

Launch Letter | September 2021

Dear Investor,

After having founded Arauca Capital Management B.V. (the management company) in March and started operations in the fund Arauca Capital (the fund) in mid July 2021, I would like to share with you various aspects of the of the fund and answer some questions I have received along the way.

First, I want to let you know that I am honoured to have the responsibility to be the steward of your capital. After a lot of hard work, we initiated all operations smoothly and I have been able to responsibly deploy our capital to the extraordinary companies that I had been holding in the preceding partnerships. I have also been busy with new ideas, some of which have transformed into new investments.

Setting up the fund has been an illuminating and at the same time challenging lesson for me. I cannot tell you it has been easy, but nonetheless I cannot be more pleased to have taken the decision to open the fund and be able to receive you as my companion on this journey of compounding the important things in life (knowledge, relationships, and capital).

In these few months I have been busy speaking and spending more time with the management teams of our companies and of companies I am interested in. I have also been contacted by smart young guys, one of them has already started helping me on the due diligence of a particular idea and I hope to engage more with him soon. Laura keeps supporting me enormously and now she is in charge of our website that should be ready in the next few months, among other things. As always, I cannot be grateful enough to her.

Over the last few weeks some of our portfolio companies have given us extraordinary news, for example Maxcyte successfully IPOed in the US, Games Workshop reported the best year since I follow the company, Well Health keeps announcing accretive acquisitions and is expected to IPO in the US in late 2021/early 2022, just to mention a few. Meanwhile, at the moment of writing, the financial markets are extremely worried of the possible default of Chinese giant Evergrande and a possible tapering announcement by the Fed, which of course has affected asset prices across the world.

These events would worry me if I had shares of Evergrande (which we do not), or shares of companies with exposure to Evergrande (again we do not). I do not see how a potential default of Evergrande or Fed-tapering would stop Warhammer hobbyists from buying Games Workshops' products, or Well Health clients from going to their clinics or using the tele health app, or Maxcyte clients from using the electroporation machines - I could continue with all our portfolio companies here but you see where I am getting at. That is why I focus on companies without exposure to the obvious risks, such as high leverage, China and or highly capital-intensive industries. The markets can and will have large

**Attention! This investment falls outside AFM supervision.
No license and no prospectus required for this activity.**



ARAUCA CAPITAL

corrections, and as long as the fundamental state of our companies does not change that can only mean opportunities for Arauca.

On another note – as a unitholder in the fund you are now able to invest amounts as little as 10k USD on liquidity day, which is at the end of the year, so in case you want to add to the fund, please ensure to let me and our administrator know by early December 2021. The best time to invest is when stocks go down for macro reasons, so while you might find it good to add when we have great periods, the best for you and for the fund is to add in periods when the financial markets are nervous and correcting. During those periods I become an aggressive buyer of more of our businesses or great businesses that I have not been able to buy due to valuation.

Why did I decide to Launch Arauca Capital?

Since 2013 I have been managing my capital and the capital of a few close family members in the previous partnerships. That set-up prevented me to accept capital from non-family members and as some of you have been interested in my endeavours for quite some time, and some have asked me to help you allocate some of your capital, I decided to open the fund. With this structure, I can readily accept investors who share my investing philosophy and have all the capital together in a single vehicle. I am delighted and honoured for the responsibility.

How have I translated the allocations of the initial partnerships into the capital allocations of Arauca?

As you know, I allow high concentration on companies that perform as long as the gain comes organically and in the case of the previous partnerships, I had some positions that were 20 baggers (meaning their initial investment multiplied increased by twenty times, such as XPEL). This has resulted that my previous structure had companies with large allocation sizes.

For Arauca, I decided to not allocate more than 10% of the NAV at cost to any investment, the largest positions were given positions between eight and nine percent and are companies I know very well and for many years. However, I will allow high concentration to occur, as long as the increase in size comes organically, as this is one of the most important aspects to generate high returns. Let the winners run. Of course, with constant verification of the investment thesis.

For which type of investor is Arauca Capital suited for?

Arauca Capital is not a business where I want to exploit most of the upside by generating recurring fees. My main objective is to compound capital at the highest rates of returns possible with the lowest level of risk (I will explain my definition of risk further down). After all, I am the biggest investor in the fund, and I want my benefit to come from the appreciation of my investments, and if I was to make gains out of the fund, they should come from performance fees. The strategy and vision of the fund need to be framed to achieve this objective. At Arauca, all decisions are taken within the following framework:

**Attention! This investment falls outside AFM supervision.
No license and no prospectus required for this activity.**



ARAUCA CAPITAL

- The Objective/Mission: Compound capital at the highest rates of returns possible with the lowest level of risk generated by the fundamental increase in value of our businesses as their management teams execute.
- For whom: For people who have worked hard for their capital and are aligned with my investment philosophy

I must avoid losing focus and say/offer things that might sound nice to perspective investors but are detrimental to the mission.

In order to do what makes sense and to achieve our mission, I need to have the type of right investors. Those investors, I have come to realise, should be often private individuals/ private families who have themselves worked hard for their money and know what it takes to keep it – remember, preserving wealth is way harder than creating it. This understanding makes them aligned with my philosophy.

In order to make sure I have the right investors aboard, I had to create some filters such as the two-year lock-up period. If any prospective investor is concerned about a two-year lock-up period, I immediately know that this investor is not suited for Arauca. The lock-up period easily helps me identify wrong type of investors.

Creating the fund gave me the experience of engaging with some institutions for the first time for a possible investment. To my surprise, the institutions did not consider reading my previous letters, did not ask me about previous investments, did not consider important knowing how I undertake investing decisions or what attributes I look for in the management teams of my largest positions and most importantly, did not show any interest in learning about my philosophy. The only questions that came where concerned with the lock-up period, the distribution between equities, bonds, other assets (if this was something possible to know), the fact that the fund is not licensed, the frequency of the NAV reporting and similar type of questions only.

I diligently answered all question and knew that these institutions were not a good fit for the fund but took the opportunity to ask why they cared only about pure technicalities but not about the important aspects of the fund. Their explanations made me realise that Arauca is constructed completely differently to how these institutions operate. The institutions explained to me that they need to maintain a low level of “risk” and they need to project their due diligence into their clients. Low level of risk was explained as maintaining a percentage not higher than (X) into equities, while the majority must be held in fixed income. To my surprise, high yield corporate bonds in highly leveraged companies were considered a low risk. This was based on volatility of the price of the assets. This “logic” is, I am afraid, completely non-sense, as corporate bonds give you limited upside (and in many cases negative real yield), but with all the downside as well (in seniority just one level above equities). If the companies perform well, investors will not enjoy the increased earnings, but if the companies fail, they still can lose all their investment. And when you take inflation into consideration and management fees, a high proportion of bonds at current rates guarantee real negative rates for the final investor - a losing proposition, but final investors are rarely aware of that. At the time of writing, close to 90% of the junk bonds (high yield) in the US are trading below CPI inflation. Imagine the risk these investors are taking by not having equities.

I realised that certain type of investors (mostly institutions, but I am still optimistic that there are some out there who share a similar investment philosophy) and I speak different languages. Therefore, Arauca is open for people like you, who care about the capital you give me, because it is yours, and

**Attention! This investment falls outside AFM supervision.
No license and no prospectus required for this activity.**



ARAUCA CAPITAL

I care because I treat your capital as it was mine (as both your and my capital are invested equally). With that said, I am happy to receive likeminded investors who share our philosophy.

How do I define risk?

I see risk as the probability of permanent losses, and the latter I see as a situation where my investment thesis is flawed, either by the appearance of new facts that would make my thesis obsolete on a fundamental basis, or by having an incorrect understanding of the business combined **with my inability to recognize those facts in a timely manner.**

Volatility is never a concern for me. Volatility is the price we pay in order to be equity investors and as I have always mentioned, there will be periods with extreme volatility, but given the nature of the fund that I do not allow net leverage/naked short positions, Arauca will not be fragile to it. What I do care about deeply, is to constantly evaluate my investment theses in order to assess if all my positions deserve to be a holding of Arauca Capital.

Another risk that we face at Arauca is if at any time I lose curiosity, turn lazy and become stubborn to change my mind. These "risks" can sound simple, but I have come to believe the opposite, as in a fast-changing world that is moving at speeds faster than the speeds our minds can adapt, flexibility of thought is not that easy.

An important risk at Arauca would be my inability to think non-linearly. I have to see any investment in the context of probabilities, and I need to use the lessons of the past combined with the context of the present. That is why today, I stopped saying that I belong to any kind of investing style, instead I only define myself as an investor. Belonging to investment styles make it harder to think independently and non-linearly.

And lastly Arauca faces a big risk if I am not able to constantly grow my circle of competence. The circle of competence should be used when deciding to add risk, outside of it, I must stop and do not put our capital there. However, that principle is not an excuse for me to not be learning about topics outside of it, otherwise how I can grow it, and how can I steer our capital better? See below how I currently operate:

- 1 - Know the boundaries of your circle of competence
- 2 - Respect the boundaries when deciding to invest
- 3 - Ensure to learn constantly outside your circle, and with that, grow it and connect more patterns.

Key elements of the investment strategy

The core of Arauca's investment strategy is holding long positions in equity investments where we see ourselves as long-term owners (as long as management executes), but it is not limited to those, as I can invest in precious metals, crypto currencies and commodities when the opportunity arises. Our analysis for the selection of equity investments is based on fundamental analysis of businesses that are trading with a significant margin of safety. Margin of safety is defined as the difference between the price the security trades at compared to the estimation of the company's intrinsic value. Intrinsic value

**Attention! This investment falls outside AFM supervision.
No license and no prospectus required for this activity.**



ARAUCA CAPITAL

is composed of quantitative and qualitative metrics, it is never a precise figure. Arauca has special interest in companies with strong pricing power and optionality, but it is not limited to only those.

Once the fund has thoroughly investigated a company and decided that its valuation offers a considerable margin of safety, the fund will allocate some proportion of its resources to each position. The weight of each position is determined mostly by the size of the margin of safety of each investment, other variables also play a role, such as the quality of the management team.

Aspects the fund considers important to determine the margin of safety:

- The measurability of potential cash flows
- The strength of the balance sheet
- The level of confidence with the management team
- Favourable growth trends in the industry
- The level of optionality, which is the potential of positive future outcomes a company has with its current projects that the market assigns no value for them

Arauca operates with a barbell strategy. On one hand we hold very safe assets, positions in large companies with long track records, precious metals, cash, and sometimes short duration government bonds; and on the other side of the spectrum the fund is expected to hold nano and micro-cap companies involved in emerging technologies, as well as crypto currencies; those positions provide a higher risk/reward profile. For me it is important that I need to allow myself to be wrong and change my mind quickly when facts change; the barbell strategy gives me that flexibility and most importantly that peace of mind. I do not mind sacrificing some returns by holding safe assets for that.

The fund will constantly monitor all its positions and will be ready to divest when it considers that the original investment thesis is no longer valid, examples of that case can be when:

- Realization that facts have changed, and the original investment thesis is no longer valid
- Lack of execution by the management team or loss of trust on the management team
- The appearance of a new investment with a better risk/reward profile

Outlook

I keep listening to people about how "expensive the market is" or how worried market participants are about the current world affairs. This view puzzles me, because unless you are afraid of an Armageddon type of situation, the world is advancing very rapidly for the better - take the field of regenerative medicine, where for the first-time humans will be able to adjust the wrong letters in a gene that make a disease appear without altering the DNA; or blockchain technologies, where now verification, trust, storage of data, market places among others will not depend only on centralized entities but in a decentralized matter and the advent of interoperable blockchains is shacking the financial and gaming industries and soon many more. The world is moving fast and for the curious there is a lot of value to be unlocked. There is an enormous number of entrepreneurs and management teams creating a better world and here at Arauca, I am looking for them.

**Attention! This investment falls outside AFM supervision.
No license and no prospectus required for this activity.**



Investor gathering April 2022

One of you had the wonderful suggestion to hold an annual meeting. I really love the idea, and if at least two of you can attend, I would happily organise it. As the fund is small, I would call it an investor gathering, where I would explain my thoughts about our portfolio and answer all your questions.

The proposal would be to hold the gathering on a Saturday at the end of April 2022 in Vienna, Austria (and if this takes off, we can change the location every year), where I will book a room for the meeting and then we could all go for a nice Austrian dinner.

Therefore, please let me know if you like the idea and would be able to attend (with two or more investors, I would be up to it) and then Laura and I would be sending the details next year. For the ones coming from abroad I would even offer a historic tour of the city of Vienna. This investor gathering would be only open for investors and their immediately families.

Again, thanks for your trust and I am excited for what's to come.

Sincerely,

Jean Philippe Tissot

**Attention! This investment falls outside AFM supervision.
No license and no prospectus required for this activity.**



Additional technical questions

What is the process if "something suddenly happens" to me?

In the event that I am not longer able to perform my duties, Circle Partners, Arauca's fund administrator would be in touch with you to arrange whether you prefer to find a new manager or withdraw your capital. In case of the latter, Circle Partners is of course able to liquidate the entire portfolio and redistribute the capital to you in a matter of weeks. I hope (more than anyone) that this situation does not occur, but there is nothing for you to worry if it does.

Why does Arauca have two classes of units in the fund?

Arauca is a very particular fund in which the management company takes care of all the costs except the bank account costs and trading fees of the fund (regardless of the level of the AUM), as opposed to charge accounting and administrator costs to the fund (to investors in other words). I have decided to go for this set-up to ensure I can charge a 1% per annum management fee with no extra costs for you with total clarity (remember that even management fees are waived if performance fees exceed them in any given year). And unlike my investors, most of my capital is invested in the fund, so in case I need to fund the management company during any particular year, I will need to perform a small withdrawal from my investment in the fund. That is the main reason why I created the Class B shares, lastly of course I want to optimize the fees and ensure my investment does not incur in fees.

With that being said, I have set aside on a personal level of cash that would allow me to fund Arauca for many years even if I did not have a single external investor. I would not expect at all to take from the fund, but I need to have the flexibility.

Why does Arauca have a two-year lock-up period?

The two-year lock-up period is a way for me to filter the right type of investor and identify the wrong ones before it is too late. As I mentioned, we will have challenging times in the markets, volatile periods and if my investors are not aligned, they can make mistakes and make me make mistakes. In order for me to protect our capital, I need to have the right type of investors only.

The fund opted not to have a license, what does that mean?

Arauca Capital is a Dutch investment company registered with the AFM, the Dutch Financial Regulatory Authority. According to the AFM rules under De Minimis (or simplified) AIFMD regime, Arauca Capital can only accept qualified investors who can invest a minimum of the equivalent of EUR 100,000.

**Attention! This investment falls outside AFM supervision.
No license and no prospectus required for this activity.**



ARAUCA CAPITAL

Alternative Investment Funds can opt to not have a license if the AUM are less than 100 million EUR, if the fund is not actively marketing and if the number of investors does not exceed 125. By not having a licence our yearly costs are a third of what they would be if Arauca was licensed. At the current size of the fund, the license is of no use for Arauca and most importantly I do not want higher expenses nor charging higher fees to you.

For this reason, you find the respective disclaimer at the bottom of each page.

You know people who might be interested in Arauca, can you tell them?

If you think they fit to Arauca's philosophy, of course I would appreciate you let them know.

**Attention! This investment falls outside AFM supervision.
No license and no prospectus required for this activity.**



Important Information – Disclaimer

This letter has been prepared by Arauca Capital B.V. ("Arauca") solely for providing background information to the person to whom it has been delivered. Arauca Capital B.V. is the manager of Arauca Capital Fund, which is a non-licensed fund manager registered in The Netherlands under the Alternative Investment Fund Managers Directive (AIFMD) light regime. The information contained herein is strictly confidential and is only for the use of the person to whom it is sent. This document is not to be reproduced, distributed, or published by any recipient for any purpose without the prior written consent of Arauca. Arauca Capital Fund is only available to qualified investors that are not resident in the United States of America. This information is not intended to provide and should not be relied upon for accounting, legal or tax advice or investment recommendations. You should consult your tax, legal, and accounting or other advisors about the issues discussed herein. Material terms of the Fund are subject to change. Any prospective qualified investor will be provided with a copy of the Fund's Information Memorandum to review the documentation relating to the offering.

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>

Light regime managers such as Arauca Capital B.V. have no license, and no prospectus is required for this activity.

Prospective investors should review the Information Memorandum, including the risk factors section, before deciding to invest.

In addition, prospective investors should rely only on the Information Memorandum when deciding to invest, although certain descriptions contained herein may be more detailed than those contained in the Information Memorandum. Past performance is no guarantee, nor does it indicate future performance. Subscriptions may only be made on the terms of the Information Memorandum and subject to completion of a Subscription Form and the approval of the Fund Manager. This document is not intended as an offer or solicitation with respect to the purchase or sale of any security. This document is not intended for distribution to or use by any person or entity in any jurisdiction or country where such distribution or use would be contrary to local law or regulation. This document is not intended for distribution in the United States of America. Opinions expressed herein correspond only to those of the Fund Manager and are subject to change without notice.

All rights reserved, Arauca Capital B.V.

**Attention! This investment falls outside AFM supervision.
No license and no prospectus required for this activity.**

