MIDWAY PARTNERS

CAPITAL MANAGEMENT

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midwaypartnersllc.com

September 30, 2021

Re: First Calendar Quarter

Dear Partners:

We have completed our first calendar quarter representing two months of active investing. This letter will serve as the first in our normal cadence to be distributed following the end of each calendar quarter.

With two months under our belt, we have invested approximately 50% of the capital from July subscriptions across eight long-equity positions. Several of these positions saw their prices swing up and down throughout the month. We expect to add to these positions over time should prices move in our favor (downward) as we build our focused portfolio. We continue to use our put writing strategy against a portion of our cash balance as mentioned in the prior letter.

Asset Prices

On September 12th the Wall Street Journal ran an article titled, "The Stock Market Fails a Breathalyzer". In the article, price comparisons are made between a variety of companies. At the time, Joby Aviation (an air taxi company with no revenue) had a higher market capitalization than Deutsche Lufthansa, easyJet, or JetBlue Airways. Carvana (a used car ecommerce platform) was priced higher than Ford Motor Co., Honda Motor Co., Hyundai Motor Co., or Volvo. Airbnb (an online vacation rental marketplace) was priced higher than Hilton Worldwide Holdings and Marriott International combined. Coinbase Global (a crypto currency trading platform) was priced higher than Nasdaq. The table below shows a selection of the comparisons described in the article based on September 30, 2021 prices, with the high-priced companies highlighted at the top of each group. Robinhood Markets (a commission-free stock trading platform) was added to the list and had a higher price than Interactive Brokers Group or MarketAxess Holdings. One does not have to look hard to find instances of market drunkenness as the article implies.

Exemplar Pricing Hysteria

As of September 30, 2021
USD in millions

Company	Market Capitalization(1)	Enterprise Value	TTM(2) Revenue	TTM(2) EBIT
Joby Aviation	$6,075	$6,075	$0	($3)
Deutsche Lufthansa	$8,225	$27,478	$13,146	($5,417)
easyJet	$6,748	$8,157	$1,132	($1,685)
JetBlue Airways	$4,940	$5,612	$3,385	($1,949)
Carvana	$53,261	$56,157	$8,951	($82)
Ford Motor Co.	$57,575	$162,774	$136,433	$2,319
Honda Motor Co.	$53,478	$95,568	$137,350	$9,550
Hyundai Motor Co.	$43,963	$93,297	$100,839	$3,954
Volvo	$45,793	$52,179	$41,781	$4,783
Airbnb	$118,702	$113,242	$4,424	($2,993)
Hilton Worldwide Holdings	$37,473	$45,245	$4,054	$195
Marriott International	$49,145	$58,262	$9,913	$1,608
Coinbase Global	$59,434	$56,298	$4,930	$2,286
Nasdaq	$32,788	$37,800	$5,941	$1,519
Robinhood Markets	$39,188	$32,476	$1,680	($1,863)
Interactive Brokers Group	$26,672	$43,223	$3,009	$2,121
MarketAxess Holdings	$16,184	$15,771	$708	$370

Note: In USD based on exchange rates as of October 7, 2021 where applicable
(1) Market capitalizations may differ based on calculations of fully-diluted shares
(2) Most recently reported trailing twelve months

We know little about each of the companies flagged above and thus cannot determine whether these prices are justified. Also, the companies used for contrast may not provide relevant comparisons. Given the lack of profitability with most of these highflyers, what we can determine is that their prices are based on significant future growth and distant cash flow profitability. We all know that the more distant the future cash flows the less valuable they are to investors today. This fact is illustrated in the table below for cash flows received one to ten years in the future at rates of return between 8% and 12%.

Present Value of $1 of Future Cash Received

Rate of Return	Received in Year 1	2	3	4	5	6	7	8	9	10
12%	$0.89	$0.80	$0.71	$0.64	$0.57	$0.51	$0.45	$0.40	$0.36	$0.32
11%	$0.90	$0.81	$0.73	$0.66	$0.59	$0.53	$0.48	$0.43	$0.39	$0.35
10%	$0.91	$0.83	$0.75	$0.68	$0.62	$0.56	$0.51	$0.47	$0.42	$0.39
9%	$0.92	$0.84	$0.77	$0.71	$0.65	$0.60	$0.55	$0.50	$0.46	$0.42
8%	$0.93	$0.86	$0.79	$0.74	$0.68	$0.63	$0.58	$0.54	$0.50	$0.46

For example, note that $1.00 of cash received in year three requiring a 10% return is only worth $0.75 today; $1.00 of cash received in year five requiring a 10% return is only worth $0.62 today; and $1.00 of cash received in year seven requiring a 10% return is only worth $0.51 today. We know this is "Finance 101", but it is important to keep in mind for companies that are losing money and require large future cash flows to justify current prices. In our opinion for the companies highlighted above, the future cash flows required to justify the current prices are likely best-case operating scenarios. In other words, they are priced to perfection. If future cash flows turn out to be delayed or smaller in any way, these stock prices only have one direction to move. We think this is best illustrated by the stock performance of Zoom Video Communications that because of the pandemic was a highflyer in 2020 and is down about 32% in the last quarter based on lower growth expectations.

This is the current market environment. Many companies are trading for nose-bleed prices. We continue to exercise discipline in our evaluation of companies using conservative projections of future cash flows, reasonable discount rates, and making purchases at prices below our intrinsic value estimates. As a result, we find ourselves with eight investments that all share similar characteristics. They have a history of consistent revenue growth, use modest leverage, gush cash, and have historically been acceptable stewards of investor capital (returning cash to shareholders and maintaining or reducing their shares outstanding).

We don't know if our formula will produce outsized future returns, but we believe the odds tilt in our favor when these types of companies are purchased at reasonable prices. We discuss one of our largest new investments below.

New Investment

During the month of September, the Partnership invested in Check Point Software Technologies, Inc. (CHKP). CHKP is one of the largest cybersecurity software and hardware technology companies in the world. The company is headquartered in Tel Aviv, Israel, and pioneered cybersecurity firewalls in the early 1990s.

CHKP is supported by several industry tailwinds. First, ransomware attacks and data breaches continue to increase. As a result, cybersecurity insurance loss ratios have climbed in recent years. Insurance policies are becoming more costly, and some carriers are refusing to write policies that pay out ransoms. Companies are left with less financial protection than in prior years. The solution is to prevent cyberattack breaches from occurring in the first place – benefitting cybersecurity providers like CHKP. Also, network security is becoming increasingly complex with integrated security required across multiple data locations, applications, user settings, and user devices. CHKP provides exactly this type of security.

CHKP generates revenue from products/licenses, software updates and maintenance, and security subscriptions. While the products/licenses and software updates and maintenance revenue has been roughly flat over the last several years, security subscription revenue has been growing at more than 10%.

CHKP faces stiff competition from namely Palo Alto Networks, Fortinet, and Cisco Systems and has been the slowest grower of the group. We think this is a result of the company's disciplined management team led by its CEO/founder Gil Shwed who owns almost 19% of the company and a shareholder-centric board of directors. For example, over the last seven years the company has returned to shareholders in the form of stock buybacks 87% of the total operating cash flow produced (inclusive of capital expenditures and acquisitions) or $6.3 billion of a total $7.2 billion produced. Also, the company's disciplined management style has resulted in the highest margins in the industry with free cash flow of more than $1 billion on total revenues of $2.1 billion. Almost 50% of every dollar of revenue flow to profits.

Here is a summary of our thoughts on CHKP:

- Strong cybersecurity industry growth
- Management team and board of directors aligned with shareholders
    - CEO/founder owns almost 19% of the outstanding shares
    - Capital returned to shareholders in the form of buybacks – reduced share count by about 37% over the past ten years
    - Minimal shareholder dilution from stock options
    - Disciplined acquisition strategy
- Fort Knox-like balance sheet
    - No debt
    - $4 billion of total cash and equivalents ($2.5 billion excluding deferred revenue)
- Highly attractive business model economics
    - ~75% recurring revenue from security subscription and software updates and maintenance
    - Extremely strong cash flow generation
    - Low working capital requirements; low capital expenditure requirements
    - Security subscription revenue growing by more than 10% annually

Without an attractive price, these factors would only make this a potentially great company not a great investment opportunity. Assuming low single-digit total revenue growth, similar future profit margins, and minimal reinvestment requirements based on the business model, we estimate CHKP's intrinsic equity value to be about $20 billion including only $2.5 billion of balance sheet cash and equivalents. At the September 30, 2021, closing price of $113.04, CHKP's total market capitalization was about $16 billion or a 20% discount to our estimated intrinsic value.

Performance

Please review your individual partnership statements for performance results. As always, we caution partners about agonizing over short-term results (positive or negative). We are focused on the long-term. We are investing in high-quality companies that generate significant amounts of free cash flow. Every day more cash builds in the coffers of these companies and indirectly accrues to the Partnership. If prices fall, our investments go on sale. If the fundamental story remains the same, expect us to increase our investment size.

Conclusion

The Partnership is actively taking new subscriptions from qualified clients. We welcome any referrals from current partners. Please contact info@midwaypartnersllc.com for more information.

We are honored that you have chosen to be a part of our Partnership.

Sincerely,

Jordan Lampos

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