

Vision Capital Investor's Letter - 2021



VISIONCAPITAL.GROUP

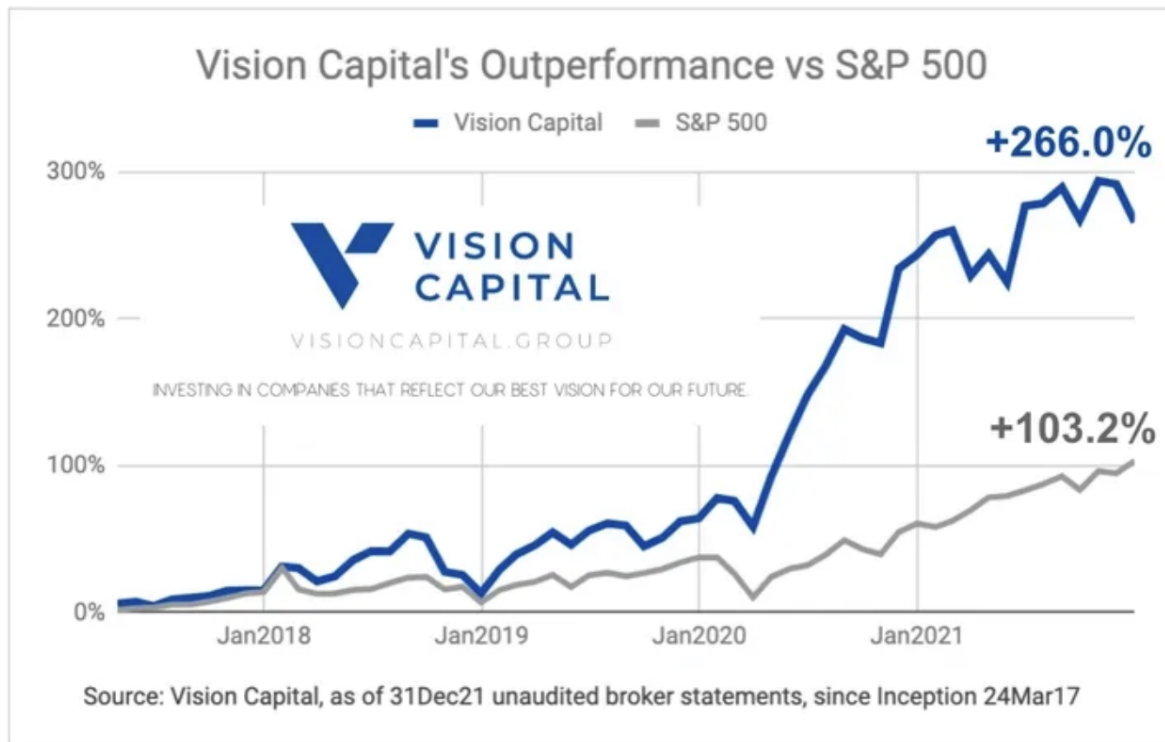
INVESTING IN COMPANIES THAT REFLECT OUR BEST VISION FOR OUR FUTURE.

Dear Investor (to myself as the single LP),

I welcome you to Vision Capital's inaugural annual investor letter.

For 2021, Vision Capital returned +6.5% versus the S&P 500's +27.0%. Since inception on 24 March 2017, it has returned +266.0% versus the S&P 500's +103.2%. The chart and table below detail in greater detail our performance thus far.

Our Historical Performance



Returns	Vision Capital	S&P 500	Excess
YTD (2021)	+ 6.5%	+ 27.0%	- 20.5%
1Y	+ 6.5%	+ 27.0%	- 20.5%
2Y	+ 123.1%	+ 47.8%	+ 75.3%
3Y	+ 224.2%	+ 90.2%	+ 134.0%
Since Inception	+ 266.0%	+ 103.2%	+ 162.8%

Returns	Vision Capital	S&P 500	Excess
2017	+ 15.0%	+ 14.0%	+ 1.0%
2018	- 1.7%	- 6.3%	+ 4.5%
2019	+ 45.3%	+ 28.7%	+ 16.6%
2020	+ 109.5%	+ 16.4%	+ 93.2%
2021 (YTD)	+ 6.5%	+ 27.0%	- 20.5%
Since Inception	+ 266.0%	+ 103.2%	+ 162.8%

Inception 24 Mar 2017. As of 31 Dec 2021. Updated monthly.

Vision Capital's investment mandate is global in nature, and we can invest in any listed stock in the world. But since the majority of our holdings are currently US-listed stocks (~95.4% as of 31 Dec 2021), it's also important to us that we compare our performance with a prominent US stock market index, in this case, the S&P 500.

Below are our reflections for 2021:

1 | Underperformance, not ideal but not unexpected.

2021 was our first year of underperformance, where we returned +6.5% vs the market's (S&P 500) +27.0%.

That said, it is always important to focus on the bigger picture where we have returned +266.0% vs +103.2% since March 2017.

Just as it is important to zoom in, it is just as important to zoom out.

2 | Judging our Performance.

Our aspirational target for Vision Capital is to generate an annualised return of 25% or more over the long run (minimum 5-7 year period and even longer).

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.”

It is not going to be easy, but we have to try. We sincerely believe that if we shoot for the moon, even if we miss, we will still land among the stars.

Investing is our Ikigai. It is what we love, what the world needs, what we think we are good at, and what we can be paid for (eventually).

It is truly our passion, and we believe we can keep doing this for the next forty years until we are well into our eighties and beyond.

3 | Returns will not be smooth.

We cannot promise consistency of returns. In fact, the only promise we can make is that returns will not be smooth. It is just how the stock market works. The broad stock market does not provide smooth returns, and returns will vary significantly from year to year.

Ultimately we ask that our investment results should be judged over at least a 5-7 year period.

We will be hitting our 5 year anniversary in three months time (Mar 2022), and we hope that our investing philosophy, framework, and longer-term track record will eventually speak for itself.

4 | The occasional underperformance, inevitable.

Whilst a period of underperformance against the S&P 500 is never welcome, it is nonetheless inevitable. We are not aware of any investment strategy that will consistently outperform every year, and every type of market condition.

Similarly we do not expect that we will be able to beat the market each month, each quarter, or each year.

5 | Playing the right long game.

We are not aiming to be the best in any given year by swinging for the fences, making bets that will cause us to lose all our capital. In fact, we think the probability of us being wiped out completely is extremely unlikely, unless the world is coming to an end.

We are not aiming to be in the top decile in any year, but rather we are aiming to have the consistency and the durability to be above average for a long time.

Howard Marks says this best in his very first memo, in the “The Route to Performance” in October 1999 of a pension manager:

We have never had a year below the 47th percentile over that period or, until 1990, above the 27th percentile. As a result, we are in the fourth percentile for the fourteen year period as a whole.

Source: [Oaktree Capital](#)

All you need is to be above average for a long time, and last longer than others, you will eventually be one of the best out there.

6 | The best too, can underperform from time to time.

So as much as we do not like it, we can and have to expect some occasional periods of underperformance from time to time.

Hopefully less, and not more is the norm. Time will be our judge.

Most of the top investors don't consistently outperform as well, nor should we expect it of ourselves.

E.g. **Warren Buffett and Charlie Munger's Berkshire Hathaway** underperformed ~1/3 of the time over 55 years from 1965-2020, but still is one of the best investments of all time, returning 20.0% CAGR vs the market's 10.2%.

Berkshire Hathaway (1965-2020)















Year	Annual Percentage Change	
	in Per-Share Market Value of Berkshire	in S&P 500 with Dividends Included
1965	49.5	10.0
1966	(3.4)	(11.7)
1967	13.3	30.9
1968	77.8	11.0
1969	19.4	(8.4)
1970	(4.6)	3.9
1971	80.5	14.6
1972	8.1	18.9
1973	(2.5)	(14.8)
1974	(48.7)	(26.4)
1975	2.5	37.2
1976	129.3	23.6
1977	46.8	(7.4)
1978	14.5	6.4
1979	102.5	18.2
1980	32.8	32.3
1981	31.8	(5.0)
1982	38.4	21.4
1983	69.0	22.4
1984	(2.7)	6.1
1985	93.7	31.6
1986	14.2	18.6
1987	4.6	5.1
1988	59.3	16.6
1989	84.6	31.7
1990	(23.1)	(3.1)
1991	35.6	30.5
1992	29.8	7.6
1993	38.9	10.1
1994	25.0	1.3
1995	57.4	37.6
1996	6.2	23.0
1997	34.9	33.4
1998	52.2	28.6
1999	(19.9)	21.0
2000	26.6	(9.1)
2001	6.5	(11.9)
2002	(3.8)	(22.1)
2003	15.8	28.7
2004	4.3	10.9
2005	0.8	4.9
2006	24.1	15.8
2007	28.7	5.5
2008	(31.8)	(37.0)
2009	2.7	26.5
2010	21.4	15.1
2011	(4.7)	2.1
2012	16.8	16.0
2013	32.7	32.4
2014	27.0	13.7
2015	(12.5)	1.4
2016	23.4	12.0
2017	21.9	21.8
2018	2.8	(4.4)
2019	11.0	31.5
2020	2.4	18.4
Compounded Annual Gain – 1965-2020	20.0%	10.2%
Overall Gain – 1964-2020	2,810,526%	23,454%

Note: Data are for calendar years with these exceptions: 1965 and 1966, year ended 9/30; 1967, 15 months ended 12/31.

Source: [Berkshire Hathaway](#)

Peter Lynch's Fidelity Magellan Fund (1977-1990)

E.g. The Magellan Fund underperformed ~14% (2 of 14) of the time over 14 years from 1977-1990, but still returned 29.2% CAGR, more than twice that of the S&P 500.

1990		-4.51%	-3.78%
1989		34.58%	27.76%
1988		22.76%	12.55%
1987		1.00%	1.56%
1986		23.74%	14.05%
1985		43.11%	28.64%
1984		2.03%	-3.94%
1983		38.59%	18.56%
1982		48.06%	32.75%
1981		16.45%	-2.13%
1980		69.94%	40.60%
1979		51.73%	32.37%
1978		31.71%	15.06%
1977		14.46%	2.56%

Source: [Yahoo Finance](#)

7 | Little to Recover from.

This is particularly so when we had a period during 2020–21, where the world was heavily impacted by the pandemic.

The negative economic effects of the pandemic were at their height, but the majority of the businesses we owned proved to be highly resilient. In fact, most ended up accelerating their growth at an even faster pace than before.

As a result, we ended up outperforming the market in 2020, returning +109.5% vs +16.4% for the S&P 500, with the majority of our >80 positions beating the market.

However, last year in 2021 was really more of a year of normalisation. Similarly, most of our companies had relatively little to recover from. In fact, most had even more challenging temporary higher comparables and higher base effects, which could well gradually normalise in the coming quarters.

8 | Bottom up Business Focused Investors, not Top-Down Macroeconomic Driven Investors.

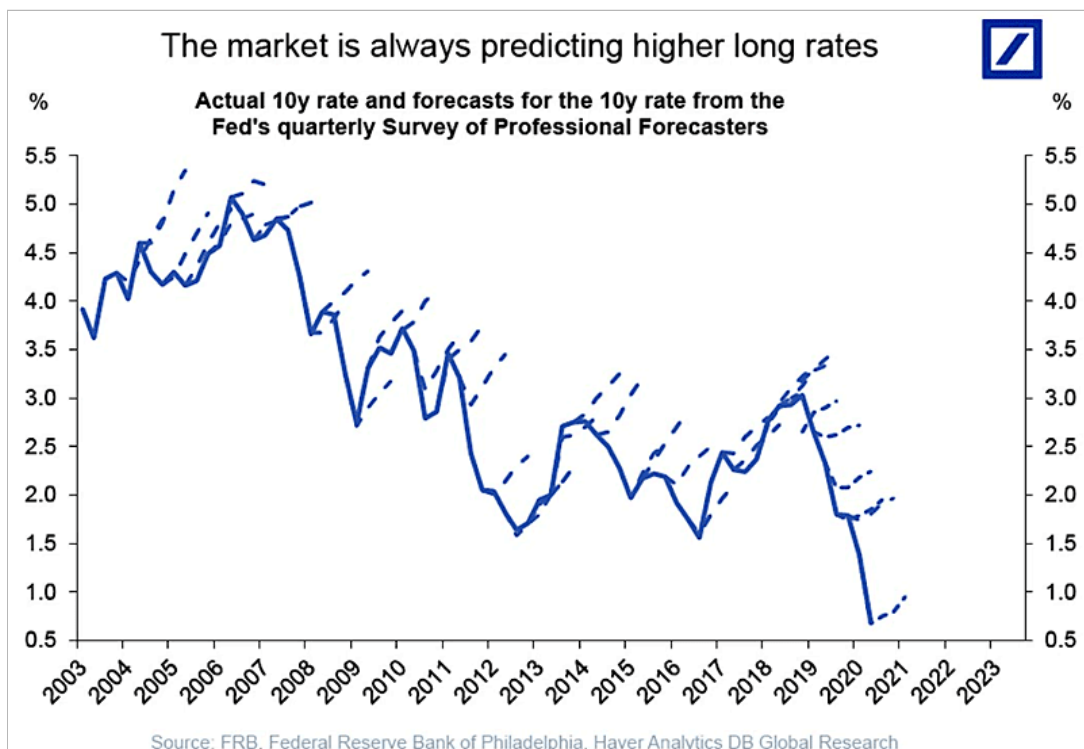
The good news is that we do not invest on the basis of our ability to forecast inflation or any other macroeconomic factor.

Most expert macroeconomic forecasters cannot consistently predict what will happen (see chart below), why should we try to. It is not a game that we want to play.

We generally understand and are aware of what's going broadly, but we do not let any of it influence our long-term investing decisions. We prefer to be bottom-up business focused investors, not top-down macro-economic driven investors/traders.

We invest in companies with long-term secular tailwinds, not rotating between countries, indices, sectors, companies based on how the economy or what the market thinks which will do better at any given year.

We might look short-term foolish because we are unlike most, but we hope to win long-term by focusing on what we do best.



9 | Rotating is not our game.

In investing and in life, very often you cannot have it both ways. It is difficult, if not impossible to find companies which are resilient in a downturn, but yet can also still benefit fully from the subsequent recovery.

Of course, we could try to trade out of the former and into the latter at the right time, but it is neither what we are good at, nor a game we seek to play.

Doing so involves getting four things right:

- (1) selling the former at the top,
- (2) buying the latter at the bottom,
- (3) selling the latter at the top, and
- (4) re-buying back the former at the low.

If you had a 60% probability of getting each right (which is very high), the outcome of getting all 4 outcomes right is ~13% (60% x 60% x 60% x 60%). Assume if you hold a 10 stock portfolio, and have to exit all 10, buy all 10, sell all 10 and buy back new 10. The constant trading and missing the best days is really a futile exercise in our opinion.

We are not aware of many perfect market timers who can do that consistently, and that's why we do not even bother trying to.

Having to time perfectly the high or the lows, which companies and the right sizing are just too many factors for us. We are most probably going to get it terribly wrong than fantastically correct.

10 | Our alpha comes from holding businesses, not trading them.

The vast majority of our returns and alpha that we generate come from the ability of the companies we own, being able to continue to grow rapidly, being able to reinvest their retained earnings at high rates of return due to strong unit economics, solid balance sheets and attractive profitability.

Durability of these companies matters, their persistence to keep growing matters, and our ability to hold them through market sell-offs matters.

In our view, it would be a terrible mistake to sell some/all of these good businesses in order to invest temporarily in cheap companies which are much poorer fundamentally still, but could have a greater temporary recovery potential.

Trying to predict and rotate amongst short-term winners is a difficult game, and one we do not want to play. We prefer to play long games with higher probable outcomes, than short games with lower probable outcomes.

That said, it would be interesting to watch once the latter companies normalize, and start guiding back to their original low single-digit top-line revenue growth rates in the coming quarters, if Mr Market continues to like them versus the types of faster and more durable growing businesses that we prefer to own.

That said, always remember the market can always stay irrational, for far longer than one thinks.

11 | Understanding the true drivers of stock market returns.

In the short-term, from quarter to quarter, there is generally little correlation between a company's fundamentals and its stock price.

Companies report earnings four times a year, whilst the stock moves 250+ working days a year. In the long-term though, there is generally a far higher correlation between a company's fundamentals and its stock price.

In the short-term, stock price movements are largely changes in valuation multiples (~46%) (typically sentiment, interest rates, etc), but in the long-term, company fundamentals (~95%) (revenues, profits and cash flows) primarily drive intrinsic value and stock returns.

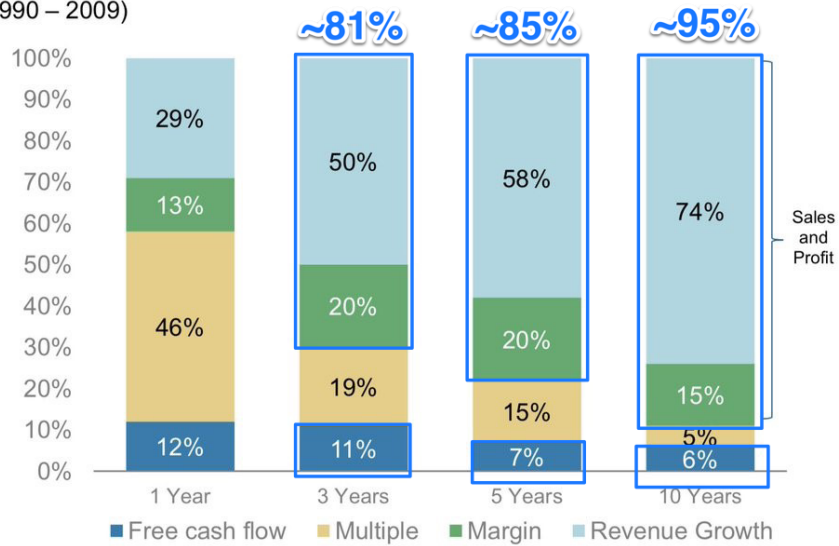
That's why we remain focused on owning quality innovative businesses run by strong management that are growing revenues rapidly and durably, delighting customers with strong unit economics with rising profits and cash flows.

Topline Growth the Long-Run Driver of Stock Performance

Sales Growth Is the Key Driver of Long-Term Stock Performance

Sources of Total Shareholder Return for Top-Quartile Performers

S&P 500 (1990 – 2009)

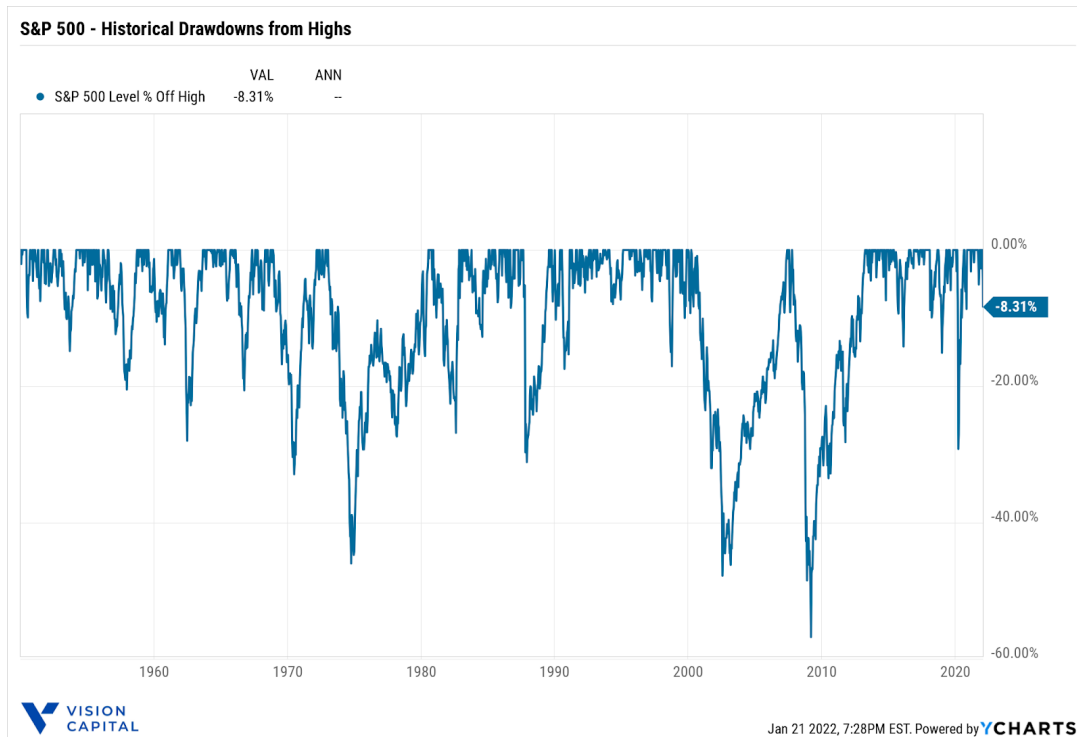


Source: BCG Analysis, Morgan Stanley Research

12 | Differentiate from Price Volatility and Business Volatility.

Short-term daily price performance almost always significantly deviates from long-term business performance.

This is a feature of the stock market, not a bug. Understanding this is extremely crucial.



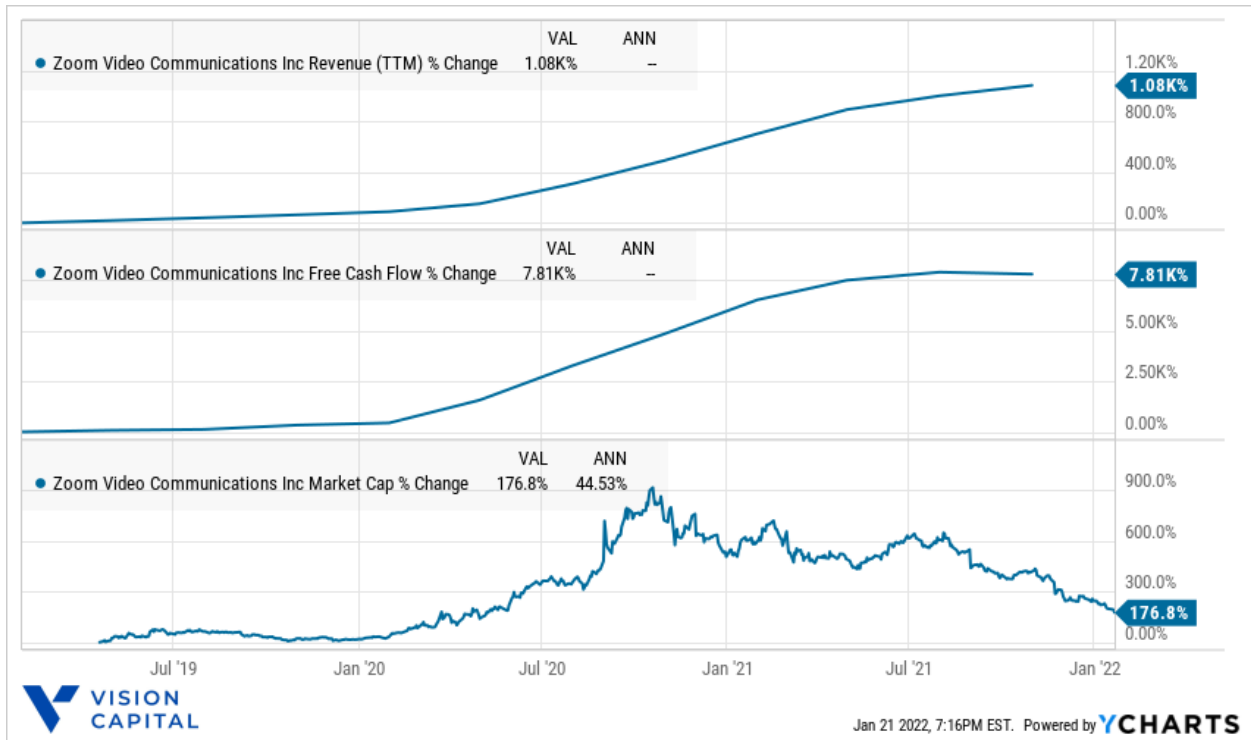
Long-term returns only come to those who are willing to bear that short-term price volatility (especially price declines), and pay that admission fee to be invested, when most won't and don't. That's our behavioural edge and is why we prefer to be business-focused investors, not a price-focused one.

13 | Five Businesses

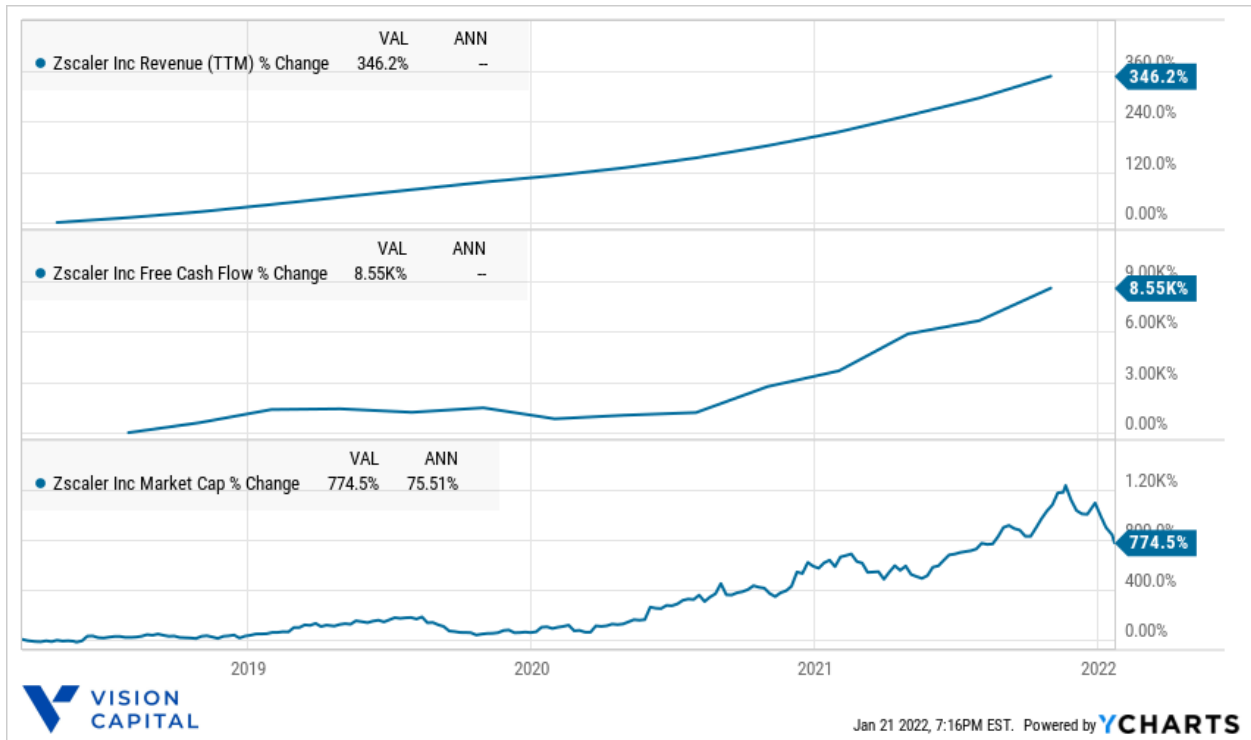
Below are charts of five businesses that we own, highlighting their trailing twelve month (TTM) revenue growth, free cash flow (FCF) growth and the market capitalization.

The first two: Revenues and FCF highlight the business fundamentals (available each quarter) and the market capitalisation (available daily) Mr Market's being a short-term noisy voting machine, but long-term weighing machine.

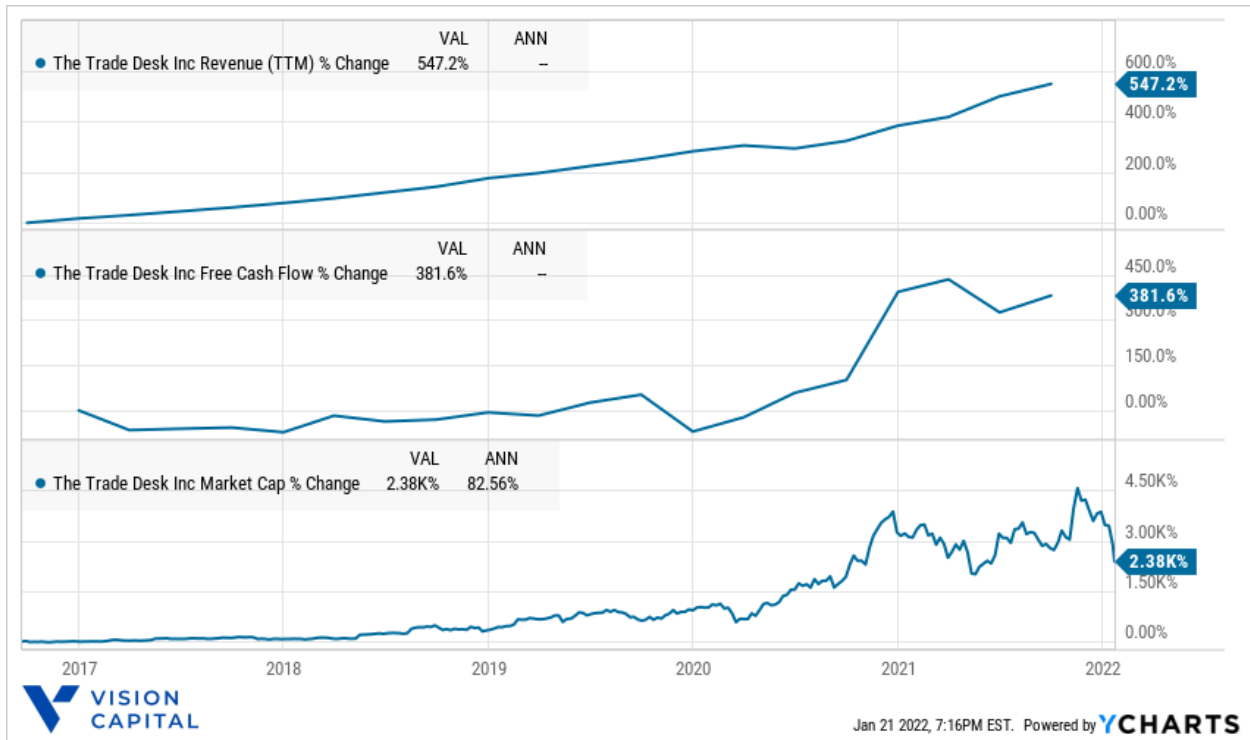
(1) Zoom Video Communications



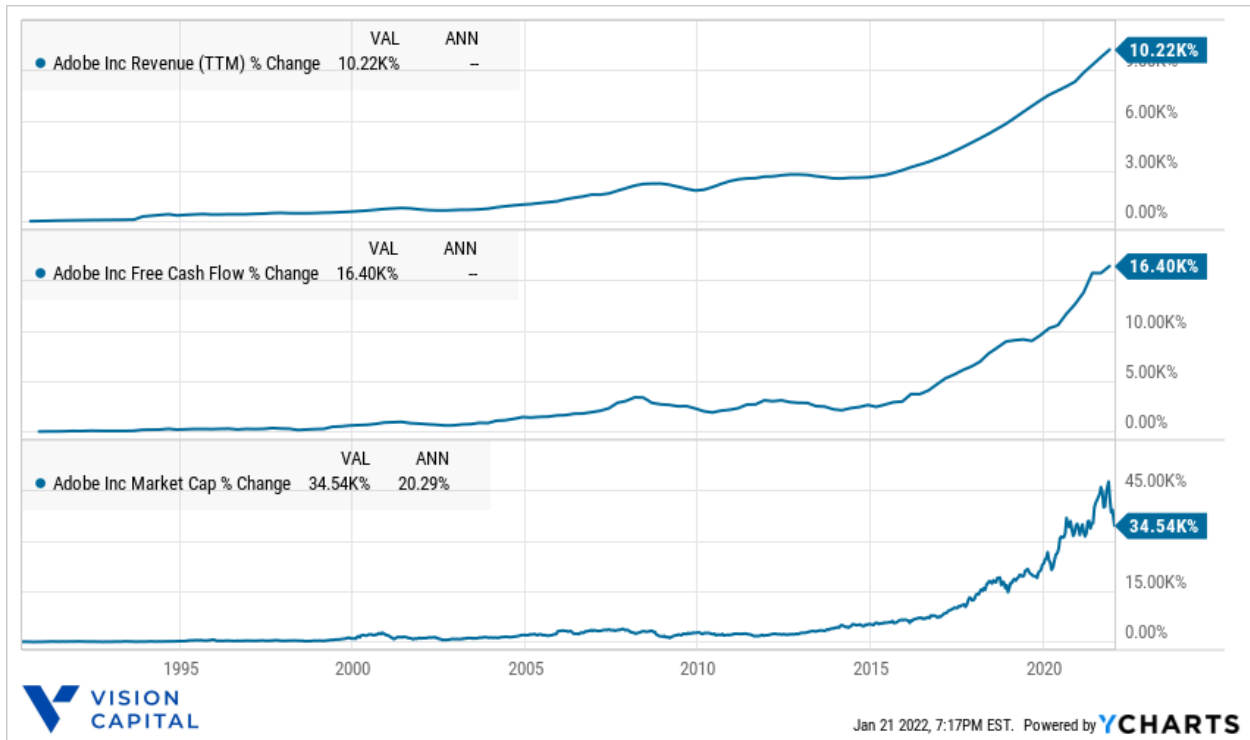
(2) Zscaler



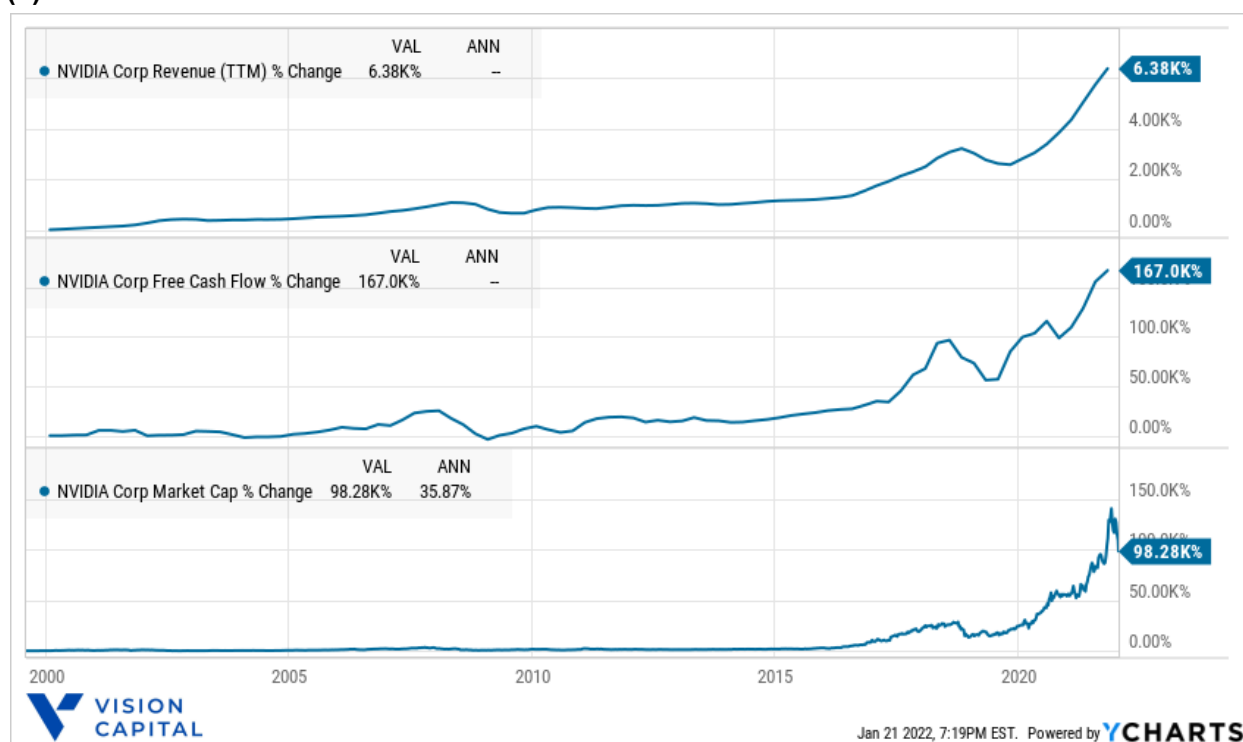
(3) The Trade Desk



(4) Adobe



(5) NVIDIA



Source: YCharts

14 | Learnings from our exits.

We are long-term business owners and our preferred holding period is forever. That is the intention that we set out each time we start or add to a position. Unfortunately, as much as we like and aim to be correct, there will be times we will get it wrong.

That is perfectly okay, as long as the losses from our losers do not wipe us out, and prevent us from continuing to play the long game.

We sell largely due to three main reasons: (1) we got it wrong, (2) structurally declining business fundamentals (declining revenue growth, no signs of improving profitability) or (3) better opportunities. We never sell just because they have risen in price, we focus solely on the business fundamentals, not the price technicals.

Most of the time, it will be due to the first two reasons, very rarely it will be for the third reason (i.e. better opportunities). As for the latter, it is something we had done once thus far, at the end 2020. We trimmed 4 positions (Facebook, Alphabet, Align & Arista Networks) which were sizable relative to the portfolio, and we wanted to re-allocate to some of our higher conviction smaller sized positions. The reallocation amounted to 4.4% of the portfolio as of 31 Dec 2020.

In 2021, we exited a total of 11 positions in its entirety, which accounted for a very small ~2.0% turnover of the entire portfolio value as of 31Dec2021.

Most of these positions that we exited had originally started as starter positions, and never saw new capital being added throughout time, as their businesses didn't quite end up going the way as per our investment thesis, and got us wanting to invest more.

The companies we exited are: Alteryx, AppFolio, BASE, Carvana, Clover Health, Disney, Fastly, HealthEquity, Invitae, Metromile and Wix.

Disney's exit was largely due to its move into gambling and sports betting, a decision undertaken by current management Bob Chapek. It was a complete departure from previous CEO Bob Iger's stance. It resulted in an immediate exit of the entire position (see more [here](#)), as it is against our philosophy of holding any companies related to gambling, as we do not see it making the world a better place (see more [here](#)).

The two SPACs, Metromile and Clover Health in particular, taught me a lesson to distinguish between insanely optimistic forward looking projections to differentiate versus what the business could really be. For the former, Lemonade has since announced the acquisition of Metromile post our exit, which seems to make sense for Lemonade to accelerate their go-to-market. That said, the insurance business is slow to build, but can become extremely durable once they get the product/service and business model right. Let's see how Lemonade does in the coming years.

For the remaining 8 exits, most of them involved numerous quarters of consecutive fundamental business declines, either a combination of very rapidly declining revenue growth and/or poor persistent profitability which gave us significantly less confidence to continue owning them.

For example, Carvana's consistently deteriorating (not improving) FCF dynamics despite their still fast topline growth left us not wanting more, which is why we exited.

15 | New Names Added.

We maintain a high conviction list of 20-30+ companies of our 84 position portfolio that we are happy to allocate new capital should there be large price declines, despite the businesses themselves still doing perfectly fine.

We have to raise our standards and set an even higher bar for new businesses to be added, they really have to be quite exceptional. We believe the sweet spot for us is probably around 50+ core positions or so.

We allocated new capital across 37 companies (mostly existing) amounting to a gross ~8.2% of the entire portfolio as of 31Dec2021.

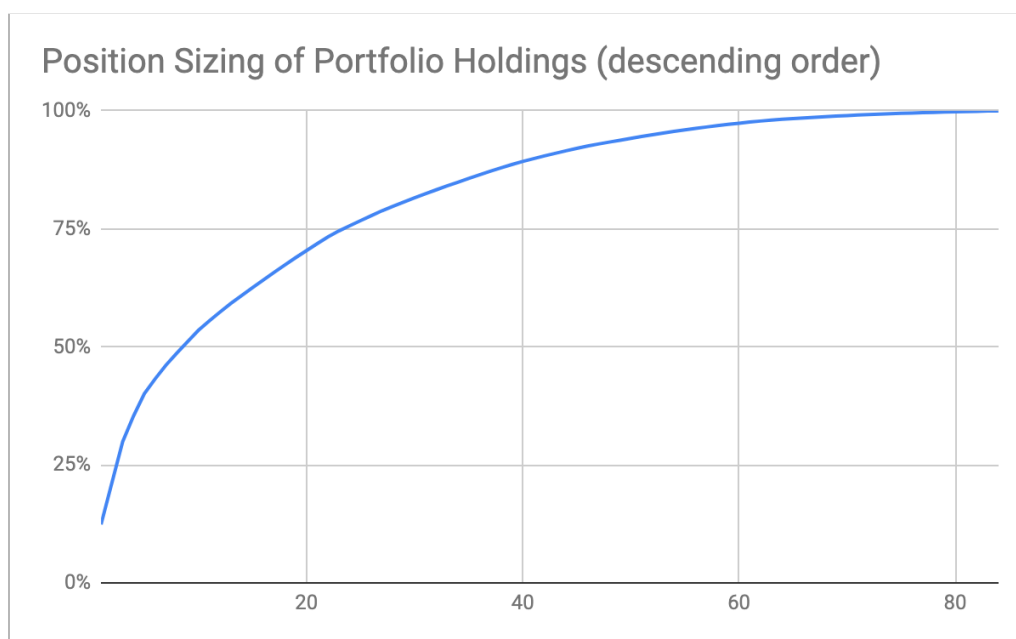
9 new names were added: ASML, Coinbase, Danimer Scientific, DLocal, Pacific Biosciences, UiPath, Upstart, Wise & ZoomInfo.

Of the 9 new names, 2 were not profitable but extremely technology innovative if they can pull it off. They are Danimer Scientific in biodegradable bioplastics (PHA) and Pacific Biosciences in long-read DNA genetic sequencing. Positions were intentionally sized very small (<0.1%) in these two, given the high expected volatility.

16 | Concentrated, and yet not overly diversified.

Despite owning a large number of companies, totalling 84. The portfolio is not overly diversified, with the vast majority in less than 50 holdings.

As of 31 Dec 2021, the top 20, 30, and 40 positions accounted for ~70%, ~80% and ~90% of the overall portfolio respectively.



Source: Vision Capital, as of 31 Dec 2021

17 | Asymmetric Payoffs

Stocks have limited downside, but unlimited upside.

The maximum a stock can go down to is -100%, thus limited downside.

But the maximum a stock can go up is theoretically infinite, unlimited upside with multi-baggers that can 5X, 10X, 20X, 50X, 100X and more.

That very favourable asymmetric risk-return profile, results in a very positive skew and power law, where very few long-term winners typically account for the majority of returns.

We had set up our portfolio and investing framework and philosophy to capitalise exactly on this.

18 | Power Laws

We let our winners drive our outperformance, because winners become more relevant with time, and losers become less relevant with time.

By allowing our winners to run, the accumulated gains from our top 10 and 20 winners accounted for 75% and 91% of the entire portfolio's accumulated gains.

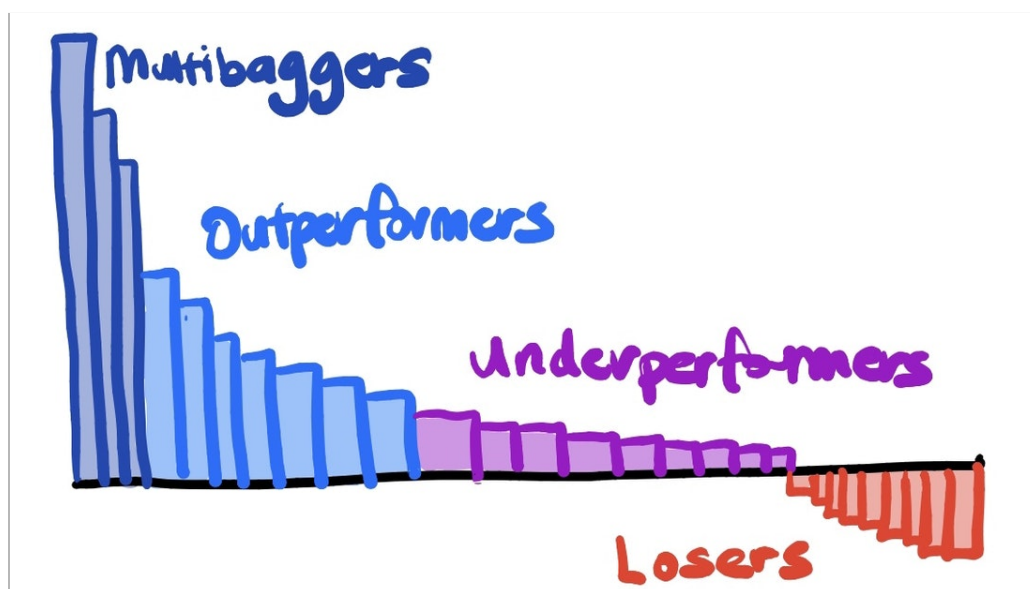
The accumulated gains from the top 13 winners accounted for 80% of the overall portfolio's gains.

When the winners in your investment portfolio keep winning, the gains from all our winners combined, will far outweigh the losses from all our losers combined many folds over.

In fact, the gains from our biggest winner is more than 3X the losses from our losers combined. Extending that to our top 10 biggest winners, the combined gains are more than 11X all of the losses combined.

Winners become more relevant, and the losers become less relevant with time.

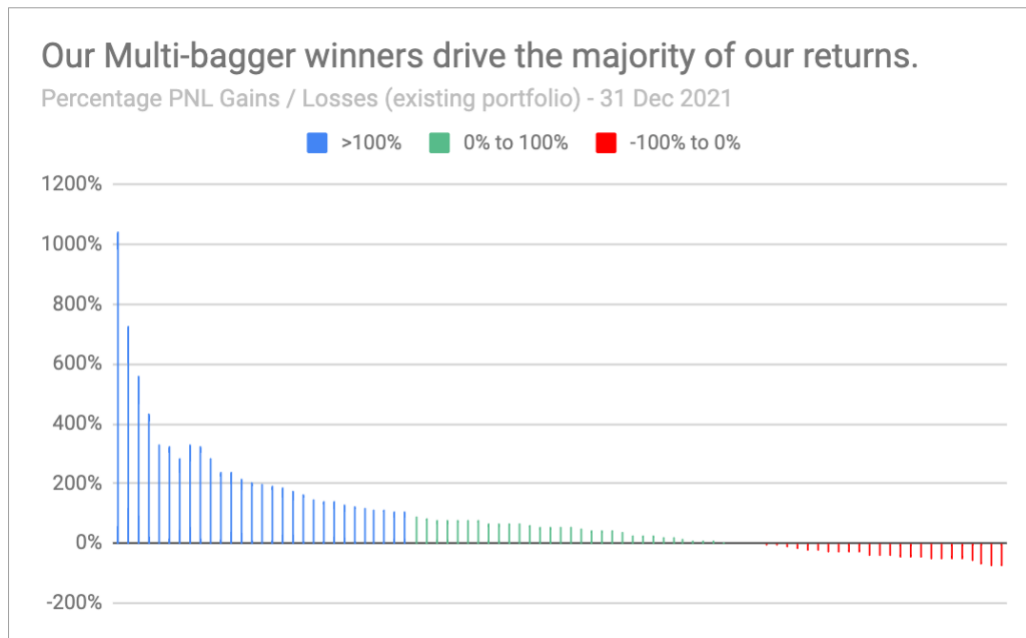
When we first started investing, we visualised that our investment portfolio would look somewhat like this chart below with time (also documented in [my book](#), Vision Investing), and become even more pronounced with time.



Source: [Vision Investing: How We Beat Wall Street & You Can, Too!](#)

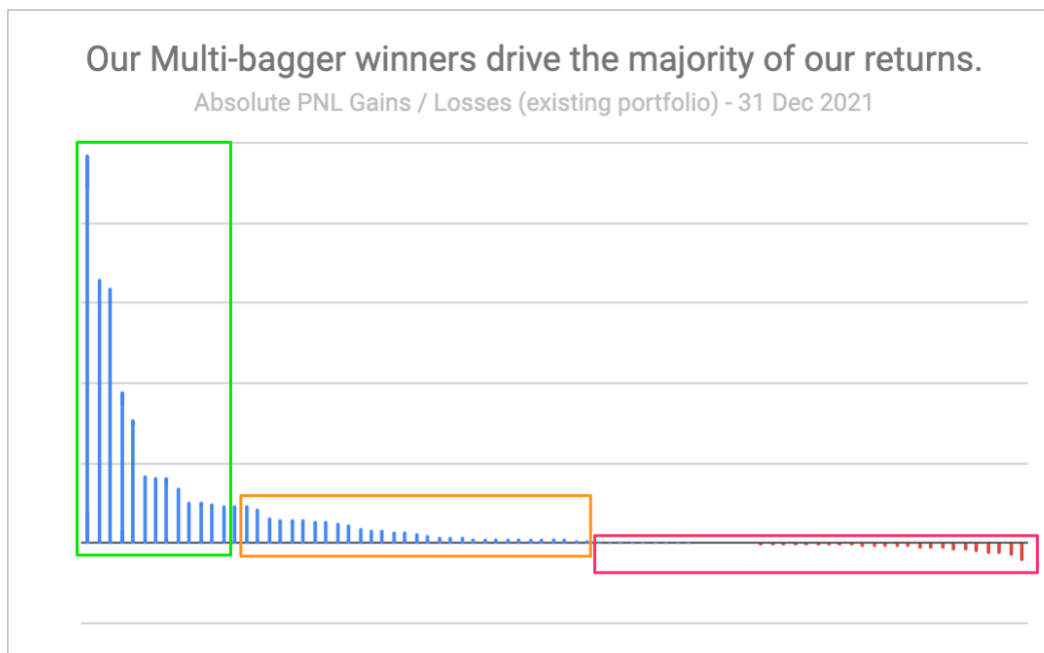
Looking on a **return basis**, we have **29 multi-baggers (~34% of portfolio) where gains are in excess of 100%**. The top 3 positions are >10X, >7X and >5X on our invested capital thus far.

Separately, there are **32 positions (~38% of portfolio) with positive gains (0-100%)** but not yet multibaggers and **26 losers (~32% of the portfolio) thus far with negative gains (-100% to 0%)**.



Source: *Vision Capital, as of 31 Dec 2021*

Looking at the **absolute gains/losses**, it becomes far more instructive, where the absolute gains from the winners more than offset the losses from the losers combined.



Source: Vision Capital, as of 31 Dec 2021

The two charts below are very instructive. We allow our winners to run very high, and let them concentrate our portfolio on their own over the long-run.

This is in sharp contrast to a concentrated portfolio of less than 5-10 stocks, where one would likely have to keep cutting their winners and reallocating capital to the next best winners.

That said, there are many ways one can win, but it is not how we think we are best suited to, and that's why we invest in our own way.

Diversification, not concentration allows us to let our winners really run.

19 | Focusing on the Business Fundamentals.

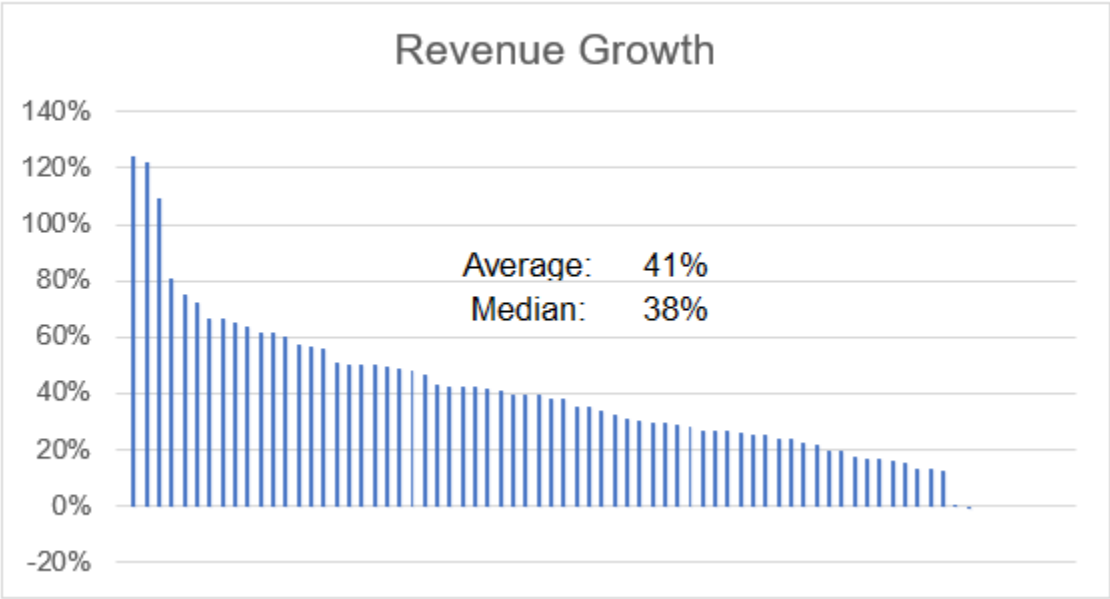
To provide a clearer picture of the core portfolio, we removed 8 outliers (total ~1.5% of portfolio) that are (1) still early stage (CRSP, EDIT, PACB, NTLA, DNMR) and (2) highly unprofitable (LMND, GH, PTON) to allow us to evaluate what the portfolio looks like.

Looking at revenues, removing COIN, the average and median (simple, not portfolio weighted) topline revenue growth is +41% and 38% respectively.

Even if we remove the top 4 fastest growers (>100%), the average and median continue to remain very high at +38% and +37% respectively.

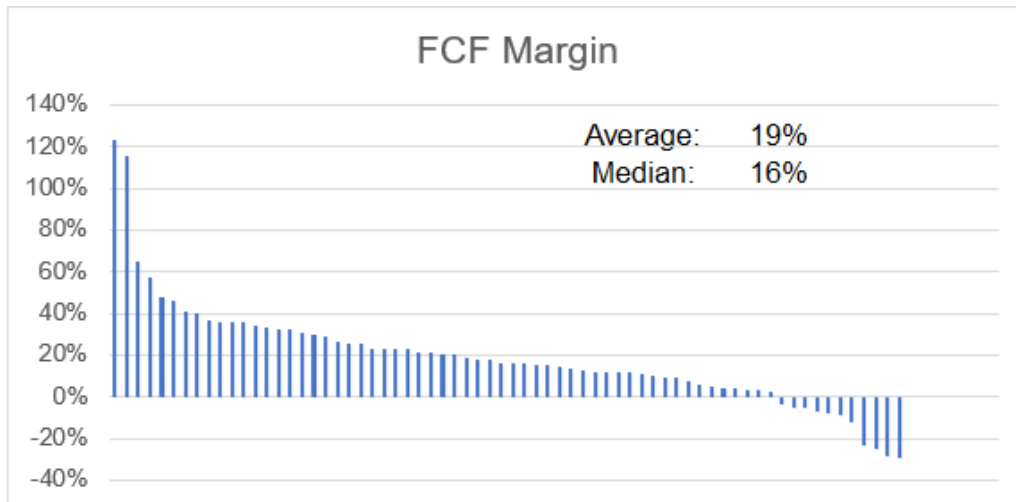
Notably, there are very few low or negative growth companies that we own, that are at least not structurally impaired for the long-term. We generally exit our positions if topline revenue growth starts to slow tremendously and persistently.

This is because profits and cash flows lead from revenues. If revenues don't grow, there will be an eventual limitation to how much profits and cash flows will keep growing. Eventually when valuation multiples fall, the stock price could well stagnate or fall with time. That's why growth is one of the margins of safety that we consider greatly.



Source: Vision Capital, as of 31 Dec 2021

Looking at **Free Cash Flows (FCF)**, we focus on owning businesses with strong unit economics, operating leverage, profitability and FCF margins that are best in class. Sometimes, FCF margins could still be negative, but we are really looking for gradual improvement over the longer-term. The average and media FCF margin for our portfolio is 19% and 16% respectively, and most are still experiencing continued FCF margin expansion. This means that FCF of our portfolio companies are growing even faster than revenues.



Source: Vision Capital, as of 31 Dec 2021

20 | Looking to the Future.

As we head into 2022, instead of looking backwards, and paddling backwards in a rowboat, instead choose to look forward, be paddling forward in a canoe, or even better choose a sailboat, to be looking forward, following the winds, and letting it take you forward even faster.

2022 is probably going to be no different from previous years, we continue to focus on what we know and do best, to find excellence, buy excellence, hold excellence, add to excellence and sell mediocrity. In doing so, investing and owning companies that best reflect our vision of the future, changing and shaping the world for the better with Vision Investing via Vision Capital.

We hope we can get more of you out there to join us too.

25 Jan 2022 | Eugene Ng | Founder & CIO | Vision Capital

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