



Bumbershoot Holdings LP
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Dear Partners,

Bumbershoot Holdings struggled to keep pace in 2019. Our fourth full-year of operation saw a gain of +13.5%, marking our first period of clear underperformance.

Our biggest investments didn't quite deliver in a year when everything else worked—as the market produced *extraordinary* gains via multiple expansion.

This has left me *out of sync*—and on many days, I find myself feeling a bit like Tom Hanks from the late '80s classic, *Big*. There is [one scene](#) in particular, at the end of an internal marketing meeting about *Transformers* action figures' sales, where he innocently raises up his hand and asks, “*I don't get it.*”

“*Well, if you had read your industry breakdown, you would see that...*” the Fed is in control. Interest rates are at historic lows—there is no alternative to equities. Too much liquidity is chasing far fewer durable profits. Technology businesses operating under a different set of scalar economics. Trade disputes put at ease for sake of an election year. A confident consumer with jobless rates at a 50-year low. Momentum in stocks. HODL!⁵

“*Oh.
... I still don't get it.*”

I'm not here to say whether that is right or wrong, but something doesn't add up. There is a *logical fallacy* in our midst—as the code of the market doesn't compile. This is not value vs. growth. It is not about political or social issues. It's valuation.

By Month:	Bumber	S&P ¹	Russell ²	FTSE ³	Barclay ⁴
Jan-2019	6.41%	7.87%	11.25%	3.58%	3.64%
Feb-2019	3.20%	2.97%	5.20%	1.52%	1.25%
Mar-2019	2.29%	1.79%	-2.09%	2.89%	0.61%
Apr-2019	-2.07%	3.93%	3.40%	1.91%	1.15%
May-2019	-4.62%	-6.58%	-7.78%	-3.46%	-1.72%
Jun-2019	5.12%	6.89%	7.07%	3.69%	2.11%
Jul-2019	-0.05%	1.31%	0.58%	2.17%	0.48%
Aug-2019	-5.10%	-1.81%	-4.94%	-5.00%	-0.96%
Sep-2019	3.68%	1.72%	2.08%	2.79%	0.32%
Oct-2019	1.09%	2.04%	2.63%	-2.16%	0.71%
Nov-2019	-0.48%	3.40%	4.12%	1.35%	0.99%
Dec-2019	4.01%	2.86%	2.88%	2.67%	1.69%

Bumbershoot Holdings L.P.

2019 Performance

		S&P ¹	Russell ²	FTSE ³	Barclay ⁴
FY-2019	13.50%	28.88%	25.52%	12.10%	10.65%
Inception	66.62%	80.13%	60.92%	30.53%	25.08%



It turns from a software company into a robot, right?
Well, what's fun about that?

If the goal was just to pick growing business models—there is no shortage of “quality” companies. But if the goal is to actually make money, then there is an issue underwriting returns in today's current environment. Capitalizations are not arbitrary or abstract. It is the sum-total of cash flow discounted back to this exact present moment. The lights flash on in brief glimmers to guide that equation, but the “truth” is only known *ex post facto* through dividends, or being stopped out via acquisition or in bankruptcy.

That equation seems *off* in the *absence* of significantly higher inflation rates; yet a significant reflation would throw a wrench into all those others factors. *Years and years of growth... itty bitty little discount rate.*

There are too many companies existing in a world that is markedly different from the current reality.

You have to get it right on price too.

I believe in our process—it has demonstrated success in finding significant outperformers. Identify the right opportunities... and take advantage when they arrive. We have huge potential and our best is yet to come.

Performance

Bumbershoot Holdings L.P. generated a positive gross return of +13.50% for the full-year 2019.

The partnership has a *cumulative* total gross return of +66.62% since inception in Oct-2015.

Looking more closely at performance, monthly returns directionally correlated with the market indices, albeit with a slight erraticism layered on by the volatility and breakdown of our most sizable positions.

From an investment perspective, while our two largest positions, **Intrepid Potash** (*IPI:NYSE*) and **Viking Therapeutics** (*VKTX:NGS*) showed little for the year, a number of slighter positions performed quite well.

Investment activity is categorized into five segments—*Core, Micro, Value, Special Situation, Discretionary*—although as previously noted, the line between certain categories can blur, making it difficult to attribute the P/L contribution of each strategy. My best estimate of performance for each category in 2019 is as follows:

By Category:		By Market Cap:	
Core	9.5%	Large	2.7%
<i>Core - Long</i>	11.1%	Mid	3.5%
<i>Core - Short</i>	-1.7%	Small	5.0%
Micro	1.3%	Micro	1.9%
Value	0.6%	Fx	0.2%
Special Situation	0.6%	<u>Misc</u>	<u>0.2%</u>
Discretionary	1.2%	FY-2019	13.5%
Fx.	0.2%		
<u>Misc.</u>	<u>0.2%</u>		
FY-2019	13.5%		

Core gains were led by **PDF Solutions** (*PDFS:NGS*), **FormFactor** (*FORM:NGS*), **Micron** (*MU:NYSE*), **Alphabet** (*GOOGL:NYSE*), **Barrick** (*GOLD:NYSE*), **Weyerhaeuser** (*WY:NYSE*), and **KVH Industries** (*KVHI:NGS*) among others.

Detracting from performance was *short positioning* of any-and-all kind; and also *Energy* sector investments including **Cimarex** (*XEC:NYSE*) and **Intrepid**.

Micro was lifted by **PFB** (*PFB:TSX*) and **Carmanah Technologies** (*CMH:TSX*), the subject of last year's case study. An investment in **Kathmandu Holdings** (*KMD:ASX*), courtesy of Samir Patel from *Askeladden Capital*, also added nicely; and various other positions such as **Charles & Colvard** (*CTHR:NCM*), **Rudolph** (formerly *RTEC:NGS*), **Graham** (*GHM:NYSE*), and **iCAD** (*ICAD:NGS*) helped round out the balance.

Value category registered a gain primarily attributable to **Adams Resources** (*AE:NYSE*).

The *Special Situation* category received a bump after **Fitbit** (*FIT:NYSE*) announced its deal to be acquired by *Alphabet/Google*. While disappointed by the final offer, we'd been positioned for a binary outcome in the company for over a year—substantially increasing the equity portion at “distressed” prices over the summer. Similarly, **Zagg** (*ZAGG:NGS*) is another takeover play that added to results. The company announced that it had retained *BoA* to explore strategic alternatives and a formal process has been underway since August. The portfolio also benefited from a rather timely addition of **Orion Group** (*ORN:NGS*) after being booted from the *S&P SmallCap 600* index in May-2019.

In general, the *Core* category remains below targeted exposure levels, while *Non-Core* categories remain at-or-above target weightings of ~5% AUM, respectively.

Case Study – PFB Corp.

Similar to last year, I'd like to take this opportunity to provide partners with a "case study" about one of the fund's investments: **PFB** (*PFB:TSX*).

PFB is a *foam* business.

Headquartered in Calgary, it is a niche manufacturer of *expanded polystyrene* (EPS) foams, which are used for rigid insulation products. It recently celebrated its 50-year anniversary, as detailed in this [catchy video](#).

Looking at its operations more closely, *PFB* employs a "*molecules to mansions*" strategy, which relies heavily on vertical integration—a hallmark of the company. It produces its own EPS resin/beads by polymerizing the hydrocarbon monomer *styrene* at its Crossfield plant.

It steam-molds these into rigid foam boards within its *Plasti-Fab* division. Boards are cut into sheets and sold in North America through retail distribution in home improvement stores like *Home Depot* & *Lowe's*.

EPS resin can also be formed into rigid blocks, which serve as the form for cast-in-place concrete. This is its *Advantage ICF System* business, which manufactures insulating concrete forms (ICF). It can also attach rigid insulation sheets to plywood/OSB to create structural insulated panels (SIPs) for custom installation, which it does through its *Insulspan* subsidiary.

It takes this one step further through a *Custom Homes Group*, which under a handful of design houses/brand names, creates beautiful mountain-style log & timber homes. Designs tightly integrate the exterior structural "envelope" of the home—with all necessary insulation & paneling being specified-in. *Hence the mantra*.

That is also how I sourced the idea.

Investors typically want to understand the process for generating ideas—but are often dismayed to hear that it is a somewhat haphazard development. While it will typically start with a high-level, secular growth theme, the path to finding a specific company investment that backs into a theme can be a bit like catching lightning in a bottle.

The *theme* in this case is the long-term sustainability and recovery in housing development, combined with a trend towards energy efficiency, etc.

The *lightning in a bottle* was ordering a free brochure from [PrecisionCraft](#) in Dec-2008. I'd just started work at *CJS Securities*. I was making \$3k/month and not in line for any sort of bonus. So, may as well brush up on my technical knowledge of log & timber cabins.

I loved that book though. The designs were *spectacular* and I'd glance at it from time to time... thinking about the mountains. *Hey, a guy can dream...*

I discovered it again as I was clearing out my desk in 2015, prior to launching *Bumbershoot* and realized it was actually part of a tiny, public company in Canada called *PFB*. I watched a [video interview](#) with the CEO that was part of a series produced by the TSX exchange called *View from the C-Suite*. (Coincidentally this also linked to another video from the series, which is how I learned about *Carmanah*. Lightning struck twice.)

The rest is history.

Bumbershoot purchased its initial shares shortly after launching the fund, establishing a bookmark position of ~5bps in Nov-2015. This was expanded throughout 2016 to approx. 20-25bps; and then more dramatically stepped up to ~80bps in Feb-2017, at an average cost of just below C\$9.05. Allocated to the *Micro* category, this made it one of the largest positions within that "portfolio-within-a-portfolio," representing 15% of the target weighting (~5%+ AUM) for the strategy.

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Turning to the financials, *PFB* is relatively efficient at converting sales to profitability. EBITDA margin is in the ~12% range, with opportunities to further leverage that foundation at greater scale.

It is conservatively managed. The balance sheet is in a net cash position. Insiders have maintained significant ownership since 1982; and valuation is not particularly demanding. Shares trade for only ~10x adjusted EPS, which equates to ~5x on an EV/EBITDA basis.

The investment has done fine by our partnership. Since our initial purchase, *PFB* raised its quarterly dividend by 50%. It paid a special dividend of C\$1.00 per share in Nov-2019, equivalent to 11% of our initial cost; and the market price has also appreciated by nearly 45%.

I suspect more to come in the years ahead.

Investment Outlook

From an economic perspective, it seems little is going to get in the way of the sustained expansion.

The mid-year “adjustment” by the *Federal Reserve* was by far the most important change to the outlook. While I suppose it is good news to avoid a slowdown and risk ending the momentum, it does also feel like it may be creating a much larger problem on the tail-end.

But that’s a future Fed Chair problem.

From a stock perspective though, it feels like valuation has run its course. Multiple expansion can only take it so far—investors still require value. That doesn’t mean traditional “value investing” as a discipline. It means real value. Getting more than what you paid... because otherwise it’s just a bad investment.

At a minimum, I’d expect it to be a much more tactical year than 2019.

Our investment process is company-specific, based on unique, fundamental characteristics of the underlying businesses. These traits can then be applied to fit broad secular themes.

I like how our portfolio is positioned; and believe that we are invested in companies that will perform well.

Administrative

From an administrative perspective, it continues to be much the same story. While it may look effortless, it is a ton of hard work behind the scenes.

From a marketing standpoint, while we welcomed new partners into the fund, it has been a slow & frustrating process to raise assets. We have had many “observers” since launching; and I am optimistic for some to come off the sidelines in the new decade.

As I said last year, referrals are also the *lifeblood* of this industry. Your support to introduce the fund to any new capital partners is enormously appreciated.

Taxes

Tax form-*Schedule K-1* for the 2019 calendar year have been prepared. Copies will be sent to each LP.

As a reminder, 2019 was a transition year for the fund. We implemented a “master feeder” structure over the course of the year to pass back long-term gains to the original fund. Along with every partner, I look forward to a much more efficient & advantageous tax strategy; and anticipate minimal taxable gains in 2020.

Summary

To leave off, I’d just remind all partners that the focus of *Bumbershoot Holdings* is on maximizing long-term returns. That objective is centered on our ‘*quality over quantity*’ philosophy to investing, which relies on deep fundamental analysis. Patience & discipline remain the foundation for our continued success.

I am incredibly grateful for the opportunity to manage your money and take that responsibility extraordinarily seriously. I am proud of everything we’ve accomplished to date and continue to have the vast majority of my personal net worth co-invested in the partnership.

In late December, I made a detailed list of *New Years’* resolutions/goals. One of my goals is to take more risk professionally. Now don’t be alarmed. I don’t mean in the portfolio in terms of any change to our investment process. But I do mean professionally.

Publish research. Raise money. Put more out there.
Our partnership is ready to take its next step forward.

Sincerely,



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¹ S&P 500 Index --
<https://performance.morningstar.com/Performance/index-c/performance-return.action?t=SPX®ion=usa&culture=en-US>

² Russell 2000 Index --<http://www.ftserussell.com/index-series/index-tools/russell-index-performance-calculator>

³ FTSE 100 Index --
<http://performance.morningstar.com/Performance/index-c/performance-return.action?t=UKX®ion=gbr&culture=en-US>

⁴ BarclayHedge Hedge Fund Index --
http://www.barclayhedge.com/research/indices/ghs/Hedge_Fund_Index.html

⁵ 'HODL' is a beloved cryptocurrency term, which originated from a misspelling of hold/holding. It has since taken on the backronym of "Hold on for dear life"—with the implication to just hold through anything.

⁶ Optimus Prime --<https://www.youtube.com/watch?v=gx...>

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Long IPI, VKTX, PDFS, MU, GOOGL, GOLD, WY, KVHI, XEC, PFB.ca, CTHR, GHM, AE, FIT, ZAGG, ORN*