

# The Next Level Portfolio

## 3Q 2021 Investor Letter

**Dear Long Term Investors,**

We are in the midst of the 3Q earnings season so it will be a good time to report on the business that we invest in.

In the last quarter, the Next Level Portfolio did not do much fund-raising. Instead, we received many referrals from you - our existing investors. We thank you for your trust and recommendation in the Next Level Portfolio, and be rest-assured that we will continue to do our best.

Therefore, after being closed for more than 3 months, we are happy to announce that the **Next Level Portfolio is opened for new accounts and top-up funding to existing accounts.**

**For new accounts**

1. Apply at <https://investwithpete.co/how-to-apply>
2. Submit both online application and the pdf forms
3. Min. investment sum is S\$50,000 or equivalent in other currencies

**For top-up funding to existing accounts**

1. Transfer your funding to the Phillip Capital account (For SGD transfer: <https://www.poems.com.sg/payment/> , Other currencies transfer: <https://www.poems.com.sg/helpcentre/PSPLTrustAccounts.pdf> )
2. State their ACCOUNT NUMBER and ACCOUNT NAME clearly in their payment instruction
3. No min. investment sum for top-up funding

**Learning from Mistakes**

Now, let me start on the previous quarter, and as usual I like to start with the mistakes where we can learn the most.

*“Mistakes of omission are more costly than bad investments” - Warren Buffett*

In the last quarter, we did not make any bad investment. This is also reflected in the 3Q earnings where the total revenue and cashflow of all our companies combined went up by more than 15% YoY.

However, the mistake is when we do not match our investment to our conviction and **invest too little**.

I am referring to **eXp World Holdings, Inc (NASDAQ: EXPI)**

For those who followed my thoughts in the Next Level Portfolio, you would know that eXp World Holdings is one of my highest conviction stock right now.

This is a company which we have done extensive research and even factoring a conservative growth number, it was egregiously undervalued. And with the “call option” on other parts of the business, we felt that we have a huge margin of safety on top of an outstanding growth of ~25% YoY.

Therefore, we opened positions on EXPI. It has since done very well for us and returned over 30% profits in a short span of time. *(However we are not too focused on the short term, as we believe this business will continue its current trajectory for more years to come)*

And here comes the “mistake”, as Buffett would say, we did not “*swing at the ball*”.

We initiated a 3-4% allocation and since then the price has gone up to \$54 as of this writing.

If we had allocated more, it would have a bigger uplift on the Next Level Portfolio. Overall, we are still pleased with the investment but we wished we were more “brave”.

We have definitely learned the lesson well and you will see us swing harder at high conviction investments in years to come. *(For starters, we will increase our EXPI allocation in the coming weeks)*

## **When It Makes a Difference**

Thankfully, we were “brave” in other investments and that made a huge difference in our portfolio.

We are referring to Tesla and Etsy. Both companies represent a significant portion of the Next Level Portfolio. Let me elaborate more on both and why we intend to stay invested rather than taking profits early.

Let me start with a story.

In 2020, when COVID struck the world, a particular industry was flourishing. It is the Ornamental fish industry, namely Koi. In hindsight, it seemed quite obvious as lockdown takes its toll, people will look towards hobbies to occupy themselves.

This created a mad rush of rearing Koi. Kois all across the world were being snapped up. Serious fish hobbyists even fly to Japan to buy them from [source](#).

One of the Japanese Koi breeders is Shintaro.

While Shintaro was putting up his top-prized matured Kois for sale, he refused to sell some of his juvenile Kois, even when he was offered more than US\$10,000 for each. This was bewildering to many.

Juvenile Kois are usually not favoured, as they have not reached their optimal size, the colouration may not be at its brightest and they may have some blemishes on the skin.

By keeping these juvenile Kois, he is potentially missing out on a few good sale.

Unbeknown to outsiders, Shintaro is actually keeping his best.

Not only is Shintaro a breeder, he is one of the top Koi fish breeders in Japan. His Kois are not the common ones found in gardens or homes. These are Champion Kois worth millions of dollars each - The Rolls Royce of Koi.



(This Koi was sold at an auction for US\$1.8m)

In one of the rare interviews he did, Shintaro revealed his secret.

He revealed that he kept those juvenile Kois because he sees huge potential in them. While they might be worth \$10,000 as a juvenile, if well-bred and groomed, they could be worth 100x more in a few years' time.

How's that for a good return on investment!

However, the most shocking response was when asked about the matured Champion Koi.

Shintaro replied, "I don't keep them, they can't grow any better than that."

While Shintaro is a Koi breeder, he probably does not invest in the stock market. I believe he would be very successful in investing.

## Tesla and Etsy

In our view, Tesla and Etsy are like the juvenile Kois. They may have some blemishes in their businesses such as negative income and higher debt. (Tesla never turn a profit on net income until 2020, while Etsy Debt-to-Equity ratio is a whopping 400%)

However, beyond these blemishes, we see a lot of potential in them.

Tesla is far ahead in the EV game and the bigger energy game. The brand factor is similar to that of Apple. When you buy a Tesla, you know you are buying a quality product that is cool.

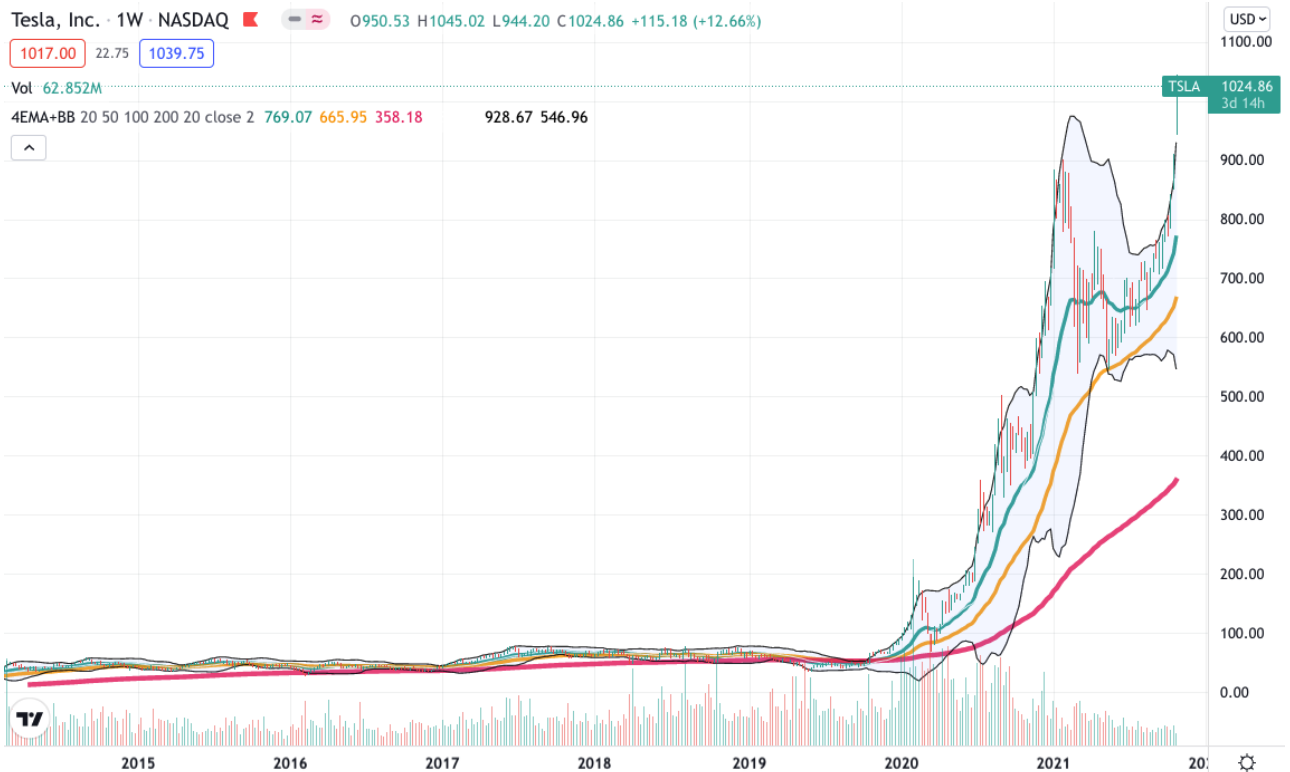
With fast increasing cashflow, the danger of Tesla going bankrupt is now only a remote possibility. Coupled with two more Gigafactories coming online in 2022, the number of vehicle delivery is very likely to increase exponentially.

Etsy also provides a very similar story. As the smaller e-Commerce player in the industry, Etsy is often unfavourably compared to Amazon. However, when you dig deeper, you will notice that this is a high gross profit margin business and its return on capital has been increasing since 2018.

However, just like the juvenile Kois, it takes time for Tesla and Etsy to mature into Champion Koi.

For example, it took Tesla more than 10 years to reach profitability, and once it achieved profitability, the share price responded accordingly.

	INCOME STATEMENT														BALANCE SHEET	CASH FLOW STATEMENT	RATIOS
Income Statement	31/12/06	31/12/07	31/12/08	31/12/09	31/12/10	31/12/11	31/12/12	31/12/13	31/12/14	31/12/15	31/12/16	31/12/17	31/12/18	31/12/19	31/12/20	LTM	
% Change YoY			20,094.5%	659.3%	4.3%	74.9%	102.3%	387.2%	58.8%	26.5%	73.0%	68.0%	82.5%	14.5%	28.3%		
Cost of Goods Sold		(2.31)	(20.58)	(102.41)	(86.01)	(142.65)	(383.19)	(1,557.23)	(2,316.69)	(3,122.52)	(5,400.88)	(9,536.00)	(17,419.00)	(20,509.00)	(24,906.00)	(36,023.00)	
Gross Profit		(2.24)	(5.84)	9.54	30.73	61.60	30.07	456.26	881.67	923.50	1,599.26	2,223.00	4,042.00	4,069.00	6,630.00	10,825.00	
% Change YoY			161.2%	263.2%	222.3%	100.4%	(51.2%)	1,417.5%	93.2%	4.7%	73.2%	39.0%	81.8%	0.7%	62.9%		
% Gross Margins		(3,063.0%)	(39.6%)	8.5%	26.3%	30.2%	7.3%	22.7%	27.6%	22.8%	22.8%	18.9%	18.8%	16.6%	21.0%	23.1%	
Selling General & Admin Expenses	(5.44)	(17.24)	(23.65)	(42.15)	(84.57)	(104.10)	(150.37)	(285.57)	(603.66)	(922.23)	(1,410.49)	(2,477.00)	(2,835.00)	(2,646.00)	(3,188.00)	(3,992.00)	
R&D Expenses	(25.00)	(60.45)	(49.01)	(19.28)	(93.00)	(208.98)	(273.98)	(231.98)	(464.70)	(717.90)	(834.41)	(1,378.00)	(1,460.00)	(1,343.00)	(1,491.00)	(2,375.00)	
Other Operating Expenses																27.00	
Other Operating Expenses	(30.43)	(77.70)	(72.66)	(61.43)	(177.57)	(313.08)	(424.35)	(517.55)	(1,068.36)	(1,640.13)	(2,244.90)	(3,855.00)	(4,295.00)	(3,989.00)	(4,679.00)	(6,340.00)	
Operating Income	(30.43)	(79.93)	(78.50)	(51.90)	(146.84)	(251.49)	(394.28)	(61.28)	(186.69)	(716.63)	(645.64)	(1,632.00)	(253.00)	80.00	1,951.00	4,485.00	
% Change YoY			162.7%	1.8%	33.9%	182.9%	71.3%	56.8%	84.5%	204.6%	283.9%	9.9%	152.8%	84.5%	131.6%	2,338.8%	
% Operating Margins		(109,497.3%)	(532.5%)	(46.4%)	(125.8%)	(123.1%)	(95.4%)	(3.0%)	(5.8%)	(17.7%)	(9.2%)	(13.9%)	(1.2%)	0.3%	6.2%	9.6%	
Interest Expense	(0.42)		(3.75)	(2.53)	(0.99)	(0.04)	(0.25)	(32.93)	(100.89)	(118.85)	(191.82)	(477.00)	(653.00)	(725.00)	(784.00)	(530.00)	
Interest And Investment Income	0.94	1.75	0.53	0.16	0.26	0.26	0.29	0.19	1.13	1.51	8.53	19.00	24.00	44.00	30.00	37.00	
Currency Exchange Gains (Loss)								11.90	2.00	(45.60)	26.10	(52.00)	2.00	48.00	(114.00)	(25.00)	
Other Non Operating Income (Expenses)	0.06	0.14	(2.21)	(2.91)	(6.58)	(2.65)	(1.83)	10.70	(0.19)	3.95	(10.55)	(9.00)	10.00	37.00	28.00	120.00	
EBT Excl. Unusual Items	(29.86)	(78.05)	(83.93)	(57.18)	(154.16)	(253.92)	(396.08)	(71.43)	(284.64)	(875.62)	(813.38)	(2,151.00)	(870.00)	(516.00)	1,111.00	4,087.00	



Similarly, Etsy only achieve positive income in 2018 and the stock price follow suit.

INCOME STATEMENT    BALANCE SHEET    CASH FLOW STATEMENT    RATIOS

Income Statement	31/12/12	31/12/13	31/12/14	31/12/15	31/12/16	31/12/17	31/12/18	31/12/19	31/12/20	LTM
Revenues	74.60	125.02	195.59	273.50	364.97	441.23	603.69	818.38	1,725.63	2,148.38
<b>Total Revenues</b>	<b>74.60</b>	<b>125.02</b>	<b>195.59</b>	<b>273.50</b>	<b>364.97</b>	<b>441.23</b>	<b>603.69</b>	<b>818.38</b>	<b>1,725.63</b>	<b>2,148.38</b>
% Change YoY		67.6%	56.4%	39.8%	33.4%	20.9%	36.8%	35.6%	110.9%	
Cost of Goods Sold	(24.49)	(47.78)	(73.63)	(96.98)	(123.33)	(150.25)	(190.76)	(271.04)	(464.75)	(562.83)
<b>Gross Profit</b>	<b>50.11</b>	<b>77.24</b>	<b>121.96</b>	<b>176.52</b>	<b>241.64</b>	<b>290.98</b>	<b>412.93</b>	<b>547.34</b>	<b>1,260.88</b>	<b>1,585.55</b>
% Change YoY		54.1%	57.9%	44.7%	36.9%	20.4%	41.9%	32.6%	130.4%	
% Gross Margins	67.2%	61.8%	62.4%	64.5%	66.2%	65.9%	68.4%	66.9%	73.1%	73.8%
Selling General & Admin Expenses	(32.81)	(48.96)	(89.52)	(132.21)	(167.86)	(190.64)	(240.90)	(332.79)	(654.99)	(843.34)
R&D Expenses	(18.65)	(27.55)	(36.63)	(42.69)	(55.08)	(71.38)	(97.25)	(121.88)	(180.08)	(212.52)
<b>Other Operating Expenses</b>	<b>(51.46)</b>	<b>(76.51)</b>	<b>(126.15)</b>	<b>(174.90)</b>	<b>(222.94)</b>	<b>(262.03)</b>	<b>(338.15)</b>	<b>(454.67)</b>	<b>(835.07)</b>	<b>(1,055.86)</b>
<b>Operating Income</b>	<b>(1.36)</b>	<b>0.73</b>	<b>(4.19)</b>	<b>1.62</b>	<b>18.70</b>	<b>28.96</b>	<b>74.79</b>	<b>92.68</b>	<b>425.81</b>	<b>529.69</b>
% Change YoY		154.1%	(671.9%)	138.5%	1,057.1%	54.9%	158.3%	23.9%	359.5%	
% Operating Margins	(1.8%)	0.6%	(2.1%)	0.6%	5.1%	6.6%	12.4%	11.3%	24.7%	24.7%
Interest Expense	(0.49)	(0.30)	(0.59)	(1.53)	(7.20)	(11.13)	(22.18)	(24.32)	(42.03)	(25.60)
Interest And Investment Income	0.05	0.05	0.04	0.32	1.70	2.39	8.96	13.20	7.10	3.54
Currency Exchange Gains (Loss)			(3.05)	(21.78)	(14.95)	29.11	(6.49)	3.01	(6.52)	6.85
Other Non Operating Income (Expenses)	(0.74)	(0.42)	(0.41)	(3.13)						
<b>EBT Excl. Unusual Items</b>	<b>(2.53)</b>	<b>0.06</b>	<b>(8.20)</b>	<b>(24.49)</b>	<b>(1.76)</b>	<b>49.32</b>	<b>55.08</b>	<b>84.56</b>	<b>384.37</b>	<b>514.48</b>



Overall, we believe that Tesla and Etsy still have a lot of potential in their future development. Therefore, we opt to be patient with these investments and selectively adding more when the prices are right.

Of course, should they mature into a Champion Koi, we will sell them just as Shintaro-san did.

### **What to expect from the market going forward?**

Q3 has been a good quarter for us, the entire portfolio was lifted by ~10%. This was mainly due to recovery from a technical correction in September.

With Biden and his spending spree, the market is flushed with cash and liquidity.

This was most visible in the run up of equity and home prices around the world. US homes on average went up by 12-13% last year, with certain states hitting almost 30%. Singapore also had a similar experience with home prices rising 9% this year and expecting to hit 10% by end of 2021.

In the near term, we expect the economic tailwind to continue to push the markets higher as asset holders continue to be rewarded. We also agree with Jack Dorsey, CEO of Twitter and Square, that inflation is upon us. This is clearly reflected in the higher cost due to supply chain issues. Commodities prices are already front running the equities market.

To ride on the wave of inflation, our strategy remains the same - To invest in great businesses at a reasonable price.

Cryptocurrencies are also brought up by the rising tide with BTC and ETH hitting an all time high as of this writing. You will notice the presence of cryptocurrencies in your portfolio.

Several of you shared that your bankers are unable to invest in crypto for you or you have difficulty investing in crypto. We are happy to share that unlike other fund houses, our investment mandate allows us to invest in cryptocurrencies.

We are strong proponents of cryptocurrencies as we see their utility and future in the financial world. At over US\$2bn market cap, we believe crypto is no longer a fad and cannot be ignored as an asset class. Therefore, we look to further allocation in cryptocurrencies in the future.

### **Till Next Level**

That sums up this quarterly letter! I hope you enjoyed reading it just as much as I did preparing it. A quick update on hiring a research analyst, we have found a great candidate and he has begun work earnestly. Thank you everyone for all the recommendations.

### **Time for SRS again**

For those who are investing with SRS funds, please remember to top up your SRS before **31 Dec 2021** to enjoy full tax benefits. Everyone can benefit from SRS, including foreigners.

**Do inform me after topping up your SRS to allow the Next Level to invest the new funds.**



**For existing cash investors, if you would like to add more funds, we are happy to assist. Please email me at [petetanpy@phillip.com.sg](mailto:petetanpy@phillip.com.sg).**

Please feel free to forward this quarterly letter to anyone who are interested in investing with the Next Level Portfolio. **We are opening new accounts!**

With that, I will see you next quarter!

Regards,  
Pete