Q1 2020 Investor Letter | *April 16, 2020*

Dear Investor,

For the three months ended March 31st, 2020, the Bonsai Partners portfolio declined -22.0% net of fees and expenses. At the end of the quarter, our gross exposure was 78.4%, with 21.6% held in cash.

Bonsai Partners Historical Returns Summary

	YTD 2020	2019	2018	Since Inception
Bonsai Gross Return	-21.8%	60.6%	-17.9%	3.8%
Bonsai Net Return	-22.0%	56.4%	-18.1%	-0.1%
S&P 500 Return	-19.6%	31.5%	-8.6%	-3.8%

Performance data shown represents past performance. Past performance is not indicative of future results. The period October 22, 2018, to April 30, 2021, presents time-weighted returns of a representative Bonsai Partners, LLC ("Bonsai") managed account with the same strategy and risk profile as Bonsai Partners Fund, LP, (the "Fund") which launched on May 1, 2021. Results from May 1, 2021, reflect the time-weighted returns of Class A shares of the Fund.

Gross returns from October 2018 to April 2021 include transaction and commission fees. Gross returns from May 2021 to the present include transaction and commission fees and fund operating expenses, such as administrative and audit fees but do not include management or performance fees. Net returns reflect the gross returns (as described) reduced by a 1.0% management fee and a 10.0% performance fee above a 6.0% cumulative compounding hurdle.

All performance figures are calculated internally by Bonsai Partners and are therefore estimated, unaudited, and subject to adjustment. The investment return and principal value of an investment with the Fund will fluctuate so that an investment, when redeemed, may be worth more or less than its original cost. Actual performance for a particular investor may be lower or higher than quoted performance due to different fee structures, share classes, beginning periods, capital additions or withdrawals, or individual compliance related mandates. Please refer to important additional disclosures at the end of this letter.

While headline performance was roughly in-line with our benchmark, I underperformed my own expectations for this period. The portfolio was not as resilient as I would have hoped, especially considering our cash position.

The largest contributing factors in the period were our outsized exposure to the hard-hit travel industry and that smaller cap stocks were disproportionately hit during the drawdown. I'm hopeful the latter impact will reverse in time.

Notable detractors of performance during the quarter were Redbubble, Travelsky Technologies, and Southwest Airlines. Modest gains were seen throughout the balance of the portfolio. I provide a commentary on each position in the **Position Update** section below.

At the end of this letter, I also share a deep dive into one of our new investments: **Genasys**.

COVID-19

To keep this section short, I'll make this clear upfront: I don't know how this situation will unfold, and I don't believe anyone else knows either.

When I think about the companies we invest in, their success does not hinge on an ability to accurately predict the virus's impact. Instead, these businesses are focused on what they can control: investing in the areas that will yield high returns in the future, such as improving their product, engaging in research & development, and deepening customer relationships.

Similarly, I continue to invest in the areas that are the key drivers of our future performance: hunting for wonderful businesses, performing investigative research to uncover valuable insights, and deploying capital at rational prices. Our process marches on because the underlying thesis remains in-tact despite the changing environment.

In this spirit, I put a meaningful amount of capital to work during the first quarter. In all, I added six new positions to the portfolio.

Portfolio Review

The first quarter of 2020 was busy from a portfolio perspective. Share price volatility allowed me to put a significant amount of capital to work, adding six new positions and trimming one: Southwest Airlines. I am not ready to disclose two of these new positions because they are not yet appropriately sized.

The volatility we saw in March was very sudden and remains one of the fastest drawdowns in stock market history. From these short-lived lows, we saw a very rapid reinflation in prices. Such sharp swings in valuations made the window of opportunity very small for investors – in some cases, there were only a few hours or days where reasonable prices were available.

It's challenging to perform complete and accurate research on a wide variety of companies in the span of a few days. Fortunately, I was able to lean on research and thinking I've done in the past to put capital to work. New positions based on old thinking include LKQ, Illumina, and Taiwan Semiconductor.

Our portfolio continues to get better through increased diversification of good ideas, rising opportunity costs, and upgrading the quality of the businesses we own. If we remain committed to the process, our portfolio will continuously improve.

Position Update

Redbubble (ASX: RBL)

Redbubble was a meaningful detractor of value during the quarter. We took advantage of share price weakness to aggressively add to our position.

Since last quarter, Redbubble has been dealing with shareholder turnover after committing an execution hiccup. Redbubble's CEO was removed, and its longstanding Chairman of the Board also stepped down. Redbubble's founder, former CEO, and largest shareholder: Martin Hosking took back the reins of the business and will remain until they find a new leader.

Redbubble remains a 'show me story' where investors need to see execution happen before they believe it exists at all. Although all signals were pointing to a strong first quarter (as earlier investments started bearing fruit), the coronavirus disrupted this momentum.

The foundations of Redbubble's business remain strong: it's an enviable two-sided marketplace with a strong take-rate and a long runway for growth. Their products deeply resonate with customers and they help artists continue doing what they love. Redbubble's valuation remains frustratingly cheap, and I believe that when they reinvigorate growth, the share price will take care of itself.

Travelsky Technologies (HKEX: 0696)

Travelsky was another weak performer during the quarter as their business was squarely disrupted by the COVID-19 outbreak in China. Since Travelsky is the leading back-end software provider for virtually all Chinese airlines, the disruptions in air traffic led to a subsequent share price decline.

Fortunately, we did two things right when we bought Travelsky: 1) we bought a resilient, high-quality, and well-capitalized company, and 2) we purchased our position at a rational price. Those factors made the drawdown more bearable and give me confidence that we'll make it through to the other side.

Over the medium-term Chinese air traffic will return to growth, and Travelsky remains in an ideal position to capitalize on the opportunity.

Southwest Airlines (NYSE: LUV)

If you recall, last quarter I initiated a position in Southwest Airlines, and my timing couldn't have been worse. I made this investment right before the COVID-19 virus was discovered in China.

While I gushed about Southwest's 47 consecutive years of profitability in my last letter, it's all but certain now that 2020 will be a year of massive losses for Southwest. I jinxed it.

During the quarter I meaningfully trimmed our Southwest position. While I hope it's unusual for me to sell something months after purchasing it, the assumptions I underwrote when I invested are no longer valid. Further, I wanted to reduce our total exposure to the travel sector due to structural changes happening in the world economy.

When I purchased Southwest, I made a bet that there was a high likelihood that air travel would continue to operate in a relatively normal fashion. While no future is certain, I also assumed that if an industry disruption occurred, Southwest would be well-positioned to handle it and even benefit due to their uniquely strong financial position.

Although Southwest probably could survive this pandemic on its own, by bailing out the airline industry, the U.S. government implicitly eliminated Southwest's financial advantage and leveled the playing field.

Similarly, a large part of the Southwest investment case relied on the company's ability to issue dividends and buy-back their own stock. These returns of capital are now on-hold for the foreseeable future.

I did not make a mistake in my decision to buy Southwest, it was the right decision at the time. However, when I recognized the thesis was broken, it was the right time to sell and adjust the portfolio.

Genasys (Nasdaq: GNSS)

Genasys shares modestly appreciated in the quarter.

I discuss our Genasys investment in detail below.

LKQ (Nasdaq: LKQ)

LKQ was a modest contributor to performance during the quarter.

LKQ is the largest provider of alternative collision and mechanical automotive parts in the United States. These include aftermarket, recycled, and remanufactured parts. In Europe, LKQ is the largest distributor of automotive maintenance parts across most European markets.

LKQ's US business is quite attractive because it provides cost savings across the auto repair value chain – saving money for insurance companies and the insured.

Recycled and remanufactured parts are difficult for an autobody shop or mechanic to source, and LKQ's value proposition comes from creating the largest nationwide logistics and inventory network for this long tail of parts. LKQ's distribution network adds a significant amount of liquidity to part buyers, and it creates provides price discovery for LKQ in this fragmented market. Further, LKQ owns the largest aftermarkets part brand: Keystone, which offers autobody shops and mechanics a one-stop-shop for all their alternative parts needs.

In Europe, LKQ more closely resembles O'Reilly Automotive, a distributor of mechanical parts, fluids, and electronics. This is also a reasonably good business given how fragmented the supplier and customer bases are and the needs for just-in-time distribution.

With the COVID-19 outbreak, the amount of automotive maintenance and repair has declined significantly, sending LKQ shares sharply downward. I believe that over time people will be driving again, and given concerns about the virus, automotive travel will increasingly be viewed as a preferable method over public transportation.

Lastly, LKQ is a strong counter-cyclical play that benefits from weakened economic conditions. As the value of the average used car declines and the car parc ages, more repairs are required on average, and more alternative parts are sourced.

The biggest knock on LKQ is that they have a significant debt burden. While their maturities are quite manageable (no meaningful maturities until 2024), their solvency remains in question. It's possible LKQ could trip a debt covenant and require a waiver if COVID-19 disrupts the auto repair chain for a prolonged period.

While I think it's likely that LKQ management will find a way to navigate this period of disruption without issue, I decided to hedge these tail risks to minimize losses if the worst-case comes to pass.

Taiwan Semiconductor (NYSE: TSM)

Taiwan Semiconductor modestly grew from our cost basis.

Taiwan Semiconductor is an interesting company introduced to me by a friend who is a sharp investor.

In a past role as an analyst, I spent a significant amount of time learning about the semiconductor industry and how value accrues across the supply chain. My main conclusion from this time spent was that most semiconductor companies aren't investable. They may design wonderfully useful chips, but most of the economics flow to the buyers of semiconductors (to an Apple or a Samsung), rather than the designers themselves.

While this held true, I didn't appreciate how much of the economics are also captured upstream by the chip foundries who physically manufacture the chips on an outsourced basis. Taiwan Semiconductor is the largest outsourced foundry in the world. Unlike Samsung or Intel, TSMC does not compete with chipmakers by designing and selling their own chips as well; they solely manufacture them on a contracted basis for their customers.

TSMC's focus is to offer the leading technology processes via extremely efficient production, at a competitive cost. The high cost of manufacturing makes it difficult for chip makers to manufacture their own products using the constantly evolving industry leading technologies. As a result, the outsourced model prevails.

What I find interesting about TSMC: the features of the business I originally found unappealing are actually what makes it a great investment in the long term. TSMC spends tremendous sums of money each year to build out cutting edge 'process nodes' and add additional manufacturing capacity. In 2020 alone they are expected to spend $15 billion in capital expenditures!

Few competitors can keep up with TSMC's investments, and this has led to an oligopoly with high returns on invested capital despite how much total money has been invested over time.

I think it's reasonable to assume that many more semiconductor chips will be made in the future, their complexity and value will increase, and more of them will be made by TSMC given their structural advantages. I view Taiwan Semi as a way to capitalize on the ever-growing demand for chips without taking on the technological risk of picking a particular chipmaker.

Illumina (NASDAQ: ILMN)

Illumina modestly appreciated from our cost basis during the quarter.

As background, Illumina is the leader in genomic sequencing instruments and reagents. The business acts as an enabling technology that is driving forward many advances in the life sciences industry. More than ever, genomic information is being used to drive decisions and gain insights across diagnostics, therapeutics, and scientific research.

Illumina operates a razor/razor-blade model through system sales and recurring reagent sales associated with the number of tests that flow through their systems. As the Life Sciences industry expands with more clinical trials, diagnostic tests, and scientific research, an explosion of genomic data will inform these complex processes, with Illumina as a key beneficiary.

Two Undisclosed Positions

I recently purchased two additional positions that I am not yet ready to disclose. I may add to these positions in the future.

New Investment: Genasys (Ticker Symbol: GNSS)

Good businesses build products that customers want, while great companies build products customers need.

Genasys sells hardware and software that alerts people to dangerous situations. These are mission critical solutions offered through three business segments:

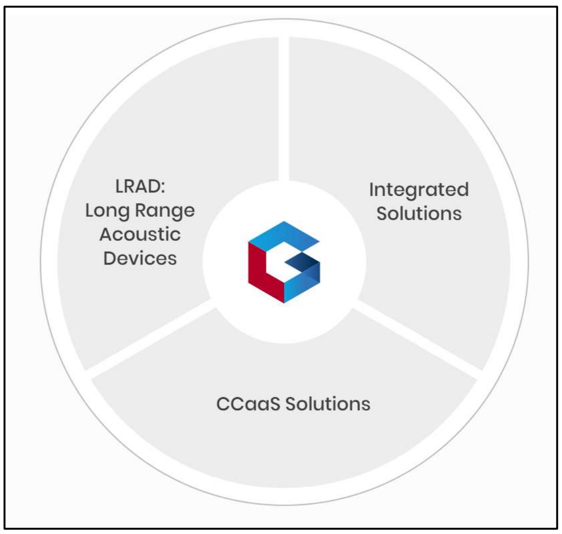
1. **Public Warning System (PWS) Software**
    a. Location-based messaging platform for government agencies to send emergency messages to their constituents’ mobile devices

   b. Sometimes referred to as "Critical Communications as a Service" (CCaaS)

2. **Long Range Acoustic Devices (LRAD)**
   a. Speaker systems that provide clear, long-range audio signals that prevent and deter potential threats

3. **Integrated Solutions**
   a. Solutions that combine both hardware and software in a single system

Genasys' products are gaining adoption worldwide because we live in an increasingly uncertain world. Increased environmental, biological, and man-made threats are driving acceptance of Genasys' solutions.



Above: Genasys Business Segments

Investment Thesis

1. **Genasys' Software Business Is In the Right Place at the Right Time**

In late 2019 the European Union mandated that all member nations acquire and deploy country-wide Public Warning Systems by June 2022.

Genasys is one of few providers of Public Warning System (PWS) software. Further, Genasys is a product leader with a track record of large deployments.

While Genasys' software business is small today, I estimate the E.U. opportunity is worth $30 to $50 million, and this event will drive further adoption locally as well as in other countries outside of Europe.

2. **Market Leading Hardware Business Generates Strong Cash Flow and Continues to Grow**

Genasys' hardware business is a market leader in a specialized defense contracting niche. The cash flows from this business are being reinvested into its emerging software and integrated solutions businesses to refocus the company into new growth vectors.

On a stand-alone basis, the hardware business has runway to continue expanding into new markets due to its secular tailwinds.

3. **Valuation Offers A Free Call Option On The Software Business Despite A High Likelihood of Success**

At the time I purchased Genasys shares, the market capitalization of the company was below $100 million, with around $20 million of net cash on the balance sheet.

Net of this cash balance, this implied their hardware-dominated business trades for roughly 20x trailing earnings.

If Genasys earns their fair share from the E.U. Public Warning System directive, that software revenue alone could add >$5m of additional net income.

If valued at 20x earnings (a low multiple for a mission-critical software business), those incremental cash flows alone represent **+100% upside to the current share price**. This ignores any growth from their current hardware business and the potential of integrated solutions.

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Genasys' software business is a sticky, mission-critical, recurring revenue stream and it will vastly improve the economics of the business overall. I believe meaningful software growth should also alter the way investors value the company.

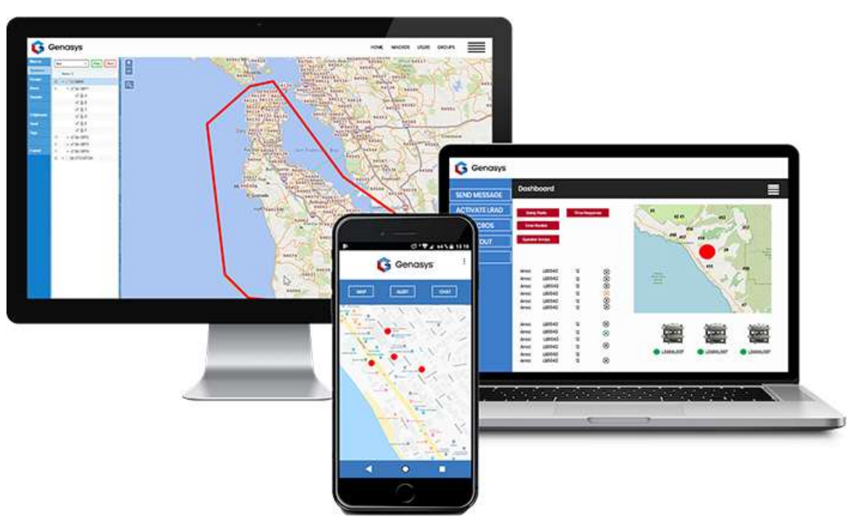
Business Overview - Public Warning System (PWS) Software

Although Genasys' software business represents a small part of its revenue base today, I believe their software platform will unlock much of the company's incremental value over the next few years.

In 2018, LRAD Corp (the predecessor to Genasys), acquired a small Spanish software company and ultimately assumed its name to highlight its shift in strategic focus.

The Genasys software business they acquired offers location-based Public Warning Systems (PWS) similar to the 'Amber Alert' system available in the United States.

Genasys' middleware sits within cell phone carrier towers while their front-end systems reside with government agencies. These systems allow government agencies to communicate alerts directly to their constituents based on their current location. The difficult part that Genasys figured out is how to provide this solution without asking users to opt-in to the service or download an application.



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Above: Genasys PWS Platform

Genasys' technology is quite complicated since it combines the physics of cell tower propagation with geolocation software. What enabled Genasys to build this platform was a 10-year history of creating unrelated location-based services when this market was emerging. This eventually led them to pivot into Public Warning Systems.

Importantly, the Genasys team has radio-frequency propagation expertise not commonly found in most software companies. In short, the Genasys software allows a government agency to send out a targeted alert message to anyone within a defined geofenced area through the existing cellular networks.

From a technical perspective, there are two ways to do this: Cell Broadcast (used by the Amber Alert system in the United States) and Location Based-SMS (LB-SMS). Location-based SMS is much more complicated than Cell Broadcast because it's more targeted, has read receipt capability, and can support two-way communication with individual users. For example, an agency using LB-SMS can monitor the traffic patterns of individuals after an alert is sent and if someone isn't leaving a danger zone, they can send a follow-up message to see if they need assistance.

From a competitive positioning standpoint, few companies can do both Location Based SMS and Cell Broadcast. As far as I understand, Everbridge is the only other company with this capability. It's important to understand that Everbridge is the 800-pound gorilla in the emergency communications industry, making them a very formidable competitor.

That said, like Genasys, Everbridge did not build their own Public Warning System: they acquired Unified Messaging Systems (UMS) based out of Norway in 2018. Everbridge also recently acquired One2Many, a Cell Broadcast business.

The other large player in the emergency communications industry is OnSolve, but I'm unclear if OnSolve can deliver LB-SMS, or if they are only focused on Cell Broadcast.

Genasys' marquee client is the country of Australia, where their solution is deployed across two of the three large mobile carriers over the past seven years. My understanding is that their system has served Australia very well, and they have been instrumental in helping communicate with the public during the 2019 wildfires.

I have demoed the Genasys software and met with members of their team. I came away impressed by their capabilities and believe that there is nothing that the Everbridge/UMS solution offers that Genasys does not. The biggest differentiation is Everbridge's brand, a larger workforce, and its balance sheet.

Now, let's discuss the biggest catalyst for PWS growth – the European Union directive.

The United States is a bit unique in that it already has an in-house, unified system, that broadcasts emergency messages to its citizens. Most countries across the world do not have any such system in place.

In 2019, the European Union passed a referendum requiring each member state to deploy a location-based public warning system for its people by June 2022. I expect that by late 2020 and early 2021 we will begin to see a significant amount of RFP and deal announcements.

This initiative represents a tidal wave of revenue that will be allocated to the existing players over a short period of time. Today, Genasys' PWS software revenue sits at a modest $2 million per year, compared to what I estimate as $30 to $50 million in contracts coming available through the E.U. This estimate might prove conservative, as Everbridge estimates this is a >$100 million opportunity.

The E.U. opportunity offers a significant amount of mission-critical, long-term, recurring software revenues, and I expect Genasys will capture a reasonable share: perhaps ~15-20% of the opportunity. While I don't believe Genasys will capture the majority of these contracts, they don't need to to be successful.

Lastly, I believe these contracts will serve as a turning point of adoption for the business. It's quite likely we'll see follow-on orders from local governments after these country-wide decisions are made. And outside of the EU, there is a meaningful runway to gain share in municipalities within the United States, as well as new countrywide deployments in emerging markets in Asia Pacific and Latin America.

Hardware Business – Long Range Acoustic Devices (LRAD)

Now that we've discussed the software opportunity, let's back up and discuss the core hardware business. While I probably wouldn't want to own the hardware business on its own, it's a nice niche business in the defense contracting space that offers a solid foundation.

In their hardware segment, Genasys manufactures and sells high performance "acoustic hailing devices," as shown below.

Above: LRAD 500x

Unlike a typical speaker system, these LRAD devices project a beam of concentrated sound over very long distances, up to miles away. Unlike a traditional soundwave that widely disperses a signal, Genasys' technology creates a tightly focused acoustic column, so if you aren't in-line with the beam of sound, you won't hear it. This allows sound to travel much further and with high clarity in ways a normal megaphone or speaker cannot.

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These acoustic hailing devices are used largely in a military setting to deter potential threats from occupying a particular space and to warn them without causing harm.

Genasys has dominant share of this niche hardware business, and while they had some competition in the past, they have largely withdrawn from this market. LRAD is the core supplier of acoustic hailing devices to the United States military, and to quote Genasys's CEO: ***"there were competitors, but we almost never see them anymore."*** This is a reasonably good business as evidenced by their greater than 50% hardware gross margins despite outsourcing much of the manufacturing.

From a product-market-fit perspective, organized militaries have a significant vulnerability that their enemies often exploit: militaries largely operate in "on/off" states. Most dangerous situations occur in an uncertain "grey zone" where it's unclear if a new presence is a threat or not. As long as an enemy doesn't "flip the switch" they can push the envelope. Such scenarios can lead to catastrophes if enemies exploit them or if a servicemember misjudges the situation. To combat this problem, the U.S. military has been making aggressive investments in non-lethal force technologies to deter potential threats and avoid unnecessary action. Genasys is a core beneficiary of this area of investment.

These acoustic devices first gained adoption by the U.S. Navy, and today, multiple LRAD devices are on every vessel in the U.S. Naval fleet. What precipitated this adoption was the 2004 attack on the USS Cole where it was difficult to identify if the quickly approaching attackers were a threat or a friendly vessel.

An LRAD device can send a long-range audible message to a potential threat, and if they continue moving closer it can deliver a very loud, harsh siren to drive away a potential enemy. The LRAD system saves lives without the use of force on potentially innocent victims.

Over the past 15 years, Genasys first focused on the U.S. Navy and more recently has been growing by outfitting the U.S. Army, where their devices are currently being deployed in most vehicle convoys. Outside of the U.S. military, Genasys' products are used in 27 militaries around the world.

While there is more growth ahead for Genasys within the Army, law enforcement, and other branches of militaries around the world, this is Genasys' legacy business, and it's not where the highest return opportunities are.

Defense contracting is lumpy, reliant on government budgets, and have few customers with long-lead times. In short, it's a difficult business to navigate. Although the current CEO, Richard Danforth has done a great job growing this legacy hardware business, he wants to diversify into more attractive markets that use their technology.

While I believe there are more large opportunities within the military, these cash flows will be reinvested in higher-value segments of the business – such as growing their software and integrated solutions businesses or making acquisitions to enhance the capabilities of their platform.

Integrated Solutions: Software-Hardware Hybrid Deployments

The Future of Genasys' hardware business is less tied to the military and is deeply connected to its software platform.

Rather than focus on the military use case for their acoustics, Genasys invented a new type of public siren hardware that offers uniform 360° coverage across miles of distance. Unlike a typical siren, these systems can broadcast verbal messages clearly.

Above: LRAD 360x

These systems are installed on poles like a traditional siren, but are controlled at a central console through the Genasys software platform. These systems can simultaneously trigger sirens, mobile phone alerts, social media alerts, and other notifications. Genasys is the only company that offers a hybrid hardware/software alerting network.

Some obvious use cases for these integrated solutions include areas prone to tornados, hurricanes, wildfires, earthquakes, or terroristic threats. Buyers of these systems typically include local governments, school systems, large companies, etc.

Management is investing in the future of these platforms, and it appears that there are large opportunities for public deployments of this technology. In the short period that Genasys and LRAD have been unified, they have won deployments in Laguna Beach, Mill Valley, Newport Beach, and parts of Puerto Rico.

Further, I believe that through acquisition they can make this platform more useful to customers and increase their lead by adding new software capabilities, sensors, and improved acoustics.

To Reiterate The Investment Case:

In short, I believe Genasys has multiple embedded options that can provide significant growth over the next few years and increase the earnings power of the business. Current valuation prices in little growth, and this means we have multiple ways to win.

I believe Genasys is at the right place at the right time with the E.U. directive, and the management team has a clear vision for building the best alerting platform. With time I expect their competitive advantage to increase as they gain new customers, improve existing products, and potentially acquire new capabilities.

Concluding Thoughts

As always, thank you for trusting me with your hard-earned savings, I don’t take this responsibility lightly.

These are very trying times, and none of us are immune to the impact of the COVID-19 pandemic. We will get through this in time.

I look forward to connecting with all of you soon.

Fondly,

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Disclaimer:

Bonsai Partners, LLC ("Bonsai") is the investment manager of Bonsai Partners Fund, LP (the "Fund").

This letter has been updated from its original version. Disclaimers were revised to reflect current standards and clarifications for the intended audience. Certain visual elements, formatting and brand identifiers have been refreshed to align with our current branding. These changes do not alter the core message of the original letter.

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The S&P 500 Total Return index is a basket of 500 large U.S. stocks, weighted by market capitalization, and is the most widely followed index representing the U.S. stock market. The S&P Total Return Index includes the reinvestment of dividends. Benchmarks and financial indices are shown for illustrative purposes only. They provide general market data that serves as a point of reference to compare the performance of other securities that make up a particular market. Such benchmarks and indices are not actively managed and do not reflect the expenses associated with managing an actual portfolio, the cost of investing in the instruments that comprise it, or other fees. No representation is made that any benchmark or index is an appropriate measure for comparison.

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