

Long Cast

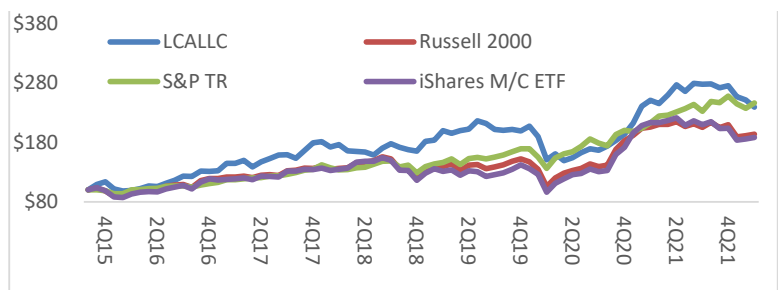
ADVISERS LLC

Dear Friends:

Welcome to our growing list of clients and followers. For the 1Q22 quarter (ended March 31, 2022), cumulative net returns declined 13%. Since inception in November 2015 through quarter end 1Q22, LCA returned a cumulative 139% net of fees, or 15% CAGR. By now you should have received your account statements from IBKR, which includes account returns, holdings, trades and fees. *Past performance is no guarantee of future results.*

Because our portfolio is concentrated on just a handful of typically small “off the beaten path” businesses that we tend to own for long periods, it is expected that returns will vary from the indices and often, as in this case, quarter to quarter.

Net returns	Long Cast	R2000	IWC	S&P TR
2015 (2-mos)	14%	-2%	-2%	-1%
2016	15%	21%	21%	12%
2017	36%	15%	13%	22%
2018	-8%	-11%	-13%	-4%
2019	21%	25%	22%	31%
2020	-3%	20%	21%	18%
2021	42%	15%	19%	29%
1Q22	-13%	-8%	-8%	-5%
Cumulative chg	139%	94%	88%	146%
CAGR	15%	11%	10%	15%



I remain grateful to have clients aligned with my long term, small company centric and research-intensive focus and I welcome the continued interest from individuals to institutions as I patiently grow the business. I remain committed to building a durable and sustainable business based on a repeatable investment process and intelligent capital allocation. *As a reminder, in an effort to align capital growth, business ownership and personal ethics, LCA does not invest in companies exposed to the hydrocarbon or defense industries.*

PORTFOLIO HOLDINGS

The quarter saw drawdowns on two larger holdings where I think the market has over-reacted to not particularly surprising news events. I’ll discuss these below and briefly touch on some newer portfolio additions. It bears worth acknowledging the obvious, that subsequent to the quarter our portfolio and most industries (excluding energy and commodities) have experienced further large and dramatic drawdowns. I’ll touch more on the general market towards the end of this letter.

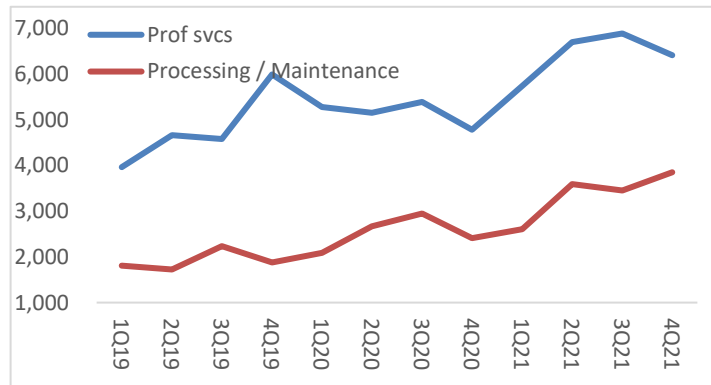
CCRD. On the last day of the quarter, [Bloomberg reported](#) that Apple was “developing its own payment processing technology and infrastructure for future financial products ... That includes payment processing, risk assessment for lending, fraud analysis, credit checks and additional customer-service functions such as the handling of disputes ... The effort is focused on *future products, rather than Apple’s current lineup of services.*” [emphasis added]

CCRD provides processing technology to Apple for its *current* credit card offering, operating through a licensing agreement with Apple (and Goldman Sachs as its bank). License fees represent a form of ownership of the software. Unless and until AAPL moves to a different processing software – and there’s no expectation they will on *current* products – CCRD will continue to generate license fees as long as active monthly account growth exceeds the next threshold. If active monthly account growth stalls or shrinks, there won’t be anymore license fees.

In either case, license fees are lumpy and unpredictable and though they go straight to the bottom line, we don’t own this for lumpy and unpredictable license fees. We own this because management has long showed an ability and effort to build something sustainable, profitable and cash flow positive. Relative to the *long term* outlook for this, I believe CCRD was cheap at \$35 and is even cheaper at \$20.

The early stages of the relationship between CCRD and AAPL saw significant software customization, which resulted in significant professional services revenues at +50% gross profit margins. As the card has matured (now two years old), the need for professional services by AAPL has diminished and as a result, professional services revenues have stabilized and gross profit margins have drifted back towards 40% levels. Margin pressure has been further compounded by labor constraints in India, where most of the engineering talent is sourced. The company has been adding offices in Dubai and Colombia in order to invest for the long term in growing its talent base and global exposure to future customers. This investment is a further temporary drag on margins.

It was always management’s view that the company would use large license customers like AAPL to build up the infrastructure for smaller processing customers, who don’t pay license fees but essentially rent the capabilities and pay akin to a per transaction fee. One can observe continued steady growth in processing revenues even as professional services has begun to taper. Processing revenue is a recurring revenue.



Concurrently, the company continues to pursue large license customers. On its last conference call, CCRD management indicated that 1Q22 would see a significant license payment, which might be driven by the recent launch of the [General Motors card through Goldman Sachs](#). However, management also indicated that the next “whale” client wouldn’t likely on-board until next year. So we’re seeing a temporary lull in large clients concurrent with broader market multiple contraction, even as processing revenues grow.

I have been adding to this position. Some say “there is a time to own and there is a time to not own” and there is certainly credence to that but I have always had most success as a buy and hold investor in what I believe to be well managed companies. There is certainly always room for improvement in discerning what is “well managed” but in my opinion a company like this that has a long history of strong performance, forward thinking management, growth, profitability, cash flow, now trading at single digit multiples at a time when the ability to buy on some form of credit is unlikely to abate, belongs near the top of the portfolio.

DAIO. Also at the end of the quarter, [DAIO announced](#) that as a result of COVID quarantines and shutdowns in China, “revenue shipments of approximately \$1 million are held up and delayed until the second quarter ... We have not received any requests to cancel orders to date and expect to deliver finished systems and other products as soon as the limitations are lifted.” The company recently reported 1Q22 earnings with strong bookings and a solid balance sheet, albeit with revenues depressed by delayed shipments.

The company is cyclical and will likely be impacted by any potential recessionary pressures notably due to exposure to two other cyclical industries; semiconductors and automobiles. However, the company has the balance sheet to sustain itself over the cycle and continues to improve its traction on sales of its “secure chip” platform called SentiX. Growing success in this area of the market could yield tremendous results over time.

Portfolio additions / subtractions. It’s been my goal and effort to narrow our portfolio and more deeply concentrate on fewer holdings. We’ve sold a few smaller positions and I’ve been working on some new ones that I believe have higher return potential.

In that regard, I’ll soon be attending an industry conference in the clean power space, digging a little more deeply into a company that benefits from, among other things, wind farm development and particularly the transition towards alternative forms of backup power. The company has a long and (to be honest) often mediocre history, but dramatic changes that began in 2016 (new hires, new managers, new business lines) appear to be bearing fruit. The company seems to be further aided by missteps from a competitor that was acquired by an automotive buyer. There is now strong backlog and profitability but it remains cheap, I think because the market is skeptical of this sudden blossoming of a long time underperformer. I am too! The due diligence trip will either allay or affirm that skepticism. I look forward to talking with other companies in the space and analyzing the industry ecosystem to better understand the competitive dynamics and expected durability of recent trends.

We have also been adding shares of a small company with a leading position in a niche market – they are considered the Nexis / Lexis type repository of scientific research - that has a new and very experienced CEO / CFO team. Years ago, I owned shares of a small company in a related space led by this same team. I was consistently impressed at their abilities and it had a successful (though premature) exit via acquisition by PE. Now we have an opportunity to invest with them again. I think they represent a massive upgrade over prior management. The market isn’t giving any credence to the change because their efforts have not yet shown up in the financials. I will write more about this opportunity in the future.

IN CONCLUSION: INVESTING WITH “BLOOD IN THE STREETS”

The economic and market environments changed substantially when Russia invaded Ukraine in February. Prior to the invasion, certain aspects of the market had been *somewhat* predictable. For example, it’s not controversial to say that early in the pandemic, when US energy “shut in”, oil prices turned negative and rig counts declined, it was fairly predictable that at some point, when the economy rebounded, energy prices could substantially increase until supply balances returned.

However, the war added a notable amount of fear and gloom into the markets, and I don't think it's overwrought to say it's also injected quite a bit of sadness into our lives. Whatever led to the invasion, whether it was Putin's desire for conquest, to energize Russian patriotism, or to control natural gas fields in Eastern Ukraine, it does not appear to be going as per his expectations. Now, the biggest folly of all is how long this will go on, and how many people will die, so he can "save face", which along with war itself, is a most debased human instinct.

There is tangible rationale why equities have declined – inflation pressures profit margins reducing future earnings expectations, rising uncertainty and fear shrink multiples, etc. – but chief among them is rising interest rates. Back when Clinton was President and I lived on Bond Street in NOHO (rent in a loft: \$500 / month), a street vendor shared with me an analogy they don't teach in business school. He said interest rates were like heroin for the American consumer; take it away by raising rates and the economy shudders like a junkie in withdrawal. It remains an apt description for today's markets.

But the market isn't just a rational machine, it is also an emotional machine, and it has a tendency to overshoot in times of excitement and despair. As sensible as it is to reconsider profit margins and multiples, today the market shows little appetite for separating quality from mediocrity. Everything is getting sold.

As always, it would be unwise to project the present into the future. I am confident current conditions won't remain forever. I don't believe it will revert back to what it was before but business will survive the tempest. I continue to be a long term shareholder of small businesses that have the opportunity to grow into bigger ones. The best time to be a buyer of such businesses is when the market is rife with fear. Whether you are an active or passive investor, with me, with another investment manager, or doing this on your own, now is a time to sharpen the pencil and buy advantageously.

I appreciate your entrusting me with your capital and the responsibility of being its steward. As always, I look forward to continuing this conversation into the future.

Sincerely / Avi
Brooklyn, NY
May 2022