GREENHAVEN ROAD
PARTNERS FUND

August 2022

Dear Fellow Investors,

The Partners Fund returned approximately -23% for the second quarter, bringing the year-to-date return to approximately -36%. U.S. markets broadly have had their worst start since 1970 with the S&P declining over -20%, the Nasdaq declining approximately -30%, and certain pockets experiencing more severe drawdowns.

So far this year, three of the managers who have compounded at among the highest rates over the years are down significantly, dragging down the average. I consider all of the Partners Fund managers to be incredibly smart and astute investors – I wouldn't have invested our money with them otherwise. However, I consider these particular three to be *actual* geniuses. Yet, at first glance, their performance in the first half of 2022 seems to say otherwise….

Now, maybe my calibration is off – could it be that these investors got lucky in the past and time is catching up with them? That is certainly possible, but even after incurring -35%+ drawdowns, their net performance has annualized at 16.0%, 19.3%, and 16.4% over their 12.5-, ~10-, and 7-year official track records, respectively. This well exceeds any and all benchmarks I am aware of. I don't believe this is a case of their luck running out.

I think part of the Partners Fund's current "underperformance" lies in the construction of the overall portfolio. One of the features that we seek from managers is concentration. I don't want to just re-create the Russell 2000 by having 20 managers with 100 positions each. Concentration allows a manager's highest conviction ideas to be large enough to move the needle. Of course, this works both ways – large positions can also move the needle to the downside. With fewer holdings comes a larger divergence from the average. Our portfolio-level sizing decisions depend on a few factors, including manager style, area(s) of focus, etc. Some funds are expected to be more volatile than others, but as long our sizing is generally prudent, the underlying concentration should be manageable over time with funds zigging and zagging as their investments develop. As discussed in past letters, I generally do not plan to "rebalance" the Partners Fund with frequent subscriptions and redemptions. Instead, the plan is more to let the cream rise to the top over time.

Besides concentration, the Partners Fund's lack of exposure to commodities such as oil was undoubtedly a source of the underperformance so far this year. I typically avoid managers with meaningful exposure to commodities given the view that commodity-based businesses have not been "good businesses" historically and that the nature of their exposures makes it hard to gain an analytical edge. As always, there are exceptions, and since we may be entering a commodity super-cycle, this is a belief worth revisiting.

That said, we are not changing our stripes. Doing so would make Annie Duke, the author of *Thinking in Bets*, accuse me of "resulting" – letting the outcome quality serve as a perfect signal for decision quality. (video link) Given the short timeframe, high levels of overall market volatility, and macro drivers of risk-off sentiment punishing certain types of companies in particular, I have not at all lost confidence in the research or decision-making skills of the managers to whom we have entrusted our capital. As one of them pointed out in their letter (attached),

> "Watching 3% - 5% daily fluctuations of individual stock prices, in both directions and on no fundamental news, reinforces our core belief that markets often act irrationally in the short term. To cite an extreme example that we do not currently own, Carvana posted double-digit daily

> price changes on 11 of the last 30 trading days, including seven positive 10%+ moves and four negative 10%+ moves, and ended up roughly in the same place it started. Clearly, the market is confused about what it "thinks" about certain growth companies."

There is plenty of historical precedent for excellent managers having periods of underperformance way longer than three months. For example, Charlie Munger was down -54% in 1972-73 while on a path to compounding at just under 20% for the duration of his partnership (vs. a market return of 5%) (link). As Joel Greenblatt pointed out in Barron's, "the statistics for the top-quartile managers for that decade were stunning: 97% of them spent at least three of those 10 years in the bottom half of performance, 79% spent at least three years in the bottom quartile, and 47% spent at least three years in the bottom decile." (link)

I believe that periods of underperformance are part of the process. They are bound to happen for most funds and, by extension, funds of funds. Over the years, these periods are to be expected and must be endured. We have been through a period where larger companies fared better than smaller companies, commodities fared better than non-commodities, and straightforwardness/simplicity fared better than complexity. Stock-picking is not dead, it just feels that way right now.

I would also point out that all the managers discussed above gravitate towards smaller companies, which makes their historical performance that much more remarkable. As Adam Wyden of ADW Capital pointed out in a recent letter,

> "Large" outperformed "Small" over our first 11 years by 350 to 500 bps annually! This phenomenon is even more staggering when you consider how much "Small" has outperformed "Large"… we estimated the average annual excess return of "Small vs. Big" between 1927-2010 (period prior to the launch of our strategies) was over 350 bps.
>
> People like to say "this time is different" but we have 84 years of data to the contrary. The US markets have lived through wars, double-digit interest rates, global pandemics, and a prolonged great depression. It always "feels different" in the moment. Our belief is that investing at these moments is the very thing that secures the next decade's returns. We have 84 years of data that would imply the sun will shine again for "small-cap" stocks and we will be prepared for that day

As I have said at the end of every letter, our fund of funds is going to be different. It will be smaller, the underlying holdings will be more esoteric, and I hope the managers will continue to collaborate more over time. I believe that it will be "good different," but only time will tell. Thank you for joining me on this journey. I will work hard to grow your family capital alongside mine.

Sincerely,

Scott Miller

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