Compounder Fund Investors' Letter: Fourth Quarter of 2024

COMPOUNDER FUND
GROWING YOUR WEALTH AND ENRICHING SOCIETY

Dear investors,

I'm presenting Compounder Fund's 2024 fourth-quarter investors' letter together with my co-founder Jeremy Chia. 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 11.2%. Over the same period, the dividend-adjusted Singapore-dollar returns for the S&P 500 was 9.1%. Tables 1 and 2 below show the returns for Compounder Fund's two share classes (the earliest series for each share class) and the S&P 500 since the birth of the fund.

Table 1

Time period	Compounder Fund Class A (after fees)	S&P 500**
2020*	11.2%	14.2%
2021	0.9%	31.2%
2022	-44.1%	-18.7%
2023	36.7%	24.4%
Q1 2024	12.7%	13.1%
Q2 2024	2.7%	4.7%
Q3 2024	0.7%	0.2%
Oct 2024	2.3%	2.1%
Nov 2024	8.9%	7.3%
Dec 2024	-0.1%	-0.4%
Q4 2024	11.2%	9.1%
Year-to-date 2024	29.7%	29.5%
Total return since inception*	11.2%	96.5%
Annualised return since inception*	2.4%	16.3%

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

Table 2

Time period	Compounder Fund Class B (after fees)	S&P 500**
2020*	6.8%	8.6%
2021	0.9%	31.2%
2022	-44.1%	-18.7%
2023	36.7%	24.4%
Q1 2024	12.7%	13.1%
Q2 2024	2.7%	4.7%
Q3 2024	0.7%	0.2%
Oct 2024	2.3%	2.1%
Nov 2024	8.9%	7.3%
Dec 2024	-0.1%	-0.4%
Q4 2024	11.2%	9.1%
Year-to-date 2024	29.7%	29.5%
Total return since inception*	6.8%	86.8%
Annualised return since inception*	1.6%	15.8%

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

Compounder Fund's investment mandate is global in nature. This means the fund can invest in any listed stock in the world. But we believe the S&P 500, a prominent US stock market index, 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 including a global index if there are significant changes to Compounder Fund's portfolio from a geographic perspective, or if US stocks start lagging their global peers.

At the publication of this letter, it's been more than four years since we started investing Compounder Fund's capital on 13 July 2020. **The results have been poor**. The fund's earliest series for its Class A and Class B shares have had positive gains since their inception, but they have substantially underperformed the US stock market. **We are encouraged by the gains in the stock prices of the fund's holdings in 2023 and 2024, with strong outperformance over the market in 2023 and a slight outperformance in 2024** (see Tables 1 and 2). But a huge gap still exists between the good performance of Compounder Fund's underlying businesses and the mediocre gains in their stock prices.

Jeremy and I are clear that Compounder Fund exists to ultimately produce a positive *and* healthy return over the long run for all of you, and not merely to invest in stocks with growing businesses. **We understand too that discussion about the fund's underlying businesses can ring empty when their stock prices have fared poorly**, ***especially*** **when**

most of the holdings had high valuations when we first invested in them (the valuation numbers can be found in our investment theses for the holdings). But I have repeatedly emphasised in our past letters how our stocks' underlying *businesses* have been doing because what ultimately drives a stock's price over the long run is its business performance. Over the short run, stock prices and business fundamentals can diverge wildly. But they tend to converge with the passing of time, as I will detail in the "*Wonderful businesses"* section of this letter with the help of examples I've shared in some of our past letters.

Jeremy and I believe that investing for Compounder Fund in the manner we have been from the start - finding companies with the potential for strong long-term growth in their businesses and holding their shares - is the best way forward. This is because we think it will produce the best long-term results. The performance of Compounder Fund has been poor so far, and we understand why you may question this approach. But based on our experience investing in the past over longer time frames, we believe this is a way of investing that will very likely work if given the time to succeed; I will explain our belief in greater detail in the "*Wonderful businesses"* section of this letter. Although the manner of our investing has not changed, **we have been - and will continue - attempting to improve the performance of the fund, a process I discussed in the "*Improving our performance"* section of our 2024 second-quarter letter.**

Times like these are not easy for any of you. We know. The late, great, Charlie Munger was once asked about the lessons he learnt from his investment fund's big losses in 1973 and 1974 (his total loss in that period was 53%). He said:

> "It didn't bother me with my own money, but it made me suffer the tortures of hell as I thought through the loss of morale of the limited partners who had trusted me."

It's the same anguish we feel when we think of you. But at the same time, you have provided us with gentle patience and the space to engage in long-term thinking about stocks - **we're incredibly grateful for this**. With your strong support, Jeremy and I 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. You should never underestimate the importance of your role in shaping Compounder Fund's long-term return. In the "*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**. In what has been a rough period for Compounder Fund over the past four-plus years, you have helped us produce this edge. ***Thank you****.*

Judging our performance

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."

We're now over the four-year mark at Compounder Fund and as I mentioned in the introductory section of this letter, the performance of the fund has been poor. The journey so far has been rough on all of us at Compounder Fund, to say the least. **If you find the performance of the fund wanting by using the minimum three-year evaluation period, we understand.** But based on the business performances of Compounder Fund's holdings, we're confident that when the fund's *stock price* performance is eventually weighed in the fullness of time, a favourable judgement is likely to result - **I discuss the reason for our confidence in the *"Wonderful businesses"* section of this letter.**

It will be very disappointing for the both of us too if Compounder Fund fails to beat 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 long-term 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 think about two sequences of returns over a seven year period, shown in Table 3:

Table 3

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Total	CAGR*
Sequence A return	+11%	+0%	-44%	+36%	+50%	+10%	+57%	+120%	**12%**
Sequence B return	+12%	+12%	-5%	+20%	+9%	+25%	+13%	+120%	**12%**

**CAGR refers to the compound annual growth rate for Year 1 to Year 7*

Both sequences result in the same total return. But the **psychological** experience with Sequence A is vastly more difficult than with Sequence B because of Sequence A's much

greater volatility. **It would also be really difficult for an investor in Sequence A to hold on from Year 1 to Year 4 because the overall return at the Year 4 mark would be -15%;** this compares with the overall return of 43% for Sequence B. The difference between Sequence A and Sequence B's psychological experience from Year 1 to Year 7, and the identical overall result, 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

On 19 December 2024, 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 that we had completely sold the fund's Cassava Sciences' position (our Sell thesis can be **found here**) and that no other material changes were made to the portfolio. Since then, there have been no significant shifts either. Here's how Compounder Fund's portfolio of 45 companies looks like as of 12 January 2025:

Table 4

Company	Weighting	Country/Region of listing	Headquarters
Meta Platforms	9.8%	USA	USA
Netflix	5.7%	USA	USA
Amazon	5.6%	USA	USA
MercadoLibre	5.6%	USA	Argentina
Alphabet	4.4%	USA	USA
The Trade Desk	4.0%	USA	USA
Microsoft	3.9%	USA	USA
Apple	3.3%	USA	USA
Tractor Supply	3.3%	USA	USA
Shopify	3.1%	USA	Canada
Chipotle Mexican Grill	3.0%	USA	USA
Costco	3.0%	USA	USA
Intuitive Surgical	2.9%	USA	USA

Table 4 (continued from above)			
Company	**Weighting**	**Country/Region of listing**	**Headquarters**
Visa	2.9%	USA	USA
Tesla	2.8%	USA	USA
Mastercard	2.7%	USA	USA
Datadog	2.6%	USA	USA
TSMC	2.1%	USA	Taiwan
Adyen	2.1%	Netherlands	Netherlands
Tencent	2.1%	Hong Kong	China
ASML	2.0%	USA	Netherlands
Salesforce	1.9%	USA	USA
Markel	1.8%	USA	USA
Medpace	1.7%	USA	USA
Adobe	1.6%	USA	USA
Nu Holdings	1.5%	USA	Brazil
Wix	1.4%	USA	Israel
PayPal	1.4%	USA	USA
Veeva Systems	1.3%	USA	USA
Wise	1.2%	UK	UK
Block*	0.9%	USA	USA
MongoDB	0.9%	USA	USA
Meituan	0.9%	Hong Kong	China
Hingham	0.9%	USA	USA
Starbucks	0.7%	USA	USA
Okta	0.6%	USA	USA
Medistim	0.6%	Norway	Norway
Haidilao	0.6%	Hong Kong	China
Paycom Software	0.6%	USA	USA
Sea	0.6%	USA	Singapore
Coupang	0.5%	USA	South Korea
Zoom	0.5%	USA	USA
dLocal	0.5%	USA	Uruguay
Fiverr	0.2%	USA	Israel
Super Hi International	0.1%	Hong Kong	Singapore
Cash	**0.3%**	**-**	**-**

**0.2% 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*

Table 5 below shows the high-level geographical breakdown of Compounder Fund’s portfolio as of 12 January 2025:

Table 5

Country/Region	% of Compounder Fund's capital based on country of listing	% of Compounder Fund's capital based on location of headquarters
Argentina	-	5.6%
Brazil	-	1.5%
Canada	-	3.1%
China	-	3.6%
Hong Kong	3.7%	-
Israel	-	1.6%
Netherlands	2.1%	4.1%
Norway	0.6%	0.6%
Singapore	-	0.6%
South Korea	-	0.5%
Taiwan	-	2.1%
UK	1.2%	1.2%
Uruguay	-	0.5%
USA	92.0%	74.5%

Wonderful businesses

Jeremy and I are pleased to report that the companies in Compounder Fund's portfolio have in aggregate continued to deliver healthy revenue growth in the third quarter of 2024. Table 6 below shows the year-on-year revenue growth rates for all the 45 companies currently in Compounder Fund's portfolio for the following time periods: The whole of 2020, 2021, 2022, and 2023, and the first three quarters of 2024.

Table 6

Company	2020 revenue growth	2021 revenue growth	2022 revenue growth	2023 revenue growth	Q1 2024 revenue growth	Q2 2024 revenue growth	Q3 2024 revenue growth
Adobe	17.3%	18.0%	11.5%	10.8%	10.2%	10.6%	11.1%
Adyen	28.1%	46.4%	32.8%	22.2%	21.0%	26.1%	20.0%
Alphabet	12.8%	41.2%	9.8%	8.7%	15.4%	13.6%	15.1%
Amazon	37.6%	21.7%	9.4%	11.8%	12.5%	10.1%	11.0%
Apple	9.9%	28.6%	2.4%	-0.5%	-4.3%	4.9%	6.1%
ASML	18.3%	33.1%	13.8%	30.2%	-21.6%	-9.6%	11.9%
Block	101.5%	86.0%	-0.7%	25.0%	19.4%	11.2%	6.4%
Chipotle Mexican Grill	7.1%	26.1%	14.4%	14.3%	14.1%	18.2%	13.0%
Costco	12.8%	17.7%	11.5%	6.2%	9.1%	1.0%	7.5%

Table 6 (continued from above)

Company	2020 revenue growth	2021 revenue growth	2022 revenue growth	2023 revenue growth	Q1 2024 revenue growth	Q2 2024 revenue growth	Q3 2024 revenue growth
Datadog	66.3%	70.5%	62.8%	29.4%	26.9%	26.7%	26.0%
dLocal	88.4%	134.4%	71.6%	55.2%	34.3%	6.3%	13.3%
Fiverr	77.0%	57.1%	13.3%	7.1%	6.3%	5.9%	7.7%
Haidilao	7.8%	43.7%	-20.6%	33.6%	-	13.80%	-
Hingham	27.4%	20.3%	3.6%	-54.5%	-39.1%	-20.4%	4.5%
Intuitive Surgical	-2.7%	31.0%	9.0%	14.5%	11.5%	14.5%	16.9%
Markel	17.0%	20.0%	22.1%	5.6%	7.5%	3.5%	0.3%
Mastercard	-9.4%	23.4%	17.8%	12.9%	10.4%	11.0%	12.8%
Medistim	-0.2%	17.7%	15.1%	7.0%	3.5%	5.5%	7.0%
Medpace	7.5%	23.4%	27.8%	29.2%	17.7%	14.6%	8.3%
Meituan	17.7%	56.0%	22.8%	25.8%	25.0%	21.0%	22.4%
Mercado-Libre	73.0%	77.9%	49.1%	37.4%	36.0%	41.5%	35.3%
Meta Platforms	21.6%	37.2%	-1.1%	15.7%	27.3%	22.1%	18.9%
Microsoft	14.7%	20.6%	10.4%	11.5%	17.0%	15.2%	16.0%
MongoDB	40.0%	48.0%	47.0%	31.1%	22.3%	12.8%	22.3%
Netflix	24.0%	18.8%	6.5%	6.7%	14.8%	16.8%	15.0%
Nu Holdings	20.4%	130.4%	182.2%	67.5%	69.0%	52.4%	37.7%
Okta	42.5%	55.6%	42.9%	21.8%	19.1%	16.2%	13.9%
Paycom Software	14.1%	25.4%	30.3%	23.2%	10.7%	9.1%	11.2%
PayPal	20.7%	18.3%	8.5%	8.2%	9.4%	8.2%	5.8%
Salesforce	24.3%	24.7%	18.3%	11.2%	10.7%	8.4%	8.3%
Sea	101.1%	127.5%	25.1%	4.9%	22.8%	23.0%	30.8%
Shopify	85.6%	57.4%	21.4%	26.1%	23.4%	20.7%	26.1%
Starbucks	-14.1%	31.0%	8.4%	11.5%	-1.8%	-0.6%	-3.2%
Super Hi	-5.0%	41.1%	78.7%	23.0%	16.6%	12.4%	14.6%
Tencent	27.8%	16.2%	-1.0%	9.8%	6.3%	8.0%	8.1%
Tesla	28.3%	70.7%	51.4%	18.8%	-8.7%	2.3%	7.8%
The Trade Desk	26.5%	43.1%	31.9%	23.3%	28.3%	25.9%	27.3%
Tractor Supply	27.2%	19.9%	11.6%	2.5%	2.9%	1.5%	1.6%
TSMC	25.2%	18.5%	42.6%	-4.5%	16.5%	40.1%	39.0%
Veeva Systems	32.7%	26.3%	16.4%	9.7%	23.6%	14.6%	13.4%
Visa	-8.7%	18.6%	18.5%	10.5%	9.9%	9.6%	11.7%
Wise	43.9%	32.3%	48.5%	28.6%	24.0%	21.6%	16.2%

Table 6 (continued from above)

Company	2020 revenue growth	2021 revenue growth	2022 revenue growth	2023 revenue growth	Q1 2024 revenue growth	Q2 2024 revenue growth	Q3 2024 revenue growth
Wix.com	29.9%	29.0%	9.3%	12.5%	12.2%	11.7%	12.9%
Zoom	325.8%	54.6%	7.1%	3.1%	3.2%	2.1%	3.6%

Source: Companies' earnings updates

Here's a table showing the simple averages of the year-on-year revenue growth rates for the fund's current holdings for each quarter going back to the first quarter of 2020 (**note the high revenue growth rates for every quarter**):

Table 7

Simple averages for revenue growth from year ago	Compounder Fund current portfolio
Q1 2020	31.2%
Q2 2020	32.2%
Q3 2020	42.1%
Q4 2020	44.5%
2020	36.8%
Q1 2021	54.6%
Q2 2021	54.7%
Q3 2021	39.5%
Q4 2021	35.7%
2021	42.5%
Q1 2022	32.2%
Q2 2022	27.6%
Q3 2022	24.5%
Q4 2022	19.9%
2022	25.0%
Q1 2023	18.1%
Q2 2023	17.0%
Q3 2023	15.3%
Q4 2023	15.2%
2023	16.2%
Q1 2024	14.1%
Q2 2024	13.5%
Q3 2024	**14.6%**

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 healthy year-on-year revenue growth of 14.6% (this is a simple average) in the third quarter of 2024**, **and this continues from the impressive revenue growth rates seen in prior quarters going back to 2020**. Table 8 below provides perspective on the superior growth rates for Compounder Fund's current holdings compared to the S&P 500.

Table 8

Simple averages for revenue growth from year ago in a certain quarter	S&P 500	Compounder Fund current portfolio
Q1 2020	Around -2%	31.2%
Q2 2020	Around -10%	32.2%
Q3 2020	Around -2%	42.1%
Q4 2020	Around -0.5%	44.5%
Q1 2021	Around 10%	54.6%
Q2 2021	Around 25%	54.7%
Q3 2021	16.6%	39.5%
Q4 2021	16.1%	35.7%
Q1 2022	13.4%	32.2%
Q2 2022	11.9%	27.6%
Q3 2022	12.1%	24.5%
Q4 2022	6.9%	19.9%
Q1 2023	7.9%	18.1%
Q2 2023	6.1%	17.0%
Q3 2023	4.7%	15.3%
Q4 2023	6.6%	15.2%
Q1 2024	4.9%	14.1%
Q2 2024	6.2%	13.5%
Q3 2024	**7.8%**	**14.6%**

Source: Yardeni Research for S&P 500; revenue growth rate for Compounder Fund is a simple average of the revenue growth from the fund's holdings

The average year-on-year revenue growth rate for Compounder Fund's portfolio companies in the third quarter of 2024 also comfortably exceeds the S&P 500's corresponding revenue growth rate (14.6% vs 7.8%). We do acknowledge that the portfolio's 14.6% growth rate is a significant deceleration from what was achieved throughout 2021 and 2022, **but it breaks the trend of the number drifting lower that was seen in the past**. The other good thing is that 28 companies in Compounder Fund's current portfolio saw higher year-on-year revenue growth in the third quarter of 2024 compared to the second quarter of 2024. More importantly, we invested in the companies that are currently in Compounder Fund's portfolio because their businesses are riding on - or creating - durable and lasting long-term trends. This means they likely still have massive market opportunities to grow into over the long run (you can read about this in detail in our investment theses for each company; note the fact that their businesses were growing healthily even before COVID).

Consistent with what I've been sharing in our past quarterly letters, Jeremy and I continue to think there's a high chance that the fund's portfolio companies will, in aggregate, produce pleasing year-on-year revenue growth in the years ahead. **And if these companies can sustain healthy average annual revenue growth 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.

Speaking of free cash flow, Compounder Fund's holdings managed to strengthen their free cash flow margins in the third quarter of 2024. Table 9 below shows two things for each company that's currently in the portfolio: (1) Their revenue growth for the quarter, and (2) the change in their free cash flow margins for the period. **During the third quarter of 2024, the simple-average free cash flow margin for all the fund's current holdings was 22.7%, up from 21.2% a year ago. This means that Compounder Fund's portfolio had, on average, grown its free cash flow by a pleasing 23% during the quarter compared to a year ago.** As a reminder, the average free cash flow margin of Compounder Fund's holdings *fell* on a year-on-year basis in the second quarter of 2024; it's good to see a return in margin-growth. We look forward to seeing more increases over time in the free cash flow margins of Compounder Fund's companies. Given the nature and track records of these companies, we think that their long-term average free cash flow margin can **reach the high-20s percentage range eventually** and be maintained at that level.

Table 9

Company	Revenue growth in Q3 2024 from a year ago	Free cash flow margin in Q3 2024	Free cash flow margin in Q3 2023
Adobe	11.1%	51.2%	30.3%
Adyen	20.0%	-	-
Alphabet	15.1%	16.9%	29.3%
Amazon	11.0%	2.1%	6.1%
Apple	6.1%	25.2%	21.7%
ASML	11.9%	7.2%	9.3%
Block	6.4%	10.5%	8.1%
Chipotle Mexican Grill	13.0%	10.7%	14.1%
Costco	7.5%	3.2%	6.2%
Coupang	27.2%	-0.6%	8.6%
Datadog	26.0%	29.5%	25.2%
dLocal	13.3%	18.4%	2.0%
Fiverr	7.7%	10.6%	25.0%
Haidilao	-	-	-
Hingham	4.5%	-	-
Intuitive Surgical	16.9%	22.5%	16.8%
Markel	0.3%	-	-
Mastercard	12.8%	65.9%	45.8%
Medistim	7.0%	16.8%	30.1%
Medpace	8.3%	26.0%	21.5%
Meituan	22.4%	-	-
MercadoLibre	35.3%	25.9%	20.8%
Table 9 (continued from above)			

Company	Revenue growth in Q3 2024 from a year ago	Free cash flow margin in Q3 2024	Free cash flow margin in Q3 2023
Meta Platforms	18.9%	40.2%	40.6%
Microsoft	16.0%	26.5%	34.5%
MongoDB	22.3%	6.7%	8.4%
Netflix	15.0%	22.3%	22.1%
Nu Holdings	37.7%	-	-
Okta	13.9%	23.2%	25.5%
Paycom Software	11.2%	9.9%	11.4%
PayPal	5.8%	18.4%	14.8%
Salesforce	8.3%	18.8%	15.7%
Sea	30.8%	23.8%	16.8%
Shopify	26.1%	19.5%	16.1%
Starbucks	-3.2%	8.1%	13.3%
Super Hi	14.6%	-	-
Tencent	8.1%	35.0%	33.2%
Tesla	7.8%	10.9%	3.6%
The Trade Desk	27.3%	35.4%	37.3%
Tractor Supply	1.6%	-2.9%	-0.6%
TSMC	39.0%	24.3%	12.4%
Veeva Systems	13.4%	22.9%	12.4%
Visa	11.7%	66.1%	76.9%
Wise	16.2%	43.4%	38.5%
Wix.com	12.9%	28.7%	11.4%
Zoom	3.6%	38.9%	39.9%
Average for Compounder Fund's current portfolio	**13.5%**	**22.7%**	**21.2%**

Source: Companies' earnings updates

(As of the publication of this letter, there's no quarterly free cash flow data available for Adyen, Haidilao, Meituan, and Super Hi. We did not include free cash flow data for Hingham, Markel, and Nu Holdings because we don't think it's as important for them - Hingham and Nu Holdings are banks, while Markel has significant exposure to insurance businesses and investment holdings.)

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

There's more to share on the business and stock price performances of our companies. Table 10 below shows a few things for the period from 30 September 2024 to 31 December 2024 for Compounder Fund's companies: The change in their trailing 12-month

revenues-per-share; the change in their trailing P/S (price-to-sales) ratios; and the change in their stock prices.

Table 10

Company	Trailing 12-month revenue per share on 30 Sep 2024	Trailing 12-month revenue per share on 31 Dec 2024	P/S ratio on 30 Sep 2024	P/S ratio on 31 Dec 2024	Trailing 12-month revenue per share change from 30 Sep 2024 to 31 Dec 2024	P/S ratio change from 30 Sep 2024 to 31 Dec 2024	Stock price change from 30 Sep 2024 to 31 Dec 2024
Adobe	US$ 46.76	US$ 47.79	11.1	9.3	2.2%	-16.0%	-14.1%
Adyen	€ 57.79	€ 60.51	24.3	23.7	4.7%	-2.1%	2.5%
Alphabet	US$ 26.24	US$ 27.23	6.3	7.0	3.8%	10.0%	14.1%
Amazon	US$ 56.54	US$ 57.93	3.3	3.8	2.5%	14.9%	17.7%
Apple	US$ 24.94	US$ 25.38	9.3	9.9	1.8%	5.6%	7.5%
ASML	€ 64.64	€ 66.66	11.3	10.0	3.1%	-13.7%	-16.8%
Block	US$ 36.91	US$ 37.55	1.8	2.3	1.7%	24.4%	26.6%
Chipotle Mexican Grill	US$ 7.72	US$ 7.97	7.5	7.6	3.2%	1.4%	4.7%
Costco	US$ 572.11	US$ 581.73	1.5	1.6	1.7%	1.6%	3.4%
Coupang	US$ 15.18	US$ 16.11	1.6	1.4	6.1%	-15.6%	-10.5%
Datadog	US$ 6.71	US$ 7.10	17.1	20.1	5.8%	17.4%	24.2%
dLocal	US$ 2.28	US$ 2.38	3.5	4.7	4.2%	35.0%	40.8%
Fiverr	US$ 9.50	US$ 9.93	2.7	3.2	4.6%	17.3%	22.7%
Haidilao	RMB 8.14	RMB 8.14	2.1	1.8	0.0%	-13.1%	-16.6%
Hingham	US$ 18.19	US$ 18.39	13.4	13.8	1.1%	3.3%	4.5%
Intuitive Surgical	US$ 20.99	US$ 21.77	23.4	24.0	3.7%	2.4%	6.2%
Markel	US$ 1059.62	US$ 1063.26	1.5	1.6	0.3%	9.7%	10.1%
Mastercard	US$ 28.29	US$ 29.28	17.5	18.0	3.5%	3.0%	6.6%
Medistim	NOK 29.40	NOK 29.87	6.1	5.0	1.6%	-17.6%	-16.2%
Medpace	US$ 63.35	US$ 64.59	5.3	5.1	2.0%	-2.4%	-0.5%
Meituan	RMB 48.85	RMB 51.58	3.2	2.8	5.6%	-13.0%	-11.8%
Mercado Libre	US$ 343.75	US$ 374.36	6.0	4.5	8.9%	-23.9%	-17.1%
Meta Platforms	US$ 57.19	US$ 59.74	10.0	9.8	4.5%	-2.1%	2.3%
Microsoft	US$ 32.82	US$ 34.03	13.1	12.4	3.7%	-5.5%	-2.0%
MongoDB	US$ 24.83	US$ 26.08	10.9	8.9	5.0%	-18.0%	-13.9%
Netflix	US$ 82.38	US$ 85.47	8.6	10.4	3.8%	21.1%	25.7%
Nu Holdings	US$ 2.08	US$ 2.24	6.6	4.6	7.7%	-29.5%	-24.1%
Okta	US$ 14.59	US$ 14.92	5.1	5.3	2.3%	3.7%	6.0%

Table 10 (continued from above)							
Company	**Trailing 12-month revenue per share on 30 Sep 2024**	**Trailing 12-month revenue per share on 31 Dec 2024**	**P/S ratio on 30 Sep 2024**	**P/S ratio on 31 Dec 2024**	**Trailing 12-month revenue per share change from 30 Sep 2024 to 31 Dec 2024**	**P/S ratio change from 30 Sep 2024 to 31 Dec 2024**	**Stock price change from 30 Sep 2024 to 31 Dec 2024**
Paycom Software	US$ 31.45	US$ 32.36	5.3	6.3	2.9%	19.6%	23.1%
PayPal	US$ 29.27	US$ 30.02	2.7	2.8	2.5%	6.7%	9.4%
Salesforce	US$ 37.25	US$ 38.14	7.3	8.8	2.4%	19.3%	22.1%
Sea	US$ 24.12	US$ 25.69	3.9	4.1	6.5%	5.6%	12.5%
Shopify	US$ 6.03	US$ 6.31	13.3	16.8	4.8%	26.6%	32.7%
Starbucks	US$ 32.07	US$ 31.81	3	2.9	-0.8%	-5.6%	-6.4%
Super Hi	US$ 1.30	US$ 1.33	1.4	2.1	2.4%	52.6%	56.0%
Tencent	RMB 66.10	RMB 68.18	6.1	5.8	3.1%	-5.3%	-6.2%
Tesla	US$ 26.86	US$ 27.26	9.7	14.8	1.5%	52.1%	54.4%
The Trade Desk	US$ 4.36	US$ 4.62	25.2	25.5	6.0%	1.2%	7.2%
Tractor Supply	US$ 135.76	US$ 136.57	2.1	1.9	0.6%	-9.4%	-8.8%
TSMC	NT 470.19	NT 511.26	11.7	12.7	8.7%	8.6%	13.7%
Veeva Systems	US$ 15.65	US$ 16.11	13.4	13.0	3.0%	-2.7%	0.2%
Visa	US$ 17.13	US$ 17.71	16	17.8	3.3%	11.2%	14.9%
Wise	£ 1.05	£ 1.09	6.4	9.8	4.1%	52.4%	58.7%
Wix	US$ 28.32	US$ 29.23	5.9	7.3	3.2%	24.3%	28.3%
Zoom	US$ 14.58	US$ 14.72	4.8	5.5	0.9%	15.9%	17.0%
Simple average	**-**	**-**	**8.3**	**8.7**	**3.4%**	-	-

Source: Companies' earnings updates

What Table 10 highlights: **Compounder Fund's businesses performed well over the last reported quarter, with average sequential trailing 12-month revenue per share growth of 3.4%. Importantly, 43 of them experienced growth in their trailing 12-month revenues per share for 31 December 2024 compared to 30 September 2024. During the quarter, many of Compounder Fund's holdings also saw their trailing P/S ratios expand slightly from an average of 8.3 to 8.7.**

We continue to think that Compounder Fund's holdings **have more-than-reasonable valuations** (similar to what we saw when I wrote the letters for 2024's **first**, **second** and **third** quarters, 2023's **first**, **second**, **third**, and **fourth** quarters, and 2022's **second**, **third**, and **fourth** quarters) **and this bodes well for the fund's future return**. As of 31 December 2024, the companies currently in Compounder Fund's portfolio **have an average trailing P/S ratio of 8.7 and an average trailing free cash flow margin of 21.6%, which equates to an average price-to-free cash flow (P/FCF) ratio of 40.** 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 on the P/S ratio of 8.7 would be even lower at 35**.

For perspective, with the average FCF margin for Compounder Fund's current holdings expanding from 18.4% in 2020 to 21.6% in the 12 months ending in the third quarter of 2024, the companies have, on average, **grown their free cash flow at an outstanding annualised rate of 30% in that period (which is even faster than their annualised revenue growth of 24%). Importantly, we think the expansion in the free cash flow margin can continue. *This* is what gives us confidence** for the following passage in the "*Judging our performance*" section of this letter:

> "But based on the business performances of Compounder Fund's holdings, we're confident that when the fund's *stock price* performance is eventually weighed in the fullness of time, a favourable judgement is likely to result."

In an ideal world, growth in free cash flow would be similar to the growth in a stock's price. **But the world we inhabit is not ideal - the 30% annualised growth in free cash flow for Compounder Fund's portfolio companies has so far resulted in a mediocre return for the fund since inception**[1]. But if Compounder Fund's companies can continue to grow their businesses - and we think they will - we believe we'll be rewarded with a pleasing positive return eventually. Yes, most of Compounder Fund's holdings carried high valuations when we first invested in them, as I mentioned in the introductory section of this letter, so we **fully expect** Compounder Fund's eventual return to be lower than the underlying growth of its holdings' businesses. **But history suggests that the yawning gap seen so far is likely to narrow in the fullness of time**.

In our **2022 fourth-quarter letter**, I shared Walmart's past business growth and corresponding stock price movement (emphases are new):

> "Walmart's stock price fell by three-quarters from less than US$0.04 in late-August 1972 to around US$0.01 by December 1974 - in comparison, the S&P 500 was down by 'only' 40%. But by the end of 1979 (when inflation in the USA peaked during the 1970s), Walmart's stock price was above US$0.08, more than double what it was in late-August 1972 (when inflation was at a low in the 1970s)...
>
> …**At the end of 1989, Walmart's stock price was around US$3.70, representing an annualised growth rate in the region of 32% from August 1972; from 1971 to 1989, Walmart's revenue and earnings per share grew by 41% and 38% per year**.
>
> …It turns out that **in late-August 1972, when its stock price was less than US$0.04, Walmart's price-to-earnings (P/E) ratio was between 42 and 68… This is a high valuation**… at Walmart's stock price in December 1974, after it had sunk by 75% to a low of around US$0.01 to carry a P/E ratio of between 6 and 7 the easy conclusion is that it was a mistake to invest in Walmart in August 1972 because of its high valuation. But as can be seen above, Walmart's business continued to grow and its stock price eventually soared to around US$3.70 near the end of 1989. Even by

> the end of 1982, Walmart's stock price was already US$0.48, up more than 10 *times* where it was in late-August 1972."

In our **2023 second-quarter letter**, I explored a little-discussed aspect of Teledyne's history (emphasis is from the original passage) :

> "…based on what I could gather from *Distant Force,* **Teledyne's stock price sunk by more than 80% from 1967 to 1974**. **That's a huge and demoralising decline for shareholders after holding on for seven years, and was significantly worse than the 11% fall in the S&P 500 in that period**. **But even an investor who bought Teledyne shares in 1967 would still have earned an annualised return of 12% by 1990, outstripping the S&P 500's comparable annualised gain of 10%**. And of course, an investor who bought Teledyne in 1963 or 1966 would have earned an even better return…
>
> …But for the 1963-1989 time frame, based on data from *Distant Force,* it appears that the compound annual growth rates (CAGRs) for the conglomerate's revenue, net income, and earnings per share were 19.8%, 25.3%, and 20.5%, respectively; the self-same CAGRs for the 1966-1989 time frame were 12.1%, 14.3%, and 16.0%. These numbers roughly match Teledyne's returns cited by *The Outsiders* and *Distant Force*"

Our **2021 third-quarter letter** contained one of my favourite investing stories and it involves Warren Buffett and his investment in The Washington Post Company (emphasis is from the original passage):

> "Through Berkshire Hathaway, he invested US$11 million in WPC [The Washington Post Company] 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*"**

Buffett first invested in WPC in mid-1973, after which he never bought more after promising Katherine Graham (the then-leader of the company and whose family was a major shareholder) that he would not do so without her permission. The paragraph above showed that Berkshire's investment in WPC had gains of over 10,000% by 2007. But by 1983, Berkshire's WPC stake had already increased in value by nearly 1,200%, or 28% annually. From 1973 to 1983, WPC delivered CAGRs in revenue, net income, and EPS of 10%, 15%, and 20%, respectively (EPS grew faster than net income because of buybacks). This is again a case of a company's stock price movement reflecting its underlying business with the passage of time.

Walmart, Teledyne, and WPC are not idiosyncratic instances. Renowned Wharton finance professor Jeremy Siegel - of ***Stocks for the Long Run*** fame - published an article in late-1998 titled ***Valuing Growth Stocks: Revisiting The Nifty-Fifty***. In his piece, Siegel explored the business and stock price performances from December 1972 to August 1998 for a group of US-listed stocks called the Nifty-Fifty. The group was perceived to have bright business-growth prospects in the early 1970s and thus carried high valuations. As Siegel

explained, these stocks "had proven growth records" and "many investors did not seem to find 50, 80 or even 100 times earnings at all an unreasonable price to pay for the world's preeminent growth companies [in the early 1970s]." But in the brutal 1973-1974 bear market for US stocks, when the S&P 500 fell by 45%, the Nifty-Fifty did even worse. For perspective, here's investor Howard Marks' description of the episode in his book ***The Most Important Thing*** (emphasis is mine):

> "In the early 1970s, the stock market cooled off, exogenous factors like the oil embargo and rising inflation clouded the picture and the Nifty Fifty stocks collapsed. Within a few years, those price/earnings ratios of 80 or 90 had fallen to 8 or 9, meaning **investors in America's best companies had lost 90 percent of their money**."

Not every member of the Nifty-Fifty saw their businesses prosper in the decades that followed after the 1970s. But of those that did, Siegel showed in *Valuing Growth Stocks* that their stock prices eventually tracked their business growth, and had also beaten the performance of the S&P 500. These are displayed in Table 11 below. There are a few important things to note about the table's information:

- It shows the stock price returns from December 1972 to August 1998 for the S&P 500 and five of the Nifty-Fifty identified by Siegel as having the highest annualised stock price returns; December 1972 was the **peak for US stocks before the 1973-1974 bear market**
- It shows the annualised earnings per share (EPS) growth for the S&P 500 and the five aforementioned members of the Nifty-Fifty
- Despite suffering a major decline in their stock prices in the 1973-1974 bear market, members of the Nifty-Fifty whose businesses continued to thrive saw their stock prices beat the S&P 500 and effectively match their underlying business growth in the long run **even when using the market-peak in December 1972 as the starting point**.

Table 11

Company	Annualised stock price return: Dec 1972 to Aug 1998	EPS growth: 1972 to 1996
Philip Morris	18.8%	17.9%
Pfizer	18.1%	12.2%
Bristol-Myers	16.8%	12.7%
Gillette	16.8%	10.4%
Coca-Cola	16.2%	13.5%
S&P 500	12.7%	8.0%

Source: Jeremy Siegel

The examples of Walmart, Teledyne, WPC, and members of the Nifty-Fifty were all from the 1970s. You may wonder, "what if *this* time is different?" It's a legitimate concern. Economies change over time. Financial markets do too. But we believe the underlying driver for the initial divergence and eventual convergence in the paths that the companies' businesses

and stock prices had taken in the past are alive and well *today.* This is because the driver was, in our opinion, the simple but important nature of the stock market: **It is a place to buy and sell pieces of a business**. This understanding leads to a logical conclusion that a stock's price movement over the long run depends on the performance of its underlying business. **The stock market, today, is still a place to buy and sell pieces of a business, which means the market is *still a weighing machine in the long run*. So, while the stock price performance of Compounder Fund has to-date left *much* to be desired, Jeremy and I are comforted by the underlying business performances and are "confident that when the fund's stock price performance is eventually weighed in the fullness of time, a favourable judgement is likely to result."**

[1] *Referring to the earliest series for Compounder Fund's Class A shares.*

Potential bargains in a niche corner

Jeremy and I first came across a niche corner of the US stock market known as thrift conversions in January 2024. Upon further research over the subsequent months, we realised it could be an interesting hunting ground for potential bargains.

For the purpose of our discussion, thrifts, which have roots in the USA tracing back to the early 19th century, are small community banks in the country that are mutually owned by their depositors. The mutual ownership structure means that these thrifts **have no shareholders**. As a result, a thrift's depositors - despite being owners - have no legal way to access its economics. In the 1970s, regulations were introduced to allow thrifts to convert their ownership structure (hence the term "thrift conversions") and become public-listed companies with shareholders. Today, there are two main ways for thrifts to convert:

- The first is a standard conversion, where a thrift converts fully into a public-listed entity at one go.
- The second is a two-step conversion. In the first-step, a thrift converts only a minority interest in itself into a public-listed entity and thus still has a partial mutual ownership structure. In the second-step, a thrift that has undergone the first-step conversion process goes on to convert fully into a public-listed entity. As far as we know, there's no time limit for a thrift that has undergone the first-step conversion to partake in the second-step of the process.

Subsequently in this section, I will be using the word "conversion", or other forms of the same word, to refer *only to* the standard conversion, unless otherwise stated.

A thrift conversion can be thought of as a thrift undergoing an initial public offering (IPO). During a conversion, **the incentives of a thrift's management and those of its would-be shareholders are highly aligned**. In the process, a thrift offers shares to management and depositors first; if there's insufficient demand, the thrift will then offer shares to outsiders. Importantly, **management would be buying the thrift's shares during the conversion *at the same price* as other would-be shareholders** (the other would-be shareholders are the depositors and outsiders; as a reminder, prior to a conversion, a thrift has *no* shareholders[1]). This means **it's very likely that management wants a thrift's shares to have as cheap a valuation as possible during the conversion**. Moreover, new capital that's raised from management and would-be shareholders in the conversion goes directly to the thrift's

coffers. This new capital adds to the thrift's equity (calculated by deducting the thrift's liabilities from its assets) that it has built from the profits it has accumulated over time from providing banking services. These features mean that **a thrift often becomes a full public-listed entity at a low valuation while having a high equity-to-assets ratio.** It's worth noting that a thrift can **c**onduct share buybacks and sell itself to other financial institutions after the one-year and three-year marks, respectively, from its conversion.[2]

Investor Jim Royal's comprehensive book on thrift conversions (referring to both standard and two-step conversions), aptly titled ***The Zen of Thrift Conversions***, referenced a 2016 study by investment bank Piper Jaffray. The study showed that **since 1982**, **thrifts that became full public-listed entities did so at an average price-to-tangible book (P/TB) ratio of just 0.75.** After becoming public-listed entities, thrifts tend to continue trading at low P/TB ratios. This is because they also tend to have very low returns on equity - a consequence of them having a high equity-to-assets ratio after their conversion - and a bank with a low return on equity deserves to trade at a low P/TB ratio. **But the chronically low P/TB ratio is why thrift conversions could be a fertile space for bargains.**

Assuming that converted thrifts have low P/TB ratios of less than 1, **those that conduct share buybacks *increase their tangible book value per share over time* even when they have low returns on equity.** Moreover, as mentioned earlier, converted thrifts tend to have high equity-to-asset ratios, which means they have overcapitalised balance sheets **and thus have plenty of excess capital to buy back shares *without* harming their financial health.** To top it off, the 2016 study from Piper Jaffray also showed that since 1982, 70% of thrifts were acquired after the third anniversary of them becoming full public-listed entities **and these thrifts were acquired at an average P/TB ratio of 1.4**[3] (the median time between them becoming fully public and them being acquired was five years).

The growth in a converted thrift's tangible book value per share from buybacks, and the potential increase in its P/TB ratio when acquired, **could result in a strong annualised return for an investor**. For example, consider a thrift conversion with the following traits:

1. It has a return on equity of 3% in each year;
2. It has a P/TB ratio that consistently hovers at 0.7;
3. It buys back 5% of its outstanding shares annually for four years after the first anniversary of its conversion, and;
4. It gets acquired at a P/TB ratio of 1.4 five years after its conversion

Such a thrift will generate a handsome annualised return of 20% over five years. Investing in the thrift on the third-anniversary of its conversion - when the thrift can legally sell itself to other financial institutions - will **result in an even more impressive annualised return of 52% when the thrift's acquired**[4]. There are also past examples of converted thrifts that go on to produce impressive gains even *without* being acquired. In his book ***Beating The Street,*** Peter Lynch, the famed ex-manager of the Fidelity Magellan Fund, shared many examples. Here's a sample (emphasis is mine):

> "In 1991, 16 mutual thrifts and savings banks came public. Two were taken over at more than four times the offering price, and of the remaining 14, the worst is up 87 percent in value. All the rest have doubled or better, and **there are four triples, one**

7-bagger, and one 10-bagger. Imagine making 10 times your money in 32 months by investing in Magna Bancorp, Inc., of Hattiesburg, Mississippi."

But not every thrift conversion leads to a happy ending. Table 12 below shows some pertinent figures of Mid-Southern Bancorp, a thrift which produced a pedestrian return from its second-step conversion in July 2018 to its acquisition by Beacon Credit Union in January 2024.

Table 12

The features of Mid-Southern Bancorp's thrift conversion	Mid-Southern Bancorp's figures
Date of second-step conversion	12 July 2018
Stock price on second-step conversion date	US$12.40
P/TB ratio on second-step conversion date	0.95
Stock price on 3rd-year anniversary of second-step conversion date	US$15.40
P/TB ratio on 3rd-year anniversary of second-step conversion date	1.0
Acquisition date	25 January 2024
Acquisition price	US$15 - US$17
P/TB ratio on acquisition date	1.1 (at US$17 price)
Annualised return from second-step conversion to acquisition	Less than 6%
Annualised return from 3rd-year anniversary of second-step conversion to acquisition	-1.4% to 1.8%

There are a few important things we look out for in thrift conversions[5]:

- The equity-to-assets ratio: The higher the better, as it signifies an over-capitalised and strong balance sheet, and would make a thrift look attractive to a would-be acquirer
- The P/TB ratio: The lower the better, as a P/TB ratio that is materially below 1 will (a) make share buybacks a value-enhancing activity for a thrift's shareholders, and (b) enhance the potential return for us as investors
- Share buybacks: The more buybacks that happen at a P/TB ratio below 1, the better, as it is not only value-enhancing, but also indicates that management has a good understanding of capital allocation
- Non-performing assets as a percentage of total assets: The lower the better, as it signifies a thrift that is conducting its banking business conservatively
- Net income: If the play is for a potential acquisition of a thrift, we want to avoid a chronically loss-making thrift as consistent losses indicate risky lending practices, but the *amount* of net income earned by the thrift is not important because an acquirer would be improving the thrift's operations; if the play is for a thrift to generate strong returns for investors from its underlying business growth, then we would want to see

a history of growth in net income and at least a decent return on equity (say, 8% or higher)
- Change in control provisions: This relates to payouts that a thrift's management can receive upon being acquired and such information can typically be found in a thrift's DEF 14-A filing; if management can receive a nice payout when a thrift is acquired, management is incentivised to sanction a sale
- Management's compensation: The annual compensation of a thrift's management should not be high relative to the monetary value of management's ownership stakes in the thrift

Expanding on the last point of what we look out for, we've seen cases of fully-public thrifts with poor long-term business results have management teams with high compensation *and* relatively low dollar-amounts in ownership stakes. In such cases, we think there's a low possibility of these thrifts being acquired in a reasonable amount of time to maximise shareholder value because it's lucrative for the management teams to entrench their positions.

The last time I discussed an attempt by Jeremy and me to widen our circle of competence was in the "*Expanding our circle of competence*" section of our **2023 fourth-quarter letter**, where I wrote about our failure to understand the oil & gas industry. **With thrifts that have converted (be it via the standard process or the two-step process), we think we have been successful at broadening the limits of our competence**. But Jeremy and I have yet to make an investment in any thrift for Compounder Fund as we're waiting for fat pitches. If any of you reading this letter is interested to have deeper conversations about investing in thrifts, please reach out, we would love to engage.

[1.] *Thrifts that undertake the two-step conversion process would have no shareholders prior to the first-step conversion. After the first-step conversion is completed and before the second-step conversion commences, these thrifts would have shareholders who own only a minority economic interest in them.*

[2.] *Thrifts that decide to participate in the second-step of the two-step conversion process after completing the first step can begin share buybacks after the first anniversary of the second-step; they can also be acquired on the third anniversary.*

[3.] *Why would a converted thrift (referring to both standard conversions and two-step conversions) be an attractive acquisition target and be acquired at a premium to its tangible book value? This is because the acquirer of a converted thrift can easily cut significant costs and make more efficient use of the thrift's overcapitalised balance sheet; this means an acquirer can pay a premium to book value (i.e. a P/TB ratio of more than 1) for a converted thrift and still end up with a good deal.*

[4.] *The potential return of a thrift that has completed the second-step of the two-step conversion process is identical to a thrift that has completed the standard conversion, ceteris paribus. This is because the former has the same important features as the latter, such as the low valuation, the over-capitalised balance sheet, and the possibility of being acquired by other financial institutions at a premium to tangible book value.*

[5.] *What we look out for in a thrift that has completed the standard conversion is the same as what we look out for in a thrift that has completed the second-step of the two-step conversion.*

When will the market peak?

By some important measures, the valuation of US stocks does *not* look cheap. For example, the S&P 500 ended 2024 with a trailing price-to-earnings (P/E) ratio of 28. Although the ratio is lower than what it was during the height of the dotcom bubble in the late 1990s and early 2000s (around 45), it is higher than the average of 25 going back 30 years to the start of 1995. Moreover, the trailing P/E ratio of 28 also looks high when compared with the S&P 500's long-term annual earnings growth rates of 6.6%, 6.4%, and 6.9%, over the past 10 years, 20 years, and 30 years, respectively.

In another instance, the S&P 500's cyclically-adjusted P/E (CAPE) ratio was 38 at the end of 2024. The CAPE ratio is calculated by dividing a stock's price with its average earnings over the past 10 years. According to **data** from economics professor and Nobel laureate Robert Shiller, the S&P 500's CAPE ratio peaked at 44 at the height of the dotcom bubble and had averaged at 28 over the past 30 years, and 17 going back to 1881.

Given these valuation figures, does it mean US stocks will peak soon and crash? We don't know - and we don't think anyone knows either. In a 2017 *Bloomberg* **article**, investor Ben Carlson showed the level of various financial data that were found at the start of each of the 15 bear markets that US stocks had experienced back then since World War II:

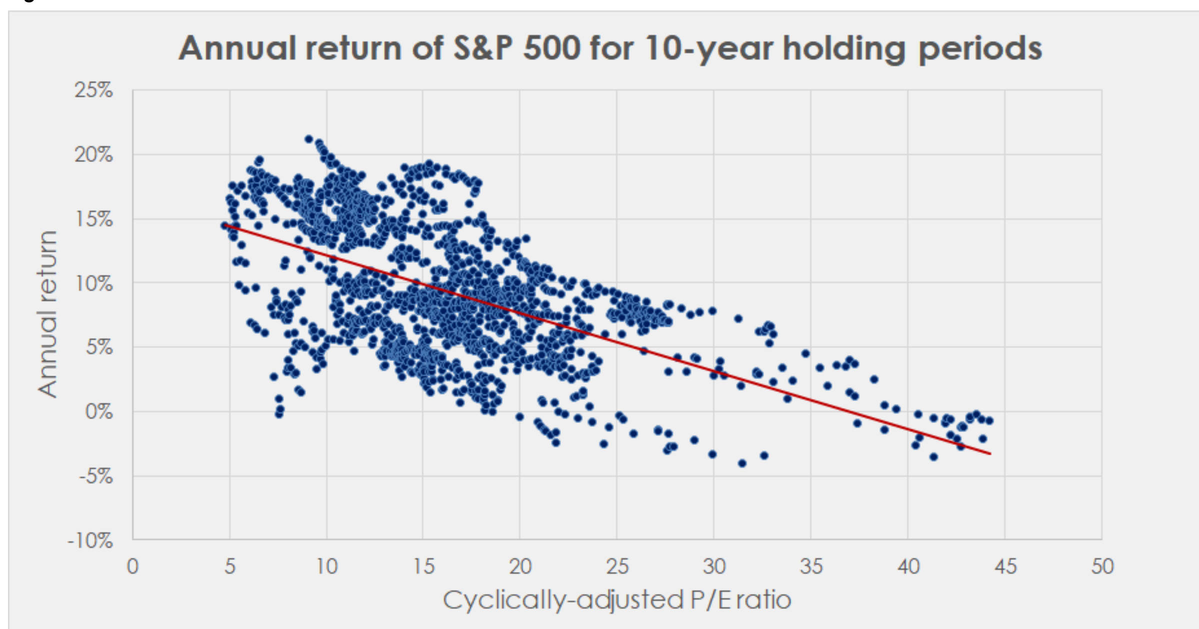
Table 13

Start of bear market for S&P 500	Subsequent decline	Trailing P/E ratio	Cyclically Adjusted P/E ratio	Dividend yield	10 Year Treasury Yield	Inflation Rate
May 1946	-26.6%	22.8	16.0	3.6%	2.2%	3.4%
Jun1 1948	-20.6%	9.0	11.6	6.0%	2.4%	9.5%
Jul 1957	-20.7%	13.6	16.9	3.7%	3.9%	3.3%
Jan 1962	-26.4%	20.4	21.2	2.9%	4.1%	0.7%
Feb 1966	-22.2%	17.4	23.7	3.0%	4.8%	2.6%
Nov 1968	-36.1%	18.8	22.2	3.0%	5.7%	4.7%
Jan 1973	-48.2%	17.1	18.7	2.6%	6.5%	3.6%
Sep 1976	-19.4%	11.0	11.8	3.7%	7.6%	5.5%
Nov 1980	-27.1%	9.5	9.7	4.8%	12.7%	12.6%
Jul 1987	-33.5%	20.1	17.3	2.8%	8.5%	3.9%
Jul 1990	-19.9%	16.4	17.8	3.3%	8.5%	4.8%
Jul 1998	-19.3%	29.4	38.3	1.4%	5.5%	1.7%
Mar 2000	-49.1%	26.8	43.2	1.2%	6.3%	3.8%
Oct 2007	-56.8%	23.4	27.3	1.8%	4.5%	3.5%
Apr 2011	-19.4%	16.3	23.1	1.7%	3.5%	3.2%

Source: Ben Carlson

The financial data Carlson presented included valuations for the S&P 500 (specifically, the trailing P/E ratio, the CAPE ratio, and the dividend yield), interest rates (in the form of the 10-year treasury yield), and the inflation rate. These are figures that the financial media and many investors pay attention to. **But they are not useful in determining when stocks will peak**. Bear markets have started when valuations, interest rates, and inflation were high as well as low. For example, the S&P 500 entered a bear market in November 1980 when the CAPE ratio was just 9.7. **But none of this is meant to say that valuations don't matter**. In fact, the starting valuation for stocks does influence their eventual long-term return. Figure 1 below uses Shiller's data and compares the S&P 500's returns for 10-year holding periods against its starting CAPE ratio from 1871 to June 2024.

Figure 1



Source: Robert Shiller data; my calculations

It's obvious that the S&P 500 has historically tended to produce higher returns when the CAPE ratio was low compared to when it was high (the red line in Figure 1 is a trendline for all the data points; notice its downward slope). **But even then, the dispersion in 10-year returns for the S&P 500 can be huge for a given valuation level**. Earlier, I mentioned that the S&P 500 had a CAPE ratio of 38 at the end of 2024. Table 14 below shows the gaping width of the subsequent 10-year annual returns of the index whenever it had a CAPE ratio of more than 30 in the past.

Table 14

10-year annual return scenario when S&P 500 cyclically-adjusted P/E ratio is more than 30	10-year annual return number
Maximum annual return	7.3%
Minimum annual return	-4.0%
Average annual return	1.4%

Source: Robert Shiller data; my calculations

To be clear, **we don't think US stocks are wildly overpriced at the moment,** so we remain long-term optimistic on the US stock market (but we also want to stress that we **have *no* knowledge of what US stocks would do in the short-term**).

In any case, instead of thinking about when the market will peak, we find it more useful to focus our mental energies on **where *individual* stocks will end up after a long period of time. This is an outcome that will depend on how a stock's underlying business fares**, **assuming the stock had a reasonable valuation at the point of investment.** On this end, Compounder Fund's portfolio comprises individual stocks that we think, in aggregate, carry reasonable valuations and have bright long-term business futures, as I had pointed out earlier in the "*Wonderful businesses*" section of this letter.

Why we're sector-agnostic

Jeremy and I mentioned in Compounder Fund's **Owner's Manual** and **website** that "the stocks we're investing in… can come… from any economic sector." This is an important feature of our investment approach. We've long been sector-agnostic when it comes to the companies we're interested in because we believe that great companies - and thus, great stocks - can come from anywhere.

Our belief was formed because of something we learnt more than a dozen years ago about the US-based airline, Southwest Airlines. Ned Davis Research was tasked by CNN's *MONEY Magazine* in 2002 to find the five US-listed stocks with the highest returns over the past 30 years. The winner was Southwest Airlines with its annualised return of 26% from 1972 to 2002; a $1,000 investment at the start of the period would have become $1 million by the end. **What is noteworthy here is airlines were widely regarded back then as businesses with horrendous economics**. In Berkshire Hathaway's 2007 **annual shareholders' letter**, Warren Buffett wrote (emphasis is ours):

> "**The worst sort of business is one that grows rapidly, requires significant capital to engender the growth, and then earns little or no money. Think airlines. Here a durable competitive advantage has proven elusive ever since the days of the Wright Brothers**. Indeed, if a farsighted capitalist had been present at Kitty Hawk, he would have done his successors a huge favor by shooting Orville down.
>
> The airline industry's demand for capital ever since that first flight has been insatiable. Investors have poured money into a bottomless pit, attracted by growth when they should have been repelled by it. And I, to my shame, participated in this foolishness when I had Berkshire buy U.S. Air preferred stock in 1989. As the ink was drying on our check, the company went into a tailspin, and before long our preferred dividend was no longer being paid. But we then got very lucky. In one of the recurrent, but always misguided, bursts of optimism for airlines, we were actually able to sell our shares in 1998 for a hefty gain. In the decade following our sale, the company went bankrupt. Twice."

And yet, it was an airline that topped the charts in 2002 for the best-performing US stock in the past 30 years. The timeframe of 30 years is also sufficiently long, such that Southwest Airlines' gains ***had* to be the result of its business's excellent long-term performance**,

and not some fortunate short-term hiccup in the fortunes of its business or its stock price.

A recent study from the highly-regarded investment researcher Michael Mauboussin, titled ***Measuring the Moat: Assessing the Magnitude and Sustainability of Value Creation***, bolsters our belief. He found that **differences in the return on invested capital (ROIC) between industries is lower than the differences in ROICs of companies within industries.** In Mauboussin's data-set, the industry with the highest median ROIC from 1963 to 2023 is Personal Care Products at around 18%. But within Personal Care Products, the companies have ROICs ranging from a low of around 5% to a high of around 40%. Meanwhile, the Wireless Telecom Services industry has one of the lowest median ROICs at around 1%. Yet, the companies within have ROICs ranging from just below 40% to deeply negative figures. Said another way, **the best company in a poor industry (Wireless Telecom Services) still has an excellent business that performs significantly better than the median company in a great industry (Personal Care Products)**.

Jeremy and I continue to believe that excellent investing opportunities can be found everywhere, so Compounder Fund will, for the foreseeable future, remain sector-agnostic. Sometimes, a gleaming diamond can be found amongst a lump of coal for those with the ability to spot a true bargain.

House-keeping matters and what's next

Compounder Fund's audit for calendar year 2024 will be conducted by Baker Tilly and should be wrapped up around the middle of this year. Once the audit report's finalised, Jeremy and I will be sending a digital copy to all of Compounder Fund's investors. As a reminder, we sent a digital copy of Compounder Fund's audited financial statements for 2023 to all of the fund's investors on 14 May 2024. If you did not receive it, or if you joined the fund as an investor after 14 May 2024 and would like a copy of the statements, 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, conducted by Baker Tilly, covered the period from November 2019 (when we started building the fund) to December 2021. Subsequent audits are for each calendar year and the audit report for 2024 will again be done by Baker Tilly. We will share the audit report on the fund's website when it is ready; as a reminder, all the audit reports for our charitable giving are available on the fund's website **here**. If you are interested to know more about our charitable giving, 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 have released the investment theses for all of Compounder Fund's current holdings (for your convenience, all our theses can be **found here**). In the future, we will also be publishing our theses if and when we add new companies to the portfolio or completely exit an existing holding voluntarily.

Compounder Fund's next subscription window will close in the middle of March 2025 and it will have a dealing date on the first business day of April 2025 (which should be 1st April). If you would like to increase your investment in the fund, please submit the relevant paperwork by the middle of March 2025. We 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. 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 8.2 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* - the desire for progress - 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 ingenuity of humanity. We will remain long-term optimistic on stocks so long as we continue to have this faith. **The only occasion we 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 year 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 (especially in difficult times like these), your belief in Compounder Fund's mission to "Grow *Your* Wealth & Enrich Society," and your understanding of the investing approach that we 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 thinking about 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 2025 first-quarter investors' letter in mid-April 2025. Till then, stay safe and take care.

Excelsior,
Chong Ser Jing
Co-founder and Portfolio Manager, Compounder Fund
13 January 2025

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

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