Q1 2022

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GREYSTONE CAPITAL MANAGEMENT

Interview Two

ADAM WILK

Adam Wilk is the Founder and Portfolio Manager of Greystone Capital Management, LLC. He began his career in professional sports, working for various NBA teams including the San Antonio Spurs and Houston Rockets as a basketball analyst, scout and operations coordinator.

Adam's introduction to value investing came in 2012 where he translated his talent evaluation skills and analytical ability into evaluating real estate and then businesses which led to discovering finance, most notably through the writings of Warren Buffett.

Adam graduated from High Point University with a degree in Sports Management and today serves as the sole Portfolio Manager for Greystone's concentrated, small/micro-cap long-only strategy.

Could you give our readers a bit of background on Greystone Capital?

Greystone Capital is a long-only equity focused Registered Investment Advisor with a concentrated value-based strategy and a focus on smallcap and microcap companies. I am the Founder and sole Portfolio Manager as Greystone is an investment 'team' of one which I remain committed to maintaining moving forward. The firm's inception was only a couple of years ago, so we are young but scaling and bringing on the perfect investors for the strategy I'm employing. I would say the first iteration of Greystone was cobbled together around 2016, mainly for family and friends to invest. Following the distribution of letters and investment research, I experienced significant interest from outside investors which led to the need to develop a more formalized structure in order to accept new investors.

The period prior to family and friends investing consisted of a stop in commercial banking and before that a number of years spent working in professional sports as a basketball analyst, scout and operations coordinator for both the San Antonio Spurs and Houston Rockets. While working in San Antonio, I gained tremendous exposure to various levels of organizational development as well as talent evaluation, contract negotiation, risk management and data analysis. I didn't know it at the time, but those skills would translate incredibly well to finance and investing, but most importantly, the founding principles of Greystone Capital were formed back then which include patience, curiosity, the constant pursuit of incremental improvement and a focus on 'pounding the rock', a motto or phrase I shamelessly stole from the Spurs organization.

My introduction to value investing took place about a decade ago following my time in sports, where I discovered finance and investing almost by accident after being introduced to a couple of books on the subject and most notably through the writings of Warren Buffett. After being 'bitten by the bug', I spent the next 4-5 years acting like a sponge, absorbing everything I could get my hands on related to investing and spending my lunch hours, nights and weekends reading books, teaching myself accounting, studying business models, reading writeups and perusing SEC filings. Eventually I was spending much more time thinking about stocks and investing than I was doing anything else, specifically my 9-5 job. This led me down a path that ended in a career pivot, where I developed the confidence to start doing my own business analysis and sharing research/writeups online (in addition to talking about stocks 24/7 with friends and family) leading to the start of managing friends and family money as mentioned.

Why do you believe your approach differs from that of other value-focused funds?

Given the length of time since inception, I would say I've definitely benefitted from luck and good timing, but the word structural comes to mind when thinking about some of the elements of Greystone that are different from other firms/funds. Before going out on my own, I attempted unsuccessfully to gain some formal experience with a firm or fund by trying to find an analyst role. I was a finalist candidate with more than one fund, but ultimately couldn't get my foot in the door. One major positive was that I met a lot of people during that experience. Also during the job search process, I came to learn a lot about the industry and had some very interesting conversations with wealth managers, financial advisors, asset managers and investors. Years of meeting people this way and collecting information allowed me to separate the firms/funds I thought were managing money in a way that would set them up for continued long term success, vs. those who weren't. There can be a lot to dislike about this industry, especially the mis-aligned incentives between investors, investment managers and companies, so I basically set out to create something I didn't dislike, and replicate the structures I thought would a. suit my personality and style best, and b. set myself up for long term success. This meant that Greystone had to be differentiated, and I believe we are in many ways. The firm is set up to place compounding client's capital as the highest priority, with a willingness to buck conventional diversification wisdom,

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concentrate on my best ideas, remain a small pool of capital as to preserve the elements of my strategy and keep nearly the entirety of my net worth invested into the firm. When people stumble upon the firm, it should be clear that I am not catering to the masses, I am not trying to develop a marketable investment 'product', and I am not interested in collecting assets for the sake of assets. I am partial to people who understand completely who they are, and I try to make it very clear who and what I am and what Greystone is about. As a result, I've typically said that Greystone will not be right for everyone but will be perfect for the right people.

That last point is key, as I am optimizing first and foremost for the right people/partners, who will drive all of the success that Greystone ends up having moving forward. Those with a long time horizon, ability to withstand some volatility, and patient capital are a great fit for us and are the types of people I hope to attract.

Our aim is to outperform the broad market or what an investor could achieve by owning a low-cost, diversified index. I would view beating the market over time as an output of following a solid investment process, so the best way to unpack how to achieve our goal would be to understand what the inputs are in developing a good process that could lead to continued outperformance. I spend most of my days managing client portfolios and our current positions as well as conducting investment research. These are the highest value add activities in investing, and given that I have limited meetings during the week, I keep phone calls to a minimum and I am an investment committee of one, I get to spend most of my time studying businesses, industries, getting to know management teams and reading all the time.

As a result of this, I can invest anywhere, move quickly if necessary and invest with conviction, which helps a lot from a portfolio management standpoint. This is important because client portfolios typically don't look anything like what's contained in various indices, leading to what should be differentiated investment results over time. We are not designed to track or look like the market and as a result end up investing in areas or specific opportunities that larger funds or firms can't own given their size or mandates. I view this not only as a competitive differentiator but also as a way to generate outperformance, as I can invest in a sub-$100mm market cap company that is executing tremendously well and potentially at an inflection point within their business but for a number of reasons isn't covered by analysts or the management team hasn't gotten out and told the story yet despite the attractiveness of the business. I'm not claiming to be the only person sifting through these investments but I'd view the odds as tilted in my favor when investing small and off the beaten path.

While some investors and allocators spend a lot of time focusing on 'edge' and where your specific advantage might be as an investor, I learned very early on that as a small, one man firm with a non-traditional background, I was never going to have the knowledge base or resources held by larger investment funds, but whenever I studied other investors or investment portfolios, or spoke with people throughout the industry about small companies, I always got the same responses which were 'this is not investable for us' or 'talk to me when the company hits a $1 billion market cap'. I understand why (a 5% position in a $1 billion dollar fund (small by investment management standards) is $50mm dollars. So realistically concentrated investors can't make smaller companies large positions without owning the majority of shares or creating liquidity problems for themselves, among other things. I found that to be a very powerful structural force, preventing very smart people from owning good companies with very strong risk/reward profiles just because of their size. As a result, I stumbled upon the idea that small pools of capital are capable of outperforming the market. So for me the question then became how can I sort of create this structural advantage for myself, and the answer was by starting to look at small companies, in addition to capping AUM at a certain level in order to allow myself to continue to be able to invest in these opportunities. So interestingly, by virtue of having too much money to manage, there is a large group of very smart, very capable people who just don't spend much time in the spaces that I do. That has definitely changed over the years, but the point I'm making is that there are just less eyeballs on some of these businesses which can open up the opportunity to find something trading for much less than it could be worth a few years down the road. Lastly, the access granted to me from most large cap management teams and IR departments pales in comparison to what I'd be able to uncover owning a smaller company. I enjoy and find it useful spending time with management teams, doing in-person company visits when necessary, and down the road, as I scale, being able to take larger positions in companies with strong prospects.

Can you explain your investment process? How do you find/establish intrinsic value?

Greystone was founded as a long-only concentrated investment firm, so I spend most of my time doing investment related research and analysis, with the aim of owning anywhere between 10-15 stocks at one time. As a result, I end up saying 'no' to most ideas, and 'no' to many more sectors, sub-sectors and industries. I'm looking for specific ideas whose share prices I believe have a reasonable chance of doubling within 3-5 years using conservative estimates and business assumptions. I spend all of my time in the microcap and smallcap spaces, with my sweet spot being companies between $100mm and $1.0 billion. I've touched on my preference for small companies in many other places, but I believe they provide opportunities for outperformance as they can often be mispriced for a variety of reasons. Building a portfolio of 10-15 stocks only means the bar for inclusion is very high and I have to make sure I'm doing deep fundamental research on the businesses we own. This allows me to go deep and develop conviction prior to making an investment, or while owning a particular business.

> ***This list is constantly being updated and monitored but outside of this, ideas can pop up anywhere. I read a ton of writeups, blogs, substacks, spend time on sites like Value Investors Club and Seeking Alpha, and talk to a lot of investors. This usually leads to interesting things to research. During times like these, the watchlist grows and certain candidates look better and better everyday.***

The process can be broken down simply as research, filter, monitor and then potentially purchase. I've developed a watch list of businesses over the years made up of companies I like, strong management teams, formerly owned businesses and companies representing themes I find attractive. This list is constantly being updated and monitored but outside of this, ideas can pop up anywhere. I read a ton of writeups, blogs, substacks, spend time on sites like Value Investors Club and Seeking Alpha, and talk to a lot of investors. This usually leads to interesting things to research. During times like these, the watchlist grows and certain candidates look better and better everyday.

From discovery to investment, the decision making process involves a few different steps including running a particular business through my intensive research framework. For a number of reasons, a new idea could present itself as attractive and actionable and worthy of further due diligence, at which point I will read the filings, learn about management, dig into the unit economics, read everything I can find about the industry, scour the internet for articles on the company and then put together a basic model or valuation framework. That part of the process provides me with enough information to get a sense of what might happen moving forward. The real work starts after this and involves determining 'reality' by speaking to everyone and anyone I can who has an expertise about the business or industry. Depending on what's required, I will speak to former employees, former managers, competitors, suppliers, vendors and investors in the space. At a high level, this allows me to do two things: one, determine if what I believe will happen is likely to happen, and two, figure out what I'm missing or how I could potentially lose money. Not many investment ideas make it this far in my process, and even fewer go from this to portfolio inclusion. As I mentioned, the bar is set very high, and even if I like everything I've discovered, valuation may not line up with my internal rate of return expectations. Assuming I've made an investment at the end of this process, the position is then monitored closely and I'm on a rampant search for disconfirming evidence as time goes on.

What are the core qualities you look for in a business before you buy, and are there any sectors you try to avoid outright?

In line with my commentary about the firm's strategy, I try to adopt the framework of 'best ideas only' when thinking about investments to include in client portfolios. As a result I have a high hurdle rate for new ideas and typically find myself saying no often when conducting investment research. Because I am the sole analyst and portfolio manager, I've learned to make efficient use of my time so filtering through ideas as quickly as possible is helpful in that regard. I have rigid investment criteria that I have to check for all potential investments, so its rare that the average company or average idea on any given day will be something that I'm interested in or something that makes it past my initial filters. Client portfolios typically hold two types of investments, core investments and special situations. The special situations segment of the portfolio is driven by corporate special situations such as management changes, significant insider buying, buyback announcements, tender or rights offerings, forced selling dynamics and many others, where usually catalysts are present. Core investments makeup our better businesses typically found within the top five holdings with an aim to hold for long periods of time. At a high level, core investments consist of good businesses capable of operating through tough economic periods as the leader in a product or service niche, with long runways for growth, favorable macro tailwinds, the opportunity for revenue growth and expanding margins, with owner operators at the helm. Significant downside protection needs to exist as well, and typically I avoid things like levered businesses, commodity related investments, highly regulated industries (banks, insurance, utilities) and binary type bets such as biotech. My favorite core investments hit on all of the criteria I just mentioned but also have limited analyst coverage, a small market cap and financials that don't paint the true picture of value creation.

I also place a tremendous amount of weight on management teams, as strong leadership and a favorable company culture are things I emphasize when looking at new investments, carried over from my time in professional sports. Owner operator led businesses are given preference almost all others. Although it can work against you in some situations, I like investing alongside managers with no fear of job security and the ability to adopt a long-term mindset in the pursuit of their own wealth creation. Given that I am a secondary investor and have no operational control, management has to be 'A+' for core positions, with boxes to check consisting of large equity ownership relative to their salary, industry experience, a strong history of capital allocation, skills as an operator, forward thinking mentality, shareholder friendly with open lines of communication. Management is a good place to start and stop when researching new investments, and in addition to certain industries I avoid, I will steer very clear of unproven operators, entrenched thinkers, mis-aligned managers and outrageous compensation packages.

Sometimes companies are cheap because they deserve to be. How do you screen for value traps in your ideas?

I'm of the opinion that the market is pretty darn smart, and quite efficient the majority of the time. There are plenty of people, systems, firms and funds with more knowledge, assets and resources than I will ever have, and to those market participants I say, I have no qualms with you nor do I wish to be competing on the basis of brainpower, resources or analytical ability. For example, I have no interest in going 'long' one of David Einhorn's shorts, or trying to out-analyze Bill Ackman on a particular stock. I'm looking for easy wins or even unfair fights.

The market participants I DO want to be competing against include those whose hands are tied behind their back during a fist fight, meaning there are structural reasons why they can't own what I own, whether that be size, investment mandates, factor elements, sector dislike or they just simply haven't done the digging. An example here would be that a quantitative based strategy is probably not all that interested in a company's culture or a management team as much as I am. If I can find a good business, trading at a bargain price, with a solid management team that knows how to create value (and is incentivized to do so) and I can clearly identify why the shares are trading at that bargain price, its possible I've found a situation worth owning.

I think your question is an interesting one especially around the topic of screening for value as the majority of investments in client portfolios with some exceptions wouldn't show up on any sort of quantitative screen, assuming one is looking for favorable fundamentals or ratios. This is intentional as businesses that are 'screenable' will most likely not be investable for Greystone or at least not hit on my investment criteria. Typically but not always, good companies with strong historical or trailing fundamentals, or cheap businesses that can be identified as cheap quantitatively have certain pieces of information embedded within them that might cause a mispricing to be more difficult to find among this group. I can run a screen for cheap businesses that would probably reveal less than stellar companies going through some real issues, or I can run a screen using backward looking metrics for the best performing businesses that may end up being too expensive or too large for us to purchase. The point is that finding good investment ideas capable of generating 15-25% returns over a number of years can't simply be done by screening for them. Because of our size, resources and differentiated portfolio construction, I also have to think differently about where ideas are going to come from and part of that process is studying intensely a variety of businesses and filtering for things that wouldn't show up on a screen at all. Examples of this could be a management change, restructuring of a compensation package in line with some new business target, quantitatively assessing a companies culture or competitive positioning, getting to know management on a deep level, finding a fast growing or attractive business segment (currently being given little credit) in addition to a company's core product or service line, or a turnaround type of situation where the trailing financials don't quite paint a picture of future value creation. These types of things can't or won't necessarily show up on a screen, as they are not predictable, mechanical or rules based, but they can be very powerful if recognized at the right time. I believe we hold a few of these types of investments today.

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Lastly, I typically view owning stocks as owning shares of businesses, and so the metrics I'm always most focused on in terms of whether a particular thesis is working revolve around the actual business performance, independent of the share price. Having said that, there are usually – not always – some indicators embedded in the price of a stock. For example, three businesses in the same industry trading at multiples of 5x earnings, 15x earnings and 30x earnings all have certain pieces of information or analyses incorporated into those valuations. The business trading at 30x earnings may drop to 25x earnings due to stock volatility and actually become a better value (depending on how the business is doing) versus the stock that drops from 5x earnings to 2x earnings, where the business may be falling apart and on its way to bankruptcy. The point is, while there is information within the price examples given, that tells you very little about what's taking place within the company.

Do you tend to concentrate on a select few ideas or manage a well-diversified portfolio?

Greystone bucks the conventional wisdom on a lot of things investing related with portfolio concentration being no exception. Given that really great investment ideas can be rare, and given the work required to gain a deep understanding about a business and develop the conviction necessary to hold through periods of turbulence, I want to make sure I'm concentrating on my best ideas and weighting them accordingly for maximum portfolio benefit. Our top five investments make up between 60-70% of client portfolios and I would imagine it will remain this way moving forward. Position sizing is the 'end all be all' in this business and I'm of the belief that our returns moving forward will most likely be generated by a select few investments that are well researched and sized appropriately.

With that said, I am always looking to place the odds in my favor as much as possible, and that level of concentration requires an extreme focus on the downside, with a complete understanding of how I might lose money in a particular investment. Our best case scenarios and highest weighted positions consist of businesses where it would be difficult to imagine a knowledgeable buyer coming along within a few years time, using conservative business assumptions, and not paying more than what we paid for our shares initially. Those are good situations in which to be concentrated because you know your downside is protected as long as the business keeps chugging along.

Could you provide an example of an investment that's worked well for you and provides a good example of your strategy in action?

Well because its fresh in my mind and somewhat still ongoing, we earned a strong short-term return in our recent investment in Houghton Mifflin Harcourt (HMHC). Disclosure, we are still long as we await the results of a recently conducted tender offer.

How did you first discover the business?

During COVID, I initially read a very well-done writeup on Value Investor's Club and then SumZero some time later, and passed on the opportunity. My high level thoughts were that the business was cyclical and it is a very tough business trying to sell education materials into schools, where many companies have had little success trying to do so (and made for bad investments as a result). But sometimes ideas tend to keep coming across my desk and following the stock reflected pretty strong performance from the COVID lows of around $2/share. But it wasn't until a friend and fellow investor passed along the idea and shared his publicly available analysis which helped highlight exactly what I was missing and laid out an incredible opportunity for significant returns.

What first attracted you to the company -- how does it fit into the strategy?

Houghton Mifflin is a leading education and learning technology company that primarily services both students and teachers throughout K-12 school districts in the areas of core curriculum, supplemental services and professional learning services. As mentioned, selling into schools is a difficult business, but it's a lot easier when, as HMHC, you've become an industry juggernaut, with your core curriculum products of math, science and reading penetrating over 90% of K-12 elementary schools and reaching 56 million students annually. HMHC's core business is incredibly strong, but the real investment 'juice' consisted of the massive additional opportunities for growth at very high incremental margins as the company

> ***Multi-year efforts from HMHC resulted in the development of a fast-growing digital business doing over $120mm in annual recurring revenue currently responsible for over 40% of TTM billings. HMHC nailed product-market-fit as digital sales are growing over 100% and sport 150% net retention numbers.***

scaled their newly developed digital segment and increased their penetration of annual education material spend.

Multi-year efforts from HMHC resulted in the development of a fast-growing digital business doing over $120mm in annual recurring revenue currently responsible for over 40% of TTM billings. HMHC nailed product-market-fit as digital sales are growing over 100% and sport 150% net retention numbers. The digital business comes with a much higher margin profile, so the continued mix shift toward digital learning products should have the effect of boosting the overall margins of the business as well as significantly increasing free cash flow generation. This aspect of the thesis was interesting because the company was being valued like a slow growth cyclical with limited cash generation ability, in line with my original opinion.

The most interesting aspect of the investment though was the emergence of significant industry tailwinds in the form of increased education spending by state and local districts, with a large boost being provided by 'catch up' spend earmarked for COVID related learning loss. This dynamic severely decreased the downside potential for us, and the incoming dollars – in the tens of billions – should also flow disproportionately in some cases to industry leading education businesses. This made HMHC a 'heads I win, tails I don't lose much' type of investment.

When did you first buy/at what valuation?

I purchased the bulk of our shares between $11-13/share, and added once again at $17/share following a leaked acquisition announcement rumor where it was noted that there was private equity interest in taking the company private.

What was the price target? How did the story play out?

I had a hard time disagreeing with some of the publicly available valuation ranges I saw, and eventually came to the conclusion that shares could be worth between $34-40/share during the next few years. This was based on HMHC's free cash flow profile looking a few years out bolstered by the acceleration of their digital segment and smart capital allocation. I woke up one day to a press release announcing that a private equity firm Veritas and the HMHC board had agreed to a tender offer valued at $2.8 billion or $21/share. I'm certainly not the first person to say this, and plenty of ink has been spilled opposing the deal price, but that valuation represents something like 7.5x my estimate of free cash flow looking out a few years. This is despite the business being at a significant inflection point, set to be massively more cash generative and optioned moving forward.
As mentioned the deal is currently being publicly opposed by a number of shareholders and fund managers, but to make a long story short, I believe the deal process was significantly flawed, rushed and not conducted to the benefit of shareholders.

It would also be interesting to know if there's has been an investment that originally ticked all the boxes but did not ultimately work out. What initially attracted you to the business? What was the valuation? What went wrong?

I've made my fair share of mistakes up to this point, which typically involve being wrong about my analysis of a specific business or industry along with misunderstanding the competitive dynamics of a particular company. In one particularly jarring case, I invested in an energy related business called Select Sands Corp., which served as a frac-sand supplier to oil and gas producers in the Permian basin. Without getting too into the weeds, the company served as the low-cost producer of frac sand with the highest quality deposits given their location in Arkansas and trucking / rail distance from some of the major basins in Texas.

Select Sands had a market cap of around $35mm at the time of my purchase and was largely undiscovered as are most companies with market caps of that size. There were no analysts, no fund manager shareholders and just a scrappy group of employees and managers working hard to seize the opportunity in front of them. The thesis was simple. The industry was utilizing a certain amount of frac sand to conduct drilling activity and given Select's quality rated sand and again, distance from the major basins, as long as they could mine sand they would have end customers to sell it to cost effectively. The company was pressing the gas in the area of sales and expanding their customer base (one customer made up 60% of sales when I initially got involved) and they also purchased a small rail operation to help further decrease shipping costs. During the few quarters I owned the business, the company was on track to generate somewhere around $9-12mm in EBITDA with some operating leverage on the horizon. I made the position way too large.

> ***Investing mistakes are the best teachers and I learned a lot of valuable lessons from that one investment. I haven't touched a commodity related business since.***

Well, of all the commodities in the world, frac-sand might be the easiest to replace, and to make a long story short, as E&P companies look to cut costs in every area possible, they realized that they were sitting on top of very similar (albeit lower quality) sand that worked just fine for their purposes. In addition, I invested in a cyclical business at an all-time low P/E, breaking a well known investment rule and setting myself up for failure as most frac sand producers were over-earning and ramping production capacity at the same time. These dynamics all played out simultaneously, and as the selling price per ton of frac sand plummeted, the company lost its largest contract with their end customer making up 60% of revenues and furloughed operations as it no longer made economic sense to mine sand at the current spot prices. Those combination of factors caused the stock to drop significantly at first and finished down 80% from my purchase price before I sold.

Investing mistakes are the best teachers and I learned a lot of valuable lessons from that one investment. I haven't touched a commodity related business since.

GREYSTONE CAPITAL MANAGEMENT

What does IDT Corp do?

The short answer to 'what does IDT Corp. do' is 'a lot of things', but recent history would reveal them to be a telecom business while also serving as a business incubator for adjacent products and service lines to be developed in-house, the value of which is then unlocked in shareholder friendly ways. I don't think the founding family of IDT, Howard Jonas and his family could have predicted what IDT would become today at inception, but the past decade has been one of strong execution, a flexible and entrepreneurial minded operating style, with plenty of shareholder value created as a result.

IDT Corporation is a telecommunications business and technology service provider to immigrant communities that has within the consolidated business a number of telecom, software and payment assets being developed outside of the core telecom business. IDT, through their Traditional Communications 'core' segment provides wholesale calling services, mobile 'top up' services as well as minutes termination services for customers across the globe. Traditional Communications is made up of three separate businesses consisting of BOSS Revolution calling services (prepaid calling cards and other prepaid services), Carrier Services wholesale calling (for global minutes termination), and Mobile Top Up (a global wireless minutes 'top up' service). Together, these businesses make up 92% of IDT revenue and generate 100% of EBITDA as of FY21.

Can you give a brief overview of the company's three main growth divisions?

IDT segments their financials into three categories, including Traditional Communications, 'Fintech', made up of National Retail Solutions (NRS) and BOSS Money Transfer services, and 'Net2Phone-UCaaS', IDT's unified communications as a service business. The three growth businesses exclude Traditional Communications, and include Net2Phone, NRS and BOSS Money Transfer.

BOSS Money Transfer is a carve out from IDT's BOSS Revolution calling brand whereby IDT is leveraging existing customer relationships and distribution by developing a money transfer business targeted to BOSS Revolution customers (a group of 3mm in the US alone), among others. BOSS Money Transfer is an international money remittance service designed to let customers send money to recipients in 37 countries, to 306,000 locations or digitally via the Boss Money app. Customers can make cash available for pickup, select home or digital delivery to a mobile wallet, or route a transaction to a bank account. During the past twelve months over 8 million transactions have been processed, with BOSS Money on track to report over $60mm in revenues for FY22.

Net2Phone is IDT's fast growing Unified Communications Services (UCaaS) business that was founded in the 1990s prior to advancements in cloud-based technology, then sold to AT&T and subsequently repurchased by IDT in 2006. Put simply, UCaaS services are modern, cloud-based business communication tools consisting of features such as cloud-based calling, in-office messaging, video conferencing and conference center outsourcing capabilities.

Anyone who has ever used modern office communication tools would understand the advantages and benefits over traditional office phone lines as UCaaS requires minimal to no hardware, less ongoing maintenance and provides more seamless communication. Net2Phone has been developing their own communication platform for five years and now sells their services through direct sales reps, master agent partners and a network of over 5,000 channel partners (reseller, service provider, vendor etc.). Net2Phone generated $42mm in revenues during FY21.

National Retail Solutions or 'NRS' is IDT's fast-growing point of sale and payments platform sold into the single operator convenience store, bodega and grocery markets. NRS followed the path of 'businesses being incubated within IDT' and was officially launched in 2016 by leveraging the 40,000+ retail relationships IDT has through selling their BOSS Revolution prepaid calling card products. Point of sale terminals (hardware) are sold to customers for a one-time payment upfront, while NRS also generates revenue through monthly software subscriptions, payment processing fees via NRS Pay and the sale of data and out of home advertising displays. NRS reported $25mm in revenues, up 105% during FY21.

> ***BOSS Money generates revenue on a fee per transaction basis, where transactions should continue to climb higher as BOSS explores new geographies, increases retailer penetration and as the BOSS Money app continues to take hold.***

How does the company's BOSS Money Transfer product differ from the competitor offerings?

IDT's third growth business is BOSS Revolution Money, a money transfer service that enables international remittances. The service was launched in 2013 to leverage the Boss Revolution brand, a highly recognizable label in immigrant communities used by 3 million people every month. BR Money allows users to remit cash to more than 300,000 payout locations in over 40 countries. Senders initiate transfers in person at a network of authorized agents (primarily convenience stores), through an iOS and Android mobile app, or online via the Boss Revolution website. In addition to the cash pickup method of delivery, senders can deposit money into a bank account, send money to a mobile wallet, or initiate a home delivery to the recipient. BR Money earns revenue through a flat per-transaction fee and a markup on the exchange rate.

BOSS Money generates revenue on a fee per transaction basis, where transactions should continue to climb higher as BOSS explores new geographies, increases retailer penetration and as the BOSS Money app continues to take hold. That last point is important as a large percentage of transactions currently take place through the app, which comes with lower customer acquisition costs due to the direct nature of transacting, high repeat customer rate at 80%, low churn and higher gross margins as retailer commissions are eliminated. The money remittance industry is massive and highly competitive with Boss Money a small player, but they serve a critical need for customers

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who rely on money remittance services to send funds to friends and relatives outside of the US. This, plus the growing market for digital remittance services should continue to provide a long runway for customer and transaction growth.

Efficient customer acquisition, the expansion of the payout network and the entrance into new geographies such as Canada and the UK have allowed BOSS Money to nearly double their transactions each year during the past four years. Transactions grew 18% year over year during Q1 2022 and excluding the impact of foreign exchange market conditions that positively affected revenue and transactions during the second half of fiscal 2020 and the first half of fiscal 2021, transactions would have increased 38% year over year. Today over 75% of BR Money remittances occur through the app, a very strong competitive advantage and customer retention tool that helps increase transaction amounts and reduce churn.

Another area of growth is the National Retail Solutions PoS system. Why do you think this product is capturing market share?

As mentioned, NRS launched by leveraging the 40,000+ retail relationships IDT has through selling their BOSS Revolution prepaid calling card products. This provided NRS with an enormous head start into the convenience store market, a small niche that is too fragmented, not big enough or profitable enough for enterprise focused point-of-sale businesses to care about. Developing a customized point-of-sale solution for its preexisting base of customers not only allowed IDT to make first-mover inroads into the immigrant, convenience store and bodega markets, but also allowed them to purpose-fit a specialized solution outside of the one-size-fits-all approach for other enterprise POS businesses. Today they have a very large installed base of over 16,000 terminals providing a very high value proposition to their merchant customers.

IDT has also made significant investments in sales reps and a bi-lingual call center that have begun to pay off as evidenced by their recent terminal and revenue growth rates. This follows the triple digit growth trajectory NRS has seen since publicly disclosing segment details in 2018. For NRS, the sales process is less intensive than it would be for competitors due to the built-in relationships as well as the bilingual requirements for NRS salespeople to penetrate these markets. Typically, NRS would be replacing a legacy cash register as opposed to another POS system, both because many store owners were made up of immigrant families less familiar with modern POS technology and because this market remains underpenetrated given the one-size fits all nature of larger enterprise POS businesses and lack of specialized sales forces. IDT estimates the TAM for NRS is a large percentage of the 200,000 single operator convenience stores and bodegas throughout the industry, providing a significant runway for growth. Importantly, during COVID, NRS rolled out self-install capabilities for merchants, no longer requiring the physical presence of a sales or tech person which should have the effect of further accelerating growth.

Which business are you most excited about and why?

Looking forward, I'm incredibly optimistic about the growth runway and opportunity set in front of NRS. Given the factors mentioned above, NRS has a somewhat unconstrained growth opportunity to continue to expand their terminal count, merchant customer count and data and advertising revenues.

While there are certainly larger and better capitalized competitors, especially on the enterprise side, IDT is content to let peers fight it out for multi-location convenience stores, restaurants and gas stations as NRS continues to attack its niche. Most importantly, there remain zero competitors with the data and advertising opportunity which cannot be overstated. NRS collects incredibly valuable scan data on each transaction, providing a look at consumer behavior in typically under-served markets and geographies. NRS merchant customers could provide CPG companies with purchase behavior information on key convenience store categories such as alcohol, tobacco, beverages and snacks. Multiple industry operators have confirmed that basic transaction data (such as tobacco / beverage purchases) can be sold for amounts up to $1,000/month. NRS monthly recurring revenue per terminal is currently $196. In addition, NRS can package, slice and dice the data to provide it in a customized way to CPG and tobacco companies meaning they could potentially sign multiple deals per terminal moving forward. The opportunity can be illustrated as such: if NRS entered into 5 data deals at just $65/month, they would earn $325 monthly recurring revenue from JUST data alone, compared to TOTAL MRR of $196 right now. Removing any conjecture are the deals NRS currently has with both Swisher and Turning Point Brands for tobacco purchase data. In my opinion, there is a $400-500 MRR per terminal opportunity for NRS moving forward that is currently in the very early stages. In this case, the economics would accrue to NRS very quickly and very lucratively. The current installed base of terminals is 15,100. At 25,000 terminals within a few years doing potentially $5,000 ARR per terminal gets NRS to $125 million in recurring revenue. At a conservative 10x revenue, IDT's

> ***Looking forward, I'm incredibly optimistic about the growth runway and opportunity set in front of NRS. Given the factors mentioned above, NRS has a somewhat unconstrained growth opportunity to continue to expand their terminal count, merchant customer count and data and advertising revenues.***

83.5% ownership in NRS would be worth over $1.0 billion, or $38/share compared to an enterprise value of $776mm for ALL of IDT today. Notably, 25k terminals would only represent a small fraction of the total addressable market.

Although it would be disingenuous to project revenue growth at triple digit rates moving forward, I estimate that NRS could finish 2026 with revenue in the range of $160-190mm, the higher end of which would represent just 35% growth from today. As data and advertising sales become a higher percentage of revenue per terminal – nearly 100% cash margin – I estimate NRS could post somewhere between 30-35% operating margins. A business growing in excess of 30% with recurring revenue, low churn, limited competition and a continued long growth runway with those unit economics should be worth at least 20x EBIT. At the low point of that revenue and margin range and utilizing a 20x multiple, NRS would be worth $960mm or $35/per IDT share.

I believe if NRS can accomplish even a fraction of what I am projecting for NRS, it should result in significant returns from today. Furthermore, NRS will shine as a standalone business following a potential spin or IPO, where growth will sustain and NRS should emerge as the convenience store point-of-sale market leader.

IDT's management has a strong track record of creating value. Can you give a brief overview of their past deals?

IDT was originally founded by Howard Jonas in 1990 as a provider of international calling termination services. After a number of completed deals to grow the company and new business services emerged, IDT shifted their focus to investing in and launching new product and service lines that they retain 100% ownership of, and then realize value through some sort of value-unlocking transaction. Since Shmuel Jonas joined the business, IDT has spun off five businesses since 2009. These businesses include IDW Media Holdings, a comic book and graphic novel publishing and media company, spun out in 2009, Genie Energy, a utility provider of electricity and natural gas services to residential and commercial customers, spun out in 2011, Straight Path Communications, an owner of wireless spectrum licenses, spun out in 2013, Zedge, a content platform for mobile device personalization, spun out in 2016 and Rafael Holdings, an owner of real estate assets and a stake in a development-stage pharmaceutical company, Rafael Pharma, which was spun out in 2018.

The historical playbook for IDT has been one of idea implementation, followed by execution and incubation, and ends with value unlocks via tax free spinoffs or dividends. Since 2012 when the company's spinoff strategy was enacted, IDT has parted ways with five businesses valued at nearly $3 billion and has collectively distributed over $200mm in dividends. This track record of value creation has resulted in every $1 invested in IDT in 2012 to be worth over $45 today.

These businesses differ in many ways and outside of Genie Energy and Rafael Holdings, the one energy and biotech related spins, the development, incubation and spinoff of IDTs businesses have typically emanated from an already established business line, product or service. IDT has don't a masterful job of catering to their core customers within each subsidiary, grooming those relationships and then using the value props provided by some of the core services to cross sell or develop new revenue streams that have turned into significant businesses over time. Examples of their recent spinoff activities include Straightpath Communications, a wireless technology business, IDW Media, a comic book and media company, Zedge Inc. a mobile phone ringtone business, and Genie Energy and Rafael Holdings.

Why do you think these managers will be able to repeat their past successes?

There are a number of reasons why past successes are repeatable. First, I believe the 'torch' has officially been passed with the implementation of Howard Jonas son, Shmuel a 1% owner as CEO of IDT. Shmuel joined the company in 2008 and was appointed to the COO role in 2010 before becoming CEO in 2014. The father-son team has generated exceptional returns for shareholders, and I continue to have a high degree of confidence that this can continue for the foreseeable future. Despite Howard Jonas's track record of success which is undeniable, Howard has somewhat of a polarizing reputation – many either like or dislike him – and so one of the things I had to sort of validate prior to investing was his day-to-day involvement in the business. While Howard certainly passes along ideas, attends board meetings and has final say on big strategic decisions, his day-to-day involvement with the core business and growth subsidiaries has waned over time, now fully in the hands of Shmuel. This has opened up the avenue for more flexibility, new ideas and increased resources being dedicated to IDT's various subsidiaries. This is not to imply that Howard was a negative or holding anything back, but fresh blood is a positive in this case and I believe has turned the page on a new chapter for the business. In addition to the current version of IDT, there are also a number of new and emerging business lines that haven't yet been broken out given their early-stage nature that could find their way among the three growth businesses we see today. This speaks to the IDT culture and technologically forward employee set within the company.

Second, the people inside of the organization are a key competitive advantage. I would put the management teams at the head of each of IDT's business units up against any business operators I've come across. This group is passionate, hungry, knowledgeable and out to prove themselves, while maintaining discipline on costs and thoughtfully implementing their strategies. Furthermore, many of IDT employees have tenures greater than 10-15 years which can be attributed to the strong and decentralized employee led culture where calculated risks are allowed (and rewarded), entrepreneurial attitudes are adopted, and managers are given the leeway and freedom to take control of their business units to drive the best results. We've seen that in recent results and I would expect much more of the same moving forward.

The Jonas family has over 70% of the voting power of the stock. Does this concern you?

The short answer is that it does not concern me, but one certainly has to gain comfort with the fact that yes, the Jonas family controls over 70% of the voting power of IDT. It's no secret that IDT likes to keep company matters within the family and has some governance items that may make some investors raise their eyebrows. For example, Jonas family members manage and hold board seats in IDT as well as in past spinoffs including Shmuel Jonas, Michael Jonas (Howard's son and CEO of Zedge), Michael Stein (Howard's son-in-law and CEO of Genie Energy) and Joyce Mason (Howard's sister and General Counsel of IDT). I don't believe there is a way around this risk of limited shareholder control, as investors will be subject to Jonas family decisions at the corporate level moving forward. With that said, if the future is anything like the past, being subject to Howard and Shmuel's decisions has worked out tremendously well for shareholders over time.

In your opinion, what are the main opportunities for the company over the next few years?

The biggest opportunities today consist of focusing on the three growth businesses and carving out a path for the spinoffs of both Net2Phone and eventually NRS. Net2Phone has an enormous opportunity to help many of Latin America's small businesses transition from on-premise communication tools to the cloud, while NRS can continue to capture POS market share within the convenience store and bodega community. Boss Money will continue to expand their transaction locations as well as total transaction footprint, and Traditional Communications will need to focus on bottom line growth moving forward. Outside of that, I believe the emergence of Mobile Top Up, the minutes top up service within Traditional Communications will be the next priority for IDT. MTU now generates 35% of IDT's total revenues and has been growing in excess of 20% throughout the past few years. An important point to note is that Mobile Top Up sells their services through both retail partners and direct to consumer. The retail channel is very low margin given payments to suppliers while direct to consumer sports about 3x the margins given less reliance on mobile carrier partners, thus lower fees and commissions. COVID drastically increased MTU's shift to direct to consumer sales, which if persists will have the result of significantly transforming the entire margin profile of Traditional, resulting in significantly higher cash flow generation.

> ***The biggest opportunities today consist of focusing on the three growth businesses and carving out a path for the spinoffs of both Net2Phone and eventually NRS. Net2Phone has an enormous opportunity to help many of Latin America's small businesses transition from on-premise communication tools to the cloud, while NRS can continue to capture POS market share within the convenience store and bodega community.***

While unit economics for MTU are not yet broken out, my work indicates that as the percentage of direct-to-consumer sales continues to grow over the next few years, MTU could generate a significantly higher portion of Traditional Communications revenues with a path to doubling gross and EBITDA margins from mid-single digits today to low double digits. This is a large opportunity for IDT and is not currently being factored into my valuation framework.

Let's talk valuation. How are you valuing the business? How much could the stock be worth in your best-case scenario?

When thinking about what IDT could potentially be worth looking a few years out, I've adopted a sum-of-the-parts valuation framework by estimating revenue growth rates and operating margins for their various growth businesses. Although sum-of-the-parts analyses aren't loved by investors as a way to value a business, IDT's subsidiary 'parts' are proven businesses executing tremendously well, not reliant on capital markets to grow with room for significant upside moving forward.

I'd estimate that Traditional Communications alone could be worth $20/per IDT share within a few years (or 5x EBITDA), netting investors (at the mid-point) cash and investments plus the remaining three growth businesses for less than $350mm. This would be in my view less than what a knowledgeable buyer would pay for just ONE of the growth subsidiaries. Optionality here exists with the not-yet-broken-out Mobile Top Up business ('MTU'), a surprising growth story within Traditional Communications given the recent demand trends for mobile top up services across world.

I estimate BOSS Money transaction volume will grow at a low to mid-teens rate on their way to processing over 15mm in transactions by 2026 with transaction fees growing low double digits to around $6.75/transaction. I'd estimate in line with payment companies and digital payment peers that BOSS could earn 18-20% EBIT margins over time, generating (at the mid-point) $19mm in EBIT on slightly over $100mm in revenues over the next few years. Given BOSS's competitive positioning, expansion opportunities, digital transaction opportunity and growth, I believe a market multiple of operating income is warranted. At 15x EBIT, BOSS Money would be worth $285mm or $10/per IDT share. I believe this valuation may prove to be conservative at 2.8x revenues.

I estimate Net2Phone can reach over 600,000 seats by 2026, earning around $16/seat in monthly recurring revenue, down 11% from today. This would peg total revenue for Net2Phone at $115 million. At a projected 20% operating margin, slightly below at-maturity peer projections, Net2Phone could generate around $23mm in operating income. I don't believe applying a slightly above market multiple of 16x would be egregious given Net2Phone's geographic advantages, gross margins, industry leading growth rates and continued runway for expansion. In this scenario IDT's 86.4% ownership in Net2Phone would be worth $317mm or $12/per IDT share. I believe this is an incredibly conservative valuation as this scenario implies a valuation of 3.2x revenues when peers in the space have regularly traded for a median of 6.6x revenues with slower growing mature businesses on the lower end and faster growing ones sporting high teens to low 20's multiples.

Although it would be disingenuous to project revenue growth at triple digit rates moving forward, I estimate that NRS could finish 2026 with revenue in the range of $160-190mm, the higher end of which would represent just 35% growth from today. As data and advertising sales become a higher percentage of revenue per terminal – nearly 100% cash margin – I estimate NRS could post somewhere between 30-35% operating margins. A business growing in excess of 30% with recurring revenue, low churn, limited competition and a continued long growth runway with those unit economics should be worth at least 20x EBIT. At the low point of that revenue and margin range and utilizing a 20x multiple, NRS would be worth $960mm or $35/per IDT share. I believe these assumptions will prove to be incredibly conservative especially as the data opportunity takes hold. I think NRS best in class gross margins, highest ARPU and revenue CAGRs among peers and location value with limited competition should allow them to trade at a premium to comps (although there aren't great comps).

With an enterprise value of $776mm today, investors are paying 8.6x Traditional Communications EBITDA for ALL of IDT and paying little to nothing for the three growth businesses set to generate over $200mm in recurring revenue by 2023, with spin-offs on the horizon.

With an enterprise value of $776mm today, investors are paying 8.6x Traditional Communications EBITDA for ALL of IDT and paying little to nothing for the three growth businesses set to generate over $200mm in recurring revenue by 2023, with spin-offs on the horizon. Notably, shares traded above this price as recently as November following two phenomenal quarters, only to decline significantly due to the market wide selloff that hit small caps especially hard.

Adding up the 2026 valuations outlined here would yield a share price of $75/share or greater than 100% upside from today's price. Keep in mind this valuation excludes a breakout of Mobile Top Up, as well as reduces cash and investments to $20mm, setting aside $125mm for potential damages relating to IDT's ongoing lawsuit with Straight Path Communications.

What is the worst-case scenario for the company and how could this impact your valuation?

Currently, IDT is facing an outstanding lawsuit relating to the Straight Path Communications spinoff, with a trial start date set for May 1st. This is a multi-year affair that has dragged on to the looming trial date, and now has the potential to settle prior to the start of the litigation. There is a non-zero chance that IDT winds up in trial, loses, and has to pay a legal settlement in excess of their current cash balance. While I would encourage everyone to do their own due diligence surrounding the suit, from everything I've learned there is an incredibly low probability of that happening. There is a lot of nuance surrounding the case, but I don't believe IDT is facing a material risk of loss outside of some kind of legal settlement to put the action behind them. Were something negative to take place, this would impact the market's view of IDT, as well as potentially cause the need to find some external financing to pay any large settlement.

Are there any markers you will be looking for over the next few quarters/ years that will signify the company is on track?

As I sit here today, IDT's stock has almost halved from early November. This is despite incredible execution and the overall improvement of the business in every aspect. So I believe things are very much on track despite what the ‘scoreboard’ is reflecting. IDT’s core Traditional Communications business, typically considered a ‘melting ice cube’ has actually returned to growing, and each of the three growth businesses continue posting record results and strong operating performance quarter after quarter. The future is bright, but so is the present. I also think the near-term and future catalysts will be good signs of IDT’s strategy playing out. The company set a date for their spinoff of their UCaaS business, Net2phone for July 31st, and National Retail Solutions will likely follow suit within 18-24 months. I think those are good benchmarks for how things are going, and I would anticipate decent valuations for both spinoffs, as well as strong operating performance from both as standalone companies. I’m very much looking forward to owning IDT through the spins and monitoring how the businesses perform.

GREYSTONE CAPITAL MANAGEMENT

Basic-Fit is the largest fitness operator in Europe. Can you provide a brief overview of the firm's operations and how it makes money?

Basic Fit is the largest low-cost fitness operator in Europe with over 1,100 gyms throughout a number of markets including the Netherlands, Belgium, Luxembourg, France, and Spain. Basic Fit operates across the value segment of the fitness industry, building big box gyms with equipment and room for classes, but leaving out higher cost elements such as pools, advanced locker room facilities and things like rock climbing walls. Today Basic Fit boasts over 2.2 million members is over 2x the size of the #2 player in Europe. What's more is that Basic Fit has an extremely long growth runway moving forward with the aim of opening over 3,000 clubs by 2030, feeding into the increasing gym member penetration throughout Europe which lags the US by a significant amount. Basic Fit's offering is simple: a typical subscription costs €19.99 euros per month and gives people access to all of their clubs plus all the benefits of mobile content via the Basic-Fit App. Members can also pay for things such as personal training and group training classes. The company was founded by former tennis pro Rene Moos, currently the largest shareholder, who opened his first fitness club called HealthCity in 1984, and eventually acquired the initial Basic-Fit clubs in 2010. Since then, Rene has expanded the club portfolio to six countries and as mentioned over 1,000 clubs while tripling revenues and underlying club EBITDA from 2014 leading up to the pandemic.

> ***Basic Fit's cost structure provides a massive advantage relative to independent operators, as I estimate the cost to operate a big box gym (1,500 sq. ft) at a fully ramped member count is nearly 20% lower than an independent operators in the same size or smaller gym. This allows Basic Fit to breakeven at a much lower membership price or revenue per member compared to an independent operator, by about 65%.***

This is a competitive market. How does the company stand out from the competition?

I've become very familiar with the gym business and various business models over the years as both an avid customer, enthusiast and someone who has worked part time in the industry over a period of years. The gym business certainly wouldn't stand out to investors as one with inherent competitive advantages as there is plenty of competition, low barriers to entry and some seasonality. However, scale offers many benefits to the largest players, and similar to the 'value' model winning out in various industries such as retail, value is winning in low cost fitness as well. For Basic Fit, the low cost model and high value prop are attractive to continue growing the membership base above and beyond competing gym chains. The business model is simple to understand – grow the membership base above your fixed costs and incremental membership dues drop to the bottom line – and in the case of Basic Fit their presence in Europe confers some advantages and barriers which help keep competition at bay. When constructing a gym, high fixed costs come before members, making it difficult for many smaller operators to either test new markets or offer low pricing in Basic Fit's markets given the lack of revenues to support multiple players. Basic Fit possesses the scale over which to spread marketing and employee costs, cleaning services, equipment purchasing (in addition to being able to afford rent in the best locations) and technology. As a result, Basic-Fit can offer memberships at the lowest prices making them, you guessed it, the low-cost provider. Therefore, what initially looks like a commodity (low-cost gym membership) actually becomes a competitive differentiator.

Furthermore, Basic Fit's cost structure provides a massive advantage relative to independent operators, as I estimate the cost to operate a big box gym (1,500 sq. ft) at a fully ramped member count is nearly 20% lower than an independent operators in the same size or smaller gym. This allows Basic Fit to breakeven at a much lower membership price or revenue per member compared to an independent operator, by about 65%. This doesn't take into account the size, technology, cleanliness and convenience advantages Basic Fit possesses, making it the superior choice for new gym goers, squeezing out mom and pop operators in select markets.

In line with the cost structure comments, Basic Fit also realizes major equipment purchasing advantages as the largest purchaser of gym equipment in Europe. I'd estimate their costs to be between 30-40% lower than an independent operator, allowing them to save on purchases as well as share these savings with customers in the form of better equipment selection as well as best in class pricing. This is an advantage that simply can't be replicated without scale.

As Basic Fit grows their total gym base and captures an increasing share of member penetration due to their high value prop, pricing and convenience, regional locations will begin to 'cluster' in line with their real estate and expansion strategy, leading to more convenience for members, higher engagement and lower churn. Members will continue to benefit from a larger gym base at no incremental costs, while Basic Fit will continue to achieve member density, eroding competition further as time goes on.

Over the past two years, gyms in Europe have faced long periods of closure. How has the business performed in the pandemic?

As you would imagine, Basic Fit did not thrive during the pandemic, as the gym business is typically one with high fixed costs that don't disappear even when your revenues drop to zero. During this period, new club openings were put on hold, the company was granted some rent concessions and they did their best to reduce any fringe costs while shut down. Competitors, especially mom-and-pops were hit especially hard during the pandemic, as its estimated by industry insiders that nearly 20% of all gyms have either gone out of business or will be out of business following the pandemic. While revenues, margins and profitability all took a huge hit during the shutdowns, size and access to capital provided advantages to businesses like Basic Fit. The company was able to issues some equity as well as raise convertible debt during this time and was very quick to adopt the customer friendly approach of taking the very significant (but short term) hit of refusing to charge membership fees during periods of lockdowns. Basic Fit also provided digital fitness offerings via their app in the form of in-home workout videos and classes. This goodwill engendered during that

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time led to tremendous customer satisfaction, reduced churn and explosive membership growth since their gyms began to re-open.

Although some would argue that the pandemic shifted consumer behavior leading to a permanently lowered capacity for gym goers, there is little evidence to support members not returning to physical gyms. As mentioned, following re-opening periods in Basic Fit's markets, membership and revenue growth has been incredibly strong indicating that keeping members engaged during the pandemic paid off as customer loyalty and the strength of Basic-Fit's offering is revealing itself. In addition, more severe lockdown restrictions for Europeans during the pandemic as well as less household space for in home fitness equipment indicates at the very least that gyms are not going away, and the quality, low-cost offering should have a place even with the most budget conscious households.

The firm has ambitious growth plans. How is it looking to expand over the next few years? Do you agree with this strategy?

As mentioned previously, the business model and strategy are simple and easy to understand. Basic Fit's strategy is to expand in both existing markets and new markets moving forward, with a goal to build around 200 or so new locations per year. As long as they can continue to open new locations with the same maturity, cash generation profiles and returns on invested capital that they've seen historically, the investment should work out very well. The company's location count has grown at a nearly 25% CAGR since 2013, and I'm projecting high teens growth in unit count through 2026. This would bring the total number of locations to 2,000 by that time period. History would point to that goal being achievable, especially as COVID dramatically altered the competitive landscape where in some areas, only the strong survived.

I'd estimate there is a reasonable path to nearly tripling the total member count over the next 7-10 years and possibly more, given Basic Fit's strong position in France, a market with 7-8 million membership potential on its own. In addition, Basic Fit could nearly triple their total member count and still have only captured a relatively low penetration rate, meaning that if Basic Fit can capture even a remotely similar low cost member market share as Planet Fitness, membership numbers could skyrocket. Today, Basic Fit is focused much more on increasing the per gym membership count as opposed to raising pricing or membership rates.

It's been mentioned that Basic Fit is attempting to replicate the 'clustering' or 'fortressing' expansion strategy laid out by Dominos with the intent of improving their relationship and value prop to customers. The idea for Dominos was to build clusters of stores in one specific geographic area to both increase customer density and benefit from shared marketing costs, shorter delivery times and improved convenience. The European gym market is fragmented and gym goers don't necessarily need to workout at one specific gym location (although brand affinity can be strong), so the brand with the most locations in the most convenient spots – close to home, work etc. – has been winning the biggest share of new membership penetration. Basic Fit's real estate strategy is backed by data as well as plenty of experience, allowing them to find and project the best retail locations in the most attractive areas. As BFIT continues to expand, the value prop for members increases due to convenience at no additional cost, while Basic Fit accrues the advantages of increased engagement, lower churn and cluster density.

> ***Basic Fit's real estate strategy is backed by data as well as plenty of experience, allowing them to find and project the best retail locations in the most attractive areas. As BFIT continues to expand, the value prop for members increases due to convenience at no additional cost, while Basic Fit accrues the advantages of increased engagement, lower churn and cluster density.***

What is your view of management? Does management have skin in the game?

My experience with the management team thus far has been very good as they have been open, detailed and optimistic about the opportunity in front of them. I place an incredibly heavy weight on investing alongside quality management teams, and this area of my process involves doing a lot of work and getting very familiar with a particular group prior to investing. Basic Fit's management team scores highly on my internal score card of which the criteria consists of business, personal and psychological items some of which have been pulled from my time working in professional sports.

The founder and current CEO, Rene Moos is a former professional tennis player who entered into the coaching business following the end of his career by renting out empty gym space to give individual tennis lessons. To make a long story short, he took a look at the rent and prices certain gyms were charging for things like personal training and realized he was in the wrong business. Rene opened his first gym, HealthCity, in 1984, reaching over 200 locations during the 2000s. Seeing the writing on the wall about value based gym chains, Rene purchased his first low cost Basic Fit location in 2010 and partnered with a private equity firm to aggressively execute a growth strategy. Rene is an insider, owner and phenomenal operator who I believe is best fit to lead the company through their expansion plans. Management has also purchased a significant amount of shares in the open market over the past few years.

Compensation is fair relative to the company's fundamentals and industry peers, while management is also incentivized to continue growing the business and focusing on key metrics such as revenue growth, EBITDA growth, and ROIC as time goes on.

What sort of returns does the company earn on new premises and how does this translate into a company-wide ROIC?

Following what one would hope is the end of the pandemic and restrictions surrounding in-person facilities, Basic Fit is back in growth mode following what was the most difficult two years in the company's history. As mentioned, the CAGR for new unit growth since 2013 up to the pandemic was just under 25% per year, aided by the very favorable returns Basic Fit is earning on their invested capital.

Assuming Basic Fit is retro-fitting an already existing gym location, the total investment to renovate amounts to €1.2 million euros. Revenue at maturity of 3,300 members should come in around €825-850k euros, with typical 4-wall EBIT margins of 50%. At the mid-point of that revenue range, EBIT would be around €418k euros, making returns on capital 35%. Keep in mind this is on the lower end of a fully ramped club's membership base, where returns improve significantly at 3,600 members. Higher end returns on invested capital can exceed 40%, reflecting Basic Fit's profitability at the unit level.

Does the firm rely on finance or profits for reinvestment?

So one of my favorite investment setups consists of businesses undertaking significant growth investments that paint the picture of negative current profitability or cash flows but have the effect of increasing long term shareholder value. An attractive aspect of high return growth investments is that they can open up avenues for mispricings because at the business level there is no optical cheapness, should one be focused on paying a low multiple of earnings or free cash flow. This focus on the 'now' can at times cause investors to miss the potential long-term effects of value creation. In the case of Basic Fit, given the returns on capital they are earning by opening new gyms (thus causing headline free cash flow to be negative), they should be continuing to do exactly that especially when those growth investments boost market share, increase scale efficiencies and increase operating leverage.

Basic Fit's 'headline' free cash flow is negative taking into account growth investments, and they have some debt on their balance sheet. At the end of 2021 BFIT's debt/EBITDA was 2.1x so clearly a manageable number. Basic Fit does utilize leverage as they grow, but are free cash flow positive by taking EBITDA and subtracting out maintenance capex. Following the release of their FY21 results, Basic Fit reiterated FY22 guidance and suggested

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that €240mm in EBITDA is possible. Netting out maintenance capex of around €55mm which is the average figure provided by management, free cash flow could come in around €185mm for 2022.

Looking out a few years, cash flow generation has the potential to explode as fully ramped clubs will generate ample cash from operations and strong cash conversion. Basic Fit receives membership payments upfront and delayed payable terms related to equipment purchases. As clubs continue to re-open and new clubs are built out, the company has guided to being able to internally fund the business model from 2023 onwards.

The positive here is that businesses such as Basic Fit's with customer captivity, a low-cost model, more efficient operating processes, and dominant market share leaders can use growth investments to keep competition at bay and continue to create value over time at the expense of current negative free cash flow.

What's your valuation target in the best-case scenario?

I tend to avoid specific price targets or valuation scenarios given the unpredictability of the future, but there is a sort of range we can look to when thinking about what Basic Fit might look like with 2,000 locations fully ramped and mature. At the low end, mature clubs sport around 3,300 members and with an unchanged average membership price of €21.5 euros/month, each gym location would generate around €850k in revenues, and fully ramped EBITDA of around €385k. Multiply that by the 2,000 location count and subtract G&A, I have Basic Fit being able to earn around €620mm in EBITDA within a few years. At a 60% FCF conversion rate, BFIT would be able to generate around €375mm in free cash flow. A 15x multiple on that figure would result in a share price 100% higher than today's price of €40/share. I am likely being very conservative in a number of areas here, as operating leverage should kick in with a larger club base (leading to lower costs, higher EBITDA and higher FCF conversion), and the high-end membership count of fully ramped clubs is 3,600 instead of my proposed 3,300. If we adjust the numbers for that blue-sky scenario, Basic Fit could generate €500mm in free cash flow on the same club base of 2,000. Using the same 15x multiple for conservatism, shares would be worth over €110/share.

What's your worst-case risk target if the firm's growth does not live up to expectations?

I've probably spent enough time talking about the competitive dynamics and cash flow generation potential of the business, so I will keep it simple answering this question by saying that today Basic Fit trades at the lowest multiple among their publicly traded peer group despite having the fastest unit growth rate, longest runway for growth and in my view strongest competitive position. If Basic Fit can execute their store buildout to anywhere close to 2,000 units over the next few years, they should be able to generate substantial free cash flow in the range of €6-8/share, or 5x today's price. We can argue about what sort of multiple the company might deserve given the quantitative and qualitative aspects already discussed, but I am confident its higher than 5x free cash flow.

What are the main growth risk factors here?

I would usually lead with execution risk surrounding attacking new markets and geographies as well as increasing member penetration, but given all that's been discussed so far, I believe Basic Fit has such a simple and well-run playbook that they should be able to continue along their growth trajectory into the foreseeable future.

> ***Management doing something stupid is always at the top of my list in terms of reasons why I might sell something we own immediately. If management decided they wanted to get into the hardware manufacturing business similar to Peloton for example, that would be a negative in my eyes.***

Risks along the lines of execution would be an inability to expand at a fast enough pace, the inability to effectively enter into new markets, clubs fail to reach membership maturity, and inflation elevates things like construction and utility costs for new gyms.

Having said that, Basic Fit has one of the most streamlined, efficient and cost effective real estate and construction processes I've seen, and meeting their growth targets moving forward is just about continuing to execute the same playbook they've been executing during the past almost decade. Certainly another shut-down of any kind would severely affect them and there is no shortage of geopolitical instability these days (albeit in different markets) but I'm confident the strategy can be executed moving forward.

Are there any potential developments that could cause you to sell your holdings?

Management doing something stupid is always at the top of my list in terms of reasons why I might sell something we own immediately. If management decided they wanted to get into the hardware manufacturing business similar to Peloton for example, that would be a negative in my eyes. Outside of something like that, I will be very diligent in monitoring future returns on invested capital for new store investments. Basic-Fit has internal targets in the range of 35-42% so should those start to deteriorate in a meaningful way, it might indicate their competitive advantages were eroding, membership growth won't live up to expectations, and gym penetration rates have hit their ceiling, among other things. If Basic Fit has less success opening new gyms in new markets, fundamentals might start to deteriorate also. The good news is that Basic Fit has one of the strongest competitive positions throughout any industry I've seen which make them an incredibly difficult competitor to displace. Management is smart, experienced and disciplined (along with being a large owner of the business), making it less likely they would engage in value destructive activities.

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