Q3 2019 Investor Letter | October 21, 2019

Dear Investor,

For the nine months ended September 30th 2019, the Bonsai Partners portfolio increased by 60.3% after fees, and since inception, total net returns were 31.3%. Gross and net returns are shown below.

At the end of the third quarter, the portfolio was 75% invested and 25% remained in cash. Since inception, our average exposure was 59% invested and 41% in cash. We don't use leverage.

Bonsai Partners Historical Returns Summary

	YTD 2019	2018	Since Inception
Bonsai Gross Return	65.0%	-17.9%	35.3%
Bonsai Net Return	60.3%	-18.1%	31.3%
S&P 500 Return	20.4%	-8.6%	9.6%

Performance data shown represents past performance. Past performance is not indicative of future results. The period October 22, 2018, to April 30, 2021, presents time-weighted returns of a representative Bonsai Partners, LLC ("Bonsai") managed account with the same strategy and risk profile as Bonsai Partners Fund, LP, (the "Fund") which launched on May 1, 2021. Results from May 1, 2021, reflect the time-weighted returns of Class A shares of the Fund.

Gross returns from October 2018 to April 2021 include transaction and commission fees. Gross returns from May 2021 to the present include transaction and commission fees and fund operating expenses, such as administrative and audit fees but do not include management or performance fees. Net returns reflect the gross returns (as described) reduced by a 1.0% management fee and a 10.0% performance fee above a 6.0% cumulative compounding hurdle.

All performance figures are calculated internally by Bonsai Partners and are therefore estimated, unaudited, and subject to adjustment. The investment return and principal value of an investment with the Fund will fluctuate so that an investment, when redeemed, may be worth more or less than its original cost. Actual performance for a particular investor may be lower or higher than quoted performance due to different fee structures, share classes, beginning periods, capital additions or withdrawals, or individual compliance related mandates. Please refer to important additional disclosures at the end of this letter.

While these initial results compare favorably to our benchmark, our cash position has been a drag on performance. In this low-interest-rate / high-equity-return environment, cash doesn't feel like king. Simply put, I have not been able to find enough good opportunities for us to be fully invested. That said, I would rather do nothing than make mistakes.

Asset prices are high, and this is the biggest factor stopping us from making new investments. Valuations are elevated for many high-quality companies, and this puts prudent buyers in a difficult position. Seeking rational prices while not compromising on business quality is a narrow tight-rope walk.

Investing isn’t a single factor game where you hunt for the best businesses, buy their shares, and call it a day. Instead, price is the great equalizer of quality. High prices act like gravity; dragging down the underlying returns that these companies generate. If not careful, this countervailing force can push investment returns into average or below-average territory while also introducing significant risks.

I know this sounds old-fashioned, but unless conservative model assumptions offer attractive returns, I am just not interested.

If you have noticed our reporting has gotten simpler, you are right. I have removed the MSCI All Country World Index (ACWI) benchmark from our reporting because it is unwise to compare myself to two different benchmarks simultaneously. Doing so invites you to compare me to whatever is doing better at that point in time rather than compare me to the most reasonable alternative. I figure the S&P 500 is a good enough approximation of the real-time ‘opportunity cost’ for you since it is the most widely held public stock index in the U.S. that you can easily and cheaply acquire instead. We will use that going forward despite obvious differences in approach.

I have no idea what our returns will look like over the next twelve months, and that will always be the case. Equity markets continue to appreciate at a rapid clip, and while I did not expect this to happen, nothing surprises me anymore. We now live in a low/negative interest rate environment, which is just another reminder to avoid applying yesterday’s assumptions to the future. I believe we stand to lose more by trying to predict a market correction than actually being involved in one, so I will keep looking for attractive investments in the meanwhile.

Portfolio Review

While our headline performance was "in-line with the market," two of our positions did see larger swings in their valuations. I provide an update below.

From a trading perspective, we did not add any new investments or sell-out of any existing ones during the quarter. However, we trimmed one position and added to another.

The portfolio may not look dramatically different compared to the prior quarter, but our pipeline of new ideas is getting better.

From a portfolio management standpoint, it was never my intention to have just three investments, but truly good ideas with reasonable valuations have been rare (for me at least). I hope to share additional investments over the coming quarters, but of course, I can't promise anything.

Position Update

Aspen Aerogels (NYSE: ASPN):

Our position in Aspen Aerogels declined approximately -17% in the third quarter. Aspen is a thinly traded stock and considering it appreciated ~185% last quarter, I'm not too concerned. I found Aspen's second-quarter results to be lackluster, and this probably contributed as well.

Although their second quarter wasn't a make-or-break period for the company, Aspen was supposed to show improvement in their operating model, yet their second-quarter gross profit margin came in below what I expected. Management laid out a laundry list of one-off reasons why this happened, and hopefully the third-quarter will be better. Further, I remain interested in their advances in lithium-ion battery technology and hope they find a partner soon.

We will see how these developments play out over the next couple of quarters.

Redbubble (ASX: RBL):

Redbubble was a bright spot for us this quarter as shares appreciated ~64%. This movement came after the company reported its second calendar quarter results, which also happened to be its 2019 fiscal year-end. The business continues to grow nicely with revenue growth of 44% and gross profit after paid acquisition costs (known as "GPAPA") growth of 48%. The company also reported an important milestone: its first year of EBITDA profitability.

In a world where high-growth / cash-burning technology businesses are rewarded with nosebleed valuations, Redbubble stands out. It is a business growing well, not burning a barn full of cash to do so, and is available at a reasonable valuation.

I'd also argue that Redbubble's two-sided marketplace is a more attractive business model than many high-flying technology companies I've evaluated. Hopefully, other investors will agree with me later.

During the quarter I finally had a chance to connect with Redbubble's management team, which left me with a few positive impressions: 1) they are competent, 2) they appear honest, and 3) their incentives are aligned with ours. This combination is harder to find than you would think.

Travelsky Technologies (HKEX: 0696):

Our Travelsky position appreciated approximately 4% at quarter's end despite some intra-quarter volatility. The ongoing trade war and Hong Kong unrest caused some concern for the outlook of Chinese air travel growth, of which the company is directly linked. Despite these media headlines, Travelsky's reported passenger growth continued to be robust. In July, reported passenger growth was ~9%, followed by ~7% in August. These are pretty good figures considering this growth is off of a base of nearly 620 million passengers who flew domestically in China last year.

While a slowdown in Chinese air passenger growth is possible over the short to medium term, the long-term trend remains clearer.

Concluding Thoughts

It's hard to believe that the first anniversary of Bonsai Partners is right around the corner (technically tomorrow). None of this would be possible without your support. I deeply value your partnership.

If you have any questions or comments, please don't hesitate to call or email me.

Fondly,

Andrew

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Disclaimer:

Bonsai Partners, LLC (“Bonsai”) is the investment manager of Bonsai Partners Fund, LP (the “Fund”).

This letter has been updated from its original version. Disclaimers were revised to reflect current standards and clarifications for the intended audience. Certain visual elements, formatting and brand identifiers have been refreshed to align with our current branding. These changes do not alter the core message of the original letter.

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