December 2021 Monthly Report plus 2021 Year in Review

Returns 31-Dec-12 to 31-Dec-21

	Norse Capital	All Ords Accum	Outperformance	Small Ords Accum	Outperformance
Inception	419.70%	139.14%	280.56%	102.11%	317.58%
Inception per annum	20.08%	10.17%	9.92%	8.13%	11.96%
CY2021	16.86%	17.74%	-0.88%	16.90%	-0.04%
CY2020	26.36%	3.64%	22.73%	9.21%	17.15%
CY2019	43.44%	24.06%	19.38%	21.36%	22.08%
CY2018	7.46%	-3.53%	10.99%	-8.67%	16.13%
CY2017	15.55%	12.47%	3.08%	20.02%	-4.46%
CY2016	9.31%	11.65%	-2.33%	13.18%	-3.87%
CY2015	36.80%	3.78%	33.02%	10.16%	26.65%
CY2014	10.81%	5.02%	5.79%	-3.81%	14.62%
CY2013	19.24%	19.66%	-0.41%	-0.76%	20.00%
1m	-6.43%	2.67%	-9.10%	1.41%	-7.84%
3m	0.48%	2.48%	-2.01%	2.03%	-1.55%
6m	5.78%	4.58%	1.20%	5.54%	0.24%
1y	16.86%	17.74%	-0.88%	16.90%	-0.04%
2y pa	21.48%	10.45%	11.04%	12.97%	8.52%
3y pa	28.39%	14.80%	13.59%	15.70%	12.70%
5y pa	21.31%	10.42%	10.89%	11.16%	10.15%
7y pa	21.59%	9.62%	11.97%	11.30%	10.29%
Sharpe Ratio	1.27	0.68	1.87x	0.48	2.67x
Sortino Ratio	2.33	0.95	2.46x	0.69	3.37x
Annualised standard deviation	14.09%	13.42%		16.00%	
Highest monthly return	11.91%	10.16%		14.27%	
Largest monthly loss	-8.94%	-20.94%		-22.38%	
Largest drawdown	-14.04%	-27.33%		-29.11%	
% positive months	73.15%	67.59%		60.19%	

Happy new year for 2022 which will be our 10th year running the portfolio. Looking forward to it and hopefully a better one outside markets than the last couple of Covid years. A short recap on December before we review 2021.

As presaged previously, volatility was once again evident with a more than -6.4% drop in December following November's ~+6.1% gain, ceding ground to the indices we usually follow with the All Ords +~2.7% and the Small Ords +~1.4% while in the US the S&P 500 rose +4.4% and the Nasdaq +0.7%.

Almost three quarters of the month's losses came from MIGI, our largest individual holding. The shares dropped -33.7% with Bitcoin itself down -20.2% on the month and ahead of January's escrow conditions release for early pre-listing shareholders (ourselves included). The specific liquidity circumstances around the release have in all likelihood contributed to the recent significant share price underperformance vs other Bitcoin miners, resulting in a substantial discount vs peers. Looking through these shorter-term supply issues should hopefully lead to a rerating as the company ramps up its mining rate with contracted mining rigs to come online.

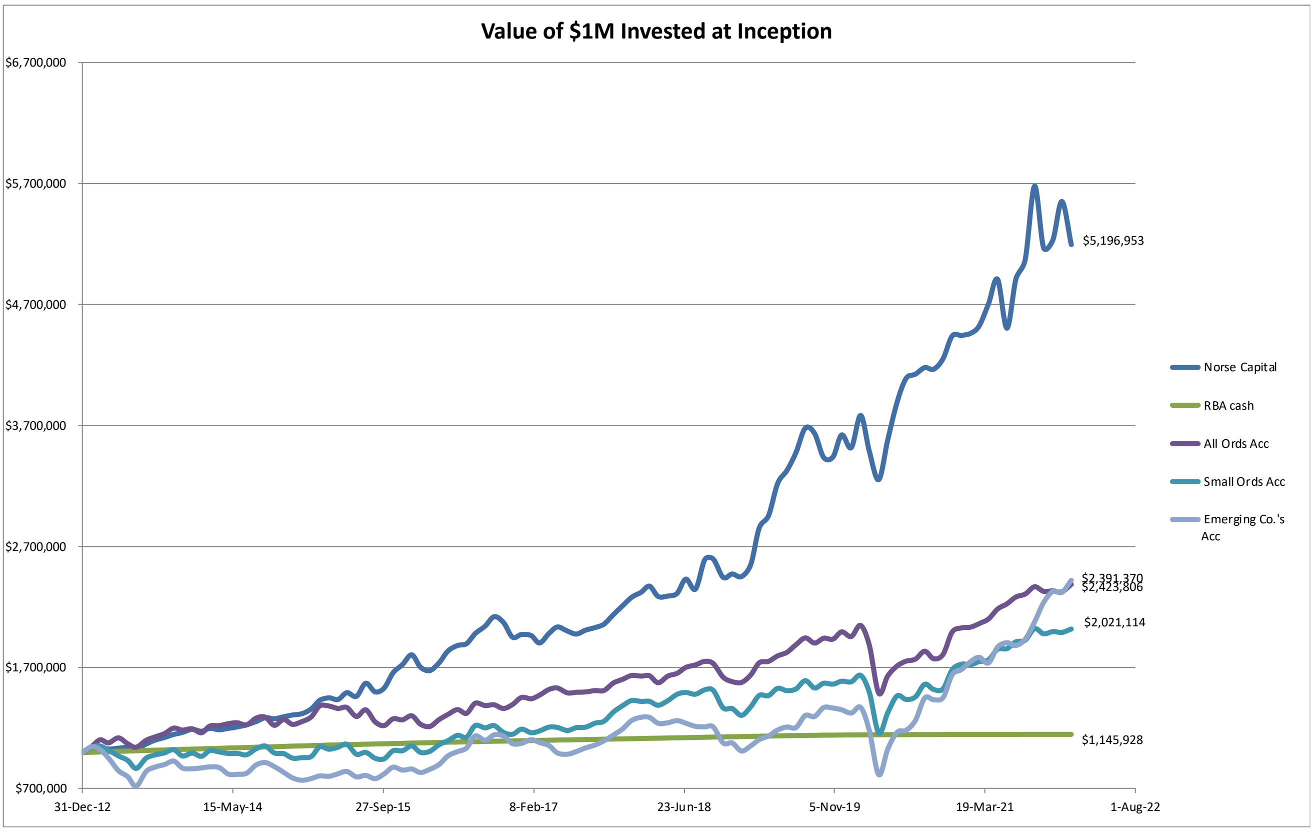
The other quarter of the month's losses came from our US-listed enterprise software basket. Another rotation out of high-growth, high-multiple stocks (higher yields contributing), has led to multiple compression in the sector which has so far continued into early 2022. For our portfolio, the biggest basket detractors in December were SHOP (-9.5%), TTD (-11.4%) and ZS (-7.4%).

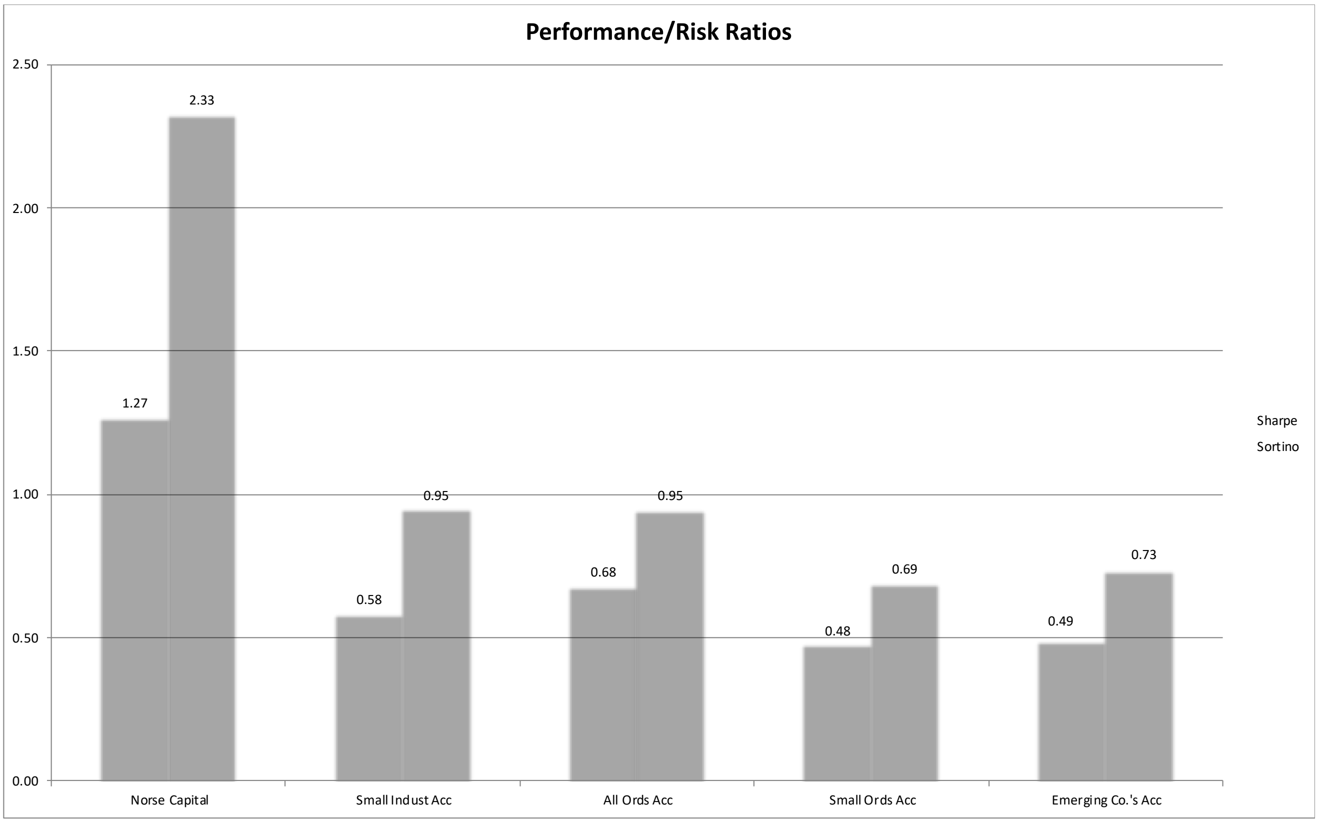
Amongst the noise, positive contributions from AAPL (+7.4%) and APX (+16.4%). Shorts and hedges cost us ~-0.2% and the almost +2% rise in the AUD-USD cost another ~-0.8%.

Portfolio Holdings:

Cash:	20.2% (AUD and USD)
Non-AUD exposure:	44.7%
Longs:	71.8%
Shorts:	-2.2%
Options delta:	12.3%
Net exposure:	81.9%
Top 5 equities (alphabetical):	AAPL, MIGI, PME, RMD, RUL

The same top 5 positions continue. Our enterprise software basket currently makes up ~18.9% of the portfolio; we've added tiny nibbles as share prices have dropped but don't intend to take the weighting above 20% at this stage. Our net exposure is only slightly lower despite December's negative performance and adding some hedges as that exposure drop is partially offset by MIGI shares coming out of escrow in January.





2021 Year in Review

The portfolio managed to return just shy of +16.9% in 2021, its ninth year. On the face of it a decent absolute return but a little short of the benchmark indices we follow with the All Ords accumulating more than +17.7% and the Small Ords +16.9%. Meanwhile the US indices did even better with the S&P 500 returning almost +27% and the Nasdaq +21.4% plus dividends. So a relative underperformance whichever way we look at it. Let's take a look under the hood to see why and what could have been done better.

At a high level, we entered 2021 with a cash weighting of 26.1% and a net exposure of 76.3 %, exiting 2021 at 20.2% and 81.9% respectively. Our average numbers for 2021 were 22.82% and 79%. Our net exposure level rose +5.8% (and cash weighting fell) as we withdrew a fair amount of personal cash from the portfolio (to fund a property upgrade). That, coupled with positive portfolio performance, outweighed the effect of our sales during the year.

We also experienced more volatility in returns in 2021 which included setting a new all-time monthly return low of -8.94% in September, straight after setting a new all-time monthly return high of +11.91% in August. Other monthly figures included consecutive ~-8% and ~+9% returns and consecutive ~+6% and ~-6.4% returns. We had presaged this possibility for the remainder of 2021 in our March report (see below commentary on our MIGI position), but also experienced a couple of bouts of multiple compression hitting our high-growth enterprise software basket (and other portfolio holdings) as the market rotated out, then back in to that sector.

As mentioned above, we took some personal cash out of the portfolio, and in order to keep our net exposure reasonable, sold out of more portfolio positions than in a typical year. Interestingly, **all** (i.e. 100%) of those sales were higher than end-2021 levels, most significantly so, and not all due to late 2021's high-growth sector sell off. Conversely, our lack of selling in what has subsequently proved to be our biggest 2021 detractor, leads to arguably our biggest opportunity for learning/what we can (hopefully) do better in the future: the art of selling, aka when to sell out of fallen angels vs when to hold firm. Let's take a look at the individual significant detractors/contributors and at the positions we did and did not exit to see if we can come to any practical conclusions (or whether it's all just too hard and we should give up and go to the beach).

Detractors:

APX: -5.1%
Appen dropped almost -55% on the year, from $24.69 down to $11.16 over the course of 2021, continuing its plunge from all-time highs above $43 in 2020. We had trimmed gradually on the way up but did almost nothing on the way down (except for a small sale near current low levels), to bring our position to just over 40% of our peak holding (in number of shares). At 2021 year-end, the shares were trading at a ~-75% discount to 2020 highs. In hindsight we did well by trimming on the way up but obviously should have been more ruthless on the way down. We stayed in as we believed in the tailwind of AI (and still do) and Appen's top position in the annotation industry; our initial thesis was merely on temporary hold from a pandemic-induced slowdown. That may possibly still be the case but increased competition from the likes of ScaleAI, the continued rise of self-learning AI on unlabelled data and the increasing importance of data privacy driving towards in-house annotation have all proved headwinds. We continue to hold our reduced position but on a tight leash pending further updates – perhaps a classic example of thesis creep where a history of strong revenue growth as the top global annotation provider has now become a "value" play…

Shorts and hedges: -2%
An almost identical detraction to last year's -2.1%. On a positive year for most equity indices, spending ~2% on hedging is about par for our course. A ~-5.6% drop in the AUD-USD helped add back ~+0.5% to the portfolio over 2021.

EML: -1.1%
EML had a volatile 2021, twice getting mentioned amongst our monthly worst performance missives and three times amongst our monthly best performers. Our EML holding started the year as one of our top 5 holdings, even after we trimmed ~17% of the position in February above $4 which we did for portfolio sizing considerations. However, after a runup over $5, news of an AML investigation by the Central Bank of Ireland in May engendered a roughly ~50% haircut and kickstarted multiple rounds of volatility over the remainder of the year as news on the investigation ebbed and flowed. We held our nerve but didn't add to the position despite the inclination to do so. AML issues have been part and parcel of the financial landscape with multiple examples of AML regulatory issues surfacing over the years, most ending with the payment of fines and undertakings to compliance bodies going forwards. We

judged the probability of an extreme negative outcome to be low (but not zero) and given the scale of the market-cap haircut, held our nerve. An example here where we did not sell and remain invested for the long-term. (And hopefully not a thesis-busting example).

<u>Contributors:</u>

MIGI: +6.6%
Our initially small (on the order of ~1% weighting) unlisted holding in Mawson Infrastructure Group (formerly Cosmos Capital) listed on the US markets in 2021, finishing the year up almost +943% from the price of the last capital raising prior; this even after an almost -60% drop from all-time highs in September. We benefitted from a rise in BTC itself, up multi-fold from when we first invested in Mawson, as well as a valuation jump on share listing onto the US OTC markets followed by a Nasdaq listing. Our comments in March upon MIGI becoming a listed entity that our portfolio returns going forwards would take a step up in volatility proved prescient: MIGI featured 4 times amongst the monthly best performers and 3 times amongst the monthly worst performers in 2021. Our MIGI result highlights the power of compounding: given the 2021 escrow provisions for early-stage investors, we did not sell a single share which allowed the entire position to compound up. Our intention is to stay invested as we believe we are still in the early innings of Bitcoin and other crypto adoption and bitcoin mining and Mawson represent a unique and different way to gain exposure to the value chain. Absent a change in our view of crypto markets, we will manage the position from a portfolio viewpoint while remaining cognisant of BTC’s well-known extreme volatility.

PME: +4.9%
Pro Medicus continued to execute well in 2021 with multiple new contract wins continuing to demonstrate the quality of the management running this company, leading to continued investment performance with the shares up almost +83% in 2021. Unfortunately, we continued to trim our position too early, selling ~25% of our remaining position between $38 and $65 (with the majority of those sales currently out of the money). Our current position is now down to only ~30% of our peak holding with our regret at selling too early countered only slightly by what continues to look like an extremely demanding valuation. Trying to tread the path between selling on valuation concerns yet holding onto a high-quality company to compound for the long-term, we are satisfied with our current ~7% weighting but acknowledge our propensity for self-flagellation for selling PME too early will no doubt continue.

AAPL: +4.5%
Our continued long-term holding in Apple shares ended the year up just shy of +34%, representing an over 73x gain (excluding dividends) from our initial purchase at a split-adjusted price (adjusted by 7:1 then 4:1 or 28x!) in the low $2s in 2006. I should have just put the entire portfolio into AAPL and sat on the beach the last 15+ years, it would certainly have been a lot less work. Obviously not something we would realistically have done but it does highlight how much selling half the position a few years ago has cost. The moronic (in hindsight) reason for selling back then was roughly in line with Apple's market-cap breaching the USD $1 trillion threshold (the first company in history to do so) and the thinking that the law of large numbers would dictate there would not be significant upside potential remaining. Of course Apple in the last few days took out the USD $3 trillion level intraday. More self-flagellation to follow in the privacy of my own home. (And no, I'm not a masochist, at least I think not…).

US-listed enterprise software basket: +3.5%
A positive contribution from our basket although quite a wide distribution of returns between the different individual components, ranging from -44% for FSLY (to where we sold out) and -34% for AYX (also to where we sold out), vs +47% for MDB, +61% for ZS and +81% for DDOG. Interestingly, the CLOU Global Cloud Computing Index ETF (a reasonable proxy for the cloud/enterprise software investment space) returned -4.9% for the year. We sold out of four basket positions in 2021, with all of them having proven in hindsight to have been good sales (so far). Even after the aforementioned sales in FSLY and AYX which were late after substantial drops from the highs, the shares went on to drop a further 27.5% and 24.5% respectively into year-end. One could argue though, that we should have sold out of FSLY and AYX much earlier. FSLY had shown tremendous growth in usage of its edge network and our investment thesis was that the best and fastest technology would lead to continued revenue growth. In hindsight a lot of their growth was driven by the pandemic and the loss of their biggest customer TikTok presaged more to come as NET is the clear edge network winner. Meanwhile AYX's slow migration to the cloud should have also been a sign to keep the position on a tighter leash. When the cost of hedging basket positions grew more expensive than we were willing to pay, we sold out of our these two, lowest conviction basket positions. We also sold out of positions in PAYC and ZM earlier in 2021, the latter just shy of $400, or more than double current levels. A fortunate exit level in

Zoom, based on our view then that Zoom, fuelled by the pandemic, had already "conquered" a significant chunk of its TAM.

RUL: +2.6%
RPM Global's +68% rise in 2021 has put our holding into the top 5 weightings in the portfolio. Another example of allowing a holding (this one at over 5x in a bit more than 5 years from initial purchase) to compound up over time. Importantly, we also added over time as our confidence in the company and our thesis regarding the transition away from licensing to subscription software proved correct.

JAN: +2.0%
Another example of a small initial position compounding up: Janison Education's shares returned just shy of +130% in 2021. We initiated the current position from late 2019 through early 2020 between 30-50c and bought slightly more mid this year at 82c. Currently around a ~3.5% position, in reality we should have been buying more as the company continued to kick goals with the PISA for schools program and with integrating the ICAS product.

In order to keep our net exposure from growing too high given our cash withdrawals, we exited several positions including: TCEHY (Tencent) above $71.50 in which we lost confidence given China's regulatory crackdown on technology firms, PPH above $1.72 after the Resi Media acquisition, VHT under $1.20 with a high valuation while they struggle to gain scale, and UOS and XRO. Interestingly all those sales are currently above current prices, most by double-digit percentages. These so-far successful sales are an argument in favour of being more ruthless with selling to cull the portfolio down even further to concentrate more on higher confidence positions.

We started the year in review by highlighting how the effect of selling or not selling has had a significant effect on 2021's returns. In fact, those decisions have also had a significant effect over the life of the portfolio. It is obvious in hindsight we should have sold more of Appen much earlier; this year alone our returns would have been > 5% higher than what we achieved, on top of losses from 2020's highs. Successful sales of other positions in 2021 also argue in favour of selling. Historically though, the costs of selling too early have been much higher: witness the forgone profits from selling Apple and Pro Medicus too early which, given the power of compounding, would have dwarfed the losses from not selling losing positions earlier. (Aside from the caveat of selling to trim a position size down to a reasonable level if it has grown too large for comfort). Yet (in my opinion) that doesn't mean holding on to everything till the bitter end. A common thread is we should have sold out quickly and ruthlessly when a thesis is broken – there are no prizes for loyalty in investing. So, easily done then: retain our long-term bias to hold positions to allow them to compound. Don't sell unless our thesis is broken but then sell out quickly. One "minor" question though – how to tell when a thesis is definitely broken? A topic for another day but if anyone knows a foolproof answer, please contact me immediately…