actually sold the bulk of our position at much higher levels in 2021, and have used this sell-off to rebuild Twilio to a substantial position.

**Roblox**

Perhaps not surprisingly, companies with the most true customer love like Roblox and Tesla, fared the best.

Roblox has been the number one grossing app in the iPhone store, ahead of stalwarts like TikTok and Tinder.



Without wanting to labour the point too much, in November Roblox reported 109% organic revenue growth and daily active users growth of 31% on tough coronavirus comps.

The stock is down 45% since, representing a remarkable opportunity to own a company that is well on its way to being one of the top global brands.

## What happens next?

The inflation impulse that triggered these moves is already starting to recede in the US, with shipping rates down and container congestion at ports starting to ease.



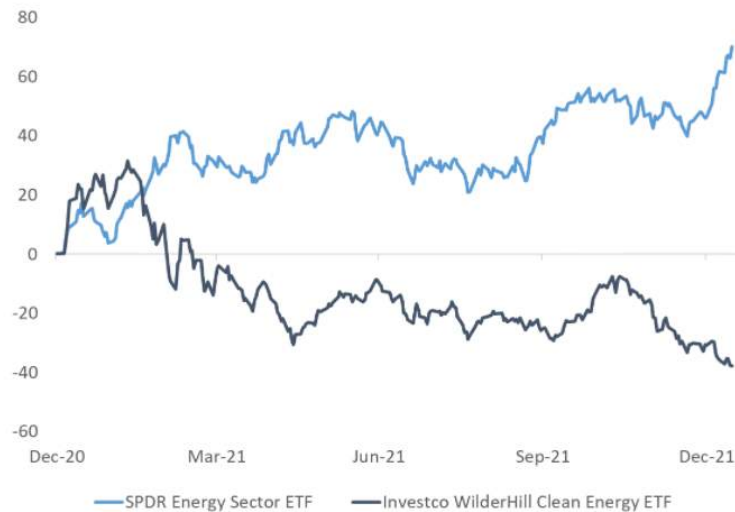
The biggest risk may turn out to be energy prices which are rallying hard, as the well-intentioned ESG movement has led to chronic underinvestment in the West.

Nevertheless, supply has started to react to higher prices, albeit slower than usual, and some analysts suggest the market could shift from deficit to surplus as early as the end of this quarter.

Interest rates could also peak surprisingly soon, and should markets deteriorate the Fed has now given itself plenty of room to soothe concerns, which would leave the institutions who just sold out of technology offside.

I doubt anyone will forget the damaging 2008 energy rip at the peak of the GFC, and people still talk about the energy crisis of the 1970s. Energy is ultimately a tax that we all have to pay.

### Oil and Gas has significantly outperformed clean energy



The investor washout has created significant opportunity in renewables, an industry with significant tailwinds from consumer demand, Governments around the world, and now higher oil prices.

Higher energy prices don't affect many technology companies directly, but they do affect the macro winds buffeting long duration assets.

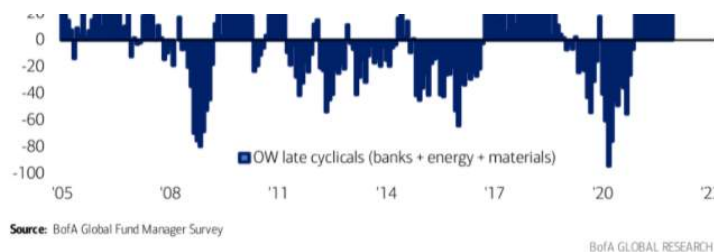
If you're wondering where the record flows out of tech have gone, they went into late cyclicals.

You have to rewind to 2008 to find flows out of tech this large - and the subsequent forward returns were exceptionally strong. Similarly, when flows reached this peak in cyclicals, forward returns for that sector were uninspiring.

**Chart 19: Highest allocation to late cyclicals ever**  
Net % OW late cyclicals (banks + energy + materials)







*Fund managers have liquidated their tech holdings en masse and piled into late cyclicals*

Ultimately, fast growing tech companies will perform in almost any environment, even as share prices are battered at times like today and March 2020 by macro concerns.

I suspect three considerations that will determine the near term direction of markets:

- market sentiment and positioning,
- valuations, and
- the actions of the Fed

The first two have now swung decisively in our favour, as shown in data from prime brokers at Goldman, Morgan Stanley and BofA. Valuations have approached and in many cases exceeded the liquidation lows of March 2020 and Dec 2018, from which our stocks quickly recovered then made significant new highs.

The Fed is still a headwind, though there have been rising rate environments throughout the last ten years (and multiple rotation/liquidation events), and looking back, these all represented excellent opportunities to buy rather than sell.

In March 2020, our fund was perhaps the worst fund to be in. Our two largest positions both dropped 75% in short order.

Short interest exploded in all our investments, institutions liquidated, and markets probed a deep, deep low.

Only a few months later, we had not only made back the drawdown, but posted a 39% net gain for the financial year, and that was the beginning of the rally. We ended up advancing several times off similar valuation lows we find ourselves at today.

As in the examples above, the difference between serious losses and returning multiples of your capital depends entirely on whether you are a buyer or a seller at times like this, which always feel like an eternity when you're in them.

Clearly, we could have sold more in February last year, and in the future we may expand our universe to include larger cap names in tech and healthcare which can provide ballast when markets sell-off.

However, now is not the time to make those changes. As they were in early 2016, late 2018 and March 2020, our fast growing companies may be both the worst place to be during the sell-off, and the best place to be after markets put in a low.

This happens well before people expect, and we are starting to reach consensus bearishness reminiscent of those times, as well as a level of seller exhaustion.

In previous sell-offs, reporting season marked a turn as investors refocused on the substantial progress our companies had made, often growing 10-20% over the prior three months with improving economics.

There is a very good reason to be invested in these kinds of companies. The bulk of investment returns over the next five to ten years will come from these sectors, and accrue to the companies growing and taking market share - the apex predators. We will be fully invested throughout and catch them in their entirety.

Best wishes  
Michael

If you'd like to invest with us, you can access our investment portal and fund documentation through the button below, or simply reply to this email and we'll be in touch.

[Invest](#)

**Please note:** We are now taking applications weekly, so if applications, funds and supporting documents are received by 2pm on a Friday, the investment will be priced for Friday COB / Monday morning start. We are also available on Netwealth, Hub24, and other select platforms.

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