LAKEHOUSE CAPITAL
A Motley Fool Company

LAKEHOUSE GLOBAL GROWTH FUND
MONTHLY LETTER
31 JULY 2018

Dear Lakehouse Investor,

Companies Held:	18
Cash Allocation:	20.3%
Top 5 Portfolio Holdings:	35.2%
Net Asset Value per Unit:	$1.0968
Fund Net Asset Value:	$83.8 million
Benchmark:	MSCI All Country World Index Net Total Returns (AUD)

July was a lively month for the Lakehouse Global Growth Fund as most of the Fund's portfolio companies reported earnings. Some companies met our expectations, some exceeded, and some fell short. On the whole, though, we remain pleased with the Fund's basket of portfolio companies and their long-term trajectories. To that end, we're still yet to sell a single share.

The Fund returned 1.1% net of fees and expenses in July compared to 2.4% for its benchmark. Since inception at the start of December 2017, the Fund has returned 9.7% compared to 6.4% for its benchmark. We're pleased that the Fund is off to a good start towards its objective of long-term outperformance, particularly given our outsized cash position. That said, we do not read much into early performance and neither should investors who embrace our long-term, high-conviction strategy.

The Fund held 18 positions as of the end of July, which is a bit shy of our typical range of 20 to 40, though we expect to shift into a normal range soon. In terms of the Fund's most meaningful holdings, the Fund's 5 largest positions in order of sizing at the end of July were in **Alphabet, Facebook, PayPal, Monster Beverage** and **Visa.**

Meanwhile, the Fund's position in cash, which is held mainly in US dollars, Aussie dollars and Euros decreased slightly from 21.4% to 20.3%. Similar to the Fund's position count, the Fund's cash balance is outside of its typical range of 5% to 15%. We similarly expect it will be within a typical range soon, however, investors should expect us to remain patient stewards of the Fund's capital.

We're also now at a point where we think breaking down sector allocation is worthwhile. The Fund's largest sector allocations as of the end of July were to information technology (45.7%), consumer discretionary (16.6%), and consumer staples (11.7%). We're larger than the benchmark in all three sectors and expect that will consistently be the case over time as we view these sectors, or at least subsets of them, as having superior economics and long-term tailwinds.

Portfolio Company News

Over to our results round-up. It would be tempting to jump to the results of each of our portfolio companies, however, a quarter is a short time against our long-term approach. Further, this is a Fund performance report, not the financial press or a newsletter, and so we'll will restrict our commentary to substantive news on impactful and key positions.

The biggest contributor to performance during the month was Australia's own **Atlassian** (+15.8% during the month), whose fiscal fourth-quarter revenue increased 40% year on year. The company also surprised and delighted investors with the announcement that, rather than continuing to spend resources competing with Slack in messaging, the two companies had formed a strategic partnership. We're pleased to see Atlassian make such a mature, albeit humbling, capital allocation decision. The company's sharper focus on other growth opportunities is sensible and we remain content investors.

Facebook, meanwhile, whose core thesis we reviewed in the recent annual letter, fell 11.2% during the month and was the most significant detractor to performance in July. The results were objectively strong: Revenue increased 38% year on year in constant currency terms, daily active users on the Facebook platform increased 11% year on year despite all the bad press, and the company revealed that 2.5 billion people each month access at least one of Facebook, Messenger, Instagram, or WhatsApp.

Investors were taken aback that quarterly revenue came in light relative to expectations, though, and that second half revenue guidance would mark a step-down, albeit partly due to currency. An even bigger surprise, and the one that sent the stock tumbling, was that the company guided for operating margins to fall in the coming years from the recent mid-40%'s to the mid-30%'s.

We expected Facebook to ratchet up spending in order to secure and enhance its platforms following the recent spate of bad press, however, the scope of its plan is enormous. The company is guiding for about US$15 billion in capital expenditures in 2018, which is roughly what was cumulatively invested across the previous 4 years. Further, the company is leaving money on the table by emphasising more meaningful engagement among users and new forms of sharing that aren't yet fully monetised.

Facebook would be grossly underearning on an operating margin in the mid-30%'s. For context, in 2009, amidst the worst recession since the Great Depression, Facebook earned a 33.7% operating margin on just US$777 million in revenue, which is around 1/100th of Facebook's expected revenue in two years' time. That's to say, Facebook plans to significantly sacrifice short-term profitability in order to strengthen and enhance its core while creating new opportunities for growth. And, while the quantum of investment was larger than we'd anticipated and watching the shares fall 21.4% over 2 days was not fun, as long-term investors we are hard-pressed to complain when one of our portfolio companies decides to prioritise the future over the present.

Zooming out further, we note Facebook would still be wildly profitable at a mid-30%'s operating margin, should that actually come to pass, and that the business has around 8% of its market capitalisation in net cash. It's also worth remembering that all these short-term sacrifices and the negative headlines they've driven -- the shares' fall was the lead story at *The Washington Post* -- could help to get regulators off the company's back.

All in all, we remain enthused about Facebook's long-term prospects. Each of Facebook, Messenger, Instagram, and WhatsApp has more than a billion monthly active users and rising, and the company is taking methodical steps towards monetising those users in different product-relevant ways. For example, after the strong initial success of a WhatsApp payments trial in India, the company is not only working towards a full launch in the country but also broadening the platform to other countries. The optionality around such large, highly engaged platforms is immense, and we look forward to continuing to follow the company's progress.

Other top 5 positions reported for the Fund during the period as well. Alphabet saw another stellar quarter with revenue increasing by 23% year on year in constant currency terms thanks mostly to strong results from the company's mobile search advertising business. Notably, Alphabet has now had 34 straight quarters of 23% growth, which is remarkable for a company of its size, and the company's long-standing investment in Waymo could soon bear commercial fruit. Remarkably, Waymo's driverless vehicles are traversing about 25,000 miles a day, which is like 5 return trips across Australia every single day. Such bets, which complement a juggernaut of an advertising business, leave us feeling that Alphabet is well placed to continue growing at high rates for a long time to come.

PayPal's results were thesis-affirming once again, with continued growth in total payment volume (up 27%, with mobile-based payment volumes growing almost 50%), active accounts (+15% to 244 million), and average transactions per account (up 9%). Pleasingly, payment volume for the Venmo platform alone was more than US$14 billion during the quarter, having grown 78% year-on-year. Venmo's functionality also continues to expand: users can now pay for their Uber rides and food ordered on UberEATS with Venmo. Ultimately, the PayPal family of brands continues to gain share of growing markets, and their strengthening networks combined with a more partner-focused strategy has solidified the company's position.

Visa's results were much in the same vein, where the company surpassed analyst profit forecasts and raised full-year guidance as a result. The broad read-across from Visa's results was reassuring: the macroeconomic environment is stable to improving, the company's execution continues solidly as before, and the integration of Visa Europe appears to be progressing well. We also note that Visa's payments volume grew more than 20% year on year in India, which is a promising long-term market in which Visa already has greater than 50% share. Put all that together with a continued emphasis on repurchasing shares -- including US$7.4 billion over the past year -- and we long-term investors have a good deal to be enthused about.

Looking Ahead

We're pleased to announce that we have added a new research analyst to the investment team, Erwin Tan. We plucked Erwin out of an incredibly deep candidate pool -- we were fortunate to have around 100 applicants for the role -- and are excited to get him on board. He's got a great set of tools and a strong passion for our style of investing. Welcome, Erwin!

As ever, thanks for your time and trust.

Best Regards,

Joe Magyer, CFA
Chief Investment Officer