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January 15th, 2022

2021 Return	October	November	December	Q4	Annual Return	Return Since Inception
MountainWorks	6.8%	-14.6%	-9.0%	-17.0%	-12.2%	101.4%
S&P 500				6.0%	28.4%	173.6%

Dear Member,

In the fourth quarter of 2021, Mountainworks lost 17% of its value, versus a 6% gain for the S&P 500, dividends reinvested (according to DQYDJ). Since inception (February 2016), the Fund has gained 101.4% against a 173.6% clip for the S&P 500. Almost on cue, at the moment I reflect on the volatility and uneven quarters expected from our investments, I ended up taking some hefty lumps. Most of my downfall this quarter was the result of FuboTV shares dropping precipitously after their latest report, as well as a mistake in Zoom Video, as the return-to-work theme brought ZM prices back down to earth. While I consistently encourage members (and readers, for that matter) not to focus too much on a few quarters, my personal pet peeve is experiencing a year in which my performance drags while the general market continues to shine – this past twelve months definitely fits the bill, and so I must do better.

Habitual readers know that I tend to highlight my mistakes in our quarterly letters; it is perhaps force of habit after experiencing tumultuous returns since Mountainworks was formed (40.7%, 29.3%, -58.6%, 33.8%, 128.6%, and so on…). For several reasons, I gravitate toward unusual situations that are considered risky[1] by traditional investment standards. Undoubtedly that leads to uneven results in the short term. For my part, I can still improve; I can humbly state that we have yet to experience a mistake-free year, and of course, that is entirely my responsibility. That said, I see the gyrations of the portfolio as a harbinger of things to come. Our system bends, but doesn't break, and to a certain extent that is the goal. In the end, I believe we are on the right track. We are at a time where the market remains overvalued and at some point, investors will have to relent.

General Stock Market Performance. Historically one can view the returns on the market at about 10% per year. Strangely enough, when you think about how perilous the stock market has been over the past 20 years (with the dot-com bubble, financial crisis, and pandemic being specific examples of "accidents"), the history of S&P 500 growth is curiously linear. Since 1900, the return has been 10% annually. If you bought into the market in 1930 (right around the depression), your returns would be

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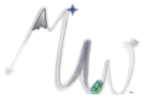
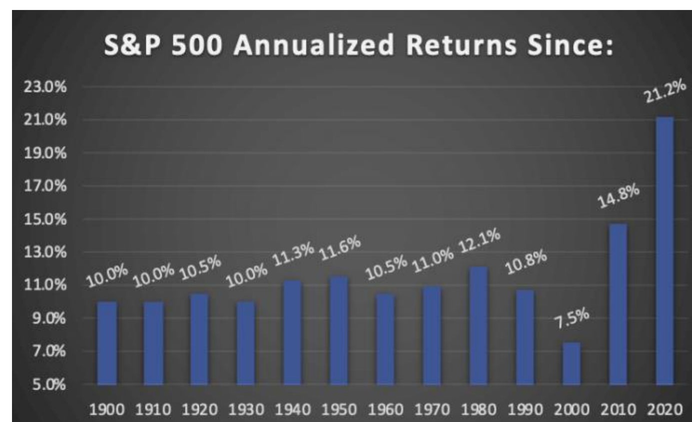
[1] See the 2021 Q3 letter for a more in depth discussion about risk



the same! If you had bought when the stock market bottomed in 1932, your annual returns would be 11.3%, less than two percentage points better, which doesn't seem like much. It is amazing to think that, over the past 100 years with so much volatility throughout history, the general market would be an unwavering bellwether for investing.

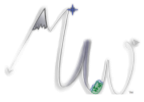
Given that the growth in equities is so linear over time[2], it begs the question as to when there has been unusual activity, if at all? It turns out that one of the worst times to invest was the year 2000 (right before the dot-com bubble). Since then, returns have compounded at a measly 7.5% per year up to the present. Yet, if you started investing in 2010, your annual rate of return would be 14.8% per year – outstanding returns. It gets even better…since 2020, the return on the market has been 21.2% per year.[3]



(Data sourced from DQYDJ, dividends reinvested)

I think there's a couple of important assertions that are hard to overlook. First, an entire generation has grown up without ever knowing high interest rates. That is, from the day you were born, a bank has never been a good place to put your money. Can you imagine? Near-zero interest rates have made banks pointless, besides being an electronic safe. It's no wonder cryptocurrency has become such a fad with Generation Z. Second, while the post-millennial babies have grown up believing "stonks"[4] are the answer, history (and the chart above) tells us the recent returns from the stock market are unsustainable. From a returns perspective, the market is way too overvalued. Problem is, value investors have been singing the same sad song for over a decade now, only to miss out on life-changing

[2] That is, prices have increased exponentially, whereas the growth rate has stayed relatively linear
[3] Mountainworks has compounded at 12.4% per year since inception
[4] Yes, I'm giving a nod to the Reddit group "Wall Street Bets"



wealth creation. As a self-proclaimed contrarian and value investor, I've been repeating this message like a broken record (the Total Market Cap to GDP ratio is 206%, and the market P/E ratio is over 39), while the market churns higher and we miss out on high fliers like Tesla and Amazon.[5]

But there's a dichotomy between market overvaluation and the Fund's performance, because although I believe the market is set up for diminishing returns, I don't sit on a lot of cash in the portfolio. Much of it is put to work, as it should be, because the high rates of inflation make sitting on cash a bad idea. Moreover, this sort of cognitive dissonance[6] – where the market is telling me one thing but I'm doing another – has been troubling. It's too easy to get excited about a company like Zoom, which shoots from $75 to $550 in less than a year and feel like you're missing out. Then, in the same irrational breath, bet on Zoom while it's trading at the top, and ride it all the way to $200/share because you think it's still a game-changer (I'm channeling my inner-Cathy-Wood, who recently doubled down on ZM after an awful price drop). No matter how much I claim to be a professional investor, my tail is between my legs; I'm the "mark" at the poker table. Not the first time, and probably not the last time.

Portfolio Reflections. The Zoom case presents a microcosm of how mistakes can be made (call it a fear of missing out, or just plain old greed) yet also how the Mountainworks system can help mitigate the risk. Without getting into too much detail – yes, this is the "secret sauce" we're talking about now – my investment in Zoom dropped from $515 down to $197.70 and was a 62% loss. However, using some active management, opportune trades, and portfolio allocation, I was able to deflect that loss to about 22%. So instead of hitting the portfolio for some 12%, my ZM losses represented 4% of the losses for the year. Although I'd prefer to not be so active in trading (as we are still long-term investors, and hell, why not just be correct from the get go), this particular example shows that the processes I have developed can shield the portfolio from compounding the problem. In other words, the issues with Zoom didn't crush us. Zoom represents about one-third of my losses for the year. As much as it frustrates me to sell out on a loss while the S&P is up double digits, at least I live to fight another day.[7]

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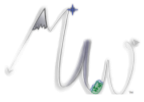
[5] Disclosure: we are short TSLA

[6] Cognitive Dissonance is a psychological term for thinking one way, but behaving in another way. Specifically related to investing, I simply mean that I think stocks are overvalued, but I invest in them anyway. On some level it would certainly set me up for failure, yet success in investing is always a function of time.

[7] In general, we can think about losses behaviorally as hurting twice as much as gains help, and this type of fear of losses ("loss aversion") contributes to the reasoning behind the saying stock "take the stairs up, but the elevator down". Probably irrationally then, a loss hurts three times as much when you think about the lost opportunity cost of buying a loser while missing out on a winner.



Much the same could be said for some of my other losers this year, including L Brands and Community Health Systems. Both were short positions that I was wrong about, and cost us 13% and 12%, respectively.[8]

On the other hand, Fubo is still a large part of the portfolio, and the stock price has suffered just as much as Zoom, and it all took place in the most recent quarter. As previously stated, Fubo is a new company, with no historical data, small revenues, and negative earnings. There are definitely some challenges to overcome, as it operates in a competitive streaming industry and is reaching into a sportsbook business that carries a lot of overhead costs.

There have been some prescient short reports on Fubo (example here), and to date the short sellers have been correct. After Fubo's latest report, the shares dropped from $33 to $15, a 55% fall. To date, my decisions on Fubo have cost roughly 15% to the portfolio. Another way to say it would be that without my mistakes on Zoom, L Brands, Community Health, and Fubo, we would have yielded a 32% gain for the year. Yes, hindsight is always 20-20, and I have to work hard to ignore sunk costs, but nevertheless, you can begin to see why I harp on my own misgivings, envisioning the returns that could bear fruit in a "mistake-free" year (as hard as that may be to come by). There is no other way to say it: the fault is mine.

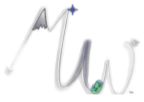
Admittedly, little recompense can be found in my writings, suffice to say that with Fubo, there may very well be an opportunity. At the current time, the company is showing subscriber growth (over 1 million paid subscribers) and revenue growth (over $600 million per year) above 100% per year, and if you believe that over 70 million households are going to cut the cable over the medium term, then perhaps there is a path to subscriber aggregation and improved margins.

No doubt that valuing Fubo has been one of the hardest tasks I've ever endeavored to do. And the results of my research have yet to prove fruitful. For now, the business doesn't make a profit, and has high content costs that squeeze just about all of the subscriber revenue.[9] That leaves a valuation on the "total addressable market", which given the number of years I have to look forward and the troubles with finding the proper discount rate, it's just tough. What's left are some qualitative factors: this is a content distributor like Comcast, with an advertising business and sportsbook optionality. Of course, publicly traded sportsbooks like DraftKings[10] have extremely high acquisition costs, which hurts Fubo's prospects as an online sports gambling company. Even still, CEO and co-founder David Gandler

[8] See the 2021 Q1 Letter for a more in-depth look at L Brands

[9] It's worth repeating – Fubo has very high subscription costs that make the company unprofitable at present. The streaming business is extraordinarily difficult to navigate. The company is a small fish competing against sharks like YouTube TV (Google), Hulu (Disney and a Comcast minority), Sling TV (Dish), and others. But if the margins improve, it could be a windfall for investors.

[10] Disclosure: we are short DKNG



has shown that he isn't afraid of a fight, and is willing to defy the odds when it comes to the highly competitive streaming business.

> *"[So] it isn't the strongest link you're looking for among individuals in the room. It isn't even the average strength in the chain. It's the weakest link that causes the problem […] When I look at our managers, I'm not trying to look at the guy who wakes up at night and says '$E=MC^2$' or something. I am looking for the people that function very, very well. And that means not having any weak links." -Warren Buffett, 1991*

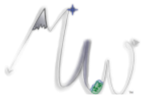
The quote above is relevant because in many ways the managers of our businesses are irreplaceable. Marcus Lemonis (Camping World), Reed Hastings (Netflix), David Kimbell (Ulta Beauty), Howard Lutnick (BGC Partners) and Daniel Zhang (Alibaba) have key roles to play in their respective businesses, and we – as eccentric business owners – put much of our faith (and assets) in their hands.

While it is my job to find good businesses using the Mountainworks process that gives us an edge, it is also important that we find good managers who don't have weak links (that means looking in the mirror as well). Good management lends itself nicely to our own portfolio goals: we operate in a loosely coupled, complex system. If one branch of our investments doesn't work out, it won't take down the entire tree. While at times that leads to volatile results, other times it serves the purpose of minimizing downside.

I hope that the discussion is worthwhile and beneficial. As always, thank you for your time & attention. If you would like to discuss anything, please don't hesitate to reach out: Justin@mountainworksllc.com.

Yours,

Justin Polce
Managing Member



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