Farrer Wealth Managed Solution Quarterly Update

Q2 FY2022 Returns Summary

(Quarter ending December 2021)

All values in SGD terms unless otherwise stated, data is as of most recent quarter end

					Year-to-Date Returns		
Model Portfolio Returns*	**Q1**	**Q2**	**Q3**	**Q4**	**Portfolio**	**Benchmark SGD****	**Benchmark USD**
FY 2022	-0.20%	-7.40%			-7.59%	6.19%	5.62%

	Cumulative	Annualized
Model Portfolio Return Since Inception***:	-7.59%	
Benchmark (SGD) Return Since Inception:	6.19%	

Top 5 Holdings (Alphabetical Order)	Key Terms:	
eDreams Odigeo	Management Fees:	1% p.a, monthly
Evolution	Performance Fees:	15% p.a/bmark
Facebook	Minimum Size:	S$250,000
IAC	High water mark:	Yes
Sea Limited	Liquidity:	30 days notice
Total Weighting of Top 5: 52.32%	Structure:	SMA

* In order to display the most accurate representation of the returns, we use a model portfolio which has been subject to full fees since the inception of the Managed Solution. While this model account is a real client account, clients should check their own statements via their Interactive Brokers accounts to ascertain their returns as fluctuations between accounts are to be expected. Model Portfolio returns are in SGD.
** We use the iShares MSCI ACWI ETF as our Benchmark. Since this Benchmark is in USD, we convert to SGD based at the prevailing FX rates for an easier comparison. All return figures are indicative only, clients should check their own statements via their Interactive Brokers accounts for accurate figures.
*** Inception was 1st July 2021; The Managed Solutions financial year goes from July-June

Background

We launched the Farrer Wealth Managed Solution ("Managed Solution") on 1st July 2021. Through the solution we aim to provide our clients with positive returns over the medium- and long-term using bottom-up research and asset selection. While the mandate of the Managed Solution is quite broad, we tend to stick to equities as it's the asset class we know best. Typically, the Managed Solution will have between 12-20 positions in assets that we believe will outperform the relevant benchmark over time. Our investment decisions are based on deep fundamental research, much of which we publish on our website. Investments are sector- and geography- agnostic, and instead focus on businesses that are growing market share in markets that are growing. The Managed Solution's goal is to give our clients outperforming returns so that they do not have to make the individual asset selection themselves. The solution does not short nor use leverage but may buy options from time to time to hedge or express a particular view.

A word on returns

This was a slightly disappointing start to the Managed Solution, which has now operated for six months. Most of the underperformance so far happened in this quarter, and was driven by two of our key holdings, Sea Limited and Sendas Distribuidora, which saw large corrections. The fall in these two stocks contributed to a loss of -3.65% and -2.34% to the portfolio this quarter respectively. This was offset by eDreams Odigeo contributing 2.91%. With regards to returns, there are four categories of performance from most to least desirable: 1) Making money and outperforming 2) Making money but underperforming 3) Losing money but outperforming and 4) Losing money and underperforming. The first six months of performance has placed us in the fourth category, but the good news is we can only move up from here.

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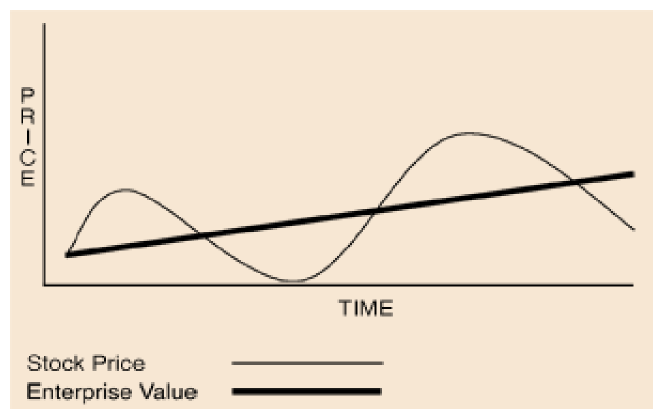
Stock prices are usually volatile. Over the short run (less than a year or even two), it's tough to predict how a stock will move, so we don't try. Instead, we focus on how the business is performing with regards to our expectations when we invested in them. With few exceptions, our businesses performed either at or better than our expectations during the last two quarters. Over time, business performance and stock performance should align, and thus we don't pay too much attention to short-term movements in our stocks. We remain excited for 2022 given the business performance of our companies and feel that most of the value in the portfolio is yet to be unlocked. As usual, we put our money where our mouth is, and a large majority of our wealth is invested in Farrer Wealth Solutions.

A follow up from the previous letter

Upon reviewing the feedback from our inaugural letter, we felt that there were two elements that are worth explaining a bit further.

1) *Why we invest over a three- to five-year period:* There are several reasons for this. For one, anyone who has ever started or run a business knows it takes time to build an enterprise worth building. Often quarter-to-quarter results don't show much, but even incremental changes over a longer period add up. This is essentially why Venture Capital and Private Equity funds originally had long lockup periods. It takes time for businesses to grow, mature, and show results. Secondly, traditionally business cycles are viewed in three- to five--year periods which encompassed both the boom-and-bust phases. While the last several years have been anything but typical, and it's possible that given the pace of innovation and central bank liquidity these phases are getting shorter, we do think taking a longer-term view helps us navigate these phases better. Lastly, one of our favourite charts is given here. The image illustrates that the value of a business is not its stock price, and that it's rare that a stock price coincides exactly with the value of a business. Most of the time it either overshoots or undershoots. While we try to invest in a business during one of the troughs, there is no telling how long that trough can last, and thus the longer the time horizon the better the chance you can exit your investment at above fair value.



2) *Why we do deep fundamental research:* There are, in our view, two fundamental ways to make money in financial markets. You can trade or you can invest. Both methods have done enormously well for those who employ it, given, and here's the catch, that those methods reflect the personality of those wielding them. Often permanent capital losses happen when market participants don't know themselves well and don't understand what game they are playing. We

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try not to make this mistake. Put it another way, we are terrible traders. We have never been good at spotting short-term movements, chasing momentum, and cannot deal with the emotions that go into monitoring a daily PnL. So, we don't trade. We do believe where we have an edge is in our patience, which lends nicely to long-term investing. But just as we stated in the previous point, over a three-to-five-year period the stocks of companies will go through good and bad times. The only way we can deal with the bad times is by knowing the companies we've invested in well and having a solid understanding of the underlying business including the value of that business. Therefore, we spend months on researching our portfolio companies before making the investment, and we dedicate a significant portion of our time re-learning, reassessing, and revaluating our current holdings.

Updates on Portfolio Companies

This was anything but a dull quarter, with several key events occurring in our portfolio companies. Below, we'll discuss the most pertinent ones.

Evolution AB (EVO):

As a quick reminder for those who read our previous letter or our research on Evolution, Evolution is a market leader in live casino, supplying online gambling services to iGaming operators globally. In late November, a complaint was made by a "competitor" to the New Jersey Division of Gaming Enforcement claiming that Evolution both allowed players to access their games from sanctioned countries, like Iran, and from countries where it is illegal to gamble, like Singapore. The allegations hit at the heart of the risks associated with the business, and investors fled, causing the stock to fall 40% in about two weeks. We wrote a blog post about the incident, which can be read here, and where we outlined where the report had validity and where it was quite off-base. We won't rehash those points here, but rather discuss what happened after we posted that blog. For one, the company learned a lot about its investor base and its investor base learned a lot about the company. EVO held a call shortly after the report was released that lasted 10 minutes and took no questions from analysts. To put it bluntly, it was a PR disaster, and investors took more from what the company did not say rather than what they did say. While this was a big misstep by the company, it was not entirely unpredictable. HQ for EVO is just a handful of people handling corporate affairs and investor relations. Most of the company, including the CEO (Martin Carlesund) is focused on operations and execution, and in our view, hadn't taken the time to appreciate that their success had attracted an investor base that was a bit blind to the realities of online gambling (and gambling in general).

However, once most of these investors were shaken out, the company announced a stock buyback, which buoyed the stock price. More importantly the company was proactive in releasing when they bought shares, and at what prices, setting a short-term floor for the stock. We also feel that during this period the remaining investor base wisened up and understood that EVO only works with regulated operators and distributors, and while there is a swathe of grey area in where iGaming companies can and do operate, there is only so much EVO can tell them to do. Put another way, if

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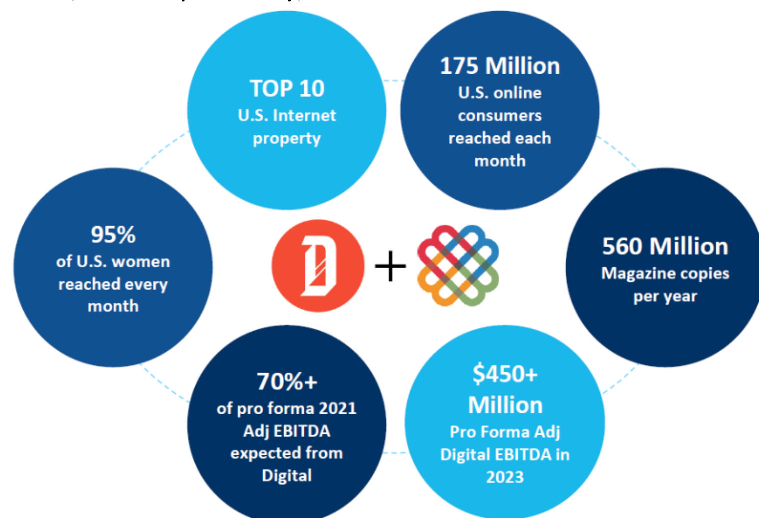
you are a supplier to a regulated market, it is up to the regulator to tell your customer what to do and what not to do, and not for you, the supplier, to police your customers. This also implies, that regulators are neither blind nor stupid, and are aware of the way the industry operates. All of this is to say, while there are murky elements to iGaming, I think EVO's investor base is now far more aware of the potential risks and are invested with eyes wide open. The company's buybacks and investor realizations boosted the stock which rallied back 45%+. We took advantage of this volatility by selling down a third of the position when the report initially released and bought almost all of it back at much lower levels. We are pleased with this outcome, and EVO remains in our top 5 position. Given how well they seem to be doing operationally both in the US and with expansions in Latin America, we suspect the future is bright and that EVO will stay as one of our top 5 positions for quite some time.

IAC:

With an investment world playing checkers, Joey Levin and the IAC team seem to be playing chess. In early October, IAC announced the combination of their DotDash business with Meredith Holding Corp. For those unfamiliar, DotDash owns several digital publishing brands (investors will be most familiar with Investopedia) catering to nearly 100 million monthly users. Meredith owns both offline and online publications including People, InStyle, and Better Homes & Gardens. The combined entities will reach 175 million monthly consumers, and impressively, 95% of US women. One of the most important parts of this deal was that in a year when investors were piling into untested companies at enormous price to sales multiples that this transaction was done at just 7.5x trailing EBITDA. Further, the company believes that the combined entity will deliver over $450 million in EBITDA in 2023. However, considering that at the time of the deal Meredith did over $358 million in EBITDA and DotDash did $88 million, we feel this is sandbagging quite a bit. Granted there will likely be an ongoing decline in Meredith's print business (which still makes up most of their revenues), there is significant efficiency to be had with IAC at the helm. For one, while Meredith is great at brand advertising, it earns about half of what DotDash does per visit on performance marketing. In a world where Apple's iOS changes make it more difficult for traditional advertising platforms to target users, platforms like Meredith and DotDash have a unique advantage. For example, there's a good chance someone viewing the Better Homes & Gardens recipe page would be interested in a slow-cooker. No user profile nor cookies necessary.



It can be difficult owning a company like IAC. It is essentially the corporate version of the Ship of Theseus experiment, which makes thinking about what the company will look like in the future

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daunting. However, when management pulls off deals that on its own would value the non-public parts of the company at between 10-12x 2023 EBITDA, you can rest easy knowing your money is in the hands of top-notch capital allocators who have proven themselves time and time again.

New Ideas…

We added only one new full position to the portfolio during the quarter, and that was Vizio Corp. We publicly published our research on Vizio, and you can read it in detail here. Vizio is the quintessential under-the-hood story where the market is looking at consolidated results and ignoring what's happening beneath the surface. We've made several of these investments in the past whether it would be the market ignoring the profitability of Garena hiding in consolidate numbers (Sea Limited), missing the success of Prime in an income statement battered by covid (eDreams), under-playing the growth of the advertising business (Spotify), or overlooking excellent deal making in its private holdings (IAC). In Vizio's case you have a good, but not great, hardware business (Vizio is the 3rd largest TV brand in America) which is growing at low-single digits, overshadowing a rapidly growing Platform+ business, which, driven by advertising, is growing at triple digit rates year on year and making up a majority of gross profits. Considering how much time we spend on our connected TVs, it's quite surprising the proportion of ad-spend on connected TVs gets versus that of linear TV. Connected TV ad spend is just 16% of total in the US and is predicted to hit nearly 30% by 2025 creating a market of nearly $30bn. This shift, we believe, will raise all boats, and in particular benefit a company like Vizio who, unlike Roku, the big name in the space, owns all its own hardware and thus has the ability to have a deeper understanding of its customer. The market is yet to see this, and we believe that Vizio is trading at less than 6x 2025 EBITDA. We believe this should change quickly, as the Platform+ business becomes a bigger portion of the pie, top line growth rates will start to look more attractive to the market at large and the company will have the profitability to support higher valuations.

Macroeconomic outlook …

The market is currently an uncertain place (although, when is it not), with a heavy rotation away from growth names and into more traditional investments such as commodities, financials, energy, and legacy retailers. Further even within the growth space, there exists a dichotomy of results. At the end of the year, only about 20% of the Nasdaq's components were trading above their 50 day daily moving average, while the index itself was just 2.57% off its peak. With rising interest rates to battle rising inflation and the potential of quantitative tightening on the horizon, the future looks tough for stocks. Unprofitable companies have been particularly hammered, bringing back memories of the early 2000 dotcom bust. That recurring is a scary thought; however, we do believe that there are several key differences between the markets then and now. For one, online businesses play a significantly larger part of our daily lives, second online businesses have much better fundamentals driven by significant operating leverage, and lastly, in the early 2000s there was a viable alternative to stocks considering interest rates were much higher.

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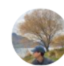
That said, only about 12% of our portfolio is made up of stocks that are either not profitable or do not have positive free cash flows. Much of this is our position in Sea Limited that has a highly-profitable gaming arm and a balance sheet with over $11 billion in cash. Further, as stated in our previous letter, our portfolio is made up of several exciting businesses in various industries around the globe. We own fast-growing tech, publishing conglomerates, cash & carry and financial businesses in Emerging Markets, European iGaming and travel stocks, as well as a few QQQ stalwarts. While there exist scenarios where all businesses do poorly, we do think we are well positioned for the current (and most) environments. Just in case we're wrong or if some of our positions drawdown further, we do currently have active hedges in the portfolio.

A concluding note…

While we are a bit disappointed at our current returns, it's very early days for this Managed Solution, and like we give our portfolio holdings several years to prove themselves we ask that our investors do the same with us. That said, this ask is a bit rhetorical as we think we have been very lucky to have an investor base that is patient and highly supportive. As Joel Cohen of MITs endowment put it in a recent tweet:



Joel Cohen
@joelmcohen

If you manage money for other people, now is a great time to have awesome, long-term oriented partners who knew exactly what they were signing up for, love what you do, and are excited that you're down (yes, they do exist).

Terrible time not to have those things.

3:02 AM · Dec 4, 2021 · Twitter Web App

We've said this before, and will repeat it often, but it is an immense privilege to manage our client's hard-earned money. It is a privilege we do not take lightly and work daily at earning and keeping our client's trust. If you are a current client and ever have any questions or just want to chat, please do not hesitate to reach out.

Lastly, for non-clients reading this letter, if you are interested in learning more about Farrer Wealth, please reach out at pratyush@farrerwealth.com. All interested parties must be based in Singapore and must be Accredited Investors (as per MAS's definition).

Pratyush Rastogi
CEO – Farrer Wealth Advisors

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