KP7

April 8, 2022
Letter #4

Dear Friends and Investors:

We added materially to our position in Kneat.com in the first quarter. Kneat designs and sells software to assist companies in highly-regulated industries manage regulatory data and documents.

The KP7 portfolio consists of twenty to thirty high-conviction investments exposed to a handful of favorable long-term investment themes. Our investment in Kneat lies in our Productivity-Enhancing Software theme. Just as word processing software replaced the typewriter and fundamentally changed the way we create documents, companies like Kneat are replacing old-school processes and procedures by offering software with compelling value propositions centered on improvements in productivity.

Kneat's customers report a 50% or more reduction in cycle time and a similar reduction in man-hours associated with validating manufacturing machines in the pharmaceutical industry. Every process, piece of equipment, and computer system in the manufacturing of pharmaceuticals needs to be validated and documented according to specific regulations. Regulators like the U.S. Food and Drug Administration conduct unannounced inspections of equipment, files, and documents to make sure the companies that make our medications make them according to their strict standards.

Historically, all the various sign-offs and protocols associated with validations were based on physical documents. Kneat's software digitizes the entire process from end-to-end, eliminating the need to store and handle hardcopy documents.

Kneat's process is not only cheaper to implement and maintain, but also results in a better product versus keeping hardcopies. Files can be searched and sorted with a stroke of a key. We believe the machine validation business could standardize around Kneat's technology. Eight of the top ten global pharmaceutical companies and sixteen of the top twenty have already signed on with Kneat's platform.

Separately, the bifurcation in the stock market we described in our last letter continues: expensive large capitalization stocks that get a bid from passive investment funds in one group and relatively cheap stocks that don't in the other. We are finding decent investment opportunities in the latter group. We initiated a position in The Children's Place in the first quarter, a company we believe is trading for just 5 times earnings and generates free cash flow equal to a fifth of its market capitalization every year. That's the kind of value we like.

Our portfolio lost 0.3% in the first quarter, versus a total return on the S&P 500 of negative 4.6%. Since the inception of our fund in July of last year, we are up 1.1%, versus the S&P 500 of +6.5%.

All the best to you and your families,