Greystone Capital Management
Concentrated Value Investing

Q3 / October 2021

Dear Clients and Friends,

During the third quarter of 2021, returns for separate accounts managed by Greystone Capital ranged from +0.06% to +5.4%. The median account return was +2.9%, net of fees. I look forward to publishing more in-depth performance data at the end of the 2021 fiscal year, reflecting a composite return number, net of fees, that will capture a portfolio built since inception of the firm. Please continue to check your individual account statements and feel free to reach out with any questions or concerns. As the firm grows and new capital onboards, it is my expectation that our returns will continue to be sporadic across client accounts given the timing and inflow of new capital.

Third quarter results compare favorably to the S&P 500 and Russell 2000 returns of +1.8% and -3.5% for the quarter. Because client portfolios are invested in a concentrated way consisting of small companies mostly outside of the major indices, our returns should typically vary from the returns generated from those indices. As a reminder, we are not the indices. My strategy is purposely designed to invest differently than the structure of the indices in terms of the types of businesses, number of investments, and weightings of those companies within client portfolios. My belief, unchanged since the inception of the firm is that it's possible for smaller pools of capital to outperform the broader market. To do so, we have to be different. I believe that we are, and our results will continue to reflect those differences, good and bad, through all market conditions.

As usual during the quarter, financial news headlines were as cheery as ever, with fears of inflation, sovereign debt crises, China's regulatory actions, labor issues and disrupted supply chains front and center. And that's the short list. Also as usual, accompanying those headlines were predictions surrounding the timing, severity, consequences and aftereffects of these worries, usually laid out boldly and often, yet rarely correct. I would consider it a positive if I never made a market prediction in one of these letters, but I can at least say this: whether its five weeks, five months, or five years from now, today's set of worries will be replaced by a new set, just as severe, just as concerning and with just as many people forecasting the market's direction as a result.

My view of the world, which does not rely on narrow predictions of the future, is ideally suited for long-term investors who can withstand portfolio level volatility brought on by occasional shocks to the market and economy. We are currently betting on dominant economic themes and own a combination of businesses capable of compounding their value into the future, along with special situations that possess favorably skewed risk/reward profiles. I believe this combination of long-duration growth and asymmetric upside is well suited to navigate any short-term issues within the market or global economy. The bad news is, I have yet to figure out how to use excessive worrying about the future to enhance my investment process or help me make good long term investment decisions. The good news is, I'd rather do something more productive. That's not to say I'm free of worry or that bad things can't happen within client portfolios. Its just to say that I remain optimistic about our positioning as well as long term economic trends.

Seeing that we own good businesses that are run efficiently, are growing, and are trading at fair valuations, my biggest problem right now isn't the abundant headline risk we're presented with daily, but rather not having enough market participants who care about the positive developments taking place within all of our companies. The market recently shrugged off what could be considered phenomenal Q2 earnings results for many of our holdings, reflecting the assumption (inherent in the valuations) that our businesses will go on to accomplish very little despite solid execution providing the opposite view. In fact, should the current dynamic persist, small and microcaps may become the cheapest and most attractive asset class in existence. I've been puzzled at times with the random price action of a number of our businesses, sometimes a good thing as we can add to our positions, but always serving as a good reminder that business execution and stock prices can often separate for periods of time. I believe our patience will ultimately be rewarded.

Portfolio Commentary

During the quarter I exited our position in Liberated Syndication to make room for newer opportunities I feel possess better risk/reward profiles. I also added to various other holdings and purchased two new investments discussed below, one of which has become a top five position. Across the firm, clients hold between 9-13 positions with the top five making up greater than 60% of client accounts. Collectively, our top five represent a collection of very strong risk/reward profiles as dominant businesses with strong competitive positionings, large market shares, long runways for growth and cash generative characteristics showing no signs of slowing down. Furthermore, they are trading at fractions of what I believe they could ultimately be worth, setting us up for favorable returns moving forward should the market continue to recognize their merits over the next few years.

In addition to what's disclosed below, I also started purchasing two new investments outside of my favored sub-$600mm hunting grounds. These companies dominate their product or service lines, have long runways for growth, are being run by talented management teams, and seem to be incredibly mispriced on conservative estimates of earnings / cash flows a few years out. In addition, multiple catalysts await to unlock value and bring some attention to these businesses moving forward. I look forward to providing more in-depth updates in future letters.

Sold Position

Liberated Syndication (LSYN)

Throughout the past few months, I had been trimming client positions in Liberated Syndication to reduce our exposure to any potential deterioration in the core business that we might face once Libsyn finally filed up-to-date regulatory filings. As of today, we have fully exited. As a reminder, our ownership in Libsyn started as part special situation/part good business with elements of a turnaround (there was an incredible amount of low hanging fruit for management to address) that once addressed, could help shine light on both the strength of the core podcast hosting platform as well as management's entrance into the podcast advertising and monetization spaces, where a new CEO (still yet to be hired) would help drive those initiatives forward. There is also a lawsuit being undertaken by the company set to meaningfully reduce the share count over the next year or so, further contributing to the attractiveness of the opportunity.

Were it not for the special situation elements, I doubt I would have made this investment as the podcast industry possesses a number of very difficult investment characteristics including plenty of competition, low barriers to entry and a rapidly changing industry. In 2004, when Libsyn in was a first mover within the industry, those dynamics mattered less. In 2021, they matter a whole lot. I'd argue that the industry has changed quite a bit since our initial investment just last year. In addition, my worries about the core business have been exacerbated with new, mostly free hosting services rapidly taking share of new podcast users, and the overall business turnaround distracting management from focusing on the core business. I don't believe this is an area where one can take their foot off the gas, and its possible too much damage has been done inside of the core business for Libsyn to now be a meaningful competitor in terms of podcast hosting. To management's credit, they stepped up in a big way by making two acquisitions and purchasing a large number of shares (including doing a private placement where both management and another large technology focused activist fund participated) signaling at the very least their confidence in the setup. The acquisitions should also serve to add some revenue on top of what has been lost within the core podcast hosting business and may even offset any damage done there.

However, several factors weighed on my continued interest in holding on to this business. Not the least of which are the amount of more favorable risk/reward, higher potential IRR investments that sit in front of us, to which I've allocated all the capital from the sale of our Libsyn shares. As mentioned, Libsyn is late on filing several financial reports, and I believe it makes more sense to sit this one out until I can get a better handle on how today's Libsyn looks. A potential nightmare scenario would include opening the newly filed financials only to see a massively deteriorated core business and much less revenue/synergies from acquisitions than expected. I have no issue with investing in turnarounds or acquisition stories, but turnarounds are hard enough on their own, while acquisitions can be more difficult to implement than organic growth, with many more variables, and most importantly, more avenues for things to go wrong. I'm reminded of an important investing heuristic here, which is, if you think you're wrong, don't wait around to find out.

There's a story within NBA circles about former All-Star forward Ron Artest, who, during his prime, lived in Indianapolis with a group of his friends and apparently, multiple dogs. The dogs weren't house trained, so each week they would defecate on the carpets, only for Artest to have the carpets replaced at the end of each month, presumably instead of training the dogs. There are parallels here, as Libsyn seems to be in the process of continuously replacing their carpets, failing to address the root of the problem which is core business deterioration. Although there remain plenty of unknowns at this stage, I'm reminded of an important investing heuristic which is, if you think you're wrong, don't wait around to find out.

Position Updates

Research Solutions (RSSS)

I added to client positions in Research Solutions following a strong Q4 report and after having a chance to digest the recent management changes announced in March of this year. On the surface, these changes don't reveal much for this sleepy microcap, but actually point to a significant development within the business and the continued realization of the initial thesis in place when I first started purchasing shares in 2018. My apologies to clients, however, as you won't be able to talk about this particular investment at your next in person gathering, unless you're interested in putting the guests to sleep. I'd *love* to talk about it, however, as this tiny document delivery company has made a strong transition toward nurturing their fast growing, high gross margin platform business that has become quite an industry presence, working with over 70% of the top 25 pharma companies in the world and currently generating nearly $6mm in annual recurring revenue.

The management changes mentioned above include founder and former CEO Peter Derycz (currently the largest shareholder) stepping into a Chairman role with interim CEO/board member Roy Olivier being elevated to the CEO post on a permanent basis. Peter will continue to oversee product development, while new CEO Roy Olivier brings experience from ARI Network Services, a business he grew from $15 million in revenues to over $100 million before being acquired by private equity firm True Wind Capital. While at ARI, Roy executed a playbook consisting of complementing organic growth with accretive M&A and now brings his skillset to RSSS where during the company's Q4 results presentation, he announced an ambitious but achievable target for the Platforms business to achieve $20mm in annual recurring revenue by 2024, up from $6mm today. Should he achieve that goal, I believe the strength of the Platform business will continue to shine through and the market will value that (now free cash flow generative) business alongside its peers at 7-8x revenues, reflecting a value – saying nothing about the Transactions business - higher than the current enterprise value of the company today.

While results won't be linear, and FY22 points to more of a build year in terms of elevated costs related to investments in people and product, RSSS is on track to generate a decent amount of free cash flow within the next few years, with a renewed focus on business strategy and a path to 100%+ returns moving forward.

New Positions

Basic-Fit NV (BFIT.AS / BSFFF)

One of my favorite investment setups consists of businesses undertaking significant growth investments that mask current profitability but have the effect of increasing long term shareholder value. An attractive aspect of high return growth investments is that they can open up avenues for mispricings because at the business level there is no optical cheapness, should one be focused on paying a low multiple of earnings or free cash flow. This focus on the 'now' can at times cause investors to miss the potential long-term effects of value creation. As a result, qualitative measures tend to be better yardsticks for analyzing value, as evaluating the competitive dynamics of an industry is much more important in determining future value than anything you can discern from publicly available financials. In a market with heavy participation by passive investors and quantitative based strategies, examining trailing financials or attempting to code certain factors into an algorithm might fail to paint the entire picture. The market is forward looking, and *future* value creation can't be uncovered by looking *backwards*. While not all businesses that fit this mold are created equal (I can point to many businesses with negative free cash flow that aren't creating *any* value), ones with customer captivity, a low-cost model, more efficient operating processes, and dominant market share leaders can use growth investments to keep competition at bay and continue to create value over time at the expense of current negative free cash flow.

During the quarter we entered into a core position in Basic-Fit NV which is my attempt at taking the Peter Lynch philosophy of 'invest in what you know' and applying it to client portfolios. I've been an avid weightlifter for nearly 20 years and having held multiple part-time jobs at various gyms, I know this space well and have learned a lot about the industry over the years. The idea was introduced to me by David

Polansky of Immersion Investments, LLC. David and his business partner Tim Delaney recently launched a fund focused on identifying mispriced small and microcap securities. I'd recommend checking them out.

Basic Fit has over 950 company owned gyms in geographies such as France, Belgium and the Netherlands among others, making them the largest fitness operator in Europe. Their offering is simple: a typical subscription costs €19.99 euros per month and gives people access to all of their clubs plus all the benefits of the Basic-Fit App. The company was founded by former tennis pro Rene Moos, currently the largest shareholder, who opened his first fitness club called HealthCity in 1984, and eventually acquired the initial 28 Basic-Fit clubs in 2010. Since then, Rene has expanded the club portfolio to five countries and nearly 1,000 clubs while tripling revenues and underlying club EBITDA from 2014 leading up to the pandemic.

While at first glance the gym business appears to be an average one consisting of low barriers to entry, plenty of competition and some seasonality, scale offers many benefits to the largest players. When constructing a gym, [high fixed] costs come before members, making it difficult for many smaller operators to either test new markets or offer low pricing given the lack of revenues to support multiple players. Scale over which to spread marketing and employee costs, cleaning services, equipment purchasing (in addition to being able to afford rent in the best locations) and technology means Basic-Fit can offer memberships at the lowest prices making them – surprise - the low-cost provider. Therefore, what initially looks like a commodity (low-cost gym membership) actually becomes a competitive differentiator. As a result of the above, in Basic-Fit's geographies where they have established 'clusters' of gyms, it's nearly impossible for mom-and-pop clubs or smaller chains to open new locations given the lack of scale to spread those costs over a larger membership and club base.

In addition, size and access to capital provide additional advantages during periods of seasonality as well during economically weak periods. The pandemic provided a good example of this, as it's estimated by industry insiders that nearly 20% of all gyms have either gone out of business or will be out of business following COVID, with the fragmented European market experiencing considerable decline as well. During the pandemic, Basic Fit did their best to replicate the gym experience and support their members by taking the very significant (but short term) hit of refusing to charge membership fees during periods of lockdowns, as well as providing digital fitness offerings via their app in the form of in-home workout videos and classes. This goodwill engendered during that time has led to tremendous customer satisfaction, reduced churn and explosive membership growth since gyms began to re-open. In fact, September of this year was BFIT's second-best month ever in terms of new memberships, with over 250,000 signups.

This situation bears resemblance to our prior investment in At Home Group, where a glance at Basic Fit's financials would reveal negative free cash flow obscuring the value creation taking place as a result of their large growth capex needs to open new gyms. Their proven ability to enter geographies and open new gyms has led to historical cash on cash returns for mature clubs in the 35-39% range. Able to reach maturity within two years and deliver 40-50% EBITDA margins, Basic-Fit's unit economics strengthen with maturity, as scale advantages with real estate, equipment and marketing lead to increased EBITDA margins. Add in the long reinvestment runway consisting of significant white space across Europe as well as the ability to acquire or takeover old clubs and convert them to Basic-Fit gyms and I would actually *hope* to see a negative free cash flow number well into the foreseeable future.

Although some would argue that the pandemic shifted consumer behavior leading to a permanently lowered capacity for gym goers, there is little evidence to support members not returning to physical gyms. As mentioned above, following re-opening periods in Basic Fit's markets, membership and revenue growth has been incredibly strong indicating that keeping members engaged during the pandemic paid off as customer loyalty and the strength of Basic-Fit's offering is revealing itself. In addition, more severe lockdown restrictions for Europeans during the pandemic as well as less household space for in home fitness equipment indicates at the very least that gyms are not going away, and the quality, low-cost offering should have a place even with the most budget conscious households. Secular growth should serve as an additional tailwind, as share gains from high-cost operators and expansion into new geographies will be bolstered by increasing gym membership penetration across Europe. The penetration rate for European gym goers is still well below the 25% in the US, coming in at 10-15% depending on the geography.

The current business excluding any growth prospects was available to us for less than 10x EBITDA, a low price considering the margin profile, reinvestment runway and strong competitive positioning. This is a business that I estimate has a few hundred million dollars in normalized earnings power, against a market cap only a few multiples above that. As fears surrounding the Delta Variant leading to pessimism among European investors may cause business results (and subsequent share price action) to be lumpy over the next 12 months, I'm confident Basic Fit will return to their growth path and solid execution that was taking place pre-COVID. The same can't be said for Basic-Fit's mom and pop competitors, who for many, if not for the government stepping in with assistance would be out of business, further strengthening Basic Fit's competitive positioning. One industry operator in Europe remarked that Basic Fit is the 'goliath' within the industry. I like that setup as well as our chances to earn good returns by owning this business.

eDreams ODIGEO (EDR.MC / EDDRF)

We also entered into a core position in eDreams ODIGEO during the quarter, a European based online travel agency (OTA) with a differentiated business model that has executed a tremendous turnaround over the past few years and now sports the largest market share in European flights among all OTAs. Predecessor Greystone clients will unfortunately remember our prior investment in Yatra Online, the India-based OTA focused on the business travel market, competing with juggernauts CTrip and Make-my-Trip, among others. Before you start to panic, know that investment mistakes are the best teachers, and while I was wrong on multiple aspects of that investment, our investment in eDreams represents a markedly different situation.

As mentioned, eDreams is the largest leisure OTA in Europe, with leading market share in flight bookings including the #1 spots in France, Italy, Germany and Spain, and #2 in the UK and Switzerland. As cost-effective distribution channels for travel suppliers, OTAs are typically good businesses as they are asset light and require minimal capital to scale, with variable cost structures that provide flexibility to respond to both periods of reduced travel activity and high demand. Although the barriers to entry are relatively low within the industry, OTAs that have reached scale can be very hard to compete against given their brands, supplier relationships, customer bases and in the case of eDreams, technology. As an OTA scales and is able to offer better pricing, selection and service, more customers book travel through them, leading to more suppliers offering inventory, leading to increased selection and more favorable pricing, leading to more customers, and so on. This is the very definition of what is referred to as a flywheel. As a result of this dynamic, leading OTA's typically sport EBITDA margins in the 20-30% range and have historically been valued at above market multiples.

And then there's eDreams.

Compared to its more highly valued competitors, eDreams has some of the strongest travel brands in many of Europe's largest markets, and through its brands GO Voyages, Opodo, Travellink and Liligo, eDreams dominates air travel in Europe with over 18 million customers. The attractiveness of the business model as well as strong value proposition were highlighted during the pandemic, where despite revenue declines of -70% as global travel demand fell off a cliff, the company was able to achieve breakeven EBITDA, while continuing to win market share, expand into new geographies, and grow their customer base.

The two primary elements of our prior investment in Yatra that I both underestimated and got wrong was the speed at which the country's mobile phone usage penetration rate would increase along with per capita income (which should ultimately flow to business travel) but also the need for, and pace at which the company would raise dilutive capital. eDreams stood out to me as the ONLY online travel agency that did not issue debt or equity during the pandemic due to their highly variable cost structure. In addition, eDreams has seen their share of trips booked via their mobile app increase from less than 10% in 2015 to over 55% today. These two data points are significant as they reflect the defensibility of the business model and highlight eDreams attempt to own the entire customer relationship from inception, which has the effect of meaningfully lowering customer acquisition costs via less dependence on Google and other meta-search platforms. This strategy is effectuated by the value proposition to both the customer in the form of lower trip prices and the OTA in the form of sourcing customers.

Efforts to own the entire customer relationship are being bolstered by eDreams subscription loyalty program called Prime, where for €60 euros per year, customers can receive discounted flight and hotel prices, the ability to book discounted group rates, and access to 24/7 customer service. The value prop for customers is huge as the payback period for the loyalty program is reflected in continued cost savings on trips, while value accrues to eDreams in the form of reduced customer acquisition cost, decreased churn and a large LTV uplift on a per customer basis. Prime has grown from *an idea* in 2017 to over 1.5 million members to date, and even grew 55% YoY during the pandemic. Currently, Prime members account for nearly 40% of all bookings, which is set to increase meaningfully as travel demand returns and as eDreams continues to execute.

Leading the charge is CEO Dana Dunne who was brought in to run the business in 2015 and has executed wonderfully. Dana has taken the positive steps of improving the product mix, strengthening the technology platform, growing the Prime program and increasing the customer value prop. eDreams has now reduced their dependence on Google as a source of revenues, increased pricing transparency and diversified their product mix. These initiatives have led to an overall stronger, more profitable business, with EBITDA and free cash flow posting a mid-teens CAGR over the past few years.

As Prime continues to scale, customer lifetime value should expand significantly, which should have the effect of improving the entire margin profile of the business in the form of increased purchasing volume and lower customer acquisition costs. Should eDreams continue to execute, on the back of increased travel demand and growth in their Prime subscribers, I believe it's possible for the business to generate around €150-200mm in EBITDA within the next few years, against a market cap of around €800mm euros. This compares to peer valuations in the range of 16-18x EBITDA. I believe we've given ourselves a significant margin of safety in both the pessimistic assumptions surrounding the business, as well as the large private equity ownership with decade-plus involvement that may be interested in using industry consolidation as an exit path.

Broad Market Commentary

The swift market recovery post-COVID has presented me with some incredibly tough competition in the form of our benchmarks, with the S&P500 in particular rising 30% in the past year and index concentration increasingly driven toward some of the largest companies in the world that continue to defy the odds with ridiculous core business growth and cash generation. This dynamic, touched on above could potentially lead investors to continue to ignore some of our small, illiquid, underfollowed businesses where value may not be apparent on the surface. I'm not seeing the incremental buyer (interested in low volatility) spending much time looking at businesses with a few hundred thousand dollars in trading volume per day, bad trailing financials, multiple business lines that need to be unpacked and valued separately, or a less-than-clear competitive advantage (that involves primary research to uncover). Especially when the indices or large cap growth are returning 20%+ per year.

Additionally, evidence suggests that when investors are faced with decreasing yields in risk free assets, their exposure to risky assets tends to climb. However, instead of public equities, it appears they are increasing their risk in other areas in pursuit of high returns, including credit, selling volatility, and *reducing* liquidity through real estate and private equity. Unfortunately, I don't believe this solves investors' need to diversify (which would look good during a stock market crash) as these actions seemingly replace the risk exposure to equities in favor of other risk assets. Furthermore, efforts to diversify this way assume that these other asset classes will meet their required rates of return. Once they fail to do so, it's my belief that investors will flood back to seemingly overlooked and ignored asset classes and realize the attractiveness of good businesses that are growing, with strong competitive positionings trading at cheap valuations. I continue to believe that time will reward the patient investor, and businesses with combinations of strong competitive positionings, effective leadership and improving fundamentals will serve client portfolios well.

Recent Developments

Greystone added four new clients during the quarter, all of whom 'self-selected' into the firm and all of whom I believe will make great long-term partners. Other than my presence on Twitter and publicly sharing my investment letters, I have done little to no marketing to date as my focus has been to generate good investment returns. In fact, not one client has joined the firm as a result of some outbound marketing or sales process. I'm incredibly proud of this fact, as I am first and foremost optimizing for the right partners.

Speaking of partners, to the 200+ non-clients currently on the Greystone Capital distribution list, referrals are always welcome. If an investment isn't for you, the highest compliment you could give me is an introduction to someone who might be a good fit. As of now, our AUM levels remain far below what I believe to be the capacity of the strategy, and the current investing environment has provided me with more good ideas than available capital.

I was fortunate enough to be invited on two different podcasts during the quarter including The Value Hive Podcast with Brandon Beylo as well as the CO/nversations Podcast from the Co-Investor Club. I had a great time speaking with each host and got to dive into Greystone Capital's background and strategy as well as talk more about our investment in Thunderbird Entertainment.

Finally, I'd like to share what will likely be the best recent update I could imagine, as in August my wife and I welcomed into the world a baby girl, Ava Vincetta Wilk. I'm happy to share that both Ava and my wife Kristin are doing great, and we couldn't be happier. I'm confident I heard somewhere that the best time to allocate to an investment manager is precisely at a time like this, with an added source of motivation!

Thank you once again for the allowing me to serve as the manager of your hard-earned savings. I am incredibly grateful and have made it my goal to reward your trust and patience. As always, please feel free to reach out anytime. Thank you for reading.

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