LAKEHOUSE GLOBAL GROWTH FUND
ANNUAL LETTER
30 June 2022

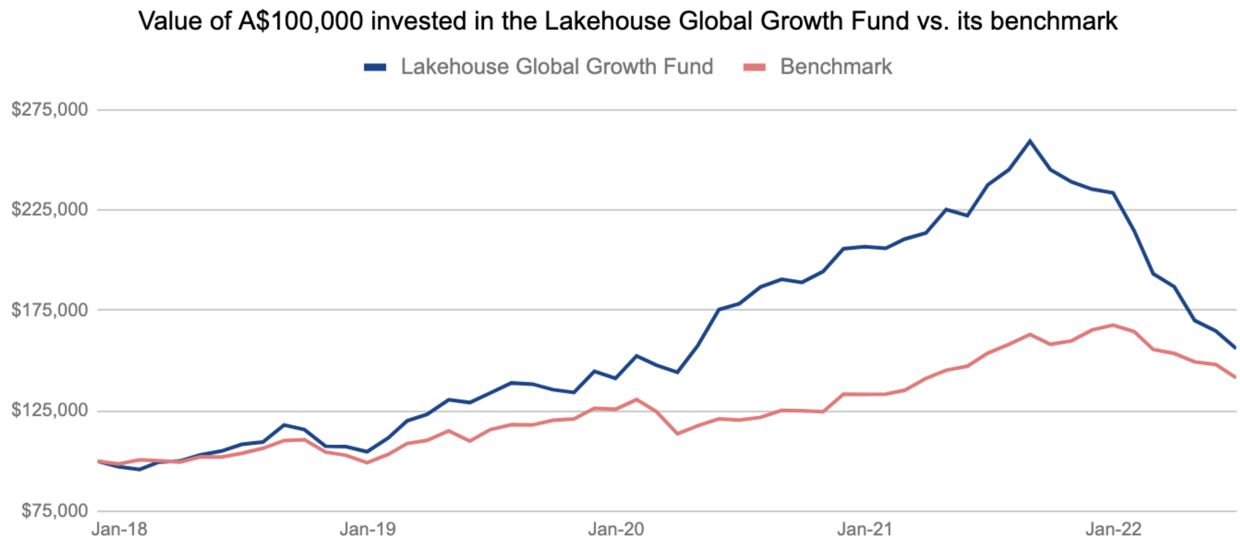
Dear Lakehouse Investor,

This past year was a challenging period for the Lakehouse Global Growth Fund as equity markets, and growth stocks in particular, sold off in response to concerns around elevated inflation, rising interest rates and a potential recession. The Fund returned -34.3% net of fees and expenses compared to -8.0% for its benchmark. Since inception at the start of December 2017, the Fund has delivered a net total return of 56.0% compared to 41.5% for its benchmark. In annualised terms, the Fund has returned net 10.2% since inception compared to 7.9% for its benchmark.

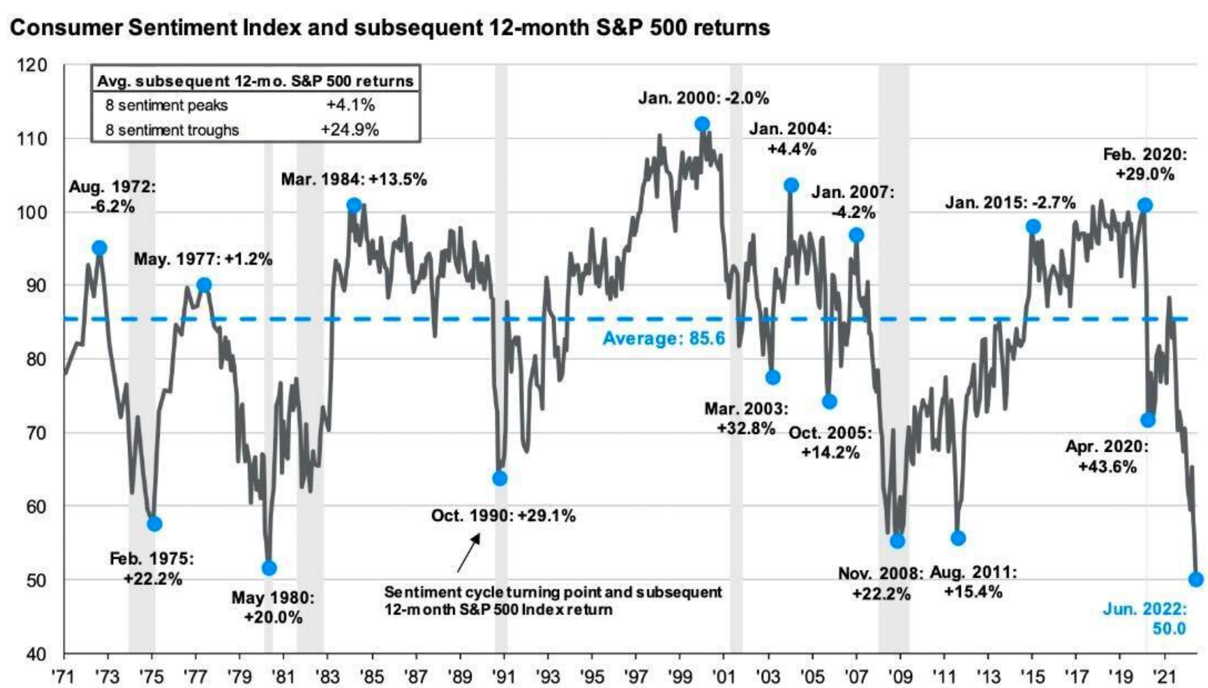
Fund Metrics	
Companies Held	20
Cash Allocation	8.9% (including reinvested distributions)
Top 10 Portfolio Holdings	61.2% (including reinvested distributions)
Net Asset Value per Unit (mid)	$1.2688 (after a 18.01c distribution)
Fund Net Asset Value	$220.3 million (after $7.8m net cash distribution)
Benchmark	MSCI All World Index Net Total Returns (AUD)

	FY18*	FY19	FY20	FY21	FY22	Inception (p.a.)
Lakehouse Global Growth Fund	8.4%	23.6%	33.2%	33.2%	-34.3%	10.2%
Benchmark	4.0%	11.3%	4.1%	27.7%	-8.0%	7.9%
Excess Return	4.4%	12.3%	29.1%	5.5%	-26.3%	2.3%

**Performance calculations are based on exit price with distributions reinvested, after fees and expenses, since inception on 30 November 2017. Benchmark: MSCI All Country World Index net total returns (AUD). Past performance is not indicative of future returns.*



Central bank rhetoric around tightening monetary policy to combat inflation began weighing on asset prices towards the end of 2021. The uncertainty and inflationary pressures were then exacerbated when two of the world's largest commodity producing nations (Russia and Ukraine) went to war in February of this year, and China began reinstating rolling Covid-19 lockdowns across various parts of the country. This convergence of exogenous factors drove equity (and bond) markets lower with the S&P 500 index declining 20.6% over the last six months alone, representing its steepest first-half decline since 1970. Even more notable is the fact that consumer sentiment (as measured by the University of Michigan) is now lower than it was during the GFC and the 1990's recession.



Source: *JP Morgan, Guide to the Markets®, 3Q 2022*

This chart provides perspective on current sentiment in the context of time. The reality is that bouts of negative sentiment are nothing new, and in times like these, acting like an owner with a long-term mindset is incredibly important. When sentiment and markets are at their greatest despair, the swing to more positive outlooks and performance is often swift and sustained. Equity markets are forward-looking and that's why shares generally start to recover well before backward-looking economic data begins to hint at a turnaround. While history seldom repeats it often rhymes.

We acknowledge that the Fund's underperformance relative to the benchmark over the last twelve months has been disappointing and it never feels good to deliver negative returns to our investors over any period. However it's important to remember that no investment style will lead over every twelve month period. Clearly growth style investing is presently out of favour but we remain confident that our investment strategy will outperform over rolling 5-year periods. Our confidence comes from the fact that our portfolio companies continue to execute on their growth opportunities and display robust fundamentals. In fact, we view the current market as a very attractive set up for future investment returns for long-term, growth focused investors.

Our commitment to our growth-focused philosophy and process has resulted in negative investment returns for our investors, particularly in the back half of this financial year, as we continued to avoid the temptation to invest in capital-intensive, price-taker materials and energy businesses, which have been the best performing sectors this year. Despite this pain, we still do not believe we possess any edge in forecasting commodity prices, and nor do we wish to invest in businesses exposed to such highly cyclical external forces, or try to time such cycles. Instead, we will continue to stick to our knitting as patient, fundamental bottom-up business analysts working towards more probable outcomes.

Ultimately, our portfolio represents a collection of businesses which exhibit clear market leadership, superior underlying economics and growth potential, and clean balance sheets. In our view, these businesses are in a very strong position relative to the majority of other businesses, whether they be considered 'growth' or 'value' style. To that end, despite all the headlines of doom and gloom, the Fund's portfolio companies still managed to grow their revenue at 21.4% year-on-year on a weighted-average basis through their latest reporting period. This points to the fundamental strength and growth of the portfolio's holdings, which has not been reflected in valuations and share price movements of late.

We will speak more to sources of return and our portfolio companies later but first, we will address the three most common questions we have been receiving from investors. Unsurprisingly, they are all macro related.

How will inflation impact the portfolio?

As we have mentioned in previous letters, we remain comfortable with the portfolio and its ability to perform should the current inflationary cycle continue. This is due to four fundamental reasons.

Firstly, pricing power is a key trait that we seek in all of our portfolio companies. The ability to pass on cost increases to customers without impairing end demand is an extremely valuable trait to have. This is true in any type of economic environment, but particularly one where inflation is running hot. Across the portfolio, we have already seen a number of companies flex on pricing in response to market conditions, with Amazon being one of the most recent examples. In February, they increased the cost of Prime membership nearly 20% and in April they added a 5% fuel and inflation surcharge to FBA fulfilment per unit rates. This, in our view, is evidence of strong fundamentals at play that steer the probabilities of success to the long-term investor who patiently waits for the current macroeconomic tide to pass on by.

Further still, our portfolio companies exhibit superior margin structures. On average, companies in our portfolio have a gross margin of 59% compared to roughly 38% for the average company. This means that a rise in input costs will have much less effect on profitability for companies within our portfolio relative to the average. Another solid line of defence in this environment.

We also own a number of businesses that have ‘toll booth’ like business models, whereby revenue is effectively a percentage of the dollar value of all transactions crossing their ecosystem. Companies of this nature, such as Amazon and MercadoLibre in e-commerce or Visa and PayPal in payments, are very well placed for an inflationary environment due to their natural inflation protection. Lastly, if one is concerned that central banks will increase interest rates materially from here to chase down inflation, then our avoidance of highly leveraged companies should also serve us well.

Inflation will likely prove challenging for capital intensive businesses that have minimal competitive differentiation. At the end of the day, the large majority of businesses in commoditised, capital intensive and cyclical industries (think airlines, energy, utilities etc) are price-takers and are less attractive businesses for long-term equity investors to own. Their destinies are impacted by a number of external factors that are often beyond their control and as a whole they tend to produce poor returns on capital over the cycle. As mentioned above, though, we don’t own these types of businesses and avoiding them is a key tenet of our investment strategy.

Do higher interest rates mean lower multiples?

The short answer is yes. All else equal, higher rates will lead to lower multiples/valuations for equities. However, it’s important to note this is true for all asset classes (be it bonds or real estate) and significant multiple compression has already occurred, particularly for long duration growth names. The market has already priced in a circa 3.5%-plus terminal Fed Funds rate by early 2023 (vs 1.6% today) and many stocks have already derated meaningfully in response.

How will the portfolio perform if we have a recession?

It's clear to all that the US Federal Reserve is currently doing its best to slow demand with the aim of taming inflation. If they do go too far and trigger a significant recession then earnings growth will slow - or go into reverse - across the board, and this is obviously not an ideal situation. That said, we are confident that if such a scenario comes to pass, our portfolio companies are well placed to perform in a relative sense.

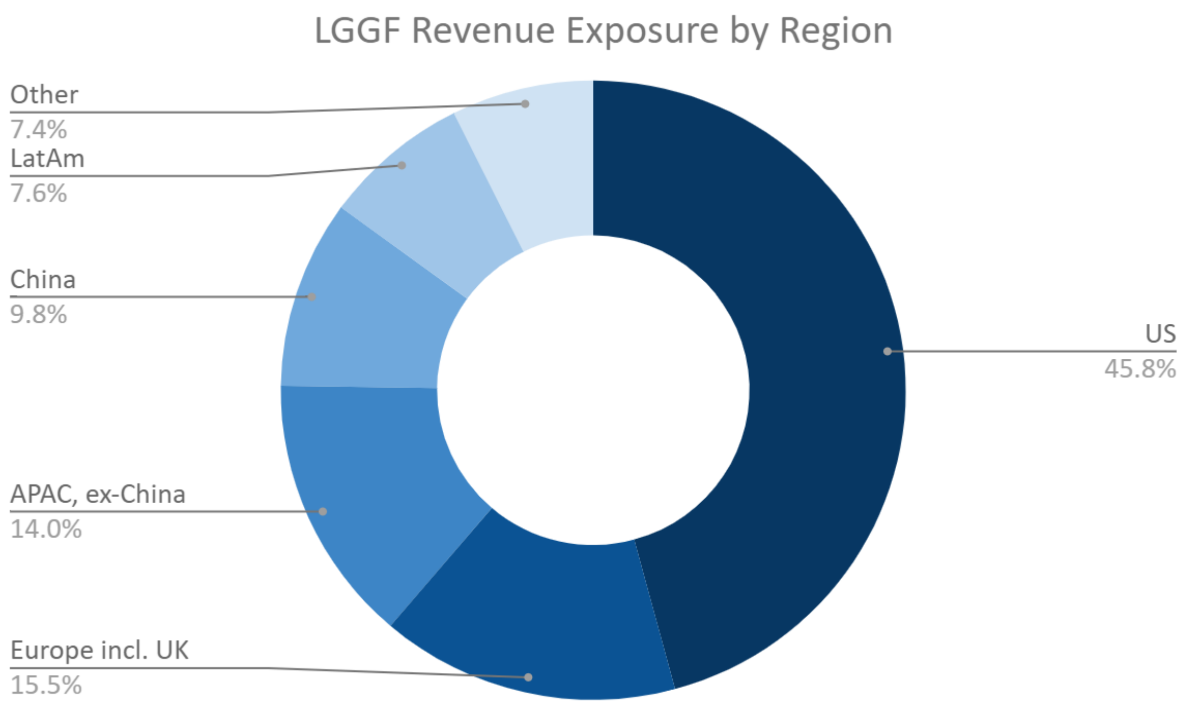
The reason being, we own secular growth companies that tend to create their own success and have limited cyclicality. If we were to enter a tough economic environment, the secular trends that drive our companies (the shift towards cloud computing; e-commerce; digital advertising etc) will endure and we believe that our companies will be able to sustain above average rates of growth. Our companies also tend to be well-capitalised, market leaders with superior value propositions, which quite often benefit during recessionary environments in a relative sense as rapid market share shifts can occur as smaller, weaker companies (particularly those reliant on external funding) tend to struggle. So, with the macro out of the way, let's turn to the portfolio.

The Fund held 20 positions as of the end of June, the ten largest of which are listed below:

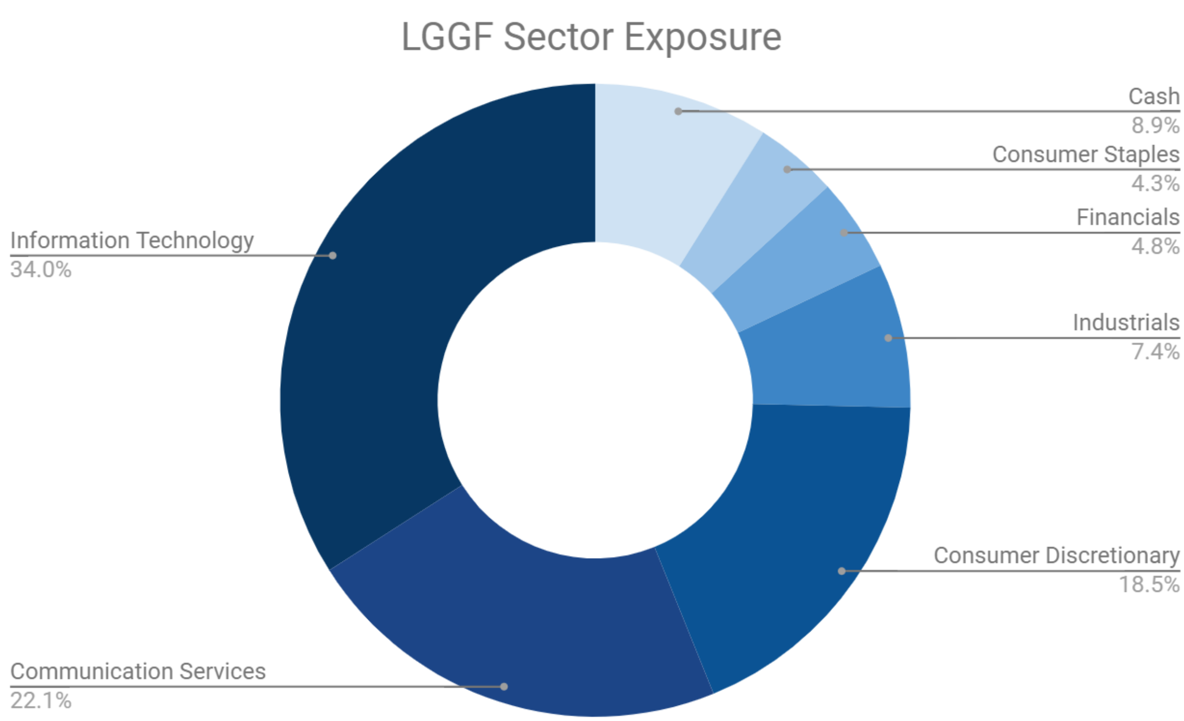
Company	**Headquarters**	**Lakehouse Investing Fascination**
Amazon	USA	Loyalty, Networks, IP
CoStar Group	USA	IP, Loyalty, Networks
Alphabet	USA	IP, Networks
Visa	USA	Networks, IP, Loyalty
Tencent	China	Networks, IP, Loyalty
Avalara	USA	Loyalty, IP
LVMH	France	IP
MarketAxess	USA	Networks, Loyalty
MercadoLibre	Argentina	Networks, Loyalty
ServiceNow	USA	Loyalty, Networks

The Fund still owns 16 of the 20 companies it owned twelve months ago, making for a position-level implied holding period of five years. This aligns with our long-term holding orientation but is not to say we have been static in those names, we regularly reassess opportunities in absolute terms and relative to the portfolio with many of those holdings moving in and out of the top 10 as we actively manage our exposures based on valuations and business fundamentals.

Turning to geography, the Fund looks US-centric judging from the preceding table, which is true to some extent as it provides far and away the largest opportunity set. That said, the Fund holds stakes in companies headquartered in ten countries: the US, Canada, Argentina, France, Netherlands, Sweden, Luxembourg, Japan, Singapore and China. Furthermore, all of the Fund's US-based holdings have operations outside the US. Flow it all through and only 45.8% of the Fund's portfolio company revenue comes from the US.



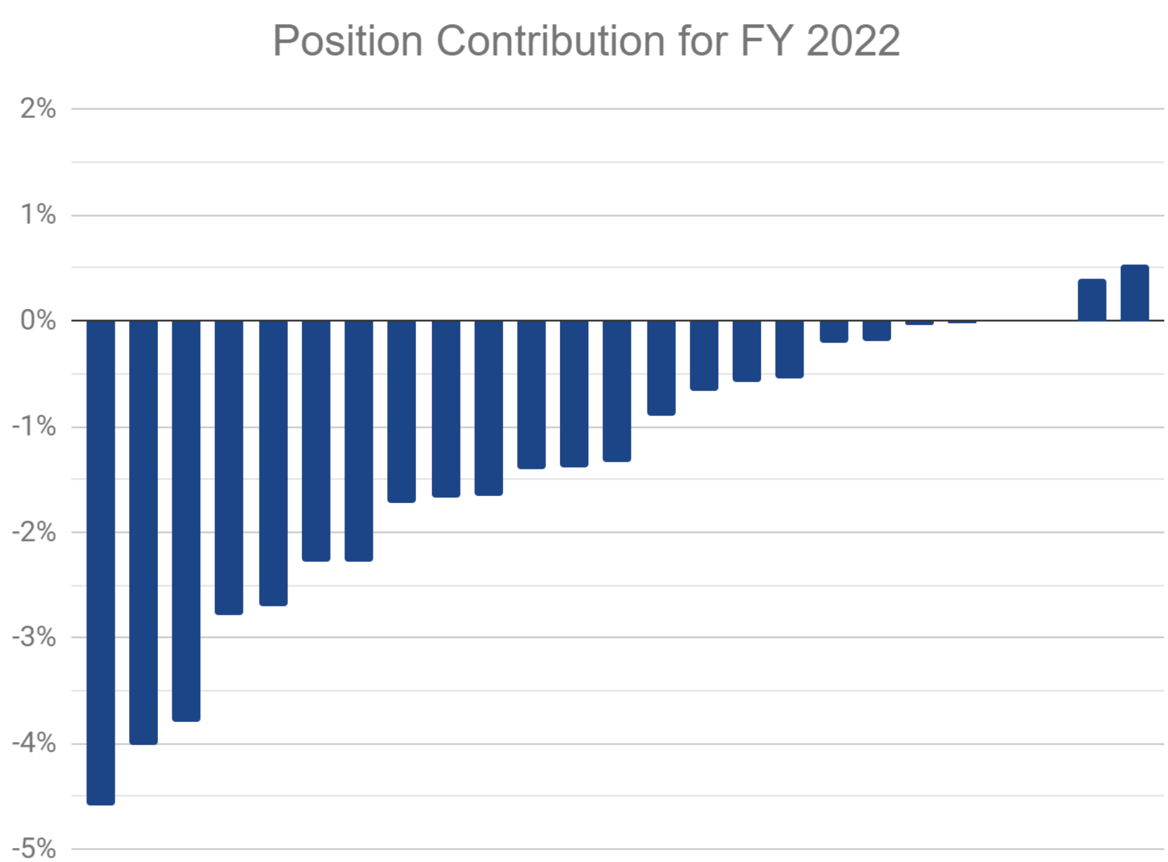
Zooming out to the sector-level, the Fund's largest allocations at year-end were to information technology (34.0%), communication services (22.1%) and consumer discretionary (18.5%). The Fund is larger than the benchmark in all three sectors and we expect that will consistently be the case over time as we view these sectors, or at least subsets of them, as having superior economics and long-term prospects.



The Fund closed out the year with a cash allocation of 8.9% (inclusive of distributions that reinvested on 1 July), down from 11.6% (inclusive of reinvested distributions) at the start of the year. We value having some dry powder and flexibility, particularly given our high-conviction approach, and we have made good use of it during the downturns in late 2018, early 2020 and more recently in the first half of 2022. We continue to target a cash allocation of 5% to 15%.

Performance

Turning to the portfolio, and the two most significant contributors to performance during the year were, in order, Monster Beverage (+10.8% during the year) and Charles Schwab (+35.5%). Note that the table below shows the total returns to the portfolio contributed by position, which reflect total returns and average position sizing during the year, while the percentage shown after each name listed above reflects the total return for the year of the individual share. We'll discuss each in turn.



It comes as no surprise to us that in a year marked by rising interest rates and mounting inflation concerns Monster Beverage was a strong performer, as investors favoured the business' defensive nature, its ability to raise prices, and maintain market share. We first initiated our position in Monster back in the early days of the Fund in March 2018, based on our analysis that energy drinks were a far more lucrative business than, say, bottled water or packaged food, and Monster's international expansion efforts would eventually pay off.

The thesis has held up well on both those fronts: energy drinks continue to grow at the fastest pace relative to other non-alcoholic beverages, and Monster's international sales have delivered a 21% compound annual growth rate over the last 5 years (to 2021) versus its US sales growing 9%. We also like that this revenue growth has come with operating leverage too: Monster's operating income in the international segment has grown nearly 3.5 times as fast as the US.

Our recent concern with the Monster investment thesis has been around rising input costs, particularly aluminium (the price of the commodity went up 65% year-on-year during the first quarter of 2022 alone) and freight (given global port congestion continues and Monster has had to air freight ingredients to meet consumer demand). Both have eaten into the company's margins, however pleasingly, sales growth in the US and international divisions has remained in the low twenties as of the first quarter of 2022. The brand's strong appeal with its target consumers has allowed Monster to raise prices in the US and Europe, with more price increases scheduled for the back half of 2022, providing further support to margins. Overall, the company continues to execute well, especially in light of the tricky macro environment, and we remain enthusiastic about its future prospects.

Charles Schwab is the largest discount broker in the United States with more than 33 million brokerage accounts, 2 million corporate retirement plans, and total client assets of US$7.9 trillion. Schwab's shares performed well during the year on the back of the company's successful merger with industry heavyweight TD Ameritrade and expectations that interest rate income would continue to grow as interest rates increased. Trading revenue on the other hand declined roughly 20%, which was not entirely unexpected, as the company had benefited from a significant surge in trading activity during the pandemic.

Despite the moderation in net new account growth and trading activity, it was pleasing to see that Schwab did not experience any material churn amongst existing accounts. As we have noted previously, while brokerage activity is cyclical, the average brokerage account itself is very sticky -- we estimate normalised annual retention rates for accounts of roughly 93% -- and that the average client assets per account grow over time thanks to asset growth and clients collectively being net savers.

Part of the initial thesis for owning Schwab was that it provided a nice natural hedge for the Fund as it tends to perform well when interest rates increase. And the position played out well for us as the shares appreciated materially in response to higher interest rate expectations. This provided us with the opportunity to harvest the remainder of our gains from Schwab in January and redeploy into other growth companies that had derated in response to higher rates. Since we sold in January, shares of Schwab have declined by more than 30% and while we remain mindful of the cyclical element of the business, we continue to monitor it closely in the event that an opportunity to re-establish a position emerges.

The three worst contributors to performance during the year were, in order, PayPal (-73.8%), Sansan (-66.5%), and MercadoLibre (-55.4%).

PayPal was our worst performing investment during the year in terms of contribution. The company experienced several challenges as it lapped a tough Covid-fueled comparable period with supply chain issues hindering growth in cross border transactions and inflationary pressures negatively impacting consumer discretionary spending. As a result the company revised lower its (ambitious) long-term guidance targets, which put a dent in investor trust and confidence in the management team. These stumbles coincided with a fairly broad based selloff across the payments sector as a whole, which ultimately led to a compression in PayPals price-to-earnings ratio from a high of roughly 55x in July 2021 to 16x in June 2022. Investor expectations quickly moved from optimism to pessimism.

On a more positive note, Paypal continues to attract users and merchants to its two-sided platform, which forms the basis of its competitive advantage. The core indicators of the platform's health continue to move in the right direction and the company ended the March quarter with 429 million active users and 35 million active merchants, up 9% and 13% year-on-year respectively. This was despite an elevated level of user churn due to some reopening headwinds. Further, the company is now starting to roll over easier comparable periods and earnings expectations have reset to a much lower base. Management have acknowledged mistakes and have committed to focusing on engaging more with core users and converting them to use PayPal's digital wallet, which doubles average revenue per account and lowers churn by 25%.

Due to reasons mentioned, we did decrease our exposure to PayPal throughout the year. That said, we still believe the business can perform well from current levels as it continues to grow at a healthy pace and is now trading at a price that has much lower expectations baked-in.

Sansan performed well throughout the year from a fundamental perspective, growing revenue 26% for the financial year ending May 2022, which was an acceleration of five percentage points from a year earlier. However, in contrast, the performance of the stock price was disappointing, as the shares sold off in dramatic fashion in response to higher interest rates. The business has been slightly impacted by lingering issues brought on by the pandemic, as the exchange in business card activity has been taking slightly longer to recover than expected. But despite this challenging environment, it was pleasing to see the company retained more than 92% of its client base throughout the year, highlighting the resiliency of its business model.

Sansan also made considerable progress towards diversifying its revenue streams with new initiatives. The most notable development has been Bill One, the company's invoice receiving service, which increased annual recurring revenue and paid subscriber numbers by 485% and 257%, respectively. Bill One has approximately 41,000 companies on its network and will only continue to grow with the introduction of invoice issuing in July. In our view, the growth of the network will only serve to further increase future opportunities to layer on additional services. Overall, we remain patient long-term supporters of the business and are excited to see its transition towards a multi-product company.

Buenos-Aires based e-commerce leader MercadoLibre was another example of a business that delivered impressive growth over the period (with revenue increasing by 60%-plus) only to have its share price underperform meaningfully. The stock price was negatively impacted by marketwide concerns around how sustainable e-commerce and digital payments growth would prove to be post-pandemic along with a very strong US dollar, which in general provides a headwind for emerging market equities. The company's EV/Revenue multiple dropped from roughly 10x in July 2020 to 3x today, which surprisingly, is the lowest it has traded since the 2008 Global Financial Crisis despite the company's consistent success and increased scale.

Business-wise, we saw strong performance across the board. The marketplace business continues to perform well, driven by an ever-improving customer value proposition, which in turn increases the loyalty of existing customers. It was pleasing to see that despite the reopening of economies in the LATAM region, buyer engagement remained sticky, with items per buyer reaching an all-time high in the most recent

March quarter. The company's investments in shipping and delivery are also bearing fruit and management noted that they are now able to deliver 79% of all volumes within 48 hours. All in all, we remain supportive and impressed with the company's execution to date and continue to see significant opportunities ahead given the relatively nascent penetration of e-commerce and the size of the underbanked population in Latin America.

Looking Ahead

Thank you to all our investors for your time and trust through what has been a truly challenging year. We remain committed to our growth-focused investment philosophy, and focused on consistently executing on our process, despite the humbling reminder the market has delivered this year.

We are extremely grateful for our investors' support and continue to reinvest in our own business to honour that trust. The team has grown from two to twelve over the past five years as we bolstered our capabilities in investing, operations, client services, and distribution. During FY22, Lakehouse upgraded to top tier partners across its operations, including:

- Responsible entity: ASX-listed Equity Trustees,
- Fund accounting, administration and registry: Apex (formerly Mainstream),
- Custody: Apex (formerly Mainstream), with JP Morgan as sub-custodian,
- Fund auditor: EY

A further development that we look forward to sharing the details of is that Lakehouse is in the final stages of appointing its first non-executive director: an industry veteran who brings great insights and perspective for Lakehouse and our clients. We look forward to sharing further details in the coming weeks.

Again, on behalf of everyone at Team Lakehouse, thank you. We look forward to a prosperous new financial year and hope you can make the upcoming webinar on 5 August 2022.

Best Regards,

Lakehouse Capital

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