f3x capital

Investor Letter 20
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INTRO

In many respects, it was a dramatic start to 2022. While Afghanistan, the last major human tragedy on which the news economy had focused, was still geographically far away and of little economic relevance, Putin's war now dominates the media and financial markets. In the last Investor Letter, we ourselves wrote that Putin was just flexing his muscles militarily. But we, like so many others, underestimated the man's madness.
The U.S. Federal Reserve has now concluded that inflation is no longer merely "transitory." Whatever that may mean, at least in the short term the next shock wave is spreading through global supply chains after the covid pandemic. Rapidly rising energy prices are being reflected in end products through many channels, such as the metal processing and chemical industries. The shortage of grain and wheat from Europe's "grain chamber", Ukraine, is serving up inflation directly on the German consumer's plate in the form of increased meat prices.

The U.S.A. therefore is pushing ahead energetically with interest rate hikes, which the markets instinctively acknowledged with sharp discounts on the valuation multiples of companies that tend to be more highly valued. Price losses of 50 - 75% were the rule rather than the exception on companies whose valuations are usually discussed in terms of sales multiples.

Even f3x, as a style agnostic, was not exempt from this. The f3x euroflex closed the first quarter with -16,3% This compares to other European indices like the MSCI Euro Small Cap with -11,8%, the TecDax -16,1% or the SDAX -14,9%.

As always, the main contributors with some details can be found on the following page. What happened in summary? For the time being, we have had a very poor investment result in the last six months with THG, where the bear case scenario has occurred and has been significantly amplified by the market phase. We are suffering from some valuation understatements in e-commerce and specifically recent IPOs as well. Why understatement? The Global Online Retail Index, run by e-commerce expert Jochen Krisch, has now fallen to a level just before Corona. No discussion, this is nonsense.

Performance of all share classes since inception

Year	2017	2018	2019	2020	2021	2022
S-Class	5.7%	-22.0%	23.9%	16.1%	4.4%	-16.3%
R-Class	5.0%	-22.6%	23.6%	14.9%	3.4%	-16.4%
I-Class	-	-18.0%	24.0%	15.5%	3.7%	-16.3%

Performance data is based on the BVI method, net of all costs . Past performance is not a reliable indicator of future performance.

INTRO (CONTINUED)

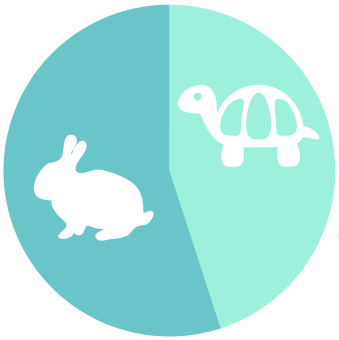
Last but not least, we scored a stage win with our top position in Modern Times Group. It was able to sell its e-sports business for 1 billion US dollars, which gave the f3x fund a jump on the day of the announcement. Operationally, the f3x holdings are not significantly affected by the Ukraine crisis. Those who regularly read our quarterly letters will also be familiar with our structural aversion to global supply chains. We see ourselves once again confirmed in our opinion. In the meantime, we are building up the second investment with exposure to 3D printing.

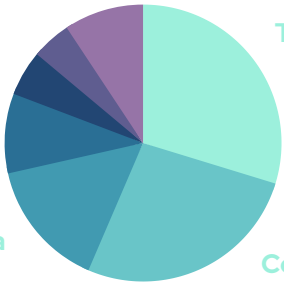
Otherwise, we can report on a new core position. At the same time, we have not shed any core positions. In the current sideways phase of the market, significant potential is building up in the portfolio at one point or another.

In the outro today, we try to contextualize our view on the central bank-interest rate-inflation complex. This is not really an exercise for fundamental investors like us, but in a world that seems to turn upside down every day, you need to set up some principles to guide you. We have been digging away from neo-liberal economists.

18

core positions



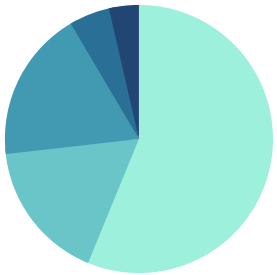


1.8

Ø market cap in €bn

16.9%

Ø sales CAGR 2021-2024



Top 10 Positions

Company	Weight	Business
Modern Times Group MTG AB	10.1%	E-Sports leaugue and mobile gaming dev
SLM Solutions Group AG	9.3%	Manufacturer of 3D printers
ADVA Optical Networking SE	7.2%	Networking infrastructure equipment
M1 Kliniken AG	6.4%	Clinic chain for aesthetic procedures
Bitcoin Group SE	5.2%	Investment and consulting company
Vita 34 AG	5.2%	Cord blood bank
Eurofins Scientific SE	4.8%	Provider of analytical testing and laboratory services
Vossloh AG	4.5%	Railway components
Acast AB	4.5%	Podcast Marketplace
init innovation in traffic systems AG	4.4%	Software & hardware for public transportation

PERFORMANCE DRIVERS

2022 Q1
in basis points to NAV

TOP CONTRIBUTORS

MTG	+476
ADVA	+74
init	+39

TOP DETRACTORS

Veganz	-310
THG	-259
Naked Wines	-228
Moonpig	-214
Fabasoft	-206

REPORTING & EVENTS OF PORTFOLIO COMPANIES

Modern Times Group (MTG)

In our last letter, we reported on the postponed capital market day for our largest position and that we expected a strategic realignment. That has come to pass. On January 24, 2022, MTG announced the sale of its e-sports division. This includes the Electronic Sports League (ESL) and the Dreamhack event series. Acquirer Savvy Gaming Group values the assets at $1.05 billion of which MTG owns nearly 92%. Previously, the entire listed group had been valued at just under $1 billion. Part of this group is also the Gaming Division, which also generated almost $130 million EBITDA in 2021. The stock jumped nearly +40% after the announcement. The proceeds will be used for share buybacks and the further consolidation of game development studios.

ADVA

In August last year, the takeover attempt by its U.S. competitor ADTRAN got under way. For a long time it was unclear whether the unusual structure involving an exchange of shares into a new vehicle followed by a dual listing in New York and Frankfurt would find enough believers. However, on January 28, 2022, the bidding company Acorn Hold Co. reported that the 60% threshold had been reached. So, our ADVA stake is part of a larger global group and may soon benefit from a valuation premium via the U.S. listing.

REPORTING & EVENTS OF PORTFOLIO COMPANIES

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The Hut Group (THG)

In August 2021, we had transparently set out our investment rationale for UK-based The Hut Group (THG). We had conducted the sum-of-the-parts valuation using market multiples and highlighted the group's relative strength through digital capabilities versus brick-and-mortar or smaller players. Part of THG's dominance was given by its ability to raise capital and use it strategically for its consolidation play - a pattern which has worked extremely well over the last five years. Operationally, not much has actually changed, but the perception of the company has changed significantly. After revisions to projected growth rates, the market withdrew confidence from the technology spin-out "Ingenuity". THG planned to offer its own e-commerce brand-building and fulfillment capabilities to third parties similar to what Ocado is doing. Softbank acquired an option to buy into Ingenuity at a $6.3 billion valuation in May 2021. All this went up in smoke last fall and winter. CEO Matthew Moulding did his part by being whiny about short sellers. We could beat around the bush that the market doesn't understand the long-term potential, etc., but with the position down 75%, we're sitting in a deep hole. Microsoft shareholders know that you can wait a very long time for share price gains, even if you have a stake in an excellent company. What now? For the moment, nothing. The position is just under 2%. Due to the sum-of-the-parts perspective, we believe that a private equity takeover attempt could be launched at any time, which could actually offer a premium of 100% without any problems. We do not want to sell this optionality right now. However, our opinion can change abruptly in one direction or the other depending on the situation.

EXITS

No positions were sold in the past quarter.

ENTRIES

This quarter we are introducing one new core position.

#1 ACAST

The Stockholm-based company operates an integrated podcast hosting and monetization business model. Independent creators and media companies such as the BBC use Acast to feed their podcasts into the RSS system so that "podcatchers" such as Spotify, Apple or Stitcher can play them out to their users. In addition, Acast places software-supported advertising in the podcasts. The podcast market is growing dynamically and monetization is still below its potential. Radio still has some user time to give up to podcasts. Acast describes its addressable market as advertising within audio formats. This was $30 billion in 2020, of which only $2 billion was attributable to podcasts. Market studies expect 19% annual growth for the podcast advertising market over the next five years. Acast plans to grow disproportionately as it has established itself as the largest independent platform and is able to acquire or displace smaller competitors. The big risk in the podcast market is that Spotify, Amazon and co. will "lock down" their ecosystems by signing podcasters exclusively and marketing the ad space themselves. But going "exclusive" makes sense for very few creators as a final exit option. For the "long tail" of the 2 million shows worldwide, however, this would only mean a curtailment of their own revenue options. And even the trend towards big exclusive signings is unclear since the Joe Rogan / Spotify scandal. Does Spotify really want to be liable as a de facto publisher of wayward creators? Acast advocates for the open ecosystem from a moral and economic logic. f3x enjoys a new diversifying portfolio component.

Sector

Media

Country

Sweden

Market cap

SEK 3,156m

Weight

4.5%

Style

Growth

Sales LTM

SEK 1,025m

Sales CAGR 2021 - '24

56%

OUTRO

The seemingly tectonic shifts in global interest rate policy has again produced many pundits. But it's hard to find financial market commentators who are agenda-free - everyone has a portfolio to "push." So, we studied more broadly.

Two books of a sociological, rather than economic, nature stood out.

Central Bank Capitalism by Joscha Wullweber (Suhrkamp 2021)

That's inside:

- Describes the increasing, forced encroachment of central banks into political responsibilities. Central banks take on challenges that require rapid response and for which democratic solutions would take too long or be unachievable. Imagine a direct democratic vote on life support for countless zombie corporations or environmentally subsidy consumers (Hello Mr. Tönnies!).

- The shadow banking sector has grown rather than shrunk after the financial crisis. Due to a lack of explicit government guarantees (like deposit insurance in the fully regulated banking sector), this area of the capital market has a systematic trust problem, which is mainly solved by collateralizing government bonds in repo transactions. There is an enormous pull effect for newly issued government bonds.

- The focus on the interest rate policy as a driver of equity valuations is too narrow. Outstanding government bonds and liquidity in the repo market are also important components.

- The high leverage of the globalized economy means that unexpected shocks can always destabilize the entire system. Central banks are forced to take ever more drastic measures, which in turn increases their responsibilities.

OUTRO (CONTINUED)

The Dangerous Rise of Carry by Tim Lee et al. (McGraw Hill 2020)

That's inside:

- Projects the model of a carry trade onto the capital market as a whole. A classic carry trade involves borrowing in a currency with low interest rates, such as the U.S. dollar, and investing in a currency with higher interest rates, such as the Turkish lira. Thereby an interest margin is collected. Carry trades are usually associated with high leverage. A carry trade works when less happens than should. Actually, the higher expected inflation in the Turkish lira and the associated currency loss should neutralize the more favorable interest rates on the debt in U.S. dollars. But there are long periods when this does not happen after all, and that is how pennies can be picked up in front of a bulldozer. Particularly when using leverage, large losses can quickly occur on a long carry trade - the so-called "carry wipe out". Carry trades come in all shapes and colors and typically there is always a new big carry bubble popping up somewhere. The mortgage bubble in the U.S. was a carry trade: cheap funds via the tranching of CDOs, which magically made risks disappear for the CDO buyer, were used to make loans to sub-prime borrowers.

- In an extended sense, a long carry trade is the position of an insurance provider.

- "Short volatility", Tesla, and buy-now-pay-later business models (Klarna, etc.) are all forms of carry trades

- Central banks stimulate the global carry trade as they themselves implement a huge carry trade. A carry crash can only be saved by initializing a new carry phase.

- It is rational to participate in carry bubbles.

- The "carry regime" leads to suboptimal allocation of financial resources from a productivity point of view.

- Each carry crash and subsequent recovery leads to increasing concentration of power

- We actually missed the exit to a "Beautiful Deleveraging" as once described by Ray Dalio with the response to the 2008 global financial crisis. There is only the escape forward into the next carry bubble.

- Trust in central banks is slowly eroding, which is why tendencies towards alternative means of payment are already visibly on the rise. Cryptocurrencies are a symptom.

OUTRO (CONTINUED)

We conclude:

- One should remain invested in shares of companies. Even in an extreme scenario such as hyperinflation and the corresponding re-sorting of debts and currencies, one is still invested in companies that can operate on the basis of subsequent payment systems.

- Re-sorting of currencies is nothing unusual. In case things get really messy, nevertheless, historically payment was not made with gold bars, but with cigarettes. Fortunately, nowadays there is "internet money", i.e. cryptocurrencies. In the Ukraine crisis, the company Starlink has impressively demonstrated how quickly one can bring Internet and thus theoretically also "money" to a place.

- If, as is to be expected, the tense situation on the capital markets is "patched up" again with the next major measures by the central banks - China is already sending signals - then it is also essential to be fully invested in equities

#onwards