Noah Investment Management Co., Ltd.

2023 Annual Letter

Performance

Year	Noah Investment Management	KOSPI
2020 (2020.12.03 ~)	+3.1%	+7.4%
2021	+18.5%	+3.6%
2022	-17.8%	-24.9%
2023	+29.8%	+18.7%
Cumulative (2020.12.03 ~ 2023.12.31)	+30.1%	-0.8%

(Professional investor type, time-weighted return, excluding IPO products)

In 2023, our annual return was +29.8% and our cumulative return reached +30.1%, outperforming the KOSPI index by 11.1% and 30.9%, respectively. Compared to the KOSDAQ—which rose more than KOSPI in 2023 (1-year +27.6%, cumulative -3.6%)—we outperformed by 2.5% for the year and 33.7% cumulatively. Just as I wrote in last year's letter when we incurred losses, I believe there is no need to over-interpret a single year's results, whether positive or negative. Since performance differences arise depending on which benchmark index is selected, comparisons against an index do not carry great significance either. I initially deliberated over benchmark selection—there are excellent alternatives such as the S&P 500, and the KOSDAQ, which contains many of our actual portfolio companies and has similar volatility. However, since we invest only in domestic companies and considering that an amateur client could most easily choose Samsung Electronics as an alternative, I decided to use the KOSPI index—which has a high correlation with Samsung Electronics—as our benchmark. Nonetheless, I remain skeptical about the meaning of index comparisons themselves. I think last year's marathon analogy, considering our 20-year target horizon, is more apt: 'We are currently passing the 6.5 km mark in the race; our pace has quickened in recent segments and we are in the lead group, but due to unfavorable conditions such as weather, our overall race time remains somewhat slow.'

Cash Ratio

A notable aspect of our 2023 performance is that it was achieved amid an unusually high cash allocation. The approximate annual average cash ratio for 2023, calculated roughly using month-end averages, was about 38%. The increase in cash was not a deliberate adjustment based on a negative market outlook, but rather the result of not finding sufficient investment targets after realizing gains on certain positions. In the financial investment industry, it is generally expected that when managing a portion of a client's portfolio, one should be 100% invested, since clients maintain their own separate cash allocations. In hindsight, had we been 100% invested, our 2023 returns would have been significantly higher. However, since our goal is to achieve high returns over the long term, we did not invest in targets where we could not expect returns exceeding that threshold. I believe that difficult goals can only be achieved through prolonged patience and concentration on investment targets that meet our criteria. From this perspective, if the result of decision-making aimed at maximizing client returns is 'cash,' then I believe it was right not to force-buy

stocks even with a knife to my throat. Fortunately, we are neither a fund that must worry about external scrutiny over cash ratios nor a structure that needs to generate trading commissions, so we can maintain a high cash ratio for several years or more. (A high cash ratio itself is not a sin.)

However, my role is not to secure a high cash position (since macroeconomic forecasting is impossible), but to find outstanding investment targets under any circumstances and maximize returns. In 2023, I invested across several companies that could barely achieve our target return, and sold some of them as my thinking changed. Finding an outstanding company worthy of concentration remained difficult. Most of my days are spent turning over as many stones as possible, and if I find something underneath, I pull out a magnifying glass to examine it closely. If it piques my interest, I bring out a microscope for further study; if not, I move on to flip the next stone. In 2023, I turned over stones to the best of my ability given the circumstances, but my performance in the role of finding outstanding companies was not particularly good—hence the high cash ratio. Therefore, this year's gold medal for failure goes to my inability to fulfill that role sufficiently. (I reflect on the causes of the high cash ratio.)

In my experience, a given year's investment performance is often the result of the previous year's efforts. Therefore, since the shortcomings of 2023 are likely to manifest in 2024's performance, it seems necessary to lower expectations for this year. However, I intend to fulfill my role this year for the sake of 2025's results. Fortunately, looking at Warren Buffett's 2022 shareholder letter, it appears there is ample time to recover.

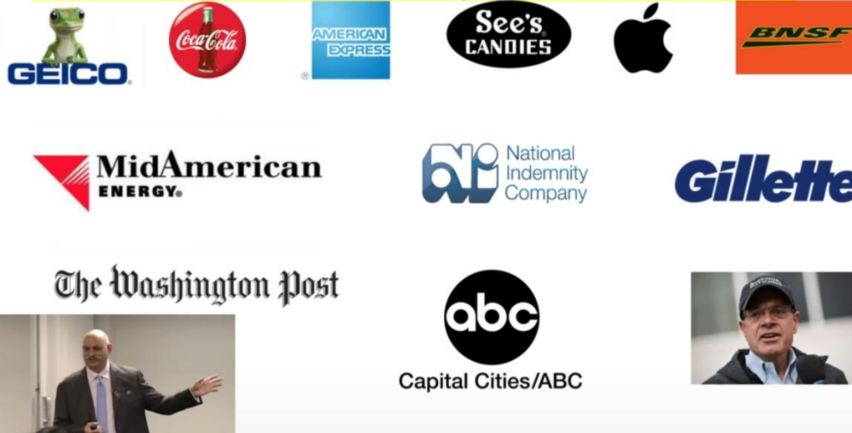
Once Every 5 Years

In his 2022 shareholder letter (written in 2023), Warren Buffett wrote the following:

> *"Over the years, I have made many mistakes. Consequently, our extensive collection of businesses currently consists of a few enterprises that have truly extraordinary economics, many that enjoy very good economic characteristics, and a large group that are marginal... In 58 years of Berkshire management, most of my capital-allocation decisions have been no better than so-so.... Our satisfactory results have been the product of about a dozen truly good decisions – that would be about one every five years"*

Source: Berkshire Hathaway 2022 Shareholder Letter

What made him who he is today were 12 outstanding decisions over 58 years; the rest were merely so-so decisions. In other words, outstanding decisions appeared on average once every five years. As I mentioned earlier, having failed to find a single outstanding company in 2023, this was an enormously comforting passage for me. Indeed, once every five years is sufficient. What we should focus on is contemplating how outstanding decisions are made—not regretting or feeling anxious about not finding investment targets quickly. According to Mohnish Pabrai's estimates, Buffett made approximately 300 investment decisions over 58 years, of which only 12—that is, 4%—were outstanding, while the remaining 96% were, in Buffett's own words, merely so-so (by Buffett's standards, a 'so-so decision' likely means roughly market-average performance). The 12 outstanding decisions Pabrai identifies are as follows.



Source: https://www.youtube.com/watch?v=SP6kKi2nMz4&t=199s

While contemplating how once-every-five-years outstanding decisions are made, I came across a passage in the book Empower Your Investing (Scott A. Chapman) describing the circumstances at the time Buffett made his outstanding decisions. This piqued my interest, and I separately looked up the financial statements and reports of the investment targets from that era.

Buffett's most iconic outstanding decision is GEICO. The GEICO investment story I had encountered through books was roughly: 'In his 20s, he showed up at GEICO unannounced, received a detailed explanation from an executive, understood the insurance industry and the company's business model, invested for the long term when the company was in trouble, and it has since become a great company.' However, when Buffett invested in GEICO in 1976, the company was suffering from deteriorating profitability due to surging claims costs caused by rapid inflation that began in 1974, and from plummeting bond values as interest rates rose to 13%. The situation at the time can be summarized as follows:

- Operating loss of $126.5 million in the prior year. Remaining capital of $36.9 million—i.e., on the verge of capital impairment
- Insufficient loss reserves—i.e., potentially unable to pay claims to policyholders
- Trading halted for approximately 2 months
- Stock price fell from $61 to $2. Fear of bankruptcy. CEO resigned
- Inflation and interest rates remained high

According to The Psychology of Money (Morgan Housel), the majority of Benjamin Graham—Buffett's mentor—'s investment success came from a single stock, GEICO, in which he invested by breaking his own rules. Graham reportedly never sold GEICO even after retirement. If true, ironically, Graham passed away in 1976—the very year GEICO's value had fallen 97% from its peak. At the time, Warren Buffett was also reportedly very surprised after calculating GEICO's loss reserves himself and discovering they were insufficient. If I were transported back to that time, even possessing Buffett's level of business understanding and valuation insight, I do not think I could have invested in an insurance company on the verge of capital impairment that might be unable to pay claims. I would not have been able to overcome the fear of bankruptcy.

American Express presents a similar case. The situation at American Express when Buffett invested was as follows:

- $150 million loan fraud at a subsidiary
- American Express's capital at the time: $83 million; annual earnings: $12 million—meaning the subsidiary fraud/bankruptcy exceeded shareholders' equity and was larger than 10 years' worth of earnings. However, there was no legal obligation to compensate

- As a Joint Stock Association, if it went bankrupt, shareholders would have to repay the debts

The situation was similar to the recent Taeyoung Engineering & Construction PF (project finance) insolvency issue in Korea. The PF debts of Taeyoung Construction—a subsidiary on the brink of bankruptcy—carry no legal responsibility for the major shareholder YTM Holdings, yet public sentiment and government pressure have prevented the major shareholder from avoiding responsibility. To use a financial company analogy: imagine KB Savings Bank, a subsidiary of KB Financial Group, going bankrupt with debts exceeding KB Group's entire capital. There is no legal liability for the subsidiary's debts, but if responsibility were assumed, it would be enough to cause capital impairment for the entire KB Group.

Investing in American Express at that time meant taking on far greater risk than a simple investment. Something I learned through this research is that American Express at the time was not structured as a 'corporation' but as a 'Joint Stock Association.' While a corporation's shareholders bear limited liability only up to their invested capital, in a Joint Stock Association, investors bear liability for the company's debts as well. Apparently, such corporate structures existed among publicly listed companies in 1964. In other words, if American Express went bankrupt, its shareholders would not merely lose their entire investment—they would additionally have to repay debts. In this structure, a subsidiary fraud exceeding the company's entire capital had occurred. In this situation, most shareholders sold their stock, while Buffett bought with 40% of his managed assets.

Buffett's GEICO and American Express investments are well known, and I had encountered them many times. But through this study, by placing my current self in those historical situations and thinking honestly, I came to understand that the ability to maintain rational judgment without being overwhelmed by fear in extreme circumstances is the core element that an ordinary investor like me cannot easily replicate.

Behind successful decisions, there must have been a clear understanding of the favorability of expected value—the combination of probability and outcome of scenarios other than the worst case (e.g., bankruptcy), weighed against the probability and outcome of the worst case itself. I believe this capacity for understanding can be developed to a necessary level through effort. However, whether one can bet according to expected value amid the fear felt when the absolute magnitude of potential loss is overwhelming—that is an entirely different domain of ability, one that cannot easily be replicated through effort alone. Fear paralyzes probabilistic thinking. In a game where you lose all (or even more than) your investment if a company goes bankrupt, even a very small probability overwhelms you due to the magnitude of the loss, shutting down probability-based thinking. And I believe this fear is reinforced by the desire to avoid loss, the urge to protect what one has—or to put it more bluntly, attachment to money.

After personal reflection, my conclusion is that the only path to eliminating the fear that obstructs rational decision-making is to separate oneself from the numbers in the account. By separating myself from the numbers in the account—making decisions as if a third party were playing a game—only then can one make concentrated bets when opportunities arise amid fear, and produce outstanding decisions and results like Buffett's 12. Of course, separating oneself from the numbers in the account is an extremely difficult—perhaps impossible—challenge. But without the shift in perspective that 'the numbers in the account have nothing to do with me,' 'it's okay to fail,' 'it's a game'—how could one, like John Templeton, increase their investment in Union Carbide immediately after a gas leak at a pesticide plant killed 1,600 people and injured 50,000?[1] A new challenge has begun.

I would like to add patience as an essential element of outstanding decision-making. Patience may seem obvious, but we need to reconsider the level of patience that produced Buffett's outstanding decisions. Buffett spent 3 years buying American Express and 6 years buying Blue Chip Stamps. He made his first investment in Coca-Cola 50 years after first taking an interest in it (with the joke that he'd buy a little sooner next time). Charlie Munger read Barron's magazine every week for over 40 years in search of investment ideas. The one idea he found came 30 years after he first started reading Barron's, and even after that, he continued reading it weekly for over 10 more years without finding another investment idea. Thus,

outstanding decisions are not made in a single moment—they are forged over long periods accompanied by an extraordinary level of patience.

I first encountered the company in which I am currently making a concentrated investment six years ago. At the time, I was interested in its new business, but the market had already priced in an overly optimistic future, causing the stock to surge, so I did not invest. However, I continued monitoring it annually, and over the following five years, the new business grew steadily to a scale that could transform the company's fundamentals, while the stock price kept declining—making it more attractive than five years prior. It still did not meet my valuation criteria, but honestly, I congratulated myself for having been patient for five years and impatiently bought a large position. Shortly after, the overall market declined, dragging the stock price down sharply. By the time it fell to an attractive price that could sufficiently achieve our target return, I had already nearly maxed out my position and had to settle for adding only a small amount. I had been patient for quite a long time, but my level of patience was insufficient. I am still invested in this position and it is in profit territory; had I maintained a sufficiently high level of patience without compromise, I would already be enjoying substantial gains.

In short, with a high level of patience combined with separating oneself from the numbers in the account, making outstanding decisions when opportunities arise amid fear—once every five years is sufficient.

0% Management Fee

Noah Investment Management charges no management fee. A management fee is a fee (typically around 1%) charged annually from client assets regardless of investment performance, and it is standard practice in the discretionary investment management and asset management industries. In truth, a management fee is an enormous temptation from the manager's perspective. With a 1% management fee and 100 billion won in assets under management, 1 billion won in fee revenue is generated annually. That is, as AUM grows, stable cash flow is generated to sustain the business regardless of market fluctuations.

One of the most challenging characteristics of equity investing is market volatility. From the perspective of someone who must bear personnel and operating costs every year, it is understandable that the more market volatility one experiences, the more desperate one becomes for management fees. However, the problem with management fees is that when a client incurs losses, the manager still generates revenue. That is, interests are misaligned. This is why Warren Buffett did not charge a management fee when running his partnership, and I am doing the same.

To avoid being affected by market volatility while not charging a management fee, one must minimize fixed costs. When Buffett first ran his partnership, he worked from his home study and shared the family telephone. Even when his assets under management exceeded approximately 40 billion won in today's value and he had over 100 clients, he personally handled account openings, dividend remittances, tax processing, and mailing. He operated alone from home for seven years before finally getting an office in 1962.[2] Li Lu ran his fund alone for eight years; only when AUM reached approximately 250 billion won in today's terms did he hire his first employee.[3] Robert Vinall also worked alone from his bedroom for over five years, during which his largest expense was purchasing a Jura coffee machine.[4] (My biggest capital expenditure was also a Jura coffee machine—I only learned much later that Vinall had done the same.) These investment masters behaved this way because they understood how important minimizing fixed costs is to overcoming market volatility and aligning interests with clients without charging management fees. And it is the reason why someone inferior to them in every way—me—toils alone in a small officetel far from Yeouido, processing receipts.

Of course, having a fair fee structure is not everything. No matter how hygienic a restaurant is, what good is it if the food tastes bad? I will strive not to become a restaurant that is merely hygienic.

[2] The Snowball, Korean edition 2021, p.457
[3] "No other investor has a life story quite as unbelievable as Li Lu," Financial Times, 7 September 2023

[4] "Some thoughts on becoming an independent fund manager," Robert Vinall, Kilchberg, 3 February 2014

1970s

With inflation becoming a hot topic recently, I read several books discussing the 1970s, and found the investment environment of that era strikingly different from the period I have experienced as an investor. To better understand the 1970s, I needed to understand the preceding era, which naturally led me to survey—at least in broad strokes—the flow of capitalism over the past 100 years. Looking at the Dow Jones index over the past 100 years on a log scale adjusted for inflation, the chart appears as follows.

Source: https://www.macrotrends.net/1319/dow-jones-100-year-historical-chart

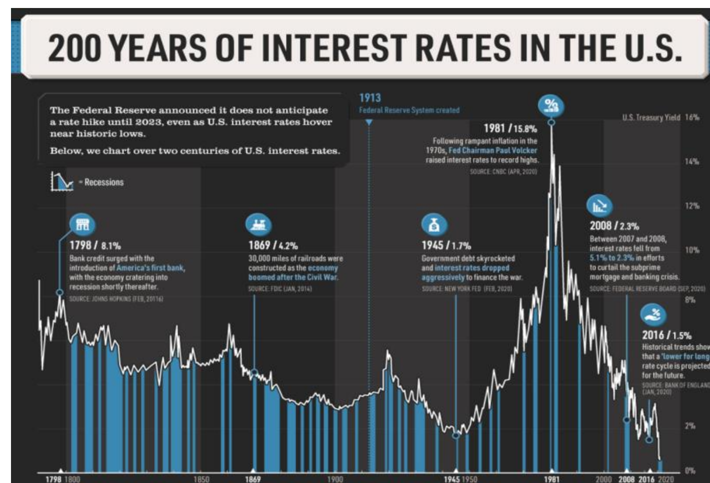
Somewhat subjectively, the past 100 years of the stock market can be divided by trend changes lasting three or more years (marked in red):

1. 1920s: Super rally (post-World War I)
2. 1930–1949: Era of turmoil (Great Depression and World War II)
3. 1950–1969: Secular bull market
4. 1970s: Secular bear market (inflation, high interest rates)
5. 1980–Present: Super rally

Since 1980, there have been sharp but short corrections—the IT bubble, the financial crisis, COVID—but for the past 40 years, the market has generally continued to rise (coinciding with the period I have been alive). The 15 years since 2008 in particular have been a super rally period (coinciding with my active investing career). However, this 40-year secular bull market was not a given in history. The preceding 1970s was an era of historically high inflation and interest rates—a decade of stagnation brought on by the aftermath of 20 years of asset appreciation, high inflation, and high rates. There was a collapse of the real estate development bubble that had boomed for 20 years; the stock market moved sideways with repeated ups and downs for a decade; and real assets, adjusted for inflation, continuously shrank. It was also the brutal period when Charlie Munger recorded -50% over two years.

What must have caused investors of that era more anguish than the magnitude of declines was the duration—ten years. Before the 1970s, there was an even longer and more brutal period: 1930–1949. It so happens that the person who began investing in earnest in 1950—right after the most brutal period ended—wound down his investment partnership just before the 1970s, and has slightly outperformed the market during the steep ascent since the 1980s, is Warren Buffett—and that is his track record. From the

1980s to the present, there has been no brutally prolonged period. The IT bubble burst, the 2008 financial crisis, and the COVID crisis were historically significant declines in magnitude, but their duration was two years or less. Most Korean investors, myself included, have never experienced a downturn lasting more than two years. Is this the result of sophisticated economic system management as the U.S. Federal Reserve's macroeconomic stewardship has become swifter and more precise? If so, our lives at the frontier of economic markets will continue to be pleasant. But what if it was the effect of 40 years of low inflation and declining interest rates since 1980?



Source: https://advisor.visualcapitalist.com/us-interest-rates/

If so, there is a probability that at some point in our remaining lifetimes, we will experience a brutal period like the 1970s.

We cannot know what the future holds, but what is certain is that having an investing career that coincides entirely with the super rally since 2008 is something to be truly grateful for, and that—as Buffett and Munger kept emphasizing in the late 1960s—we must lower our expectations going forward.

Goodbye Munger

The revered Charlie Munger passed away 33 days before his 100th birthday. Through Pabrai's YouTube channel, I had heard that the living gurus, including Buffett, were gathering for a party on his 100th birthday, and I was eagerly awaiting news—but he departed with about a month to go. Seven years ago, after obtaining the original edition of the only book Munger was involved with and struggling through his unfamiliar vocabulary, I became his devotee. Since then, I felt emotionally closer to him than to Buffett. It was not merely because of his razor-sharp logic and wisdom, or his words and writings that were aggressive like bitter medicine yet profoundly beneficial. Perhaps I was more drawn to the human aspects that cannot be found in Buffett—starting investing at a somewhat late age, a painful personal family history, illness, and significant losses in the mid-1970s. Perhaps his personal stories, which felt like secrets known only to a few, resonated more closely than Buffett's overly well-known narrative.

I marveled at his life as I heard stories through his close associates Pabrai and Li Lu—such as how he purchased 200,000 pyeong of land (now worth trillions of won) featuring a private beach on the Pacific, from a widow with impeccable timing and negotiation for 100 billion won, and donated it to UC Santa Barbara. I chuckled listening to Todd Combs—one of Berkshire's designated successors—describe on a podcast how chatty Munger was during their first meeting, which became his gateway into the Buffett and Munger world. It saddens me that this is no longer possible. The fact that we can no longer hear brief comments on current affairs—like 'Investing in Bitcoin is insanity'—is, cold-heartedly, a fundamentally different world from before. Encountering someone through posthumous books and records feels dimensionally different from living in the same era and occasionally hearing real-time commentary on current issues. The next generation born today will encounter Charlie Munger merely through written

words, with sentiments similar to how we regard figures from centuries past. Along with this sense of regret, I feel gratitude for having lived in the same era as him.

In 2024, I will continue diligently turning over stones, and when I encounter a company where achieving our long-term target return is expected, I have no intention of hesitating to invest. Even if—unknowably—a long-term downturn of ten years or more awaits in the near future, I look forward with excitement to meeting a company like a salmon swimming against a raging current, and deploying all our cash. To make outstanding decisions when that time comes, I intend to spend this year focused on cultivating a high level of patience and practicing the separation of myself from the numbers in the account.

March 2024

Jonghyun Shon

Noah Investment Management

Sincerely

Appendix

<Returns>

번호 (정렬기준 유형순, 가입일순)	기간	기간 수익률	비고	수수료율
1	2023.01.01 ~ 2023.12.31	29.2%	전문투자자, 상장 주식	기본보수 0%, Hurdle rate 6%, 성과보수 25%
2	2023.01.01 ~ 2023.12.31	27.0%	전문투자자, 상장 주식	기본보수 0%, Hurdle rate 6%, 성과보수 25%
3	2023.01.01 ~ 2023.12.31	32.4%	전문투자자, 상장 주식	기본보수 0%, Hurdle rate 6%, 성과보수 25%
4	2023.01.01 ~ 2023.12.31	30.2%	전문투자자, 상장 주식	기본보수 0%, Hurdle rate 6%, 성과보수 25%
5	2023.01.01 ~ 2023.12.31	42.1%	전문투자자, 상장 주식	기본보수 0%, Hurdle rate 6%, 성과보수 25%
6	2023.01.01 ~ 2023.12.31	36.0%	전문투자자, 상장 주식	기본보수 0%, Hurdle rate 6%, 성과보수 25%
7	2023.01.01 ~ 2023.12.31	36.2%	전문투자자, 상장 주식	기본보수 0%, Hurdle rate 6%, 성과보수 25%
전문투자자, 상장주식 최고		42.1%		
전문투자자, 상장주식 최저		27.0%		
전문투자자, 상장주식 평균	2023.01.01 ~ 2023.12.31	29.8%	시간가중평균	
9	2023.01.01 ~ 2023.12.31	44.8%	공모형	기본보수 0%, 성과보수 실현수익의 20%
공모형 최고		44.8%		
공모형 최저		44.8%		
공모형 평균	2023.01.01 ~ 2023.12.31	44.8%	시간가중평균	

Disclosure

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