
BOXWOOD

CAPITAL MANAGEMENT, LLC

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It was the recap of Q1 2018 when these pages first discussed the fallout of the Facebook Cambridge Analytica scandal. Pressure on the company has been relentless ever since. Whether that pressure was coming from the political left or the right, whether it was state attorneys general or the US attorney general's office, all the way to the President himself, the company couldn't seem to catch a break.

In subsequent quarters the regulatory and political scrutiny of FB continued to be highlighted here, implying there might be negative consequences to our investments (with big Tech being attacked in general). The business of collecting massively large amounts of users' data and then targeting ads to them was at risk. No longer could Big Tech hide under the veil of providing free services, as is the case with FB and Google, or offering consumer goods at relatively low prices, as is the case with Amazon. Regulators were/are coming after them. The model of Facebook and Google is at risk of becoming less of a free public good and more of a regulated public utility.

Remember, *The Jensen Opportunity Fund's* thesis for its investment decisions is largely premised on the idea that target companies operate in a monopoly, duopoly or at the least in an oligopoly. They are in a high margin business, and they have large impenetrable moats. They also have large cash positions on their balance sheets, which can either be plowed into research and development, furthering their winner take all advancement, or can be deployed to purchase innovative newcomers (the top 5 market cap tech companies had \$90B in capital spend in the last 12 months alone). All characteristics which are quite different than the qualities of a typical regulated public utility.

In addition to the scrutiny over the collection and handling of consumer data, the Fund's portfolio companies were/are also being attacked precisely because of the reason for the Fund's investment decision, i.e. monopoly status. The antitrust regulators have gone so far as splitting up the turf, with the Federal Trade Commission investigating Amazon and Facebook, while the Justice Department will be looking into Google and Apple.

Wow, that is a one-two punch. The prodding of politicians and regulators isn't good for business. The Fund's positions were/are under attack, and it was justified for these pages to write about such and warn of the investing implications.

Indeed, just look at Facebook's stock. The day before the Cambridge Analytica scandal broke was March 16th, 2018. Between that March day and June 14th, 2019 (more on the importance of that day), an approximate 15-month span, FB's stock was down 2.3 per cent! Not exactly the type of return that is expected out of the Fund's portfolio companies.

And then on June 17th everything changed. Abracadabra, Libra, Calibra. What? Yes, Facebook announced their intention to launch a cryptocurrency, named Libra (and Calibra is the digital wallet which will be used to store the Libra). A game changer. Over the 14 trading sessions since the announcement, the stock is up 8.3 per cent.



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In *The Wall Street Journal's* June 25th edition, they write, "the technology transforms the social media giant's own business." In analyst Mark May's research note titled, "**Facebook's Path to Printing Even More Money**," he writes, "Libra could introduce a meaningful new product and profit stream for Facebook over the coming years." Another analyst, Mark Mahaney, wrote, Libra "may prove to be one of the most important initiatives in the history of the company to unlock new engagement and revenue streams." The Fund's concern over the political and regulatory scrutiny of FB's advertising business could, in part, be put to rest.

Would the introduction of Libra alleviate FB's revenue from being almost solely reliant on digital advertising? Although no monetization plan has been announced for Libra, it is easy to conceive of an idea whereby Messenger and WhatsApp could be leveraged. At least initially, Calibra, the digital wallet, will reside in those two platforms. And with each platform attracting 1.5 billion daily active users, it is plausible that extracting just a small percentage of transaction fees could generate massive, high margin revenue.

Although this new business initiative has already been attacked by politicians too, in Facebook's white paper on the matter, it lays clear that they have been working alongside with regulators during development. This will be key. If FB has the regulators on their side, and they are able to bring low cost banking to the 1.7 billion adults that are underserved, it will make it more difficult for politicians to have a fight. As FB notes, "hard-earned income is eroded by fees, from remittances and wire costs," and "payday loans can charge annualized interest rates of 400 per cent or more." As long as the regulators have been kept abreast along the way, it is hard to argue against solving those problems. Can anyone say Facebank?

I am pleased to announce The Jensen Opportunity Fund gained 6.52 per cent, while the S & P 500 index fund only advanced 3.79 per cent. Another outperformance.

Until next time,

Todd Shorb

