JDP
CAPITAL MANAGEMENT

Survivor & Thriver Fund, LP

3Q 2024 Investor Letter

"Progress is often equal to the difference between mind and mindset." — *Narayana Murthy*

**Narayana Murthy is the Co-founder of Infosy and a pioneer of the Indian IT sector.*

Dear Partner,

In 3Q 2024 the Survivor & Thriver Fund was up 12.4% net to investors bringing our year-to-date return to 33.9%. This compares to a year-to-date gain of 22% for S&P 500 including dividends.

Reintroducing the quarterly letter

In 2017 I stopped writing quarterly letters and transitioned to half-year and full-year letters. Although LPs receive monthly statements from our administrator, I felt that writing less frequently than is common in the investment industry would allow me to provide a clearer snapshot of important portfolio developments.

At the time, I felt there was often not much fundamental change at the companies we owned between consecutive 3-month periods compared to every six months. What has changed is that the velocity of technological, regulatory and political change affecting our holdings is happening much faster.

Today I see more developments between quarters that might not be immediately reflected in a stock's financial statements but might be important to our investment thesis. The intention of the quarterly letter is not to discuss every stock in the portfolio but to highlight a stock or sector experiencing outsized change that I would want to hear about if I was in your shoes.

Overview and Outlook

In the 2024 Half Year Letter I mentioned that the bulk of our gains through June 30 had largely come from only Spotify and Amazon. Our opportunity in the second half was a rebound in other areas of the portfolio. This started to play out in 3Q with gains in the China basket, Tesla, CyberArk Software (sold out), continued gains in Spotify and other smaller positions, offset by flat returns on Caesars Entertainment and a realized loss on Paramount Global and an undisclosed toehold.

A broadening of the market rally continued to pick up in September when the Fed kicked off its rate easing cycle. Lower rates will help re-boot stagnant growth and unlock idle balance sheets especially for smaller companies.

The "higher for longer" narrative that began in 2021 has taken a toll on companies with a high cost of capital or that are still reinvesting all gross profits back into their businesses.

For more than three years, management teams have been pushed towards conservative capital allocation, aggressive cost cutting, returning capital to shareholders and paying down debt, largely at the expense of investing for growth. The US is now littered with small and mid-cap stocks with strong balance sheets, lean cost structures and pent-up demand for catch-up growth projects.

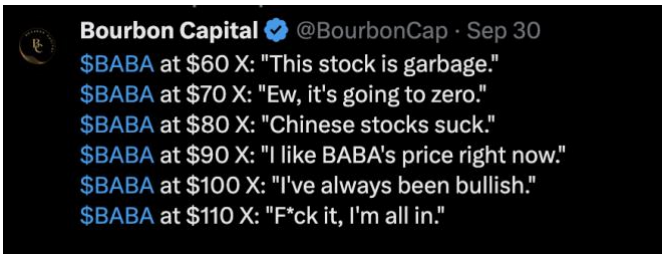
Although there is never an official "all clear" light in markets, declining interest rates, a record $6.4 trillion of cash on the sidelines[1], increasing appetite for capital investment and M&A[2] and a good-enough US economy, is a strong setup for corporate growth to surprise to the upside over the coming quarters.

China basket update

The most noteworthy development in the last quarter has been the rally in Chinese equities sparked by a major government economic stimulus package to help the country pull out of its financial crisis. We did not invest with the expectation of government stimulus, or any catalyst other than the most important businesses in the Chinese economy were selling for distressed valuations. Until last month the basket had been a drag on our performance.

After the recent rally our China basket has become over 15% of assets and is comprised of Tencent, Alibaba and Ping An Insurance. Each company dominates large and important consumer-facing segments of the Chinese economy, is growing key areas at double the rate of Chinese GDP and was purchased for single digit multiples of after-tax earnings. Each also has enormous amounts of cash and liquid investments including stock portfolios worth tens of billions of dollars, and large stock buyback programs. Even after the recent rally, Chinese equities are still down by about 77% compared to the S&P 500 over the last 10 years.[3]

A bit of satire but this post by @BourbonCap and recent Bloomberg headline sums up the manic swing in Chinese equities from "this is garbage" to "I'm all in".



Hong Kong Brokers Swamped by 'Once In a Century' Stock Frenzy

- Hang Seng Index has its best day in almost two years
- Market participants cancel holidays as frenzy picks up pace

By John Cheng, Charlotte Yang, and Winnie Hsu
2 October 2024 at 12:09 CEST

We would consider adding other names to the basket with new capital or in a market pullback, but for now the position is large enough to have an outsized impact on our performance as Chinese stocks continue on their long road to recovery.

Caesars Entertainment update

In the Half Year Letter, I wrote about Caesars (CZR)'s long-term growth opportunity in digital gaming and near-term opportunity to buy back its own stock at a single-digit multiple of 2025 free cash flow[4].

[1] Bloomberg, Funstrat
[2] JDP research
[3] Fundstrat macro research
[4] JDP estimate

Although CZR trades just above our cost basis of $41 per share and the investment has been a drag on performance so far this year, there have been several recent bullish developments that led us to add to the position.

Beneficiary of lower interest rates. Caesars is an example of a smaller US business primed to be an outsized beneficiary of lower US interest rates. Lower rates reduce the interest expense on Caesars debt and boosts cash flow used for buybacks. Declining interest rates also stimulates consumer demand for travel, hotel, gaming, restaurant. Additionally, the "bazooka" Chinese stimulus package mentioned should help jumpstart pan-Asian travel to Vegas for business and pleasure.

Rapidly growing online gaming US market value. The recent Flutter Entertainment investor day presentation (parent company of market leading online sports betting app FanDuel) was bullish for the US online gaming market. Although we do not own Flutter, the presentation is confirmation of the broader opportunity for large players like Caesars. On page 58 of the Flutter presentation the company revised its 2022 estimate of the US online gaming market from $40 billion $70 billion by 2023. What percent of the pie will Caesars get as the largest US land casino footprint and rewards program?[5] My guess is that the market value estimate will continue to go higher with online revenue ultimately surpassing brick-and-mortar as states continue rolling out legalization. In our opinion Caesars's online growth is not taken seriously by investors and is not priced in the stock today despite CEO Tom Reeg reconfirming $400 to $500 million EBITDA run rate from online by 2024 yearend.[6]

Surprise early new buyback program. On October 2, 2024 CZR surprised the market with a quiet SEC filing disclosing it had just bought $150 million of stock at $36.38 per share and authorized a new $500 million buyback (5% to 6% of outstanding shares). In the same disclosure the company said it had completed the sale of the World Series of Poker IP rights for $250 million in upfront cash and $250 million in future consideration. As an example of what I like about CEO Tom Reeg is, the ink is barely dry on this transaction, and he is allocating nearly every penny to buy up as much stock as possible at fire sale prices. We still expect a larger buyback once new hotel construction spend winds down late this year and/or larger asset sales are announced.

Closing remarks

A combination of declining interest rates and a US economy that is holding up, is positive for corporate growth and stocks overall. The second half of the year is off to a great start as our smaller and more economically sensitive holdings finally catch a well-deserved bid.

The majority of my family's net worth is invested alongside yours. Thank you for your trust and support.

Sincerely,

Jeremy Deal

[5] JDP research and estimate, Caesars Entertainment SEC filings
[6] Caesars Entertainment 2Q 2024 earnings call