

# Far View Capital Management

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July 15, 2022

Dear Partner,

Welcome to performance update for Far View Partners L.P. (Far View) for the half-year that ended on June 30, 2022.

## **Portfolio Performance**

During H1 2022, Far View generated a return of -45.43% net of all fees and expenses, which comprised -27.89% in Q1 2022 and -24.32% in Q2 2022. Since inception on July 1, 2011, Far View Partners has generated a cumulative net return of +121.11%, a +7.48% CAGR.

In H1 2022, Far View suffered significant losses in our European e-commerce positions including Westwing Group SE and CDON AB. Russia's attack on the Ukraine weakened European consumer confidence and combined with cyclical headwinds faced by the e-commerce industry to hurt near-term results and destroy investor sentiment. While our businesses should benefit from long-term tailwinds as European e-commerce penetration continues to climb to US levels, these macro and industry challenges led our securities to experience large losses in H1 2022. Finally, Far View's worst losses were suffered in Naked Wines PLC, discussed below.

Far View enjoyed gains in Distribution Solutions Group (formerly known as Lawson Products) as the company completed its game-changing three-way merger with TestEquity and Gexpro Services. We also had gains in our equity index hedges as they benefited from market declines.

On June 30, 2022, the Far View's portfolio consisted of long equity investments in the United States, Canada, United Kingdom, Sweden, Germany, Spain, and Australia as well as short positions in equity indices as a hedge. Far View was fully invested at the end of the quarter and maintained short positions in various currency futures for hedging purposes.

## **Naked Wines**

Far View's biggest loser in 2022 has been Naked Wines (WINE). The stock performed well in 2020 as COVID stimulated a purchasing boom for online wine. While I trimmed the position during an abnormal spike in 2021, I held onto most of Far View's shares because I believed that the pandemic generated a new level of demand by raising customer awareness of WINE's superior solution. I expected this increased awareness to help the company accelerate growth and take market share in an underpenetrated online market.

WINE uses a subscription business model based on investing capital upfront in advertising and first-order discounts to acquire customers (this is the customer acquisition cost or CAC). The customers then subscribe to purchase products and their subscriptions generate stable, long-term cash flow for the company (this is the customer lifetime value or LTV). WINE looks to earn an LTV that is approximately double the CAC for a customer cohort over five years. If they achieve this goal, the company earns high returns on the capital invested in customer growth and generates growing long-term cash flow.

Because of this business model, WINE faced significant headwinds in late 2021 and early 2022. Apple's new consumer privacy regulations lowered online advertising effectiveness. The combination of lowered effectiveness with higher advertising costs significantly increased WINE's CAC. Compounding this problem were input cost inflation and supply chain challenges that lowered per-unit profitability, a significant LTV driver. WINE's LTV/CAC declined well below their ~2x target and the returns from new customer acquisition dropped below acceptable levels, making an investment in growth less attractive.

Unfortunately, WINE's management failed to adjust promptly to this new reality. The company was slow to open new avenues for customer recruitment and to upgrade underperforming areas of the acquisition funnel. As a result, customer recruitment and conversion lagged. Furthermore, WINE chose not to increase prices until recently to offset cost inflation and protect the company's profitability. WINE is now making these changes, but they should have happened earlier.

WINE also has not been careful enough with corporate spending. Comparing forward guidance to last year's results, the company projects general and administrative expense to grow more than 40%, an unacceptable increase compared to the expected 3% revenue growth. While WINE's management would argue that they are investing in the foundation for long-term expansion, these increased corporate expenses during a time of challenging near-term customer growth hurt the company's current profitability and suggest a lack of cost discipline.

Finally, WINE overinvested in inventory in fiscal year 2022, almost doubling it despite weaker new customer recruitment. This significant cash outflow to grow inventory combined with limited near-term profitability to weaken the company's previously pristine balance sheet. This problem was exacerbated by a poorly-structured credit facility, creating unnecessary and damaging concerns about the company's capital position.

Since the results release in June, I have spent significant time assessing my investment thesis to determine whether the company remains an attractive use of our capital.

I continue to believe WINE enjoys an advantageous competitive position in a market where direct-to-consumer retailing adds significant value to both consumers and winemakers. The company has barely begun penetrating the available addressable market and remains poised to grow as it makes necessary improvements. At scale, I expect WINE to generate attractive cash flows and sustained long-term growth.

While I believe WINE is a valuable business at its core, the company needs better execution or a strategic buyer. I have begun to work with the management team to create a plan to remove balance sheet concerns and return the company to profitable growth. Our continuing investment in WINE will depend on my assessment of this new plan and its implementation. Depending on the progress, I may materially increase our WINE investment or exit it if I no longer think it is the best use of our capital.

While I can't change the losses we have suffered on WINE in 2022, I am working hard to find the best path forward from our current situation. Please feel free to reach out if you would like to discuss it in more detail.

### **The Far View Partnership**

At the end of June 2022, Far View switched our administrator from Atlas Fund Services to Core Fund Solutions. I expect this transition to be seamless. Angie from Core Fund Solutions has acted as Far View's outsourced CFO for almost 10 years and understands Far View's operations. I have also contracted with The Alpha Cooperative to provide outsourced CFO, COO, and compliance services from this point forward. I would like to thank Atlas for six great years as Far View's administrator.

I am frustrated with the Far View's large losses so far in 2022. While these periods of weak performance are almost certain in a long-term investment career, that inevitability does not make them any less difficult. As a reminder, I have invested the vast majority of my net worth in Far View, and I am the largest investor. I feel the pain of these declines alongside my partners as my net worth has shrunk materially.

While recent returns disappoint me, I remain optimistic about Far View's long-term potential. I believe we own competitively advantaged companies with promising, long-term prospects. While our holdings' share prices are out of favor, I believe our portfolio continues to increase its long-term value.

Furthermore, I believe recent share price declines have created attractive opportunities across our portfolio and watchlist. During H1 2022, I trimmed and exited lower conviction positions and recycled the capital into more compelling new and existing investments. I am excited about the opportunities in which we have invested capital in 2022.

Most importantly, Far View is structured to thrive during these volatile periods. Our partnership consists of thoughtful investors who understand our long-term investment strategy and the opportunities that can arise during downturns. Unlike many funds who are facing redemptions, I am honored that Far View has enjoyed net subscriptions in H1 2022 and am thankful to be partnered with long-term oriented investors.

Feel free to contact me with questions about Far View as I am always interested in discussing Far View's investment journey with like-minded, long-term partners.

Sincerely,



Brad Hathaway  
Managing Partner

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