

## Unfair Fights

**Y**en Liow's pedigree was little in question when he launched Aravt Global in 2014. A native of Australia, he started his career as a consultant at Bain & Co., spending five years in its San Francisco, Singapore, Sydney and Beijing offices. He then earned an M.B.A. from Harvard before a 13-year run at Ziff Brothers Investments, where he was ultimately responsible for its investments in media, telecom, energy and agriculture. Aravt at launch had more than \$1 billion in assets.

It hasn't been smooth sailing since, but Liow has much wisdom to impart about why and how he overhauled his process and strategy, where he looks for opportunity now and why he thinks he's got it right this time.

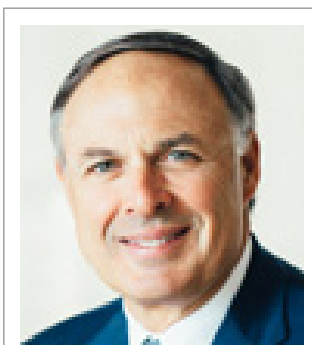


**Yen Liow**  
Aravt Global

## Weighing Anchor

**F**or an investor with an accomplished career – including co-founding RS Investments and being named Morningstar's 1999 Domestic Stock Manager of the Year – Jim Callinan is where he wants to be in managing Osterweis Capital's small-cap Emerging Opportunity Fund. "I enjoy learning about companies and picking stocks," he says, "and that's what I spend all of my work time doing."

Quite well, we might add. The fund since its inception in 2012 has earned a net annualized 18.5%, vs. 12.4% for its benchmark Russell 2000 Growth index. Callinan and team today see opportunity in such areas as contact-center software, lease-to-own retail, specialty managed care and law-enforcement technology.



**James Callinan**  
Osterweis Capital

## Stepping Up

**I**t's not uncommon for professional investors rising through the ranks to specialize. For Bill Costello that meant becoming the "energy guy" for The Boston Co., where he ran all of the firm's energy research and managed its Dreyfus Natural Resource Fund. "I was perfectly fine if that turned out to be my lot in life," he says.

It turns out it wasn't. In 2010 he joined Westwood Holdings to co-manage the all-sector Westwood SmallCap Fund, which over the past 10 years has earned a net annualized 11.6%, vs. 8.7% for the Russell 2000 Value index. Targeting companies with unrecognized earnings-growth potential, he's finding upside today in such areas as pet and garden supplies, housing and casual dining.



**William Costello**  
Westwood Holdings

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# Investor Insight: Yen Liow

Yen Liow of Aravt Global describes how he broadly recast his approach after a rocky start for his new firm, why on the long side he focuses only on “horses,” where he’s finding Covid-related short ideas, why he’s prepared for a “wide-diversion, high-volatility” future, and why he’s high on the prospects for Cellnex, Safran, Boyd Group and Keywords Studios.

**Yours was a high-profile launch when Aravt Global opened its doors in 2014. Describe your basic going-in strategy.**

**Yen Liow:** We knew the world didn’t need another hedge fund. But we’d spent the previous seven years studying market history to discern the fundamental characteristics of both right and left tail equity-performance outliers, and we believed we were ready to apply what we’d learned to a modern context. We built an enormous case-study library to help groove pattern recognition and thought we could substantially outperform markets by deploying the frameworks we’d identified through an advantaged, low-net-exposure long/short balance sheet.

Our first three years were literally the worst three, by far, that I’ve had in 19 professional investing years. To have a protracted period that was so divergent with my own history, something clearly had changed or was wrong. So starting in the summer of 2016 we did an extensive review to try to figure out what that was.

Maybe to step back a bit, I chose a traditional hedge-fund strategy that had a flexible balance sheet that enabled more gross exposure and provided all the tools that increased the odds of superior, through-the-cycle returns. Hedge funds prior to the 2008 financial crisis went through a golden era, with 10 to 15 years of incredibly strong performance, irrespective of market conditions. Then the strategy went stone cold for nearly a decade. How does that happen?

The first thing we looked at was the hypothesis that it had become so competitive that alpha had disappeared. Based on our study from 1990 to 2016 at the time, we found some slight alpha fade that could be attributed to competition, but it wasn’t nearly enough to explain the underperformance of an entire asset class. We suspected something structural had changed.

What we found to be the most-important change was the vastly different interest-rate environment. We had traditionally been paid a rebate when we shorted, which prior to the financial crisis was the effective fed-funds rate minus the cost of borrow and came to 500-600 basis points. With markets through the cycle returning 8-10% annually, it didn’t require hedge funds to generate herculean short alpha

## ON CHANGE:

**Hedge funds prior to 2008 went through a golden era, then the strategy went stone cold. How does that happen?**

to add value and deliver uncorrelated returns. As the rebate went to zero and then negative after the financial crisis, the game fundamentally changed on us and the short alpha required from stock selection just to keep up doubled or tripled.

The other big issue post-crisis had been the long run of strong equity returns. In a long/short equity structure, anything less than 100% net exposure is defensive, designed to reduce downside capture and enhance through-cycle return. The strategy isn’t optimized to keep up when equities are returning in the mid-teens or better, as they had been. Through the cycle long/short could still make sense, but consistently strong markets amplified the negative impact on long/short performance.

Our conclusion was that we could keep a lower-net structure of 30-40% exposure, but we’d have to accept lower net returns. That’s not necessarily a bad path to go down, as there is clearly institutional demand for uncorrelated returns that supplement traditional long-equity portfolios and can generate higher returns than what

you can reasonably see today from bond portfolios. There’s very little in the bond market today that is going to help institutional clients hit their 6-9% overall return targets. So there’s a tremendous use case for long/short equity that acts more like a bond proxy. We could deliver that with a more traditional hedge-fund structure.

Or we could shift the structure and go for total return and the aspiration of significantly beating the market. We increased net exposure, were willing to vary it more, and adjusted gross exposure higher. That wouldn’t fully address the headwind if markets only go up, but we believe that through the cycle the reduction in downside capture and the still-advantaged balance sheet can generate strong returns.

Starting in January 2017, we shifted from targeting 30-40% net exposure to targeting 55-85% net, widening the range depending on the opportunity set but sitting most of the time in the 70s. We expanded our gross exposure as well, from a range of 130-140% to 145-170%.

**That wasn’t the end of your strategic and operating overhaul. Describe some of the other key changes you made.**

**YL:** I’ve studied excellence for decades and one universal characteristic of those who succeed is focusing on strengths. So the first key adjustment we made was to narrow our focus on the long side to the types of companies that dominate the right tail of returns and in which we’d had the most success, which we call “horses.” Because horses live in a fairly narrow set of sectors, we refined where we would play by removing cyclicals, energy, financials and – while this one may come back in time – healthcare. Given our renewed focus, we could delayer the organization, leaving the research work to three analysts plus me. We also built more robust internal risk systems, focused on allowing us

to better visualize what we owned and the resulting portfolio exposures we had.

Since implementing these changes at the beginning of 2017 we've turned around our performance to be among the top decile of global long/short equity funds, also handsomely beating the broad market.

**Explain what you consider a “horse” and why they are now your exclusive focus on the long side.**

**YL:** Game selection is the most important decision a leader and asset manager can make. We're choosing to focus exclusively on unfair fights, which means investing only in companies with built-in advantages that allow them to win a lot more than they lose every single day and compound earnings power at a very high rate.

One absolute law of markets is the return reversion to the market cost of capital. We are explicitly hunting the 3% of securities that do not mean revert, and the absence of mean reversion is our variant perception. Typically our expectations over the first year for these companies isn't much different from consensus. What can be vastly different is what happens over two, five or ten years. The market in general will fade growth rates, earnings power and the multiple. We try to underwrite businesses we think can maintain growth and high returns for long periods of time.

So what is a horse? We look at everything across eight basic dimensions, which I can go through one by one.

These are businesses with moats, primarily economic monopolies and functional oligopolies. They're natural market-share takers with pricing power and high returns on invested capital.

They have large addressable markets. They have won and we believe they can continue to win and grow at a rapid clip for five, ten or more years.

The third characteristic is that they're translating market power and growth into earnings increasing at 2-3x the rate of the market. Multiples can drive return in the short term, but very little over long periods. Earnings power has to increase strongly and sustainably.

Number four is management quality, which means that we want to partner with people who are ethical, highly capable, hungry and aligned with us.

We look for additive, not detrimental, balance sheets. We don't want to count on returns that are excessively levered, but we do believe balance sheets can enhance the earnings algorithm and they should. Part of the reason the private-equity community has created value is that there are so many businesses that are under-levered.

### **ON "UNFAIR FIGHTS":**

**We focus only on companies with built-in advantages so that they win a lot more than they lose every single day.**

Number six is valuation. It's number six because as long as the first five hold, we think it's a matter of when, not if we'll get an attractive entry point. But we have to be patient to take advantage of the greatest risk/reward skew.

We look for earnings power that is predictable, which is why we focus on durable strengths that protect the business even when a major crisis hits. A significant portion of our portfolio companies have subscription-type business models.

Finally, there are stages in the lifecycle of a business, from proof of concept, to replication and on to maturation. The replication phase is when you've demonstrated leadership and operational competency, and now you're scaling. That phase is exclusively where we focus.

**How about a real-time horse example, say using one of the new positions you added in the second quarter?**

**YL:** All three are all excellent examples, but let's talk about Cellnex [Madrid: CLNX]. It's Europe's largest independent cellular-tower company, with over 60,000 towers and leading market positions in Spain, Italy, France, Switzerland, Portugal,

the U.K., Ireland and the Netherlands. It meets very well all our criteria for a horse.

With respect to the competitive moat, independent cellular towers is one of best businesses out there. It saves wireless carriers money relative to owning the towers themselves, there are high barriers to entry, and every existing tower is basically its own little monopoly with a massive cost advantage over a new tower. Incremental costs to add new tenants to a tower are minimal relative to the incremental revenue received.

The addressable market is large and growing. Only about 30% of Western Europe's 500,00 towers are run by independent operators, compared to approximately 90% in the U.S. There's a tremendous amount of towers still to move to independent hands, and there's also expansion and densification of the network still to come, especially with 5G and the continued growth in mobile data usage.

All that leads to attractive growth. We think revenues can organically grow 8% per year, allowing for 10% or so annual EBITDA growth. With leverage – which we consider additive, not detrimental – and incremental M&A, we expect earnings to compound in the mid to high teens. Predictability is high on the organic side, given the company's long-term contracts with price escalators. The business is also clearly in the replication phase, scaling through operational competence.

We're quite impressed with management, which is long-tenured in the business and clearly focused on shareholder value creation. The management team saw the potential for Cellnex to be a pan-European consolidator when it was still part of Abertis, a Spanish infrastructure company, and pushed for it to become independent through an IPO.

Finally, with respect to valuation, the stock trades at 26x next year's consensus recurring levered free cash flow – similar to the Adjusted Funds From Operations for U.S. REITs – and 24x estimated 2022 RLFCF, neither of which incorporates incremental M&A. The company just raised in a rights issue another €4 billion to fund deals. As it grows, the realized multiples

will come down considerably. As with all our horses, we expect our returns as shareholders to at least match the compounding earnings power of the company.

Consistent with our focus on horses, I should mention the system-design changes we made in 2016. We wanted an operational model that is patient and waits for price. Our returns are based on the long-term earnings power of our companies, so there's no impetus to act at any particular moment. We went 17 months including all of 2017 when we bought one stock. But when provoked we can act quickly – in both Q4 of 2018 and Q1 of this year we bought three stocks in one week each.

We have three books running all the time. The live portfolio is book one. Prepared inventory – stocks on which we're fully up to date and are just waiting for the right price – is book two. Book three is the remaining curated universe of stocks that meet our basic horse criteria but where we'd have work to do to get fully up to speed. We own 15 to 20 longs at a time but have multiples of that prepared to go. Patience is an incredibly important part of investing. The better we're prepared, the easier it is for us to act when provoked by price, or to be quiet when we are not.

**You decided in your reboot to continue shorting. Describe why and what you look for in attractive short ideas.**

**YL:** We short for two reasons, both of which we believe improve through-cycle returns. The first is to protect the long portfolio. The second is to create alpha. We execute on those two things through distinct means. One is through bespoke short baskets designed to hedge market and industry risk in our long book. The other is through idiosyncratic, single-name shorts.

You're lucky in a diversified short portfolio to have a 50% batting average, which means it's hard to make up for big mistakes with a better slugging ratio. We're keenly focused on avoiding risks that expose us to the right tail of stocks that run away from you, devastate your short book and are very difficult to overcome.

What don't we do? We don't short hypergrowth, irrespective of valuation. We don't short fads or frauds. The problem with all of those is that the stocks can go up 3x, 5x, 7x before your thesis eventually starts to play out. So we just avoid them – they're not fights we need to pick.

We've also implemented a strict rule that if we lose 100 basis points of alpha on any single short, we cover it and quarantine the idea for 12 months. We usually have between 10 and 20 live shorts at a

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### ON SHORTING:

**It's sexier to pitch the down-50% ideas or the zeros. We tend to play more for the 20-30% down ideas instead.**

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time and our backup book has 40-plus ideas in wait. No single short matters to us, so we just move on to the next one. There are accomplished short-sellers who have been short Tesla for years, or short Zoom this year. Those types of things can blow holes through your portfolio that are very hard to recover from.

**Talk about where you're active on the short side today.**

**YL:** It's sexier to pitch you on the down-50% ideas or the zeros. But among the top decile of high-performing stocks in any given year, about half of them are what people would regard as great shorts with significant downside potential. They're low-quality businesses, often levered, but they also may start to come out of a macroeconomic situation that was depressed. We don't want to get caught when they ricochet up and to the right.

We tend to play more for the 20-30%-down ideas instead. We short mature businesses that used to be good or great but aren't any more and the market hasn't fully recognized that. We also look for companies at or near cyclical peaks, but priced as if the good times roll in perpetuity.

One area we've been active in is branded consumer goods. In many cases these were low-growth, stagnant or even declining businesses, but Covid brought forward surge demand that is, one, not sustainable in our view and, two, took the shares of many companies benefitting from it to valuations that we think are going to look absurd when Covid is over. We're also seeing some of the same behavior in leisure and recreation areas that have actually benefitted from Covid in the short term. When we get to the other side of it we expect to see tremendous mean reversion.

We also spend a lot of time on structural shorts. Again, they're often formerly good or great businesses that are now challenged by either new technology and/or business models. Everybody talks about how the cloud is disrupting the world of software, with new competitors luring customers with more-flexible, more-secure and less-expensive offerings. We're looking at the other side of that, the legacy software and legacy infrastructure that may still be extremely profitable but is becoming less and less relevant in a cloud-based world. We're finding that to be a bountiful area for short-selling.

**We spoke early this year [VII, January 31, 2020] about your bull case for jet-engine maker Safran [Paris: SAF]. How have you processed all that's gone on in its business, and with its stock, since?**

**YL:** Safran was obviously directly impacted by the hit across the board to aerospace. Aftermarket revenues that provide most of the company's profits were down 66% in the second quarter and are guided to be down 60-70% in the second half.

The first test we put everything through with the pandemic was liquidity. Despite the horrendous aftermarket trends, the company should earn more than €1 billion in free cash flow this calendar year. It came into the crisis with only around 0.8x net debt to EBITDA, and after raising new debt as a precaution now has €4.4 billion in cash and another €4 billion in undrawn credit lines, versus about €3 billion of debt maturities through 2022.

Given that we were comfortable with the solvency, we then looked at this as an open-ended option where we had to assess the reversion to what mean and when. While the propensity to travel has clearly been impacted, we don't believe that's permanent and think it's reasonable to expect a return to 2019 passenger-mile levels within the next three to five years. There may be some change in the way business is conducted, but air travel is really more a proxy on the emergent middle class and their powerful drive to see the world – that's been a secular tailwind for air travel for more than 30 years and we don't see that fundamentally changing.

We believe Safran's moat hasn't been challenged at all and that the drivers of

revenue and profit growth we talked about before are still there. The 737 MAX issues that have cost the company close to €700 million in cash flow will get resolved. Narrow-body planes that Safran supplies will continue to take market share. After-market pricing will continue to increase. The LEAP engine – Safran's newest engine – will start generating material high-margin aftermarket revenues starting in 2023.

On our math in March, if it took three years to recover to 2019 passenger-mile levels, we expected to make a roughly 30% IRR on the stock. If it took five years, it would be closer to a 20% IRR. We considered the shares to offer more than fair compensation for the risks we were taking, and we still do.

**Explain why Canada-based collision-repair company Boyd Group also made it off your prospect list and into the portfolio in the second quarter.**

**YL:** This is one of the largest collision-center operators in North America, with nearly 700 locations in the U.S. and Canada. It's one of three national-scale players – along with Caliber Collision and Service King, both of which are private – in a highly fragmented \$40 billion collision-repair market. More than 90% of its revenues are generated in the U.S. and 90% of the business as well comes from insurance companies.

The auto-repair market is generally recession resistant and Boyd benefits competitively from scale, which allows for lower input costs, better systems and IT infrastructure, more standardized and efficient processes, better labor utilization, better-trained employees and better customer relations. This results in auto insurers like Geico directing more repair volume to Boyd each year and is why its average revenue per location is 3x the industry average.

The growth potential is high. The top three players only control maybe 6% of total U.S. locations and 16% or so of total industry revenue. We think that industry share can easily reach 30-40% and that Boyd is a significantly advantaged acquirer. It can both leverage existing relationships to generate incremental revenues for acquired stores while also sharply lowering operating costs. We expect revenues to compound in the mid-teens annually, from 3-5% same-store growth and 10%-plus growth from opening and acquiring new locations. The company raised C\$230 million through an equity offering in April – decreasing its net debt to 0.8x trailing EBITDA – and it should be able to put that to work as many mom-and-pop shops are having to navigate financial distress.

Management here is also superb. Boyd was the second-best-performing stock on the Toronto Stock Exchange over the past 10 years under the direction of long-time CEO Brock Bulbuck. He stepped down

INVESTMENT SNAPSHOT

**Safran**  
(Paris: SAF)

SAF PRICE HISTORY



Share Information (@9/29/20):

Price	€85.30
52-Week Range	€51.10 – €152.30

Valuation Metrics (@9/29/20):

	SAF	S&P 500
Trailing P/E	53.1	35.5
Forward P/E (Est.)	22.8	24.9

ORIGINAL BOTTOM LINE – January 31, 2020

Yen Liow believes concerns related to Boeing's 737 MAX and to the economics of new fixed-price maintenance contracts are overdone, masking the company's bright overall prospects that he expects will "drive a high-teens to low-20% annual shareholder return."

NEW BOTTOM LINE

Its shares were hit head on by the pandemic, but Yen Liow believes the growth dynamics of its industry and its company-specific advantages remain well intact. "We considered the shares to offer more than fair compensation for the risks," he says, "and we still do."

Sources: Company reports, other publicly available information

earlier this year but remains Executive Chairman, while his COO, Tim O'Day, took over as CEO.

**How are you handicapping the industry's recovery from the pandemic recession?**

YL: There has been a significant impact on the business as people stayed home, drove less and as a result got into fewer accidents. Demand has increased as people return to work, but industry revenues are still down 20-30%. In general, we expect this to be a question of when, not if, and

that the return to normal for driving will likely be quicker than for flying, maybe more like to two to three years. If people end up driving more rather than taking mass transit, that would be an incremental positive.

This one's all about offense. Boyd's two major competitors have heavily levered balance sheets and don't have the flexibility it does to step up acquisitions at the bottom of the market.

**Is more collision-avoidance technology in cars today a risk to Boyd's business?**

YL: Collision-avoidance systems have advanced tremendously, but unfortunately for the world, collision incidence hasn't materially declined, in no small part due to people being increasingly distracted by their cellphones and texting while driving. Another mitigating factor from a collision-repair standpoint is that the costs of repair keep going up due to the increasingly sophisticated materials and equipment used in cars today.

Autonomous driving is another potential long-term risk, given that when it's fully implemented in theory there would be fewer collisions. In this case we think the level of implementation that might have a negative impact on Boyd's business is many, many years and a tremendous replacement cycle away before it does.

**How are you looking at valuation with the shares trading at around C\$207.75?**

YL: The stock currently trades at 26x and 21x consensus free cash flow per share for 2021 and 2022, respectively, which again does not fully incorporate incremental M&A. Including the M&A potential we see, we think those multiples are more than reasonable for a company that can compound as quickly and for as long as we think this one can.

We expect the mid-teens annual revenue growth I mentioned earlier to translate into at least 20% compound growth in free cash flow per share for the next five years. Because we don't expect multiple compression, we believe our total return should be commensurate with the growth in free cash flow per share.

One last thing I'd mention on Boyd is that it has traded for much of its public-company life as a Canadian income trust, which restricted the amount of U.S. ownership of its shares. It converted to a C Corporation at the start of this year, so those restrictions have been lifted. Over time there's a case to be made that as the shareholder base expands and liquidity improves the valuation accorded the stock will increase relative to history. It's not something we're counting on, but a potential positive nonetheless.

**INVESTMENT SNAPSHOT**

**Boyd Group Services**  
(Toronto: BYD)

**Business:** Owner and operator of close to 700 collision-repair centers in North America, branded under the Boyd name in Canada and under the Gerber name in the United States.

**Share Information**

(@9/29/20, Exchange Rate: \$1 = C\$1.34):

<b>Price</b>	<b>C\$207.73</b>
52-Week Range	C\$125.01 – C\$231.52
Dividend Yield	0.3%
Market Cap	C\$4.41 billion

**Financials (TTM):**

Revenue	C\$2.21 billion
Operating Profit Margin	5.3%
Net Profit Margin	2.0%

**Valuation Metrics**

(@9/29/20):

	<b>BYD</b>	<b>S&amp;P 500</b>
P/E (TTM)	88.5	35.5
Forward P/E (Est.)	33.9	24.9

**Largest Institutional Owners**

(@6/30/20 or latest filing):

<b>Company</b>	<b>% Owned</b>
Capital Research & Mgmt	4.8%
Manulife Inv Mgmt	3.3%
Mawer Inv Mgmt	3.2%
Vanguard Group	2.7%
Massachusetts Fin Serv	1.5%

**Short Interest** (as of 9/15/20):

Shares Short/Float	n/a
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**BYD PRICE HISTORY**



**THE BOTTOM LINE**

The company is well positioned to take share in the North American collision-repair industry both from smaller players and from its two large, debt-burdened competitors, says Yen Liow. He believes it can generate 20% compound annual growth in free cash flow over the next five years and expects shareholder returns to compound at a similar rate.

Sources: Company reports, other publicly available information

Describe why you're high on the horse-like characteristics of Keywords Studios [London: KWS].

YL: This is an interesting company that I don't think a lot of U.S. investors know about. It is the largest technical-services provider to the videogame industry, providing through a global network of studios a wide variety of design, audio, localization, testing and customer-support services on an outsourced basis. The analog is the motion-picture industry, where studios focus primarily on developing their own intellectual property and then outsource a lot of the related services – as much as 90%, in fact.

The idea makes sense: take the central code base of a game and then use third-party service providers to translate it into different languages and designs around the world, customize music, test all the payment systems, set up all the call centers – any number of tasks that can be hired out more cheaply to an expert with scale that can speed up time to market and help meet surge demand. Keywords counts 23 of the top 25 videogame publishers in the world as clients.

As the largest outsourcer in a fragmented market, the company benefits from high switching costs – 80% of revenue comes from repeat business at existing customers – scale to meet global-customer needs, the ability to cross-sell, and a reputation for quality and cost-effective delivery. Once you've earned the customer's trust, they're not quick to go somewhere else to save a few bucks.

The growth potential here is better than just high. Videogame publishing is moving increasingly from relying on console cycles to games being permanently updated and made available online. That requires faster and constant development cycles, which is a big positive for Keywords. The global videogame technical-services market is estimated to currently generate at least \$6.5 billion in revenues, of which about 35% is outsourced today. We don't know if that gets to 90% like with movies, but crayon math – you don't need a sharp pencil – can get you to a lot

higher penetration than 35%. Keywords' share of the outsourced total can also be much higher than the current 15% or so.

The company has also proven to be an advantaged buyer, with acquired revenues contributing an average of 30% to top-line growth over the past four years. Given the company's size and ability to dramatically improve the performance of whatever it buys, there often isn't a credible second bid when they go after something. All in, we think revenues here can grow organically at a low- to mid-teens rate, with 6-8% of that coming from in-

dustry growth, 2-4% from increased outsourcing, and 2-3% from Keywords gaining share.

The balance sheet?

YL: Not an issue. They have £100 million in net cash that they recently raised through an equity offering in order to more aggressively pursue acquisition opportunities they see coming out of the crisis. Additionally, they have £100 million in available credit facilities.

INVESTMENT SNAPSHOT

Keywords Studios

(London: KWS)

**Business:** Ireland-based provider – through more than 50 independent studios located in 21 countries – of outsourced creative and technical services to videogame developers.

Share Information

(@9/29/20, Exchange Rate: \$1 = £0.78):

<b>Price</b>	<b>£21.62</b>
52-Week Range	£10.69 – £23.14
Dividend Yield	0.0%
Market Cap	£1.60 billion

Financials (TTM):

Revenue	£326.5 million
Operating Profit Margin	6.6%
Net Profit Margin	3.0%

Valuation Metrics

(@9/29/20):

	<b>KWS</b>	<b>S&amp;P 500</b>
P/E (TTM)	126.2	35.5
Forward P/E (Est.)	35.4	24.9

Largest Institutional Owners

(@6/30/20 or latest filing):

<b>Company</b>	<b>% Owned</b>
Franklin Templeton	7.8%
Octopus Inv	5.6%
Liontrust Inv Partners	4.5%
T. Rowe Price	4.3%
Oberweis Asset Mgmt	4.0%

Short Interest (as of 9/15/20):

Shares Short/Float n/a

KWS PRICE HISTORY



THE BOTTOM LINE

Yen Liow sees "better than just high" growth potential for the company as its end market grows, its sector grows as a share of the end market, and it takes a greater share of its sector. Even assuming some moderation in the high current valuation, he believes the shares can generate at least a 20% compound annual return over the next five years.

Sources: Company reports, other publicly available information

**At the recent share price of nearly £22 the valuation seems, let's say, full. How are you looking at upside from here?**

**YL:** The valuation is a bit extended now, with the shares trading at 39x and 33x the EPS expected in 2021 and 2022, respectively. Again, that doesn't include incremental M&A, which here we think will be particularly impactful. I mentioned our estimating organic growth in the low- to mid-teens – we think deal-making can at least double that over the next five years.

If top-line growth comes in at 25-30% or better, even assuming flattish margins we can moderate our multiple assumptions and still expect a 20% or so IRR on the stock over five years. Because there's so much deal potential this one maybe isn't as predictable, but given the runway for growth we see here, we're OK with that.

**You said recently that you expected long/short strategies to be “potent in a wide-dispersion, higher-volatility market.” Is that what you think we're in for?**

**YL:** I do think we're in for a more volatile existence. I believe the rules of engagement for maybe the next decade are low interest rates and more government involvement in the economy. Low interest rates put upward pressure on multiples and government involvement typically creates a great deal of uncertainty. Both of those things likely mean more volatility.

We've tried to design our business to thrive through volatility. We're trying to compound earnings power through the horses we've chosen, whose businesses we expect to be much less volatile than the economic environment. If no new stocks come to us, we do nothing. If the world becomes more volatile, we can still do nothing, but we can also upgrade the portfolio with ideas waiting and ready. As for the shape of the recovery, I don't know what shape it takes, but I think it's more likely to be a K than a U or a V. The world has been shaken, and in many areas the gap between leaders and followers is widening at an accelerated rate. Active long/short management should allow us to take

advantage of that, on both the up part and the down part of the K.

**We're curious about the origin of your firm's name.**

**YL:** One of the top five books an investor can read is Jack Weatherford's *Genghis Khan and the Making of the Modern World*. Genghis Khan's army had 200,000 cavalymen who over 30 years in the 13th century conquered 10 million square miles of the planet. Aravt means ten in Mongolian, which was the smallest individual unit size in Khan's army and is meant to represent our humble beginnings. Beyond that, the central premise of his strategy was that he hated putting his men in harm's way so he only chose to pursue unfair fights. I spoke about that earlier and it's incredibly relevant to investing. You can't compound capital if the odds are not well in your favor, so we're looking at every step for unfair fights, where we – and the companies we invest in – have advantages that are both material and repeatable. VII

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