Compounder Fund Investors' Letter: Third Quarter of 2021

COMPOUNDER FUND

GROWING YOUR WEALTH AND ENRICHING SOCIETY

Dear investors,

Together with my co-founder Jeremy Chia, I welcome you to Compounder Fund's 2021 third-quarter investors' letter.

During the quarter, Compounder Fund's overall net-of-fee return for the earliest series of its Class A and Class B shares were both -1.2%. Over the same period, the dividend-adjusted Singapore-dollar returns for the MSCI World Index and the S&P 500 were 1.1% and 1.6%, respectively. The tables below show the returns for Compounder Fund's two share classes (the earliest series for each share class), the MSCI World Index, and the S&P 500, since the birth of the fund.

Total Return	2021 Q1	2021 Q2	Jul 2021	Aug 2021	Sep 2021	2021 Q3	Since inception *
Compounder Fund Class A (after fees)	-1.0%	9.3%	0.8%	3.1%	-4.9%	-1.2%	18.9%
MSCI World Index**	6.9%	8.0%	2.5%	1.8%	-3.1%	1.1%	33.7%
S&P 500**	8.0%	8.7%	3.0%	2.3%	-3.6%	1.6%	36.2%

**Inception date: 13 July 2020*

***MSCI World Index and S&P 500 returns are in Singapore-dollar terms, with dividends reinvested*

Total Return	2021 Q1	2021 Q2	Jul 2021	Aug 2021	Sep 2021	2021 Q3	Since inception *
Compoun-der Fund Class B (after fees)	-1.0%	9.3%	0.8%	3.1%	-4.9%	-1.2%	14.2%
MSCI World Index**	6.9%	8.0%	2.5%	1.8%	-3.1%	1.1%	28.9%
S&P 500**	8.0%	8.7%	3.0%	2.3%	-3.6%	1.6%	29.4%

**Inception date: 1 October 2020*
***MSCI World Index and S&P 500 returns are in Singapore-dollar terms, with dividends reinvested*

Jeremy and I are comparing Compounder Fund's performance with that of the MSCI World Index and the S&P 500 to provide an indication of how the fund is faring against a broad group of stocks that are listed across the world and in the USA.

As you know, Compounder Fund's investment mandate is global in nature. This means the fund can invest in any listed stock in the world; it also makes the MSCI World Index a sensible index to use for context about Compounder Fund's performance. But since most of Compounder Fund's holdings are currently US-listed stocks, it's also important to Jeremy and me that we compare the fund's performance with a prominent US stock market index, in this case, the S&P 500. If Compounder Fund is doing better than the MSCI World Index, comparing the fund's return with the S&P 500 helps us to see if the outperformance is simply due to a rising tide in US stocks.

It's been around a year and a quarter since we started investing Compounder Fund's capital on 13 July 2020. The fund's return has substantially underperformed both market indices since its inception. Other than the fact that it's unpleasant to see the underperformance, what else can be gleaned from the fund's return so far? Nothing really. The time frame is still too short for any useful observations to be made. With your strong support, we are playing the long game here at Compounder Fund. **And please never underestimate the importance of your role in shaping Compounder Fund's long-term return**. In the "*Investing thoughts: What's our edge?*" section of our **2020 fourth-quarter letter**, we discussed the three sources of investing edge that exist in the stock market and how all of you - Compounder Fund's investors - **play a critical role in helping Jeremy and me produce the behavioural edge**.

Judging our performance

In all our **previous quarterly investors' letters**, I've provided a discussion on how Jeremy and I intend to judge Compounder Fund's performance. If you've read any of our previous letters, this section will be familiar, but there's no harm in a refresher! If this is the first investors' letter from us that you're seeing, then *please* read this section (no cheating allowed!).

Our target for Compounder Fund is to generate an annual return of 12% or more over the long run (a five- to seven-year period, or longer) for the fund's investors, net of all fees. When Warren Buffett was running an investment fund in the 1950s and 1960s, he shared his thoughts on a suitable time frame to assess the performance of an investment manager:

> "While I much prefer a five-year test, I feel three years is an absolute minimum for judging performance. It is a certainty that we will have years when the partnership performance is poorer, perhaps substantially so, than the [market]. If any three-year or longer period produces poor results, we all should start looking around for other places to have our money. An exception to the latter would be three years covering a speculative explosion in a bull market."

Jeremy and I fully agree with Buffett. **We hope that you, as an investor in Compounder Fund, will judge its performance over a three-year period at the *minimum***.

It will be very disappointing for the both of us too if Compounder Fund fails to beat the MSCI World Index and S&P 500 over a five- to seven-year timeframe. Jeremy and I believe that having a thoughtful investment framework to find Compounders, and the willingness and ability to hold the shares of Compounders for years, will likely lead us to market-beating returns. (Do note, however, that we harbour *no* illusion that we're able to beat the indices each month, each quarter, or each year.) The willingness comes from our ingrained long-term view towards the market. The ability, though, comes from *your* keen understanding of our investment approach - so thank you for taking the time to understand how we're running Compounder Fund and for seeing the logic of our ways.

Some caution is needed here: **The stock market is volatile**. The returns of Compounder Fund will very likely *not* be smooth - this is just how stocks work. If the market falls, you should expect Compounder Fund to decline by a similar magnitude or more. But this will likely only be short-term pain. Jeremy and I believe in the long-term potential of the stock market, and especially in the underlying businesses of the stocks in Compounder Fund's portfolio (more on the businesses later).

Speaking of volatility, I want to discuss the important concept of 'the destination'. I first heard about it from a friend - an incredibly impressive young investor and person - who in turn learnt about it from Nicholas Sleep, one of the best investors I've read about. After retiring a few years ago and initially wanting to be outside the public eye, Sleep recently published a collection of his investment letters on the **website** of his charitable foundation, I.G.Y (do check out his letters - they're a fantastic read). To illustrate the concept, I will need you to first think about two sequences of returns over a five year period:

	Year 1	Year 2	Year 3	Year 4	Year 5	Total
Sequence A return	+50%	+28%	+3%	+15%	+5%	**139%**
Sequence B return	+5%	+15%	+3%	+28%	+50%	**139%**

Both sequences result in the same total return - the journey is different, but the destination is the same. Interestingly, even though the end results are identical, we humans tend to prefer Sequence B over Sequence A. This is because Sequence B's return looks better to us compared to Sequence A's, since the former improved over time while the latter deteriorated. As humans, we exhibit natural psychological biases that cause us to favour more recent data.

This is important to note because **when investing in stocks, it's often much easier to know the destination than it is to know the journey**. Jeremy and I have absolutely *no* control over the journey of returns for Compounder Fund - what we have is a great degree of control over the destination. This 'great degree of control' comes from our careful selection of the companies that Compounder Fund owns shares in. And I say 'a great degree of control' and not 'full control' because luck *will* play some role in Compounder Fund's eventual gain. So you should expect Compounder Fund's return - and indeed, that of all stocks - to bounce around wildly in the short term. Over the long run, Compounder Fund's return should gravitate toward the long term business performances of the companies it owns partial stakes in. There's no guarantee that this gravity will be a strong upward pull! The direction of the gravitational force will depend on whether our insights - on the abilities of the companies in Compounder Fund's portfolio to grow at high rates over the long run - turn out to be correct.

Portfolio changes

On 23 August 2021, I **published an update** on Compounder Fund's portfolio on the fund's website and also notified all of you via email. In the update, I shared all 47 holdings in the fund's portfolio and also mentioned that a new company - Upstart - was added in early-August. As of the date of this letter, the portfolio contains the same 48 holdings, plus two new companies. At first glance, this brings the total number of companies in Compounder Fund's portfolio to 50. As a reminder, Compounder Fund is supposed to have between 30 and 50 companies in its portfolio at any point in time. But two companies in the portfolio - Afterpay and Square - will become one entity soon (we will discuss this development later in this section). So we think it is more appropriate to see Compounder Fund as having 49 holdings instead of 50.

As you know, Compounder Fund is able to accept new subscriptions once every quarter with a dealing date that falls on the first business day of each calendar quarter. In the middle of September 2021, Jeremy and I successfully closed Compounder Fund's fourth subscription window since its initial offering period (which ended on 13 July 2020) and raised S$0.84 million.

This new capital was deployed quickly in the days after the last subscription window's dealing date of 1 October 2021. Jeremy and I invested the new capital in one existing Compounder Fund holding, which is Upstart. The two new companies that we invested in are dLocal and Wise. A few quick words on the new duo:

- Headquartered in Uruguay, dLocal was listed only in June this year. Handling online payments in emerging markets can be a complicated affair as banking penetration rates are low (less than 20% in some cases). Moreover, according to dLocal, "local

card, bank transfer-based payment methods, digital wallet, and cash-like payments, such as using Boleto in Brazil or UPI in India, and making payments at Oxxo in Mexico, are the predominant payment methods for end users" in emerging markets. To help global merchants deal with this complexity when operating in these markets, dLocal provides a fully cloud-based software platform for payments (which merchants can access through one direct API) that reaches 30 emerging markets and is connected with more than 600 local payment methods. Through dLocal's platform, global merchants can safely and efficiently accept and make payments for both cross-border and local transactions in emerging markets. dLocal's platform appears to have struck a chord with global merchants. From 2019 to the 12 months ended 30 June 2021, the total payment volume processed by dLocal has grown at an astounding annualised rate of 102.5%, from US$1.29 billion to US$3.71 billion. Over the same period, dLocal's revenue has increased from US$55.3 million to US$164.7 million, which is an equally remarkable growth rate of 107.0% per year. What's even more impressive is that dLocal has grown this quickly while generating substantial free cash flow. In 2019 and 2020, dLocal produced free cash flow margins (free cash flow as a percentage of revenue) of 52.5% and 81.2%, respectively. There's still plenty of room for dLocal to grow, with more than US$1.2 trillion in total e-commerce-related payment volume taking place in 2020 in most of the countries the company operates in.

- Wise is another incredibly customer-centric company in Compounder Fund's portfolio. The company, which is based in the UK, has its core business in facilitating cross-border money transfers. Wise's customer-centricity can be found in its mission to (emphasis is ours) "build money without borders: instant, convenient, transparent, and **eventually free**." International money transfer is a huge market, with £9 trillion being moved by SMBs (small/medium businesses) and individuals in 2020. But the user experience is poor. According to Wise's July 2021 IPO prospectus, consumers are typically charged a fee of 3% to 7% by traditional banks and the vast majority of consumers don't even know how much they're actually paying. Moreover, the transfers are slow, taking between two to five business days in general. In contrast, Wise charges a much lower fee of around 0.7%, is transparent with its fees, and moves money really quickly (38% of Wise money transfers arrive instantly, and 83% of transfers arrive within 24 hours). With a drastically better product, it's no surprise that Wise has experienced strong growth in its business. The company's number of active customers grew by 82% from 3.3 million in FY2019 (financial year ended 31 March 2019) to 6.0 million in FY2021, with the volume of money transfers doubling from £27.1 billion to £54.4 billion over the same period. This has helped to propel Wise's excellent revenue growth of 53.8% per year from £177.9 million in FY2019 to £421.0 million in FY2021. Wise has not just grown quickly - it has done so while consistently generating profits and free cash flow. From FY2019 to FY2021, Wise's profit and free cash flow grew at impressive annual rates of 73.2% (from £10.3 million to £30.9 million) and 524.8% (from £2.9 million to £113.2 million), respectively.

As of this letter's publication, we have released our investment theses on all the companies that are currently in Compounder Fund's portfolio, except for dLocal and Wise, and they can be **found here**. You can expect to see our theses for dLocal and Wise in the weeks ahead.

In Compounder Fund's **Owner's Manual**, we mentioned that "if Compounder Fund receives new capital from investors, our preference when deploying the capital is to add to our winners and/or invest in new ideas." Upstart's share price had increased by 46% from our first purchase to the time we deployed our new capital in the latest subscription window. But this is not why we think Upstart has been a winner. The company is a winner because its business performance has been brilliant over the longer term as well as in recent quarters. You can find out more about Upstart's business performance in our **investment thesis for the company** as well as in the *"Wonderful businesses"* section of this letter. Here's how Compounder Fund's portfolio looks like as of 10 October 2021:

Company	Weighting	Country/Region of listing	Headquarters
MercadoLibre	4.8%	USA	Argentina
Facebook	4.7%	USA	USA
Netflix	4.5%	USA	USA
PayPal	4.5%	USA	USA
Shopify	4.2%	USA	Canada
Amazon	3.8%	USA	USA
Tencent	2.9%	Hong Kong	China
DocuSign	2.8%	USA	USA
Microsoft	2.7%	USA	USA
Etsy	2.6%	USA	USA
Alphabet	2.5%	USA	USA
Tractor Supply	2.5%	USA	USA
Chipotle Mexican Grill	2.4%	USA	USA
Sea	2.3%	USA	Singapore
Costco	2.3%	USA	USA
The Trade Desk	2.2%	USA	USA
Intuitive Surgical	2.1%	USA	USA
ASML	2.1%	USA	Netherlands
Apple	2.1%	USA	USA
Medistim	2.0%	Norway	Norway
Square	2.0%	USA	USA
Adobe	2.0%	USA	USA
Datadog	2.0%	USA	USA
Okta	1.9%	USA	USA
Veeva Systems	1.8%	USA	USA
Tesla	1.7%	USA	USA
Illumina	1.7%	USA	USA

Salesforce	1.7%	USA	USA
Visa	1.7%	USA	USA
Mastercard	1.6%	USA	USA
Twilio	1.6%	USA	USA
Upstart	1.5%	USA	USA
Markel	1.5%	USA	USA
Starbucks	1.5%	USA	USA
Fiverr	1.4%	USA	Israel
Zoom Video Communications	1.4%	USA	USA
MongoDB	1.3%	USA	USA
Wix	1.3%	USA	Israel
Meituan Dianping	1.3%	Hong Kong	China
Activision Blizzard	1.2%	USA	USA
Pushpay	1.1%	Australia	New Zealand
Wise	1.0%	UK	UK
Haidilao	1.0%	Hong Kong	China
Paycom Software	0.8%	USA	USA
Teladoc	0.7%	USA	USA
Afterpay Touch	0.6%	Australia	Australia
Dlocal	0.5%	USA	Uruguay
Coupang	0.2%	USA	South Korea
Alteryx	0.2%	USA	USA
a2 Milk	0.2%	Australia	New Zealand
Cash	**1.4%**	**-**	**-**

When we first invested in Upstart, it had a **weighting of only 0.6%** in Compounder Fund's portfolio. We wrote in our thesis that "we appreciate all the strengths we see in Upstart's business, but our enthusiasm is currently tempered by the company's high valuation and the fact that the company's AI models have yet to prove itself in a prolonged recession for the US economy." Our concerns on Upstart's valuation and AI models remain. But we still decided to increase our allocation to Upstart because we wanted more exposure to a company that is not just growing rapidly, but doing so while generating healthy profit and free cash flow margins. As of 10 October 2021, Upstart makes up 1.5% of Compounder Fund's portfolio, which can still be considered to be a small position.

Coming to Afterpay and Square, the two companies announced in August 2021 that the latter would be acquiring the former. Square would be buying Afterpay in its entirety and it would pay for each Afterpay share with 0.375 Square shares. Based on Square's share price when the acquisition was announced, Afterpay was valued at A$39 billion (US$29 billion). The deal is expected to be completed in the first quarter of 2022.

Square's announcement to acquire Afterpay surprised us. We think Afterpay is a company with tremendous room for growth (see our **investment thesis**), so we're disappointed that we can no longer directly participate in its future developments once it becomes a part of Square. But there are aspects of the deal that we do like:

- First, we think acquiring Afterpay makes great strategic sense for Square. Square's current business has millions of merchants in its Seller Ecosystem (we have a detailed description of Square's business in our **investment thesis on the company**) and more than 70 million consumers in its Cash App ecosystem. But there's so far no connective tissue that can bind and strengthen both ecosystems. This is where Afterpay comes into the picture. Afterpay's core BNPL (buy now, pay later) service, which also includes merchant discovery functions, can be directly integrated into Cash App. This improves Cash App's consumer engagement. Meanwhile, Square's Seller Ecosystem becomes even more attractive to merchants with the addition of a BNPL function that already has 16 million active users (number of active Afterpay users as of 30 June 2021).
- Second, Afterpay's economic structure could potentially improve by joining Square's family. Currently, Square's Cash App enables consumers to store money. When Afterpay is integrated with Square, Square could potentially allow consumers to pay for their purchases with Afterpay directly with the money they've stored in Cash App and bypass existing payment rails altogether, leading to better profit margins for Afterpay.
- Third, Afterpay's co-founders and current co-CEOs - Anthony Eisen and Nick Molnar - will join Square and continue running Afterpay's business when the acquisition is completed. In our Afterpay thesis, we said that we "rate Eisen and Molnar highly when it comes to execution and innovation." So we're pleased that Afterpay will continue to have them leading the charge. We also think it's a positive signal on the growth prospects of Square + Afterpay that Eisen and Molnar accepted an all-stock offer from Square and will both be joining the company.

Our current intention - which is subject to change depending on developments with Square/Afterpay and the stock market in general - is for Compounder Fund to hold onto its Afterpay shares and have them be automatically converted into Square shares once the acquisition is completed. In this way, we save on unnecessary trading fees. We're eager to observe the growth of the combined entity and are happy to see Square's weighting in Compounder Fund increase because of its acquisition of Afterpay.

Here's a quick high-level geographical breakdown of Compounder Fund's portfolio as of 10 October 2021:

Country/Region	% of Compounder Fund's capital based on country of listing	% of Compounder Fund's capital based on location of headquarters
Argentina	-	4.8%
Australia	2.0%	0.6%
Canada	-	4.2%

China	-	5.2%
Hong Kong	5.2%	-
Israel	-	2.7%
Netherlands	-	2.1%
New Zealand	-	1.3%
Norway	2.0%	2.0%
Singapore	-	2.3%
South Korea	-	0.2%
UK	1.0%	1.0%
Uruguay	-	0.5%
USA	88.4%	71.5%

Wonderful businesses

Jeremy and I are pleased to report that the companies in Compounder Fund's portfolio have, in aggregate, delivered strong growth in the second quarter of 2021. The table below shows the year-on-year revenue growth rates for all the 50 companies that are currently in Compounder Fund's portfolio for each quarter of 2020 and the first two quarters of 2021:

Company	Revenue growth in Q1 2020 from a year ago	Revenue growth in Q2 2020 from a year ago	Revenue growth in Q3 2020 from a year ago	Revenue growth in Q4 2020 from a year ago	Revenue growth in Q1 2021 from a year ago	Revenue growth in Q2 2021 from a year ago
a2 Milk	34.2%	34.2%	-16.0%	-16.0%	-42.9%	**-42.9%**
Activision Blizzard	-2.0%	38.4%	52.4%	21.5%	27.2%	**18.8%**
Adobe	14.0%	13.8%	14.4%	26.3%	22.6%	**22.0%**
Afterpay Touch	96.9%	96.9%	89.4%	89.4%	69.8%	**69.8%**
Alphabet	13.3%	-1.7%	14.0%	23.5%	34.4%	**61.6%**
Alteryx	43.2%	17.3%	25.5%	2.6%	9.1%	**24.8%**
Amazon	26.4%	40.2%	37.4%	43.6%	43.8%	**27.2%**
Apple	0.5%	10.9%	1.0%	21.4%	53.6%	**36.4%**
ASML	9.5%	29.5%	32.5%	5.4%	78.8%	**20.9%**
Chipotle Mexican Grill	7.8%	-4.8%	14.1%	11.6%	23.4%	**38.7%**
Costco	7.3%	12.4%	16.7%	14.6%	21.5%	**17.4%**

Coupang	79.0%	85.5%	94.6%	99.8%	74.3%	**71.3%**
Datadog	87.4%	68.2%	66.3%	56.2%	51.3%	**66.8%**
dLocal	132.0%	47.9%	95.9%	94.4%	123.7%	**185.6%**
DocuSign	38.8%	45.2%	53.5%	56.8%	57.9%	**49.6%**
Etsy	34.7%	136.7%	128.1%	128.7%	141.5%	**23.4%**
Facebook	17.6%	10.7%	21.6%	33.2%	47.6%	**55.6%**
Fiverr	43.7%	81.9%	87.8%	89.2%	100.1%	**59.7%**
Haidilao	-16.5%	-16.5%	26.9%	26.9%	105.9%	**105.9%**
Illumina	1.5%	-24.5%	-12.5%	0.0%	27.2%	**77.9%**
Intuitive Surgical	12.9%	-22.5%	-4.5%	4.0%	17.5%	**71.8%**
Markel	10.5%	11.8%	20.9%	24.4%	18.0%	**28.4%**
Mastercard	3.1%	-18.9%	-14.1%	-6.7%	3.6%	**35.8%**
Medistim	16.2%	-12.1%	-2.5%	-1.6%	-0.5%	**33.1%**
Meituan	-12.6%	8.9%	28.8%	34.7%	120.9%	**77.0%**
Mercado-Libre	37.6%	61.1%	85.0%	96.9%	111.4%	**93.9%**
Microsoft	14.6%	12.8%	12.4%	16.7%	19.1%	**21.3%**
MongoDB	45.8%	39.2%	37.8%	38.4%	39.4%	**43.7%**
Netflix	27.6%	24.9%	22.7%	21.5%	24.2%	**19.4%**
Okta	46.0%	42.7%	42.0%	40.3%	37.3%	**57.4%**
Paycom Software	21.2%	7.2%	12.3%	14.2%	12.3%	**33.3%**
PayPal	11.9%	22.2%	24.7%	23.3%	30.6%	**18.6%**
PushPay	33.2%	52.7%	52.7%	30.9%	30.9%	**-**
Salesforce	30.2%	28.9%	20.1%	19.9%	22.6%	**23.1%**
Sea	103.2%	102.2%	98.7%	101.6%	146.7%	**158.6%**
Shopify	46.7%	97.3%	96.5%	93.6%	110.3%	**56.7%**
Square	44.0%	63.8%	139.6%	140.5%	266.2%	**143.3%**
Starbucks	-4.9%	-38.1%	-8.1%	-4.9%	11.2%	**77.6%**
Teladoc*	114.6%	124.7%	109.3%	145.0%	150.9%	**108.7%**
Tencent	26.4%	29.3%	29.0%	26.4%	25.2%	**20.3%**

Tesla	31.8%	-4.9%	39.2%	45.5%	73.6%	**98.1%**
The Trade Desk	32.8%	-12.8%	31.6%	48.1%	36.8%	**100.9%**
Tractor Supply	7.5%	34.9%	31.4%	31.3%	42.5%	**13.4%**
Twilio	56.5%	45.7%	51.8%	65.5%	61.7%	**66.9%**
Upstart	226.3%	-46.6%	32.1%	38.1%	70.8%	**1307.7%**
Veeva Systems	37.7%	32.5%	34.4%	27.4%	28.6%	**28.8%**
Visa	6.6%	-17.2%	-16.9%	-6.1%	-2.1%	**26.7%**
Wise	-	50.6%	42.1%	40.6%	28.2%	**43.1%**
Wix	23.9%	27.3%	29.2%	38.1%	40.8%	**34.0%**
Zoom	169.0%	355.0%	366.5%	368.8%	191.4%	**54.0%**

Source: Companies' earnings updates
**Numbers for first and second quarters of 2020 are for Livongo; numbers for the third and fourth quarters of 2020, and for the first and second quarters of 2021, are for Teladoc*

Here's a table showing the simple averages of the year-on-year revenue growth rates for the fund's holdings for each quarter of 2020 and for the first quarter of 2021:

Simple averages	Revenue growth in Q1 2020 from a year ago	Revenue growth in Q2 2020 from a year ago	Revenue growth in Q3 2020 from a year ago	Revenue growth in Q4 2020 from a year ago	Revenue growth in Q1 2021 from a year ago	Revenue growth in Q2 2021 from a year ago
Current portfolio	38.6%	36.5%	45.8%	47.7%	56.8%	**79.3%**
Current portfolio (excluding only Upstart)	33.9%	38.2%	46.0%	47.9%	56.5%	**53.7%**
Current portfolio (excluding Upstart, dLocal, and Wise)	32.6%	37.7%	45.1%	47.1%	55.7%	**51.1%**

Source: Companies' earnings updates

In Compounder Fund's **2021 second-quarter investors' letter**, I wrote (emphasis was in the original passage):

> "It's wonderful to see the continued acceleration in revenue growth for Compounder Fund's holdings. But we do not expect our portfolio companies to constantly post an acceleration in their year-on-year revenue growth rates - this would be completely

> unrealistic. In fact, **we expect the portfolio's average year-on-year revenue growth rate for the second quarter of 2021 to decelerate from what was achieved in the first quarter**, as some of our portfolio companies lap a strong second quarter of 2020."

When I wrote that, Compounder Fund's portfolio did not contain Upstart, dLocal, and Wise, meaning there were only 47 companies in the portfolio back then. It turns out that we were right: The simple-average revenue growth in the second quarter of 2021 for the 47 companies had decelerated from the first quarter. But we are still pleasantly surprised that the deceleration was minimal, from growth of 55.7% to growth of 51.1%. **This is the wonderful thing that comes with owning great businesses - they can positively surprise you.** For the second quarter of 2021, the simple-average year-on-year revenue growth rate for all of Compounder Fund's current holdings (excluding Upstart, since the company produced exceptionally high revenue growth that would materially distort the average) was an excellent 53.7%.

We think there's a high chance that our portfolio companies, in aggregate, will continue to achieve pleasing year-on-year revenue growth in the years ahead, although it will be *unrealistic* to keep expecting 50%-plus growth rates. **And if these companies can sustain average annual revenue growth of 25% or more in aggregate for the next five to seven years, *while producing healthy free cash flow* (an important requisite!), we believe it will be exceedingly difficult for Compounder Fund's portfolio to *not* do well**. We're excited to see what the future brings!

And speaking of free cash flow, Compounder Fund's holdings did not manage to strengthen their cash flow muscles in the second quarter of 2021. The table below shows the revenue growth for each company in Compounder Fund's portfolio for the quarter as well as the change in their free cash flow margins for the period. **During the second quarter of 2021, the simple-average free cash flow margin for all the fund's holdings was 15.6%, down from 19.7% a year ago**. A few positive standouts include Datadog (13.3% → 18.1%), Intuitive Surgical (14.1% → 31.9%), and Square (-15.8% → 7.8%). Jeremy and I would have preferred to see growth in the free cash flow margin, but we're not troubled by the decline for two reasons. First, the decline was not significant. For perspective, a company that grew revenue at 53.7%, but saw a fall in the free cash flow margin from 19.7% to 15.6%, would have *increased* its free cash flow by 21.7%. Second, one quarter of decline does not make a trend. Moreover, quarterly cash flows can vary considerably due to the timing of working capital changes and the timing of capital expenditures. We still expect the average free cash flow margin for Compounder Fund's current crop of portfolio companies to grow to around 25% over time.

Company	Revenue growth in Q2 2021 from a year ago	Free cash flow margin in Q2 2021	Free cash flow margin in Q2 2020
a2 Milk	-42.9%	18.6%	28.2%
Activision Blizzard	18.8%	16.3%	39.1%
Adobe	22.0%	33.3%	40.7%

Afterpay Touch	69.8%	-16.8%	27.4%
Alphabet	61.6%	26.0%	22.0%
Alteryx	24.8%	-13.2%	-19.5%
Amazon	27.2%	-1.4%	14.8%
Apple	36.4%	23.3%	24.6%
ASML	20.9%	82.6%	4.2%
Chipotle Mexican Grill	38.7%	6.9%	2.6%
Costco	17.4%	2.9%	6.4%
Coupang	71.3%	-3.1%	-10.4%
Datadog	66.8%	18.1%	13.3%
dLocal	185.6%	-	-
DocuSign	49.6%	31.6%	29.2%
Etsy	23.4%	22.0%	51.3%
Facebook	55.6%	29.7%	3.3%
Fiverr	59.7%	19.9%	9.9%
Haidilao	105.9%	-5.6%	-15.1%
Illumina	77.9%	18.6%	31.9%
Intuitive Surgical	71.8%	31.9%	14.1%
Markel	28.4%	-	-
Mastercard	35.8%	44.8%	37.8%
Medistim	33.1%	18.2%	19.8%
Meituan Dianping	77.0%	-8.8%	-5.9%
MercadoLibre	93.9%	5.9%	68.4%
Microsoft	21.3%	34.1%	32.3%
MongoDB	43.7%	-10.8%	-10.0%
Netflix	19.4%	-2.4%	14.6%
Okta	57.4%	-1.2%	3.4%
Paycom Software	33.3%	8.1%	-0.7%

PayPal	18.6%	17.0%	30.0%
PushPay	-	-	30.8%
Salesforce	23.1%	2.7%	6.1%
Sea	158.6%	4.8%	-2.4%
Shopify	56.7%	5.2%	23.3%
Square	143.3%	7.8%	-15.8%
Starbucks	77.6%	18.8%	-17.7%
Teladoc	108.7%	7.9%	12.6%
Tencent Holdings	20.3%	12.5%	24.7%
Tesla	98.1%	5.1%	6.6%
The Trade Desk	100.9%	1.2%	54.2%
Tractor Supply	13.4%	14.3%	26.8%
Twilio	66.9%	0.5%	-4.3%
Upstart	1307.7%	47.7%	111.1%
Veeva Systems	28.8%	25.0%	28.2%
Visa	26.7%	69.1%	58.7%
Wise	43.1%	-	-
Wix	34.0%	4.7%	19.8%
Zoom	54.0%	44.5%	56.1%
Simple average (excluding Upstart)	**53.7%**	**15.2%**	**17.7%**
Simple average (with Upstart)	**79.3%**	**15.6%**	**19.7%**

Source: Companies' earnings updates

(As of the publication of this letter, there's no quarterly free cash flow data available for dLocal, Pushpay, and Wise for the second quarter of 2021. We did not include free cash flow data for Markel because we don't think it's as important for the company - it is predominantly an **insurer and investment holding company**, so we think the book value holds more meaning.)

In summary, we are pleased with the aggregate business performance of Compounder Fund's portfolio holdings.

Investing thoughts: Investing in China

Ever since Jeremy and I started working on Compounder Fund, we've been regularly asked - by some of you and some of the fund's prospective investors - about our views on investing in China. Compounder Fund is able to invest in stocks all around the world and its portfolio currently has three companies that are based in China, namely, Haidilao, Meituan, and Tencent (in alphabetical order). Given the recent crackdown on the business practices of Chinese companies across a broad range of industries by the country's regulators (*Reuters* and *Bloomberg* have good summaries that can be found **here**, **here** and **here**), we think now's a good time to share our current thoughts on investing in the country more widely with all of you.

When we've been asked about investing in China, our response has always been along these lines:

> China has high potential to achieve strong economic growth for a long time and there's a powerful current of technological innovation flowing through the country. These traits make China-based companies attractive to us. But we still would not be comfortable enough with Chinese companies to make them a significant part of Compounder Fund's portfolio. In our opinion, China's one-party political system - where the Chinese Communist Party has near-absolute power to implement any policies they favour without the civic deliberation and mechanisms for checks-and-balances that are common in democracies - is a huge risk.

As a reflection of our stance, Haidilao, Meituan, and Tencent collectively accounted for 8.0% of Compounder Fund's portfolio in **early August last year**, when we had finished deploying the fund's initial capital. With the recent developments in China, there's been a slight change to our stance. **We still like Chinese companies, but we're even *less* inclined now to have them be a significant part of the fund's portfolio.** As I showed in the "*Portfolio changes*" section of this letter, our three Chinese companies have a total weighting of 5.2% in the portfolio as of 10 October 2021.

In totality, we think the recent changes in China's regulatory landscape are a net positive in the long run for Chinese society and thus Chinese businesses. For example:

- Education companies in China are barred from making profits now, but this significantly reduces any unnecessary education-related mental pressure that a large group of the country's society (students and their parents) have been suffering from.
- The ability for dominant Chinese technology companies to exhibit monopolistic behaviour has been reduced and this could spur entrepreneurship and innovation in the country.
- Delivery workers' interests are now better protected and this is a win because companies are better able to grow sustainably if they take care of all their constituents (employees, suppliers, shareholders, and the community).
- The disparity between the haves and have-nots in China is wide and the slew of regulatory changes the Chinese government has implemented in recent times are also meant to help reduce inequality in the country.

But in reading the current regulatory reforms, we can't tell what the key intention of the Chinese government is. Does the government harbour a desire to consolidate power and the reforms seen to-date are just the beginning of a process to do so? Or does the government want to strengthen the foundation of China's private-sector economy? **We don't know, and this is what worries us. Our biggest fears when investing in China are politically-motivated compulsory confiscation and regulatory destruction**. And in a one-party political system such as China's, there is no effective recourse when the government is acting in an unjust manner toward private-sector companies and their shareholders. There are two things in particular we've only learnt about recently that have concerned us.

First, in April 2020, the Chinese government took a 1% stake in the US-listed Chinese social media company, Weibo, for RMB10.7 million. But according to *Stratechery* founder Ben Thompson, a 1% stake in Weibo at that time should have been worth around RMB531 million based on the company's market capitalisation. Second, according to the *Sinocism* newsletter founded by Bill Bishop, China's president, Xi Jinping, praised a few individuals as exemplars of patriotic entrepreneurs in a July 2020 speech. Xi said:

> "[Original Mandarin speech] 从清末民初的张謇，到抗战时期的卢作孚、陈嘉庚，再到新中国成立后的荣毅仁、王光英，等等，都是爱国企业家的典范。
>
> [My English translation] From Zhang Jian in the late Qing dynasty, to Luo Zuofu and Chen Jiageng in the Sino-Japanese war, to Rong Yiren and Wang Guangying after the founding of the People's Republic of China, and many more - they are all role models of patriotic entrepreneurs."

But Bishop noted that the entrepreneurs that Xi name-dropped all appeared to have suffered:

> "Zhang Jian I believe died broke, Lu Zuofu killed himself in 1952, and Rong Yiren and Wang Guangying "donated" all their businesses to the government."

Jeremy and I are definitely not experts in Chinese politics. My sharing in this section is *not* meant to be seen as the "correct" interpretation of what's going on in China. I just want to share, as clearly as I can, how we currently think about investing in Chinese companies. We're open to changing our minds (in both directions!), and we would love to hear from any of you who are keen to engage with us on investing in China. The more diverse viewpoints we can learn from, the better-informed we'll be.

Investing thoughts: The need for patience

One of my favourite investing stories involves one of Warren Buffett's best - maybe even his best - investment returns. This return came from his 1973 purchase of The Washington Post Company (WPC) shares. Today, WPC is known as Graham Holdings Company. Back then, it was the publisher of the influential US-based newspaper, *The Washington Post*.

Buffett did not invest much in WPC, but the percentage-gain is stunning. Through Berkshire Hathaway, he invested US$11 million in WPC in 1973. By the end of 2007, Berkshire's stake in WPC had swelled to nearly US$1.4 billion, which is a gain of over 10,000%. But the percentage gain is not the most interesting part of the story. **What's interesting is that, first, WPC's share price fell by more than 20% shortly *after* Buffett invested, and then stayed in the red for three *years*. Second, WPC was a great bargain in plain sight when Buffett started buying shares**. In Berkshire's **1985 shareholders' letter**, Buffett wrote (emphasis is mine):

> "We bought all of our WPC holdings in mid-1973 at a price of not more than one-fourth of the then per-share business value of the enterprise. *Calculating the price/value ratio required no unusual insights.* Most security analysts, media brokers, and media executives would have estimated WPC's intrinsic business value at $400 to $500 million just as we did. And its $100 million stock market valuation was published daily for all to see.
>
> *Our advantage, rather, was attitude*: we had learned from Ben Graham that the key to successful investing was the purchase of shares in good businesses when market prices were at a large discount from underlying business values."

Buffett has investing acumen and privileged-access to deals that many of us do not have. But there are also times when common sense and patience are more important traits than acumen in making a great investment. Buffett himself said that no special insight was needed to value WPC back in 1973. **What was needed for him to earn a smashing return were simple and attainable things: The right attitude and patience**.

How many investors do you think have the patience to hold on through three years of losses? Not many, would be my guess. But Buffett did, and he was eventually well rewarded. Not every form of participation in the financial markets requires patience. **But for market participants who look at stocks as a piece of a business and are investing on the basis of a business's underlying value (like what Jeremy, I, and all of you are doing at Compounder Fund) patience may well be *necessary*, even if you have purchased shares of the best company at a bargain price.** This is why we often talk about the importance of having a long-term investing mindset.

Buffett's experience with WPC - of first losing, then winning - is far from an isolated incident. Another of my favourite investing stories has the same element. The story starts on 2 July 1998, when brothers David and Tom Gardner - co-founders of The Motley Fool, and two of my investing heroes - **were invited** to an American television programme called *The View*. In the show, the Gardner brothers were asked to name a stock for the programme's new host to invest in and they happily obliged.

About six weeks later, the Gardners re-appeared in *The View*. But this time, they were booed by the live audience. David even found out later from his friend, a long-time follower of *The View*, that no guest had ever been booed on the show prior to this. It turns out that the Gardners' recommended stock had fallen by a third in value in the six weeks between their first and second appearances in *The View*. But the brothers still had faith in the investment and urged the host to hold on for the long-term.

I don't know if *The View's* host ever did invest in the company that the Gardners recommended. But if she did, and had she held on since 2 July 1998, she would likely be very happy today. The stock in question is the global coffee giant, Starbucks, which is also one of Compounder Fund's holdings. In September 1997, Starbucks had less than 1,500 outlets and was mostly a domestic growth story in the USA. Today, it's a bona fide global company with more than 33,000 stores in many different countries around the world. On 2 July 1998, Starbucks's share price was US$3.54. About six weeks later (on 14 August 1998), it was US$2.40. A year after 2 July 1998, Starbucks's share price was US$3.45, lower than when the Gardners first appeared in *The View.* Today, the coffee powerhouse's share price is more than US$111. In a similar manner to WPC, Starbucks looked like a loser over the short-term, but turned out to be a world-class winner over the long-term.

House-keeping matters and what's next

Jeremy and I are happy to note that earlier this year, Compounder Fund completed its first-ever annual audit for 2020. With the support of the teams at Baker Tilly (Compounder Fund's auditor) and Crowe Horwath First Trust (Compounder Fund's fund administrator), the audit was a smooth process. On 14 May 2021, we sent a digital copy of Compounder Fund's audited financial statements to all of the fund's investors. If you did not receive it, or if you joined the fund as an investor after 14 May 2021 and would like a digital copy of the audited financial statements for 2020, please let Jeremy and me know.

As Jeremy and I have shared before, giving back to society is one of the four key pillars of Compounder Fund's mission to "Grow *Your Wealth* & Enrich Society." In the fund's website, we **mentioned** that "we are setting aside at least 10% of every dollar we earn from Compounder Fund in each year for charities of our choice" and that "we will audit our giving." We have contracted Baker Tilly to perform the audit for us. The first audit will cover the period from November 2019 (when we started building the fund) to December 2021. After which, an audit will be conducted on an annual basis. If you are interested to know more, feel free to reach out!

Another of the key pillars of Compounder Fund's mission involves investor education. To this end, Jeremy and I are running Compounder Fund transparently. We already mentioned that we have released the investment theses for 48 of Compounder Fund's current holdings (for your convenience, they can be **found here**) and that we will be publishing the theses for the remaining two holdings (dLocal and Wise) in the coming weeks. We will be informing you when they're published.

Compounder Fund's next subscription window will close in the middle of December 2021 and it will have a dealing date on the first business day of January 2022 (which should be 3rd January). If you would like to increase your investment in the fund, please submit the relevant paperwork by the middle of December 2021. Jeremy and I are happy to help you with any queries you may have.

Optimism (as always!)

There are a myriad of important political, social, economic, and healthcare issues that are plaguing our globe today. But Jeremy and I are still long-term optimistic on the stock market. This is because we still see so much potential in humanity. There are nearly 7.9 billion individuals in the world **right now**, and the vast majority of people will wake up every morning wanting to improve the world and their own lot in life. *This* is ultimately what fuels the global economy and financial markets. Miscreants and Mother Nature will occasionally wreak havoc but we have faith that humanity can clean it up.

To us, investing in stocks is ultimately the same as having faith in the long-term positivity of humanity. And we will remain long-term optimistic on stocks so long as we continue to have this faith. **The only exception is when stocks become wildly overpriced - and we don't think this is the case today**. This does *not* mean that stocks are cheap or that stocks won't fall in the months or next year or two ahead (remember, we don't know what the journey will look like!). It only means that we think valuations are somewhat reasonable and that investing now will likely lead to a satisfactory outcome, if we have a multi-year time horizon and we're invested in fast-growing companies. **With your support, we have both ingredients at Compounder Fund.**

Final words

If you have any questions related to Compounder Fund's administrative matters or our general investment thinking, please know that our email inboxes are always open to you. Thank you again for trusting Jeremy and me with your hard-earned capital. We deeply appreciate your trust and support, your belief in Compounder Fund's mission to "Grow *Your* Wealth & Enrich Society," and your understanding of the investing game that Jeremy and I are playing. (I discussed the investing game we're playing in the "*Investing thoughts: Playing the right game*" section of Compounder Fund's **2021 second-quarter investors' letter**.)

Your deep understanding of our long-term approach gives us the space we need to do our work (analysing businesses and their possible long-run futures) to the best of our abilities, for you. **So, thank you all for being the wonderful investors that you all are. And again, never underestimate your importance in helping to shape Compounder Fund's long-run return.**

You can expect to see Compounder Fund's 2021 fourth-quarter investors' letter in mid-January 2022. Till then, stay safe and take care!

Excelsior,
Chong Ser Jing
Co-founder and Portfolio Manager, Compounder Fund
12 October 2021

P.S.: You can find all of our **past investors' letters here**.

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