GREENHAVEN ROAD PARTNERS FUND

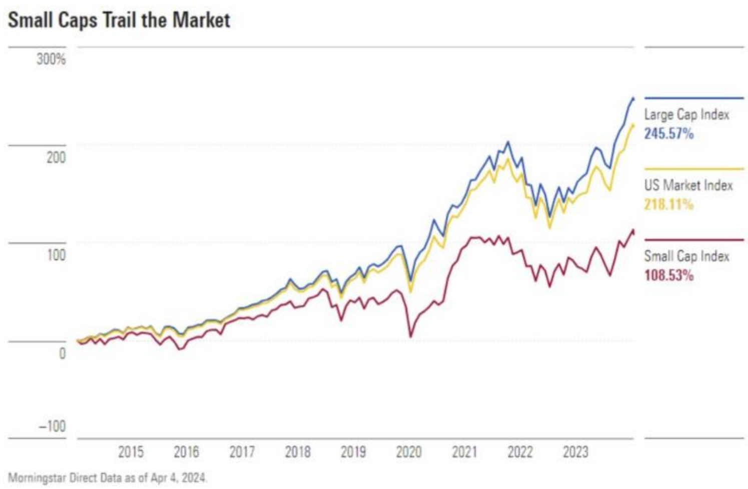
August 2024

Dear Fellow Investors,

The Partners Fund was down less than 1% net in the second quarter, bringing YTD performance to approximately +6% net.[1] Please check your individual statements for your returns.

No matter how you slice the data, the second quarter was uninspiring for smaller companies, which were left behind as gains continued to accrue and capital continued to flow to the largest companies (the "Magnificent Seven").

Smaller companies have suffered these dynamics for longer than just the past quarter. Using the Russell 2000 and the S&P 500 indices as proxies for small and large companies, large has beaten small handedly for the past decade.



This outperformance has not always been the case. As Rich Howe, the author of Stock Spinoff Investing, recently posted on Twitter, small cap companies historically have outperformed in 67% of rolling 10-year periods by an average of 285 basis points annually.

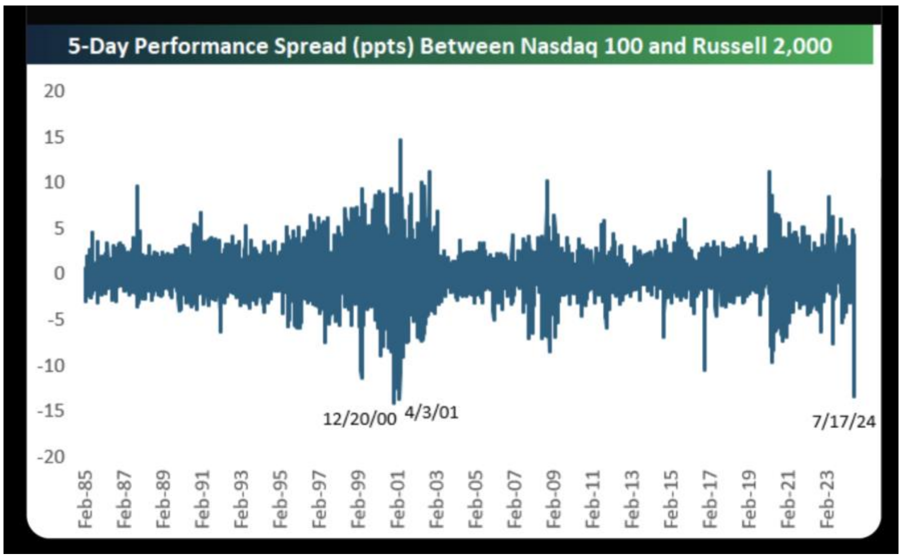
Small Cap Minus Large Caps: Trailing 10-Year Relative Performance (%)

% of rolling 10-year periods when small caps outperformed	67%
Average annual relative performance	+285 bps
Average annual relative performance in periods of 10 year outperformance	+547 bps
Average annual relative performance iin periods of 1-year underperformance	-130 bps

[1] Performance: (i) is representative of a "Day 1" investor in the Partnership, (ii) represents returns earned by Class B investors assuming a 0.75% annual management fee and no incentive allocation, and (iii) is stated net of expenses. Year-to-date performance for an individual investor may vary from the performance stated herein as a result of, among other things, the timing of their investment and the timing of any additional subscription and withdrawals.

The historical data suggests that when smaller companies work, they really work. During the periods of outperformance for small companies, they outperform their larger brethren by 547 basis points. That said, while the above chart provides a source of optimism, historical data does not put food on the table.

The question plaguing every investor who has not owned Nvidia or the Mag 7 (a group that includes the managers in the Partners Fund) is, "when?" Is this time in fact different? Will there ever be a rotation from large back to small? For a brief period in July, there was a once-in-40-years outperformance of smaller companies over larger companies. One of the CNBC "cool kids" trades became selling Mag 7 and buying small caps. The data below uses the Nasdaq 100 as the proxy for large technology companies to illustrate this divergence. The outperformance vs. the S&P 500 was more muted but still generational as hundreds of billions of dollars looked for a new home.



Around the Greenhaven Road office, there were multiple expressions of the word "finally," starting with a tinge of disbelief ("finally?") and progressing over several days to "FINALLY!!!!!" I would not call a turn based on a few days or even a month, but July was giddy.

In the past several letters, I have profiled individual managers or the opportunity in smaller companies… but how does the Partners' Fund compare to the Russell 2000? Answering this question is not as simple as it sounds, as it involves either looking at historical data or "consensus estimates" for forward data, which Partners Fund managers would argue are often flawed. Additionally, the Partners Fund has more international holdings as well as holdings that are both too big and small to be included in the Russell 2000. The Partners Fund is more than merely a subset of the Russell 2000. Still, they are both places that investors can go for exposure to smaller companies.

Several of our managers would also argue that a purely quantitative comparison misses the point, that they are trying to buy companies that don't screen well or where the GAAP financials hide the actual value. Matt Sweeney of Laughing Water Capital did a presentation (link) at ValueX Vail this summer highlighting the opportunity of buying companies before the health of the business shows up in the "backward looking" quantitative data. As he said in his most recent letter, "Of particular note are our investments in companies that don't "screen well," which effectively makes them invisible to the huge percentage of the market that relies entirely on quantitative inputs to guide their investment decision making."

The whole presentation is worth reading, but the following graphic highlights both the opportunity in smaller, misunderstood companies and the challenges of the data.

- Deliberately look for value that quants can't see
  - Misleading trailing financials
  - Nonexistent or poorly done forward estimates
  - Discount to private market value
  - Hidden asset value
- Have a view on how value will surface, forcing quants to notice.

Tangible examples of distorted financials may be a company that is underearning because it's investing in new products that will be released shortly. Another distortion in GAAP financials may occur when assets are held on a balance sheet at cost while their market values have appreciated significantly.

With the major caveat that a purely quantitative comparison is likely to dramatically understate the relative undervaluation of the Partners Fund, the below comparison does provide a quantitative comparison showing that, on average, the Partners Fund holdings have a significantly lower PE multiple, are more likely to be profitable, have less debt to equity, and higher returns on equity (all good) than the companies of the Russell 2000.

	P/E	% of Stocks Loss-Making	EV / EBITDA	Debt/ Equity	ROE
Partner's Fund	27.0x	30.3%	11.8x	92.2%	11.2%
Russell 2000 (IWM)	42.7x	40.0%	17.6x	117.9%	4.4%

Interestingly, one our managers, North Peak, undertook a similar analysis for the six largest holdings in their portfolio. Their point of comparison was the S&P 500, but the idea of relative undervaluation holds the same:

Big Six Valuation[3]
(In Comparison to Fundamental Characteristics)

Name	2025 Yield	2025 Revenue Growth	2025 Net Income Growth	2025 ROIC (Tangible)
Hilton Grand Vacations	19%	6%	10%	18%
Basic-Fit	17%	17%	34%	22%
Delivery Hero	12%	11%	>100%	30%
Smartsheet	6%	15%	43%	71%
Workday	4%	16%	36%	33%
ECN	17%	14%	64%	57%
NPC (Weighted)	**13%**	**13%**	**42%**	**35%**
S&P 500 (Equal-Weight)	*5%*	*7%*	*14%*	*24%*
S&P 500 (Cap-Weight)	*4%*	*10%*	*15%*	*32%*

North Peak points out that their six large holdings have "tripled earnings over the last 30 months while their prices have fallen by more than half…….If the Big Six were valued at triple their current price by the market, they would have a yield in line with the S&P 500, and still have better economic characteristics – more revenue growth, substantially more earnings growth, and higher return on capital. At today's price, they have those superior economic characteristics and offer roughly triple the yield."

Another tangible example of the compelling valuations within the Partners Fund holdings lies in Desert Lion, the South Africa focused fund. South Africa is the land of real companies trading for single-digit P/E multiples. Remember, when a company goes from trading at a 5 PE multiple to a 6 PE multiple, the share price rises 20%. Starting from a low base can spring load future returns. One of Desert Lion's largest holdings is an Industrial company which, despite its listing on a South African exchange, typically derives more than half of its revenue outside of Africa. The company ended June trading at a 5 PE and 70% of tangible book value despite being debt free with excess cash and growing EPS at a 34% CAGR over the past 5 years. Using some of that excess cash, the company recently announced another acquisition (outside of South Africa) that will enhance earnings and immediately adds 10% to their EPS. This is over and above strong organic growth and the boost from continued share repurchases at 5 PE multiples.

A recent letter from the Royce Funds (where we are not invested but do admire) lays out the opportunity in the following quote: "We have also been small-cap specialists with a long-term investment horizon for long enough to know that patience really is a virtue – and that finding attractively valued opportunities during periods of relative underperformance creates the foundation for rewarding long-term results." Only time will tell if the turn to smaller companies started in July, but in my opinion, the underlying value is there today.

As I have said at the end of every letter, our fund of funds is going to be different. It will be smaller, the underlying holdings will be more esoteric, and I hope the managers will continue to collaborate more over time. I believe that it will be "good different," but only time will tell. Thank you for joining me on this journey. I will work hard to grow your family capital alongside mine.

Sincerely,

Scott

Note on preceding analysis of Partners Fund holdings: Sources include FactSet, Furey Research Partners for Russell 2000 data, and underlying Partners Fund managers. Data as of 6/30/2024 provided by the underlying managers and was relied upon in the aggregate analysis. Companies that did not have current financials filed with the SEC were excluded from the analysis. Holdings below 2% in size were excluded.