Year-end Update | December 2021

Dear Investors,

I hope everyone is healthy and well and you had a wonderful holiday time. I truly wish you a happy new year and all the success for 2022.

Just as a note, this is not my annual letter and results are preliminary as the administrator statement is the only official result, which is why below I use the word "approximately". In this update I want to highlight three elements of our activities that must be evaluated, from the least important to the most important: absolute return (the stock prices at end of a period); the fundamental development of my investment thesis (the business performance of the companies we hold); and the most important one, my decisions (my behaviour and thought process).

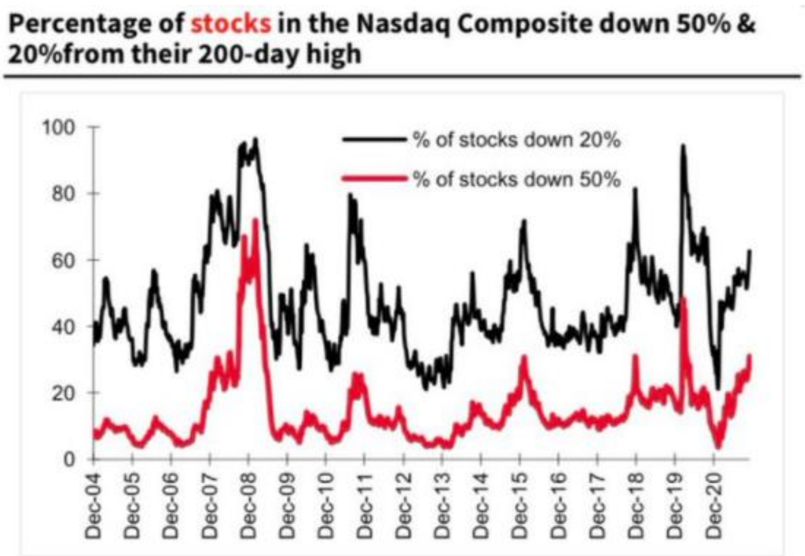
I start by the least important in the short term. Please note that I will providing hyperlinks to words that might not be familiar to all of you, so you can click those to see the definition online.

Absolute Returns

The fund returned approximately -11.9% for the second half of 2021. These declines are normal and must be expected, especially after the robust performances of the stocks we held in 2020 and H1 2021. In the short term the difference between what businesses are worth and their stocks prices can be extreme, and short term moves (like in our case of over 5 months) are irrelevant as they barely follow fundamentals but the noise of the day. However, in the long run, this is almost never the case, as stock prices follow the fundamental performance of the business. Stock volatility is the price of admission we investors must pay for the long term returns they provide, and time in the markets is much more important than timing the markets. That is why judgement of our process can only come over multi-year periods.

For all new investors, I remind you - as I have written in my previous letters - since 2013 I have not had a single year where drawdowns (peak to through declines at some point during a year of the portfolio value) were less than 10%. As an example, in 2020 I had a 20% drawdown, in 2019 a 15% drawdown, in 2018 a 27% drawdown. I can continue, but the point is, they always occur. In 2018 I had an almost +30% year by October that ended flat with the correction of December 2018. This is what equity investing looks like. But when you zoom-out you see the evolution of returns, and how they reflect the fundamental performance of our businesses. I have been disciplined in highlighting that my job is to deploy our capital in the best opportunities I see for the next few years. I never think about what the best opportunity is for the next six months, and my focus will never be trying to beat the market in any given quarter or year. Another reminder, as I am not able to predict the market gyrations, I will never try to minimize short term volatility of the portfolio value to provide an illusion of safety to investors. My job is to put our capital to work and behave correctly, that is what you entrusted me for.

To give you an understanding of why our stocks have been affected - there is no valid reason but the constant macro-economic worries, such as inflation, Omicron, China, Fed tapering. There is a large correction in some corners of the markets, particularly for small companies and in many industries, such as health care. While the indices do not show that effect, as the main constituents of those like Apple, Amazon, Facebook, Google and Microsoft are at close to all-time highs, more than 60% of all the Nasdaq constituents were down 20% or more, and 30% of constituents were down 50% or more as of mid-December; please see the chart below. There was a strong correction eclipsed by the concentration of the indices. In some cases, the correction is warranted, such as in MEME stocks or companies without any quality, but it has also had a much broader effect on various industries and companies. In the S&P 500, for instance, Microsoft, Google, Tesla, Apple and NVDA represent one third of all the year-to-date gains of the index. The indices are extremely concentrated to those few names.



Source: FT

When these corrections occur in smaller companies, there is no difference between quality names and bad businesses, but these are the times when I add to our quality names. We have always operated like that and will continue to do so. Behaving properly in moments like this is what makes all the difference in this business.

My behaviour / What I have done

Something I have learnt at investing is that it is more important to have the right businesses than waiting to have the right businesses at a bargain price. I cannot wait for market corrections for entry and remain in cash for years, I might never own the right businesses, as those business execute and increase their intrinsic value over time. That is why I acquired most of our businesses (the same I held during the partnerships) during the months of July, August, and September 2021, cost averaging through time and I still left a considerable portion in cash, which I will explain below.

As promised, no single stock represented more than 10% of the value of the portfolio at cost, and that will continue to be my policy at inception of the fund, so if stocks keep falling, I can be adding to single names as long as the amount at cost is not higher than 10%. This will prevent me from endlessly adding to names - discipline above all. In case of inflows/subscriptions to the fund, as we just had the case with inflows from existing investors, I will be allocating the capital similarly to how the portfolio was constructed at year end.

As I am not naively euphoric about the state of the markets and I am very well aware of macro-economic risks, the barbelling part of the portfolio (the ultra-safe assets with low expected rate of return) and cash (which has negative expected rate of return but positive optionality) was at some of the highest levels I have ever had. At the beginning of December, I held 25% of our portfolio in cash (this is safe in the short term and very damaging in the long run), 3.7% in Berkshire, 3.6% in Exor (Exor just sold Partner-Re for 9 billion in cash, which is roughly half of Exor's market cap) and 4% in TPL. On top I have a put option covering approx. 5% of the portfolio on a single name. This results that the fund had around 31% of fire power in cash (cash and the put option if exercised) and 11% on ultra-safe assets, for a total of 42%. Please note that this is a big size for this side of the barbelling (particularly in cash) and I expect cash to diminish as stocks fall or as I find different opportunities, as it happened in December. Normally, I want to have this side of the barbell not higher than 20% (Cash + Berkshire+ EXOR and TPL). Given the strong correction during the first two weeks of December, I was able to deploy more cash at bargain prices and the fund ended with approximately 12% in cash. Given the inflows to the fund, I will be having even more firepower in 2022.

The big size of this part of the barbelling reflects my awareness of market risks and my inability to know the second order effects of those. We have Omicron - is it going to be milder and potentially the end of the pandemic? Or it is going to be another March 2020 with full lockdowns, high number of deaths and the collapse of the economy. I do not know, I can only say, today is not March 2020, we better understand the virus, we have vaccines with boosters that improve the efficacy and more importantly we can modify vaccines to emerging variants of concern if needed. I would be foolish to extrapolate March 2020 to today and take portfolio decisions based on that. The world has already dealt with many variants, and I think of this event as an opportunity rather than a threat.

We have inflation and tapering; this is something I have been anticipating for a while and is the reason why I am not comfortable with cash. We hold TPL and Berkshire which are extraordinary direct inflation beneficiaries. We do have only two names that can be somehow affected by inflation as their present value of future cash flow are worth a little less, like Maxcyte and Clearpoint, but that is why they are a fraction of what they used to be in the partnerships. I cannot sell them either, as those businesses, I believe, will be worth multiples of what they are today, and **most importantly the bulk of our portfolio**

companies are all inflation beneficiaries. Take JDC, they get a cut on insurance commissions that grow with inflation, and similarly happens with all our companies with high pricing power, such as IDT, Games Workshop, Xpel, Well Health. Inflation normally brings volatility but at the end the only real hedge is owning assets, particularly companies with high pricing power and that is the bulk of our portfolio.

On the other side of the barbell, I opened a Kraken account and put 3.7% of our assets there. This reflects my positive view on blockchain technologies. I am aware this is the most volatile part of our portfolio, and I know some of you can consider it the riskiest of all. I do not, given the small allocation, I consider a higher risk not to be exposed to blockchain. I also own shares of two companies that are involved in blockchain technologies, one of them produces an extraordinary level of cash in earnings. The company is called Coinshares and I wrote an extensive write-up that you can find here, I recommend you to read it. I also have been engaged in constant talks with management and I am very optimistic on how the company is developing.

I have spent the last six months researching blockchain and its real uses, such as in gaming, finance, security, identity and the more I learn the more impressed I get. I have had the opportunity to engage with some of you on the topic, which I encourage all of you to do. I end up learning every time I speak with my investors. In my full annual letter, I will explain in detail why I see blockchain as a must have in our portfolio, but I must recognize that this is a nascent industry, there are countless participants engaged in only speculation and my priority is to extract value and cut noise. That is reflected by how I constructed our portfolio, I believe our investments in blockchain can become many multiples of what I put at cost in a few years.

To finalize the topic of blockchain, we do not own Bitcoin directly, but all the industry is somehow correlated to it, and Bitcoin has all the possibilities to shine in an inflationary environment. Let's see how it behaves, it is too early to tell.

There had been only two relevant intrinsic data points that made me act decisively with some of our holdings. All other companies have the widest discrepancy of how the businesses are performing compared with the stock price performance over the last five months. Our portfolio today is worth multiples of what is currently quoted.

Behaving properly is the most important aspect, and I feel I have behaved exactly as promised to you and as I have operated in my eight years investing.

Business Performance:

As mentioned, that this is not my annual letter, so this part will be very brief. I will expand in my letter in a few months.

Except for four names, every single company we hold provided the best fundamental results in their history in 2021, this is out of 16 positions we currently hold. It is an outstanding portfolio.

My investment framework can be summarized as looking and holding companies with substantial unrecognized earnings potential, these are the characteristics of our top holdings.

Top three positions:

JDC Group: This is a company digitalizing the insurance sector in Germany. They are in the middle between insurance companies and companies selling insurance. Currently JDC has approximately 130 Mio. EUR in revenues and 8 Mio. in EBITDA; the company signed a deal with the two largest public insurances (one of them becoming a large shareholder) for deals that together can add 200 Mio. in revenue, and my research indicates that the singing of these large deals will continue. JDC is our largest independent holding as it offers the largest margin of safety and earning potential.

XPEL: XPEL continues growing very rapidly and, more impressive, expanding its margins and business lines. Growth in the last quarter was 48% y/y and with the recent acquisition of Invisiframe, XPEL expands to the bicycle market. This is a company executing very well. Despite an extraordinary business performance, XPEL stock price is having a drawdown that from peak to through reached 40% at some point in December, the fund is taking advantage of this opportunity.

IDT: IDT is a business composed of many companies, managed by Howard Jonas, one of the best value creators of the last decade. IDT currently has two companies that, I believe, will be worth more, far more, than the entire value of IDT today. These are Net2Phone and NRS. Both companies are expected to be spun-out, Net2phone imminently and NRS within the next two years and both are showing impressive growth and profitability, while the legacy core businesses of IDT remain in great shape. This is an absolute bargain after the move in the stock price from 67 USD to 43 USD in the last few weeks of the year.

A portfolio holding worth mentioning is WELL Health, this is a company that the stock price is currently completely disconnected to business fundamentals, and it is offering an extraordinary opportunity for the fund to add to the position. I have been in discussions with the CEO (who is the largest shareholder) to push for the spin-out of some companies within the group, such as WISP and Circle Medical that alone can be worth more than Well Health. Surprisingly the CEO was already looking into that. Well Health, while not being in the top 3 of our holdings, offers one of the largest risk rewards for Arauca Capital after the recent drawdown.

In December I also entered in new positions that I am still buying and will disclose eventually, it was a very busy month for the fund as I was happy taking advantage of the low prices in some great businesses.

Conclusion:

I am very excited with how Arauca is positioned for the future, with our process, investment philosophy and discipline. I was tested big time in 2021, I never imagined what the year had in store. Laura and I finally we got married, we changed countries, had some personal setbacks, opened the fund, sold our yoga business. Looking back into the past year, I am impressed what we achieved despite the challenges and how we positioned ourselves and the fund for a bright future. I can only say that when you have correct mental models, the right people around and you are humble with your convictions, good things happen and you are able to overcome any difficulty.

On a high-level note, I want to remind you that negative views highlighting all the risks of the economy always sound smart and allowing those views to affect how we think is dangerous for investors. While Central Banks will make mistakes, a large number of people will keep being engaged in rampant speculation, other negative surprises will show up and we might have inflation, the constant is that there is an enormous effort by great people to improve how we live and create value. Some technologies are disrupting old ways of doing things and I believe there is an immense value to be unlocked. It is so important to have a balanced view on the state of the world.

I am honoured to be the steward of your capital and I thank you for your trust. Let 2022 unfold.

Jean Philippe

January 2nd, 2022

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At the time of writing this letter, this investment fund falls outside the supervision of the Dutch Financial Markets regulator, or AFM (Autoriteit Financiële Markten).

Therefore, the fund manager is registered with the AFM as an AIFMD "light regime" or "de minimis regime" (not supervised) manager. The registration number of this Fund is **50026641**, and the updated registry of "light regime" managers can be obtained on the AFM website: https://www.afm.nl/en/professionals/registers/vergunningenregisters/beleggingsinstellingen

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