University of Virginia

DARDEN
Capital Management

THE ADVISOR

Q1 2020

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A LETTER FROM THE CEO

May 1, 2020

To Our Friends and Partners,

Church Waesche, DCM CEO

Since our last newsletter in January, the world has changed in more ways than many of us thought possible in such a short period of time. In light of this new reality, I begin this commentary by extending my sincere hope that you and your loved ones are well, and that everyone remains healthy in the months ahead.

On March 5th, the Class of 2020 walked off Darden Grounds not realizing it would be our last day on campus together. Unbeknownst to us, we would never get the chance to enjoy the Darden in-class experience we all cherish so much ever again. We didn't know we had already sipped our last First Coffee or competed in our final Darden Cup event. We didn't have the opportunity to relish in any of those "last" moments. Instead, we were relegated to online classes and required to socially distance ourselves from each other during a time when we expected to be doing quite the opposite. Moreover, we won't have the opportunity to celebrate the enormous amount of hard work we have all put in over the last two years at graduation on the Lawn. We've been forced to accept the reality that our last quarter at Darden was nothing like we had envisioned.

Despite these unfortunate circumstances, we remain in high spirits and are making the most of the current situation. At Darden Capital Management, many of us were worried that our unique experiential learning platform would be eroded without the shared experience of being in the Capital Markets Room together. After all, that is where the magic of DCM happens. Thanks to technology and the resilience of our teams, we have been able to stay connected rather seamlessly, with weekly meetings taking place via Zoom in what we've dubbed the "Virtual Capital Markets Room." We've also been able to move our Speaker Series online and have found these sessions just as effective as those held on Grounds.

Of course, the stock market and DCM's portfolios were not immune to the negative effects of this crisis. After hitting all-time highs on February 19th, the market quickly sold off, as investors began pricing in the severe economic consequences of COVID-19. In just a few short weeks, we saw our portfolio lose roughly a quarter of its value. The decline was historic in its speed and left many of us in utter disbelief. The dislocation has been unique, as consumers have been compelled to stay at home and most businesses forced to close or operate in a limited fashion due to a public health crisis rather than a financial crisis. More companies have suspended or cancelled their dividends so far this year than the previous 10 years combined. Even high-quality, prudently run companies have seen their businesses and share prices punished.

This unique reality prompted our teams to take several approaches to tackling the current investing environment, with a focus on those things within our control. All teams quickly re-evaluated and stress tested many of our holdings to ensure they could withstand a prolonged period of tough conditions. Ultimately, some teams chose to stay the course, confident in the market's inevitable recovery and their team's ability to tolerate the volatility. Others sold businesses they felt were permanently impaired or whose risk/reward profiles no longer seemed attractive given the leverage on their balance sheets, among other things. Finally, some funds played offense, taking advantage of indiscriminate selling to acquire high quality businesses that will endure far beyond this crisis. All in all, four out of five funds managed to outperform their benchmarks for both the quarter and year ended March 31, 2020.

While many negatives have arisen due to the current crisis, some of which I outlined at the onset of this letter, there have been many positives too. Among the positives is that the last two months have provided our teams with an incredible learning opportunity before venturing into our professional careers. The experience and wisdom gained in just the last few weeks alone is more than some investors learn in a decade. As special as the Darden academic experience is and as talented and brilliant as our faculty are, the lessons we've learned during this unprecedented time simply could not have been realized in the classroom.

In addition to the lessons we've learned organically through managing money through this crisis, we've also had the opportunity to connect with and acquire considerable wisdom from many of our alumni in the investment management industry. Over just the last several weeks, we've hosted nine alumni to speak to DCM virtually. These sessions have enabled us to draw on the collective past experiences of these gracious individuals and solicit their advice on investing and managing money through a crisis. We can't thank them enough for their willingness to provide their time and insights during a period when many of them were likely stressing over their own portfolios and fielding dozens of client calls a day.

In the end, while our class would have loved to be remembered for our investment returns through December 31^{st} and not March 31^{st}, I am confident that we will all look back in several years and realize just how fortunate we were to have gone through the trying experience of the last few months. There is no doubt, we are all better leaders and investors for it.

I'd like to take the last part of this letter to thank a few of the many people who have made Darden Capital Management possible over the last year. First, I'd like to thank the rest of the Executive Team – Clarke Ryan, Bevin Landry, and Trent Hegseth – who were amazing to work with from start to finish. Taking over an already outstanding organization like DCM and trying to make it even better wasn't an easy task, but each of them found ways to contribute in a meaningful manner and DCM is better for it.

Second, I'd like to thank our five Senior Portfolio Managers — Charles Perkins, Adrian Moral, Nicholas Kordonowy, Katharine Watson, and Scott Steever — who proved to be tremendous stewards of capital over the last year. I would invest my personal capital with any of them and I would encourage everyone to read their investor letters in the remaining pages of this newsletter. I'm confident that you all will not only be impressed by, but will also learn a thing or two from these talented individuals.

Finally, my sincerest thanks to our Faculty Advisor, Pedro Matos, and the Mayo Center for Asset Management for their continued support of DCM. They have been incredible partners and played a big role in helping DCM connect with alumni and secure high-quality speakers throughout the year, among many other things. We are grateful for all that they do for DCM.

Looking forward, we are confident DCM is in great hands for the next year. The incoming class, led by the Executive Team of CEO Rachel Gibson, CIO Tim Wills, CFO Sarah Silke, and DOR Daniel Shipman, is as impressive as ever. While we are sad to be handing off the reigns, we are excited about the initiatives that they have laid forth and have already begun to implement to make DCM even better. We wish them all the best!

In closing, I want to reiterate what an amazing experience this has been for me personally. Getting the opportunity to lead Darden Capital Management for the past year has been one of the greatest privileges of my life. DCM was one of the primary reasons why I came to Darden and my experience with the organization exceeded all expectations. The knowledge gained and lessons learned, about both leadership and investing, are ones that I will carry with me and draw from for the rest of my life. I can say without reservation what many of my predecessors have proclaimed: Darden Capital Management is *the* premier experiential learning platform at Darden.

Thank you to all who have engaged with Darden Capital Management throughout the last year. I hope we've made you proud to be associated with DCM and that in one small way or another, the organization has progressed over the past year because of the things we were all able to accomplish together. Thank you again for your continued support!

Sincerely,

Church Waesche
CEO, Darden Capital Management
WaescheA20@darden.virginia.edu

2019–2020 DARDEN CAPITAL MANAGEMENT TEAM

EXECUTIVE TEAM

Church Waesche	Chief Executive Officer
Clarke Ryan	Chief Investment Officer
Bevin Landry	Chief Financial Officer
Trenton Hegseth	Director of Research

JEFFERSON FUND

Adrian Moral	Senior Portfolio Manager
Andres Campos	Portfolio Manager
Zachary Elkaim	Portfolio Manager
Anna Mazur	Portfolio Manager

CAVALIER FUND

Charles Perkins	Senior Portfolio Manager
Vin Paruchuri	Portfolio Manager
Robbie Hoffman	Portfolio Manager
Dalton Werner	Portfolio Manager

MONTICELLO FUND

Katharine Watson	Senior Portfolio Manager
Carson Willoughby	Portfolio Manager
Yujing Sun	Portfolio Manager
Aditya Singh	Portfolio Manager

DARDEN FUND

Nicholas Kordonowy	Senior Portfolio Manager
Jade Palomino	Portfolio Manager
Ragini Bhuyan	Portfolio Manager
Cameron Hector	Portfolio Manager

ROTUNDA FUND

Scott Steever	Senior Portfolio Manager
Ann-Catherine Begley	Portfolio Manager
Waleed Jehandad	Portfolio Manager
Christian Pratt	Portfolio Manager

ALUMNI INTERVIEW SERIES

As we carry through on our commitment to highlight our strong alumni base in the field of investment management, this issue features an interview with Jon Friar of T. Rowe Price. Mr. Friar is a former Chief Investment Officer of Darden Capital Management. We thank him for contributing his time and insights and hope you enjoy reading! We look forward to highlighting other outstanding alumni in the investment management industry in future editions of *The Advisor*.

Jon Friar, Darden Class of 2011

Biography: Jon Michael Friar is a vice president of T. Rowe Price Associates, Inc., and T. Rowe Price Group, Inc. He is the sector portfolio manager for Business Services. Previously, he was an investment analyst in the U.S. Equity Division, following financial companies. Mr. Friar is a member of the Investment Advisory Committees of the Capital Appreciation, Dividend Growth, Growth Stock, Financial Services Equity, and the Structured Research Strategies.

Mr. Friar has 12 years of investment experience, seven of which have been with T. Rowe Price. He joined the firm in 2011 after serving as a summer intern with T. Rowe Price in 2010, covering health care facility outsourcers. Prior to business school, he was an associate in structured product sales for Barclays Capital.

Mr. Friar earned a B.A. in government and foreign affairs from the University of Virginia and an M.B.A. from the University of Virginia, Darden School of Business.

DCM: What do you value most from your time in Darden Capital Management (DCM)?

JF: The opportunity to work closely with smart people that shared an interest in investing. I learned so much from my DCM peers in such a short period of time. I distinctly remember the book list that McGavock Dunbar (Class of ’10) gave me and how generous he was in reviewing my first DCM pitch. I still have the copy of Value Investing by Bruce Greenwald that I bought on Mac’s recommendation and I regularly recommend the book to Darden students that contact me about asset management and equity investing. Gary Ribe (Class of ’11) and I started having regular conversations about stocks and investing while in DCM together nearly a decade ago and that dialogue continues to this day.

DCM: What was the transition like from being an Analyst to a Portfolio Manager?

JF: I still think of myself as an analyst. I’ve always taken a lot of pride in the industry knowledge I developed as an analyst in payments and financials and I’ve always been a little leery of how we sometimes over-value a generalist portfolio manager’s skillset. When I had the chance to be a PM, it was important to me that respect for the analyst was at the core of how I managed the portfolio and ran our team. Nothing about that has changed in the three years I’ve had this position. We see our best outcomes when I’m amplifying the ideas of an insightful analyst.

DCM: What do you believe is T. Rowe Price’s edge? Why has the firm been able to consistently perform at the level it has for such a long period of time?

JF: It’s cliché to say culture, but T. Rowe is a unique place. Every year some of our best analysts and portfolio managers take on new responsibilities and new roles, and still performance remains strong. Putting the client first, having a long-term orientation, and doing true fundamental research are the core of what we do and that doesn’t change. I think what separates us from others is a culture that insists on high quality fundamental research while still being fair to everyone on the team.

DCM: What characteristics make an attractive investment to you?

JF: Over a multiyear period, the best ideas tend to have increasing returns and accelerating growth relative to market expectations. But there are only so many insights like that at any moment. We believe that capital allocation, management, business model, and industry structure are the most important drivers of returns and we lean into names where those characteristics are getting better. I don't think that framework is unique which is why we try to stay focused on the research process. The quote about execution eating strategy for breakfast comes to mind.

DCM: Are there common characteristics/traits that differentiate good investors from bad investors?

JF: I love the question. I'm just not sure there are many universal traits other than hard work and a reluctance to become wedded to prior assumptions. I've seen investors be incredibly successful with different mandates and different frameworks. The investors I admire most work incredibly hard on each idea while remaining flexible to new information as it is uncovered. It's a rare person who can spend months or years working on an idea while remaining open to new information that may require a change in their thesis.

DCM: What are the most common mistakes you see young investors/analysts make? What are the most important lessons you've learned from your almost decade of experience thus far at T. Rowe Price?

JF: Be respectful of management. You can demonstrate this respect not only in tone but also in how you prepare for meetings with management and what level of knowledge you choose to bring to the conversation. Investors are privileged to have access to management and it's an incredible opportunity to learn about the company from the people that know it best. Younger analysts tend to be so focused on their list of prepared questions that they miss an opportunity to let management reveal their concerns and priorities.

DCM: Are there particular companies, industries, or subsets of the market that you find particularly attractive right now? On the flip side, are there areas where you advise investors to proceed with extra caution?

JF: In general, there is greater uncertainty around near-term fundamentals in this environment and the market is putting a lot of value on companies that have high visibility to near-term earnings and earnings growth. Most of the opportunities I am seeing have high near-term uncertainty but their business models, industry structures, and free cash flow profiles allow us to project out beyond this crisis. We see this most acutely in some traditionally high-quality stocks that service small and medium sized businesses.

DCM: What advice would you give to Darden students interested in a career in investment management?

JF: Reach out to the broader Darden network. It's hard to find a job in investment management directly out of Darden, but if you're patient and leverage the Darden network there are opportunities out there. And if your first job out of Darden isn't perfect, stay positive. There are wonderful places (industry, banking, consulting) that allow you to develop the kind of differentiated industry knowledge that fundamental investors value.

Portfolio Updates

CAVALIER FUND

To Our Friends and Partners:

	Cavalier	S&P 500
Year to Date	-19.2%	-19.6%
4/1/2019 - 3/31/2020	-2.7%	-8.8%

In these trying times for humanity globally, we are thankful and appreciative for the opportunity to have managed the Cavalier Fund on behalf of Darden over the past year. While we hate to move on in the midst of such market turmoil, we are confident in the capable team who will steward the portfolio over the coming year. The past two months of our leadership tenure have been extraordinarily challenging and humbling, but managing real capital through this downturn has been an invaluable learning experience. As we have endeavored to remain rational and disciplined in the face of significant uncertainty, the importance of mental fortitude, thorough underwriting, and collaboration has resonated in a new way. We will carry this experience with us as we leave Darden and look forward to building upon it in our careers and life after graduation.

CORONAVIRUS CRISIS

It feels like every aspect of life and markets has been thrown into upheaval over the last two months as the coronavirus pandemic wreaks havoc across the world. The speed and magnitude of the market selloff completely caught us off guard. Over the last few weeks, however, we have been working diligently as a group to quantify the impact that this crisis will have on our holdings. We are meeting with increased frequency to work through each company in our portfolio to assess the near-term effects of the pandemic and to confirm that our long-term investment theses are still intact. While we haven't taken any drastic measures, we have made some adjustments to the portfolio at the margin. We added to names that we felt were showing a temporary dislocation despite the quality of the business, and shifted capital to the most attractive risk/reward opportunities.

As I am writing this letter, many of the stocks have rallied substantially from their March lows. However, there is no way to know if this rally will continue or if pessimism will set in once again. Instead of anticipating the bottom, we remain hyper-focused on identifying which securities we believe are mispriced today. In a recent memo from Howard Marks, he provides some simple yet valuable advice for these uncertain times, "if something is cheap – based on the relationship between price and intrinsic value – you should buy, and if it cheapens further, you should buy more." We are doing our best to be rational and patient, but are also trying to take advantage of good opportunities when they present themselves.

PERFORMANCE & POSITIONING

The Cavalier Fund was down -19.2% in the first quarter, only slightly outperforming the benchmark by 40 bps. Since taking over the portfolio last year, the Fund returned -2.7%, compared to -8.8% for the S&P 500 Index. Our largest detractors during the quarter were Walt Disney (-33.2%), HCA Healthcare (-38.9%), Live Nation Entertainment (-36.4%), and Nexstar Media (-50.3%). These companies experienced heavy selling pressure in March as investors tried to determine the near-term impact from coronavirus with limited information. Two of our largest contributors for the period came from the short book, the Communications Sector ETF (17.5%) and Yelp (33.5% since inception). The only long investment with positive performance over the three-month period was Activision Blizzard (0.1%) as many believe the video game developer could benefit from the current crisis. Costco (-2.8%), Franco-Nevada (-3.4%), and American Tower (-5.2%) also held up relatively well.

Currently, the portfolio is comprised of 21 long and 5 short positions, with the top ten long positions representing more than 60% of capital. The investment team was busy during the quarter developing six new ideas and making position sizing adjustments to reflect our level of conviction. One of our primary objectives was to bolster the short book by adding more names. We had been losing confidence in Hertz and LPL Financial, and eventually decided to replace these positions with three new ideas. So far, results have been mixed.

NEW POSITIONS

In February, we initiated positions in two retailers, **Dollar General** and **Tractor Supply Company.** Dollar General is the leading low-cost retailer in the US, operating half of the 32,000 domestic dollar stores. It excels in a niche market by focusing on rural communities with smaller populations that cannot sustain a large retailer. Its tremendous scale allows for buying power on the wholesale market, which allows Dollar General to price products materially lower than grocery and drug stores. We think the company is very well-run and has strong control over staples distribution in the markets it serves. Tractor Supply Company is a retailer of farm and ranch products and also caters to rural communities. It strives to be a "one-stop-shop" by providing agriculture, home improvement, maintenance, pet care and animal products to recreational farmers and ranchers at low prices. It is the only farm store chain with national scale, and few can compete with the company's unique variety of product offerings. Both companies have a strong rural footprint and their "immediate use" products insulate them relatively well from Amazon and e-commerce disruption. We think that both retailers have good growth opportunities, strong free cash flow generation, and provide a level of downside protection that give us comfort owning them in this type of environment.

At the end of March, we started buying shares of **Zillow** after the stock experienced a sharp selloff. Zillow is the leading internet real estate company that provides an online marketplace for third party brokers and potential home buyers. The company has been transitioning its business to directly participate in real estate transactions by buying and selling home inventory. This new segment allows Zillow to expand beyond advertising revenue and increase its addressable market to include the $1.8 trillion in annual transactions of the US housing industry. We think that Zillow's brand strength and scale makes it well positioned to capitalize on the new market opportunity. While the current pandemic provides some uncertainty around the housing market in the near-term, we think that the stock price reflects a worst-case scenario. Zillow is in a strong financial position with $2.5 billion in liquidity and we believe that they will be able to easily weather the storm, and might even be able to take advantage of it.

We began shorting shares of **Yelp** in early February. Our success in the position has been a function of the broader market selloff and less a result of the actual thesis playing out. While we admit that its sometimes it is better to be lucky than right, we still think that the stock has room to go lower. Yelp competes intensely with Google and Facebook for advertising dollars, and larger competitors have been able to generate substantially higher advertising ROI for their customers. In an attempt to spur growth, management is focusing on new initiatives and cost cutting to improve operational efficiency. We believe that their decision to downsize the sales team to boost margins will have an adverse impact on advertising sales and will ultimately increase customer attrition in the long-run.

We initiated two other short positions during the quarter, **Kroger** and **Wayfair.** Kroger's management has a poor track record of capital allocation, and we think that the pathway to growth is limited. The company has been late to adopt e-commerce capabilities and logistics automation and is now trying to catch up. After the original pitch, it emerged that Berkshire Hathaway had taken a small stake in the company, which boosted the share price. Furthermore, coronavirus stockpiling has increase sales which sent the stock higher in March. While Wayfair has seen impressive revenue growth over the last several years, the company continues to burn through cash and has yet to demonstrate a clear path to profitability. We don't believe that their cost cutting efforts will be enough to generate positive earnings and we anticipate more competitive pressure from Amazon and Walmart. The stock was hit hard in the beginning of March and I elected to short additional shares to maintain exposure. Not long after, management gave an interim business update to assure investors that sales growth was strong and to announce that they had raised additional capital through a convertible note. The stock rallied substantially off of the lows and short covering further exacerbated the move higher. We still think the original theses for both Kroger and Wayfair have merit, but the impact of coronavirus could dictate the direction of these stocks in the short-term. Thus, we are currently in the process of reevaluating both positions.

CLOSING REMARKS

Recently, we have been focused on transitioning the portfolio to next year's Cavalier team. The new team has been navigating the turbulent markets alongside us over the last month and we will continue to work together in managing the portfolio until the end of the school year. We have provided documents that detail our thoughts on all of the positions along with educational resources that focus on investing more broadly. Given the recent market pullback, the second-year class has elected to focus on re-pitching the companies we currently own to provide the new team with a better understanding of core positions and reaffirm our level of conviction.

Overall, managing the Cavalier Fund has been an extremely rewarding and eye-opening experience. We believe that DCM is the best experiential learning that Darden has to offer. We wanted to reiterate how thankful we are for the opportunity and we are excited to see how the Fund progresses in the future. Lastly, we wanted to thank the mentors, alumni, and faculty for your continued support and confidence over the course of the year.

Sincerely,

Charles Perkins
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DARDEN FUND

To Our Friends and Partners,

We hope this letter finds you remaining in good spirits despite the decade being off to a rocky start (it is astounding how much has changed since our Q4 letter was penned!). While the Fed continues to be extraordinarily accommodative in supporting the plumbing of the credit markets and we are pleasantly surprised by the swiftness of the fiscal response from Washington, the actions are akin to pushing on a string in the face of unprecedented stay at home orders across the globe which have caused tremendous market dislocations. In this environment, we feel reassured about decisions we made throughout the year to remove over-levered, cyclical businesses such as Winnebago and Terex from our holdings, and our outperformance compared to the Russell 2000 in this time of stress speaks volumes to the diligence we undertook to manage the fund for what we viewed as the inevitable end of a cycle which was long-in-the-tooth (without knowing that a wet market in Wuhan would be the butterfly which flapped its wings – we were just looking at record low unemployment and an inverted yield curve!). On a serious note, we hope that you and your families are safe and that the global community triumphs over this pandemic in a quick fashion. While we don't believe a V shaped recovery is likely, we feel confident that our portfolio of companies will continue to lead the Darden Fund to outperformance in the years to come.

What follows is a brief update of our fund for the benefit of our friends and partners whose support makes DCM possible.

PORTFOLIO CHANGES

Sell: National Vision Holdings (EYE), February 2020

We exited our position in National Vision Holdings in late February at a gain of 22% overall, and 30% from when we increased our position in May 2019. We had become increasingly concerned with the threat of e-commerce and direct to consumer offerings of prescription eyewear as a secular disruptor to this brick-and-mortar based retailer of prescription eyewear. Additionally, the price volatility experienced this year while the Walmart contract was renegotiated led us to question the long-term economics of the business and how Walmart has substantial leverage in the relationship to extract profits from National Vision through future lease renewals. Finally, we were also concerned with the high leverage of the business in what we viewed as an economy at risk due to rumblings of Coronavirus. This was a smart move as the stock is down over 30% since we sold.

Sell: Apergy Corporation (APY), February 2020

We finally (and painfully) exited our position in Apergy Corporation in late February at a loss of 50%. While we continue to believe that Apergy is a best-in-class oil field service provider with leading product offerings, the fact is we couldn't continue to fight the market. With oil prices today hitting negative territory for the first time in history this appears to be the right move. The stock is down over 62% in the two months from when we sold it. We believe that there is more pain to come to oil field service businesses as E&P firms cut production and attempt to stave off restructuring, and cut our losses.

Buy: Telaria (TLRA), March 2020

We initiated a half position in Telaria after an informative pitch by Jade Palomino who identified this leader in the connected television (CTV) space. As the only independent CTV platform, we believe Telaria holds a sustainable competitive advantage as content publishers will not want to partner with the existing sell-side CTV competitors which are owned by cable companies, their natural competition. Additionally, we believe Telaria's large and expanding total addressable market provides a tailwind which multiplies the gross margin expansion we anticipate as it continues to gain market share in the sell-side premium video publisher category. We initiated at partial position March 5th due to concerns we had regarding COVID-19 and its impact on advertising spend due to anecdotal conversations with a personal friend who publishes newspapers who said her auto clients cut their spend to $0. In retrospect, this was warranted, and indeed we should have waited longer (and sold Grey Television too, another holding with substantial advertising exposure), as Telaria is down 45%

since then. We continue to be believers in the long-term value of Telaria and see its recent merger with Rubicon Project as reinforcing its value proposition to content creators who seek to capitalize on the shift from cable to digital television.

PERFORMANCE

As a reminder, the Darden Fund's investment philosophy is as follows:

> *"The Darden Fund's objective is long-term growth of capital while minimizing the loss of permanent capital, through a diversified holding of companies tracking the sector weights of the Russell 2000 index. We seek attractively valued, small-cap companies with easily understandable business models, and a clear runway to compound free cash flow generation over the long-term. We take the perspective of investors buying businesses, not stocks. We seek alignment of management interests, effective capital allocation, and lasting competitive advantages."*

While the Darden Fund is operated with these long-term objectives at top of mind, we would like to share our performance since taking over management of the fund.

The Darden Fund lost 18.9% during the twelve months ended March 31, 2020. It is worth noting that our benchmark, the Russell 2000 Total Return Index lost 24.0% during this same period. Our top three performers as of April 20, 2020 were **Axon Enterprises** (+42%), **Central Garden & Pet** (+27%), and **Houlihan Lokey** (+23%).

Our bottom three performers were **Grey Television** (-51%), **Cloudera** (-50%), and **Apergy** (-50%). While we exited Cloudera and Apergy, we continued to hold Grey Television, on the belief that political ad spend will provide a boost and that over the longer term the share price should bounce back as advertising spend ramps up as quarantines are lifted.

CLOSING REMARKS

It has been our honor to serve as temporary stewards of Darden's capital and we feel confident the fund will be in good hands under the stewardship of the next class of Darden students.

Thank you for your time.

Sincerely,
Nicholas Lyman Kordonowy, CFA
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JEFFERSON FUND

To Our Friends and Partners,

Once again and sadly for the last time, hello from the entire Jefferson Fund team. It is tough to write to you during the current circumstances but we sincerely hope that you are all staying safe and healthy and for everyone that is experiencing the effects of the pandemic from proximity, our thoughts are with you. I firmly believe that we will all come out of this together and stronger.

This time I wanted to use this opportunity to say goodbye by thanking you all for making this incredible and invaluable experience possible for us. I speak from my heart when I say that this has been the best educational and transformational experience I've had in my life. In the next paragraphs, I want to share with you some of the lessons I learned and how I benefitted from this experience and the opportunities and doors that DCM opened for me.

LESSONS LEARNED

First of all, I want to thank our friends and partners that make DCM possible. As I mentioned in my first letter to you. This is the premier experiential learning experience at Darden and it would not be possible without your effort and support. I want you to know that this experience has a real impact on us students and our lives. Let me speak from my own experience and share with you how it changed mine. From about 6 years ago I decided that I wanted to pursue a career in investment management and I crafted a career path to achieve this. As part of that career path, I came to Darden with one and only one goal in mind and that was to get a job in investment management. I knew that DCM was going to be fundamental to achieve this goal and since my first days at Darden I committed to being as active as possible in DCM. I can now say that thanks to DCM, the experience it provides and the network it opens for its students I was able to fulfill this goal. I can't thank you enough for this opportunity and I will forever be grateful to all of you, Darden and DCM.

One of the goals we had set as a team as part of our experience managing the Jefferson Fund was to develop our very own investment philosophy. I can say that after a year learning from the great minds of our preceding teams and a whole other year managing the Jefferson Fund I have developed my very own investment philosophy built on top of different frameworks and mental models that I learned during the past two years and I think this has not only been fundamental for my personal development but will continue to be for years to follow in my professional development and career.

As mentioned in the last letter one of the biggest challenges that we faced was approaching portfolio changes given the quality of the companies that we own. I think we all learned from this experience and we, as a team, successfully developed a framework and process to approach this situation. I can say that I have personally learned from this experience and I want to believe that we have also left our mark in the Jefferson Fund.

Finally, DCM gave us a once in a lifetime opportunity. Not everyone gets to live, experience, and learn from an unprecedented market environment as close as we did during our student years. I believe that although this has been an incredibly challenging time it also has been a learning experience that we will never forget and we will talk about in years to follow.

PORTFOLIO CHANGES

Next, I would like to walk you through some of the decisions and changes we made to the Jefferson Fund during this final quarter. We made several changes to the portfolio not only in reaction to the current pandemic and its effects on some of the industries to which our portfolio was exposed but also in anticipation of our transition of the portfolio to the new team and as we wanted to leave them with very high-conviction names and enough runway to make opportunistic investments.

Buy: Alphabet (GOOGL), March 2020

We initiated a full position on Alphabet. I wanted to pitch Alphabet to the Jefferson Fund and pair the analysis with our current holding of Facebook. I believe these two are and will continue to be the two big winners of the fast-growing and world-changing industry of digital advertising. However, I believe that Alphabet is poised to gain the upper hand over Facebook, as Facebook deals with the indirect competition for time-spent on the internet or on different forms of entertainment, something that Alphabet does not have to worry about as they do not own the platforms competing for the attention of users but the platforms used to navigate and communicate through the digital space and tools used daily by users' to make their lives easier.

Buy: Broadridge Financial Solutions (BR), March 2020

We initiated a full position on Broadridge Financial Solutions. Given the market environment during March we found an incredible window of opportunity to buy Broadridge Financial Solutions, which is an incredible business with a long-standing and sustainable wide-moat, at what we believe was a price below its intrinsic value. For this new pitch, we used our previously mentioned framework of reassessing current holdings together with a new idea and we analyzed S&P Global together with Broadridge Financial Solutions. See below for our assessment on S&P Global. (Please find the attached pitch for Broadridge Financial Solutions in the Featured Investment Ideas section).

Sell: Eastman Chemicals (EMN), March 2020

We sold our position on Eastman Chemicals. As you remember at the beginning of our tenure and as part of one of our first decisions, we decided to initiate a position on Eastman Chemicals as an opportunistic investment. This investment not only was not fruitful over the subsequent months after the purchase but also it was especially affected by the recent market environment. We decided not to leave the succeeding team with this position and we sold our position at a heavy loss. This was a tough and painful decision but I can say that I have personally learned from it.

Sell: S&P Global (SPGI), March 2020

We sold our position on S&P Global. As part of our reassessment of S&P Global we concluded that although S&P Global is an incredible business, it lacks reinvestment opportunities. S&P Global is an outstanding high-quality business. It has not only been capable of maintaining an incredibly high and steady operating margin but also has been able to grow it for the past 7 years. S&P Global has been able to achieve an astounding average EBITDA-to-Free Cash Flow conversion of ~70% and ROIC of ~46%. All these points are evidence of the incredible quality of the business. However, the problem is that there is not much reinvestment into the business, therefore there are no opportunities to take advantage of the incredibly high returns they can earn on invested capital. This may be caused by either the fact that there are no investment opportunities in which they can earn those same returns or that there aren't any other areas in which they can grow smartly. This is evidenced by the fact that S&P Global has been returning ~80% of its FCF in the form of buybacks and dividends to its shareholders over the last 4 years, putting the reinvestment strain on us shareholders to reinvest that capital somewhere else. One of the biggest lessons I learned during this past year was this next concept. It doesn't matter if you have a savings account that can return 100% each year if you can only deposit $1 in it. This is similar to the situation with S&P Global. For this reason, we thought that investing in Broadridge Financial Solutions was a better option for the Jefferson Fund. Finally, one other thing I learned from this and from living through the market environment during March was to approach evaluating selling incredible businesses during market times like these in favor of incredible investment opportunities and to evaluate the decision not only from a comparative analysis of the businesses but also from a perspective of opportunity cost.

Sell: United Rentals (URI), March 2020

We sold our position on United Rentals. This was an incredibly tough decision as this is personally one of my favorite pitches from the team that preceded us. However, we thought that United Rentals operates in an industry that will likely get hit pretty badly from an economic slowdown and therefore from an opportunity cost angle there may be better investment opportunities for the near future given the current market and economic environment.

Sell: Booking Holdings (BKNG), March 2020

We sold our position on Booking Holdings. Ever since the last couple of months of last year, we started to lose conviction on Booking Holdings and the whole travel fare aggregators industry given the increase in fierce competition from Google. If we add to that the effects of the current pandemic on traveling, we firmly believed that the Jefferson Fund is better off investing that money elsewhere.

PERFORMANCE

Finally, as it has been usual, I would like to finish by updating you on the Jefferson Fund's performance hitherto.

The Jefferson Fund lost 6.0% during the twelve months ended March 31st, 2020 reversing and more than offsetting our gains during the first nine months of our tenure. It is worth noting that our benchmark, the Russell 1000 Value Total Return Index lost 17.2% during this same period. Our top three performers as of April 17, 2020, were **Microsoft** (+62.3%), **Activision Blizzard** (+46.9%), and **American Tower REIT** (+28.9%).

On the other hand, our top three detractors were **Eastman Chemicals** (-39.3%), **Mylan** (-32.7%), and **Realogy** (-27.1%). Two of our bottom three performers (Eastman Chemicals and Realogy) are companies that we have sold out of our portfolio.

CLOSING REMARKS

To conclude this letter, I want to reiterate that it was truly my honor to have your time and attention through these letters and to manage the Jefferson Fund during the past year. I can't thank you all enough for your effort and support and everything that you do for DCM and to make this invaluable opportunity and experience possible for us.

Gracias totales.

Sincerely,
Adrian Moral
MoralA20@darden.virginia.edu

MONTICELLO FUND

Greetings,

I hope this note finds you and your family safe, healthy, sanitized, and social distancing.

“It’s called a shock for a reason. If you’d have expected it, it wouldn’t have been a shock!” – *Unknown*

OUR YEAR IN SUMMARY

Over the past year, our discussions consistently centered around whether potential investments were fairly valued or overvalued by the market. We’d have preferred to discuss discounts to intrinsic value and kept crossing our fingers for some kind of investable market correction. First, we were hoping for a correction to invest in companies at real discounts. Second, we were keen for the learning opportunity a correction would provide. Since we took on the Monticello Fund in March 2019, the market steadily trended upwards. We were excited for the opportunity to make big bets, but we were always concerned about investing our dry powder at the market peak and having nothing left to invest when prices finally fell. Instead of making big bets at potentially high prices, we invested only a couple percentage points of our AUM into any given name.

The market chaos started just before we embarked on our “staycation” spring breaks. As we departed from Grounds, we analyzed three strategies: 1) move to cash, 2) rebalance our exposures, or 3) do nothing. We decided to stay the course and made no changes to our portfolio. We knew the Monticello Fund might face some tough times. We didn’t think we’d experience a *planetary* shock.

OUR FUND AND PERFORMANCE

Though affected by the COVID-19 market chaos, the Monticello Fund still generated 400bp 1-year alpha, and 320bp 3-yr alpha over the MSCI ACWI, our benchmark. Analyzing our performance over time has taught us to be cautious about measurement. From March through December 2019, the fund’s value appreciated by ~16%. Yet, as measured from March 2019 through February 2020 (the portfolio’s bottom to-date), the fund depreciated in value by ~16%. Year-over-year as I write, in the midst of the market chaos, our actual fund performance is approximately flat. Market turmoil is a humbling and sharp professor. It’s hammering into me more than any textbook or case study the importance of unbiased measurement, the realities of standard deviation and black swan events, and that perhaps returns, on average, really are mean reverting over time. On average, our fund has earned alpha since inception. Amidst the market chaos, I questioned how we accomplished such a feat.

SEEKING ALPHA: SKILL, LUCK, PASSION, AND PERFORMANCE

Academics, professionals, and Main Street investors have debated for years about how much of investing is skill versus luck. When our portfolio value rose from ~3.5M to ~4.1M in the time we managed the Monticello Fund and consistently outperformed our benchmark, our team felt pretty good. Our outperformance led me to question how we as new, unexperienced investors generated alpha. We didn’t learn it from a Darden case or undergraduate textbook, so where did it come from?

I believe the Monticello Fund portfolio management team generated both positive and negative alpha.
We generated positive alpha through our passion, candor, and diversification. Our professor, Pedro Matos, placed management of the Monticello Fund into the hands of a diverse group of individuals with varying interests and biases.

Carson is big on industrials, tangible products, and monopoly or duopoly structures; Yujing had a broader focus and increased the healthcare technology exposure into our portfolio. Aditya is our tech guy – he can't get enough of what's hot and what's not, and he's not afraid to change his mind or share a fresh idea. I'm the nerd who's obsessed with the financial services industry.

Each of us contributed expertise and interest in our own passion projects, but also rolled up our sleeves to value other industries that piqued our curiosity. When one of us considered pitching in another's interest area, we leaned on each other to temperature-check the company even before it was pitched. We've been healthy skeptics of each other's ideas. I believe it's the passion and candor of each Monticello Fund portfolio management team that has led to the positive deviation of our returns from our benchmark. This passion also led us to deviate from our benchmark in our holdings. To quote a former DCMer Mike Kellett, "We also do not believe that diluting relative returns (and more closely mirroring the benchmark) by investing in an index ETF is true to the ideals of DCM – we are here to generate great returns over the long-term by using our critical thinking skills and Darden education to understand the qualitative aspects of great businesses, then using our human judgment and discipline to buy those stocks when they offer us attractive prices." Not infrequently did I check the top holdings of our benchmark the MSCI ACWI and consider why and how our performance deviated. In part, it deviated because our top 10 holdings include a diverse group of high-quality companies that haven't been the top targets of momentum trading. These same companies (WMT, BRK, DE, JNJ) propelled us forward through the market upticks for the past few years and have kept our returns more stable and upward sloping over the past month of downward spirals and wacky volatility.

Our negative alpha came from not following through on a commitment to follow some wise words from Charlie Munger we'd stumbled upon last year: "You have to stick within what I call your circle of competence." When we took on the Monticello Fund, we identified a few holdings about which each of us was relatively ignorant, namely in the mining, chemicals, animal farming, and energy sectors. While we selectively researched and cleansed the portfolio of a few names (e.g., SQM, IBA), we kept a few companies that we didn't think were necessarily bad holdings, but that we didn't know inside and out and didn't have significant conviction. While some of these have performed well, we'd have been better off had we exited a few (AER (-51%), TOT (-33%)). For other names (SYF (-50%), DFS (-50%)), we'd waffled whether (and which) to sell until we'd completed more detailed research. Waiting to make a trade until we were better informed was a fine strategy so long as the market kept creeping upwards, but when the music stopped and the pandemic hit, we were left dancing for too long. We should have been more confident to trade based on our gut feeling. Whether going for a joyride or driving off a cliff, the market waits for no one. I hope to remember this the next time around.

Part of our performance over the past year has been due to luck. Our top performers are MSFT (+34%), AAPL (+34%), and WMT (+16%). These companies have been the apple of many an investor's eye, regardless of their strategy. I've fought hard to keep these as our two largest positions, rather than trimming either. Why would I trim a stock that I believe will continue to outperform most others? In the case of MSFT and AAPL, I don't think we keep either in our portfolio due to any real skill we have. We keep them there because we think they're great companies that we and everyone else continues to love, and we're ok dealing with some volatility. They keep making us get lucky, and we think it will be a while before the Law of GDP and mean-reversion force their returns to level off. These companies have proven to us that it is possible to enjoy holding great companies at fair values.

RECENT TRADING ACTIVITY

Since the last time we distributed this newsletter, we purchased shares in Visa (NYSE: V) and MercadoLibre (NASDAQ: MELI). We sold Industrias Bachoco (NYSE: IBA) and Citizens Financial Group (NYSE: CFG). One of our goals was to rotate our financial services industry holdings. Visa drew our attention because of its revenue-driven margin expansion and market leadership in core franchises. The company has been making intelligent and "first-to" investments, partnerships, and acquisitions in disruptive/systemic related financial technologies. We believe these will be accretive to the company's near- and long-term global leadership and returns to shareholders. MercadoLibre stood out to us as an alternative to investing in private or overpriced peers and provides desirable exposure to Latin America. We believe MELI will continue its revenue-driven growth through existing and new customer acquisition, particularly in serving underbanked, underserved, underdeveloped, highly fragmented markets with FDI inflows. A copy-cat of Alibaba, FlipKart, and Amazon, MELI is embedding ecommerce into daily life across decentralized marketplaces in markets with little other competition. As part of our financial sector rotation, we exited CFG. Not only is its exposure limited to the US, which does not fit with our global fund objectives, but management consistently fall short of value creation targets in both business and acquisition activity. We grew tired of waiting for CFG to protect and enhance its foothold in the northeastern US, but it keeps chasing geographic and expertise expansion in areas in which it does not have a competitive advantage. We also grew weary of IBA. The company operates in a low growth industry (commodities) with falling consumer demands and rising input prices in both the near-term and long-term. Further, it provided geographic exposure only to Mexico and the US. With our purchase of MELI, we gained more desirable exposure to Mexico. And, we're comfortable with many of our other holdings providing exposure to US equity markets.

CURRENT STATE OF THE MARKET

Usually our fund meetings are characterized by intense, yet respectful debate and disagreement before we arrive at consensus decisions. Since the pandemic hit, our disagreements have been few. We believe that the erosion of company fundamentals is lagging the erosion of market value. If the market is efficient, this makes sense. The market should be valuing future cash flows and future risks. However, we also agree that the value destruction as measured by market capitalization declines in March went too far. The market overreacted to move against many companies before they could even be hit by supply and demand shocks or regulatory changes (e.g., SYF share price dropped by more than 50% in March alone). Some of these shocks will not materialize, while others will be worse than the market anticipated. The overcorrection hit the entire market, regardless of industry. This nondiscriminatory correlation among equity price movements is concerning because it is not reflective of the diverse states of the fundamentals of industries, let alone idiosyncratic risks. This is just one of many signs that market inefficiencies are abound.

While we'd love to think the market has bottomed out, we're cognizant that once companies start to release poor earnings, when a vaccine hasn't saved us all by June, and the economic recession really hits, things could get much worse. This has made it difficult for us to feel convicted to invest more now or hold off for another few months. We have our eyes on several holdings that we believe are great companies, such as Visa and Alphabet, and we'd love to invest more heavily in these firms. Yet, we're being patient. For example, though Visa should prove resilient, the company is suffering as customers cut back on expenditures. It's a great company, but we'll hold off on adding to our position until we're a little further through the muck.

THANK YOU, TO DARDEN, DCM, AND OUR INVESTORS

Thank you for providing us with the opportunity to manage real funds as part of our Darden education. In full disclosure, none of us on the Monticello Fund have ever worked through a crisis. In 2007-2008, we were just starting college. When we graduated, the economy was recovering. This recovery lasted until now. As we emerge from Darden into the business world, our opportunity to manage the Monticello Fund through COVID-19 provided us with a (very) small taste of "hand's on" crisis management. When the next crisis hits, we'll be able to leverage this experience. We're thankful we weren't totally sitting on the sidelines for the planetary pandemic of 2020. It's true, we weren't fielding frantic investor calls or watching the stock price drop 3% in the time between entering the # shares to trade and execution, but at least we have some little experience. DCM may have provided us with the best learning experience we've had in over a decade. For this, we thank you.

It's with bittersweet excitement that we hand over the reins to the rockstar incoming DCM class. We've tremendously enjoyed being a part of DCM and sharing our learning experiences with you. Please do keep in touch.

All the best,
Katharine, Yujing, Aditya, and Carson

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ROTUNDA FUND

Dear Friends and Partners,

I write to you today for the last time in these strange and challenging times, with well-wishes for the health and financial stability of you and your loved ones. Hindsight is always 20/20, however it would have been particularly difficult to predict (excluding Bill Gates)—and even more so to act on said prediction—a global pandemic to the effect of the COVID-19's scale and its effect on the lives and livelihoods of ourselves and those close to us. With all that has transpired since our last letter, it has been easy for myself and likely a large part of you to become engulfed by the minute-by-minute news updates and subsequent market reactions. So before diving into the pandemic's effect on the Rotunda Fund, our thoughts on the market's reaction, and our tactical reactions taken to best position the fund in this time, I would personally like to reiterate our wishes and focus on the well-being of you all and those close to you—this pandemic is a global health emergency first and foremost.

It is bittersweet to be signing off of DCM in such an interesting and opportunistic time in the investing world, particularly in the ESG space. The recent outperformance of ESG-tilted active portfolios and passive vehicles reinforces our original investment thesis and reinvigorates the industry, as unprecedented levels of capital flows into various strategies of ESG ETF's. Similarly, with the market swinging wildly throughout much of March, the door of opportunity to move on several overreacted-upon securities and sub-sectors has swung wide open. However, much like life itself, all we can truly leave behind to the portfolio is what we've created, and our words of wisdom and experience gathered over the past year – something I will briefly touch on later in the note. Despite all of this, I am proud and excited to be leaving the portfolio in extremely capable and diligent hands of the rising class. Strong contributions have been made throughout the year by the new team, and I am confident they will continue to improve the fund's structure and performance, and take advantage of the unique opportunity afforded by you all, our stakeholders, over the next 12 months.

PERFORMANCE

As of March 31, 2020, the Rotunda Fund, which comprises $3.2mm (19.4%) of DCM's aggregate $16.5mm portfolio, ended the first quarter at a loss of (-22.0%), in comparison to the S&P 500 benchmark of (-20.0%) for a net underperformance of (-2.0%). In viewing the fund's performance since our team has taken over, the fund is down (-12.0%) relative to the S&P 500's (-8.8%), for a net underperformance of (-3.2%). While this underperformance is a tough pill to swallow, both for you as stakeholders and shareholders, and us as ultimate owners of these losses, we feel optimistic about the long-term outcome of the fund and understand that several key major losses were the vast contributors to this underperformance over the year. Additionally, in taking these lessons and working heavily with the next year's class, we are positive that the transition will be seamless and that a tradition of tribal knowledge has been passed on to ensure nothing falls through the cracks.

The top contributors to our performance across the last quarter have been: Gilead Sciences, Inc. (NASDAQ: GILD), American Water Works (NYSE: AWK) and NextEra Energy, Inc. (NYSE: NEE), returning 11.16%, (-6.16%) and (-8.54%), respectively. While the healthcare sector on the whole had a strong performance this quarter, being both a defensive industry as well as extremely relevant and news-packed given the global circumstances, Gilead was a standout performer as they became a centerpiece player in the COVID-19 response with their ongoing Phase III trials of remdesivir, a leading antiviral in the race to a vaccine. Similarly, our asset-heavy public utility stocks have outperformed as the market shifts to a value-oriented opportunistic market environment. With NEE and AWK being best-in-class ESG companies, we expect their popularity to continue to attract retail passive capital flows as the consumer has shown its tendency to prefer publicly responsible companies in times of duress.

Top detractors from performance across the first quarter included: Delta Airlines, Inc. (NYSE: DAL), Capital One Financial

Corp. (NYSE: COF) and V F Corp. (NYSE: VFC), returning (-59.57%), (-56.88%) and (-51.43%), respectively. While we, as a fund, remain long-term and value-oriented in the execution of our ESG thesis, we acknowledge the cyclicality and try to limit our exposure during risky times in the market. In this vein, our timing was especially unlucky in our purchase of DAL in January. While we still believe DAL is poised to become the head-and-shoulders leader within the airline industry, we had not anticipated the severity of the global pandemic and its related effects on global travel closures, and unfortunately were caught out of position and have absorbed the short/medium-term losses. Similarly, VFC still provides sound underlying fundamentals core to an investment, however resides in an industry currently under severe distress. While VFC's underlying brands are somewhat protected given their diversified customer portfolio, they are still subject to the same top-line and vendor issues the rest of the industry is facing; albeit less-so-much. COF was re-evaluated in early March and deemed to be cyclically and fundamentally deviating from our investment thesis, and in a tough environment, we cut our holdings.

A GLOBAL PANDEMIC ARISES

Needless to say, the broadness and depth of this pandemic far exceeded our, and most experts', bear-case scenarios. Admittedly, we were caught flat-footed on a few of our legacy and new holdings; through our forecasting, we had decided the effects of COVID would be short-lived, temporary and wouldn't severely alter the long-term fundamentals of many of our holdings. While we still vehemently stand by the application of this thought towards many holdings, we have since revised (both upwards and downwards) our thoughts on several industries, and seen encouraging performance from ESG holdings and funds. Similarly, in times of market turbulence, we witness and thus shift our valuation thoughts and portfolio composition to a value tilt and divest from several market-reliant growth names.

As the quarantine time extends and further tamps down airline EPS expectations significantly in the short-term, as well as spiraling their capital requirements and cost structures in the medium term, we see a more socially-oriented issue for long-term losses rise to the surface. Airlines have begun losing mass brand equity from consumers through the "mothballing" of airlines in an attempt to curtail their operational expenses, reduce supply and stabilize a heightened price level in the short-term. This, combined with what we believe to be an implicit backing by the government (as an essential national product and service, as well as an anti-trust barrier), as well has created a quasi-regulated environment without necessary legal consumer-protective measures in place that would be standard for a regulated industry. While, from a financial standpoint, these measures may create a valuation floor for the airlines – this also creates a substantial opportunity for certain airlines to claw back brand-equity in an industry whose revenue split errs more and more towards more price inelastic business travelers. DAL, which has delivered quite a blow to our returns, still remains best-in-class and poised to outperform in what we expect to be a vicious competition once travel restrictions lift.

This turbulent time has also created many opportunities moving forward. Specifically, within the ESG space, we are seeing the outperformance of holdings and funds in these times. Some of this can be attributed to capital flows, where in times of global distress a camaraderie bias takes over a large part of the retail universe. However, a significant portion of this derives from the ESG-oriented competitive advantage. Consumers in such an empathetic time, have become more active with their wallets in terms of buying from socially conscious and responsible companies. Additionally, treating your employees fairly and empathetically in a time of crisis can be a source of competitive advantage in the short and long-run when competitors are forced to resort to layoffs or furlough – the battle for talent is especially highlighted amongst blue-chip enterprises. This stability and outperformance can be illustrated through the performance of socially oriented fixed income instruments relative to the market.

In viewing industries who are poised to outperform on their ESG, as well as their core business metrics, the industries which we have been screening to identify best-in-class financial and ESG performers are: biotech of all capitalizations (for different reasons), and specifically orphan drug-oriented companies. We also see chronic-disease device and software manufacturers (e.g. TNDM, DXCM) strongly positioned to continue their high-growth stories and be attractively valued growth-stocks in a beaten down environment.

CLOSING REMARKS

In closing, on behalf of our team, I want to thank each and every one of you for staying with us, paving the path forward and providing us the unique opportunity to learn, experiment and grow as students and investors. This was the reason many of us chose Darden, and it more than lived up to its reputation, and was an incredible opportunity and source of pride and responsibility that we all relished week in and week out. As we look towards the future, I am confident that the hard work the many generations before us left us, as well as that small piece left by our team, will leave a lasting mark on the tribal knowledge and foundation of the Rotunda Fund and ESG and socially responsible investing, ensuring a smooth transition and learning experience for those generations to come. We are eternally grateful for your time, trust and advice for the years preceding and throughout our tenure.

Looking to the a potentially turbulent and exciting future, I am extremely proud and have the utmost confidence and respect for Hannah Coffin, Hyder Chowdry, Mollie Laverack and Hedan Liu as the 2020-2021 leaders of the Rotunda Fund. With every succeeding generation, a new wave of passion and understanding for sustainable and impactful investing washes over the market and those before them. We appreciate your large part in giving us one small part in contributing to this mission.

Please do not hesitate to reach out with any questions, comments or suggestions about our time or decisions while in charge of the fund, or anything else. We are all incredibly passionate about ESG investing and love chatting and learning from alumni – a hallmark of the Darden experience – and are looking forward to connecting with all of you. Wishing you all safe and healthy wishes.

Sincerely,

Scott Steever
SteeverS20@darden.virginia.edu

Featured Investment Ideas

YELP, INC. (YELP)

TARGET PRICE: $26 (-20%)

Charles Perkins, Cavalier Fund

Company Data	
Price	$33.96
Market Cap	$2.3bn
Enterprise Value	$2.2bn
EV/EBITDA – NTM	8.3x
P/E - NTM	34.4x

Company Description:

Yelp is website/mobile app that allows consumers to discover, review, and interact with local businesses across many different sectors. Through product reviews, tips, photos and videos, users are able to make better buying decisions and share their own experiences. Users can also transact directly with local businesses and to make reservations and schedule appointments on its site. The platform also creates an opportunity for businesses to reach out to potential customers by providing advertising space, which is Yelp's main source of revenue. The majority of advertisements are sold on a cost-per-click basis. Yelp primarily focuses its operations in the US and Canada after winding down its international business in 2016.

Executive Summary:

Yelp competes intensely with Google and Facebook for advertising dollars, both of which have been able to generate higher advertising ROI for their customers. Since its IPO in 2012, Yelp stock has significantly lagged the broader market. In an attempt to spur growth and boost the stock, management is focusing on new initiatives and cost cutting to improve operational efficiency. Instead of investing in salesforce productivity, the company is downsizing the sales team with the belief that margin expansion simply comes from improving its cost structure. The reality is that the business model is mainly based on driving new account growth in excess of attrition, which is heavily reliant on a commission-based salesforce. Early warning signs of lower advertising efficiency have already surfaced in the local advertising sales business (~65% of revenue) which has declined so far in 2019. The transition to non-term advertising packages and "self-serve" model will create interim volatility with higher customer churn over time. Management believes that their new strategy will lead to mid-teens revenue growth and substantial margin expansion in the near-term. These aggressive assumptions require perfect operational execution, which something that the company has yet to deliver.

Investment Thesis:

1. Intense Competition Within Digital Advertising: While Yelp will continue to benefit from the secular trend of online local advertising spend in the US, the company competes directly with Google and Facebook who dominate the market. Google, in particular, has been focusing more on its local advertising business through local search and Google Maps. Google is the gateway to internet search and local businesses can pay for prominent placement in Google search results with more attractive ROI metrics. Even though it competes directly with Google, Yelp also relies on the search engine to drive a significant amount of traffic to its platform. Any changes to Google's search algorithm can have outsized impacts on Yelp's traffic trends. There is still significant runway for advertising penetration of local businesses, as only 4% of the ~3.7mn claimed businesses on the platform actually use it to advertise. However, it will be difficult to gain share from Google and Facebook and the increased competition will likely result in lower ARPU and net additions over time.

2. Strategy Shift Will Increase Churn: Yelp is changing the model in which it sells advertising. Historically, its sales team was responsible for attracting new businesses to its platform, but now the company is downsizing its salesforce and relying on the companies to initiate a relationship. This "self-serve" model allows businesses to purchase advertising directly on its website without having to go through a sales representative. While this cuts down on personnel costs, it runs the risk of reducing customer volumes over the long-term. Due to the highly fragmented SMB market, a large commission-based sales force is necessary to secure new customers. Additionally, Yelp is transitioning away from fixed-term contracts that locks the customer in for a specified period to non-term contracts. Non-term contracts provide more flexibility for the customer, but makes results less predictable as advertisers now have more discretion over when they advertise on Yelp. In both cases, Yelp is attempting to boost margins by reducing marketing expenses, but will likely increase churn in the process.

3. Overly Optimistic Growth Projections: As part of its turnaround plan, Yelp is targeting a ~17% compounded annual revenue growth rate from 2020-2023. Management believes that top line growth will be driven by secondary markets such as Home & Services and National Businesses. While Yelp has experienced recent sales momentum from these segments, it will be difficult to capture incremental customers given alternative outlets for digital advertising with higher ROI. Management also expects operating margins to increase from 19% to 30-35% by 2023. This assumes a significant reduction in Sales & Marketing expenses which the company hopes to realize through a reduction in sales representatives. Sales leverage is inherent in Yelp's business model, and the margin improvement is largely predicated on the company's ability to achieve its revenue growth targets which are deemed very aggressive. Executive compensation is almost entirely related to stock price performance and management's growth strategic plan could just be a way to artificially inflate compensation packages.

Valuation:

Valuation was derived using a combination of DCF and multiples approach with 3 operating cases. A summary of the outputs and key drivers is presented below:

Scenario	Price	Upside to Current Price	Description
Bull	$17	46%	Assumes stagnant revenue growth as churn increases, with terminal growth of 2%. Operating margin expansion from cost cutting. Failed strategy shift keeps multiples low.
Base	$26	20%	Assumes revenues increase HSD in near term slowly declining to terminal growth of 2.5%. Operating margin expansion from cost cutting. Multiples remain depressed because lack of op execution.
Bear	$52	-61%	Assumes LDD revenue growth as advertising model gains traction and terminal growth of 3%. Operating margin reaches management target. Multiples re-rate higher on growth story.

The DCF approach is based on a 6-year forecast period and the base case scenario assumes a terminal growth rate of 2.5% and a WACC of 9.3%. I am using both an EV/EBITDA and P/E multiple to determine an appropriate range for the stock. Currently, Yelp is trading at 8.3x NTM EBITDA and 34.4x NTM earnings. Valuation remains below historical levels, but higher than most of its peers.

Risks:

1. Changes Spur Faster Account Growth: The move to "self-serve" could provide customers with the desired flexibility to advertise on Yelp, and non-term contracts may be more appealing to certain users. Additionally, better than expected sales force productivity could provide an inflow of new paying accounts that could offset a decrease in average revenue per user.

- **Mitigant**: Cutting the sales force will likely have a negative impact on productivity at a certain point. Historically, there has been a strong correlation between sales headcount and advertising revenues.

2. Growth in New Initiatives: Yelp has been investing in new initiatives to supplement its advertising revenues. Transaction revenues are mainly from an online food ordering partnership with Grubhub and subscription revenues are generated from its reservation system, which allows customers to make reservations or check wait times online. Management believes that there is a lot of potential to monetize these services, and also views the restaurant vertical as a way to acquire new users at a lower cost.

- **Mitigant:** Advertising still makes up 96.5% of the sales mix and will be the largest contributor to the bottom line in the near-term. In 2018, Yelp generated approximately $20-$25mn in operating losses from Nowait, Reservations, and WiFi as they have yet to gain significant traction. For comparison purposes, Booking Holding took a nearly $1bn non-cash impairment charge against OpenTable's goodwill as similar initiatives failed to transpire for the company.

3. Capital Allocation Upside: Yelp remains in a good financial position with little debt and $381mn of cash on the balance sheet. The company has increased its stock buybacks recently and is now emphasizing its repurchase program as a way of enhancing shareholder value. Further share repurchases may put a floor on the stock price and demonstrate to investors that management is serious about finally rewarding its shareholder base. Additionally, the asset light business model and healthy FCF generation could be viewed favorably by financial or strategic buyers that might pay a premium to acquire the company.

- **Mitigant:** Yelp has a poor track record of capital allocation and has prioritized value destructive M&A at the expense of shareholders (see appendix). With no direct comps, it is hard to believe a strategic buyer would want to acquire the company, especially with its bloated cost structure.

BROADRIDGE FINANCIAL SOLUTIONS (BR)

TARGET PRICE: $131 (+43%)

Adrian Moral, Jefferson Fund

Company Data	
Price	$91.57
Market Cap	$10.5B
Enterprise Value	$12.1B
EV/EBITDA	18.6x
P/E	25.2x

Company Description:

Broadridge Financial Solutions (BR) is a global financial technology leader providing investor communications and technology-driven solutions to banks, broker-dealers, asset and wealth managers and corporate issuers. BR's services include investor communications, securities processing, data and analytics, and customer communications solutions. BR serves a large and diverse client base across four client groups: Banks/broker-dealers, asset managers/mutual funds, wealth management firms and corporate issuers. For capital markets firms, BR helps their clients lower their costs and improve the effectiveness of their trade and account processing operations with support for their front-, middle- and back-office operations, and their administration, finance, risk and compliance requirements. BR serves asset management firms by meeting their critical needs for shareholder communications and by providing investment operations technology to support their investment decisions. For wealth management clients, BR provides an integrated platform with tools that create a better investor experience, while also delivering a more streamlined, efficient, and effective advisory servicing process. For corporate issuer clients, BR helps manage every aspect of their shareholder communications, including registered and beneficial proxy processing, annual meeting support, transfer agency services and financial disclosure document creation, management and SEC filing services. BR operates their business in 2 segments: Investor Communications Solutions and Global Technology and Operations.

Investment Thesis:

1. Moat/Compounder – BR is a capital-light compounder than benefits from several important and well-known root causes of compounder businesses. Such as a "government-granted" monopoly, economies of scale, good and smart capital allocation and a large TAM. BR has been able to leverage its network and relationships with banks, broker-dealers and wealth management firms to grow its business in a smart and similarly profitable way. From a capital allocation and organic growth test it appears that BR has been able to grow revenues by investing only 47 cents into the business per every $1 dollar of new revenues generated. BR currently captures ~11%-18% of its Total Addressable Market ($25-40B) and this creates an incredible opportunity to keep growing both organically and through tuck-in acquisitions through the use of its network and relationships and its strong CF generation. Finally, an evidence of the quality of the business and BR's compounder nature BR has been able to steadily maintain an above-average operating margin of around 15.4%, generate 92% of recurring revenues, and achieve an EBITDA-to-FCF conversion rate of around 60% and an average ROIC of 17.4% for the past 12 years, even during the financial crisis.

2. Valuation – Given the incredible quality of the business and the reasons mentioned above BR has always traded at a very high price but due to current market environment a window of opportunity to purchase a wonderful business for a wonderful price has opened.

Valuation:

Scenario Analysis	Price	Upside to Current Price	Description
Bull	$182	98%	Value compounding at 17.7% for the next two years with multiple expansion from current 18.6x LTM EV/EBIT to 25.5x.
Base	$131	43%	No-growth EPV with multiple expansion from current 18.6x LTM EV/EBIT to 25.5x.
Bear	$100	9%	No-growth EPV.

Risks:

1. Industry Headwinds – There has been some industry headwinds such as fewer listed companies and fewer no. of shareholders as indexing has increased and to continues to do so.

- BR has diversified its business to other areas outside of investor communications such as customer communications, wealth management, etc. as evidenced by the company's continuous top-line growth under a decade of industry headwinds.
- The ICS segment also offers investor communications solutions for other type of investments outside of equity such as Mutual Funds and ETFs which on the other side have been benefiting from important tailwinds for the past decade.

2. Blockchain – Risk of blockchain enabling direct-to-shareholder communication.

- Although the technology exists nowadays to enable a "dematerialized" and secure system it is not only a matter of having the technology at hand but also a matter of removing the current "indirect holding system" which is not going anywhere.
- Aside from this fact, BR has been investing in blockchain technology to stay at the forefront of technological advancements in their business. During the past 3 years BR has invested $135.0 million dollars on blockchain IP and technology applications.

3. Disruption – If there is a total disruption due to restructuring or change in regulation of the current shareholder and proxy system.

- As mentioned earlier there are very strong incentives and interests from banks and brokers to keep the system in place and therefore it is unlikely for the "indirect holding.

TRINET GROUP (TNET)

TARGET PRICE: $72 (+20%)

Trent Hegseth, Executive Team

Company Data	
Price	$59.60
Market Cap	$4.06B
Enterprise Value	$4.24B
EV/EBITDA	15.8x
P/E	22.0x

Company Description:

TriNet Group ("TriNet", "TNET", or the "Company"), is a leading provider of human resources solutions to small and medium sized businesses (SMBs). Specifically, TriNet operates as a professional employment organization (PEO) utilizing a co-employment model with SMBs to assume certain responsibilities of being an employer and helping clients mitigate certain-employer related risks while managing many complex and burdensome administrative processes. TriNet leverages its scale to provide clients access to a broad range of cost-effective employee benefit and insurance programs generally not available or cost prohibitive to individual SMBs. For 2019, TriNet processed $41.7B in payroll and payroll taxes for 18,900 SMBs constituting approximately 340,000 ultimate employees.

Executive Summary:

TriNet is the #1 dedicated PEO in the United States and competes against divisions of larger organizations (ADP, Paychex) as well as smaller PEO peers. As the leading dedicated PEO, TriNet is poised to achieve faster than peer growth by utilizing its unique combination of scale and focus to create valuable, vertical-oriented SMB solutions (healthcare, non-profit, professional services, technology). The increasing burden of managing regulation, administration, and healthcare/insurance has become unsustainable for SMBs. PEOs have proven to be invaluable to their SMB clients, driving continued penetration of the SMB workforce. Overall, the company's holds a sustainable position in an industry with multiple long-term tailwinds driving higher than GDP growth.

Investment Thesis:

1. ESG – TriNet, as the leading PEO, strives towards employee empowerment and control of their healthcare decisions and data. TriNet is consistently rated as a top ESG company with an AA overall ESG rating and an 85-composite score, ranking them in the top 50 of ESG companies according to investors.com.

2. White Space to Grow – PEOs have continued to gain acceptance in the United States, now making up 6% of the SMB workforce. TriNet is targeting a total addressable market of $49B through continued penetration and providing additional employer solutions where SMB employees basic needs are not being met. The combination of compliance, complexity, and cost for SMBs to meet their workforce's needs has been demonstrated to be unsustainable for employers to meet serving as a long-term industry tailwind

3. High Cash Flow Conversion – As a co-employer, TriNet does not maintain traditional working capital such as inventory or accounts receivable. Instead, TriNet holds a negative working capital position that consists of accrued payroll tax, workers compensation, and health insurance liabilities, partially offset by unbilled revenue. As the company grows, it will continue to increase its negative working capital position while needing minimal capex to support growth.

Valuation:

Valuation scenarios anticipate varying levels of continued PEO penetration of the SMB workforce. Different cases represent TriNet's ability/inability to maintain its #1 independent PEO position and the corresponding impact this could have on margins. Target prices are based on an average of a perpetuity growth and exit multiple DCFs. Exit multiple of 17x (modest discount to ADP/Paychex) used in base and bull case, with a 15x multiple used in the bear case, a modest decline to current trading multiple.

Scenario	Price	Upside to Current Price	Description
Bull	$86	45%	Top-line growth of 150 bps over base case. Company able to realize operating leverage of 120 bps
Base	$72	20%	Top-line grows at 3-year average, declining towards GDP over time. Operating leverage drives 20 bps of margin improvement.
Bear	$48	(19%)	Top-line growth 150 bps below base case. Margins are squeezed 100 bps as PEO competition theoretically increases.

Risks:

1. PEO Market Competition – As PEO's continue to penetrate and gain market share, TriNet's margins and organic growth could be challenged.

- Mitigant: Company has demonstrated the ability to maintain its position over the last decade as PEO's have gained share and continuously innovated and acquired competitors to keep its leading position in serving SMBs and removing administrative complexity.

2. Regulation – PEO's are relatively newer organizations, slowly evolving in the 1980's and 1990's as staff leasing companies but truly reaching current form due to the market need and the technology to serve that need being created in the 2000's/2010's. PEOs rely on their needing to be significant complexity and administrative burden for SMBs to manage and if government reform simplifies this, the need for PEOs could be significantly reduced.

- Mitigant: TriNet provides a myriad of solutions driving down cost, complexity and compliance issues for SMBs. Government regulation that would significantly impact TriNet's ability to provide each of these is unlikely and TriNet's continued expansion into adjacent revenue streams diversifies the business away from this risk.

TELERIA, INC. (TLRA)

TARGET PRICE: $13 (+10%)

Jade Palomino, Darden Fund

Company Data	
Price	$11.81
Market Cap	$550M
Enterprise Value	$514M
EV/EBITDA	NM
P/E	NM

Business Description:

Telaria, Inc, which was founded in 2005 and is headquartered in New York, New York, operates a programmatic[1] video management platform to help premium video publishers optimize their digital ad inventory through software and selling ad space to brands. Its technology enables publishers to manage and deliver their directly sold and programmatic video inventory through a single platform. The company serves the sell side of the programmatic ad market, with a specific focus on high-quality connected-TV (CTV) publishers- television streamed over the internet. The company offers publishers with real-time analytics, data, and decisioning tools to control their video advertising business, as well as a monetization solution to optimize yield across their supply of digital video inventory. Following a multiyear transformation process that included hiring a new CEO, the sale of its buy-side ad technology platform so it could focus solely on the supply side, and a move to double down on CTV, Telaria has morphed into a leader in one of the fastest-growing areas of advertising: CTV programmatic advertising.

Executive Summary:

Telaria is well-positioned to drive continued top-line growth given CTV's ever-increasing scale and penetration, the growth of ads for CTV content, and a rapidly emerging programmatic opportunity in the space. Telaria will continue to experience increased profitability primarily through active customer growth and a growing and thriving client list of premium video publishers. Telaria warrants a premium multiple given: its strong top-line growth; its CTV-centric premium video publisher strategy; its potential merger with top competitor, Rubicon Project (NYSE:RUBI), which would position Telaria as the world's largest independent sell-side advertising platform; its gross margin expansion via increasing its eCPM[2] as well as its operational efficiencies; and finally, its participation in a fast growing marketing: CTV.

Investment Thesis:

1. The market underappreciates Telaria's large and expanding TAM and strong customer growth resulting from industry tailwinds in CTV. In 2019, total ad spend in CTV grew nearly 40% to reach 6.94B and is forecast to exceed 10B by 2021. Traditional linear television (i.e. cable and satellite television) is also vulnerable. According to a Telaria investor report published in November 2019, 72% of U.S. households had a CTV device in 2018, up from 61% in 2016. By 2021, the report projects that 77% of U.S. households will have a CTV device. With Telaria's total revenue up 23% YOY and CTV revenue, which accounts for 44% of the company's total revenue, jumping 115% as of November 2019, the company's successful execution of its CTV-centric strategy is evident and promising. While Telaria isn't consistently profitable yet, it is already guiding for full-year positive adjusted EBITDA between 2M and 5M, up from negative 0.4M in 2018. In 2018, Telaria continued to advance its CTV initiative by doubling the size and geographic reach of its agency-and-brand sales team.

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[1] "Programmatic" means buying digital advertising space automatically, with computers using data to decide which ads to buy and how much to pay for them.

[2] Effective cost per mile (eCPM) - the amount an advertiser pays for every thousand ad impressions.

2. The market underappreciates the accelerated growth and cost savings that Telaria would likely receive from its potential merger with Rubicon.[3] By combining, the two companies believe that Telaria would benefit from 15 to 20M in annual cost savings resulting in "substantial operating leverage" and "attractive adjusted EBITDA margins," and better serve customers with a single supply-side platform and improved tools for publishers. The merger would also make the newly merged entity an indispensable partner to buyers, giving platforms like The Trade Desk (the leading buy-side advertising platform) access to quality, scaled inventory across all channels.

3. The market underappreciates the growth opportunities presented by Telaria's gross margin expansion via its niche premium video publisher strategy, as well as its ability to achieve increased operational efficiencies. As of May 2019, the company had 5 of the top 7 virtual multichannel video programming distributors as customers. Some of the company's notable customers include premium video publishers like the Discovery Channel, Sling TV, Fox News, Hulu, and Sinclair's NewsOn, which provides access to live and on-demand local news broadcasts from over 200 stations, covering more than 90% of the population. Telaria's trailing-12-month gross margin is 84%- higher than The Trade Desk's gross margin of 76% over the same timeframe. This impressive margin is due to Telaria's emphasis on premium video publishers, which generally boast digital ad inventory that monetizes at a higher eCPM than other digital ad products. The company's eCPM rose to an all-time high of $15.68 in Q3. This translates to 27% year-over-year growth for the key metric. Aside from growing its eCPM, Telaria has achieved greater efficiencies in its SG&A expenses: it cut these expenses by $1.32 million, or about 2.3% in 2018, but was able to nonetheless increase its sales by 26.0%.

Valuation:

Scenario Analysis	Price	Upside to Current Price	Key Drivers
Bull	$20	72%	Long, sustained high growth via new premium customer acquisition as a result of increased market size, market penetration, and product offerings.
Base	$13	10%	Expanding CTV market and increased growth of new premium customers. Decreased SG&A as the company realizes economies of scale through decreased: selling and distribution costs, general and administrative expenses, and marketing expenses as a result of its increased brand equity.
Bear	$10	(18%)	Telaria fails to realize as many operational efficiencies as it scales. CTV market growth slows and increased competition in space causes decreased customer growth and contracted margins.

Risks:

1. Fending off other sell-side platforms and continuing to innovate and offer increasingly advanced programmatic-based features.

- Mitigated by heavy focus on and investment in R&D. R&D expenses in 2018 were $9.93 million- the equivalent of 18.0% of sales. Telaria currently has a major competitive advantage when it comes to competition. Its two

[3] Because the likelihood of the merger deal closing is currently around 50%, I decided to perform a more conservative stand-alone valuation.

biggest sell-side CTV competitors are FreeWheel and SpotX, both of which have compromised value propositions to content publishers because they are owned by cable companies (a content publisher generally does not want to partner with a platform that is funding a competing content publisher).

2. Trying to manage its non-CTV revenue. Revenue from desktop and mobile video still represent over half of Telaria's top line. Because of headwinds in desktop, Telaria's non-CTV revenue fell from about $10 million in Q3 2018 to $9.3 million in Q3 2019.

- Mitigated by strategy of focusing on and expanding the CTV portion of the business. Telaria's potential merger with Rubicon could address this problem, as Rubicon is thriving in non-CTV channels.

3. Telaria's merger with Rubicon is not completed. If it fails, Rubicon may begin investing heavily in CTV -- an area where it only has a nascent offering. If Rubicon succeeds in growing its CTV business, the company could take share from Telaria.

- Mitigated by Telaria's deep expertise and substantial R&D investments in the CTV space.

TENCENT (TCEHY)

TARGET PRICE: $75 (+41%)

Yujing Sun, Monticello Fund

Company Data	
Price	$53.30
Market Cap	$510B
Enterprise Value	$505B
Trailing P/E	39.3x

Business Description:

Tencent is a technology leader in China. The company is established in 1998 through social media networks and gradually expand its business operations into gaming, fintech, advertising, and cloud system to eventually build up a product ecosystem. Tencent nowadays has China's largest social communication and gaming platforms and is shifting from the PC platform to the mobile platform. For merchant services, Tencent is dedicated to connecting small business and municipal services to consumers through Wechat and QQ in-app functions which further enhance the user stickiness.

Revenue Generation:

1. Social Network (23% of sales): Building upon the largest social media user base of China, Tencent expands into digital content services and charge value-adds services such as membership privileges, content subscription, and virtual gifts. The most active mobile platforms, WeChat and QQ, have an active monthly user of 1,804M as of 9/20/19.

2. Online Gaming (29% of sales): Tencent generates fee-based services through in-app purchases of smartphone and PC games. Tencent gaming takes up 64% market share on PC and 48% market share on mobile devices of the Chinese market. The company actively co-develop popular titles with major gaming companies to enhance its global footprint. Tencent cooperated with Activision Blizzard on the Call of Duty Mobile game, which reached more than 100M downloads within the first month of launch. Domestically, in 2017 Tencent has established its flagship gaming platform, WeGame, to provide a diversified gaming portfolio from battle games and role-playing to board games and puzzles.

3. Advertising (19% of sales): Major sources of advertising revenues are through media and social ads. Media traffics are from the banner, content feed and video pre-roll advertisements from Tencent app, webpage and video portal. Tencent video portal has been dedicated to producing its own shows or establishing exclusively broadcasting relationship with hit titles to attach traffics. Social media advertising provided more targeted leads and higher click-through rate as it's based on user's location information and targeted promotional coupons.

4. FinTech and Business Service (28% of sales): For FinTech service, fees are collected through a percentage of the merchant transactions, cash withdraw and credit card repayment charges on WeChat Pay. WeChat Pay has made great efforts to penetrate the rural areas of China to provide the convenience of cashless transactions. The total daily payment transaction volume exceeded 1 billion in 2018, with commercial transactions accounted for more than 50% of the transaction. In addition, Tencent also provides cloud infrastructure that charges usage-based billings on enterprise technology and smart industry solutions.

Investment Thesis:

1. Strong customer stickiness creates barriers to entry – Tencent has shifted from a purely social/communication platform to digital content, financial service and enterprise technology provider to build up an ecosystem that connects merchants and users. Tencent leverage its social media platform and unbeatable outreach to penetrate into an individual's everyday life. Through 3rd party cooperation, individuals could enjoy a wide range of services, from transportation hailing, food delivery, online shopping, wealth management, charity and day-to-day bills payment. In addition, with its long history in China, most privately-run enterprises still use QQ as business communication tools, instead of using skype for business. Backed by the local government, in February 2019, 22 among the 34 provinces and municipals has cooperated with Tencent to enhance SmartCity and roll out digitalization campaigns for residents and business owners. The cooperation with local governments greatly enhances Tencent's influence in enterprise services while also expand its customer base for Wechat. The virtuous cycle and ecosystem effectively maintain Tencent's dominant position.

2. High growth potential on mobile gaming, digital content and online advertising with the roll out 5G and the shift to mobile device – Tencent has devoted resources to co-invest with top gaming companies to develop hit titles on mobile ends. Tencent has partnered with 8 out of the 10 top gaming companies, such as EA, Activision Blizzard and Nintendo to enhance its global presence. Internally, Tencent also developed its gaming developer contest organized by Tencent Institute of games to source new ideas and diversify its current game offerings. Social media content sharing and advertisement revenue have grown 32% YoY by Q3 2019 through WeChat Moment, Mini Program (mobile version of self-media website) and targeted ads.

3. Diversified product and service portfolio helps reduce the risk of economic downturn -Tencent's diverse revenue sources put the company in a good position again economic depression. Revenue from social networks, online games, advertising, financial service and enterprise services each take up between 20%-30% of the total revenue. The revenue sources are allocated pretty evenly rather than skewing towards one specific sector. In addition, what differentiates Tencent is its customer base and all other services are built upon the wide customer reach. The well-balanced product and services profile can help the company to survive through financial difficulties.

4. The outburst of coronavirus pushes the progression of virtual transactions and cloud services – As the government regulated the mobility within the city, most in-person transactions are now conducted virtually. Such as in Beijing, only one person in one household is allowed to leave the neighborhood every two days. The convenience and benefits provided by the Tencent ecosystem will help increase its market penetration, especially for the older generations who are used to face to face transactions. Moreover, most companies require employees to work from home. This provides more opportunities for Tencent's enterprise and cloud service to expand. Indeed, Tencent will not likely have a good financial performance due to the impact of the coronavirus and the economy, however, it's a company with comprehensive products and services that would recover after the crisis.

Valuation:

Upside Scenario	$87 (+64%)	Light disruption from Coronavirus on operations, less competition in the field
Baseline Scenario	$75 (+41%)	Base case
Downside Scenario	$35 (-34%)	Heavy disruption on operations, new entrants steal market share

Risks:

1. Government approval required to get games on shelves. Due to government reorganization, the approval process was frozen for 9 months from March to December 2018. The regulation risk would impact the profitability and new releases.

2. Disruption from emerging media provider, Bytedance. Competition from Alipay to compete in the Fintech market also puts pressure on the company.