

# MANAGEMENT'S LETTER TO PARTNERS

## Dear Partner,

I hope that you are doing well and that you and your family are coping as best as can be expected with the pandemic.

In 2020, the Aquamarine Fund returned **11.3%**. This compares with **18.4%** for the S&P 500. Since the fund's inception in September 1997, our capital has compounded at a rate of **9.6%** annually vs **8.1%** for the S&P 500, **8.5%** for the Dow Jones Industrial Average, and **3.2%** for the FTSE 100. The Aquamarine Fund's total return from inception is **739.2%**, versus **514%** for the S&P 500.

<sup>1</sup> These figures are net of all management expenses, incentive fees, and brokerage expenses, so these are actual returns. The figures for the S&P 500 include dividends, making this an apples-to-apples comparison.

## Where do we stand right now?

**T**hese days, events are moving in rapid and unpredictable ways, so I want to take a moment to share with you a brief snapshot of where we are right now—and how strange and unprecedented it is. As I write this, the Covid-19 pandemic is at the peak of its second wave. New variants threaten. Hospital wards are filling up, and the death rate is mounting. Unless you live in one of a handful of countries, the savior vaccines are painfully slow to roll out.

In response, half the planet is in lockdown, with an enormous impact on economic activity, employment, and psychological health. Restaurants and shopping malls are closed. Hotels are empty, and thousands of airplanes are sitting idly on runways. Eighteen months ago, this would have all seemed almost unimaginable. Now it's our daily reality.

Yesterday, here in Zurich, I walked to Sternen Grill, the city's favorite sausage spot on Bellevue, to buy takeout Kalbsbratwurst (veal sausage) for lunch. Dining inside restaurants isn't allowed these days, and there are usually long lines for takeout. As I took my place in the queue, for the first time in my ten years of living in Zurich, I counted no fewer than three people asking for money. Judging from their Swiss-German, they were certainly Swiss—not travelers from other countries. I was shocked. Switzerland has one of the best social support systems in the world. Three people begging is a revealing sign of these troubled times. And if this is happening in Switzerland, I hate to think about the conditions in many other countries.

That said, investors who entered this crisis with savings have had a very different experience of

the pandemic and could be almost oblivious to this wide-spread economic trauma. In March and April, we experienced a vicious plunge in the value of financial assets, with the market losing a third of its value in a matter of weeks. But those values then came roaring back by the end of the year, richly rewarding patient investors like us who kept their nerve, held on, and actually *bought* stocks amid that brief outbreak of extreme volatility and panic.

How did this period of extraordinary economic disruption turn out to be so benign for investors? The obvious answer is that governments around the world have opened the sluice gates, enacting the largest stimulus programs in history—even greater than we saw during the global financial crisis of 2008-9.

In the fiscal year 2020, the US federal government ran a deficit of \$3.1 trillion, which was more than triple the deficit of 2019. The 2020 deficit amounted to 15.2% of GDP—the greatest deficit as a share of the US economy since 1945. And the central banks have accommodated this by massively expanding the money supply. Consider that, in 2007, the Federal Reserve balance sheet was less than \$1 trillion. By the time the global financial crisis was over, at the end of 2009, the Fed's balance sheet had more than doubled to \$2.2 trillion. Over the course of 2020, the Federal Reserve balance sheet surged once more, rising from \$4.3 trillion to \$7.2 trillion. In the financial history of the world, this is unprecedented.

Even more surprising to me personally is that, despite being a fiscal conservative and a monetary hawk, I wholeheartedly agree with these actions. Tight money and a lack of fiscal stimulus would surely have led to a 1930s-style depression. We owe enormous gratitude to our economic leaders for taking these bold steps, despite predictable

It's not surprising that we're seeing extremely high valuations, given the combination of low interest rates, readily available credit, stimulus checks, and many people sitting at home without much action and excitement to engage them. This combustible mixture has fueled the rise of many stocks to irrationally exuberant levels.

accusations from some quarters that they've been recklessly spendthrift.

But the truth is, nobody—absolutely nobody—knows how things will play out from here, or what the consequences of this fiscal largesse will be. So far, one clear consequence has been that a lot of money has found its way into asset markets—specifically the equity markets. As a result, the market price of many assets has soared, quite likely to bubble territory.

The mania is perhaps best exemplified by the newfound fame of David Portnoy, Robin Hood, and GameStop. In normal times, David would be commenting on and enabling sports betting. But with a dearth of sports—and sports betting—

to focus on, he turned his attention to the stock market, as have a flood of individual investors. It's not surprising that we're seeing extremely high valuations, given the combination of low interest rates, readily available credit, stimulus checks, and many people sitting at home without much action and excitement to engage them. This combustible mixture has fueled the rise of many stocks to irrationally exuberant levels that are probably unsustainable, with their valuations completely divorced from financial reality.

David Einhorn, a battle-hardened value investor, recently remarked that “certain stocks are held exclusively by valuation-indifferent investors.... When the last holder of a stock that has valuation as part of the process exits and the shares are held more or less exclusively by members of those groups, the stock becomes disconnected from fair value. Valuation becomes irrelevant, and the stock price itself may as well be a random number.”

As you know from my previous shareholder letters, I don't pretend to have any ability to predict where the market is headed. I don't believe that anyone else can make successful market predictions with any consistency, either. In fact, I think this is a particularly good time to remind ourselves of these limitations—and to proceed with an appropriate measure of humility and caution.

Looking back to this time last year, I don't believe that any of these historic events were knowable or predictable. I, for one, certainly could not have foreseen how any of this would unfold, either economically or for global financial markets. More important, I can't tell how it will unfold from here. It's also true that I've consistently underestimated the severity and impact of the pandemic over the last year.

Why am I telling you these unsettling truths? For the simple reason that they are true. And you deserve the truth, even though it's uncomfortable to admit my own limitations and to acknowledge the extreme murkiness of the current situation.

Moreover, anyone who suggests that they *do* know how things will unfold from here is most likely deceiving you—and quite possibly themselves. Fortunately, I can also point to a more comforting silver lining, which we'll get to shortly. This silver lining isn't based on rosy predictions of blue skies ahead, but on a deeply held and rational optimism that is rooted in realism.

### Our singular goal and focus: long-term compounding

But before we get there, I'd like to review with you my goals for the Aquamarine Fund, since it's important for you as a partner in the fund to know what I'm about, what to expect from me going forward, and what exactly we're trying to achieve. My goal in running the fund is simple. I'm trying to build wealth and financial security for all of us by taking advantage of the miracle of long-term

compounding—and to do so in a way that allows you and me to sleep well at night. My hope is that this steady, resilient, and durable accumulation of wealth will also help us to build rich and meaningful lives, both for ourselves and others.

In my case, this emphasis on long-term wealth accumulation is deeply rooted in my family history. I only have to look back two generations to find ancestors whose lives and prosperity were destroyed by the calamities of the twentieth century, including World War II and the Holocaust. Having helped my family to recover and rebuild, my firm intention is to make the foundation more and more secure—for me and future generations. To the extent that this is possible, I want to ensure that no event, conceivable or inconceivable, can derail the patient and steady accumulation of wealth and financial security for my family and yours.

The good news is that if you can continue compounding for long enough, your wealth *really* builds up. Just consider that, from the Aquamarine Fund's inception in September 1997 to the end of 2020, we generated a cumulative return of 739.2% (versus 560.5% for the Dow

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Jones Industrial Average, 514% for the S&P 500, and 110.3% for the FTSE 100). I mention this not in the spirit of self-congratulation but to emphasize just how powerful it is to compound over a long period, even at rates that seem relatively modest. In our case, an annual return of 9.6% sustained over 23 years has delivered a very considerable increase in wealth and financial security, while also allowing us to beat the S&P by a margin of 225 percentage points.

For me, this overarching goal of *long-term compounding* is so important and precious that I'm willing to compromise on many other things in order to get this one big thing right. This emphasis informs everything we do here at Aquamarine, including my own behavior, the structure of the fund, the nature of the investments we make, and the orientation of our partners. All of these things need to exhibit specific (and relatively uncommon) qualities if we are going to succeed in reaching our chosen destination of long-term wealth creation.

We can even take that logic one step further. Our investment vehicle needs to work in such a way that it will get us there despite all of the flaws in the system. That doesn't just include the specific investments I make, some of which will prove to be mistakes. It also includes my mental limitations, my inability to see the future, and my temperamental weaknesses—and yours, too. We need to set things up for success, despite our various forms of fallibility. In short, the Aquamarine Fund must be robust enough to carry us through, no matter what.

Another way of putting this is that we're not riding in a sleek Formula One Ferrari that will perform optimally only if the conditions on the racetrack are perfect. Rather, our desired vehicle looks more like a sturdy, mud-spattered Jeep that must be capable of crossing all terrain even when the conditions get really tough. Our jeep needs to make progress

despite all of the imperfections that exist in the environment, the passengers, and the driver.

If you plan to compound money for an awfully long time—which is our singular goal here at Aquamarine—we're going to do it despite all of the mistakes and misjudgments that I, like any human, am capable of making.

### How did I do in 2020?

I would love to report that I acted with remarkable aplomb in 2020. That I saw the crisis coming, presciently reduced risk before the market sank in March, then bought aggressively before it surged again. That I foresaw that this was going to be good for particular businesses and cleverly rotated into them while cashing out of companies that were bound to suffer.

Of course, I did nothing of the sort. Rather, I missed several early warnings that, in retrospect, I should have taken more seriously. My first indication that something ominous was about to hit all of us came from European friends living in Shanghai. In December 2019 and January 2020, they talked about large parts of China being in lockdown and mentioned that people weren't allowed to leave their homes or neighborhoods. Instead of being shocked, viewing this as a warning signal, and thinking through the implications for Aquamarine, I discounted the potential impact, assuming that this wasn't relevant for us, since it was occurring on the other side of the world. As with avian flu, I figured that this new virus would primarily affect China and parts of Asia, not the United States or Europe.

Despite having the network and connections to recognize this threat early, it was only after watching a video on the 3BlueOneBrown YouTube channel that I truly grasped how Covid-19 could spread exponentially. I instantly warned vulnerable



members of my family about the risk to their safety. But until the stock market crashed in March, I remained convinced that the economic impact would be minimal. Even as case numbers rose in Western Europe, I continued to underestimate the fallout for global financial markets.

Why? Because there was nothing in my personal experience that prepared my thinking for what could happen in this particular case. I've lived through various financial crises. I was a 21-year-old economics student at the time of the 1987 market crash. I then managed the fund through the Asian financial crisis, the first Internet bubble and crash, 9/11, the SARS and avian flu outbreaks, and the 2008-9 global financial crisis. But compared to our current pandemic, those events proved relatively mild and short-lived. My experiences gave me an implicit narrative about how things would work out this time around, and I fitted the facts that I saw to support that narrative. All of this led me to do nothing to adjust the portfolio in advance of the crisis hitting.

Even if I *had* been more fearful of this coronavirus, there's no way that I could have predicted its astounding impact on specific industries and companies. For example, Covid-19 brought enormous tailwinds to some businesses, primarily cloud-based computing and online companies. As investors realized that even more economic activity would shift online, stock prices for these companies took flight. For example, Zoom, the videoconferencing company, soared from a market value of \$13.2 billion at the start of 2020 to \$75 billion by yearend.

It won't surprise you to hear that the Aquamarine Fund didn't (and doesn't) own any of these high-flying stocks, which were too richly valued to offer the margin of safety we require. As I've explained in the past, I'm perennially reluctant to pay a high

price for a rosy future. My risk aversion has kept us out of plenty of trouble over the last 23 years, but it has also cost us during heady periods when it pays—at least, for a while—to throw caution to the wind.

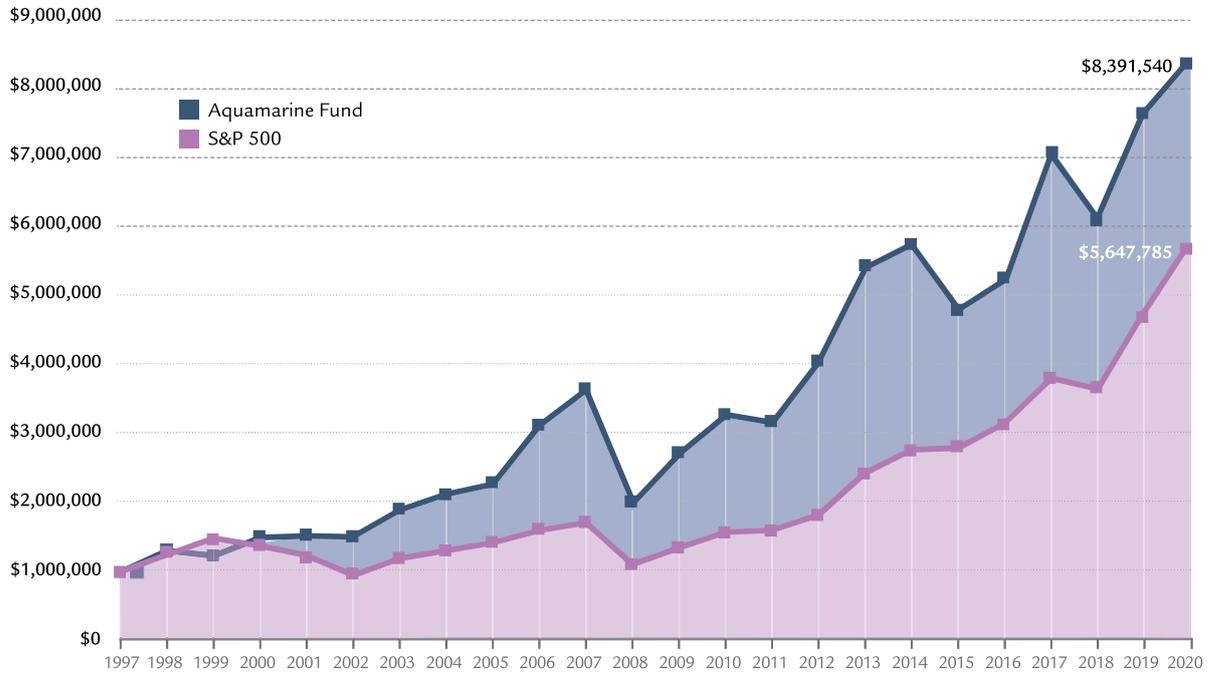
During the current bull market, shares in many of the most popular businesses have risen to stratospheric valuations. Many companies that may, in fact, have fantastic futures have fantastic valuations to match. That list seems to include Twilio, Alteryx, Snowflake, Roku, Salesforce, Amazon, Carvana, and other companies that I've researched but not bought.

While the pandemic was giving a gigantic tailwind to cloud and online businesses, it posed grave challenges to many physical businesses, especially in travel and retail. Prior to Covid-19, I could hardly have imagined that there could be an event that would affect every single physical retailer and every single shopping mall around the world—or one that would ground the majority of the world's airplanes. The idea that industries like these would come to a standstill, regardless of their geographic diversity, would have been inconceivable.

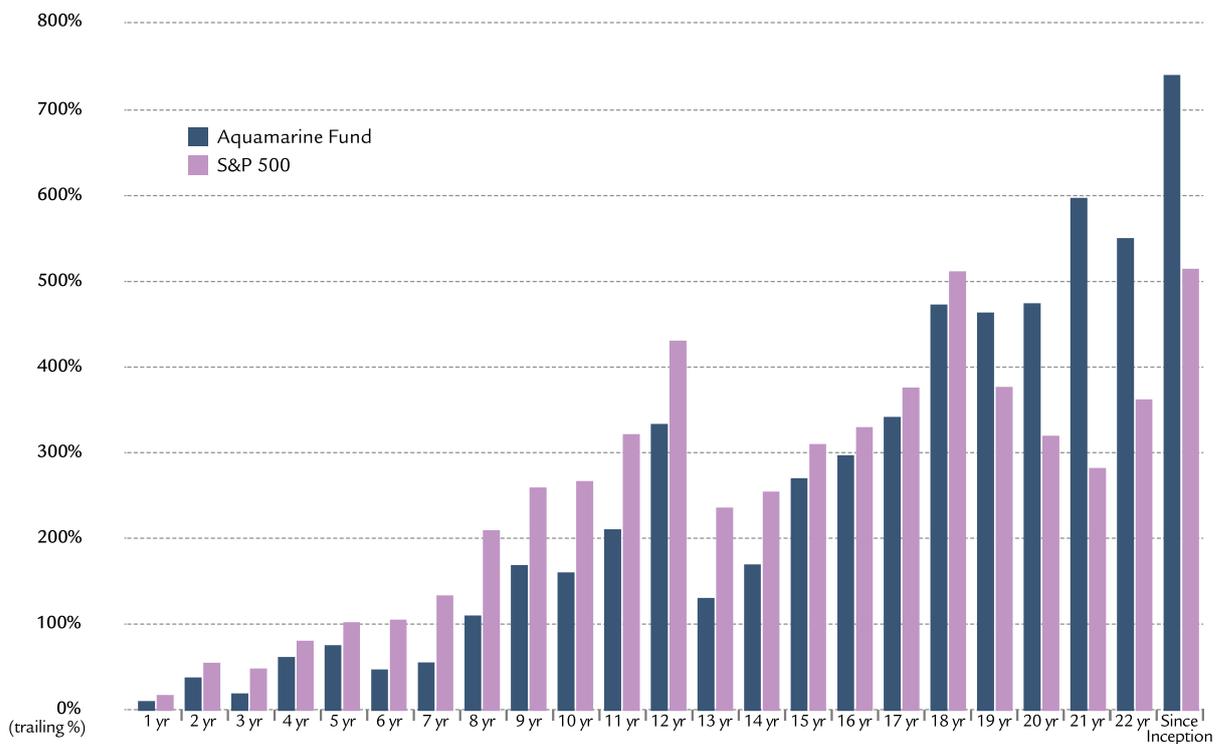
In our case, we dodged the carnage in hotels and airlines. But two of our portfolio businesses were seriously impacted: Seritage Growth Properties, which owns a portfolio of retail malls; and American Express, the credit card and payment network giant, which has a significant travel-related component to its business.

Still, here's where we come to what I hope is a silver lining for you. To the best of my ability, I've consciously invested in a way that's intended to make the portfolio anti-fragile, so that unexpected setbacks—and even a massive economic disruption like this pandemic—may be painful, but not catastrophic. That means owning a portfolio that

## AQUAMARINE FUND PERFORMANCE RELATIVE TO THE S&P 500 INDEX



## CUMULATIVE RETURNS FOR THE 23-YEAR PERIOD 1997-2020



can take the worst that the world can throw at it and still survive and grow, despite the unknown and unknowable vicissitudes of life. Just as this pandemic was unknown and unknowable, there will likely be many more of these events over the balance of my investing career.

Instead of giving you a lengthy rationale for investing in Seritage or providing a blow-by-blow account of how things unfolded for the company in 2020, I want to share with you a few essential insights. These insights not only made me confident enough to continue holding the stock, but also to take advantage of the market turmoil in the spring of 2020 to add to our existing position, increasing our stake in Seritage at extraordinarily low prices. It was one of two businesses that we invested in during that tumultuous period. The other was EXOR.

Seritage is not just an owner of retail space in malls for rent to big-box retailers. The company also controls large tracts of land around those malls, with attendant air rights, rights of way, and other permissions. They are located around major transport arteries in the centers of developing suburbs, reflecting the Sears footprint from a century ago, when the company was the Amazon.com of its day. A while back, a friend quipped to me, “Buy land, they’ve stopped making it.” But it matters very much which parcel of land you buy. Location is of paramount importance. If you own a field in an agricultural area of Ohio that’s far from any cities or towns, the value might not change very much for decades.

By contrast, the value of a plot of land that’s close to the center of an urban development can shoot up quite rapidly. It starts slowly as the land changes from agricultural to industrial use. Then, as the use of the land shifts from industrial to retail and then to vertical and mixed

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use, values continue to change dramatically. Today’s deurbanized population wants easy and convenient access to a combination of amenities: home, office, gym, restaurants, coffee shops, and cycle paths. A large number of the Seritage sites, sitting underneath former Sears malls, are located in a nexus of road, transportation, and infrastructure links that make them prime candidates for this sort of mixed-used, vertical development. Think, for example, of Canary Wharf and Nine Elms in London. Useless marshland became urban hinterland, filled with assorted warehouses. Then the land was transformed into a vertical urban and residential landscape, with property values rising to many multiples of their original values.

Another essential insight is that, for as long as there are people in the United States (around 330 million at last count, growing at a rate of 1-2 million per year), the vast majority will want to congregate in places where a nexus of

services and activities already exists. Real estate professionals call this a process of densification. This should lead inexorably to a growing and, in some locations, an exponential demand for land. Despite the shock of the pandemic, this process makes Seritage a sound and attractive proposition for the long term.

In my quest to build resilient wealth, I try to imagine what could negatively impact or derail us along the way. One of the few things I can conceive of that could destroy the long-term value of Seritage would be a large asteroid taking out some (or most) of the US population or the land mass itself. Otherwise, patterns of geographical settlement—including population growth and the process of densification around existing areas—should take care of our upside over the long run. This sort of *deep inevitability* is what I'm looking for in all of our investments. I believe that the majority of our investments meet this criterion.

It's this sort of thinking that makes me wary of many apparently attractive investment ideas that a lot of fund managers now find irresistible. They seem to be willing to pay almost any price for some "sure-fire" winners that have so far proven invulnerable, confirming their faith that these companies can prosper in pretty much any environment. My experience of the first Internet bubble in 1999 leads me to believe that this confidence can quickly disintegrate.

My wariness also extends to countries and regions that are, despite their economic success, authoritarian. Turkey, Russia, and even China are far less attractive to me than what I would term as core markets: Western Europe and North America, plus a handful of others. When it comes to protecting people's right to long-term ownership of economically attractive assets, the

world's capitalist social democracies are much more likely to stand the test of time.

The point is, I'm striving to invest our assets in such a way that we will continue to succeed despite all of my misjudgments and imperfections—and the impossibility of predicting future shocks and setbacks. This approach to investing seems both resilient and realistic. It's also more honest than pretending that I somehow navigated us brilliantly through the dangerous straits of the last year by dint of superior intelligence, predictive powers, and general master-of-the-universe awesomeness.

This is the silver lining that I alluded to earlier. I've told you about all of the things that I failed to foresee and all of the ways in which I failed to act because it's important to emphasize that I take these limitations into account whenever I make an investment. While I was unable to predict the pandemic or accurately assess its impact, the land that Seritage owns and the economic realities underlying that land are more enduring than the pandemic.

None of our other holdings were affected as badly as Seritage, and I have no doubt that it will do extraordinarily well over time. As I write this in the first quarter of 2021, the stock has already more than doubled from its lows in 2020. It should continue to compound over many years, playing a useful role as a long-term component of our all-terrain portfolio.

As with Seritage, the vast majority of the Aquamarine Fund is invested in opportunities where there seems to be a deep inevitability to the long-term outcome. This is the diametric opposite of the type of short-term speculation we've witnessed lately in stocks like GameStop, which has careened between \$2.57 and \$483 per share over the last 12 months.

To give you a clearer sense of how your money is invested, here's a snapshot of our largest positions—at cost and at their current market value—as of December 31, 2020:

Holding	Market Value \$	Percentage of Partners' Capital	Original Cost \$	Gain/ (Loss) \$	Gain(Loss) %
Berkshire Hathaway	43,035,372	15.77%	13,381,800	29,653,572	222%
BYD Auto	40,623,751	14.89%	4,986,800	35,636,951	715%
American Express	25,391,100	9.30%	10,906,129	14,484,971	133%
Mastercard	23,468,805	8.60%	1,019,194	22,449,611	2,203%
Bank of America	23,273,382	8.53%	5,181,863	18,091,519	349%
Ferrari	18,437,896	6.76%	332,807	18,105,089	5,440%
Cash	26,504,927	9.71%			

My plan is not to mess with these positions much, if at all, and simply to let compounding do its thing.

As you may have noticed, one stock missing from our portfolio is Fiat Chrysler, which was recently renamed Stellantis. Fiat gave us a wonderful ride, transforming our initial investment of less than \$10 million into more than \$50 million. The new CEO, Carlos Tavares, will be working hard to reap the benefits of scale while moving the company into an electric and self-driving world. The pressure to pull off that transition will be a constant headwind. With the combined size of Fiat and Peugeot, Stellantis has a far better chance of success. But I think it will be a hard slog and the outcome doesn't seem to me sufficiently inevitable.

As you can see from our 20-fold appreciation in Mastercard, the best thing to do with a long-term compounder is absolutely nothing. Psychologically, it's not easy. But this strikes me as a good example of a situation in which it

makes sense to disregard high current valuations, forget the old adage that “you never lose money by taking a profit,” and ignore the naysayers who deride the apparent sloth and inactivity required to stay patiently on a successful course.

## Cash

In addition to those long-term positions, there are two other components of our portfolio. First, we have a fairly sizeable amount of money in cash. Second, there are starter positions that I'm hoping will turn out to be the long-term compounders of the future.

Why hold cash? Simply put, it's there for a rainy day. It obviously reduces our returns in a heady period like the one we've experienced in recent months. But cash provides us with protection and buying power in the event of a sharp or prolonged market pullback.

Given the valuations and speculative excesses we've seen lately, I'd prefer our cash levels to

be somewhat higher than they are today. But I also know that it's futile for me to try to time the market. From time to time, I do trim larger positions that have performed well to raise cash or to reinvest in other long-term compounders. I am, however, reluctant to do this. Evidence shows that, if we trim our long-term compounders, it hurts our long-term returns.

I've been expecting a market pullback for the best part of the last decade. At some point, I'm sure that we will have higher interest rates and higher inflation—and this may well (but not necessarily) be accompanied by a market decline. While this seems inevitable, I have no idea about the timing. Will it happen this year, next year, or ten years from now? Nobody knows.

If I had sold down our investments every time that fears of a market pullback flared up, we would have performed dismally. We would have sat out most of the bull market over the last decade and would still be waiting in vain for an opportunity to buy our stocks back at a cheaper price. I prefer to remain committed to equities that are highly likely to compound over time, while retaining enough cash to give us the flexibility to buy if things *do* get gnarly.

Our 9% cash position feels fairly comfortable to me, while 20% would feel very comfortable. But I also take comfort from the fact that some of our biggest positions—Berkshire Hathaway, American Express, Bank of America, Wells Fargo, and Mastercard—should all perform extraordinarily well in an environment of higher interest rates, higher inflation, or both. In addition, I take into account that Berkshire recently had about \$160 billion in cash and Treasury bills, which accounts for roughly a third of the company's market value.

## Our starter positions

We also have a few starter positions that might well work out to be multi-bagger investments. One is Care Ratings. I have had a long and largely happy history of investing in rating agencies, having previously owned stakes in Duff & Phelps Ratings (which is now part of Fitch IBCA), Crisil Ratings in India, and Moody's.

Care Ratings is the largest independent rating agency in India. It recently blotted its copybook badly by giving an Indian financial company a much higher rating than it deserved. Care has a lot of catching up to do to reach the standards of some of its competitors. Still, I am optimistic about the company's future. How come?

As with Seritage, I have a basic, core insight with Care Ratings: if we fast forward 50 years to a time when India is the largest English-speaking economy on the planet (who knows what Elon Musk will achieve on Mars), India will want to have a high-quality, homegrown ratings agency that doesn't take orders from New York. I believe that this is an element of national sovereignty, an instrument of soft power. Not only should a truly sovereign nation be able to borrow in its own currency. It should be able to rate its domestic debt instruments and those of other nations. If this insight proves to be correct—and if Care Ratings retains its position—then the company's future will be bright.

In writing about my investment rationale, I'm also happy to express my support publicly for Care Ratings and its leaders—including its highly-regarded CEO, Ajay Mahajan, and its head of business development, Dinesh Sharma. Ajay and Dinesh have a lot of wood to chop, but I'm impressed with what they're doing so far. By openly supporting them and the company,

I hope that I can help to give it a reputational boost. Consider it my version of gentle activism.

### Partnering with the right CEOs

Speaking more broadly, Aquamarine's success hinges largely on the quality of the leaders whom we're partnering with at the companies in our portfolio. I'm not sure that I paid close enough attention to this critical factor in the past, and this caused me to miss a number of extraordinary investment opportunities.

A few years ago, I had a brief conversation with Netflix CEO Reed Hastings at the TED conference in Vancouver. As a dissatisfied international customer, I was snarky and slightly rude. In retrospect, I regret the way I spoke to him and my choice of subject. As I recall this interaction now, what strikes me is his response. Despite my tone, Hastings treated me with respect, making me feel like I was important to him and that my views mattered, no matter how insignificant I actually was. In short, he displayed some of the same personal qualities that I've seen in great leaders like the late Donald Keough, a former board member of Coca-Cola and Berkshire Hathaway, and Jack Byrne, a former CEO of Geico and White Mountains Insurance.

Based on this experience, I should have paid closer attention to Netflix as a potential investment. CEOs like Reed Hastings don't get lucky by chance. If we consider the way he responded to me and repeat it—many times a week and thousands of times a year—it adds up to an extraordinary personal moat. Someone who behaves in this way will develop a large army of people who feel grateful and appreciative and who stand ready to help if called upon. It's an important part of what gives people like him an edge.

Our pantheon of exceptional CEOs with similarly impressive qualities includes Warren Buffett at Berkshire, my Harvard Business School classmate Mark Schneider at Nestlé, John Elkann at EXOR, Ajay Banga at Mastercard, Wang Chuanfu at BYD, and Bryan Moynihan at Bank of America. Each of them has achieved remarkable things for the companies they lead.

I would also include Ben Schall in this list. He was the CEO of Seritage until late 2020 when he left to become CEO of AvalonBay. I was sorry to see him go, but he certainly leaves with my blessings and gratitude. Ben led the company's spin-off out of Sears and did an admirable job of transforming it and enhancing its long-term value. Under his guidance, Seritage dramatically reduced the percentage of its rental income that comes from Sears, and he steered the company into a number of exciting mixed-use projects.

As CEO, Ben interacted with an array of superstars associated with Seritage, including Eddie Lampert, Warren Buffett, Mohnish Pabrai, and Sharon Osberg. So it's not surprising that he was noticed and courted by other first-rate companies. I always want to work with—and invest with—people whose talents, diligence, and achievements make them compelling candidates for other top jobs. Thankfully, another aspect of such stellar CEOs is that they work to make themselves dispensable. Ben built a terrific team at Seritage, and the nature of its assets means that there is still tremendous value even without Ben at the helm.

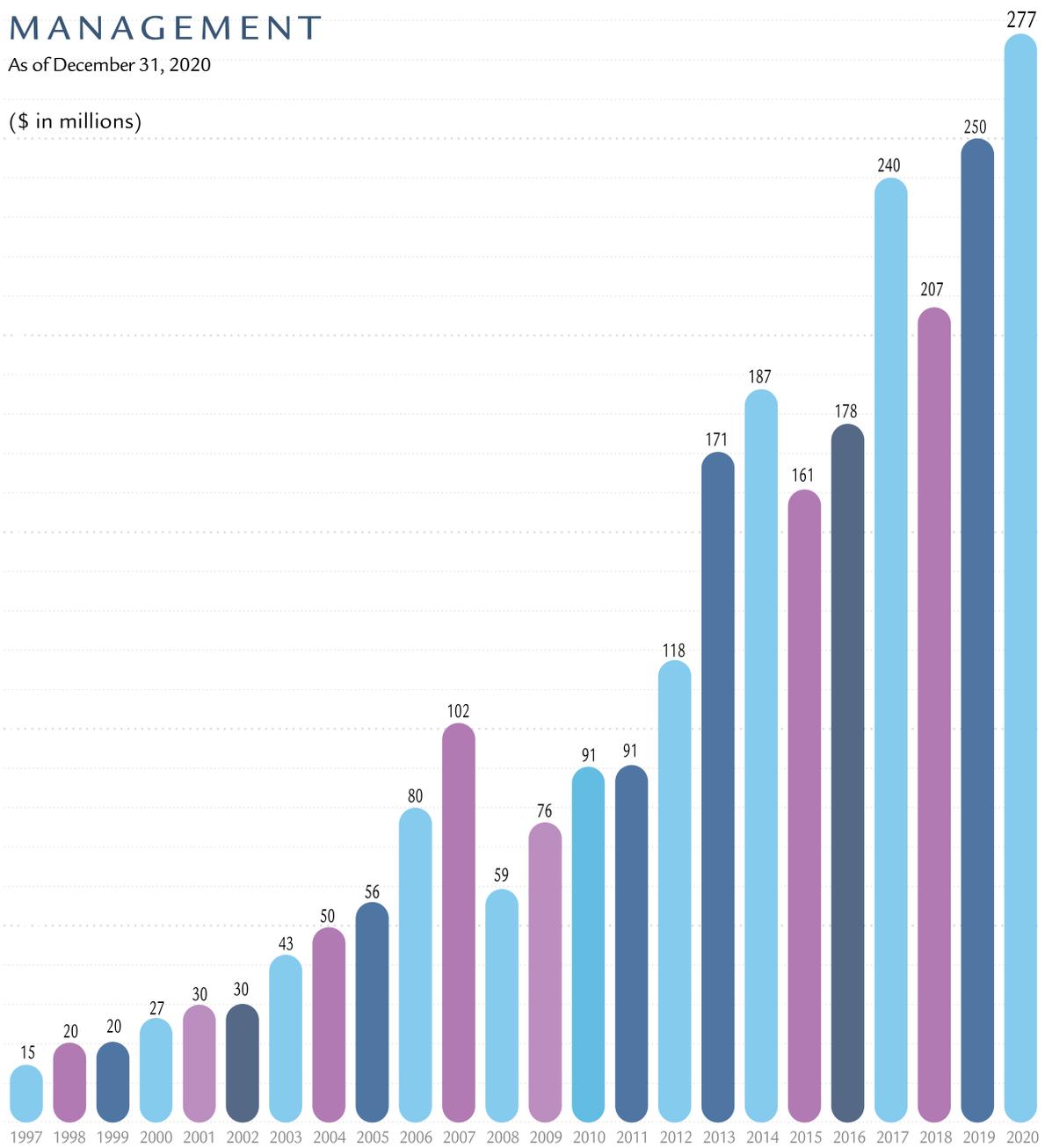
### How is Aquamarine positioned for the future?

If there's one thing we've learned in 2020, it's that none of us knows what the future holds. As I heard Charlie Munger say in a talk last year,

## ASSETS UNDER MANAGEMENT

As of December 31, 2020

(\$ in millions)





I've increasingly come to believe that sustainability should be a central consideration when it comes to selecting stocks. When a company's mission is not in the best interests of the society it serves, it is, in a way, setting itself against that society. At some point, the shareholders may well have to pay to make amends.

"Everybody failed to predict that the pandemic would happen. But now they all want to tell us, authoritatively, what will happen next."

I'm just one human living in Zurich, sometimes reading, sometimes gazing at my Bloomberg monitor, sometimes attending conferences, sometimes exchanging insights with a broad network of highly intelligent people. I'm doing my best, but I often remind myself of how little I know and how little can be known about our world. The forces of nature are just so complex and unpredictable, and the set of possible trajectories is too vast to be knowable.

How can one individual know any better than anybody else what will unfold? How can we be sure that any individual or group of individuals has some special quality of mind or personality or decision-making skills that will ensure superior returns?

Even when it comes to Warren Buffett, there's no way of knowing to what extent his success is attributable to his exceptional abilities and personality. Perhaps the environment that he

was born into and grew up in, just after the Great Depression, was also important. Maybe it was a lucky interaction between the ideal genes and the ideal environment—and if one of them had been missing, the result would have been very different. Warren himself has said that he might have been a manual laborer if he had been born in a different time and place.

Given our own limitations and the fact that the future is so uncertain, how can we invest well? How can we protect our hard-earned wealth and prepare to withstand all of the unknowable disasters that could potentially happen?

Before I share my plans for doing that, I want to look back. A long way back. There is a consensus among some historians that the worst year on record was 536. While the bubonic plague—the pandemic of that era—was raging, an asteroid hit the Earth and caused the sun to be effaced from the sky for 18 months. Crops failed. Many died of starvation, and many more died of the plague. Without wanting to be unduly pessimistic, we need to be prepared for that kind of calamity, instead of assuming that a single disaster strikes and then quickly passes.

My emphasis on surviving exceptionally tough times no doubt has something to do with my own family background, dating back to grim periods like the 1860s and the 1930s. Some of my mother's ancestors came from towns around Manchester, the heart of the Industrial Revolution, where they must have worked in squalid conditions in the nineteenth century. They left in search of a better life in South Africa, then a burgeoning colony of the British Empire. Having landed in Pietermaritzburg, the capital of Natal province, they built a good life for themselves. But it didn't last. The injustices of apartheid caused many of them to leave in search of more just societies, including Australia and the UK. Meanwhile, on my father's side, my ancestors fled from Germany to Israel in the 1930s. In both cases, and with each move, my family had to leave everything behind and start again from scratch.

Why am I telling you this? Because long-term investors can never afford to be complacent. If you're fortunate enough to survive a period like this with your finances and your health intact, it might be tempting to sit back, breathe a sigh of relief, and say, "Well, that was the big one." But the reality is that the big one may be yet to come. And as we know from history, it's usually not the things we worry about that catch us. It's the things that are completely unexpected, the unknown unknowns. With that in mind, I'm trying to remain as vigilant as ever at a time when many investors seem to have let down their guard.

What I also want to share with you are some of the key ingredients that I believe are required to build resilient wealth that will continue to grow through our lifetimes and beyond. It all starts with husbanding a nest egg and investing it in a way that harnesses the power of compounding.

As I've mentioned already, it also involves investing the bulk of your portfolio in businesses where a favorable long-term outcome seems deeply inevitable. In addition, I think it's also of paramount importance to be honest.

As a fund manager and as a stock picker, I need to be brutally honest both with myself and you. This is an idea that I have learned from David Hawkins, the author of *Power vs Force*, and more recently from the Canadian professor and writer Jordan Peterson. As Peterson explains, if we make honesty our practice, we are setting ourselves in alignment with reality—even if we don't know exactly what reality is. By contrast, if we lie or even just allow mistruths to get through, we are setting ourselves against the reality of the universe. And in that contest, there is no doubt that the universe is more powerful.

Writing to you honestly about my limitations, mistakes, and uncertainty about the future is important not just out of some highfalutin desire to be truthful and forthright—although it is that, too. It's because honesty is the best tool if my goal is truly to build a resilient future for Aquamarine, creating something that will stand the test of time. Some readers will not like this. They would prefer some sugarcoating, some soothing sales-speak, some reassuring veneer of authority and wisdom. But a small percentage of investors will be drawn to unvarnished candor. If you're one of them, welcome. I think we can do great things together.

As for our investments, I've already mentioned the type of businesses that I look for and the national jurisdictions where I'm most comfortable investing. I would add that I've increasingly come to believe that sustainability should also be a central consideration when it comes to selecting stocks. My view is that all

intelligent investing is sustainable investing. One of the best ways to reduce our fragility and minimize our risk is to invest sustainably.

Essentially, this is a recognition that, for a company to thrive over a long period, it will sooner or later have to align itself with the best interests of humanity. It's not enough for the leader of a business simply to maximize shareholder wealth within the current legal and ethical framework, assuming that this framework will remain fixed. For example, we can't rule out the possibility that a gunmaker will, in the future, be held liable for the deaths caused by the guns it produces. When a company's mission is not in the best interests of the society it serves, it is, in a way, setting itself against that society. At some point, the shareholders may well have to pay to make amends.

For this reason, we want to own businesses that are not only a win-win for their immediate ecosystem: customers, suppliers, employees, and others. We want to invest in businesses whose mission is, in the broadest sense, to make civilization better.

If we put businesses on a moral spectrum, at one end we'd have industries like tobacco, gambling, and brothels (yes, there is at least one publicly traded brothel company). At the other end, we'd have companies like Tesla and SpaceX, whose high-minded mission is to move humanity forward to a more compelling future. It took me a long while to come to understand Tesla in this dynamic regulatory context—one where the company aligns itself with a political sentiment in moving us to a carbon-free economy. Mission-driven companies don't necessarily need such lofty goals. Costco, for one, has a simpler mission, as do Care Ratings and Berkshire Hathaway. But they are still worthy missions.

These are companies that are seeking to create a better future, rather than just maintaining the status quo.

Looking back, I realize how blinkered I was when I studied economics at college. I bought into Adam Smith and the invisible hand so completely that I failed to see that a business can be more than just a player on the field. Businesses can shape the field or move the goalposts. Businesses can (and increasingly should) be a powerful moral force in society, seeking to build a better, fairer, more gentle society. This ethos also provides an extra layer of protection for investors, expanding their margin of safety and bolstering their portfolio's anti-fragility.

### Our mission at Aquamarine

While I will never be Elon Musk and Aquamarine will never be Tesla, we do have worthy goals—an honorable mission that I believe in wholeheartedly. It starts with compounding wealth for our investors in a prudent and responsible way, while always operating in an honest, ethical, and transparent manner, so that partners in our fund can sleep well at night. We want to achieve this compounding of wealth by aligning ourselves with first-rate people. That includes great CEOs and management teams, a great community of suppliers, and great partners. We want to enrich all of our stakeholders' lives in a way that is (gulp) sustainable.

That means we are also in the business of helping to build businesses that improve the world. Take, for example, Care Ratings. Over time, I believe that Care Ratings will enable India to project its soft power and will be a business that Indians all over the world can be proud of. As a committed shareholder and long-term partner in the business, I look forward to playing my

part in making that happen. In that regard, I'm enormously impressed by the mission at EXOR and the culture that John Elkann is creating there. On the front of EXOR's presentation to investors is the phrase "We Build Businesses." I like that a lot.

In our own small way, I'd like to think that we are also building businesses, creating an environment in which some of the world's best companies can flourish. In doing so, I hope that we can help all of the stakeholders to build better lives and a better future. Ultimately, I also hope that the businesses we invest in will feel proud to include us among their investors.

This mindset may sound idealistic or naive, but I don't think it is. Those of us who are in positions of influence have a responsibility to do what we can to help build societies that are full of opportunity, that treat people fairly, and that have good safety nets. This isn't just a moral and laudable goal. It's also the best way to protect against the calamities that can come from social inequality and instability—an enduring historical lesson that my family and millions of others learned from the injustices that spurred the rise of Nazism in Germany and from the appalling injustices of apartheid-era South Africa.

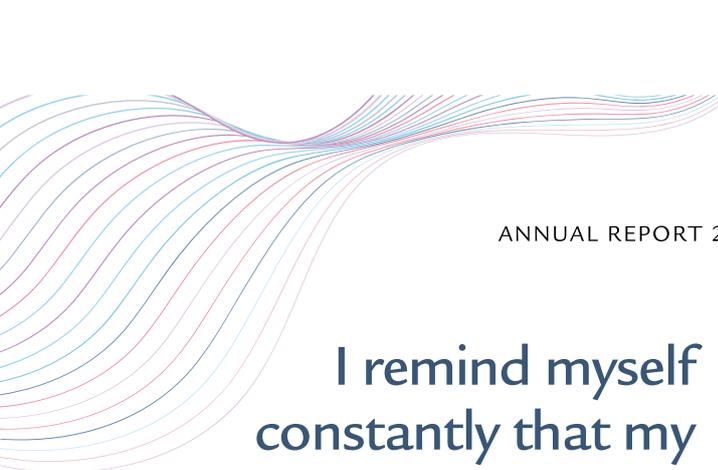
### Crypto, FOMO, and the perils of envy

I have watched with fascination the recent rise and rise of Bitcoin. One key to the long-term compounding of wealth is to continue to invest in what I understand, and not to invest in what I don't understand. The key point about crypto that I've made on various occasions is that, unlike a farm or a building or some other tangible asset that can generate cash flows, Bitcoin does not and cannot generate cash flows. As such, it's not

The key point about crypto is that, unlike a farm or a building or some other tangible asset that can generate cash flows, Bitcoin does not and cannot generate cash flows. As such, it's not an asset that I can analyze.

an asset (if it is an asset) that I can analyze. That's the reason that I have not even considered it for investment.

However, the more I have read about it, the less confident I am that its end price will be zero (although it might well be). Bitcoin stands at the very center of the crypto-currency universe and there is an enormous amount of physical, computing infrastructure that is invested into its success. So it might well succeed. But I still can't value it, so it's not an investable asset for me. The broader point is this: if you plan on being a successful investor over many decades, then there will regularly be one group or another that is getting rich at a much faster rate than you. And, of course, that group tends to speak loudly and proudly about its superior insight and success.



I remind myself constantly that my principal responsibility is to build wealth prudently for all of the partners of Aquamarine. I always take great delight in the fact that your family and my family are on the same side, and that I'm only compensated if I perform well on your behalf.

My approach is to simply be okay with that. Ultimately, people getting wealthier is a good thing, and I'm delighted to have many more people joining the ranks of the rich. What's important is that we can't allow envy or a fear of missing out to knock us off our chosen path. Our path may seem slower (at least, in the short term), but it's likely to be more resilient and more profitable in the long term. It's helpful to recognize that we're playing a very different and much less speculative game in which patience is likely to deliver much richer rewards.

### Aquamarine's value proposition

As I write to you each year, I remind myself constantly that my principal responsibility is to build wealth prudently for all of the partners of Aquamarine. I always take great delight in the fact that your family and my family are on the same side, and that I'm compensated only if I perform well on your behalf. I continue to believe that the Aquamarine Fund offers exceptional value to its investors, and I've explained many times before that the Aquamarine value-add is built on three pillars:

- Low and often zero management fees.
- Alignment of your interests and mine, so the fund is truly structured as a partnership.
- A conservative, long-term, value-oriented strategy in which we partner with the best businesses we can find, compounding wealth in a disciplined and durable manner.

### Assets under management, subscriptions, and redemptions

In 2020, we received \$7.2 million in new capital and received redemption requests for \$7.6 million. I regard this as part of the normal ebb and flow of assets as our investors' life circumstances change. I'm always sorry to see investors redeem, but it gives me deep satisfaction to see friends and family benefiting from the appreciation of their holdings in the Aquamarine Fund. We ended 2020 with \$277 million in assets, which gives us sufficient scale to run the fund comfortably, but still allows us the trading flexibility to react nimbly.

### Thanks

I feel extremely fortunate to have such a remarkable group of shareholders. The Aquamarine Fund's

base of sophisticated and faithful partners has stood firm over many years, enabling us to take advantage of the great buying opportunities that arise during times of heightened uncertainty and instability, just as we saw in 2020.

Most of the partners in our fund came to us through recommendations from existing shareholders who were pleased with our performance and our ethos. If you know of someone who might benefit from investing in the Aquamarine Fund, please don't be shy about introducing them. Feel free to contact me about referrals or anything else by calling +41 44 210 1900 or +1 212 716 1350 or via email at [investorservices@aquamarinefund.com](mailto:investorservices@aquamarinefund.com).

I am happy with the current size of the fund and have no interest in promoting it merely in the hope of growing bigger. Naturally, I'm always pleased to partner with the right shareholders: that is to say, patient, value-oriented, long-term investors who'd like to join us in compounding wealth over many years, without unnecessary risk.

I'm particularly delighted to partner with investors who have valuable experiences, insights, and networks of their own—for example, people who have started their own businesses or who have run divisions of larger corporations. I've enjoyed an ongoing dialogue with many of our partners about different industries and companies and have found their views extremely thoughtful and enlightening. Whenever we can welcome such people into the Aquamarine fold, I regard them as a very valuable addition.

While I was unable to travel much in 2020, I learned a lot and shared some of these new lessons in my podcast series, which (like my book) is called *The Education of a Value Investor*. Some of the 14 interviews that I did for the podcast were with people associated with the fund. I hope you enjoy

these podcasts and will continue to join me in sharing your insights.

Thank you for joining me on this journey. I would like to think that I'm now approximately halfway through my career as the manager of the Aquamarine Fund. If the next 23 years match the last 23, Aquamarine's original investors will make about 68 times their money over 46 years. That's not a Buffett number, but we're off to a solid start. I will be working hard over the next 23 years to be worthy of, and to reward, the faith you have placed in me.

Warm regards,

A handwritten signature in black ink, appearing to read "Guy Spier". The signature is fluid and cursive, with a large initial "G" and "S".

Guy Spier  
Managing Partner