SYMMETRY INVEST A/S

Newsletter

H1 2022

SYMMETRY INVEST A/S

CVR: 35056467

The purpose of this Newsletter

Every month, Symmetry sends out a portfolio update to the shareholders. In them, we report the last month's return, news regarding our investments, and much more. In addition, we send out write-ups and a yearly investor letter analyzing our biggest positions. This newsletter will not replace our copy of the above-mentioned activities, since they are issued exclusively to Symmetry's shareholders. The free newsletter will therefore to a very limited extent be able to reflect on individual holdings, as this is reserved for our shareholders. Instead, this newsletter will touch upon general trends and developments in the markets and explain how Symmetry navigates them.

The newsletter will from time to time discuss specific stocks in which Symmetry could have a long or short position in, or no position at all, but an interest in.

The newsletter aims to increase awareness of Symmetry for all our stakeholders, including current investors, potential investors, and others who follow the stock market. Symmetry will continuously describe our strategy and make it as easy to understand as possible for readers.

We will, among other things, include quotes from well-known value investors and substantiate claims with graphs and other material that can be used to support our point.

We hope that as many people as possible will find the material useful and easy to read and that it will help sign up new people to the newsletter to follow us.

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Stocks commented on in the newsletter should not be construed as a buy, hold, or sell recommendation of the stock in question. Symmetry is a registered manager of alternative investment associations (FAIF) with the Danish Financial Supervisory Authority. Symmetry is NOT a registered/authorized investment advisor and on this basis does not provide any recommendations on specific shares. The newsletter exclusively describes Symmetry's viewpoints on the market and individual shares.

Under no circumstances is Symmetry liable for losses due to investments based on the use of the newsletter. Symmetry will, in some cases, owns shares in companies mentioned in the newsletter. Symmetry reserves the right to buy or sell shares in companies mentioned without further notice. Our opinion or price target for shares may be changed on an ongoing basis after the publication of the newsletter. We are not obliged to provide updates on them.

Investing in shares is associated with high risk, and it is therefore always recommended to consult a competent financial adviser beforehand. Images and other material used in the newsletter are copyrighted and may not be redistributed

In the newsletter we mention "us", implying Symmetry, and sometimes "I", implying Andreas Aaen.

The data comes from unaudited figures and may therefore be subject to uncertainty. The figures come from extracts from Symmetry's custodian banks, etc. and it is our best belief that they represent factually correct numbers. Return data and net asset value are audited once a year by the company's auditor at the end of the year.

Newsletter

In this newsletter, we will look into how to handle the "terminal value" in "pre-scale investments" as well as looking into how our shorts have helped to protect our returns YTD.

H1 2022:

Table: Historical return in percentages

The table shows historical returns and the funds net exposure since its foundation in 2013

%	Jan	Feb	Mar	Apr	May	June	July	Aug	Sep	Oct	Nov	Dec	FYTD	Avg. Net Exposure
FY13						8,1			7,9			15,0	**34,1**	N/A
FY14			3,2			10,2			2,8			17,0	**36,8**	N/A
FY15			6,8			23,2			-13,3			5,7	**20,5**	76,0
FY16			1,3			10,6			3,5			3,4	**19,9**	44,3
FY17	6,2	3,2	0,7	4,0	5,1	-2,7	1,1	-2,7	0,6	3,3	-2,1	-0,7	**16,8**	46,5
FY18	1,9	-4,5	-4,4	0,8	-0,8	-5,9	-4,5	-1,8	-0,9	-12,8	1,9	0,3	**-27,7**	75,2
FY19	7,3	6,4	4,5	4,5	-2,4	6,3	0,5	-7,1	5,8	0,3	10,0	2,5	**44,4**	73,3
FY20	2,0	-4,1	-37,2	22,6	14,5	10,1	1,2	9,0	-0,2	1,8	17,1	12,9	**40,4**	74,9
FY21	9,0	8,3	8,0	5,0	0,1	-0,5	2,2	4,8	-2,7	3,9	-5,3	0,9	**37,8**	75,6
FY22	2,0	-6,0	-2,3	-7,0	-1,0	-3,7							**-16,9**	71,7

As always, returns and portfolio updates are sent to shareholders on a monthly basis through the website.

Table: Performance compared to MSCI ACWI

Below is our long-term and short-term performance compared to MSCI ACWI and Euro Stoxx 600

	2022	Total	IRR
Symmetry	-16,9%	418,8%	19,3%
MSCI ACWI	-18,5%	99,3%	7,7%
Stoxx 600	-16,5%	41,5%	3,8%

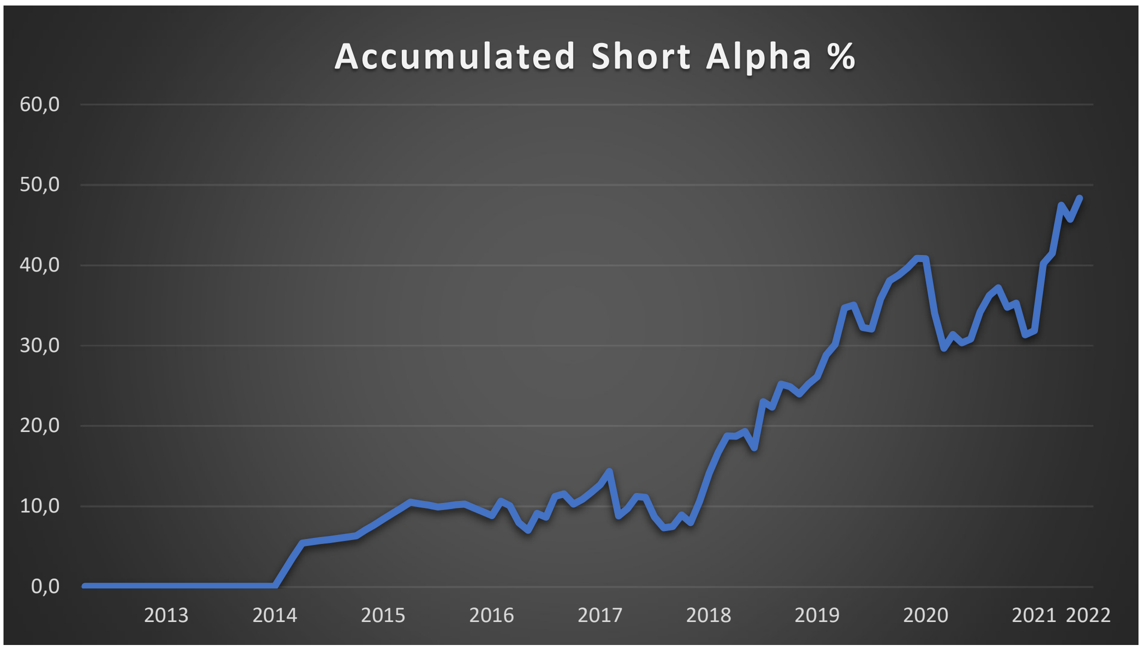
Our returns in the first half of 2022 have been satisfactory without being good. We can never be satisfied with us losing a double-digit percentage. This despite the fact that we have outperformed most relevant benchmarks and several of our peers. The reason for our above-average returns have not come from better stock selection on the long side. Our relative alpha has instead come from our shortbook and hedges that have performed extraordinary well. This is after a 2021 that was quite hostile to short selling and where we underperformed on the short side and outperformed on the long side. As managers of others people's money, it is our responsibility to detect changes in the market sentiment and react on this. To deliver great outperformance over time we must make sure we stay in the game during bad times. In that sense we are feeling okay with the start of 2022 as we have managed to protect the downside of our portfolio despite beating significantly on the upside in the last 3 years. Now we are trying to position ourselves for the next leg upwards.

Shorts:

We are as mentioned before not totally satisfied with our returns for the year. This is because our long book has lagged the general market as it has declined 26 % YTD compared to only 18 % for the market. This is not acceptable in our view even if it can be explained by normal volatility.

The only reason we have kept up with the market this year has been a stellar performance in our short book. As we mentioned in our FY21 annual letter, last year was a hard year to keep a short book.

We showed the below graph in our FY21 annual letter – Here it is updated with YTD 2022 alpha as well:



In the first 6 months of 2022 our short book declined on average with 37 %. This is double the amount of the general market at 18,5 % and thus represent high alpha. This has been one of the best markets for individual short selling for the last 10 years. Shitty companies finally went down and covid-winners followed. Our short book today is lower in size than going into the year. We are still finding good opportunities but is aware of not taking excessive risk in a pullback scenario for the overall market.

This is not the whole story of our hedges. Besides individual single name shorts we have also run several market hedges. In 2021 we started to identify idiosyncratic risks in our portfolio and focused on market valuation, inflation and interest rates. On that background we have this year profited from short positions in 20-year US bonds, short positions in HY ETF's, long positions in commodities and put options on the Nasdaq to name a few.

We have slowly scaled down our short positions and hedges to reallocate more resources to some of our longs.

Terminal value risk in pre-scale investments:

Something I have started to appreciate more over the last 12 months is how difficult it is to value terminal values in a model. This is especially the case when we have to consider if the terminal value even exists. We have seen companies like Carvana being valued at 20-30x 2025 EBIT multiples, while months later people question if Carvana even exists in 2025. We have also felt that pain on our own body with our investment in Naked Wines. At one point it was only a question how much of the TAM they would capture – only to see the stock decline 50 % in 2 days and the question being if they will survive the next 12 months.

There has been a lot of companies that just burned money because they were "investing for growth". But now when the growth has stopped the losses have not turned to profits. In most cases the losses have just widened even further. Many of these companies never had good unit economics in the first place and therefore never had a way to become profitable. The other issue is that most management teams have never experienced other environments than to just burn money. It requires a totally different mindset to lay off people and do share buybacks than to hire people and raise capital. Only few CEO's can manage and be good at both.

While we won't exclude the possibility of investing in companies without a finished moat in the future, we will be more skeptical around them and use a more conservative valuation approach. Symmetry has over the years made many successful pre-scale investments. When we first invested in JDC Group, they had only signed the first LOI with Provinzial and was around breakeven on an EBIT-level. Today they are rolling out with huge distributors around Germany and is seeing their margins expanding rapidly. The moat is quickly being build. This gives us comfort to start raising the exit multiple we have on the terminal value. It was the same situation with Franklin Covey. When we invested, they were still early in the AAP transformation and was barely cash flow positive. Today they have increased the free cash flow manyfold and AAP is the vast majority of the revenue. FC therefore deserves a high multiple now.

There are many business models that deserves to trade at high multiples if they win their market and builds a moat around their business. But we have all learned the last 12 months that unfortunately its only a fraction of the total companies that ends up doing that. While we also in the future will work hard to identify the companies that will end up building this moat, we need to have more respect for the variability of the outcome. We have therefore internally started to use lower multiples on pre-scale investments and then increases the multiple while the moat is being build.

Fortunately for Symmetry we have always stayed quite disciplined on valuation metrics and have tried to avoid paying to much for a stock. In retrospect there have been stocks where we did pay to much, but fortunately for us this was always in some of our smaller positions. Our largest positions are growing rapidly still, but in comparison to the 2020/2021 stock darlings our stocks are profitable and is trading at low multiples.

We will mention some of them below:

Portfolio update:

Despite the fact that it has been a volatile year so far, we have not made many changes to our long book. We have used imbalances to reallocate our positions but overall, we are mostly long what we owned going into the year. We have been more active on the short side and profited on a lot of broken stories.

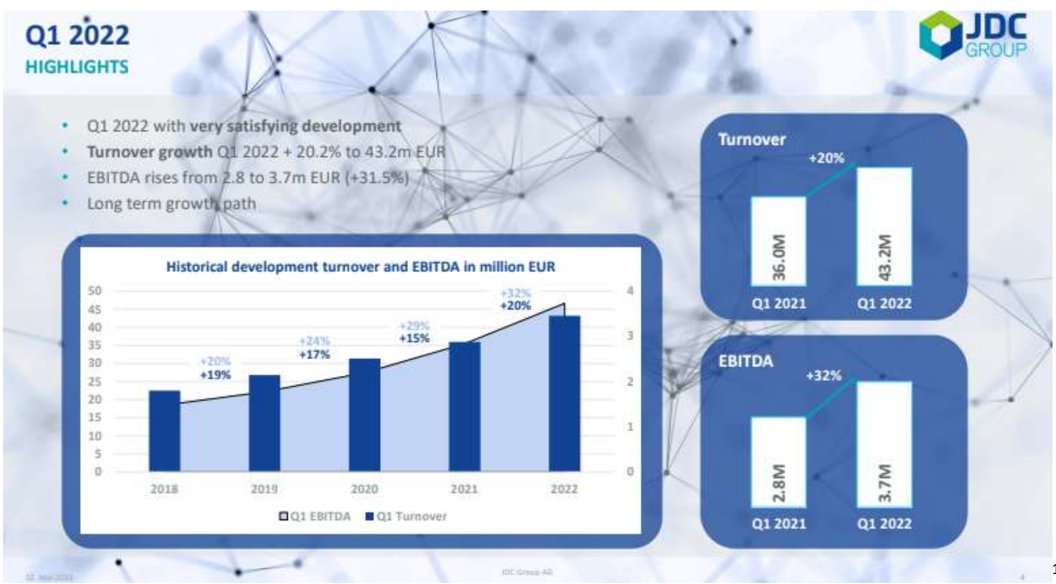
On the long side we choose to sell our shares in Kindred as well as both buying and selling TPL and GLRE. We are also in the process of buying a new interesting stock that we hope to share in the latter half of the year.

Our sale of Kindred was because of us wanting to bring down our exposure to the gambling sector, but also because Kindred will need to invest a lot of money in Netherlands and the US and we were quite uncertain about the ROI here.

TPL and GLRE ended up being more short-term positions than we normally do in Symmetry. In both cases the stocks appreciated meaningfully while our other positions declined. We therefore choose to reallocate the money. On TPL we were worried that the stock appreciated ahead of the Oil&Gas prices. With GLRE we were negative influenced by a meeting with the management team where they (after we pressured them several times) couldn't deliver a satisfactory answer on how to get the ROE to sustainable levels.

For the rest of the book our positions have mainly delivered good results despite the stocks being down.

JDC delivered the best Q1 results in their history with 20 % revenue growth and 32 % EBITDA growth. This despite the fact that all their new distribution agreements have not yet started to contribute.



[1]

[1] JDC Group Q1 2022 earnings presentation

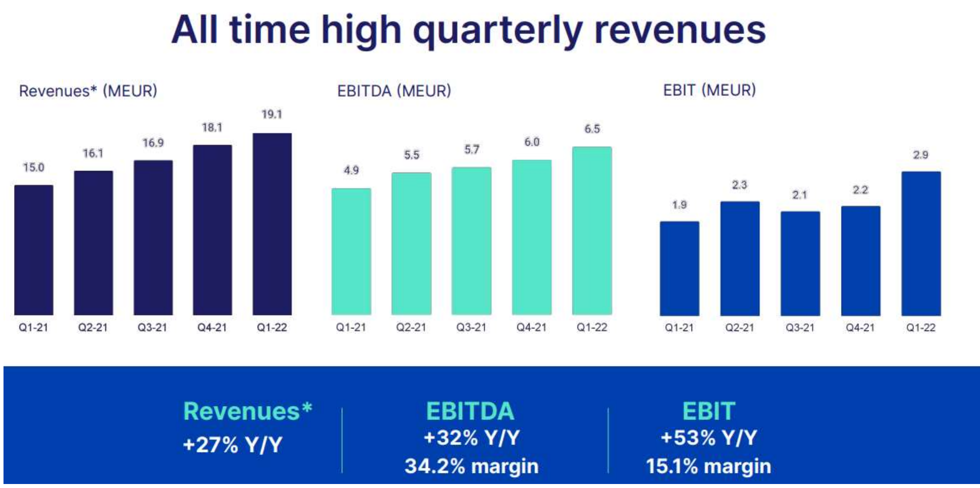
JDC also continued to win new agreements that should contribute meaningfully to the growth over the next few years. Another positive factor was the initiation of a stock repurchase program. As the CFO said: "when we guide for +33 % EBITDA growth and our stock is down 20 % it gives us a perfect opportunity". This is the reason we invest with owner operators. They think as shareholders because they are shareholders.

JDC announced this Friday a new JV together with Bain and Canada Life. We don't think the market have yet appreciated the opportunity this JV has for JDC. Basically, Bain and Canada life will contribute the vast majority of the capital to the JV to roll up broker pools. But JDC will take a cut of all the revenue as they process it through their platform. While the opportunity in the end depends on how much M&A the JV will do, we think it can be substantial.

Optically JDC can look expensive at around 50x P/E. But if one digs deeper, we can see they have a lot of amortizations of intangibles and run with a negative working capital. Over the last few years, the EBITDA/FCF conversion have been +80 %. Based on a FCF multiple JDC is closer to a 25x multiple. For some this can still look expensive but its important to understand that they are still pre-scale. The current EBITDA margin is around 7 % compared with the long-term guidance at 14 %. In another way, the company is trading at 12x FCF using mature margins despite the revenue growing +20 % for years to come. We still think JDC can end up being a ten-bagger from here.

Protector Forsikring continued to deliver great results in a challenging market. They managed to raise prices and those offset inflationary pressures and still keep good growth and profitability. They have on their investments delivered significant outperformance to the market YTD on both stocks and bonds. The CIO Dag Marius must be like a child in a candy store at the moment, where he can buy cheap stocks and HY-bonds at attractive multiples. This will secure high earnings for Protector for years to come.

Gaming Innovation Group also continued its good development in 2022 with a new all-time high quarter in Q1. At the same time, they also delivered a strong trading update for April - setting them up for a good Q2 as well.



[2]

We still find the valuation of GiG totally ridiculous. Based on our estimates GiG is trading at 4x EBITDA and 5x free cash flow on our 2023 estimates. A 20% FCF yield for a company that is growing +20 % organic is just too good to pass on.

Epsilon Net also had a fantastic Q1 2022 report with 75 % revenue growth (or witch more than 50 % was organic) and expanding margins.

Basic Financial Figures of 01/01/2022 – 31/03/2022:

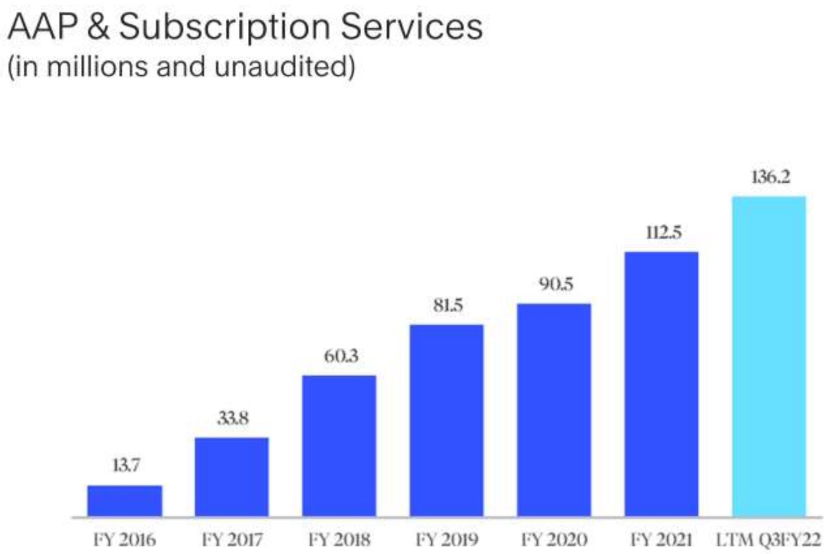
GROUP FINANCIAL FIGURES (in thousand €)	**01/01/2022-31/03/2022**	**01/01/2021-31/03/2021**	**%**
Revenue	14,133.76	8,067.73	**75.19%**
EBITDA	4,719.12	2,689.31	**75.48%**
Earnings before Taxes	4,029.75	2,235.49	**80.26%**

[3]

Epsilon is in the process of digitalizing small and medium sized businesses in Greece. They are still at an early stage here and we would expect many years of high growth ahead for them. At the same time management is using the high cash conversion for accreditive M&A without diluting shareholders (they also recently approved a share buyback program). Despite this favorable situation for Epsilon, the stock is trading at 10-12x earnings.

[2] Gaming Innovation Group Q1 2022 earnings presentation
[3] Epsilon Net Q1 2022 trading update

Franklin Covey delivered another astonishing quarter last week. They just keep exceeding even my most optimistic assumptions quarter after quarter. The stock improved 22 % on the results announcement but we still think there is plenty of room to go from here.



[4]

FC is only trading at 15x our 2023 free cash flow estimates and only 8x our 2025 estimates. At the same time, they have started to aggressively buyback their own shares and managed to buy 3 % of shares outstanding just in the last quarter. FC is today our biggest position and we think the stock is worth more than 100 $ even in the short term.

Naked Wines also reported their FY22 numbers (runs to 31/3 2022). The numbers were already pre-disclosed so it was mostly the FY23 guidance we were looking forward to. This guidance was overshadowed by some going concern risks in the auditor's report. Naked Wines have been our biggest looser so far this year. We had expected a weak trading update (and have hedged that with other consumer short positions that have worked well) but we were still surprised to see the stock go down 50 % in 2 trading days. The FY23 guidance was below expectations but not something that can explain a 50 % drop. The big drop came primarily because of some going concern issues in the report like these:

The Board has also reviewed the potential impact of other reasonably plausible downside scenarios. In particular, should Repeat sales show a progressive deterioration versus our expectations (-5% in Q2, -7.5% in Q3, -10% in Q4 of FY23 and -10% in Q1 of FY24), cash reserves would be further reduced. If no management actions were taken, additional sources of funding would be required in Q4 of FY23 and Q1 of FY24.

[4] Franklin Covey Q3 2022 earnings presentation

A downside scenario resulting in a 7.5% to 20% sensitivity against the base case forecast for Repeat Customer sales could result in a breach of this covenant. When taking into account actual trading results to date which are below forecast, a downside scenario of 3.7% against forecast would result in a breach of this covenant at June 2022 and as a result of the sensitivity in the downside scenario, management have identified a material uncertainty on meeting this covenant[5]

Comments like that of course get investors to totally panic sell their shares as it seems like they are close to filing for bankruptcy soon. Management tried on the earnings call to explain it as a technical issue with the auditor and something "that is not related to reality". The confusion is total here. Below are some comments from the management around the issue:

"Yes, happy to talk directly to that, Mark. I think the first thing that's important to say is the accounts have signed off on a going concern basis and the management team were very confident that's the appropriate situation for them. In the real world, we've got a strong balance sheet to end the year with GBP 40 million of cash. And as you see, the business, profitable in FY '22 in terms of the main trading operations of the business has been kind of positive or cash neutral over the course of the last 2 to 3 years. So we've got a good amount of cash.

Our operations don't burn through that cash. Really what the flag raised in the audit process says is if you apply a severe downside scenario, which it's important and prudent as lot of audit work to do and if we didn't choose to trade the business any differently, and we've got lots of levers we could pull. And if under that scenario, we no longer had access to any borrowing, then we could have -- that's where the disclosure comes from. I think that's 2 or 3 hypotheticals on top of each other. I think in the real world, we're confident about the level of funding we have in the business and that we have appropriate funding to deliver our plan."

"We had -- so there's nothing exceptional to kind of call out there. And as I say, it's a case of Deloitte really just prudently doing their work as auditors and saying, we should apply some severe downside tests, and that's an appropriate thing to do at a time where, obviously, there is a degree of macroeconomic uncertainty. But I think ultimately, Naked is well positioned to look for opportunity in that type of environment. So obviously, no one enjoys going through the technical process of audit review. But in the real-world context, and I feel very confident about where Naked is and the fact that we're well positioned to deliver on a year of looking for responsible growth."

And on top of that, we talked about expecting to manage the business to a breakeven adjusted EBITDA, which is something that we -- is also explicit in the guidance that we provided today. So I think as we talked about -- the technical point here, I think, that's being made is there's a number of confluence of ifs -- if/then statements that would get to that. So if the performance was worse than expected, if we didn't trade the business differently as a result of that, if we didn't do anything additional to conserve cash, in that case, we're reliant on the loan and like most credit facilities, there are financial covenants in the credit facility. So...

Yes, I think that's important. And look, I think a really important issue for us to spend a bit of time reflecting on because I know it will attract ton of questions. I'm sure lots of people on the call have got questions. Look, things were being clear about here are, number one, we don't have a plan that is reliant on us using external borrowing, but we thought it was prudent to put a little bit more flexibility into the balance sheet; number two, we don't think we're going to have any problems with the covenant on that loan, but under a downside scenario, we could have problems. That's a technical point that's being raised.

Directly to your point, Brad, we're not stating or guiding here that there's a likelihood or an intent of us as a management team to raise capital in the fourth quarter. Nearly what our auditors are saying is were there to be a severe deterioration in the business and were we not to take measures to address that and were we not have recourse to this loan, then we would have a requirement for capital. So I think another way of thinking about it really simply is not only did the business generate profit last year, but you see it generate materially higher levels of standstill profitability.

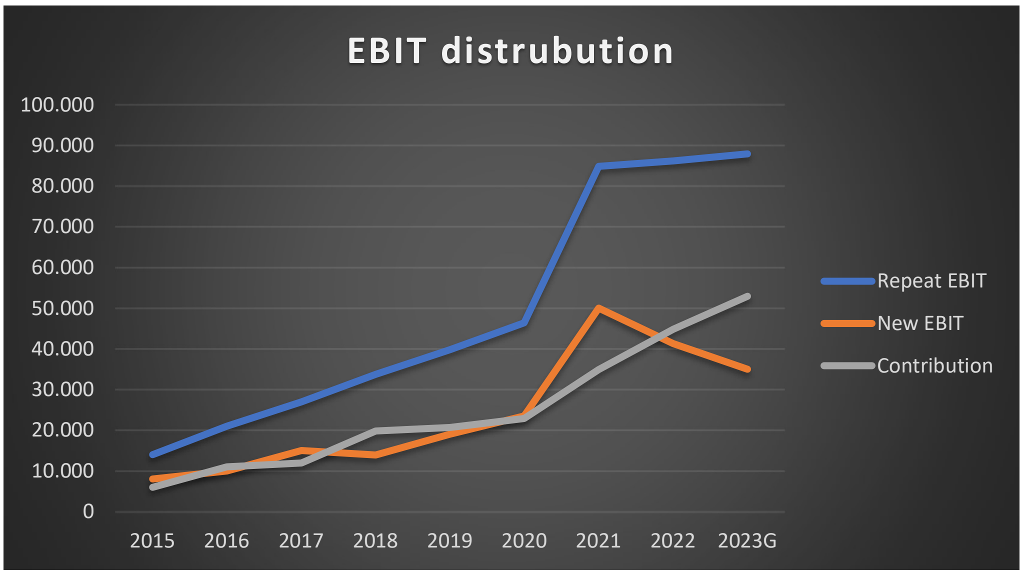
And what that shows is we have a lot of choices in this business, we can get to a number of different P&L outlooks of the end of the year. We could deliver materially higher short-term profitability were we so minded or if we needed to. So there's a lot of optionality in the business. There's a lot of discretionary expense, whether that's discretionary marketing expense or SG&A expense that we could unwind out of the business were it to be necessary. So I think that's really important. Ultimately, what we've got here is a technical challenge, which says, hey, if you layer a few hypotheticals on top of each other and you don't change your actions, then you have some requirements.

To be very clear, were we to see materially deteriorating consumer behavior and were that to impact our generation of contribution in the way it's highlighted in a severe downside scenario, we would trade the business differently such that we wouldn't have this requirement. So I think it's important to spend a bit of time on that, and thank you very much for the question, Brad" [6]

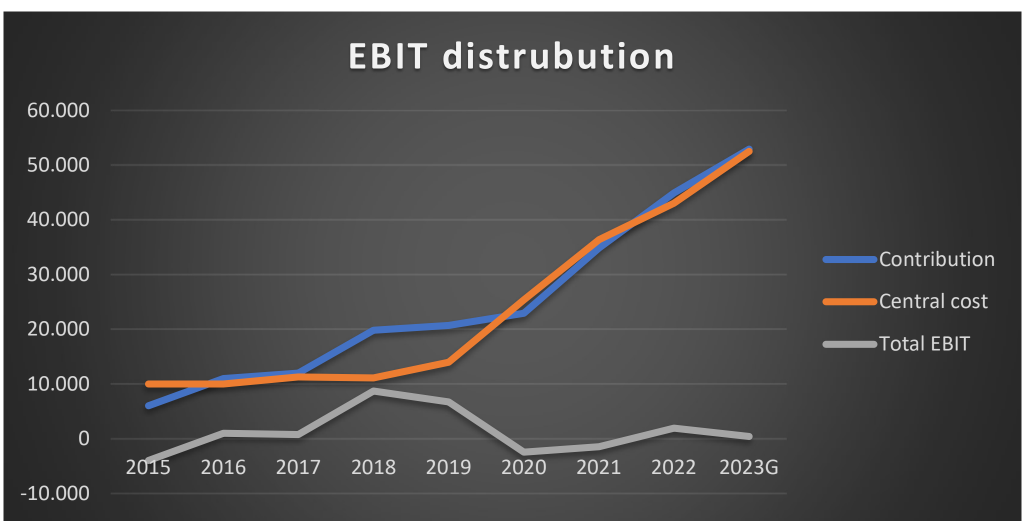
[5] Naked Wines FY22 results announcement
[6] Naked Wines FY22 earnings call

Where are we now then? We still haven't made up a decision on what to do from this level. For us the going concern issue was not the biggest concern – we think like management that it is something they can solve. Unless they have a bank-run from their angels we don't see them having cash issues.

To us the biggest issue was the guidance around their fixed expenses. If we look at how the underlying business does it actually works the way the management have told us. In periods of high investments (new EBIT) the total contribution gets hit but in periods when they take new investments down it does not affect repeat EBIT to the same degree and those deliver rising contribution profits.



As can be seen above the company actually guides for contribution profit to exceed 50 million £ in FY23, a clear ATH and around 50 % of the total market cap today. The existing customers is still loyal to them and have value. The big issue with the guidance is the fixed expenses – the company is burning money like there is no tomorrow here, instead of showing the same discipline as they have done on the "new investments".



The management team have always told they can scale the fixed investments as they grow and therefore capture a high “standstill-EBIT”. This argument no longer holds. All market participants don’t believe it anymore when they say its fixed expenses. It seems like its just variable expenses growing in line with contribution. And if that’s the case then Naked will never have a path to profitability.

Just since FY22 the fixed expenses have grown by 130 %, significantly more than repeat EBIT of 91%.

We understand management think they can invest in different areas that will make the business better and priorities this ahead of profits. But we also think a disciplined management team would focus on the stock price and think about capital allocation here. Share buybacks (buying back existing customers) seems like a better option and ROI than investing in new ones at this point.

If management have instead chosen to curtail fixed expenses (just for one year) and show to the market that they can cut these without hurting the business, they would bullet proof the unit economics and solve any liquidity concerns at the same time. Now they have put themselves in a situation where no one believes them and instead they have a significantly higher cost of capital that distracts them from delivering on their long-term goals.

The end of this story is still not unclear. We will keep our investors updated in our monthly tear-sheets if we decide to change our opinion here.

Conclusion:

2022 have been a difficult year so far to be an investor. Not only stock investors but also bond investors. While there are several things we could and should have done better – in the end we managed (to a degree) to protect our investors capital in the worst market decline in 15 years. To achieve high results over the long term one needs to survive in the short term. 2022 so far have given us some bruises but not any life-threatening wounds.

We are ready to capture the opportunities the market brings to us. With a low gross and net exposure, we have amble powder ready to deploy into attractive opportunities when they arrive.