RICHTWERT CAPITAL

Rational by Design, Fair by Choice

Partner- & Co-Investor Letter 2020/2021

"There are two times in a man's life when he should not speculate: when he can't afford it and when he can."
- Mark Twain

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PERFORMANCE OVERVIEW

	RICHTWERT (EUR) before Profit Share	RICHTWERT (EUR) after Profit Share	iShares S&P 500 (EUR)	iShares MSCI World (EUR)
2014 (Aug – Dec)	12.0%	10.3%	7.2%	4.6%
2015	-1.1%	-1.1%	0.2%	1.4%
2016	7.8%	7.4%	9.6%	7.6%
2017	11.5%	9.9%	18.8%	16.5%
2018	0.7%	0.7%	-7.7%	-9.6%
2019	59.3%	45.7%	27.0%	24.3%
2020	0.6%	0.6%	15.2%	11.5%
2021 (Jan. - May)	19.8%	16.4%	12.0%	11.1%
Compound Annual Gain	14.8%	12.3%	11.6%	9.4%
Overall Gain	156.7%	121.1%	111.4%	84.9%

	RICHTWERT (CHF) before Profit Share	RICHTWERT (CHF) after Profit Share	iShares S&P 500 (CHF)	iShares MSCI World (CHF)
2016	5.9%	5.7%	8.8%	6.8%
2017	21.3%	17.2%	18.3%	16.1%
2018	-2.7%	-2.7%	-8.4%	-10.2%
2019	55.7%	44.1%	26.7%	24.0%
2020	0.0%	0.0%	15.2%	11.5%
2021 (Jan. - May)	21.3%	17.5%	12.0%	11.0%
Compound Annual Gain	17.2%	14.1%	12.9%	10.4%
Overall Gain	136.1%	104.0%	92.7%	70.9%

	RICHTWERT (USD) before Profit Share	RICHTWERT (USD) after Profit Share	iShares S&P 500 (USD)	iShares MSCI World (USD)
2016	3.3%	3.3%	11.9%	7.8%
2017	26.5%	21.1%	21.8%	22.5%
2018	-3.7%	-3.7%	-4.4%	-8.4%
2019	57.2%	45.6%	31.4%	28.1%
2020	8.8%	8.1%	18.4%	16.1%
2021 (Jan. - May)	19.5%	16.1%	12.6%	11.7%
Compound Annual Gain	19.1%	15.7%	16.5%	13.8%
Overall Gain	157.1%	120.2%	128.1%	101.0%

Small deviations in calculations may occur due to rounding.

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RICHTWERT does not charge any fees and is only compensated based on performance:
Starting 2020: Profit Share = 25% of the annual performance exceeding an annual hurdle rate of 6%
Until 2019: Profit Share = 25% of the annual performance exceeding an annual hurdle rate of 5%

RICHTWERT EUR/CHF/USD: Performance incl. gross dividends, after costs in EUR/CHF/USD
iShares S&P 500 EUR/CHF: iShares S&P 500 EUR/CHF Hedged ETF (Acc), Performance incl. gross dividends, after costs in EUR/ CHF
iShares MSCI World EUR/CHF: iShares MSCI World EUR/CHF Hedged ETF (Acc): Performance incl. gross dividends, after costs in EUR/CHF
iShares S&P 500 (USD): iShares S&P 500 ETF, Performance incl. gross dividends, after costs in USD
iShares MSCI World (USD): iShares MSCI World ETF, Performance incl. gross dividends, after costs in USD

Dear RICHTWERT Partners and Co-Investors,

2020 was a memorable year in many ways. The coronavirus pandemic unfortunately cost millions of lives and brought large parts of the global economy to a standstill. US and global GDP fell by more than 3%, more than at any time in the last 60 years[1]. The U.S. stock index S&P 500, on the other hand, gained more than 18% in the same period, once again demonstrating short-term market forecasting to be pointless.

We also experienced some of the best as well as the worst in human potential. My realization from this was that this difference is even greater than we think and can also have a much greater impact than we admit. Our society, for instance, is seething with tensions that I am convinced will increase. Globally, we face choices with far-reaching consequences. The more we acknowledge these differences in potential and the more we recognize their sources, the better we can nurture gifted people and task them with our toughest challenges to create a brighter future for all of us. You will find my thoughts on this in the section "What Kind of Society Should We Want? Is Inequality Good or Bad?".

In last year's partner letter, I described why our portfolio companies were well positioned to withstand the pandemic. Overall, they increased their intrinsic/business value by almost 17% in US dollars (USD) and the equivalent of 7% and 6% in Euros (EUR) and Swiss Francs (CHF). Since our firms benefit from crises, I expect continued business strength in 2021 and beyond.

However, our portfolio companies' market performance was only 8.8% in USD, 0.6% in EUR and 0% in CHF in 2020. The reason for this delta was that I shifted from companies that became more highly valued to ones that were more attractively valued while market participants continued to pay little attention to the latter despite their solid business performance and standing. You have often heard me say that short-term performance needs to be taken with a grain of salt and 2020 was no different. Just in the first 5 months of this year our portfolio's market performance has gained approximately 20%. In the section "Business Performance vs. Market Performance", I provide more detail about our business and market performance, introduce you to three of our investments and reflect on the portfolio decisions I made on our behalf.

Since the outbreak of the global financial crisis in 2007-2009, governments and central banks have intervened even more than usual in the economy to mitigate the effects of crises and protect us from further ones. Their vigorous intervention has not only benefits but also significant costs and side effects such as distortions, exaggerations and risks in the capital markets. RICHTWERT's mission to *"help people invest intelligently so they can live the lives they deserve"* came about because I sensed that there would be a massive wealth transfer from savers to borrowers and investors and that the majority would eventually be forced to choose between very low returns and high risks. As you can see from the characterizations in the section "Where We Stand", risks are both widespread and significant.

Since the current situation requires an even higher level of differentiation in terms of investments, RICHTWERT's mission is even more relevant today. In the section "How We Are Positioned and What to Expect" I share how I have deployed our capital and what we can expect if I am mostly right.

As in every partner letter, I include a copy of our goals at the end so we can compare our results to our original goals.

[1] The Worldbank: https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG

What Kind of Society Should We Want? Is Inequality Good or Bad?

The massive support measures and their costs do not benefit and burden everyone equally. In a capitalist system, the more productive usually benefit from these measures at the expense of the less productive and the risk-takers at the expense of the risk averse. But the capitalists among us should not cheer too soon, because we all pay in the form of higher prices, soon also likely higher taxes and at some point, also higher interest rates - some more, others less.

I can understand that significant assistance was temporarily necessary but maintaining most of that for 12 years was selfish for the beneficiaries and irresponsible towards large sections of the population. The resulting enormous wealth transfer was unjust, and understandably has resulted in considerable tensions in our society around the world, which are repeatedly expressed in the form of populism and unrest, among other things. With the outbreak of the pandemic, governments and central banks now had no choice but to offer exceptionally strong support again, which in turn will significantly increase societal tensions.

How do we deal with the continuously growing inequality and the resulting tensions? The way we respond to these pressures has a big impact on where we end up. This is a challenge for us all and I would like to suggest three measures:

- We must teach upcoming generations more about business and economics earlier so that they can take more personal responsibility and take better care of themselves. I myself wish I had learned much of this earlier.
- We must also create intelligent long-term incentives so that decision-makers act less in their own self-interest and more for the good of society. That alone, for example, would go a long way toward ensuring that politicians support and regulate only as much as necessary and as little as possible.
- We must view and treat inequality in a differentiated way, because there are several types of inequality. Some are harmful to us, others are beneficial. For this, we need only look at the past year.

In 2020, we experienced some of the worst and best that humans can bring about. From people locking up their neighbors to protect themselves from infection to scientists discovering effective vaccines in record time. From people and governments who selfishly bought or stole vital supplies, to doctors and nurses who put their lives on the line, and companies that helped those in need even though they were not part of the pharmaceutical industry. From governments that could not even inform their citizens for months, let alone care for them, to a government that built hospitals for thousands in a matter of days. From businesses that had to close without a perspective of when or if they would be able to reopen, to companies that experienced massive growth due to the pandemic. From investors who were very short-term oriented and fearful at the beginning of the pandemic, to investors who have a time horizon of several decades toward the end of the pandemic and are suddenly investing or speculating in very risky ways.

A clear insight for me is that people generate inconceivable positive as well as negative performance. This divergence has much greater implications for all of us than we acknowledge. To ensure that adverse circumstances do not waste the potential of individuals with great potential, we must address the widespread inequality of opportunity wisely, urgently, and vigorously. Yet inequality of outcomes is both natural and necessary to our prosperity because it is often what creates the necessary incentives in the first place. This inequality has increased with technological progress and globalization and it will continue to do so.

If we aspire to quality of life and prosperity, we must not put unnecessary obstacles in the way of those who are highly capable. Instead, we should set the ground rules, entrust them with our most important challenges and reward them accordingly so that they can realize their full potential. For one thing, they will lift many with them into prosperity. For another, governments will then have the opportunity to redistribute this greater prosperity through sensible taxation to further reduce inequality of opportunity worldwide and to unleash the potential of even more highly talented people.

Let us wish for parents, teachers, leaders, politicians, and media who teach us to refrain from envy and protectionism and instead guide us to be more curious, imaginative, experimental, open-minded, tolerant, ambitious and more self-reliant.

Business Performance vs. Market Performance

In last year's partner letter, I described why our portfolio companies are well equipped to withstand the Corona crisis and even profit from it. But the true test failed to materialize, because the U.S. Fed intervened very forcefully early on and, in addition to rock-bottom interest rates, virtually guaranteed almost all corporate liabilities. This proved hugely effective because it reduced the risk for market participants immensely from one day to the next, thus opening the floodgates of the capital market. Further, most governments stepped in supportively so that the worst economic effects of the Corona crisis did not materialize.

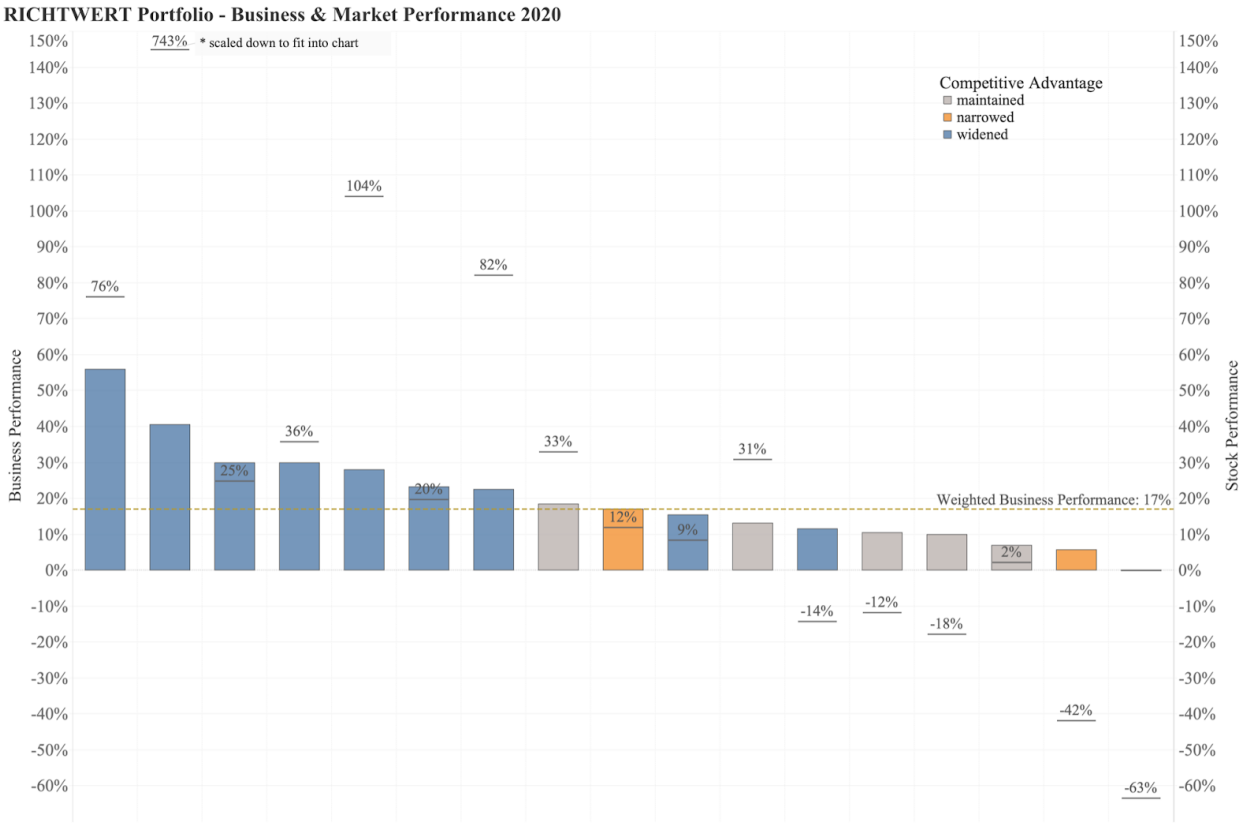
We at RICHTWERT also benefited from this in the short-term, but in the mid- and long-term it cost us for the time being, as our companies were unable to fully exploit their competitive advantages. However, we need not despair because anything that cannot go on forever will end. The opportunity for our companies will then possibly be all the greater.[2]

Overall, our companies increased their intrinsic/operating value by almost 17% in USD and 6% and 7% in CHF and EUR, respectively. At RICHTWERT I only follow one strategy, so all portfolios are nearly equally invested. The difference stems from the fact that we were heavily invested in US companies while the dollar came under pressure last year. Due to the cost of hedging and the fact that most of our businesses operate internationally and thereby offer a natural currency hedge in the mid-term, I usually do not hedge currencies. In the short-term, our performance tends to fluctuate a bit more as a result, but this need not worry us as long-term investors in productive businesses in a globally interconnected economy.

The following chart shows the business and the market performance of our portfolio companies for the year 2020 independent of purchases and sales on my part. In addition, the colors of the bars show whether our firms were able to defend or extend their competitive advantages, which is necessary for long-term value creation.

- In terms of business performance, those of our companies that provide e-commerce, cloud services, online gaming, and digital exchange between people and businesses, as well as Tesla, topped the list. They were followed by our investment and media businesses. As expected, our other financial services providers, which mainly provide credit/leasing, achieved the lowest increase in value in this environment. It was pleasing to observe that almost all our firms were able to increase their value even in the year of the pandemic. Since our businesses benefit from crises, I expect them to perform better in the coming years relative to what they would have done in the absence of the pandemic.
- Even more encouraging was that, on a weighted basis, just about half of our portfolio was able to extend its competitive advantages, about 40% of the portfolio was able to defend them, and only 11% lost competitive advantages. By the way, my assessment is strict because I expect especially our strongest companies to expand their competitive advantages not only against the broad set of competition but also against their direct competition. Alphabet and Facebook, for example, undoubtedly made gains against traditional media companies last year, but the comparison with other Internet platforms is more challenging.
- As important as increasing business value is, it is only one side of the coin; the other is the price we pay for it. When it comes to investing, the key is to invest in those assets that will increase their value the most relative to their price. As you can also see from the chart, our firms' stock performances ranged from -63% to +743%! It was therefore once again not a year for the faint-hearted! With this range of performance, some firms potentially become very cheap, and others may no longer be attractively valued. Hence, I decided to sell/reduce some of our investments and deliberately invested also in companies that grew more slowly in the short-term because in these cases the relationship between value and price was very favorable.

[2] That is, of course, the investing view. The social view may be different, but I doubt it. In the medium and long term, we will not be doing ourselves any favors by rescuing everyone, including companies, that no longer have viable business models and stakeholders who have acted irresponsibly.



Compared to their business performance, our portfolio´s market performance was meager last year (8.8% in USD, 0.6% in EUR and 0% in CHF). RICHTWERT partners & co-investors know from experience that such discrepancies have usually offered attractive opportunities. Indeed, our portfolio has achieved a price gain of roughly 20% between January and May 2021.

RICHTWERT Portfolio	USD	EUR	CHF
Business Performance	17%	7%	6%
Market Performance	8.8%	0.6%	0%

The main driver for last year´s delta between business and market performance was that I reduced or sold our investments in companies that I considered less attractive due to increased prices and invested the proceeds in businesses that in my view offered a better margin of safety as well as better profit potential. This included significantly increasing our already heavyweight investment in Grenke, which faced five simultaneous challenges in 2020. It also involved increasing our midsize investment in Wells Fargo. I considered both companies to be massively undervalued during 2020. The increase in Wells Fargo has already paid off and I strongly expect that we will also earn a lot from Grenke in due course - more details on Grenke in the next section.

Insights into three of our portfolio companies (Grenke, Discovery, Credit Acceptance)

In my letters to you, I provide insights about some of our investments so that

- you can better assess what you actually own;
- you can judge in a few years whether our performance was the result of luck or skill; and
- you can learn more about investing from my mistakes and successes if you wish.

In view of current circumstances, I will report on Grenke first. Then I will introduce Discovery, one of our media companies, to you before explaining why I sold our investment in Credit Acceptance. Finally, I reflect on my other portfolio decisions.

Grenke

Grenke is a specialized international provider of financial services for small and medium-sized enterprises. It generates the lion's share of its business by leasing companies all sorts of equipment they need. In addition, Grenke offers banking and factoring.

As a leasing provider, Grenke was affected firstly by increased defaults and delays in payment by customers due to the pandemic. Second, demand for leasing decreased because most firms refrained from investing for the time being. Third, Grenke was attacked by a well-known short seller and massively accused of having deceived and misled investors. The fact that this short seller had recently exposed Wirecard as a fraud had a strong effect and frightened most investors. As a result, Grenke had to undergo a thorough audit by three auditing companies at the same time to counter the allegations. This not only caused considerable additional costs but also inevitably diverted attention from the company's business activities during an economically delicate phase. It was thus the perfect storm!

In short, I considered and still consider most of the short seller's accusations to be nonsensical and, in part, negligent or fabricated. As the combined challenges caused Grenke's share price to fall far below its mid- and long-term value in a very short period, I took the favorable opportunity to significantly increase our investment in Grenke. The following is the detailed version for those who would like to learn more.

Crises are always part of investing. They can rarely be predicted, but you can certainly prepare for them. I invest in companies like Grenke, not least because they are well prepared for crises and because they profit from them. Grenke's business model is highly profitable because automation and economies of scale allow Grenke to offer leases that are unprofitable for competitors, and because Grenke can reliably predict the default probability of its receivables. Grenke can cope well with higher temporary default rates, firstly thanks to its high profitability and secondly because the company can be more selective in difficult times. In addition, Grenke is very solidly financed and broadly diversified both geographically and in terms of customers. Moreover, this is not the first crisis that Grenke has mastered, and unlike other crises, this time governments assured corporate aid from the beginning, which will indirectly benefit Grenke.

But what about the allegations?

Before I go into these, it is important to understand what short sellers do. Short sellers bet on falling prices and borrow securities, which they sell at the current market price, hoping to buy them back later at lower prices. I never understood why intelligent, experienced, and honest investors sell securities short because unlike ordinary investing, the potential for profit is limited (a security usually cannot be worth less than zero) and the potential for loss is unlimited.

Thanks to this short seller attack, I now suspect that there are hardly any short sellers who are intelligent, experienced *and* honest. While I think short-selling can help keep managers honest and capital markets efficient, in practice short-selling is also abused to secure short-term profits by spreading panic, whether the accusations are justified or not. There is currently a significant, harmful gray area here that regulators should eliminate to protect firms and investors. But now to the allegations:

The short seller made the following allegations and wrote a 64-page analysis of his accusations:

1. *Grenke's profits, balance sheet values (receivables) as well as cash are faked because the products Grenke leases (e.g. printers and copiers) have become obsolete and it cannot be that Grenke generates that much growth with these products. In addition, Grenke balances overpriced values of about 7500 Euro on average per printer or copier. The fact that Grenke is constantly raising expensive debt and equity capital, even though the company appears to have excess capital, is further evidence of the deception.*
2. *Grenke seriously neglects governance issues and defrauds investors by buying unattractive franchise companies owned by Grenke insiders at inflated prices for at least a decade, thus enriching insiders or people close to them at the expense of shareholders.*
3. *Grenke is an accomplice in fraudulent transactions in which dealers rip off customers with overpriced leases.*
4. *Grenke is negligent with internal controls at Grenke Bank, accepting customers who were blacklisted by BaFin and thus aiding and abetting money laundering.*

After studying the short seller's analysis, I concluded that he was bending the facts and probably jumping to conclusions either negligently or maliciously based on potential fraud patterns only. Subsequently, Grenke also responded with press releases and an investor conference where they denied all allegations. On September 21, 2020, I shared my following assessment with RICHTWERT partners/customers:

Regarding the 1st accusation:

- Grenke reported that the cash in question in fact exists and that 80% of it was deposited with the German Bundesbank.
- Moreover, according to my analysis, Grenke has always been prudent and had consistently insisted on above-average equity capital to cope with planned expansions and to withstand potential crises. The company also demonstrated this during the global financial crisis between 2007-2009. In 2019, Grenke raised further equity to prepare for its planned expansion into the USA. Furthermore, at the beginning of 2020, Grenke Bank created incentives for private customers to secure funds in the form of bank deposits to be better prepared for the Corona crisis.
- Both the equity and debt capital raises were always on attractive terms from the perspective of existing investors and made a well-thought-out impression. As far as I could see, there was no sign of expensive loans or any detrimental dilution of shareholders. Grenke's capital raises always made sense and were advantageous in the context of the leasing business and its expansion goals.
- As for printers and copiers, the short seller either negligently or maliciously mixed facts from 2010 and 2019 to support his point. He also seems to have *overlooked* the fact that a lease can often include multiple printers and copiers. The percentage of leases with these items decreased from 31% to 18% during this time, and I believe the absolute growth is due to Grenke's regional expansion and market share gains.

Regarding the second accusation:

- Grenke encouraged former Grenke managers to found franchise companies abroad with the aim of buying them in 4-6 years at predefined valuation criteria, provided they proved to be promising. In the last 12 years, Grenke paid about 100 million euros for acquired franchise companies. Today, these companies generate approx. 20% of Grenk's new business and achieve a total annual contribution margin that corresponds to the entire purchase price. To speak of overpriced purchases here requires a certain level of inexperience, imagination, or audacity.
- It is probably correct that company founder Wolfgang Grenke, his family and persons close to him could have been advantaged by purchases of these franchise companies by Grenke AG, but as described next, I still think that there was no fraud here. After all, a potential conflict of interest is not necessarily proof of fraud.
- In the last 10 years, Grenke generated nearly 800 million euros of profit. Towards the end of 2019, Grenke had a market capitalization of almost 5 billion euros. More than 40% of Grenke AG is owned by the family of founder and longtime CEO Wolfgang Grenke. It makes little sense to enrich oneself over 10 years at a purchase price of about 100 million euros in the company, in which one owns 40% of the shares worth almost 2 billion euros. This would only make sense if the company was actually a fraud and in reality, was not worth nearly as much. But then one would rather sell one's own overpriced shares instead of holding on to them long-term, as the Grenke family does.
- Finally, I once had the opportunity to meet Mr. Grenke personally and ask him questions. He made a very friendly and down-to-earth impression on me, spoke passionately about the company he has founded and has run for decades, and was intimately familiar with its success factors.

Regarding the third accusation:

- I believe black sheep in a partner/dealer network can never be completely ruled out. This is all the more true the more products are involved and the more partners are supported. The business with questionable partners among Grenke's dealer partners accounted for significantly less than 1% of the total leasing volume. Grenke has excluded them from the dealer network and introduced processes to identify them earlier. Even if someone at Grenke had deliberately looked the other way, one can certainly not assume systematic fraud.

Regarding the fourth accusation:

- Grenke also contradicted the accusation of money laundering. The short seller named three bank customers who were on the BaFin blacklist. Two of these had not been accepted by Grenke as customers and one customer was found to have suspicious transactions that led to the customer being terminated before the customer was on the BaFin blacklist.

In the meantime, the three auditing companies have submitted interim reports to Grenke which, taken together, firstly provided evidence of the cash and the recoverability of the receivables, secondly confirmed the advantageousness of the franchise company

purchases overall, thirdly could not identify any systematic fraud on the part of Grenke with regard to overpriced leasing contracts and fourthly could not identify any aiding and abetting of money laundering.

In addition to these exonerating results, there were also objections of procedural nature, which, in my view, are by no means surprising when three auditing companies under pressure from the press, politics and the public meticulously take apart the history of a company. Grenke, meanwhile, has already taken significant steps to rectify these complaints and to be in an even better position in the future.

Finally, I am not surprised that Grenke successfully and profitably completed 2020 despite these enormous and simultaneous burdens. But it gets even better, because the auditing company found that Grenke had accounted too conservatively, so that profits were ultimately 10% higher than Grenke had reported. Now that is a correction to my taste!

In investing, there are never 100% certainties. Every analysis, no matter how thorough, can turn out to be wrong and fraudsters find amazing ways to deceive you. My analysis of Grenke can still turn out to be wrong. Still, it never ceases to amaze me how little investors investigate companies they invest in. In the case of Grenke, the accusation of a single, admittedly well-known, short seller was enough to cast doubt on Grenke's more than 40-year track record and cause the share price to collapse. Not only is the short seller's history much shorter than Grenke's, the short seller has been wrong several times with his accusations. Anyone who had looked into Grenke and taken the trouble to study the short seller's analysis would have found that it does not take Grenke's business model into account at all and, moreover, probably contains negligent or possibly intentional analysis errors.

Because I am personally invested with all my liquid net worth as a RICHTWERT partner/client just like you are, I know how difficult it is to remain calm and objective when the headlines shout *fire* and cause rapid share price declines. Of course, it is even more challenging for you because you usually know the portfolio companies less well. Therefore, I greatly appreciate the trust you place in me. This is anything but self-evident and motivates me even more to earn your trust. I hope I could bring some perspective to the headline-ridden situation of Grenke.

Discovery - An Overlooked Pearl in the Media Industry

Can I understand Discovery?
Discovery is a leading global media company focused on lifestyle entertainment as well as hobbies and documentaries. When I decided to invest in Discovery for us, it offered its content primarily through traditional ad-supported TV and pay TV channels. Its target audience is broadly diversified geographically and demographically. The company's business model is based partly on fees paid by network operators for broadcasting its content and partly on advertising revenues. Discovery has many local and global competitors, who compete for viewers' favor with either the same or different types of content and media, depending on the region.

Does Discovery have an attractive medium- and long-term future?
I find the entertainment industry attractive because we all seek entertainment besides family, work and hobbies and pay for it directly or indirectly via advertising. The industry benefits from economies of scale as content created can be broadcast globally, repeatedly, and efficiently with adaptations. In a world where demand for products and services is lower than their supply, manufacturers and suppliers are increasingly seeking the attention of their target audiences and are willing to invest heavily for targeted advertising.

Discovery creates customer-segment-specific programs that enjoy great popularity and thus have a loyal audience. It not only owns the global rights for almost all its content but also has this content in many languages. In addition, it benefits from the fact that its content rarely requires expensive actors, licensing rights or blockbusters, but is geared to our daily lives, interests, and hobbies. This differentiates Discovery from the competition in terms of content on the one hand and production costs and time-to-market on the other. For distributors and advertisers this content is inexpensive relative to the market share it demands and therefore offers Discovery attractive pricing power.

Discovery has already had valuable early experience distributing its content via apps and has the potential to bring its popular content to its target audience either via partners or through its own streaming service. While streaming content requires significant investment, it also offers great benefits. Discovery, for example, has a very large library of content that has not been effectively broadcast or consumed thus far. In addition, low pay TV penetration in many countries limits its addressable market. Furthermore, traditional media as well as indirect customer access via partners hinder direct customer feedback, which is essential for both content and advertising effectiveness.

Is Discovery's management trustworthy, competent, and motivated?

Discovery has two dominant and long-term control owners and a very experienced and established management team that has been working together in key positions for 10-14 years. Their long-term track record of content creation, licensing, geographic expansion, corporate profitability, and capital allocation with respect to acquisitions and share repurchases is impressive.

They maintain open and detailed communication with shareholders and have a history of communicating challenges, opportunities, and competitive advantages as well as goals transparently. They also have a track record of achieving their goals.

Can we become a shareholder in Discovery at an attractive price?

The fact that this is our third time investing in this company may surprise you. At the same time, it will explain why I use more discretion with some of our portfolio companies.

When we first invested, market participants thought Discovery was on the decline in the traditional TV world and was also making bad strategic decisions. I completely disagreed and saw an opportunity to acquire shares in an attractive business with competitive advantages and continuous profit growth at a very attractive price. Since the share price recovered quickly at that time and we had other opportunities, I initially sold our shares.

After about a year, Discovery demonstrated that their strategic choices were even better than they or I had thought. Moreover, Discovery was determined to enter streaming through partners or on its own. Appreciating the competitive advantages, I found even the increased stock price attractive and invested for a second time. What I did not anticipate was that we were on the verge of a pandemic that would shut down large parts of the world.

As the Corona virus subsequently spread, Discovery consistently used its competitive advantages to gain market share and simultaneously advanced its streaming strategy, but the stock price still fell sharply. The time was ripe to act opportunistically like a true business owner. Encouraged, I stocked up at ever lower prices. I still remember the walks I made to reflect on my analysis of the company to make sure I was not making mistakes or overlooking anything. What was also interesting was the length of time the stock remained at such low price levels while the rest of the stocks recovered strongly from the pandemic scare. From my perspective, the company was doing everything right! As is often the case, I did not understand what investors were thinking, but I did not let myself be swayed.

When the stock started to soar, I remained patient because I believed the company was significantly undervalued. After the share price doubled and tripled, I began to gradually sell our investment because we had more attractive opportunities.

Meanwhile, the share price suddenly plummeted more than 50% in a matter of days. Some say what goes up must come down, but there are real businesses behind stocks. Therefore, I used now the third opportunity to increase our investment at once again attractive prices. Later it turned out that a hedge fund with a lot of borrowed capital had bet on some companies including Discovery and due to losses on another stock, could not meet its obligations. Lenders were therefore forced to liquidate its shares with haste. Although I did not know this at the time of our purchases, I was glad to have helped them in the case of Discovery!

Recently, Discovery announced its intention to merge with Time Warner to better advance their strategy with combined forces. I consider Discovery to be more differentiated and attractive on their own, but considering the past performance of their management, I am happy to give them the benefit of the doubt and be proven wrong.

This example shows how important it is to differentiate between companies and their stocks. During the time that Discovery's stock was going through several steep ups and downs, the company was steadily moving forward with discipline to a brighter future. I am delighted to participate in the success of our companies as long-term investors. In addition, I am happy to potentially use exaggerations in both directions to our advantage as with Discovery.

As described in our Partner's RICHTWERT Partner & Co-Investor Letter, we do not need to be unethical to achieve attractive returns. A requirement for all our investments that is motivated both ethically as well as business-wise is that our companies must benefit society on balance.

Now, the conventional wisdom regarding some of our businesses is that they do not benefit society. But I am not interested in conventional wisdom, because it is often simply wrong. I care about being right and I am proud of our companies. However, whenever I come to a negative assessment myself, as was the case with Credit Acceptance, I act accordingly.

Credit Acceptance

Credit Acceptance finances used cars in the USA for people who are not considered creditworthy and cannot otherwise obtain credit. In the process the company makes car dealers participate in the credit risk. To do this, it holds back part of the purchase price and only pays it out to dealers once customers have repaid their loans.

I thought the business model was a win-win situation for all parties involved: In the USA, public transportation is not an option outside large inner cities and the population relies on private vehicles.

1. Individuals who need a car but cannot otherwise obtain credit are more likely to be able to afford a car through a Credit Acceptance loan and have a chance to improve their credit score by meeting their obligations.
2. Auto dealers are more likely to be able to sell their used vehicles through a loan that only Credit Acceptance makes possible, and because they participate in the credit risk, they are more motivated to sell a vehicle that a) works and gets the customer to work and that b) the buyer is more likely to be able to afford.
3. Credit Acceptance can make profitable loans to people who cannot be profitably serviced by other lenders.

The firm has often been accused of causing damage, but I thought these accusations were unfounded, as it is unavoidable with such a business model that many customers are dissatisfied. After all, who likes to lose their car, even if it is their own fault? Of course, dissatisfaction increases in difficult economic times like in 2020. In my eyes, the company gave borrowers a second chance, while charging much higher interest rates due to the much riskier loans.

After studying a lawsuit, I changed my mind and sold our investment. I now understand that the company is truly giving everyone a second chance, even though it knows this will hurt a substantial number of them. All in all, Credit Acceptance earns so well on its loans that the benefits of more loans outweigh the advantage of more selective loans.

Thus, the only party with an incentive to offer a beneficial deal to all parties is the dealer because of the prospect of earning the holdback. But dealers raise prices on vehicles to compensate for the risk of missing out on the holdback. Thus, it appears to me that the superficially very good incentive to make the car dealer participate in the risk is in fact often a misaligned incentive that penalizes those with the weakest financial means. I believe that this fact has not escaped Credit Acceptance´s attention.

On top of that, most car dealers convince buyers to accept an expensive optional service contract that they and Credit Acceptance earns handsomely from, while Credit Acceptance readily tolerates the very high acceptance rate of optional service contracts at most dealers. Legally, this is likely a gray area, but given the high prices and the dire financial situation of some customers, it amounts to exploitation.

My conclusion is that Credit Acceptance has an even much better business model than I first thought. But the way the company conducts its business does more harm than it generates value for a significant portion of its customers. The company is adept at predicting who is most likely to default on loans and could at least refuse credit to the most financially vulnerable customers, when the loan goes hand in hand with dealer markups and high acceptance rates on expensive service contracts. It could even find ways to accommodate some customers and make profits at the same time. The fact that most borrowers with the lowest credit scores end up in an even worse situation does not fit with the self-image of a purpose-driven company. The analogy I would rather make is that of a surgeon who also performs surgeries out of self-interest, even though he knows that they do more harm than good to some patients.

True to Richard Feynman's motto, *"The first principle is that you must not fool yourself - and you are the easiest person to fool."* I believe Credit Acceptance's management is making themselves believe that they are doing the right thing by giving everyone a second chance. The sad truth is that a second chance is not in the best interest of many Credit Acceptance customers.

Further Portfolio Decisions - I Should Have Spent More Time with Family and at Lake Zurich

I began last year's partner letter with the motto: *"To be exceptionally successful in investing you must have the humility to know you could be wrong, the vision to see the opportunities nevertheless, the courage to invest in them with conviction and the patience to hold*

them.”. It was a good thing, too, because if I had not put those thoughts on paper, I would have sold some of our investments way too early. With the benefit of hindsight, however, I should have been more precise: *"... and have the patience to hold great companies, even if they stumble or seem expensive or you think you have found better investment opportunities."*

Let us just say, I would have done us all a big favor if I had devoted myself exclusively to my family and Lake Zurich last year because my shifts from Alphabet, Amazon, Apple, and Tesla into Grenke, Alibaba, and two other companies I will not name yet cost us a lot last year. As you can see from the table below, the companies I sold/reduced in our portfolio performed very well business-wise and phenomenally well market-wise in 2020. I did wait with reallocations until I was pretty sure that firstly we were getting a fair price for our companies and that secondly, we had better alternatives, but even after my sales these stocks performed excellently.

That's how well the stocks I sold or reduced in 2020 performed	
Business Performance Range	13% - 56%
Market Performance Range	31% - 743%
Market Performance Range compared to our average selling prices	7% - 426%

Selling Amazon taught me a lesson. I sold Amazon because, in my view, the company was letting its very large competitive advantage in the form of customer reviews slip, and because Amazon's market valuation reached a level where I thought Alibaba was half the price. In addition, I thought Alibaba's business model was further along than Amazon's. What was not to like about the exchange? What I obviously overlooked was that Alibaba's competition in China was also further along than Amazon's. Hence, Amazon has been able to grow much faster than Alibaba since I replaced it. Alibaba’s slower growth was also caused in part by its founder who overconfidently antagonized with China's regulator. Regulatory action was to be expected sooner or later anyway, but his confrontation made it arrive sooner.

In my defense, I want to point out that what happens is always only one scenario among many possible ones. In investing the rearview mirror is always much clearer than the windshield:

- Tesla, for example, was financially on shaky ground when the pandemic started and could have come under severe pressure not for the first time. Apart from that, Tesla's market valuation has contained a lot of euphoria and fantasy for the past year. Even Elon Musk, company founder and mastermind of Tesla, wrote shortly after I sold Tesla for us that Tesla was overvalued and repeated his statement regularly without being heard. As far as I can influence it, I never want us to be dependent on the (speculative) goodwill of market participants for our investments.
- Apple's market valuation had already risen significantly and, together with Apple's enormous size, clouded future expected returns. But Apple's very strong business performance surprised even me, although I have long been convinced of Apple's competitive advantages.

It is also crucial to distinguish between the short- and the mid- to long-term. Investing is not a sprint but rather a marathon:

- Just because last year's decisions were detrimental does not necessarily mean they were wrong.
- Holding on to companies that you think are overvalued is speculation and therefore wrong.
- Furthermore, I think very highly of our current investments. They do not need to hide behind the companies we sold, and I also think they are more attractive in terms of price.
- I also emphasize that some of our investments are unlikely to perform as well in the short-term as related alternatives that I am aware of. Nevertheless, I am deliberately choosing these disadvantaged securities in the short-term because I believe that these handicaps will be eliminated over time, giving us the prospect of even better performance at lower risk.

I look forward to reporting on their development in the coming years. Grenke, by the way, has already made a start in this respect.

Where We Stand

Since the global financial crisis 13 years ago, central banks and investors have kept interest rates very low, allowing governments and companies to take on significant debt, giving the economy an additional boost. Many countries and businesses thus spent large amounts of money that they have not yet collected or earned.

Because of these distortions, resources have been deployed ineffectively. For example, we are left with many non competitive firms that tie up financial and human capital and hold us back. We also gave away much of our dry powder for unforeseen times like the current pandemic. Now that the pandemic is here, we have no choice but to continue to keep interest rates very low and to continue to take on massive amounts of debt.

In the past you had to fear getting too close to the cliff. But governments and central banks have bailed out almost everyone. Since we have used up most of our dry powder and have taught the masses that personal responsibility and prudence are unnecessary, we should not be surprised when a future crash becomes all the more devastating.

Far-sighted leadership looks different! In contrast to the strongly one-sided criticism of China, we in the West should take more than a slice of their foresighted stewardship. They are more likely to recognize risks early and intervene proactively for the good of the majority. Meanwhile, there are plenty of excesses in the West that require attention and intervention.

Excesses

- Long-term government bonds with a maturity of 10-30 years have yields so low that they can only generate losses either before or after inflation.
- Many states and companies have accumulated mountains of debt that can only be serviced if interest rates remain low.
- After decades of falling interest rates and years of declining taxes in some countries, interest rates could rise due to rising inflation and taxes could rise due to significantly higher government debt.
- Investors have increasingly turned from safe, short-term government bonds at low inflation to risky, longer-term bonds with possibly higher inflation, from attractively valued real estate and stocks to expensive real estate and stocks, and from productive assets like real estate and stocks to speculation in gold and cryptocurrencies.
    - The price of the cryptocurrency "Dogecoin"[3] created as a parody to mock cryptocurrency madness, increased nearly 300-fold in the last 12 months - so much for justifying cryptocurrency valuations based on inflation....
    - Governments of Western countries and their central banks know that they cannot allow non-government cryptocurrencies to be accepted as a means of payment, but are reluctant to communicate this to market participants, putting many market participants at risk of potentially losing a lot of money.
    - I highly recommend these videos on cryptocurrencies[4,5]. At the very least, they are honest and amusing but I think they are also insightful (more on this in the section "Investing vs. Speculating").
    - There are even *independent Bitcoin advisors* today touting Bitcoin vending machines charging 12% in fees[6].
- Numerous IPOs rose more than 50% on the first day of trading above the price that informed insider sellers like the company founders apparently thought was appropriate.
- SPACs, corporate shells, also referred to as "blank checks", promising to buy up private companies within about two years to take them public with less regulatory oversight, raised more than $40 billion within the first 6 weeks of 2021[7]. This was sometimes accomplished with the help of celebrities. In this context, I cannot help but think of the celebrities who idolized WeWork, a company that, among other things, wanted to promote a dorm-like lifestyle to working professionals. Furthermore, I find it ironic that WeWork, after a failed IPO attempt, now wants to go public itself via a SPAC[8].
- Not only Corona spread exponentially, but also the share prices of so-called "disruptor" firms, which compete against existing companies with new technologies and business models. Many investors today, for example, are willing to pay prices for the sales

[3] "Dogecoin's Founder Bewildered at Cryptocurrency's Sudden Popularity", WSJ, Ostroff C. (2021): https://on.wsj.com/33btLoF, Yahoo!: https://yhoo.it/2RjPBn2
[4] "The Rise of Bitcoin and Other Stupid Meme Currencies", https://bit.ly/3oFLHlj
[5] "I Am Now the Baron of Bitcoin Featuring The Winklevoss Twins", https://bit.ly/3hOK4QS
[6] Vending machine for Bitcoin giftcards: https://bit.ly/3ueWapB
[7] "OK, What's a SPAC?", New York Times, Kurutz, S. (2021): https://nyti.ms/3ta9aM4
[8] "After failed I.P.O., WeWork will go public through a merger", New York Times, Eavis, P., & Hirsch, L. (2021): https://nyti.ms/3nNradZ

of such companies that I would rarely, and only after ample analysis, pay for their profits. In the process, today's investors overlook the fact that the companies currently under pressure were also once considered disruptors.

- *Thanks* to new apps, even novices can speculate with fractional shares or cryptocurrencies in a matter of seconds[9]. I cannot stand inefficiencies, but it doesn't take a degree in financial market theory to sense that too little friction in investing can also be very dangerous. The fact that many inexperienced investors are less engaged in otherwise normal activities because of the pandemic and may have a little more money left over, coupled with capital markets that have been rising for 12 years, makes for additional risk.
- And so, I am not surprised that people in my own circles, who until now did not touch stocks with a yardstick, suddenly want to bet on individual stocks or the stock market and *"just give it a try"*.
- The attitude toward risk taking is also reflected in the language used. Too many market participants today talk about *"betting"*. I remember very well 2009 and 2010 after the global financial crisis when I (unsuccessfully) tried to get investors interested in stocks because stock prices were very cheap. I can assure you: nobody was talking about "betting" on stocks back then.
- Today's so brave and young market participants claim, for example, that they will use drops in share prices to stock up, but only if the market correction is less than 10%[10].
- I also find it frightening that some so-called quant "investors", including even trained financial analysts, proudly announce that they know neither the names nor the activities of the businesses in which they invest for their clients.

After reading these risks you will surely be asking how we can still be fully invested at RICHTWERT. The answer is that there are also many opportunities at the same time. We are still at the beginning of the technological revolution and globalization and the world is still so incredibly inefficient. In addition, as already explained many do not invest but speculate on hot trends and thus underestimate attractive businesses that I value greatly.

Investing vs. Speculating

"There are two times in a man's life when he should not speculate: when he cannot afford to, and when he can." - Mark Twain

Many think there is no difference between investing and speculating in the stock market. Even more do not know when they are investing and when they are speculating. Yet the distinction is essential.

Borrowing from what Benjamin Graham wrote about 90 years ago, I would define an investment this way: An investment is an activity in which, after thorough analysis, one can expect with a high degree of probability that one will get back the capital invested together with an adequate profit. You can only *know* that if you can estimate and value the returns that an asset will produce, and if the value of those returns provides a sufficient margin of safety over the price you pay for the investment. Activities that do not meet these requirements are speculation.

If you examine the above excesses by this definition, you will find that almost all of them constitute speculation because the assets in question either produce no returns at all (e.g., gold and cryptocurrencies) or the returns can hardly be estimated (e.g., SPACs and IPOs) or the value of the returns does not represent a sufficient margin of safety relative to the price (e.g., expensive bonds, real estate, and stocks, as well as SPACs and IPOs). Market participants are speculating here because they are only or primarily concerned with prices and hope for buyers who will pay even higher prices but investing, they are not!

Care for an example?
How much is one Bitcoin *worth*? $1, $10, $100, $1000, $1 million, $1 billion, $1 trillion, ... or maybe nothing at all?

[9] Can an app be too efficient? https://youtu.be/rfrnD7SRjog?t=245
[10] "Retail traders say they're not going anywhere", Yahoo! Finance, Myles Udland, February 26, 2021: https://yhoo.it/2RM6De6

How We Are Positioned and What to Expect

At RICHTWERT, I always try to heed this wisdom from Warren Buffett: *"The less prudence with which others conduct their affairs, the greater the prudence with which we should conduct our own affairs."*

First, this means that I steer us clear of obvious speculation such as the aforementioned excesses. Second, it means that while I worry top-down, I always invest bottom-up by focusing on the individual businesses we invest in and allowing this business rationality to outweigh top-down worries if and when the businesses we can invest in are sufficiently attractive.

Experience also shows that the biggest losses do not occur from paying somewhat too much for high quality assets, but rather from buying low quality assets during booming times. The extraordinary measures taken by governments and central banks have stimulated the economy markedly. They have also obscured the differences in quality hence making most things appear attractive.

How can we separate the wheat from the chaff and limit our investments to qualitative assets? The more complex the world, the more important it is to get back to basics. At its core investing is about deploying capital as reliably and as productively as possible. And as we live in an ever faster-changing world, it's even more important that I think about the end game for our businesses. The key questions I ask myself are:

- Which products and services do we need today as well as 5, 10 and 20 years from now?
- Who will have lasting competitive advantages as well as the necessary adaptability to emerge as a winner?
- Which companies have management today and in the future that will not only win, but also act in the interest of owners?
- Can we become co-owners of these companies at a price that protects us as much as possible in the event of failure and rewards us handsomely in the event of success?

I have great respect for these questions and know that I only stand a chance if I think and act like a true business owner. To me this means thinking long-term, limiting myself to my core competencies as well as being disciplined and opportunistic when the risk-to-reward ratio is significantly in our favor.

Usually, investment managers present charts at this point showing the industry and country allocation of their portfolio. I doubt this will do you any good, as industry definitions are too rudimentary, and companies today often cover numerous regional markets. Instead, I currently characterize our portfolio as follows:

- We are currently invested in 12 companies, four of which make up about 70% of our portfolio.
- At least 45% of our portfolio provides financing, investment, and payment services.
  - These are services that have been around for centuries and will likely be around for at least another hundred years.
  - Equally important, I believe, to know what is essential for most of these services and who is likely to possess enduring competitive advantages.
- In addition, our companies are either leaders or among the leaders in the following areas:
  - Internet platforms, communications, augmented & virtual reality
  - Media, advertising, entertainment & gaming
  - IT Infrastructure & Cloud Services
  - (E-)Commerce
  - Renewable Energy, Infrastructure & Real Estate
  - Food
  - Logistics
  - Education
- The pandemic caused an acceleration in demand for 70% of our portfolio that will benefit our companies for years to come.
- For the first time since RICHTWERT was founded, we are no longer majority invested in American companies. This has no macro background, because except for Credit Acceptance, I have been very reluctant to sell or downsize our American companies. It is just that I have found more attractive investments in Europe and Asia than before.
- What unites almost all our businesses are exceptional financial strength; significant competitive advantages such as a strong corporate culture, dominant brands, solid pricing power/protection against inflation, significant economies of scale, low capital intensity and low marginal costs; proven, energetic, long-term oriented and shareholder-friendly management with broadly supported young talent; and their undervaluation.

Thanks to these strengths, our companies are not only prepared for crises, but also beneficiaries of them. We are therefore in the luxurious situation of being able to leave the speculation surrounding macro and market developments, which no one can reliably predict, to others and focus all the more on the factors that matter long-term.

As you can see from the operating areas of our companies, we are more than sufficiently diversified despite the high portfolio concentration. The biggest potential risks to our portfolio are technological disruption and significantly rising, widespread inflation, along with much higher interest rates. What gives me some comfort is that I do not currently know how we could protect ourselves better against such risks than with our companies.

The usual recommendation to bet on commodity or energy companies and so-called "value stocks" when inflation is imminent and interest rates are possibly rising is, in my view, unwise or even wrong, since these macro-based decisions result in market timing and usually involve investing in companies that are less attractive in the medium and long term. So called "value stocks" usually refer to capital-intensive companies that in fact suffer as inflation rises.

With one deliberate exception, our companies are financially very well positioned and have good pricing power or benefit to some extent from rising inflation and higher interest rates due to their business models.
Almost all other assets including cash are more at risk from these risks than our businesses and I hope I was able to adequately warn about the dangers of speculating in gold, cryptocurrencies and other unproductive assets in the sections "Where We Stand" and "Investing vs. Speculating".

If our businesses deliver what I expect, they will perform operationally similar to the last three years (2018: +16%, 2019: +19%, 2020: +17%). Since I believe they are undervalued, their shares could do even better. Consequently, even with rising inflation and interest rates, they would probably achieve satisfactory results. We cannot choose the conditions under which we invest, but we can certainly choose how we position ourselves.

I thank you very much for your trust and for the excellent partnership in both good and challenging times. Please do not hesitate to contact me if you have any questions or suggestions.

Respectfully,

Bahram Assadollahzadeh, CFA
May 2021

APPENDIX A – INVESTMENT OBJECTIVES

I repeat the objectives we defined in our Partner's Manuel in every letter so that we can compare our results to our goals. Please keep in mind that a track record only becomes meaningful after 5-10 years. Until then, and even after that, I recommend that you base your decisions on the investment approach described in Richtwert's Partner Manual.

I can't promise you any results, but I do want you to know the qualitative and quantitative goals Richtwert is aiming for.

Our qualitative goals over the mid- and long-term are:

1. *To protect the purchasing power of our wealth.*
2. *To maximize our wealth.*

You can find more details regarding our qualitative goals in our Partner's Manual.

Our quantitative goals over the mid- and long-term are:

A. *To achieve average annual rates of return before profit-share and taxes of at least 10%*

or

B. *to exceed the S&P 500 index performance (hedged in our reference currencies) by 3% on average before profit-share and taxes.*

Ideally, we want to meet both goals, but I will be satisfied if we meet either goal. For instance, if we achieve goal A) but fail to meet goal B), I believe the performance of the S&P 500 index is exaggerated and that future returns from the S&P 500 will be lower allowing us to meet goal B) in the future. On the other hand, if we achieve goal B) but fail to meet goal A), I believe the performance of the S&P 500 index has been too low and that it will improve over the course of the next few years. Our performance should also improve in absolute terms as long as we continue to perform better than the S&P 500.

Therefore, if our record is better than any of the targets mentioned above, I believe we have been successful. If our record fails to meet both targets, I believe we should look for alternative ways of investing our capital.

