



## IMMERSION INVESTMENTS

### CONFIDENTIAL – DO NOT DISTRIBUTE

Immersion Investment Partners, LP  
4Q 2023 Partners Letter  
January 2024

### Net Returns as of December 31, 2023

	ITD <sup>(1)</sup>	2023	4Q23
Immersion Investment Partners, LP Net	-17.32%	34.69%	13.62%
Russell 2000 Index	-7.35%	16.93%	14.04%
MSCI Europe Small Cap Index <sup>(2)</sup>	-15.71%	17.34%	14.84%
Russell Microcap Index	-19.34%	9.33%	16.06%

(1) Inception to Date measures from fund launch date of 6/1/2021

(2) iShares MSCI Europe Small Cap ETF

Unaudited; assumes 2% management fee and 20% performance fee

*See disclaimers*

Dear Partners,

Immersion Investment Partners, LP returned 34.69% in 2023 vs. 16.93% for the Russell 2000 Index. Please check your individual statements for your quarterly and annual returns.

There is a great irony, accompanied by mild frustration, in Immersion's investing strategy. We are constantly looking for companies that are being mispriced and frequently overlooked by the market, but once we discover one, we are often cursing how long it takes for other investors to notice what we have seen. A joke we have thrown around internally is "Wow, look at this company that has been mispriced for a long time but now has a catalyst for change. Let's invest in it." <Wait for subsequent earnings reports where the company does exactly what we thought they would do, yet the market ignores them.> "I can't believe the market is not rewarding this company that they have ignored and left for dead for years!" OK, so we are not comedians, and the joke may be a little niche, but the point is that financials matter and management execution matters. At some point, the continued execution of a management team cannot be ignored by the market.

The longer it takes for a company to be recognized by the market as a winner, the more potential energy is stored in the stock. We visualize this dynamic as a spring which is coiled tighter and tighter as more positive news flows out of the company and is stored in the stock price. At some point, the potential energy is converted to kinetic energy, and the stock price moves up violently. As we have written in past letters, focusing on what the company is accomplishing is much more valuable than the fluctuations of the stock price, which is not to say stock price is not important.



## IMMERSION INVESTMENTS

While several of our contemporaries will claim they do not pay attention to the stock price, as stewards of your money, of course we are watching the stock price. What we are paid to do is discern what is being projected by a stock price: noise, opportunity, or caution.

The most common output from stock price action is simple noise. Stock prices move up and down for generally no discerning reason other than there are more buyers than sellers or sellers than buyers on a given day. 95% of the time, there is nothing to do when noise is the prevailing storyline other than take advantage of small movements within the price. However, a sharp rise or drop in price, without any catalyst, will cause an investigation.

Without any obvious news or events to move a stock, we look at the volume and, if identifiable, the buyer or seller that caused the move. Often these large moves are not based on company performance itself, but rather a factor trade (where an investor is trading a company based on certain current financial metrics, geography, size, or industry, rather than company-specific attributes), perceived macro issues, or the personal needs of the investor – estate planning issues, etc. These moves based on no information offer us the opportunity to add to a position at a lower price or sell at a higher price. We are highly valuation conscious but are admittedly more reluctant to sell because of a move to the upside.

Large opportunities can also arise from a stock price doing nothing at all. Those that argue in favor of the efficient market theory believe that all publicly available information is already priced into a stock. We wholeheartedly and vehemently deny this assertion – particularly in the sub \$5 billion market cap arena where we invest. We have seen countless examples where an opportunity is created when one of our companies will report fantastic earnings after market close, and when the market opens the following day, the stock does not move for several hours. We are often able to add more to the position and then be rewarded in a short amount of time as the market plays catch-up. On the flipside, we can exercise caution where a company has issued a press release or reported poor earnings and something has gone awry with its business plan, and inexplicably it will take the market time to realize the stock should not be valued as highly as it currently is trading. At this point we decide if this is a short-term issue or something that is fundamentally detrimental to our investment thesis which would require us to sell ahead of the drop or add more to the position if the negative news is transitory.

We are proud of our 2023 performance and to see several of our coiled springs finally explode to the upside. We are equally pleased that we were able to generate this performance even though Celsius, which ended the year as our largest position, did not participate in the fourth quarter rally.

Before we get into portfolio updates, we have a few administrative items. Our audit has been completed and issued to us. We will distribute it shortly. Further, we anticipate K-1s to be completed in advance of April 15. Lastly, please be on the lookout for a save-the-date to our annual partners meeting, which we will hold (virtually) in March.



## IMMERSION INVESTMENTS

### Portfolio Updates:

At the time of writing (late January 2024), we hold fourteen positions ranging in market capitalization from \$30 million to \$13 billion and a median size of \$700 million. We exited several names in the quarter, using the proceeds to add to existing positions, and did not initiate a meaningfully sized new holding in the partnership in the last six months of 2023. Our five largest investments (*alphabetical*: Bel Fuse, Celsius, eDreams Odigeo, Griffon, and Potbelly) make up 64% of NAV.

Since we provided detailed thoughts on Bel Fuse and Celsius in our previous letter, we will provide updates on **eDreams (EDR.MC)**, **Griffon (GFF)**, and **Potbelly (PBPB)**.

#### **eDreams Odigeo (EDR.MC – Ugly Duckling)** – *all numbers discussed are in euros*

eDreams remains dramatically undervalued even as it marches towards its FY2025 goal for 7.25 million subscribers and 180 million euro in cash EBITDA. The stock performed quite well in 2023 but has been broadly flat for the past two years. As we highlighted in our first partner letter in 2021, and in subsequent updates, eDreams is on a journey of becoming the first subscription-led online travel agency (OTA). This program has seen tremendous growth since its initial launch in 2017, from a standing start to 5.1 million members at the end of September (EDR's fiscal second quarter). The subscription program, eDreams Prime, is a win-win for consumers and the company. Customers receive exclusive discounts on flights and hotels as well as priority customer service. The company benefits from a direct customer funnel, circumventing middlemen like Google and metasearch engines, and it provides them with a steady stream of recurring cash flow. Today, nearly 60% of bookings are performed through a mobile device (a proxy for direct bookings because customers tend to perform Google and meta search for flights on a desktop) vs. a third at the time of Prime's launch. And the company's EBITDA and cash generation has smoothed considerably.

The company delivered expectation-beating results again in its fiscal second quarter (ending September 30<sup>th</sup>), with revenue and adjusted EBITDA up 19% and 66%, respectively. Germane to the bull case for eDreams, we have witnessed a substantial improvement in year-to-date percentage margin and cash generation. For the first six months of the fiscal year, reported operating profit swung to 18.2mm vs. a 15mm loss in the prior-year period. Adjusted EBITDA margin rose an impressive 660 basis points, to 17.5%. Free cash generated improved from 5.5mm (1.7% margin) in the first half of fiscal 2023 to 50.7mm (14.0% margin). We foresee 140mm in adjusted EBITDA and 100mm in free cash flow for fiscal 2024 vs. an enterprise value and market capitalization of 1.2 billion and 890 million, respectively. A >10% free cash flow yield on a business like eDreams, which is dramatically shifting its business to a recurring revenue model accompanied with significant margin expansion potential, is extremely inexpensive. Should the market continue to ignore these dynamics, we see the initiation of a buyback and/or a strategic review as a very real possibility sometime over the next twelve months.



## IMMERSION INVESTMENTS

### **Griffon Corp. (GFF – Social Pariah)**

We initially purchased Griffon as a Social Pariah. The business is high quality, but the stock suffered from poor investor perception due to lackluster governance and capital allocation. We also benefited from an ongoing strategic review process that could have resulted in a partial or full sale of the business. The process ended without the company taking any action and elected to increase its buyback authorization by \$200mm and pay a \$2.00/share special dividend. Regardless, we've wound up better off because few acquirers would have been willing to pay the current share price for the business a year ago. Since then, execution has been strong and capital allocation has improved (accelerated buybacks over M&A). Notably, there have been significant strides made on the corporate governance and executive compensation front. The board has been declassified and the percentage of voting power required to call a special meeting has been reduced to 25%. Further, since fiscal 2021, total executive compensation for its four named executive officers has declined 27%.

In our previous letter, we bemoaned the market's unwillingness to assign the company a real valuation multiple, due to the widespread belief that the garage door segment (Homebuilding products – HBP) margins would mean revert. We noted that there have never been widespread price cuts amongst garage door manufacturers. Investors are coming around to our side after management guided HBP EBITDA margin for 2024 "to be in excess of 30%" on its fiscal fourth quarter (ending September 30<sup>th</sup>) call on November 15<sup>th</sup>. This was a surprise for many on both the buy-side and sell-side. Deutsche Bank, which initiated coverage of the stock just two weeks prior to the fourth quarter report, had estimated a 29% margin for the HBP segment in 2024, and, based on our conversations, we know many on the buy-side had assumed a reversion to the high-teens/low-twenties. This strong guidance, coupled with some dovish federal reserve commentary (we don't think repair and remodel spending vis-à-vis garage doors are "discretionary" so much as they are "necessary", and thus effected by rates, but that's a different topic) sent shares up 54% in the fourth quarter. Even after such a strong performance, we believe there is still further upside to results and the shares. The consumer products division (CPP) is undergoing restructuring and is significantly underearning (sub-5% margins vs. up to low-teens historically). And although HBP has been the star of the show, most of the improvements in operating results have been price and mix driven; volumes have declined for each of the past two years. Any volume recovery in the market should provide further upside to the business. Lastly, shares remain cheap, trading at roughly 10x EBITDA and 14x GAAP earnings, slightly under its own long-term averages and a discount to peers.

### **Potbelly (PBPB – Underdog)**

Potbelly continues to execute on its turnaround with a new management team led by former Wendy's COO Bob Wright. In November, the company reported strong third quarter results, handily beating the company's restaurant-level and EBITDA guidance provided on the second quarter earnings release. With each location averaging \$1.3 million in annual sales and nearing mid-teens store-level operating margins, both of which are best-in-class for sandwich concepts,



## IMMERSION INVESTMENTS

we believe that the brand is extremely well-positioned to attract high-quality franchisees. To that end, Potbelly announced 150 total location commitments in its third quarter earnings press release. Shortly thereafter, Potbelly announced a 13-restaurant deal in the Seattle-Tacoma area. On January 8, the company announced preliminary fourth quarter results, again beating the company's guidance. Simultaneously, they updated the new location commitment figure to 192. Based solely on current commitments and the existing estate, we see line of sight to \$40 million of EBITDA and over \$1.00 in free cash flow per share vs. a current enterprise value of \$350 million and share price of \$12.50.

The investment narrative surrounding Potbelly is rapidly shifting from one of a low-end, regional company-operated concept to a fast-growing, franchised business with national scale. Despite the terrific progress on the turnaround, which includes eight consecutive quarters of beating guidance, right sizing the chain's unit economics, and accelerating franchise development, Potbelly still trades at a discount to its peers, none of which can match it in terms of forward-looking franchise unit growth. The one exception is Wingstop, the leading SMID-cap restaurant concept, which trades for a sky-high 55x EBITDA vs. Potbelly at 11x EBITDA. Potbelly has miles to go before anyone would be willing to assign a Wingstop-type multiple (if ever) but at a minimum, execution to date merits at least a peer multiple, if not a slight premium. Until such a time passes, we foresee roughly 20% annual growth in free cash flow per share.

We appreciate your trust and support and remain aligned with almost all our personal liquid net worth invested alongside you. Please feel free to reach out with any thoughts or questions.

Sincerely,

David Polansky

Tim Delaney



## IMMERSION INVESTMENTS

### Glossary – Ideal Immersion Setup (IIS)

#### 1. The Underdog

The Underdog is overlooked and underappreciated by most investors. Generally, there are surface level reasons for being dismissed, which are transitory and serve as an impediment to ownership. For example, The Underdog is too small for many institutional investors to even consider and/or does not belong to a major market index such as the Russell 2000. This generally correlates to thin or no analyst coverage and little-to-no institutional ownership. Ultimately, this issue is corrected through a combination of continued growth, improved liquidity, and/or increased analyst coverage.

#### 2. The Babushka Doll

The Babushka Doll has a hidden asset (or assets) inside of it that could be worth significantly more than the value being assigned to it by the market. The typical Babushka Doll takes the form of a large, legacy, no-growth business presently dominating the financials on the outside, but it contains a small, scrappy, subsidiary growing rapidly on the inside. Babushka Dolls are often overlooked investment opportunities because they do not screen well on surface level quantitative statistics of growth and/or profitability. Aligning ourselves with a management team willing to dedicate resources towards unlocking the value of the “hidden asset” can generate significant returns.

#### 3. The Social Pariah

The Social Pariah is perceived to be a toxic asset by investors because the business is either misunderstood and/or suffering from transitory issues. Often The Social Pariah is labelled toxic for good reason but a change in that perception, due to better performance, management turnover, etc. can result in significant stock price appreciation.

#### 4. The Ugly Duckling

The Ugly Duckling is a fundamentally good business which is not readily apparent in the financials due to significant investments in people and capital, which are masking underlying profitability. The Ugly Duckling is usually a sub-scale business early in its lifespan and growing rapidly. Over time, as the business grows up, investors will come to appreciate The Ugly Duckling and afford it a higher value per dollar of earnings. The Ugly Duckling, of course, turns into the swan.

#### 5. The Doubted Champion

The Doubted Champion is a simple but effective investment. This type of business is one that is growing rapidly and exhibits strong financial characteristics (margins, returns on capital, etc.) but the market does not expect its performance to sustain. In other words, its further growth may be overly discounted. If we can correctly identify a Doubted Champion, we will be handsomely rewarded when the market realizes that the business can continue growing at an accelerated rate for far longer than originally anticipated.





## IMMERSION INVESTMENTS

### Important Information

Certain statements made have not been audited or verified by the Fund's auditor or third-party administrator. Please see your individual statements for your performance. Adjusted/modified performance disclosures are intended to give deeper insight into the Fund's performance but should never be substituted for actual net results, as reported by the administrator, and reflected in audited financial statements.

Results are compared to the performance of the Russell 2000 Index, iShares MSCI Small Cap Europe ETF, and Russell Microcap Index (the "**Comparative Indices**") for informational purposes only. The Fund's investment program does not mirror the Comparative Indices and the volatility of the Fund's investment program may be materially different from the volatility of the Comparative Indices. The securities included in the Comparative Indices are not necessarily included in the Fund's investment program and criteria for inclusion in the Comparative Indices are different than criteria for investment by the Fund. The performance of the Comparative Indices reflects the reinvestment of dividends, as appropriate.

The Immersion Investment Partners, LP Net Returns reflects the USD investment performance of an investor that committed capital at inception of the Fund (June 1, 2021) and is subject to a 2% management fee and 20% performance fee. Net returns will vary by investor. Each partner will receive individual statements showing returns from the Partnerships' administrator. Performance returns are estimated pending the year-end audit. Past performance is not indicative of future results. Actual returns may differ from the returns presented. The portfolio is under the sole trading authority of the general partners. A portion of the trades executed may take place on non-U.S. exchanges.

This material does not constitute an offer or the solicitation of an offer to purchase an interest in Immersion Investment Partners, LP (the "Fund"), which such offer will only be made via a confidential private placement memorandum (the "Memorandum"). An investment in the Fund is speculative and is subject to a risk of loss, including a risk of loss of principal. There is no secondary market for interests in the Fund and none is expected to develop. No assurance can be given that the Fund will achieve its objective or that an investor will receive a return of all or part of its investment. All statements herein are qualified in their entirety by reference to the Memorandum, and to the extent that this document contradicts the Memorandum, the Memorandum shall govern in all respects.

This material is confidential and may not be distributed or reproduced in whole or in part without the express written consent of Immersion Investments (the "Investment Manager"). This material is not intended to provide, and should not be relied on for, tax, legal, or accounting advice. You should consult your own tax, legal, and accounting advisers before engaging in any investment transaction.

This report contains views and opinions which, by their very nature, are subject to uncertainty and involve inherent risks. Predictions or forecasts, described or implied, may prove to be wrong and are subject to change without notice. Investment processes are subject to change without notice. Any portfolio risk management processes discussed herein are an effort to monitor and manage risk but should not be interpreted as and do not imply low risk or the ability to control risk. References to investment objectives, targeted returns or other goals that the Investment Manager seeks to achieve are aspirational only and should not be considered a prediction or guarantee that such results will be achieved.

The Investment Manager takes care to ensure the information provided in the report is accurate at the date of publication. However, it is provided without warranties of any kind, either expressed or implied.

**PAST PERFORMANCE IS NOT NECESSARILY INDICATIVE OF FUTURE RESULTS.**