Compounder Fund Investors' Letter: Second Quarter of 2022

COMPOUNDER FUND
GROWING YOUR WEALTH AND ENRICHING SOCIETY

Note (24 May 2024): Information related to a global stock market index has been redacted from this letter because of intellectual-property restrictions. As such, we believe the S&P 500 is currently sufficient for context about Compounder Fund's performance. This is because the fund's portfolio is heavily weighted toward US stocks. In addition, the S&P 500's return has been higher than a broad collection of global stocks since Compounder Fund's inception, and US stocks have by far the largest market capitalisation among stocks around the world. We will revisit our decision on displaying global stock market returns data in the future if there are significant changes to Compounder Fund's portfolio from a geographic perspective, or if US stocks start lagging their global peers.

Dear investors,

Together with my co-founder Jeremy Chia, I welcome you to Compounder Fund's 2022 second-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 -27.0%. Over the same period, the dividend-adjusted Singapore-dollar returns for the [redacted] and the S&P 500 were -13.9% and -14.0%, respectively. Tables 1 and 2 below show the returns for Compounder Fund's two share classes (the earliest series for each share class), the [redacted], and the S&P 500, since the birth of the fund.

Table 1

Time period	Compounder Fund Class A (after fees)	[redacted]	S&P 500**
2020*	11.2%	[redacted]	14.2%
2021	0.9%	[redacted]	31.2%
Q1 2022	-18.9%	[redacted]	-4.1%
Apr 2022	-15.3%	[redacted]	-6.9%
May 2022	-7.2%	[redacted]	-0.7%
Jun 2022	-7.2%	[redacted]	-6.9%
Q2 2022	-27.0%	[redacted]	-14.0%
Year-to-date 2022	-40.8%	[redacted]	-17.5%
Total return since inception*	-33.7%	[redacted]	23.7%
Annualised return since inception*	-18.9%	[redacted]	11.4%

**Inception date: 13 July 2020*
***[redacted] and S&P 500 returns are in Singapore-dollar terms, with dividends reinvested*

Table 2

Time period	Compounder Fund Class B (after fees)	[redacted]	S&P 500**
2020*	6.8%	[redacted]	8.6%
2021	0.9%	[redacted]	31.2%
Q1 2022	-18.9%	[redacted]	-4.1%
Apr 2022	-15.3%	[redacted]	-6.9%
May 2022	-7.2%	[redacted]	-0.7%
Jun 2022	-7.2%	[redacted]	-6.9%
Q2 2022	-27.0%	[redacted]	-14.0%
Year-to-date 2022	-40.8%	[redacted]	-17.5%
Total return since inception*	-36.3%	[redacted]	17.5%
Annualised return since inception*	-22.8%	[redacted]	9.7%

**Inception date: 13 July 2020*
***[redacted] and S&P 500 returns are in Singapore-dollar terms, with dividends reinvested*

Jeremy and I are comparing Compounder Fund's performance to that of the [redacted] 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 [redacted] a sensible index 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 [redacted], comparing the fund's return with the S&P 500 helps us see if the outperformance is simply due to a rising tide in US stocks.

It's been two years since we started investing Compounder Fund's capital on 13 July 2020 and it's been disappointing. The fund's return has not only been negative since its inception, but it has also substantially underperformed both market indices. The poor stock price performance of many of Compounder Fund's holdings in 2021 has continued in 2022 thus far. I discussed the stock price performances in a number of past Compounder Fund letters (the **2021 fourth-quarter letter**; the **Solidarity** letter sent on 27 January 2022; and the **2022 first-quarter letter**). In all of them, I pointed out the stark differences between the growing businesses of Compounder Fund's holdings and their declining stock prices. I will have more to say on this topic in the "*Wonderful businesses"* section of this letter.

Compounder Fund's poor return since inception is painful to experience. But the time frame is still too short for any useful observations to be made. Stock prices and business fundamentals can diverge wildly in the short run and this is what is happening to Compounder Fund. Over the long run, business fundamentals and stock prices tend to converge. With your strong support, we are taking the long-term approach here at Compounder Fund, where the fund's return will come from the underlying business performances of its holdings. **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**, I 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**. Jeremy and I are thankful that, in a period of volatile stock prices as was seen over the recent past, **all of you have helped us produce the behavioural edge.** You have provided us with gentle patience and the space to engage in long-term thinking about stocks. **Most importantly, you did *not* panic. So, *thank you* - Jeremy and I are incredibly fortunate to count everyone of you as investors in Compounder Fund**.

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 [redacted] and the 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.

Some caution is needed here: **The stock market is volatile**. The returns of Compounder Fund in the future will very likely *not* be smooth - this is just how stocks work. And indeed, we've already experienced significant volatility in the results of Compounder Fund since its inception. If the market falls in the future, 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.

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 in the mid-2010s and initially wanting to be outside the public eye, Sleep published a collection of his investment letters in 2021 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, shown in Table 3:

Table 3

	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. We've already seen such a bounce happen in an unwanted direction (downwards!) but 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 though! The direction of the gravitational force will depend on whether our insights - on the abilities of Compounder Fund's companies to grow their businesses at high rates over the long run - turn out to be correct. **In this regard, it's been so far, so good, as I'll discuss in the "*Wonderful businesses"* section of this letter**.

Portfolio changes

Compounder Fund's **2022 first-quarter letter** was published on 13 April 2022. In it, I shared all 50 holdings that were in the fund's portfolio at the time. Since then, there have been no changes to the fund's holdings, although some involuntary removals could soon happen.

First, there's the acquisition of Activision Blizzard by Microsoft that I first discussed in the 2022 first-quarter letter. Activision's shareholders approved the all-cash deal in late April and it is expected to be completed before 30 June 2023, subject to regulatory approval by US authorities. Our intention with Activision's shares - which could change depending on developments at both companies and the stock market in general - remains. We intend for Compounder Fund to hold onto its Activision shares and receive the cash from Microsoft once the acquisition is completed. Doing so can prevent Compounder Fund from paying unnecessary trading fees. Moreover, the significant gap between Activision's stock price and the acquisition price that I first mentioned in the 2022 first-quarter letter still exists; selling now would mean forfeiting a potential gain of around 20% (a stock price of US$78 as of 10 July 2022 compared to the acquisition price of US$95; a stock price of US$80 was mentioned in the 2022 first-quarter letter).

Second, Pushpay announced in late-April and late-May that it had received unsolicited and non-binding offers by multiple third parties, including two existing shareholders, to acquire the company. After Pushpay received the first offer, management appointed investment bank Goldman Sachs as a financial advisor. There's been no update by Pushpay since, but we assume that discussions are ongoing between the company's leaders and these third-parties. Jeremy and I think Pushpay's long-term growth prospects are healthy and we intend for Compounder Fund to hold onto its Pushpay shares for now (our intention is, again, subject to change depending on developments at the company and stock market in general). We'll make new decisions as and when Pushpay releases information about the offers.

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 June 2022, Jeremy and I successfully closed Compounder Fund's seventh subscription window since its initial offering period (which ended on 13 July 2020) and raised a net amount of S$0.28 million. This new capital was deployed quickly in the days after the last subscription window's dealing date of 1 July 2022. Jeremy and I invested the new capital in five existing Compounder Fund holdings. They are (in alphabetical order): Adyen, Datadog, dLocal, Microsoft, and TSMC.

As of this letter's publication, we have released our investment theses on all 50 companies that are currently in Compounder Fund's portfolio. We've also published our thoughts on why we sold a2 Milk and JD.com in early-April this year. All our theses can be **found here**. In the future, if and when we add new companies to the portfolio or completely exit any of the 50 companies, we will be releasing our detailed thoughts for these actions.

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." Not all of the five existing holdings in Compounder Fund's portfolio that we added capital to have seen their stock prices rise strongly after we initially invested in them. But all of them have executed well since our investments and they've produced great results (with the exception of Adyen, because the company has yet to release any new earnings updates since our initial investment) as I'll soon touch on in the "*Wonderful businesses*" section of this letter. They are winners, according to our definition. Here's how Compounder Fund's portfolio looks like as of 10 July 2022:

Table 4

Company	Weighting	Country/Region of listing	Headquarters
Amazon	4.3%	USA	USA
Meta Platforms	4.3%	USA	USA
Microsoft	4.2%	USA	USA
Tractor Supply	4.2%	USA	USA
Costco	4.1%	USA	USA
Alphabet	4.0%	USA	USA
MercadoLibre	3.8%	USA	Argentina
Apple	3.5%	USA	USA
Tencent	3.4%	Hong Kong	China
Tesla	3.1%	USA	USA
DataDog	2.9%	USA	USA
Chipotle Mexican Grill	2.8%	USA	USA
Markel	2.5%	USA	USA
Mastercard	2.4%	USA	USA
Visa	2.4%	USA	USA
The Trade Desk	2.4%	USA	USA
Medistim	2.3%	Norway	Norway
Intuitive Surgical	2.2%	USA	USA
Netflix	2.2%	USA	USA
Adobe	2.1%	USA	USA
Veeva Systems	2.1%	USA	USA
ASML	2.1%	USA	Netherlands
PayPal	2.0%	USA	USA
Activision Blizzard	2.0%	USA	USA
MongoDB	1.9%	USA	USA
Shopify	1.8%	USA	Canada
Etsy	1.8%	USA	USA
Salesforce	1.7%	USA	USA

Table 4 (continued from above)			
Company	**Weighting**	**Country/Region of listing**	**Headquarters**
Starbucks	1.7%	USA	USA
Meituan Dianping	1.5%	Hong Kong	China
Okta	1.4%	USA	USA
Illumina	1.3%	USA	USA
Zoom	1.3%	USA	USA
DocuSign	1.2%	USA	USA
Block*	1.2%	USA	USA
Adyen	1.2%	Netherlands	Netherlands
PushPay	1.2%	Australia	New Zealand
TSMC	1.1%	USA	Taiwan
Haidilao	1.0%	Hong Kong	China
dLocal	1.0%	USA	Uruguay
Sea	1.0%	USA	Singapore
Twilio	0.9%	USA	USA
Paycom Software	0.8%	USA	USA
Wix	0.8%	USA	Israel
Fiverr	0.5%	USA	Israel
Wise	0.5%	UK	UK
Teladoc	0.5%	USA	USA
Upstart	0.3%	USA	USA
Alteryx	0.2%	USA	USA
Coupang	0.2%	USA	South Korea (Republic of Korea)
Cash	**0.5%**	**-**	**-**

**0.3% of the Block position comes from Block shares that are listed in Australia, but for all intents and purposes, we see the Australia-listed Block shares as being identical to the US-listed variety*

Our biggest addition in early-July 2022 was to Datadog, which provides a software platform for companies to monitor and analyse the performance of their technology stack (see **our thesis on Datadog** for more details). The company's growth has been impressive. Table 5 shows Datadog's revenue growth and free cash flow margin in each quarter going back to 2020; note the rapid increases in revenue and the improvement in the free cash flow margin to an excellent 35.8% currently. The table also lays out the high dollar-based net retention rate and robust growth in customer numbers that Datadog has achieved.

Table 5

Quarter	Datadog year-on-year revenue growth	Datadog free cash flow margin	Datadog dollar-based net retention rate	Datadog customers
Q1 2020	87.4%	14.7%	>130%	11,500
Q2 2020	68.2%	13.3%	>130%	12,100
Q3 2020	66.3%	18.5%	>130%	13,100
Q4 2020	56.2%	9.4%	>130%	14,200
Q1 2021	51.3%	22.4%	>130%	15,200
Q2 2021	66.8%	18.1%	>130%	16,400
Q3 2021	74.9%	21.1%	>130%	17,500
Q4 2021	83.7%	32.7%	>130%	18,800
Q1 2022	82.8%	35.8%	>130%	19,800

Source: Datadog earnings updates

Datadog's platform is becoming ever more critical for companies that are migrating to the cloud and/or undergoing a digital transformation. These trends are still early and, in our view, they are durable over the long run. Moreover, Datadog's business could be resilient even in the face of a weakening economy. Here are some pertinent comments from Datadog's management in the company's latest earnings conference call held in May this year:

> "We remain confident that cloud migration and digital transformation are drivers of our long-term opportunity and our multiyear trends that are still early in their lifecycles. We believe it is increasingly critical for companies to embark on these journeys in order to move faster, create competitive differentiation, enable strategic change, and serve their customers. And we believe we can help customers manage the complexity that comes with this transformation and that the Datadog unified platform is more than ever critical to understand, improve and secure their modern stacks and businesses…
>
> …[Question] As the economic environment and the outlook for GDP growth continues to be a little bit wobbly with higher rates, how should we think about the defensibility of the Datadog consumption business?
>
> [Answer] We believe that digital and cloud projects are still very high priority and are not being deprioritized. We haven't seen that. We think we're still early on. So with the data we have so far, we think there will be continued strong investment. There is always some volatility across our customer base. Our customer base is very well diversified across industries, and we benefited from that over time. So whereas we're not macro forecasters, and there may well be some sensitivity. We believe the long-term trends in digital migration and cloud will still be very strong throughout that cycle."

Despite the impressive execution by Datadog's management and the presence of powerful and lasting tailwinds behind the company's back, the stock price was down by 47% in the first half of 2022. We think the wide divergence between Datadog's stock price and business fundamentals presents a good chance for us to add to our position in the company.

Here’s a quick high-level geographical breakdown of Compounder Fund’s portfolio as of 10 July 2022:

Table 6

Country/Region	% of Compounder Fund’s capital based on country of listing	% of Compounder Fund’s capital based on location of headquarters
Argentina	-	3.8%
Australia	1.2%	-
Canada	-	1.8%
China	-	6.0%
Hong Kong	6.0%	-
Israel	-	1.3%
Netherlands	1.2%	3.3%
New Zealand	-	1.2%
Norway	2.3%	2.3%
Singapore	-	1.0%
South Korea	-	0.2%
Taiwan	-	1.1%
UK	0.5%	0.5%
Uruguay	-	1.0%
USA	88.4%	76.0%

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 first quarter of 2022. Table 7 below shows the year-on-year revenue growth rates for the first quarter of 2022, as well as for each quarter of 2020 and 2021, for all the 50 companies that are currently in Compounder Fund’s portfolio (the ones in Table 4):

Table 7 (Year-on-year revenue growth)

Company	Q1 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021	Q2 2021	Q3 2021	Q4 2021	Q1 2022
Activision Blizzard	-2.0%	38.4%	52.4%	21.5%	27.2%	18.8%	5.9%	-10.4%	**-22.3%**
Adobe	14.0%	13.8%	14.4%	26.3%	22.6%	22.0%	20.0%	9.1%	**14.4%**
Adyen	26.6%	26.6%	29.1%	29.1%	46.0%	46.0%	46.7%	46.7%	**-**
Alphabet	13.3%	-1.7%	14.0%	23.5%	34.4%	61.6%	41.0%	32.4%	**23.0%**
Alteryx	43.2%	17.3%	25.5%	2.6%	9.1%	24.8%	-4.8%	8.3%	**33.0%**
Amazon	26.4%	40.2%	37.4%	43.6%	43.8%	27.2%	15.3%	9.4%	**7.3%**
Apple	0.5%	10.9%	1.0%	21.4%	53.6%	36.4%	28.8%	11.2%	**8.6%**
ASML	9.5%	29.5%	32.5%	5.4%	78.8%	20.9%	32.4%	17.2%	**-19.0%**
Block	44.0%	63.8%	139.6%	140.5%	266.2%	143.3%	26.7%	29.1%	**-21.7%**
Chipotle Mexican Grill	7.8%	-4.8%	14.1%	11.6%	23.4%	38.7%	21.9%	22.0%	**16.0%**
Costco	7.3%	12.4%	16.7%	14.6%	21.5%	17.4%	16.6%	15.9%	**16.2%**
Coupang	79.0%	85.5%	94.6%	99.8%	74.3%	71.3%	48.1%	33.5%	**21.6%**
Datadog	87.4%	68.2%	66.3%	56.2%	51.3%	66.8%	74.9%	83.7%	**82.8%**
dLocal	132.0%	47.9%	95.9%	94.4%	123.7%	185.6%	122.5%	120.1%	**117.2%**
Docu-Sign	38.8%	45.2%	53.5%	56.8%	57.9%	49.6%	42.4%	34.8%	**25.5%**
Etsy	34.7%	136.7%	128.1%	128.7%	141.5%	23.4%	17.9%	16.2%	**5.2%**
Fiverr	43.7%	81.9%	87.8%	89.2%	100.1%	59.7%	42.0%	42.7%	**26.9%**
Haidilao	-16.5%	-16.5%	26.9%	26.9%	105.9%	105.9%	11.5%	11.5%	**-**
Illumina	1.5%	-24.5%	-12.5%	0.0%	27.2%	77.9%	39.5%	25.7%	**11.9%**
Intuitive Surgical	12.9%	-22.5%	-4.5%	4.0%	17.5%	71.8%	30.2%	16.7%	**15.1%**
Markel	10.5%	11.8%	20.9%	24.4%	18.0%	28.4%	14.9%	18.9%	**27.0%**
Master-card	3.1%	-18.9%	-14.1%	-6.7%	3.6%	35.8%	29.9%	26.6%	**24.4%**
Medistim	16.2%	-12.1%	-2.5%	-1.6%	-0.5%	33.1%	22.5%	19.7%	**13.2%**
Meituan Dianping	-12.6%	8.9%	28.8%	34.7%	120.9%	77.0%	37.9%	30.6%	**25.0%**
Mercado Libre	37.6%	61.1%	85.0%	96.9%	111.4%	93.9%	66.5%	60.5%	**63.1%**
Meta Platforms	17.6%	10.7%	21.6%	33.2%	47.6%	55.6%	35.1%	19.9%	**6.6%**
Microsoft	14.6%	12.8%	12.4%	16.7%	19.1%	21.3%	22.0%	20.1%	**18.4%**
Mongo-DB	45.8%	39.2%	**37.8%**	38.4%	**39.4%**	**43.7%**	**50.5%**	55.8%	**57.1%**
Netflix	27.6%	24.9%	22.7%	21.5%	24.2%	19.4%	16.3%	16.0%	**9.8%**
Okta	46.0%	42.7%	42.0%	40.3%	37.3%	57.4%	61.3%	63.2%	**65.3%**
Paycom Software	21.2%	7.2%	12.3%	14.2%	12.3%	33.3%	30.4%	29.0%	**29.9%**
PayPal	11.9%	22.2%	24.7%	23.3%	30.6%	18.6%	13.2%	13.1%	**7.5%**

Table 7 (continued from above; year-on-year revenue growth)									
Company	**Q1 2020**	**Q2 2020**	**Q3 2020**	**Q4 2020**	**Q1 2021**	**Q2 2021**	**Q3 2021**	Q4 2021	**Q1 2022**
PushPay	33.2%	52.7%	52.7%	30.9%	30.9%	9.3%	9.3%	17.0%	**17.0%**
Salesforce	30.2%	28.9%	20.1%	19.9%	22.6%	23.1%	26.6%	25.9%	**24.3%**
Sea	103.2%	102.2%	98.7%	101.6%	146.7%	158.6%	121.8%	105.7%	**64.4%**
Shopify	46.7%	97.3%	96.5%	93.6%	110.3%	56.7%	46.4%	41.1%	**21.7%**
Starbucks	-4.9%	-38.1%	-8.1%	-4.9%	11.2%	77.6%	31.3%	19.3%	**14.5%**
Teladoc*	114.6%	124.7%	109.3%	145.0%	150.9%	108.7%	80.6%	44.6%	**24.6%**
Tencent	26.4%	29.3%	29.0%	26.4%	25.2%	20.3%	13.5%	7.9%	**0.1%**
Tesla	31.8%	-4.9%	39.2%	45.5%	73.6%	98.1%	56.8%	64.9%	**80.5%**
The Trade Desk	32.8%	-12.8%	31.6%	48.1%	36.8%	100.9%	39.3%	23.7%	**43.5%**
Tractor Supply	7.5%	34.9%	31.4%	31.3%	42.5%	13.4%	15.8%	15.3%	**8.3%**
TSMC	42.0%	28.9%	21.6%	14.0%	16.7%	19.8%	16.3%	21.2%	**35.5%**
Twilio	56.5%	45.7%	51.8%	65.5%	61.7%	66.9%	65.2%	53.8%	**48.4%**
Upstart	226.3%	-46.6%	32.1%	38.1%	70.8%	1,307.7%	249.5%	251.6%	**155.6%**
Veeva Systems	37.7%	32.5%	34.4%	27.4%	28.6%	28.8%	26.1%	22.4%	**16.5%**
Visa	6.6%	-17.2%	-16.9%	-6.1%	-2.1%	26.7%	28.6%	24.1%	**25.5%**
Wise	-	50.6%	42.1%	40.6%	28.2%	43.1%	25.4%	33.9%	**31.6%**
Wix	23.9%	27.3%	29.2%	38.1%	40.8%	34.0%	26.2%	16.2%	**13.6%**
Zoom	169.0%	355.0%	366.5%	368.8%	191.4%	54.0%	35.2%	21.4%	**12.3%**

Source: Companies' earnings updates
**Numbers for first and second quarters of 2020 are for Livongo; subsequent numbers 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 the same time frames as Table 7 (**note the high revenue growth rates for every quarter**):

Table 8

Simple averages for revenue growth from year ago in a certain quarter	**Compounder Fund current portfolio**
Q1 2020	37.3%
Q2 2020	35.0%
Q3 2020	45.3%
Q4 2020	47.1%
Q1 2021	57.5%
Q2 2021	78.7%
Q3 2021	39.9%
Q4 2021	35.2%
Q1 2022	**28.1%**

Source: Companies' earnings updates

As I mentioned in the "*Judging our performance"* section of this letter, it's been 'so far, so good' for the business results of Compounder Fund. **The fund's current crop of portfolio companies produced strong year-on-year revenue growth of 28.1% (this is a simple average) in the first-quarter of 2022**, **and this continues from the impressive revenue growth rates seen in prior quarters going back to 2020**. Table 9 below gives perspective on the far-superior growth rates for Compounder Fund's holdings compared to the S&P 500.

Table 9

Simple averages for revenue growth from year ago in a certain quarter	S&P 500	Compounder Fund current portfolio
Q1 2020	Around -2%	37.3%
Q2 2020	Around -10%	35.0%
Q3 2020	Around -2%	45.3%
Q4 2020	Around -0.5%	47.1%
Q1 2021	Around 10%	57.5%
Q2 2021	Around 25%	78.7%
Q3 2021	16.6%	39.9%
Q4 2021	16.1%	35.2%
Q1 2022	**13.4%**	**28.1%**

Source: ***Yardeni Research*** *for S&P 500 data (data for S&P 500 is as of 21 June 2022; revenue growth rate for Compounder Fund is a simple average of the revenue growth from the fund's holdings)*

Similar to what I've been saying in Compounder Fund's past quarterly letters, Jeremy and I continue to think there's a high chance that the fund's portfolio companies will, in aggregate, carry on producing pleasing year-on-year revenue growth in the years ahead. **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 over the same timeframe and when measured from the fund's inception**. We're excited to see what the future brings. Although, we do note that the second quarter of 2022 - and perhaps for the next few quarters too - could see the fund's companies produce slightly weaker revenue growth because of tough comparisons.

And speaking of free cash flow, Compounder Fund's holdings did not manage to strengthen their cash flow muscles in the first quarter of 2022. Table 11 below shows the revenue growth for each company that's currently in the portfolio (the 50 companies in Table 4) for the quarter as well as the change in their free cash flow margins for the period. **During the first quarter of 2022, the simple-average free cash flow margin for all the fund's current holdings was 13.8%, down from 18.9% a year ago**. Jeremy and I would have preferred to see growth in the free cash flow margin, but we're not troubled by the decline for a few reasons.

First, the huge drop in Upstart's free cash flow margin (from 35.0% to -87.7%) was a significant contributor to the decline in the average free cash flow margin for the portfolio. This fall in Upstart's free cash flow margin is likely to be temporary. As a reminder, Upstart runs an AI-powered lending platform that connects borrowers with banks (see our **thesis on Upstart** for more details). The loans that are originated through the platform are either held by the bank or purchased by Upstart, which then (1) immediately resells the loans to institutional investors, (2) holds the loans for a period of time before selling them to institutional investors, or (3) retains them. During the first quarter of 2022, the company purchased US$443.2 million in loans that it intends to hold for some time. This compares with just US$18.2 million in loan purchases for the same purpose last year. Without the huge increase in the amount of loans purchased in the first quarter of 2022, Upstart's operating cash flow would have looked a lot better, as shown in Table 10. Upstart increased its loan purchases for two reasons:

- The company is in the process of launching new loan categories on its platform, including auto loans and newer segments of personal loans (reminder: Unsecured personal loans are currently the largest category of loans for Upstart). When doing so, Upstart has to prove to its bank partners that these new loan categories work. The best way to do so would be for Upstart to test these new loans itself by purchasing them. During the first quarter of 2022, around three-quarters of Upstart's loan purchases were for these research & development purposes.
- Upstart also experienced a gap in funding during the quarter. Institutional investors that were purchasing Upstart-powered loans lost some appetite to do so when interest rates in the US increased rapidly. For context, the two-year Treasury yield - the most relevant benchmark for Upstart's business - tripled from 0.73% at the end of 2021 to 2.34% at the end of March 2022. The higher interest rates caused institutional investors to demand higher yields for loans that they wanted to purchase. Upstart's platform could not adjust to this desire for higher yields at an appropriate pace (the company is improving this aspect of its platform) and had to make a choice: The company could either step in to cover the funding gap with its own capital by purchasing loans, or let these loans slip away. Upstart's management chose to cover the gap in this instance, and it accounted for the remaining 25% or so of loan purchases for the quarter (around 75% was for research & development, as mentioned earlier). To be clear, we would reconsider our investment in Upstart if the company starts large scale purchases of loans on a regular basis or has to constantly step in with its balance sheet to cover funding gaps. For now, Upstart's management has decided to stop the practice of plugging funding gaps, electing to let some loans slip away in the future. We are watching this development but we trust Upstart's management team. Moreover, the amount of loans involved in the funding gap during the first quarter of 2022 was relatively low; Upstart originated US$4.5 billion in loans during the quarter, while the funding-gap-loans were just around US$150 million.

Table 10

Quarter	Upstart operating cash flow	Upstart purchase of loans held-for-sale
Q1 2021	US$43.1 million	US$18.2 million
Q1 2022	-US$266.8 million	US$443.2 million

Source: Upstart earnings update

If Upstart's numbers were removed from the averages for Compounder Fund, the portfolio's average revenue growth for the first quarter of 2022 would still be strong at 25.3% and the free cash flow margin would be 16.2%, down slightly from 18.5% a year ago. A company that grew revenue at 25.3% but saw a fall in the free cash flow margin from 18.5% to 16.2%, would still have *increased* its free cash flow by 9.7%.

Second, although the average free cash flow margin for Compounder Fund's holdings have declined for a few quarters when compared to their respective year ago periods (the margin also fell in the second, third, and fourth quarters of 2021) and we're watching this, a few quarters of declines do not make a trend. Third, quarterly cash flows can vary considerably due to the timings of working capital changes and capital expenditures. We think the average free cash flow margin for Compounder Fund’s current crop of portfolio companies can grow to around 25% eventually and be maintained at that level.

Table 11

Company	Revenue growth in Q1 2022 from a year ago	Free cash flow margin in Q1 2022	Free cash flow margin in Q1 2021
Activision Blizzard	-22.3%	35.5%	36.1%
Adobe	14.4%	43.6%	49.3%
Adyen	-	-	-
Alphabet	23.0%	22.3%	21.1%
Alteryx	33.0%	-0.3%	17.1%
Amazon	7.3%	-15.2%	-7.3%
Apple	8.6%	26.4%	24.2%
ASML	-19.0%	-23.7%	-26.1%
Block	-21.7%	4.8%	-1.3%
Chipotle Mexican Grill	16.0%	9.2%	12.6%
Costco	16.2%	0.7%	5.1%
Coupang	21.6%	-5.7%	-7.8%
Datadog	82.8%	35.8%	22.4%
dLocal	117.2%	83.8%	4.3%
DocuSign	25.5%	29.7%	26.2%
Etsy	5.2%	8.7%	26.3%
Fiverr	26.9%	7.9%	6.0%
Haidilao	-	-	-
Illumina	11.9%	9.1%	22.0%
Intuitive Surgical	15.1%	8.6%	31.8%
Markel	27.0%	-	-
Mastercard	24.4%	28.3%	30.7%
Medistim	13.2%	17.4%	16.8%
Meituan Dianping	25.0%	-	-
MercadoLibre	63.1%	-16.5%	-28.0%
Meta Platforms	6.6%	27.9%	30.3%
Microsoft	18.4%	2.7%	23.0%
MongoDB	57.1%	3.2%	5.3%
Netflix	9.8%	10.2%	9.7%
Okta	65.3%	2.4%	21.0%
Paycom Software	29.9%	23.4%	23.6%
PayPal	7.5%	16.2%	25.5%
PushPay	17.0%	27.9%	32.7%
Salesforce	24.3%	47.2%	51.2%
Sea	64.4%	-	-
Shopify	21.7%	-5.8%	13.2%

Table 11 (continued from above)			
Company	**Revenue growth in Q1 2022 from a year ago**	**Free cash flow margin in Q1 2022**	**Free cash flow margin in Q1 2021**
Starbucks	14.5%	-3.8%	8.4%
Teladoc	24.6%	-11.1%	-6.9%
Tencent Holdings	0.1%	11.2%	24.4%
Tesla	80.5%	11.8%	2.7%
The Trade Desk	43.5%	43.2%	27.7%
Tractor Supply	8.3%	-1.8%	2.7%
TSMC	35.5%	22.4%	-5.6%
Twilio	48.4%	-4.0%	-1.9%
Upstart	155.6%	-87.7%	35.0%
Veeva Systems	16.5%	94.8%	109.7%
Visa	25.5%	44.8%	55.3%
Wise	31.6%	1.4%	27.8%
Wix	13.6%	-9.8%	4.9%
Zoom	12.3%	46.4%	47.5%
Simple average	**28.1%**	**13.8%**	**18.9%**

Source: Companies' earnings updates

(As of the publication of this letter, there's no quarterly free cash flow data available for Adyen, Haidilao, Meituan Dianping, and Sea for the first quarter of 2022. 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.

Near the beginning of this letter, I mentioned that I will have more to share on the stark differences between the business performances of Compounder Fund's holdings and their declining stock prices. Table 12 below shows a few things for the period from 31 March 2022 to 30 June 2022 for the fund's current crop of 50 companies: The change in their trailing revenues-per-share; the change in their trailing P/S, or price-to-sales, ratios; and the change in their stock prices. I'm using revenue instead of earnings or cash flow because some of Compounder Fund's holdings are still heavily reinvesting in their businesses for future growth. As a result, they currently are deliberately loss-making, have negative free cash flow, or have low profit and/or free cash flow margins.

Table 12

Company	Trailing revenue per share on 31 Mar 2022	Trailing revenue per share on 30 Jun 2022	P/S ratio on 31 Mar 2021	P/S ratio on 30 Jun 2022	Trailing revenue per share change from 31 Mar 2022 to 30 Jun 2022	P/S ratio change from 31 Mar 2021 to 30 Jun 2022	Stock price change from 31 Mar 2021 to 30 Jun 2022
Activision Blizzard	US$11.26	US$10.56	7.1	7.4	-6.2%	3.7%	-2.8%
Adobe	US$33.98	US$35.29	13.4	10.4	3.9%	-22.6%	-19.7%
Adyen	€32.65	€32.65	55.4	42.5	0.0%	-23.3%	-23.3%
Alphabet	US$380.18	US$404.96	7.3	5.4	6.5%	-26.4%	-21.6%
Alteryx	US$7.98	US$8.48	9.0	5.7	6.3%	-36.3%	-32.3%
Amazon	US$46.06	US$46.93	3.5	2.3	1.9%	-36.0%	-34.8%
Apple	US$22.9	US$23.53	7.6	5.8	2.8%	-23.8%	-21.7%
ASML	€45.35	€44.29	13.3	10.3	-2.3%	-22.9%	-28.8%
Block	US$35.20	US$30.59	3.9	2.0	-13.1%	-47.9%	-54.7%
Chipotle Mexican Grill	US$264.71	US$276.53	6.0	4.7	4.5%	-20.9%	-17.4%
Costco	US$472.66	US$488.97	1.2	1.0	3.5%	-19.5%	-16.8%
Coupang	US$10.5	US$11.00	1.7	1.2	4.8%	-31.1%	-27.9%
Datadog	US$3.33	US$3.45	45.5	27.6	3.6%	-39.4%	-37.1%
dLocal	US$0.79	US$0.93	39.6	28.2	17.7%	-28.7%	-16.0%
DocuSign	US$10.71	US$11.15	10.0	5.1	4.1%	-48.5%	-46.4%
Etsy	US$15.88	US$16.07	7.8	4.6	1.2%	-41.8%	-41.1%
Fiverr	US$8.28	US$8.58	9.2	4.0	3.6%	-56.4%	-54.8%
Haidilao	RMB7.74	RMB7.74	1.6	2.0	0.0%	25.7%	19.1%
Illumina	US$29.97	US$29.28	11.7	6.3	-2.3%	-46.0%	-47.2%
Intuitive Surgical	US$15.54	US$16.10	19.4	12.5	3.6%	-35.8%	-33.5%
Markel	US$760.38	US$813.69	1.9	1.6	7.0%	-18.1%	-12.3%
Mastercard	US$19.04	US$20.28	18.8	15.6	6.5%	-17.1%	-11.7%
Medistim	NOK23.12	NOK23.84	11.4	11.9	3.1%	4.2%	7.4%
Meituan	RMB29.67	RMB31.20	4.2	5.3	5.2%	25.2%	24.8%
Mercado Libre	US$141.95	US$157.49	8.4	4.0	10.9%	-51.7%	-46.5%
Meta Platforms	US$42.13	US$43.64	5.3	3.7	3.6%	-30.0%	-27.5%
Microsoft	US$24.45	US$25.5	12.6	10.1	4.3%	-20.1%	-16.7%
MongoDB	US$13.53	US$14.44	32.8	18.0	6.7%	-45.2%	-41.5%
Netflix	US$65.22	US$67.12	5.7	2.6	2.9%	-54.6%	-53.3%
Okta	US$8.78	US$9.39	17.2	9.6	6.9%	-44.0%	-40.1%

Table 12 (continued from above)							
Company	**Trailing revenue per share on 31 Mar 2022**	**Trailing revenue per share on 30 Jun 2022**	**P/S ratio on 31 Mar 2021**	**P/S ratio on 30 Jun 2022**	**Trailing revenue per share change from 31 Mar 2022 to 30 Jun 2022**	**P/S ratio change from 31 Mar 2021 to 30 Jun 2022**	**Stock price change from 31 Mar 2021 to 30 Jun 2022**
Paycom Software	US$18.14	US$19.53	19.1	14.3	7.7%	-24.9%	-19.1%
PayPal	US$21.39	US$22.03	5.4	3.2	3.0%	-41.4%	-39.6%
PushPay	US$0.17	US$0.18	4.7	4.2	5.9%	-10.1%	4.0%
Salesforce	US$27.2	US$27.91	7.8	5.9	2.6%	-24.3%	-22.3%
Sea	US$18.69	US$19.94	6.4	3.4	6.7%	-47.7%	-44.2%
Shopify	US$3.62	US$3.83	18.7	8.2	5.8%	-56.3%	-53.8%
Starbucks	US$25.8	US$26.89	3.5	2.8	4.2%	-19.4%	-16.0%
Teladoc	US$12.95	US$13.36	5.6	2.5	3.2%	-55.4%	-54.0%
Tencent	RMB57.71	RMB57.53	5.2	5.3	-0.3%	0.2%	-5.3%
Tesla	US$47.42	US$53.75	22.7	12.5	13.3%	-44.9%	-37.5%
The Trade Desk	US$2.4	US$2.67	28.9	15.7	11.3%	-45.6%	-39.5%
Tractor Supply	US$109.92	US$114.21	2.1	1.7	3.9%	-20.1%	-16.9%
TSMC	NT306.15	NT330.96	9.8	7.3	8.1%	-24.8%	-21.6%
Twilio	US$16.32	US$17.29	10.1	4.8	5.9%	-52.0%	-49.1%
Upstart	US$8.95	US$10.87	12.2	2.9	21.5%	-76.1%	-71.0%
Veeva Systems	US$11.41	US$11.87	18.6	16.7	4.0%	-10.4%	-6.8%
Visa	US$11.8	US$12.58	18.8	15.7	6.6%	-16.7%	-11.2%
Wise	£0.51	£0.54	9.8	5.5	5.9%	-43.7%	-39.9%
Wix	US$22.27	US$22.74	4.7	2.9	2.1%	-38.5%	-37.2%
Zoom	US$13.41	US$13.75	8.7	7.8	2.5%	-10.2%	-7.9%
Simple average	-	-	**12.3**	**8.3**	**4.5%**	-	-

Source: Companies' earnings updates

What Table 12 highlights: **Compounder Fund's businesses have performed well over the past quarter (nearly all of them saw growth in their trailing revenues per share for 30 June 2022 compared to 31 March 2022), but the stock prices of many of them have fared poorly because of large declines in their P/S ratios**.

The lower P/S ratios lead to falling stock prices, which is not a pleasant experience. **But there's also a silver lining: There is *better value* for all of us as investors**. As of 30 June 2022, the companies currently in Compounder Fund's portfolio **have an average trailing P/S ratio of 8.3, and an average trailing free cash flow margin of 16.9%, which equates to an average P/FCF ratio of 49**. If Compounder Fund's companies had an average free cash flow margin of 25% today - around the level we think they could achieve, eventually -

the implied P/FCF ratio would be even lower at 33. For perspective, the implied P/FCF ratio of 33 comes from a group of companies - Compounder Fund's current portfolio - that produced impressive revenue growth rates of 45.2% and 28.1%, on average, for the whole of 2021 and the first quarter of 2022, respectively.

Investing thoughts: Facing uncertainty

The [redacted] ETF, an exchange-traded fund that tracks the [redacted]. The S&P 500 index has also fallen 19% from its high over the past year. It's fair to say that stocks around the world have been beaten down lately. Unfortunately, there's much that could continue to derail financial markets. An incomplete list includes high inflation in the USA and Europe, rising interest rates in the USA and the risk of a recession happening there, supply chain problems all across the world, the ongoing war between Russia and Ukraine, and China's dynamic zero-COVID policy. To make matters worse, Stanley Druckenmiller, a legend in the investing business, shared in an **interview** last month that he's unaware of any precedent in history for the economic conditions he's currently seeing in the USA, where the economy is weakening while inflation is high and bond yields are low. For anyone investing in stocks, the current environment seems incredibly uncertain compared to the recent past.

What should a stock market investor do? I can't speak for others, but what Jeremy and I are doing at Compounder Fund is to continue to stick to our investment philosophy. This is because the philosophy is built on something that is likely to remain stable over time, and there's tremendous value in doing so. I explained in the "*Investing thoughts: Why we focus on business quality"* section of Compounder Fund's **2021 second-quarter letter**:

> "...[if] we were to boil [our investment philosophy] down to one sentence, it would be this: "A stock's price will do well over time if its underlying business does well too."...
>
> …why the statement is a cornerstone of our investment philosophy. I'll start the discussion with something Jeff Bezos once said (emphasis is mine):
>
>> "I very frequently get the question: "What's going to change in the next 10 years?" And that is a very interesting question; it's a very common one. *I almost never get the question: "What's not going to change in the next 10 years?" And I submit to you that that second question is actually the more important of the two -- because you can build a business strategy around the things that are stable in time*. ... [I]n our retail business, we know that customers want low prices, and I know that's going to be true 10 years from now. They want fast delivery; they want vast selection."
>
> Similarly, we believe that we can build a **lasting *investment* strategy around the things that are stable in time. And we want to do that for Compounder Fund.** There are many important things about the stock market that can change (such as the behaviour of market participants and their level of collective knowledge). But one thing about the stock market which we have observed to be stable over the long arc of history is that it has remained a place to buy and sell pieces of a business. And we think this trait about the stock market will very likely continue to be stable over time. With this observation, what logically follows is that a stock's price over the long run will continue to depend on the performance of its underlying business over the same period. In turn, a stock's price will eventually do well if its underlying business does well too.

I have another thought about uncertainty and investing that I want to discuss. I'll begin with the **State of the Union Address**, a speech that the President of the USA delivers near the start of every year. It's a report on how the country fared in the year that passed and what lies ahead. It's also a barometer for the US population's sentiment on the country's social, political, and economic future. This is part of the speech for one particular year:

> "We are fortunate to be alive at this moment in history. Never before has our nation enjoyed, at once, so much prosperity and social progress with so little internal crisis and so few external threats. Never before have we had such a blessed opportunity -- and, therefore, such a profound obligation -- to build the more perfect union of our founders' dreams.
>
> We begin the [year] with over 20 million new jobs; the fastest economic growth in more than 30 years; the lowest unemployment rates in 30 years; the lowest poverty rates in 20 years; the lowest African-American and Hispanic unemployment rates on record; the first back-to-back budget surpluses in 42 years. And next month, America will achieve the longest period of economic growth in our entire history.
>
> My fellow Americans, the state of our union is the strongest it has ever been."

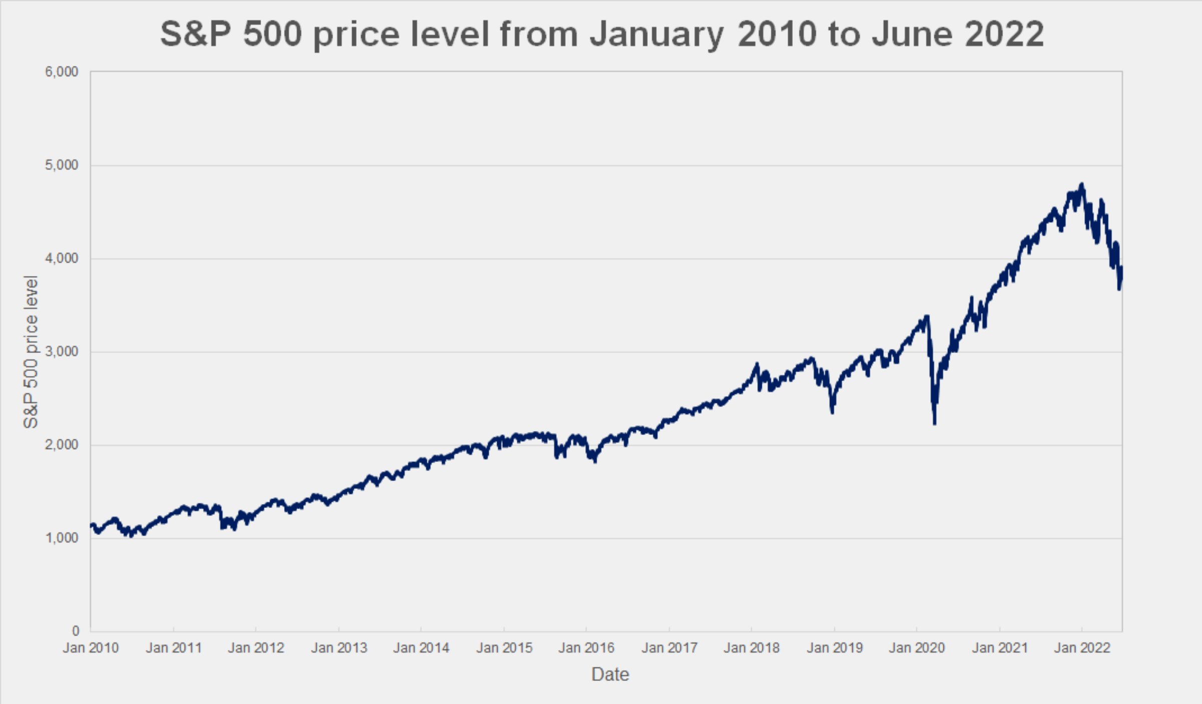
In short, things looked great for the USA. There was nothing much to worry about for the country. In another particular year, the then-president commented:

> "One in 10 Americans still cannot find work. Many businesses have shuttered. Home values have declined. Small towns and rural communities have been hit especially hard. And for those who'd already known poverty, life has become that much harder. This recession has also compounded the burdens that America's families have been dealing with for decades -- the burden of working harder and longer for less; of being unable to save enough to retire or help kids with college."

This time, the picture looked bleak and major problems were festering in America.

The first speech was **delivered** in January 2000 by Bill Clinton. What happened next: The USA entered a recession in March 2001; terrorists struck the World Trade Center six months after the recession, the first time the country was attacked since Pearl Harbour in 1941; and the dotcom bubble burst, with the S&P 500 peaking around the middle of 2000 and falling by nearly half at the bottom near the end of 2002. Meanwhile, the second speech was **from** Barack Obama and took place in January 2010, when the US was starting to recover from the Great Financial Crisis. What came after: The next recession took more than 10 years to arrive (in February 2020, after COVID-19 emerged) and the S&P 500 has moved in pretty much one direction since the speech (up and to the right), as shown in Figure 1.

Figure 1



Source: Yahoo Finance

The two State of the Union addresses and their subsequent events illustrate that **it is only people's *perception* of uncertainty that changes**. When times are good, uncertainty seems to disappear and when times are bad, uncertainty looms large. **But the reality is the level of uncertainty did not change - it was always present**.

Earlier in this section, I wrote that "For anyone investing in stocks, the current environment seems incredibly uncertain compared to the recent past." **This is *not* true**. **The world we live in today is no less uncertain compared to yesterday, or a month ago, or a year ago. It's only our perception that has changed**. There are always risks that could endanger stocks and the global economy. At times the world collectively pays more attention to these risks. At other times, no one's looking. **But Jeremy and I are *always* looking**. So, we will remain steadfast in staying invested with businesses that we think will do well over time. This is the best way we know - it's not the only way, but it's the best *we* know - to deal with the ever-present uncertainty that is inherent in the world.

Investing thoughts: What really matters

"Ouch. It's been a brutal year for many in the capital markets… As of this writing, our shares are down more than 80% from when I wrote you last year." These words are penned by the founder of one of Compounder Fund's companies. In an interview, the founder also said (emphasis is mine):

> "The stock is not the company and the company is not the stock. So as I watched the stock fall… I was also watching all of our internal business metrics: number of customers, profit per unit, defects, everything you can imagine. *Every single thing about the business was getting better, and fast. So as the stock price was going the wrong way, everything inside the company was going the right way*."

The founder in question is Jeff Bezos and the company is, of course, Amazon. Although his written words would fit nicely with many of Compounder Fund's holdings today, they are actually excerpts from his **2000 letter** to Amazon shareholders, which was written in the throes of the infamous dotcom bubble more than 20 years ago. The interview I mentioned **happened in 2018**, when Bezos recounted the searing experience. After sharing that Amazon's stock price was down by more than 80% over the past year, Bezos continued in the 2000 letter:

> "Nevertheless, by almost any measure, Amazon.com the company is in a stronger position now than at any time in its past:
>
> - We served 20 million customers in 2000, up from 14 million in 1999.
> - Sales grew to [US]$2.76 billion in 2000 from [US]$1.64 billion in 1999.
> - Pro forma operating loss shrank to 6% of sales in Q4 2000, from 26% of sales in Q4 1999.
> - Pro forma operating loss in the U.S. shrank to 2% of sales in Q4 2000, from 24% of sales in Q4 1999.
> - Average spend per customer in 2000 was $134, up 19%.
> - Gross profit grew to [US]$656 million in 2000, from [US]$291 million in 1999, up 125%.
> - Almost 36% of Q4 2000 U.S. customers purchased from one of our "non-BMV" stores such as electronics, tools, and kitchen.
> - International sales grew to [US]$381 million in 2000, from [US]$168 million in 1999.
> - We helped our partner Toysrus.com sell more than [US]$125 million of toys and video games in Q4 2000.
> - We ended 2000 with cash and marketable securities of [US]$1.1 billion, up from [US]$706 million at the end of 1999, thanks to our early 2000 euroconvert financing.
> - And, most importantly, our heads-down focus on the customer was reflected in a score of 84 on the American Customer Satisfaction Index. We are told this is the highest score ever recorded for a service company in any industry."

Something similar is happening with Compounder Fund's portfolio. At a high level, the companies within have put up quarter after quarter of strong revenue growth while producing healthy free cash flow margins. **The internal business metrics, taken in aggregate, are moving in the right direction. The stock prices however, are not**. In his 2000 letter, Bezos also shared his thoughts on the divergence between his company's business performance and stock price:

> "So, if the company is better positioned today than it was a year ago, why is the stock price so much lower than it was a year ago? As the famed investor Benjamin Graham said, "In the short term, the stock market is a voting machine; in the long term, it's a weighing machine." Clearly there was a lot of voting going on in the boom year of '99—and much less weighing. We're a company that wants to be weighed, and over time, we will be—over the long term, all companies are. In the meantime, we have our heads down working to build a heavier and heavier company."

Over the past year, Amazon has been down-voted significantly with its stock price falling by 31%. But over the long run, the weighing mechanism has worked beautifully. As Amazon's revenue surged from US$2.8 billion in 2000 to US$477.7 billion over the last 12 months, its stock price has also climbed from US$5.33 at the peak of the dotcom bubble (and from US$0.30 at the trough) to US$115 as of 10 July 2022.

If Compounder Fund's portfolio companies can continue to grow their businesses well (there's no guarantee, but we think they will), their stock prices, in the fullness of time, will likely make the levels of today look like bargains. Eventually, if they become heavier businesses, their weights should matter.

Investing thoughts: Developing fortitude

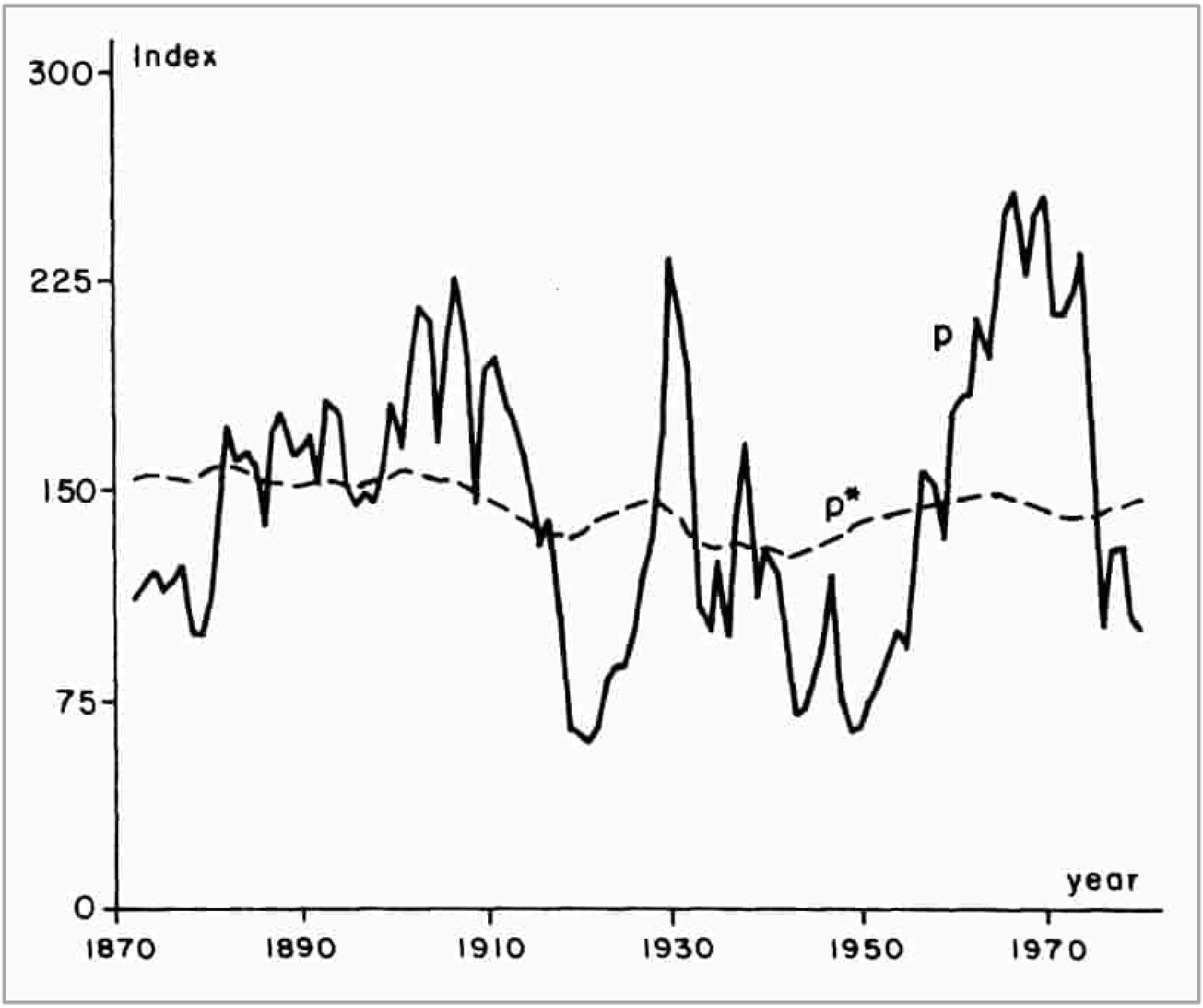
I think one of the toughest challenges that stock market investors face is finding the fortitude to hold onto stocks when prices are down. Not every stock is worth holding onto. In fact, many of them are *not* worth our patience. A 2014 **study** from JP Morgan showed that 40% of all stocks that were part of the Russell 3000 index in the US since 1980 have suffered a permanent decline of 70% or more from their peak value. But it's also true that throughout history, many stocks that have generated tremendous long-term returns have gone through bouts of significant declines in prices. I showed this in a number of previous Compounder Fund quarterly letters:

- The "*Investing thoughts: The need for patience"* section of the **2021 third-quarter letter**;
- and the "*Investing thoughts: Equanimity and patience"* section of the **2021 fourth-quarter letter**

Given the recent fall in stock prices around the world - and especially for Compounder Fund's holdings - I thought it would be apt for me to share, in this letter, more information about how stock prices can diverge wildly from underlying business fundamentals.

Figure 2 below is from **research** that Nobel-Prize-winning economist Robert Shiller published in the 1980s. In his paper, *"Do Stock Prices Move Too Much to be Justified by Subsequent Changes in Dividends?"*, Shiller wanted to determine if stock prices were too volatile when compared to the actual change in underlying business fundamentals. What he did was to study the US stock market (he looked at two indexes, the S&P 500 and the Dow Jones Industrial Average) from 1871 to 1979 and compare the market's actual performance with how it should have rationally performed if investors had perfect knowledge on the future changes in its dividends. The result for the S&P 500 is Figure 2 (it's a similar picture for the Dow Jones Industrial Average):

Figure 2



Source: Robert Shiller paper, "Do Stock Prices Move Too Much to be Justified by Subsequent Changes in Dividends?"

The solid line is the S&P 500's actual performance while the dashed line is the rational performance. **Although there were violent fluctuations in US stock prices, the fundamentals of American businesses – using dividends as a proxy – were much less volatile**. To borrow Ben Graham's famous analogy that Jeff Bezos referred to in his 2000 Amazon shareholder letter, plenty of shorter-term voting had taken place in the US stock market over the course of history. But importantly, the weighing scale did function beautifully. From 1871 to 1979, **historical data** on US stocks maintained by Shiller show that the S&P 500's dividend and price had increased by 2,073% and 2,328%, respectively. Jeremy and I have known about Shiller's research for a number of years and it has served us well in helping us produce good investing behaviour. We hope it's helpful for you too.

Investing thoughts: How we'll win, *together*

Near the beginning of this letter and many other previous Compounder Fund quarterly letters, I've emphasised the critical role that all of you play in helping Jeremy and me produce the behavioural edge for Compounder Fund. A conversation I had recently with a trusted source showed just how important this partnership can be in shaping Compounder Fund's long-term return.

During the conversation, I learnt that fund managers with institutional investors (pension funds, family offices, university endowments etc.) as clients sometimes face the agent problem. These clients theoretically have really long time horizons for their investments. But a fund manager has to face agents, who are individuals tasked with managing the capital of the clients. Some of these agents have to deal with career risk and incentives, and thus end up having short investing time horizons. What happens is that a fund manager is sometimes unable to be patient with his or her investments, and thus can't produce the intended behavioural edge for the end clients.

Jeremy and I count our blessings every day that we have assembled a group of thoughtful investors at Compounder Fund - that's all of you! - who understand our investment approach and are investing with the appropriate time horizons. **Together, we'll strive to win, with the behavioural edge as the winds on our backs**.

House-keeping matters and what's next

In Compounder Fund's 2022 first-quarter letter, I mentioned that the fund's "audit process [for 2021] has dragged on for a few weeks longer than we expected, but it should be completed in the coming weeks. When the audit is done and the report's finalised, Jeremy and I will be sending a digital copy of the report to all of Compounder Fund's investors." On 11 May 2022, we sent a digital copy of Compounder Fund's audited financial statements for 2021 to all of the fund's investors. If you did not receive it, or if you joined the fund as an investor after 11 May 2022 and would like a digital copy of the audited financial statements for 2021, 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." The first audit for our giving covered the period from November 2019 (when we started building the fund) to December 2021; subsequent audits will be conducted on an annual basis. The first audit report is available on the fund's website **here**. 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. I already mentioned that we have released the investment theses for all of Compounder Fund's 50 current holdings as well as our "Sell" theses for a2 Milk and JD.com (for your convenience, all our theses can be **found here**). We will inform you when we publish any new theses.

Compounder Fund's next subscription window will close in the middle of September 2022 and it will have a dealing date on the first business day of October 2022 (which should be 3rd October). If you would like to increase your investment in the fund, please submit the relevant paperwork by the middle of July 2022. Jeremy and I are happy to assist 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 (I covered some of them in the "*Investing thoughts: Facing uncertainty*" section of this letter). 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 8.0 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. We will remain long-term optimistic on stocks so long as we continue to have this faith. I recently learnt of the history of two Japanese companies that I think are wonderful examples of the value that human ingenuity and determination can create even in the face of extreme adversity.

The first is Sony Corporation. The *Acquired* podcast, of which Jeremy and I are huge fans, had two recent episodes on the company (**here** and **here**). In them, *Acquired*'s hosts - Benjamin Gilbert and David Rosenthal - shared how Sony was founded in 1946 in Japan as a consumer electronics firm. Note the year and country. When Sony was founded by Akio Morita and Masaru Ibuka, Japan had just lost World War II. Half of the population in Tokyo, the capital, were homeless because many houses were destroyed during the war. Japan's GDP (gross domestic product) per capita was just *US$17* in Sony's founding year. **I think it would be really difficult to imagine tougher conditions in which to build a company.** But Ibuka and Morita managed to grow Sony over the decades before they passed on in the late 1990s and the company has a market capitalisation of US$100 billion today. Along the way, Morita even became an inspiration to Apple's legendary co-founder, the late Steve Jobs, for his innovative spirit.

The second is the retailer Aeon. The *Wall Street Journal* recently published a stirring **obituary** of Chizuko Kojima, which recounted how she inherited Aeon in 1939 at the age of 23. At the time, Aeon's business consisted of a single clothing store in Japan's Mie prefecture. Again, note the year and country. Through Kojima's leadership, Aeon survived World War II and Japan's traumatic post-war years, and then went on to prosper over the next few decades. When Kojima passed away in May this year, Aeon's annual revenue was US$64 billion and it had thousands of stores in Japan and other parts of Asia, according to the *Wall Street Journal*. The obituary contained incredible stories of Kojima's leadership and my favourite was this:

> "After taking over the family business, Chizuko managed to keep it going during World War II until a U.S. bombing raid destroyed much of their home city of Yokkaichi in June 1945, including the Okada store's stock.
>
> At the time, customers held coupons similar to gift certificates entitling them to store goods. The store no longer had anything to offer, but Chizuko posted notices throughout the city saying her shop would give cash in exchange for the coupons, recalled her younger brother, Takuya, in a 2005 autobiography. It was a way of maintaining customers' loyalty that would pay ample dividends in years to come."

The only time Jeremy and I will turn pessimistic on the long-term returns of stocks is when they 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 approach that Jeremy and I are taking.

Your deep understanding of our long-term-oriented investment style 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 again for being the wonderful investors that you all are. And please, *never* underestimate your importance in helping to shape Compounder Fund's long-run return.**

You can expect to see Compounder Fund's 2022 third-quarter investors' letter in mid-October this year. Till then, stay safe and take care!

Excelsior,
Chong Ser Jing
Co-founder and Portfolio Manager, Compounder Fund
12 July 2022

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

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