To: Culibrk Partnership Partners
From: Stefan Culibrk
Date: July 11th, 2018

Dear Partners,

The Partnership recorded a gain of 1.7% during 1.4.2018. – 30.6.2018.

	Return	S&P 500[1]
Quarter	1.7%	3.4%
2018	3.0%	2.6%
Since inception (Jan 2015)	116.8%	41.9%

We take care of the capital you have entrusted us with as if it was our whole net-worth and if our investment time horizon was forever. Although new partner inflow might over time cause my family to stop accounting for majority of the Partnership assets, we have no intention of changing the approach. This has implications on how we allocate capital.

There is no geographic, sector or company size mandate. We do not think of investments as value or growth. Although we have usually been invested in more than ten companies, we do not think we are reducing risk by spreading ourselves too thin. Quite the contrary. We think sounds risk management rests on understanding what we invest in.

We are willing to invest up to 1/3 of the Partnership assets (at cost) into a single business. It would likely be a business with high returns on capital and a long growth runway. We need to be able to understand it and be comfortable that the time is on our side. It would have to be available at a price far lower than its value, a price that makes our fortunes immune to surprises. We won't invest a penny if the operator in place is not competent and aligned with us as shareholders.

You can see S&P 500 returns next to our own because we think such a comparison is helpful in assessing whether we have added value over the long haul versus the returns you could have generated at no cost, with little effort, while assuming a broadly similar type of risk.

We refuse to lower the bar for deploying capital. As of June 30th, we held 17% of the Partnership assets in cash. We understand that money costs money. The capital you have entrusted us with should be deployed within a reasonable time frame. The opportunity set of today is not the only opportunity set we are considering. It is hard to predict the attractiveness and timing of the opportunity set of tomorrow. It is nonsensical to ignore its existence.

We think long-term investing success rests on being opportunistic to the situation presented. Sensible framework of paying ¢50 for growing dollars is immune to change. When there is nothing to do, we'll wait. We'll learn about businesses we would invest in at the right price. When the opportunity presents itself, we'll be ready.

[1] Note: S&P 500 returns measured by SPX

New position

Alliance Data Systems

We have acquired shares of Alliance Data Systems (ADS) at $233/share. It is currently 9% of our portfolio.

Alliance Data Systems creates and operates loyalty and marketing campaigns for thousands of consumer-facing companies. It does so via three related, but independent business units: Card Services, Epsilon and LoyaltyOne. All three benefit from a shift from traditional mass marketing towards targeted marketing programs that have a clear and measurable return on investments.

Card Services

Card Services provides retailers with a combination of a loyalty program and a private label credit card for its consumers. Alliance Data bears credit risk and collects interest on the credit cards. It funds them via commercial deposits and securitization.

Alliance Data partners with more than 160 retailers. They range from traditional such as Victoria's Secret (largest client, together with its affiliates accounts for 16% of revenues) and IKEA, to Ulta Beauty and pure-play ecommerce retailers such as Wayfair. Average credit card receivables portfolio per retailer is $100m+. Retailers partner with private label credit card operators because a sizeable proportion of sales on credit are incremental sales. Alliance Data brings the same appeal, but more importantly, its loyalty programs capture and process transactional data, helping the retailer better understand consumer behavior and drive further sales. Additional benefit is that retailers don't pay interchange fee on Alliance Data cards as they do when their consumers use Amex, Visa or Mastercard. Much of the fee savings get reinvested into the loyalty program.

An important point in an era of sensitivity to data collection practices: when registering for the loyalty program, consumers give consent to Alliance Data to utilize the SKU-level information in order to market to them solely on behalf of the retailer. Retailer learns where its consumers shop, what device they use, what time of the day they prefer to shop, what are they looking for and the specific message that will spark their interest to purchase an item.

In the age of Amazon, all retailers need such intelligence, but many are sub-scale to pay for it or lack the expertise to develop it in house. Alliance Data offers a convenient solution: by linking the credit card program to the loyalty program, consumers end up paying for the insights that retailer uses to boost sales. Consumers are mostly prime credit, female and use cards to access retailer's loyalty program to unlock discounts on purchases. They carry a small balance on the card ($688 in 2017, less than 20% of a general purpose credit card balance) and pay subprime interest rates (25%+) although they are prime credit.

Is the consumer being irrational? Using loyalty programs doesn't feel like paying high rates because the interest rate is blended with discounts by the retailer (standard discount is 5% and goes to 30% on promotions). Small balances and short payback periods help make interest rates don't appear prohibitive. Consumers don't perceive six monthly payments of $100 for a $600 product that they paid $530 on a discount, as a 28% APR. In contrast to general purpose credit cards, consumers of all ratings tend to have broadly similar rates in the private label credit card business.

Card Services business will continue to grow via three levers: same store sales growth at its retailers, tender share (share of credit sales vs. cash purchases at existing clients) and new retailer additions. Alliance Data recently lost retail partners due to bankruptcies (Bon-Ton).

When there is no restructuring or a continuation of retailer existence in some form, credit sales are lost. Once consumers of a bankrupt retailer pay off their cards, the steady state level of receivables is reduced. Receivables repayment is not related to the health of the retailer, but to the health of the consumer.

Annual retention of retailer clients has been 99%. Alliance Data analytics become mission critical to the retailer, which increases the switching cost. Competitive advantage versus Synchrony Financial / Capital One in loyalty program expertise translates into lower through the cycle charge-offs and significantly higher returns on equity.

Alliance Data has built in risk mitigants in its business model. When consumers hit hard times they tend to finance themselves with any money they can find. General purpose credit card delinquencies accelerate. Private label credit card delinquencies increase at a much slower pace. A credit line at Victoria's Secret is not going to help someone get through in a recession. This usage pattern protects the downside for Alliance Data in a crisis. In addition, due to low absolute exposure per credit line, Alliance Data would need to have five times as many clients default as a typical credit card operator to have the same absolute loss.

Quality of private label credit card receivable portfolios is similar today across the industry (85% of volume, 2/3 of balances by superprime and prime) as it has been historically. Credit card balances as a % of GDP are currently at the lowest level they have been in the past 15 years[2] . Subprime and deep subprime accounts are an increasing number of new accounts, but still a stagnating proportion of balances, as superprime accounts get larger credit lines. Alliance Data tends to avoid credit weaker than prime, which causes its charge-offs to be half the industry average in good and bad times.

It is of great comfort to an investor in a credit-sensitive business that has operated smoothly, with the same model, for the past 20 years. At the depths of the recession, return on equity of the business was above 20%. During the past 15 years, this business delivered an average return on equity of 35% and annual book value growth rate of 18%.

Credit is a cyclical business and we need to get comfortable with how bad do things need to get for Card Services to start losing money. We need a combination of: credit cycle turning for the worse with losses double the typical recession and equal to the Great Recession, retailer client bankruptcies of 20%, a 20% drop in receivables, doubling of interest rates paid and completely fixed operating expenses. This is a fat margin of safety. We like our chances.

As the portfolio transitions from slow growing and bankrupt retailers toward higher growing ones, credit sales will expand from currently reported 2-3% growth to low double digits. Credit sales growth would have been 12% and receivables growth would have been 17% in 2017 without the bankrupt accounts. Increasing credit sales will drive receivables growth. At the current pace, fast-growing retailers such as Wayfair will account for more than 50% of credit sales in about four years.

Normalized for charge-offs (2018 should be an average year for the credit cycle), free cash flow of the business is c. $1bn (within Alliance Data - more on that below). About 30% of that free cash flow needs to be redeployed into receivables growth to keep growing free cash flow at low double digit rates without changing the capital adequacy of the banks that are funding the business.

[2] Consumer Financial Protection Bureau — Consumer Credit Card Market Report 2017

Epsilon

Epsilon is a digital marketing agency, ranked by Ad Age as #1 US agency five years in a row. Epsilon uses data to create analytics that help its clients more effectively acquire, retain and grow consumer relationships. Epsilon offers strategic consulting, technologies around consumer database, omnichannel marketing, loyalty management, predictive modeling, etc. On behalf of its clients, Epsilon develops highly targeted and personalized marketing programs that reach individual consumers across channels. We take for granted that Amazon offers us a brown belt that goes with those brown shoes we've just bought. For most of the other retailers, having that insight is impossible on their own. Epsilon helps them compete.

Epsilon has 1,600 clients, among whom are nine of the top 10 banks, eight of the top 10 retailers, 10 largest pharmaceutical companies and seven of the top 10 automakers. Clients allow Epsilon to analyze first-party purchase-level data and augment it with its knowledge of digital data about anonymized, segmented consumers. Epsilon also has capability to do omnichannel analytics and see if the marketing actually resulted in return on investment for the advertiser, even if the return comes via a bricks and mortar store.

An example of projects Epsilon does: creation of Walgreens loyalty program, revamp of BP loyalty program and consulting on Norwegian Cruise customer acquisition process.

Card Services business uses Epsilon loyalty platform, demographic/psychographic data and digital distribution channels for all of its retail clients. In the past five years, Card Services has developed "mini-Epsilon". With 500 data scientists, it is self-sufficient with minimal contracting of Epsilon. This shows willingness to spin/sell Epsilon.

Epsilon's closest publicly-listed peer, Acxiom Marketing Solutions, has agreed to be sold for $2.3bn to IPG on 2nd July 2018 (3.5x EV/Sales, 14x EV/EBITDA). Epsilon segment generated revenues of $2.3bn over last twelve months, EBITDA of $451m and pre-tax FCF of c. $344m. IPG/Acxiom transaction would imply a range on EV of Epsilon between $6.2bn to $8bn.

LoyaltyOne

LoyaltyOne designs, operates and implements loyalty programs. It uses information gathered in loyalty programs to help clients create effective marketing programs. It operates through two units: AIR MILES and BrandLoyalty.

AIR MILES, a Canadian coalition loyalty program founded in 1992, is owned and operated by LoyaltyOne. The coalition program has 200 sponsors (Sobeys, Shell, Amex, Bank of Montreal, etc.), 400 suppliers and a presence in two thirds of Canadian households (10m). Customers ("collectors") collect points when doing everyday purchases at sponsors (for example: buying gasoline at Shell using Amex, shopping at Sobeys using Bank of Montreal card). Sponsors pay a fee to AIR MILES per point issued to the collectors. Collector can exchange points into rewards at suppliers. When they do so, AIR MILES pays the suppliers. An advantage to using AIR MILES for the sponsor (rather than having their own program) is that AIR MILES sees what collectors are doing at 200+ sponsors, enriching the knowledge for each individual sponsor. An advantage for the collector is that accumulation of miles is multiple times faster than participating in multiple loyalty programs at the same time.

AIR MILES provides marketing, customer service and redemption management for the program. AIR MILES makes a spread between what the sponsors paid for the point and what the suppliers receive per point. Breakage, points that are forgotten by collectors and never redeemed, presents another source of profits. The company estimates breakage of 20%. A loyalty program operator also benefits from investment income it has from float, an estimated 38-month mismatch in duration between the time of purchase of a point and

redemption of a point, during which AIR MILES can invest the cash paid for the points. AIR MILES is owned by LoyaltyOne, which differs from a program simply executed by Epsilon as a service provider (typical for the US).

Due to the remarkable penetration rate in Canadian households, this business can be expected to grow in-line with the rate of nominal GDP. Revenue for 2017 was $743m. At a 24% EBITDA margin, it yielded $180m in EBITDA. AIR MILES is a rare business where cash flow from operations is consistently substantially higher than EBITDA, due to a three year long negative working capital cycle. I think a conservative multiple for this business is 10x EBITDA, for an enterprise value of $1.8bn.

BrandLoyalty is a loyalty platform that sets up short-term loyalty programs for grocers in Europe, Asia and Canada. It creates and operates 200+ programs per year. The data obtained from the program is processed by BrandLoyalty to help the grocer understand its customer base. It has recently signed a pilot with Kroger, their first US client. This business has grown 10% annually. 2017 performance was less than satisfactory (revenue -12%) due to delays in promotions in anticipation of the Olympics/World Cup. The company expects double digit revenue and EBITDA growth to continue starting 2018.

Alliance Data acquired 60% of BrandLoyalty in 2014, 10% in 2015 and 30% in 2016 for a total payment of $750m (implied valuation of $1.3bn based on the price for the final 20%). I value it conservatively at $500m (7x EBITDA, 1x revenue), one third less than what was paid for it between 2014 and 2016.

Management

Ed Heffernan has been with the company since 1998 and has been the CEO since 2009. Most of his compensation is tied to a reasonably challenging annual earnings before taxes target and two-year shareholder returns relative to the S&P 500. He owns $50m of shares (38x base salary) which he has mostly received as compensation over time. He usually sells 5-15% of his shares annually (typically offset by rewards).

Heads of Epsilon and LoyaltyOne own 39x and 41x base salary in shares. Card Services head owns shares worth 6x her salary.

Bruce Anderson, founder of WCAS, a private equity that founded Alliance Data, has been on the board since the IPO and owns a personal stake worth $200m. Two other board members own $20m+ in shares.

ValueAct owns 10.6% of the company (15% of their US equity portfolio by our estimate) and has installed its partner, Kelly Barlow (ex-Adobe board member), on the board in 2017.

Capital allocation

Management deserves praise for buying back more than a third of the shares outstanding during 2008/2009 at $63/share. In the past three years they bought back 17% of current shares outstanding at an $243/share. They have indicated that a more aggressive repurchase will continue at current levels. This is music to our ears, as the company is currently trading at the lowest multiples historically. Track-record on M&A is average. The company is targeting 2-3x financial debt to EBITDA. Leverage is currently at 2.7x EBITDA ($6.1bn).

Valuing Alliance Data together

Combined businesses will generate $1.5bn in free cash flow in 2018, of which $115m will be paid out as a dividend and about $350m will be needed to support growth of the credit card

receivable portfolio at a 12-15% growth pace. This leaves $1bn in free cash flow that is set to grow 10+% per year. At 12x free cash flow (pre-dividend, but after credit card portfolio growth investments), we are paying an attractive price for a collection of superior businesses, run by able management, that grow at a solid rate.

Valuing Alliance Data apart

We think that the logic for the spin-off is a sound one and that the value hidden in the Card Services could be unlocked by showing its true economics and allowing it to repurchase its own stock in the market. We'd rather own Card Services than Epsilon, especially if it is trading at a 70% cheaper multiple than Epsilon.

We value LoyaltyOne at $2.3bn and Epsilon at $4.6bn, a 33% discount to the recent IPC/Acxiom transaction. Combined enterprise value of the two is $6.9bn (equity of $4.1bn, after accounting for pro-rata $2.8bn in corporate debt). This would leave the credit card business priced at $8.1bn, at 8.8x price/normalized 2019 free cash flow and with $3.3bn in financial debt.

This is strikes me as cheap for a 35% return on equity business that can keep growing free cash flow at low double digits for years. Fair multiple for this business is not less than 15x free cash flow.

We can see 25+% annual returns in the next five years if Card Services is spun out. Returns might be even higher if LoyaltyOne/Epsilon are sold. Investing to support the growth of the credit card receivables portfolio should continue with the same discipline. The most rational deployment of excess capital at 9x price/free cash flow are buybacks. In a no-lose scenario, a slower pace of share price appreciation, or a recession, is fine with us. The business will be able to retire its shares faster.

We think that the margin of safety is attractive both on the business quality and on valuation. There are multiple ways to win substantially owning Alliance Data Systems at current prices.

<u>Sizing changes</u>

We have sold GCI Liberty preferred shares and redeployed capital into Liberty Broadband and GCI Liberty ordinary shares. We have marginally increased our Interactive Brokers position and sold portions of our stakes in MEI Pharma and Discovery, as prices reached closer to fair value.

As of June 30th 2018, cash was 17% of our portfolio.

Culibrk Partnership
Largest Gains and Losses
For the Three Months ended June 30th 2018
(% contribution to the portfolio)

Largest Gains	Largest Losses
MEI Pharma (+2.2%)	GCI, Liberty Broadband (-3.2%)
Discovery (+1.8%)	Cimpress (-0.5%)
Idorsia (+0.4%)	Interactive Brokers (-0.1%)

GCI, Liberty Broadband

Charter shares declined on Q1 earnings, as video subscriber decline was worse than what Mr. Market expected. It was much better than what we anticipated in our model. Video subscribers are barely free cash flow positive for the business. More likely, they will soon be more profitable when they cut the video cord and move to a broadband-only offering.

CEO, Tom Rutledge, is pursuing a sensible path of expansion of the customer base while improving value for money, service and offering, before resorting to tapping pricing power. Charter EBITDA margins are deliberately one of the lowest in the industry. This will change.

Although Charter shares declined 5% in the quarter, Liberty Broadband declined 10% and GCI Liberty declined 14%, as discounts to NAV widened. We used the occasion to add to our positions.

We like Charter at current valuations, but we like the Malone-controlled vehicles at discounts even better. We wouldn't be surprised if by the end of 2019 the discounts to NAV get closed by consolidating the three entities (Charter, Liberty Broadband and GCI Liberty) into the same structure.

MEI Pharma

We bought the shares in December 2016 at $1.55/share. At the time, net cash per share was $1.4. Today the shares are trading at $4.5 and have $1.2 of net cash per diluted share. The situation has evolved from having substantial free optionality to one where the future returns will come to investors that command pharmaceutical expertise. We care about protecting our downside and have no PhD, so we started selling our shares.

Shares jumped 90% in the second quarter on the back of increased investor awareness to the company. Wells Fargo upgraded their target price from $4/share to $11/share. We can't resist noticing Wells Fargo Securities was a joint lead placement agent on the $75m private placement in May 2018. Mr. Market liked the offering very much. It was filled with renowned names in pharmaceutical investing (and was too dilutive for our taste).

The purpose of the cash raised is to fund clinical development of ME-401 (PI3K oral inhibitor). The drug is intended to be used for treatment of adults with relapsed or refractory follicular lymphoma. Promising results were presented in June at the 2018 American Society of Clinical Oncology Annual Meeting. The company anticipates moving into single-agent registration study by the end of the year.

MEI Pharma's main asset is its drug in phase 3, pracinostat. It is intended to treat adults with newly diagnosed acute myeloid leukemia. In August 2016, MEI Pharma entered into a development and commercialization agreement with Helsinn Group. MEI Pharma is set to receive up to $444m from milestones and a tiered, mid-teens royalty on net sales.

Discovery

Our one-year old journey with Discovery is a prime example of why we love to partner with Mr. Market so much. We don't think much has changed with the business or its prospects since we bought shares in the third quarter of 2017. Yet, Mr. Market has offered us Discovery shares at $26 in July 2017, at $16 in November 2017 and again at $26 in June 2018. We continued accepting his generous offers and bought on the way to $16. We have started to accept some of his bids recently as the share price increase has shifted risk/reward from being a no-brainer back to simply being attractive.

Insider buying since August 2017 has reached $50m, as John Malone bought more shares for $33m in June 2018 at c. $23/C class share. Gunnar Wiedenfels, CFO, and David Wargo, board member, also purchased shares.