03/27/2021: MO Discount Shopping List

Operators,

Tuesday's market downturn got us thinking about what stocks we'd ***love*** to own at ***much lower*** prices. We love our current portfolio, so the hurdle rate is high for new company entrants. That's a *good* thing. It allows us to stay patient and wait for our pitch.

But it's crucial to develop a "shopping list" of names to buy if this downturn morphs into a bonafide correction. In the heat of a correction, we won't have time to make our shopping list. And if we started during the middle of a correction, we'd miss the opportunity to buy at basement-level prices.

It's not complete, but it helps you understand how we're thinking about playing a potential downturn.

Here are the companies on our shopping list:

- Cardlytics (CDLX)
- Five Below (FIVE)
- Guidewire Software (GWRE)
- Goodfood Market (FOOD.CN)
- John Deere (DE)
- Nvidia, Inc. (NVDA)
- Ollie's Bargain Outlet (OLLI)
- Sea, Ltd. (SE)
- St. Joe (JOE)
- Scotts Miracle-Gro (SMG)
- Target (TGT)

We've covered (and invested in) a handful of the names above. Where we did, we'll provide links to our original research. We'll hit a few key points with each company, discuss why we like it, and the price at which we'd love to buy.

A few of these companies will only become available at bargain prices if the market has a **monster** downturn. But that's okay. We don't *need* to buy these stocks. Our portfolio is like a fancy nightclub. There's a waiting list to get in, and the line wraps around the back of the building.

Let us know if any other companies should make the above list. We're always on the lookout for new watchlist candidates.

Let's get after it!

Cardlytics, Inc. (CDLX): Native Banking Advertising

CDLX is a native bank advertising channel that enables marketers to reach consumers through their trusted and frequently visited online and mobile banking channels. It also provides solutions that will allow marketers and marketing service providers to leverage the power of purchase intelligence outside the banking channel.

You can read our original write-up here.

We bought CDLX in early August 2020 but were shaken out the next day on a failed breakdown. Three months later (November 5), we bought again at $88/share. The stock ran from 4x EV/Sales (our initial purchase in August) to over 15x by the time it hit $150/share.

Why We Like CDLX:

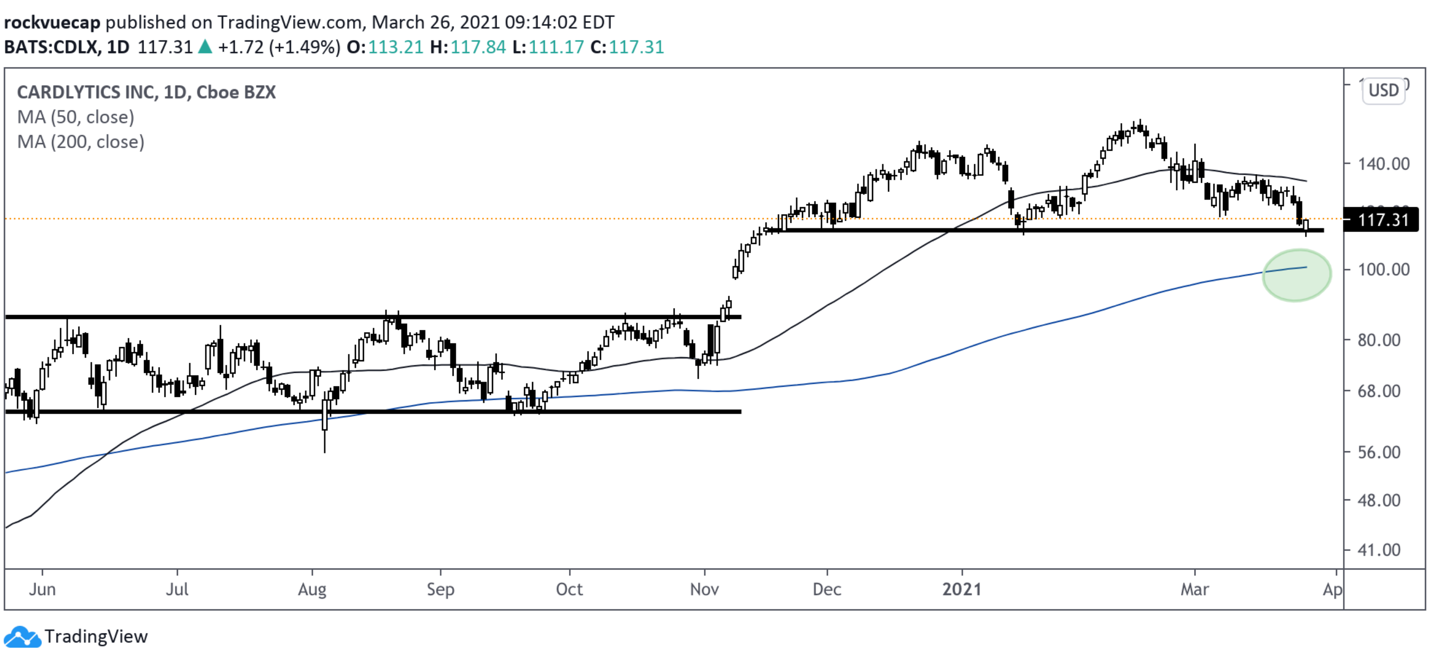
- Sticky product with high network effect potential
- Founder-led with long-term shareholder base (CAS Investments owns 16% of the company)
- Long runway for revenue growth and margin expansion
- The product gets better with each new bank that joins the platform
- Top-line solid revenue growth (35% 5YR CAGR)
- Fortress Balance Sheet (more cash than total liabilities)

Where We'd Want To Buy: $90/share or Lower

The company expects to hit $370M in revenue by 2022. If we could buy CDLX for $90/share, we'd pay 7.7x sales for the business. At that point, the company should generate ~$35M in EBITDA as it leverages its fixed cost base.

So while we'd pay more than we did in August for the same business, we're getting a company that is EBITDA positive and building on its powerful flywheel with consumers, advertisers, and bank partners.

Also, $90/share would put the stock right at its 200MA on the daily chart (see below):



Five Below (FIVE): A Fantastic (But Expensive) Business

FIVE is a specialty value retailer that offers a wide assortment of products for around $5. The stock's returned 380% over the last five years, sporting a 36.8% CAGR. The S&P 500 returned 92% during the same timeframe.

The company has a fantastic business model. They only build in areas with higher incomes ($73K+) and cater to Gen Z and millennials through their vast product offering. Stores are small (8,500sqft), which reduces total rent expense. Yet it's FIVE's unit economics that steals the show.

It costs ~$300K to build a new store. By the end of its first year, that new store will do ~$450K in EBITDA. That's a 150% ROI per-store in its first year, translating to an 8-month payback period. To compare, a couple of our favorite "per-store" company theses (LGRS, GYM, and KRUS) average ~40% ROI per store.

FIVE operated 900 stores at the end of 2019. On a run-rate basis, the company estimates they can use 2,500 stores nationwide. In other words, they've tapped a mere 36% of their addressable market.

If FIVE can reach 2,500 stores and maintain current unit economics, they'll do ~$1.12B in annual EBITDA.

What We Like:

- Easy-to-understand business model
- Previous success with per-store investments
- Long runway for continued store expansion
- Defensible during an economic downturn as consumers trade down for lower-priced goods
- History of share price outperformance
- 150% ROI per store

Where We'd Want To Buy: $145-$150/share & Lower

At $145/share, we're paying ~$8.8B for the entire business. Remember, if FIVE hit 2,500 stores nationwide, the company would generate $1.12B in annual EBITDA. So you're paying 8x EBITDA at $145/share. That's fantastic given the unit economics of this business.

To get to our price target, we'd need a 26% decline in the stock. It will take a broad market correction for FIVE to test that price level.

Moreover, $145 marks the company's 200MA on the daily chart (see below):

Guidewire Software (GWRE): Property & Casualty Insurance Software Provider

GWRE provides software products for property and casualty insurers worldwide. The company offers Guidewire InsuranceSuite comprising Guidewire PolicyCenter, BillingCenter, and ClaimCenter applications. It also provides Guidewire InsuranceNow, a cloud-based platform, which provides policy, billing, and claims management functionality to insurers.

P&C insurance is a massive market ($2.5T TAM). GWRE focuses exclusively on P&C insurance and sports over 400 providers on its platform. The company is at the heart of an industry transition from outdated infrastructure to a cloud-based SaaS offering. Currently, 75% of P&C IT spend is to “keep the lights on.”

GWRE’s cloud-based platform provides every tool necessary for P&C insurers to meet their clients’ needs.

The company’s revenue growth isn’t what you’d expect from a software business. But remember, they’re *just now* making the change from on-premise-based pricing to cloud-based SaaS models. As the company merges new/existing customers on the SaaS model, revenues and margins should trend significantly.

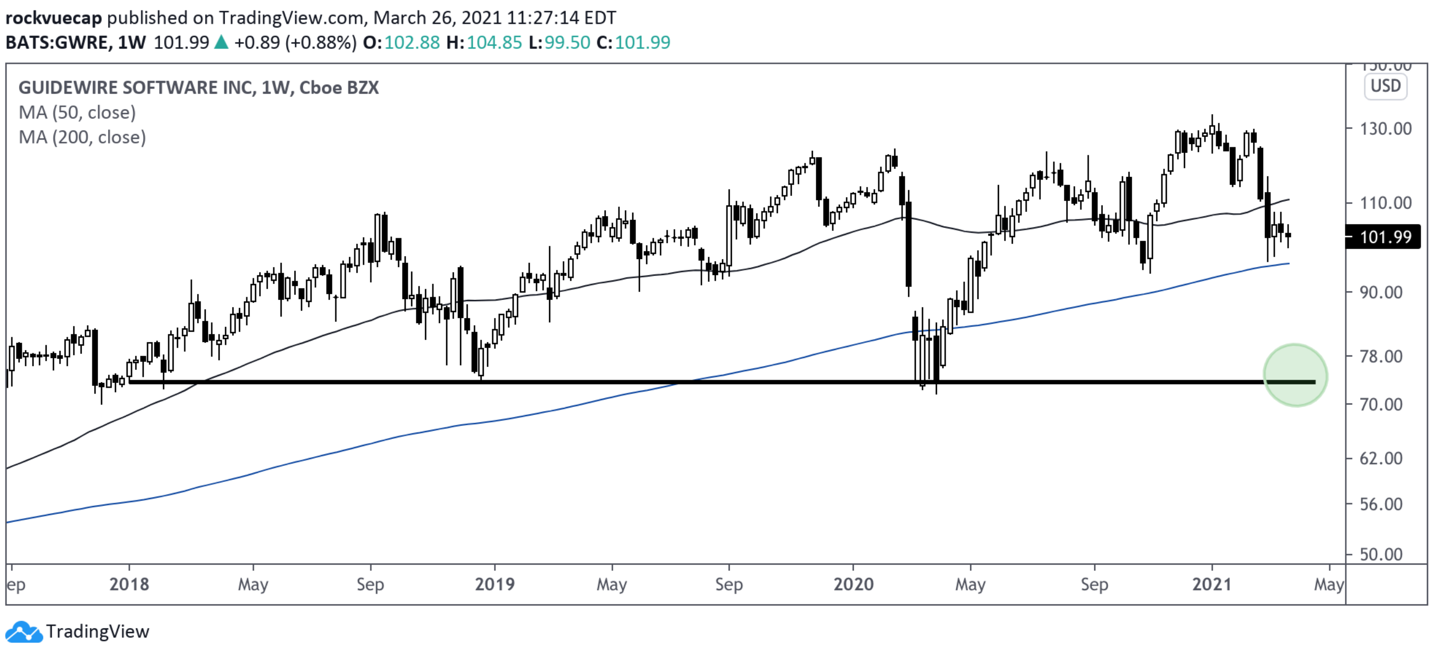
What We Like:

- Large addressable market with sticky product attributes
- $700M in net cash on the balance sheet
- Misunderstood due to change in business model
- Optically expensive could drag down the share price

Where We'd Want To Buy: $72/share & Lower

At $72/share, you're getting the business for ~$5.3B EV. The company's expecting ~$790M in revenue by 2022 (7x EV/ FY22 Sales estimates) with $40M in EBITDA (5% margins). After completing its transition to the cloud, the company should regain its normalized 18% EBITDA margins.

Getting to $72/share requires a 28% decline in the share price. Again, I don't see GWRE getting there on its own, and it will likely take a sustained correction in the NASDAQ for us to see those prices. That said, if it does get there, it will have solid support on the weekly chart (see below):



Goodfood Market (FOOD.TSE): Canada's Online Grocer

FOOD is an online grocery company, delivers fresh meals and grocery products in Canada. The company has experienced ridiculous revenue expansion, growing from $15.39M in 2017 to $218M in 2020.

Granted, COVID accelerated years of revenue growth into one. At the same time, COVID accelerated Canadian adoption with online grocery delivery as their primary method of buying groceries.

The reason we have FOOD on our shopping list is becuase of its online grocery delivery business. Meal-kit delivery is a bad business. It has no barrier to entry and low unit margins. There's also little differentiation companies can use in their products besides fancier ingredients and better-looking delivery containers.

Grocery delivery is a better business for three reasons:

1. It requires substantial CAPEX spend to build a logistics network
2. Winner-take-most category
3. Benefits from top-of-mind customer share when shopping

FOOD's blue-sky bull thesis hinges on its ability to create the online grocery delivery infrastructure for all of Canada's grocery stores. The company has seven grocery delivery sites built throughout Canada and offers 550+ products for same-day delivery.

What We Like:

- Recognized brand name with solid penetration in Canadian grocery stores
- Transitioning from low-margin meal-delivery kit business to capital-intensive grocery delivery infrastructure
- Off-the-beaten-path means fewer investors looking at the idea
- $40M in net cash on the balance sheet
- Currently cheap

Where We'd Want To Buy: CAD 8.40/share & Lower

The stock is currently cheap at 1.42x EV/Sales. That multiple is way too cheap if the company can successfully pivot and become Canada's leading online grocery fulfillment infrastructure. Unlike most of the names on this list, FOOD looks cheap now. Plus, it has a killer chart. Check out this falling bullish wedge:

John Deere (DE): Bet On Agri-tech Future

DE manufactures, sells, and finances various agricultural/farming machines and products. The list of equipment is impressive: utility tractors, tractor loaders, combines, cotton pickers, cotton strippers, and sugarcane harvesters; harvesting front-end equipment; sugarcane loaders and pull-behind scrapers; tillage, seeding, and application equipment comprising sprayers, nutrient management, and soil preparation machinery; self-propelled forage harvesters and attachments, balers, and mowers; riding lawn equipment, golf course equipment, utility vehicles, and commercial mowing equipment along with associated implements; integrated agricultural solutions and precision technologies; and other outdoor power products.

Crop prices are through the roof. Corn and soybean futures are at their highest since 2014. Higher commodity prices mean greater profits for farmers. Greater profits for farmers means fancier equipment to continue operating. That's where DE comes in.

DE's *Precision Ag* line focuses on "cash crops" like cotton, corn, soybeans, small grains, and sugar cane. And with arguably the greatest mind-share with farmers, DE looks like the logical equipment upgrade choice.

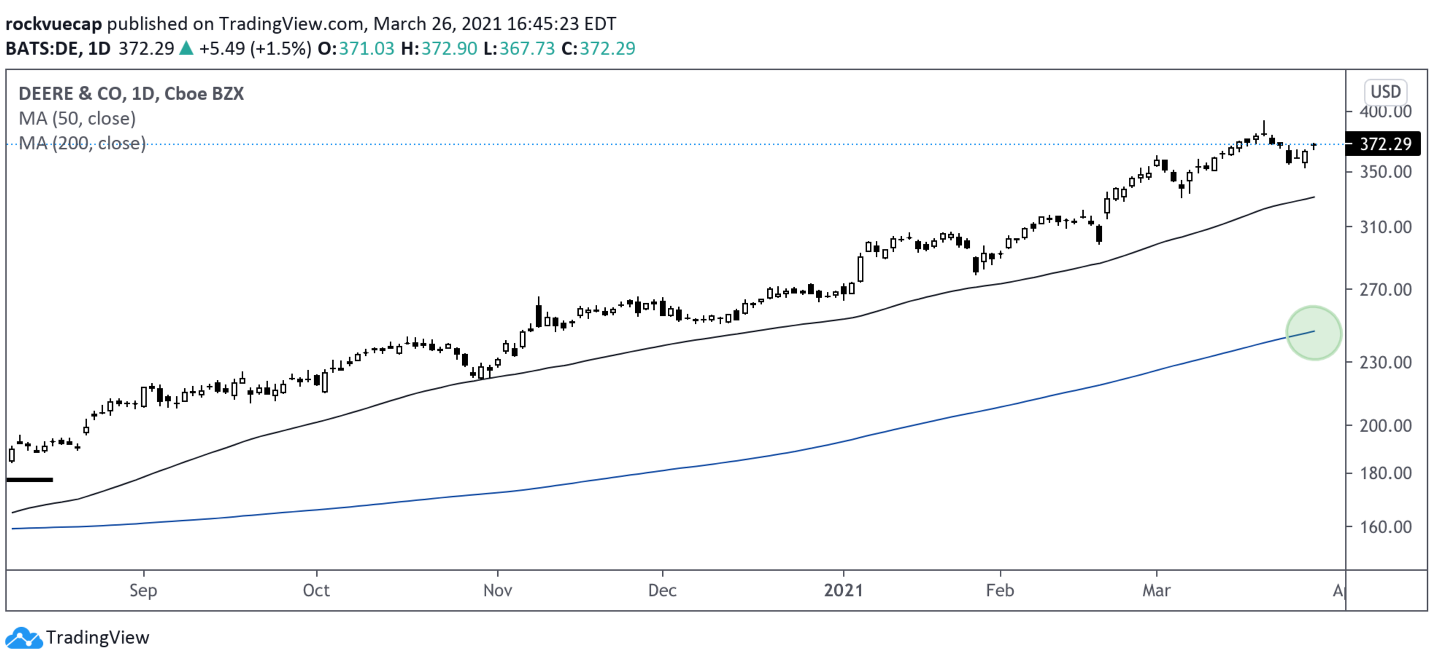
Finally, DE is a perfect play for our Fourth Turning thematic, complimenting SANW and BIOX.

What We Like:

- Long-standing brand name associated with industry and quality
- Great way to play the coming food shortage/agriculture tech boom
- Durable competitive advantages against the competition (financing, manufacturing, etc.)
- Call-option on agritech future and precision agriculture

Where We'd Want To Buy: $250/share & Lower

We'd love to own it for around $250/share. Granted, we'd need a 34% haircut from current prices. At $250/share, you could buy the entire business for $117B EV, or 21x its current operating income. The $245-$250 price also gets us to the 200MA on the daily chart (see below):



Nvidia Corporation (NVDA): Best-in-Class Visual Computing Company

NVDA operates as a visual computing company. The company's products are used in gaming, professional visualization, datacenter, and automotive markets. NVDA is the leader in gaming Graphics Processing Units or GPUs. NVDA GPUs create self-reinforcing mechanisms to keep NVDA's products in high demand.

Here's how it works. NVDA creates high-powered GPUs that allow gamers to render better graphics on their gaming devices (PCs, mainly). In turn, this enables game developers to constantly push the boundaries of what's technologically possible in gaming, which requires, of course, *even better* GPUs for more advanced games.

The company also wins in cloud computing infrastructure. For example, the top four cloud computing companies have used NVDA's accelerators in 97.4% of all instances. That's nuts.

What We Like:

- Industry-leading company with best-in-class products
- Strong long-term tailwinds in gaming and cloud computing
- It fits within our Digital Transformation Thematic
- A long history of revenue and earnings growth
- Consistently outperforms broader indices
- $3B in net cash on the balance sheet

Where We'd Want To Buy: $270 & Lower

I know. There's a chance NVDA never gets there. We'd need a near 50% decline in the stock price to hit our desired target. That would take a herculean effort from Melvin Capital and the rest of Wall Street. That's why we have shopping lists. NVDA can stay in our cart until it lands in the "Clearance" section.

At $270/share, we could buy the entire business for $164.4B. That *still* puts us at 10x revenues and 35x operating income. Again, NVDA might never look quantitatively "cheap." But we'd *love* to own this thing at sub-40x operating income.

Ollie's Bargain Outlet (OLLI): Discount Retailer We Want At A Discount

OLLI is a retailer of brand-name merchandise. The company offers food products, housewares, books and stationery, bed and bath products, health and beauty products, floor coverings, electronics, toys, and other products, including hardware, personal health care, candy, clothing, and sports pet and lawn, and garden products.

The company sells 'good stuff cheap.' If you've seen Parks and Recreation, think of OLLI as a *Food & Stuff* store. Here's how they generated revenue in 2019:

- 5% housewares
- 10.8% food
- 10.5% bed and bath products
- 8.6% books and stationery
- 65.1% Other items

OLLI generates ~16% ROI while growing revenue at an 18% CAGR over the last five years. The company's expanded EBITDA margins during those five years from 13% to 17%.

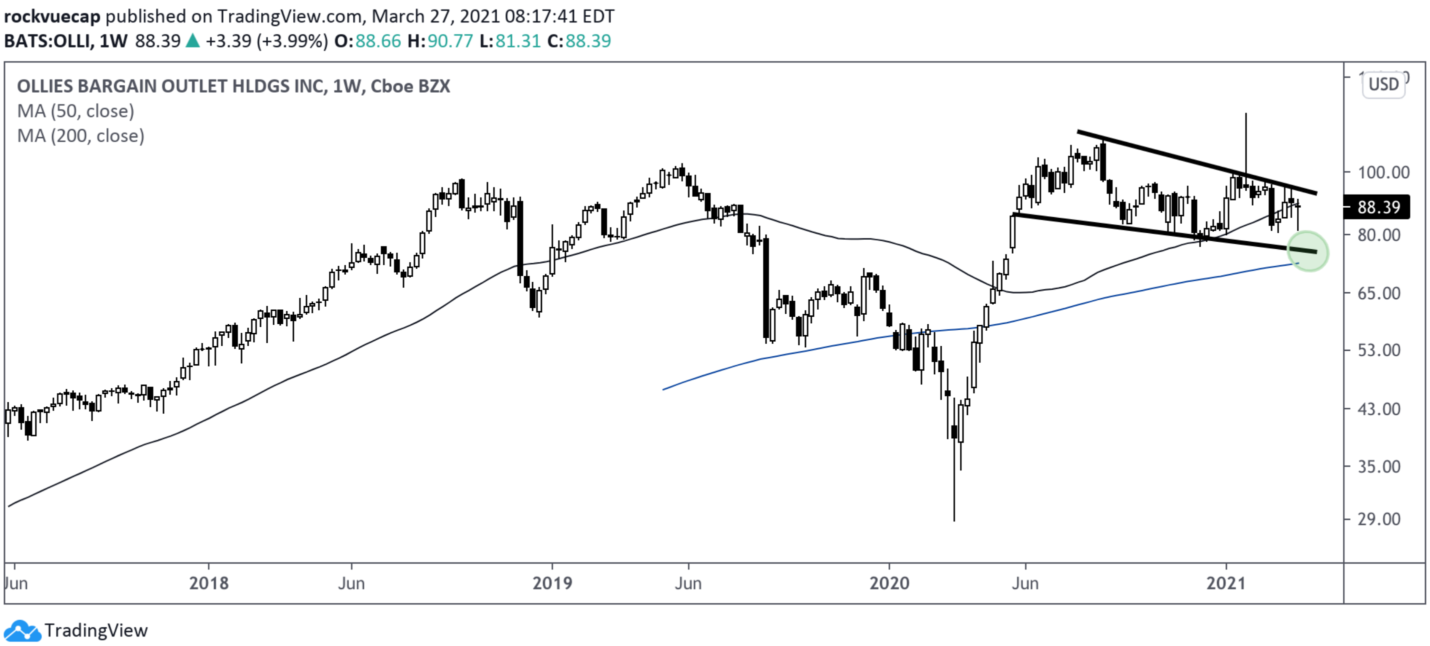
What We Like:

- Easy-to-understand business model
- History of revenue growth and margin expansion
- $60M in net cash on the balance sheet
- 14% Unlevered FCF margin
- Long-term shareholder base

Where We'd Want To Buy: $75/share & Lower

OLLI is trading within a descending bullish wedge pattern. We'd love to scoop shares at the bottom of the range (around $75/share). At that price, we could buy the entire business for $4.85B EV, or 17x EBIT. That's an excellent price for a company growing revenues 20% per-year with expanding EBIT margins and net cash on its books.

Plus, it's always a great idea to bet on a company that offers excellent stuff at low prices (any WMT lovers?).



Sea Limited (SE): Digital/Mobile-First Conglomerate

SE is a digital entertainment, e-commerce, and digital financial service business in Southeast Asia, Latin America, and Asia. The company offers mobile/online games, digital payments, e-commerce platforms, and chat/forum-based platforms. In short, SE does it all.

The company is arguably one of FinTwit's most beloved children. *Everyone and their mother* have shares in SE. There's a good reason. SE's three business segments (gaming, e-commerce, and fintech) have grown 160% YoY, *and* the company was recently awarded its banking license.

Since 2015 SE's grown revenues from $281M to $4.375B, those growth rates are almost impossible to comprehend.

But it comes at a price -- a high price! The company currently trades ~24x NTM EV/Sales and will likely face stiffer competition as new entrants look to take some of that precious revenue growth.

What We Like:

- Dominant business attacking three highly-profitable industries (gaming, fintech, and e-commerce)
- Leading presence in Southeast Asia (high-growth area)

- Incredible revenue growth
- Decreasing Days Sales Outstanding and Cash Conversion Cycle

Where We'd Want To Buy: $125/share & Lower

The company's aggressively issued shares over the last five years, but we're assuming share counts stay roughly the same. At $125/share, you could buy the entire SE business for ~$60B, or 13.6x NTM sales. I know, that *still* sounds expensive. But the company's monster revenue growth and market leadership in Southeast Asia make 13x a *steal*.

Of course, we'd need a near 40% correction in the stock price to get there. We could see that in a broad market recession, but we're not banking on it.

St. Joe Company (JOE): Long Florida Land Values

JOE operates as a real estate development, asset management, and operating company in Northwest Florida, the United States. It operates through three segments: Residential, Hospitality, and Commercial.

The thesis here is simple. The land JOE owns is worth vastly more than they paid for it. And with the Great Silicon Valley migration to the Sunshine State, that land value *has only increased*.

The company sells land for residential housing and retail development. They also own/operate private golf clubs, marinas, hotels, and other vacation rental spots on their property.

JOE currently trades at an extraordinary 28x EV/Sales. But take this with a grain of salt. The company hasn't sold off all the land on its books, and when it does, it will command meteoric prices.

What We Like:

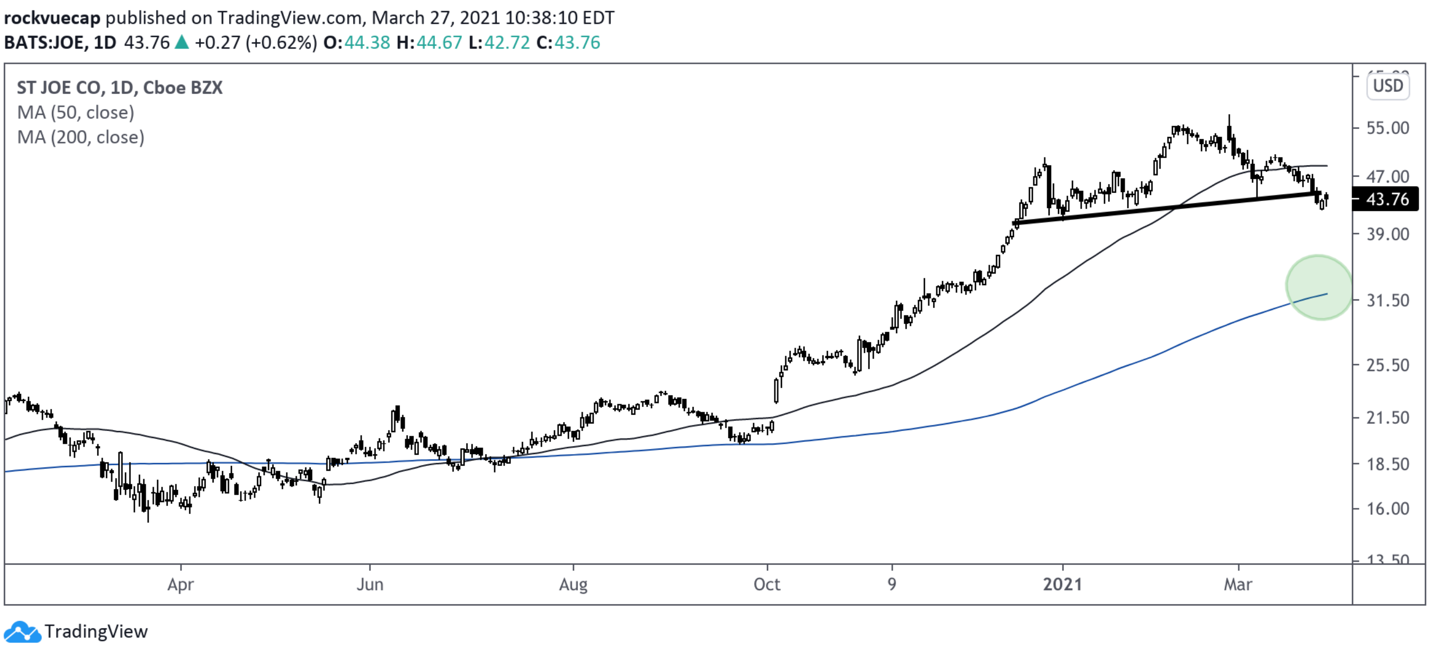
- A direct way to play the "Bull Miami" thesis

- Solid shareholder base (Gabelli, Royce, Praetorian, etc.)
- Long-term asset value tailwinds

Where We'd Want To Buy: ~$32/Share & Lower

We don't want to chase JOE at these prices. We're looking at the $32/share target and lower for an entry. This price coincides with the 200MA on the daily chart. We'd need a 26% price decline to get there, which is doable if we get any anti-Miami/nationwide reopening.

Plus, the contrarian in me wants to fade the *ever-popular* desire to flock to Miami.



Scotts Miracle-Gro (SMG): Bet on Agritech, Cannabis, and Hydroponics

SMG manufactures, markets, and sells consumer lawn and garden products in the United States and internationally. The company operates through three segments: U.S. Consumer, Hawthorne, and Other. It offers lawn care products, such as lawn fertilizers, grass seed products, spreaders, other durable products, and outdoor cleaners, as well as lawn-related weed, pest, and disease control products.

When people think SMG, they think of the generic lawn care products at Home Depot and Lowes. What they don't consider is the massive hydroponics/cannabis business the company is developing.

Since 2015, SMG has acquired five hydroponics companies:

- 2015: General Hydroponics
- 2016: 75% of Gavita and 100% of Botanicare
- 2017: Canfilters
- 2018: Sunlight Supply

The company segments its hydroponics/cannabis business into its “Hawthorne” division. Hawthorne is responsible for most of the company’s top-line growth. For example, SMG’s grown its Hawthorne revenue from $344M in 2018 to $1.08B in 2020.

What We Like:

- An industry leader in hydroponics, lawn care, and fertilizer
- Best positioned to capture significant cannabis market share
- CEO owns 26% of the company
- Consistent history of share buybacks
- Decent valuation

Where We’d Want To Buy: $173/Share & Lower

SMG is interesting because the chart looks impressive *right now*. A beautiful inverse H&S breakout on the daily chart. That said, we’re making our shopping list which means we get to pick our price. We’d love to buy shares at $172. That price brings us the entire business for ~$11.8B, or ~16x Operating Income.

Target Corporation (TGT): Great Brand, Great E-commerce Infrastructure

TGT operates as a general merchandise retailer in the United States. The company offers food assortments, including perishables, dry grocery, dairy, and frozen items; apparel, accessories, home décor products, electronics, toys, seasonal offerings, food, and other merchandise; and beauty and household essentials.

The TGT thesis is simple. The company is well-positioned to capture significant market share in the shift from a purely in-store sales model to an omnichannel service offering. TGT can leverage its physical stores as localized distribution hubs to better serve its customers through BOPIS (buy online pick-up in-store).

The company's grown online sales like gangbusters, and many are quick to discount those growth rates due to COVID. Bulls are betting that the recent growth accelerations from BOPIS and omnichannel sales *are here to stay*.

If you want to learn more, please give this Gavin Baker thesis video a watch. It's great.

What We Like:

- Great way to play shift to omnichannel sales distribution
- Strong growth rates that look sustainable
- Trades <2x EV/Sales
- Monthly store visits remain strong
- Brick-and-mortar stores will remain important in the shift to online sales

Where We'd Want To Buy: $175/Share & Lower

The stock recently broke out of a semi double-bottom pattern on the daily chart. We missed the entry on this one (argh!) but will look to enter on a pullback. At $175/share, you can buy the business for ~$93B, or <1x EV/Sales.