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Best Ideas 2018

Joe Magyer

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Data in this presentation is current as of 19 December 2017.

Lakehouse Capital: About Us

Fast Facts

- Formed in 2016
- ≈ A\$200 in FUM
- Based in Sydney, AU

Style

- Long-Term
- Low Turnover
- High Conviction
- High Active Share

Security Selection

- Strong positions in growing markets
- Pricing power
- Durable competitive advantages
- Aligned and experienced management
- Conservative balance sheets
- Attractive valuations

Lakehouse Capital: Funds

Lakehouse Small Companies Fund

- Launched November 2016
- ≈ A\$134 million in assets
- Focused on small-caps in Australia and New Zealand
- Closed to new investors as of year-end.

Lakehouse Global Growth Fund

- Launched November 2017
- ≈ A\$66 million in assets
- Focused on mid- and large-caps in developed markets



Afterpay Touch Group

Fast Facts

- ASX:APT
- Formed: June 2017
- HQ: Melbourne, Australia

Market Data

- Recent Price: \$5.56
- Market Capitalization: \$1.2B
- ADTV: ≈\$5M

All currency references in Australian dollars (AUD).

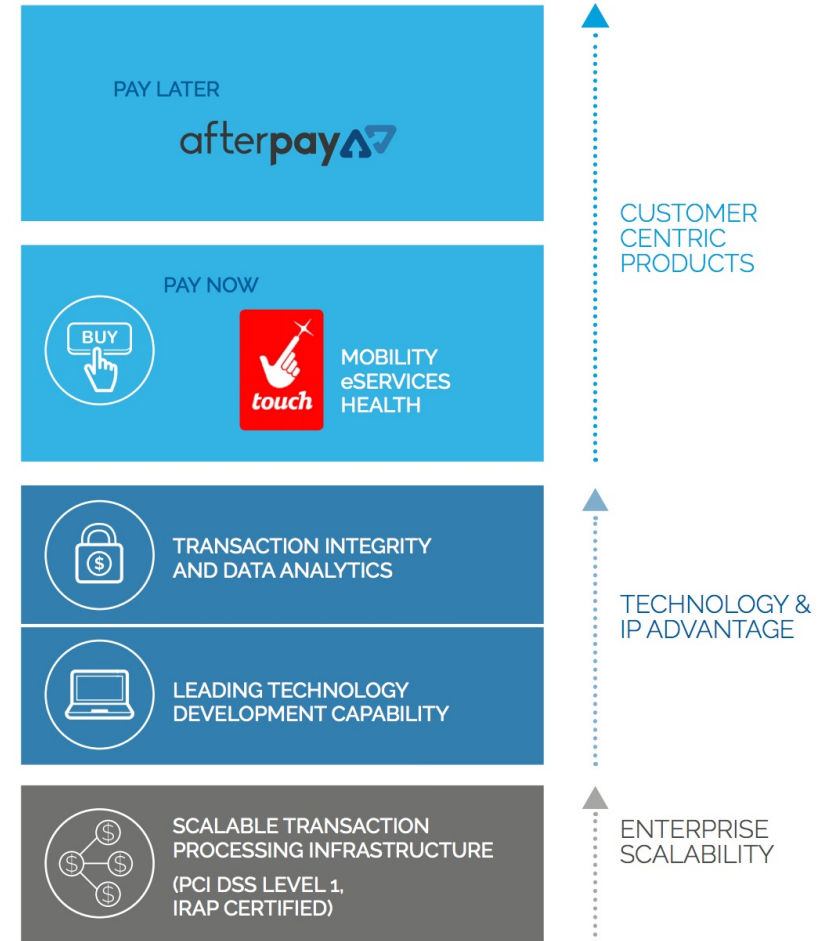
Afterpay Touch

Afterpay: Pay Later

- Consumer payment platform
- Take home now, pay in 4 interest-free installments
- Allows 1.3M+ users to buy now and pay later at 10,000+ merchants across AU and NZ

Touch: Pay Now

- Payment processor
- Underpins Afterpay



The Big Idea

Significant Growth

- 0 to 1M+ Afterpay users in just 3 years

Strengthening Network Effect

- Rapid growth in users, merchants, and spend per user

Multiple Growth Levers

- Room to gain share of growing online category, go into more storefronts, and go abroad

Attractive Economics

- Low net transaction loss rates and high capital velocity

Recent History

Afterpay

- Founded: 2014
- IPO: May 2016
- Co-founded by Anthony Eisen and Nick Molnar
- Seeded and supported by Touchcorp
- Series of expectations-beating results

Afterpay & Touchcorp Merger in June 2017

- Strong strategic sense
 - CEO of Touchcorp had died suddenly
 - Touchcorp owned 27% of Afterpay
 - Afterpay's business sat on top of Touchcorp's platform

Afterpay: How it Works

DAVID JONES

Gift Registry | Wish List | Contact us | Search David Jones online

Sign In or Create an Account | Shopping bag (0)

Brands | Christmas | Women | Men | Shoes | Bags & Accessories | Beauty | Kids | Home & Food | Electrical | Gifts | Sale | JONES

Home | Single Breasted Blazer

D'URBAN Single Breasted Blazer

DETAILS

- 100% wool
- Single breasted
- Notched lapel
- Twin flap pockets, single chest pocket to front, three internal pockets

More ▾

OFFERS

FREE Standard Delivery in time for Christmas – Ends Monday!



\$799.00

Shop with points: 107,865

or 4 fortnightly interest-free payments of **\$199.75** with afterpay [Learn more](#)

Blue

SIZE ▾

Add to Wish List

Size Guide

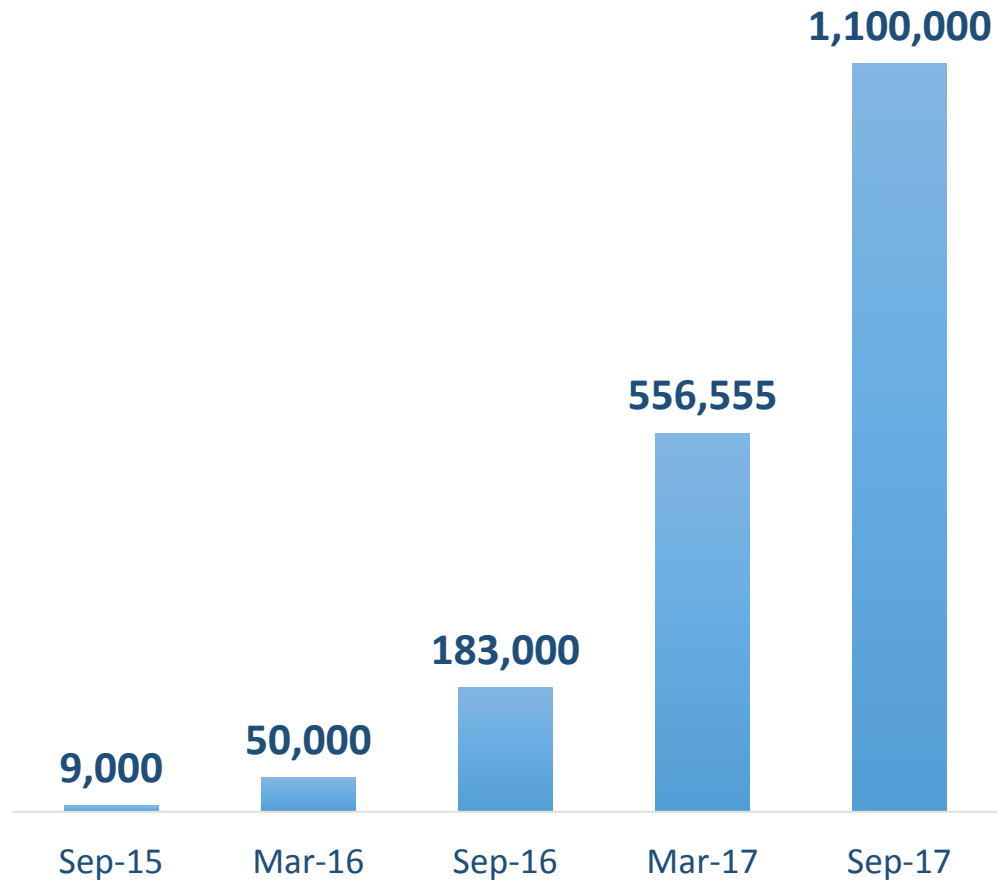
1 ▾ **ADD TO BAG**

AVAILABILITY

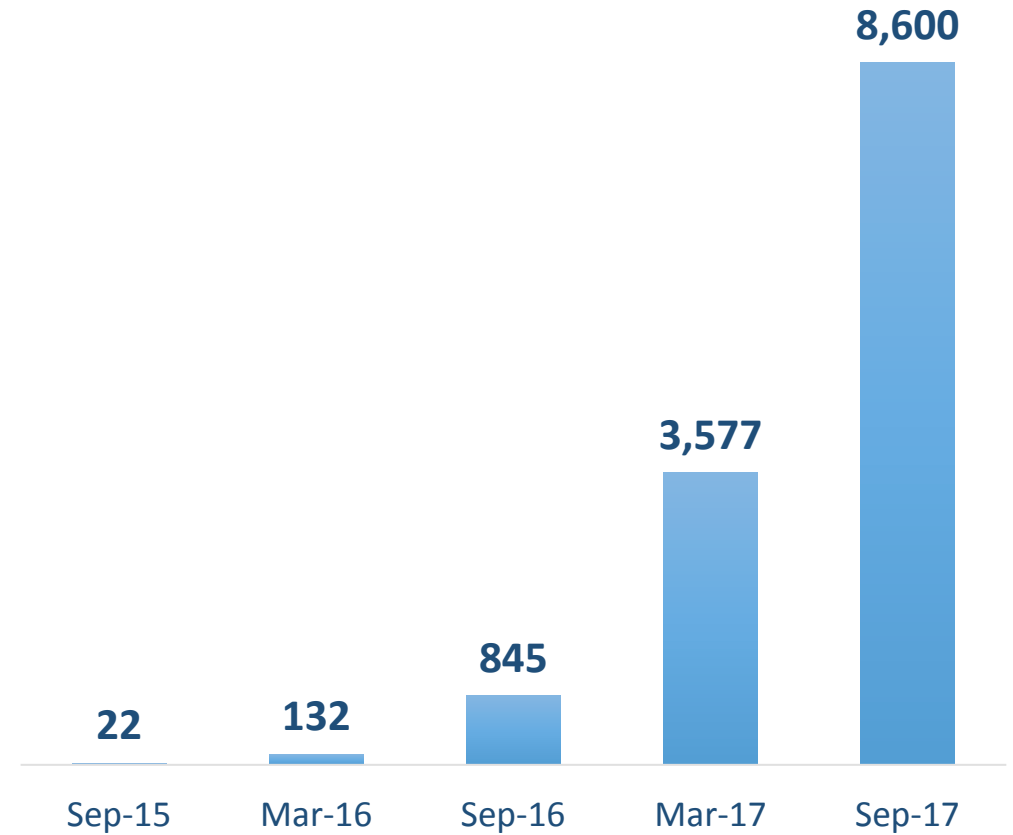
Note: Many retailers promote Afterpay prior to other payment options



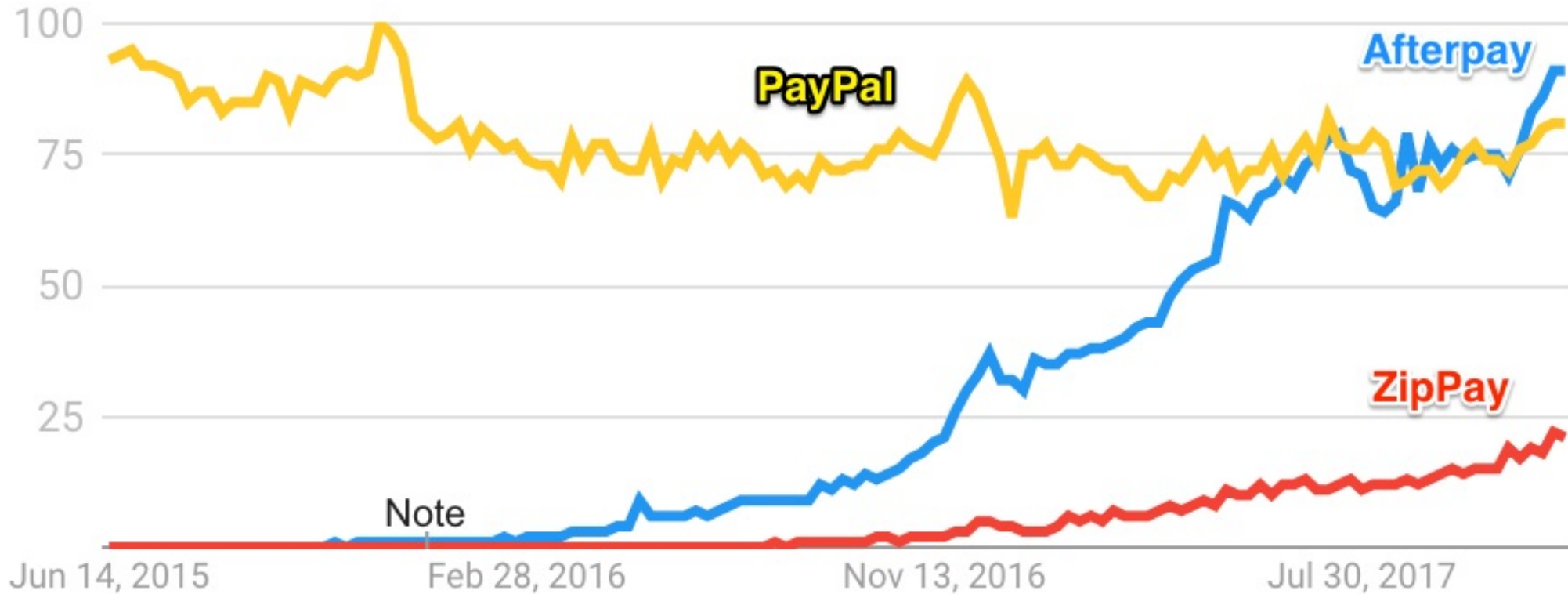
Afterpay Active Users



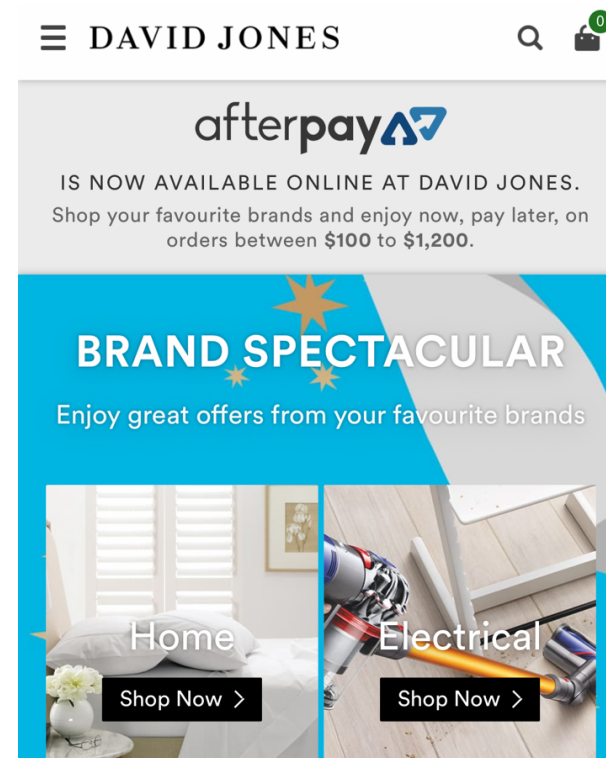
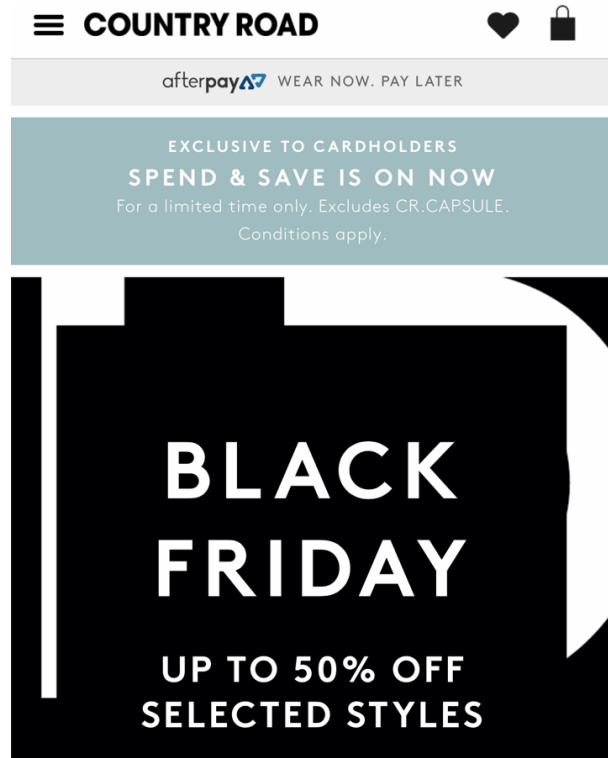
Live Afterpay Merchants



Afterpay: Google Trends (AU)



Retailers Promoting Afterpay



Afterpay does not pay for these placements or spend money on outbound marketing to merchants.

Afterpay Value Proposition

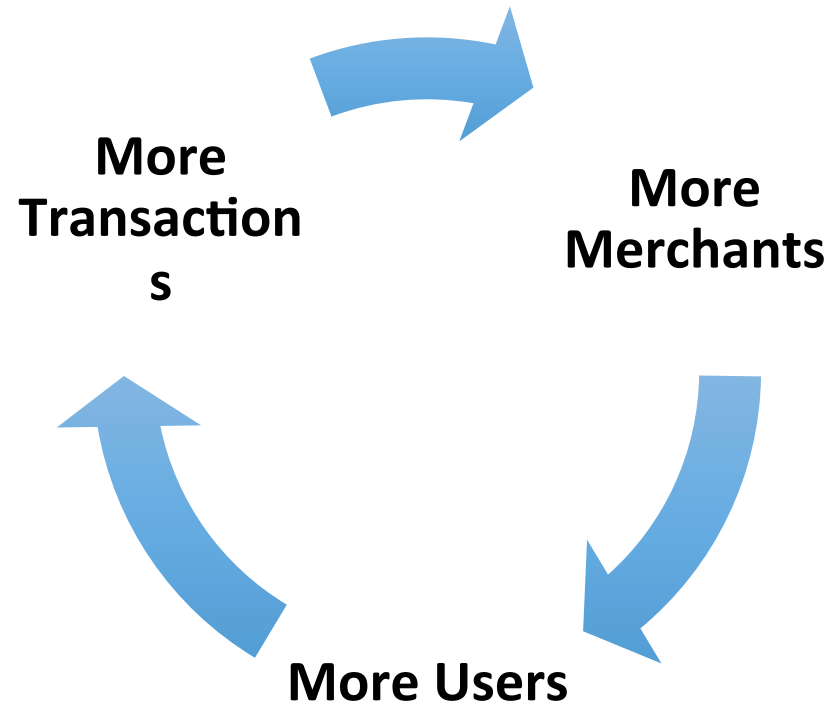
Consumers

- Buy now, pay later
- Straightforward
- No interest
- No establishment fees
- Widely accepted

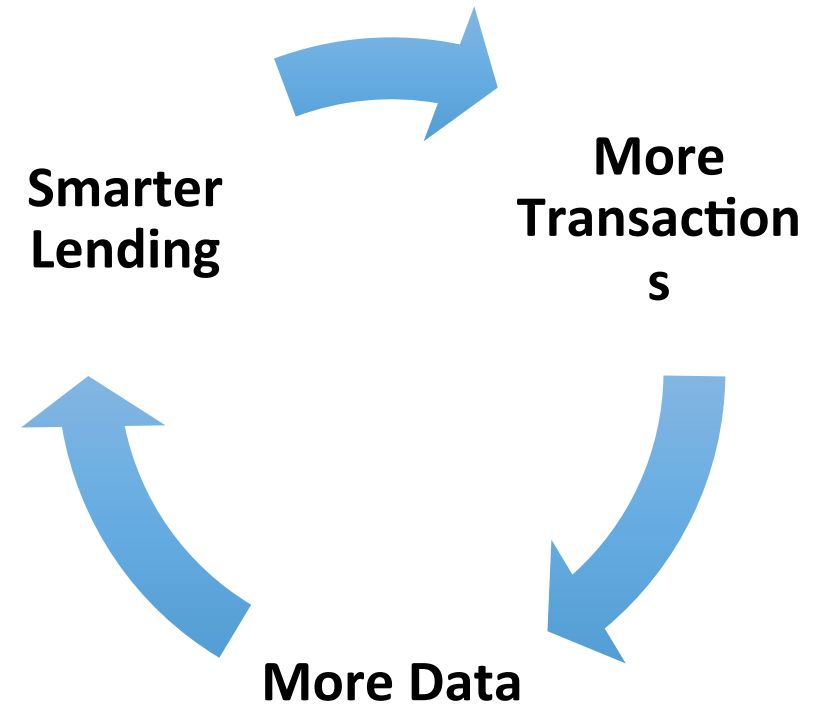
Merchants

- Bigger orders
- Higher conversion rates
- Eliminates chargebacks
- Simplifies layby programs
- Popular with consumers

Self-Reinforcing Dynamics



Evidence: Rising Spend per User



Evidence: Falling Net Transaction Loss Rates

Fraud & Risk Management

Dynamic Model

- Proprietary algorithms, not credit scores
- Real-time assessment of individual transactions
- Enhanced by Touchcorp customers (e.g. Optus)

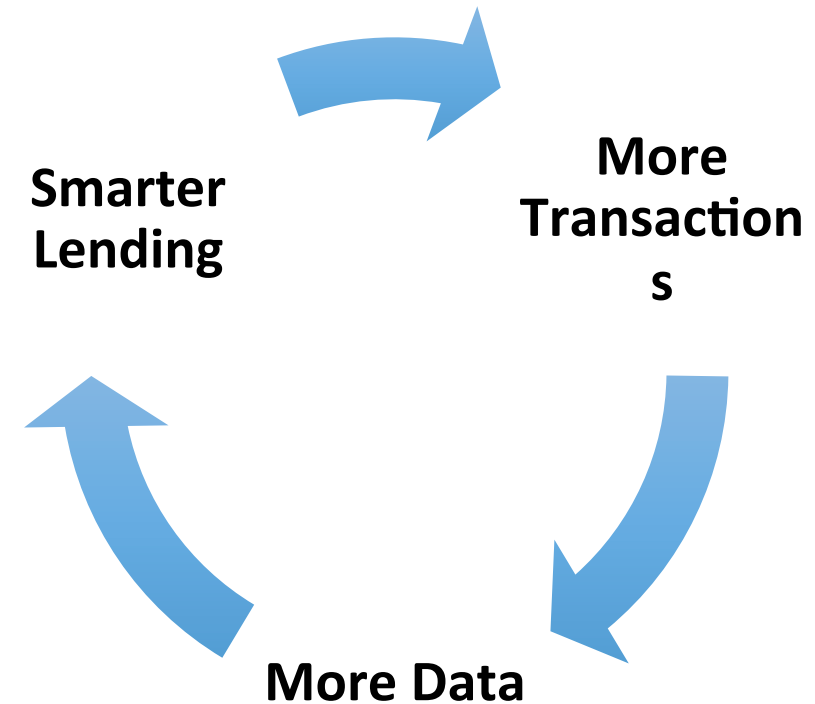
Transaction Statistics

- ≈25% of transactions rejected
- >80% of transactions by value by returning customers
- Transactions linked to cards
 - ≈ 85% debit
 - ≈ 15% credit

Transaction Integrity Engine

Transaction Factors

- Location
- Merchant
- Item
- Card history
- User history
- User address history
- Operating system
- And more...



Growth Drivers

Existing Market Focus

- More merchants
 - 29 new adds a week
- More users
 - 1.3 million today
 - PayPal at 6-million-plus
- Higher spend per user
 - Up 28% YOY

Adjacent Drivers

- New verticals
 - Travel pilot underway
 - Beyond apparel
- New markets
 - New Zealand test tube
- In-store retail
 - Promising early returns

Management Team

Led by Co-Founders

- Anthony Eisen: Executive Chairman
- Nick Molnar: CEO of Afterpay

Strong Alignment

- Own combined 23.3% of company
- Did not sell into May 2016 IPO
- Escrow until May 2018

Afterpay Economics

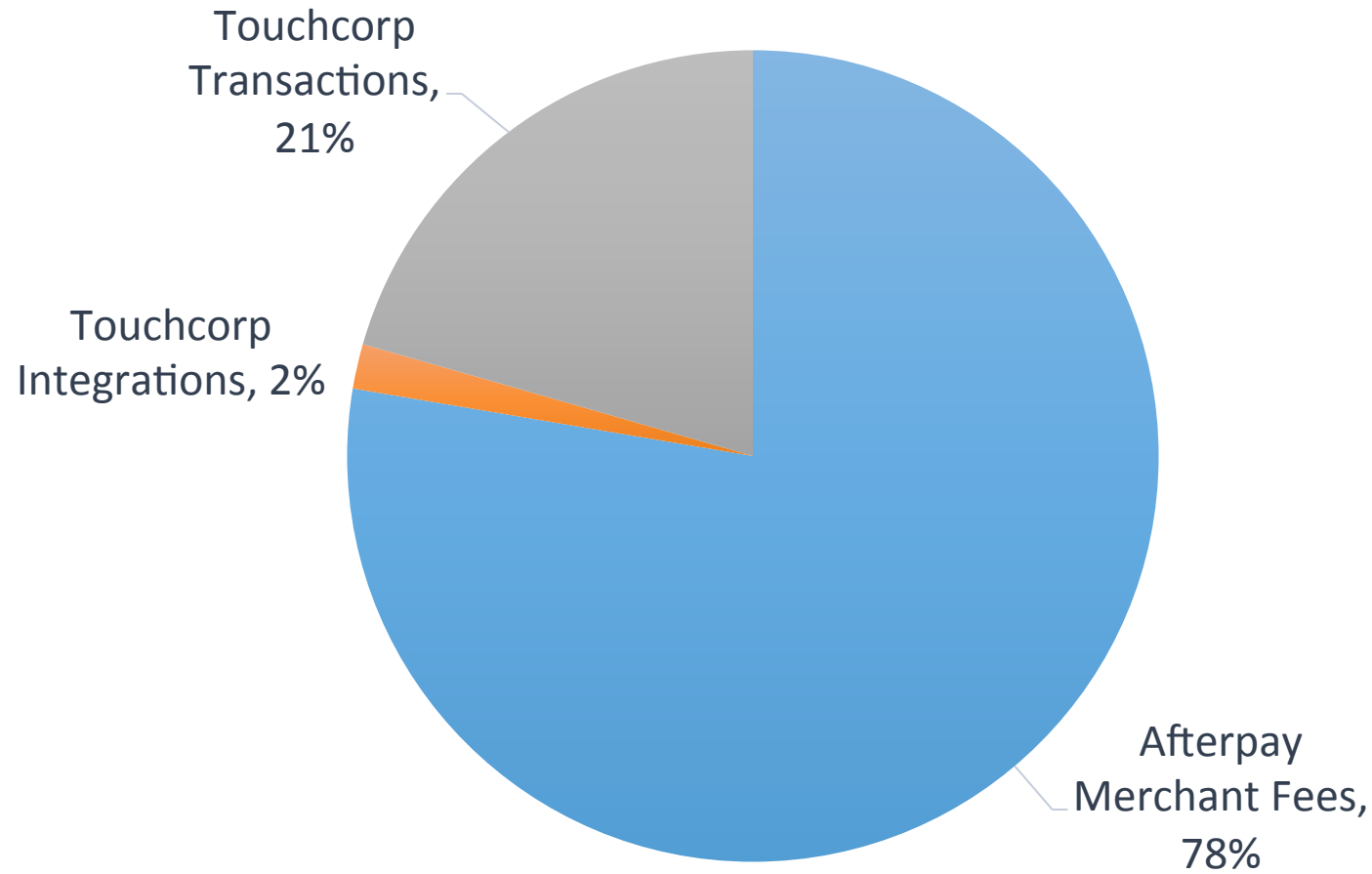
Transaction Level

- Take rate: 4.1%
- Net Transaction Margin: 2.5%
- Net Transaction Loss Rate: 0.6%

Balance Sheet

- Recycling Capital \approx 30 Days
- Credit Facilities: \approx 370 Million

LHC Forecast FY18 Revenue Mix



Operating & Financial Data

	FY2017 Pro-Forma	LHC FY2018 Estimate	Δ
Ending Afterpay Users	0.8 million	1.9 million	228%
Ending Afterpay Merchants	6,000	16,400	173%
Afterpay Merchant Fees	\$22.9 million	\$93.0 million	306%
Touchcorp Revenue (Ex-AFY)	\$25.6 million	\$25.6 million	0%
Total Afterpay Touch Revenue	\$48.5 million	\$117.0 million	141%

Note: Australian fiscal years end 30 June (e.g. FY18 ends 30 June 2018).

Valuation

It's Complicated

- Not conventionally cheap
- Did not post statutory profit last year
- No ready public comps as fairly unique model
- EV/Rev approach is iffy because company is a lender
- Lenders notoriously challenging to value
- Did I mention it was complicated?

Affirm vs. Afterpay Touch

	Affirm	Afterpay
Founded	2012	2014
Merchants	1,200+	10,000+
Users	Undisclosed	>1.3 million
Volume Measure	>1 million loans	> 8.5 million transactions
Entered Second Country	No	Yes
Valuation	Latest Round: A\$2-A\$2.6 billion	\$1.2 billion

Afterpay Touch: Key Risks

Rapid Growth

- Introduces execution risk
- International forays may eat up capital and/or fail to reach profitable scale
 - ...but the company has thus far gracefully navigated its rapid growth

Australian recession

- Loss rates would increase if Australian economy struggled
- Typical Afterpay purchase is discretionary and could be put off during tough times
 - ...but each transaction is assessed in real-time, so the company could quickly tighten standards

Regulatory

- Sector under review by ASIC
- Could force tighter new client checks, affect late fees, require additional layers of regulation or compliance, or introduce some form of capital requirements
 - ...but the company's rapid adoption and market leadership speaks to happy consumers

Other risks exist – see annual report – but these strike us as the most significant.

Afterpay Touch: Conclusion

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