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INVESTMENT CHRONICLES

Issue No. 9 | December 2023

PORTER & CO. INVESTMENT CHRONICLES

Welcome to *Porter & Co. Investment Chronicles*, our guide to the most important and interesting stories from the worlds of investing, finance, and economics that's available exclusively to Partners and *Big Secret* Elite members.

Each month, my team and I share the most valuable insights we come across from the hundreds of sources we regularly read and review – hedge-fund letters, annual reports, Securities and Exchange Commission ("SEC") filings, investment newsletters, newspapers, X (Twitter) threads, conferences, podcasts, and more – and digest them into one carefully curated, easy-to-read resource.

With *Investment Chronicles*, you'll have your finger on the pulse of the markets without having to spend hours scouring the internet each day.

You can navigate each issue using the hyperlinked Table of Contents below. All content also includes links back to the original source when possible, so you can easily dig in for more details, to see a larger version of a chart or image, or to learn more about accessing paid content.

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Porter Stansberry
Stevenson, MD
December 2023

Note: Quotes, transcripts, and excerpts are generally reproduced as they appear in the original.

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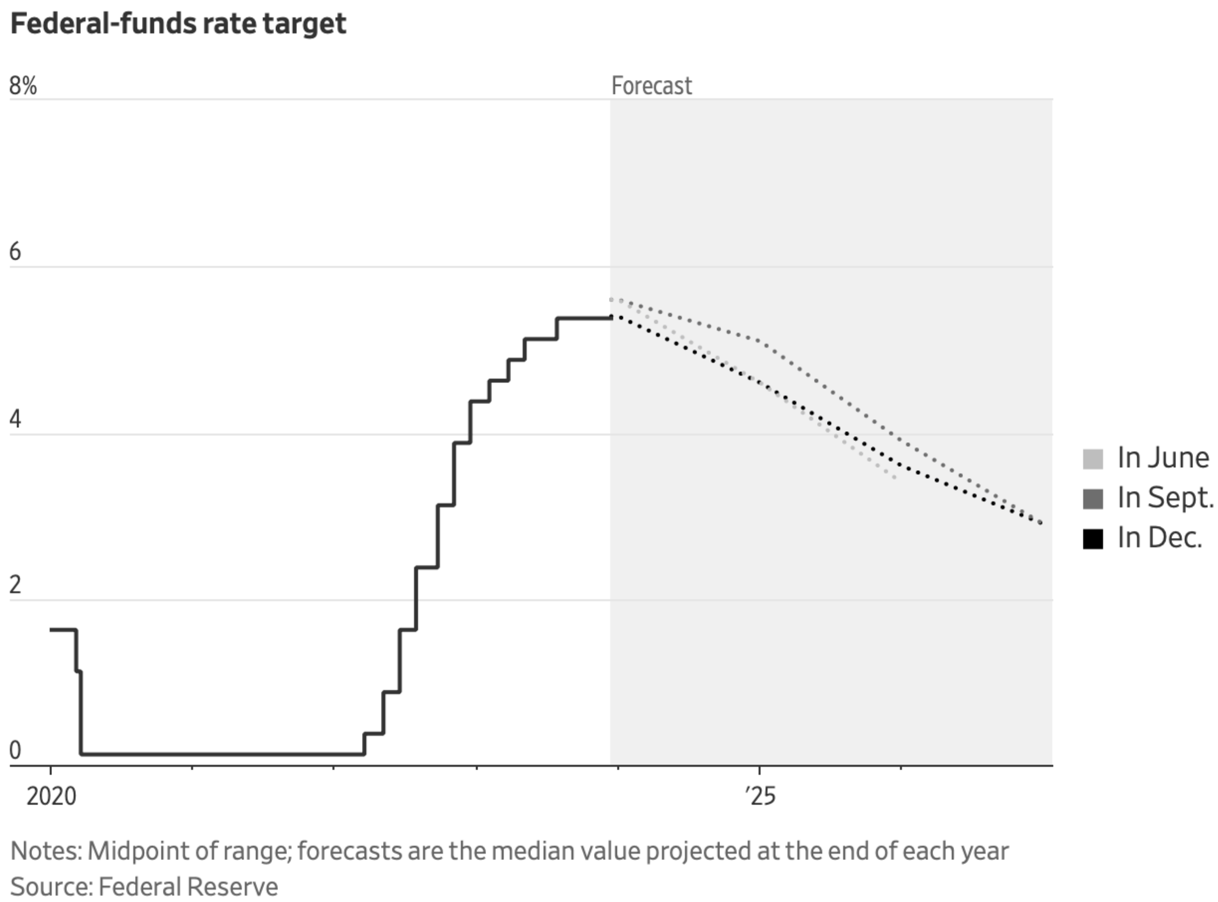
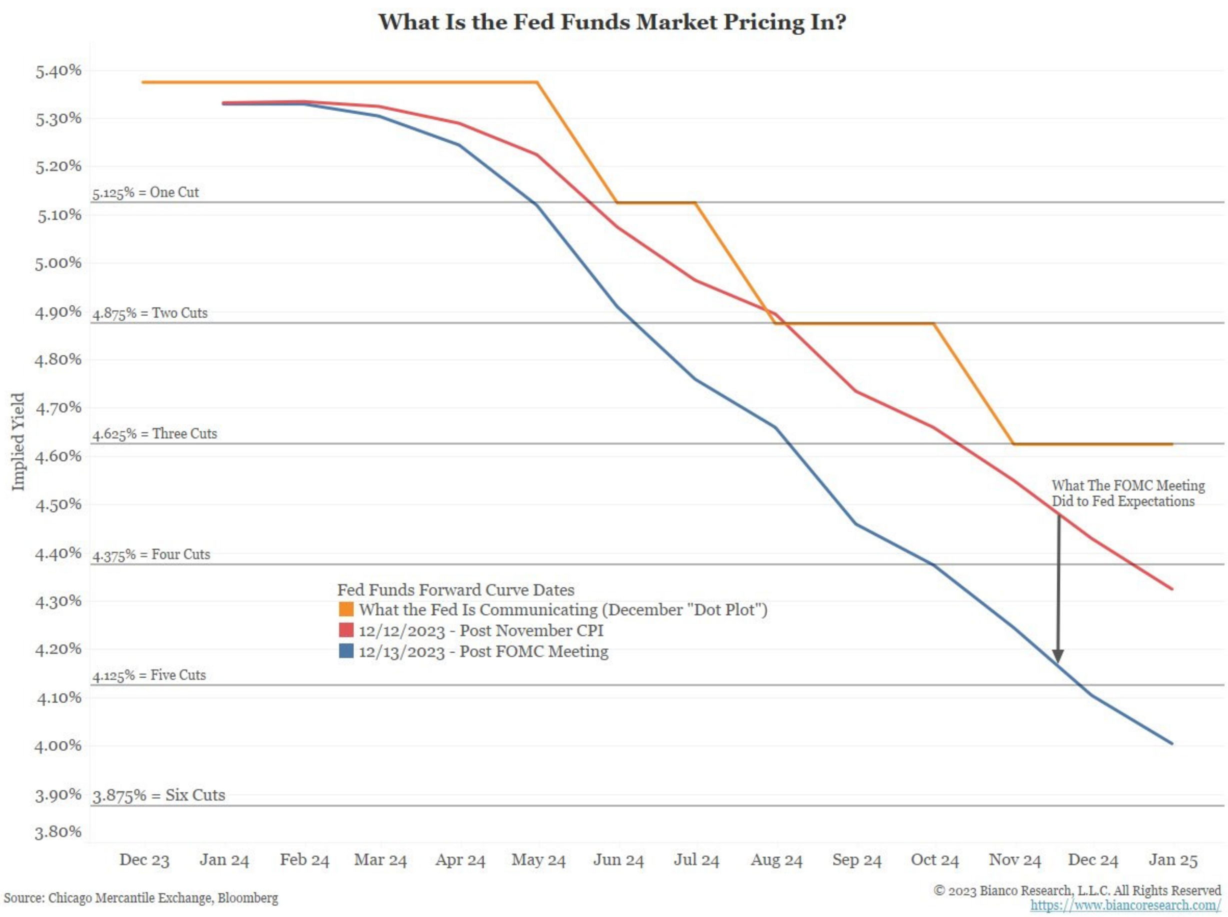
THE FIVE

The Most Important Charts We're Watching This Month

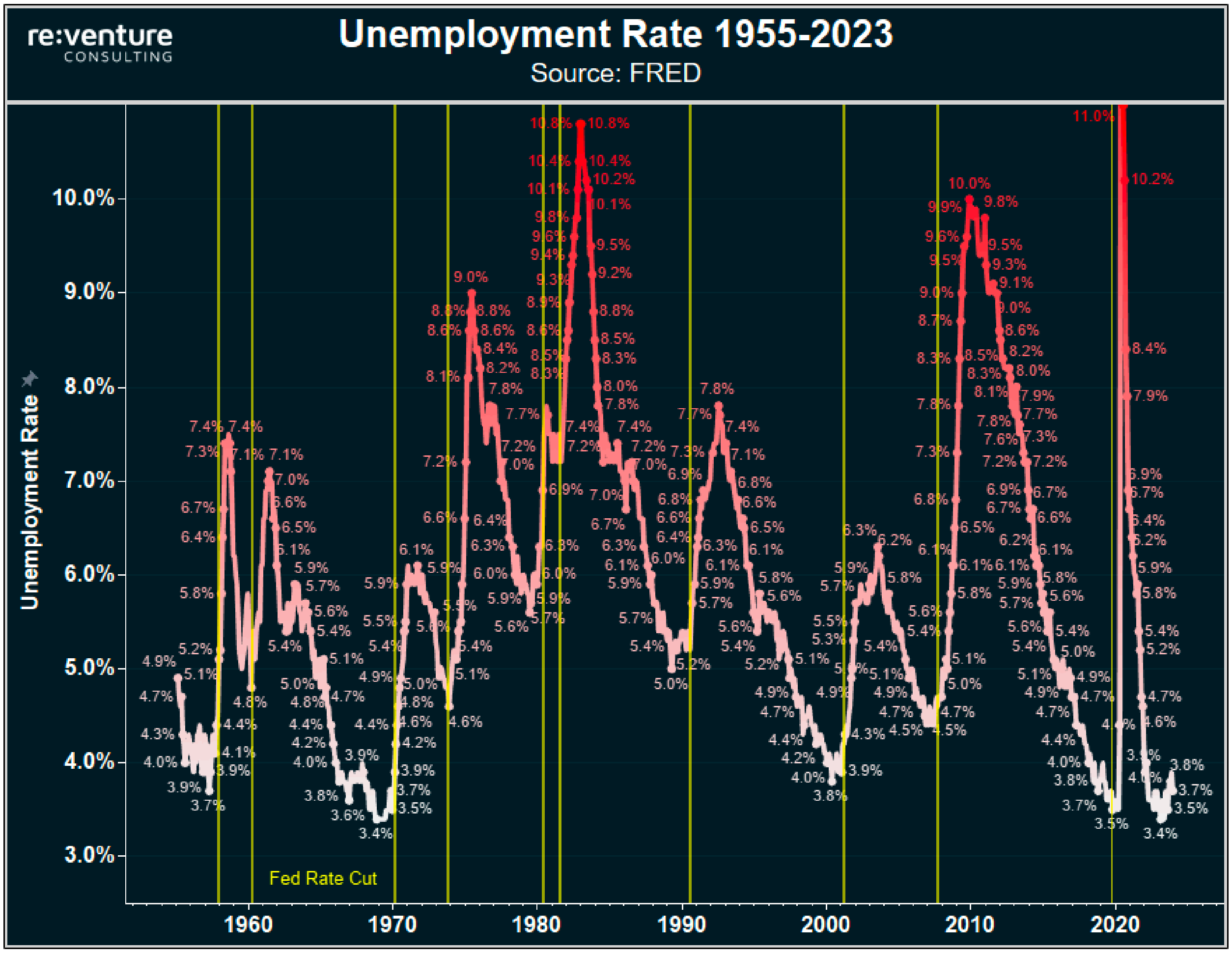
The big story this month was the apparent policy "pivot" from the Federal Reserve. At its latest Federal Open Market Committee (FOMC) meeting on December 13, Fed officials signaled a likely end to its aggressive rate-hiking campaign and projected it would likely cut interest rates three times in 2024 ([from *The Wall Street Journal*]())...



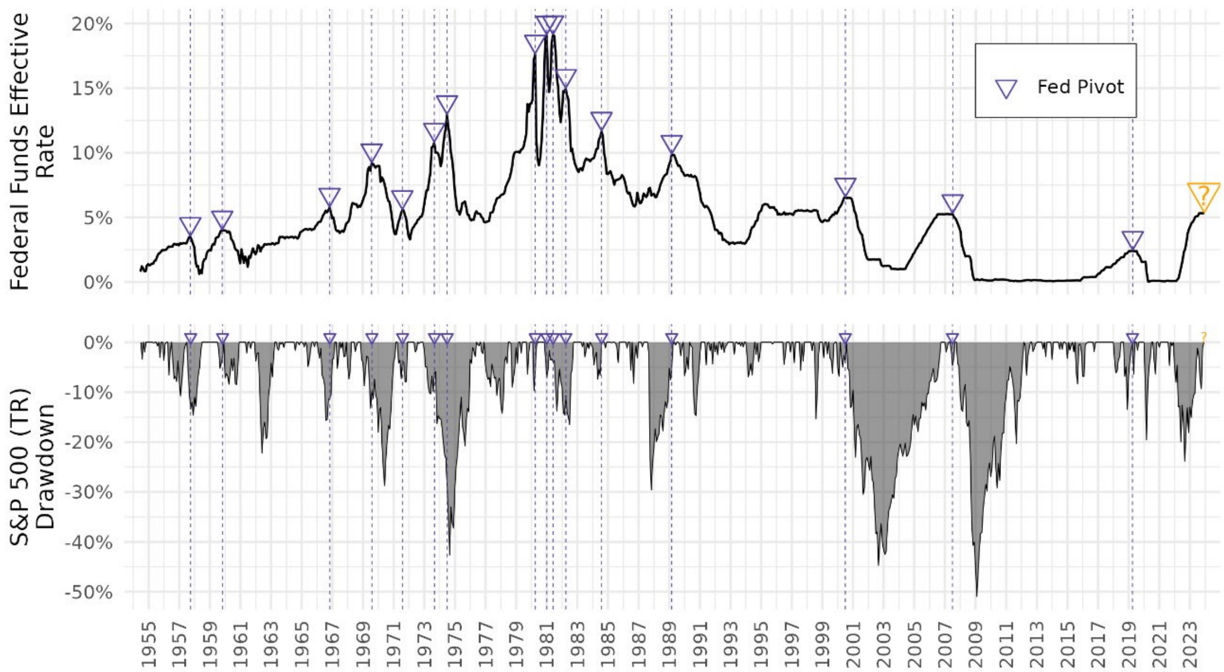
Futures markets quickly became even more "dovish" than the Fed, pricing in up to six interest rate cuts next year (from Jim Bianco via X)...



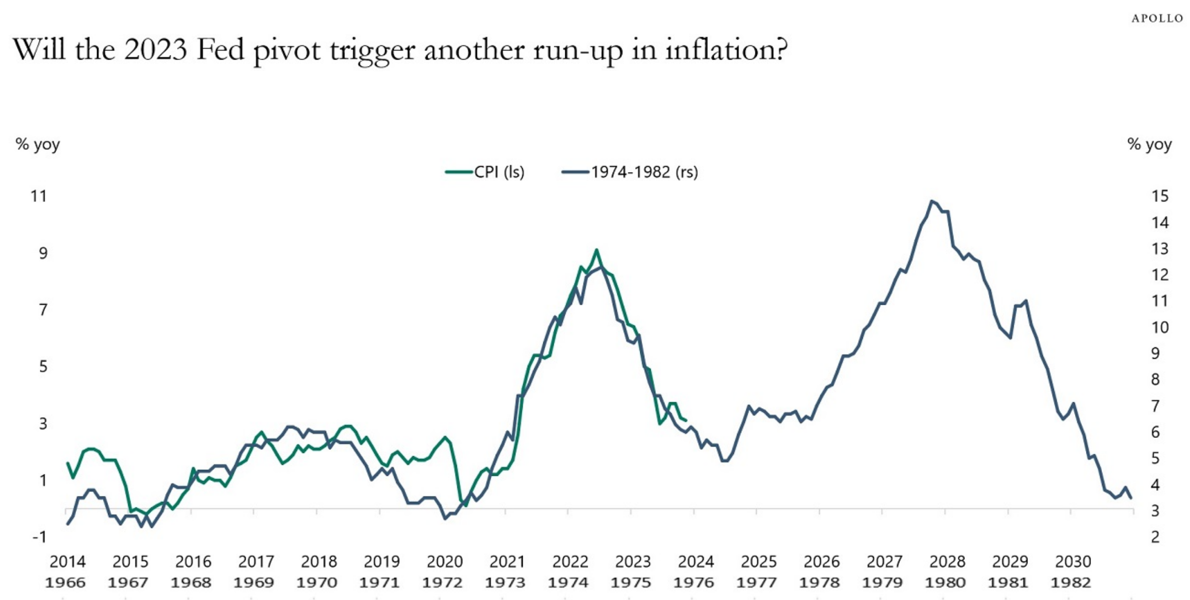
Investors broadly cheered the news as positive for both the economy and risk assets. However, history suggests caution is warranted. Going back to at least the 1950s, Fed pivots have been highly correlated with rising unemployment ([from The Kobeissi Letter via X](#))...



Over the same period, Fed pivots have also generally been bearish for stocks over the intermediate term. This has been particularly true following aggressive cycles when inflation has been high, stock market valuations have been extreme, and corporate and consumer debt burdens have been elevated – all of which are true today (from Michael A. Gayed, CFA via X)...



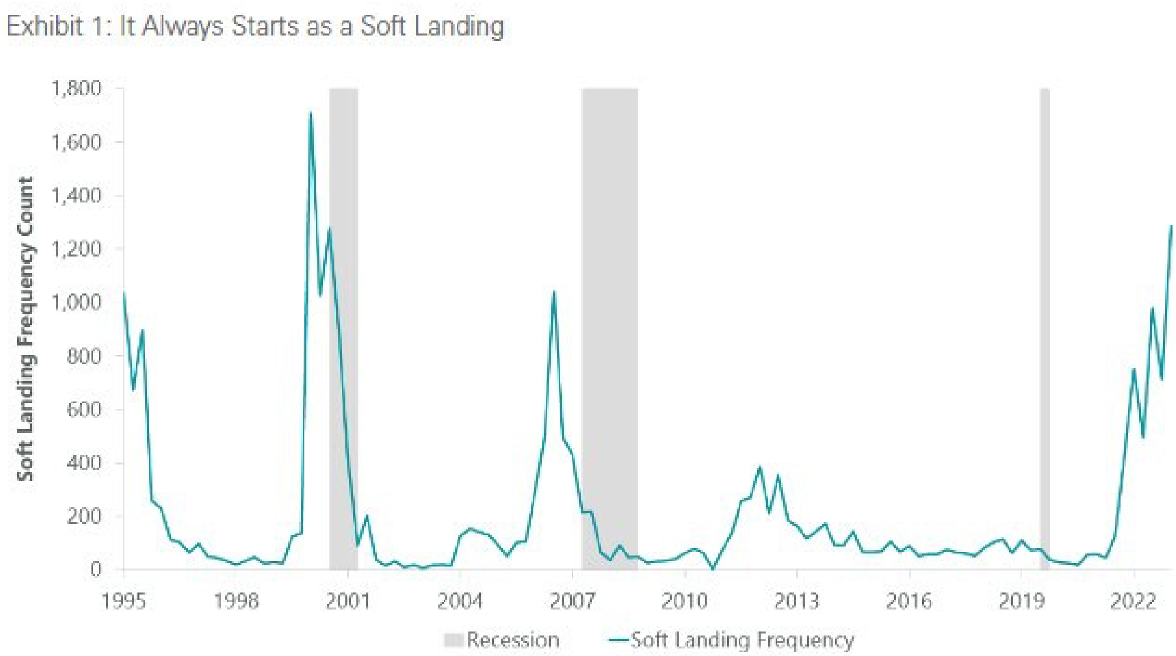
Meanwhile, this policy shift is occurring with headline consumer price inflation still well above the Fed's official target, setting the stage for a sharp potential rebound like that which occurred in the late 1970s ([from Torsten Slok via The Daily Spark]())...



ECONOMICS AND MARKETS

Every recession looks like a "soft landing" initially (from Win Smart, CFA via X)...

It's always called a soft landing. At first...



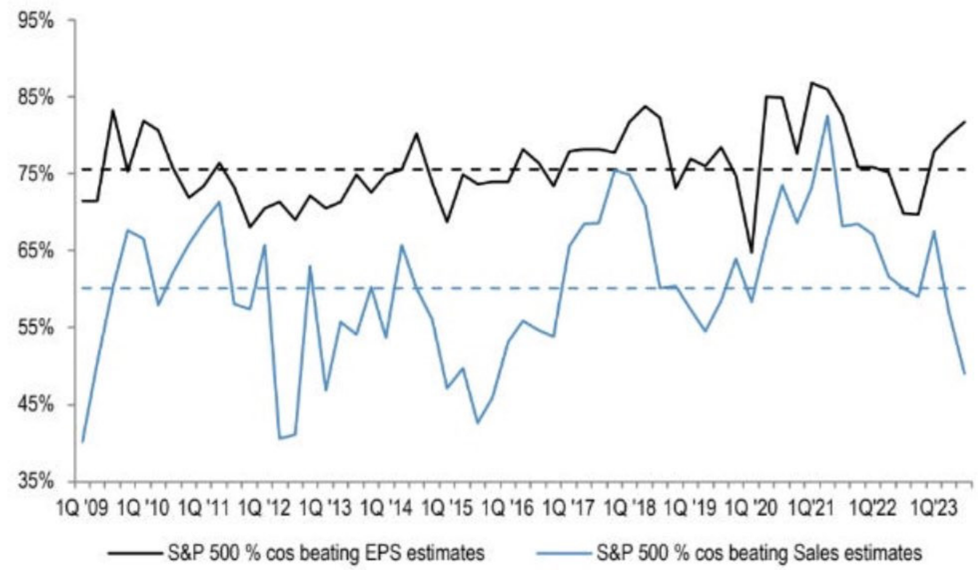
Note: Soft landing frequency is the count of mentions of the term "soft landing" in company filings, transcripts, and presentations since 3Q95. Data as of Sept. 30, 2023. Source: NBER and Bloomberg.

Data suggest corporate revenue has peaked ([from Albert Edwards via X](#))...

The unusual divergence in the chart tells me that the sales cycle has decisively turned downward in the last quarter (aka recession) but that companies have used the cover of rapidly falling raw material input costs to boost margins even further – aka Greedflation.

29. Q3 earnings vs. estimates. With 90% of the S&P 500 reported, 82% have beaten EPS estimates despite 51% missing on the top line.

Figure 4: % of S&P500 companies beating quarterly EPS and sales estimates



Source: Bloomberg Finance L.P., J.P. Morgan, dotted lines denote median EPS and Sales beats

[Mislav Matejka - JPMorgan](#)

Here's a contrarian look at "liquidity" (from Alf via X)...

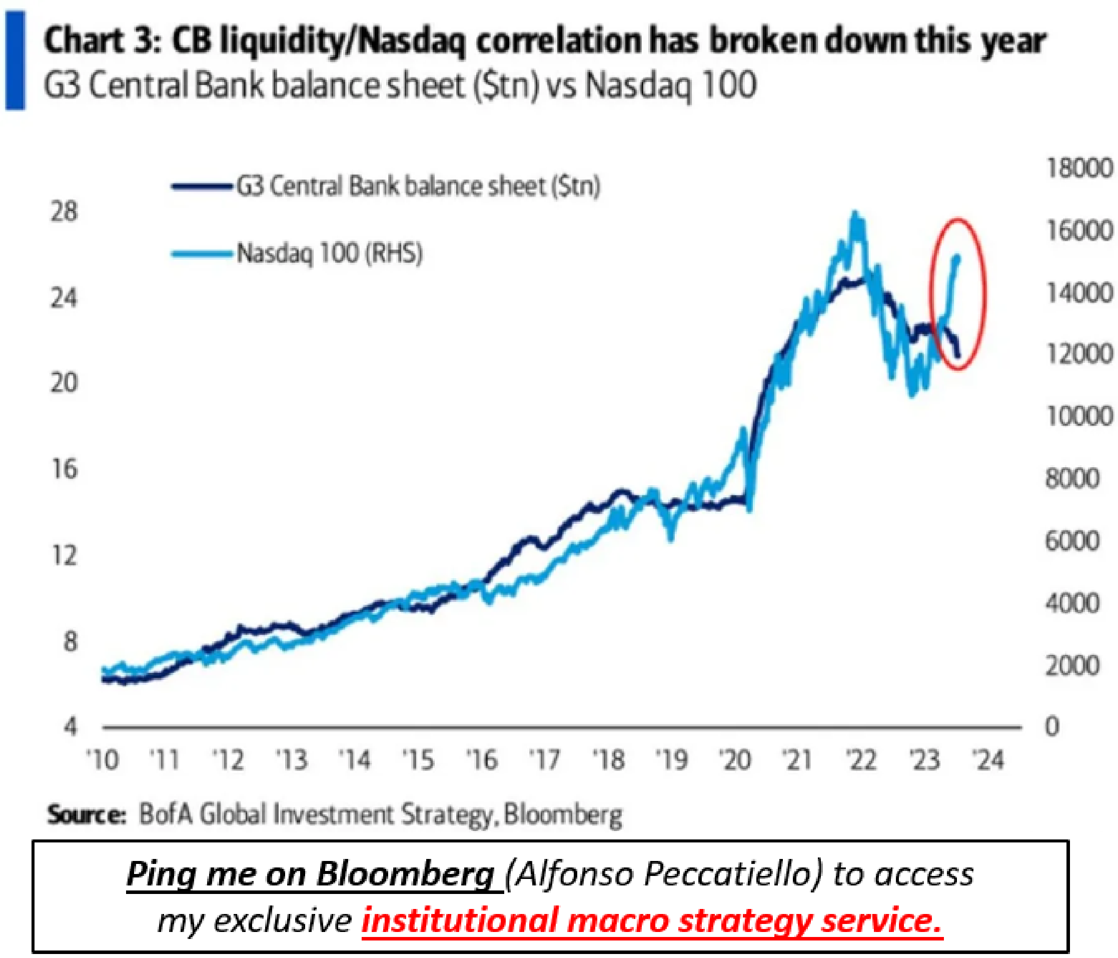
Liquidity is one the most important yet misunderstood macro variables.

This thread will help you understand how it works.

This is one of the most popular and yet misleading charts in macro.

People like simple narratives: the Fed is "pumping money" into the "system" and that's why equity markets go up.

That's just NOT how it works - let's explain why.

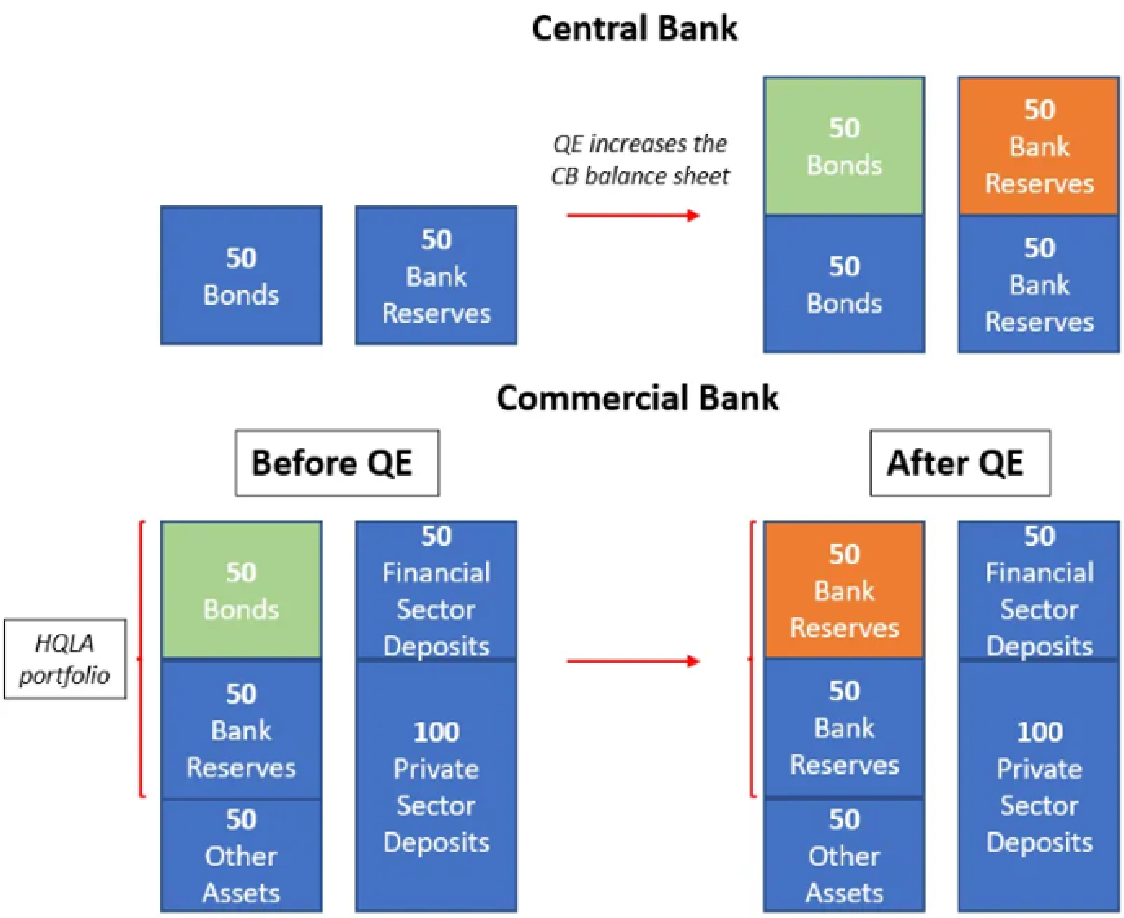


A good starting point is asking ourselves what's "money" and what's the "system".

Let's start from money.

Central Banks' balance sheets expand mostly through monetary operations: the most known is QE, but there are also other tools like the recently created Fed's BTFP.

In any case, when the CB expands its balance sheet by acquiring assets (QE) or providing financing in exchange of collateral (e.g. BTFP, TLTRO) it also expands the liability side - it prints "money", but to be more precise it prints bank reserves.



Ping me on Bloomberg *(Alfonso Peccatiello) to access my exclusive* ***institutional macro strategy service.***

Bank reserves are bank-money, not real-economy money: only banks can transact in bank reserves with each other, and these reserves can never (I repeat, never) reach the private sector.

Banks DO NOT buy stocks with bank reserves!

The idea behind the "famous" chart is just wrong: as the Fed creates new bank reserves ("liquidity") there would be a mechanism for which banks deploy these reserves in financial assets hence pushing equity markets up.

But banks don't do that.

What are reserves ("liquidity") used for?

Mostly to settle transactions against other banks.

They also account as a High Quality Liquid Asset (HQLA) together with government bonds and certain corporate and mortgage-backed securities.

Equity ownership as a % of HQLA buffers from big European and US banks is negligible - conditions are so strict you could say it's almost 0%.

Stock of High Quality Liquid Assets

Item	Factor
Level 1 assets:	
• Coins and bank notes • Qualifying central bank reserves • Domestic sovereign or central bank debt for non-0% risk-weighted sovereigns	100%
Level 2 (maximum of 40 % of HQLA):	
• Sovereigns qualifying for 20% risk weighting • Qualifying corporate debt securities rated AA- or higher • Qualifying covered bonds rated AA- or higher	85%
Level 2B assets (maximum of 15% of HQLA)	
• Qualifying corporate debt securities rated between A+ and BBB-	50%
• Qualifying common equity shares	50%

I know what you are thinking now: the portfolio rebalancing effect.

If banks are bidding corporate bonds away from each other's HQLA buffers, spreads will tighten and this should invite a more aggressive stance from equity investors too.

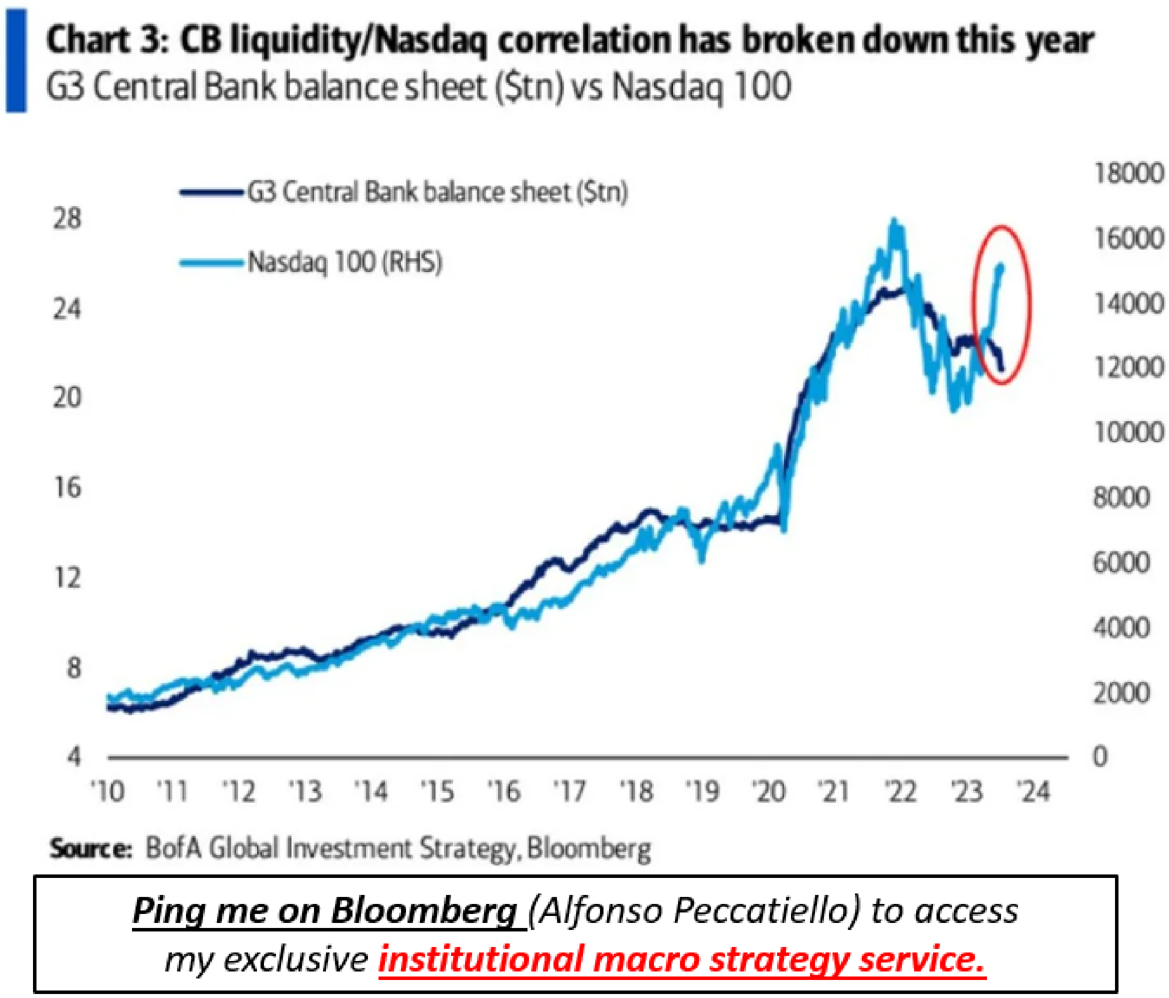
That's partially true but it's a potential second-order effect which also requires fundamentals (!) to back the thesis: banks aren't gonna blindly over-allocate to corporate bonds because they have more reserves if they smell the risk of rising defaults.

2008 is a good example.

These two series trended up over the last 15 years for different reasons:

- Central Banks kept accommodating through QE ("they added liquidity")

- The Nasdaq went up because tech stocks delivered excellent earnings, had strong balance sheets, and low rates helped



Don't believe me yet?

Let's do some basic math.

If it's really true that "liquidity" drives stock market returns, regressing one against another should show liquidity has excellent explanatory power.

It doesn't: only 3% (!) of SPX returns can be explained by liquidity.

Sorry to ruin the narrative, but "liquidity" doesn't predict stock market returns

Regression of 6m changes in US reserves vs 6m SPX returns (lagged by 3m & 6m)

SPX returns (3m and 6m lag)

US Reserves ("liquidity")

	us_res	
	(1)	(2)
spx3	0.412*** (0.158)	
spx6		0.359** (0.156)
Constant	0.056*** (0.019)	0.052*** (0.019)
Observations	170	167
R2	0.039	0.031
Adjusted R2	0.033	0.025
Residual Std. Error	0.229 (df = 168)	0.225 (df = 165)
F Statistic	6.839*** (df = 1; 168)	5.314** (df = 1; 165)
Note:		*p<0.1; **p<0.05; ***p<0.01

__Ping me on Bloomberg__ (Alfonso Peccatiello) to access my exclusive __institutional macro strategy service.__

Central Banks pumping "money" into the "system" and driving stock higher is an easy narrative to follow

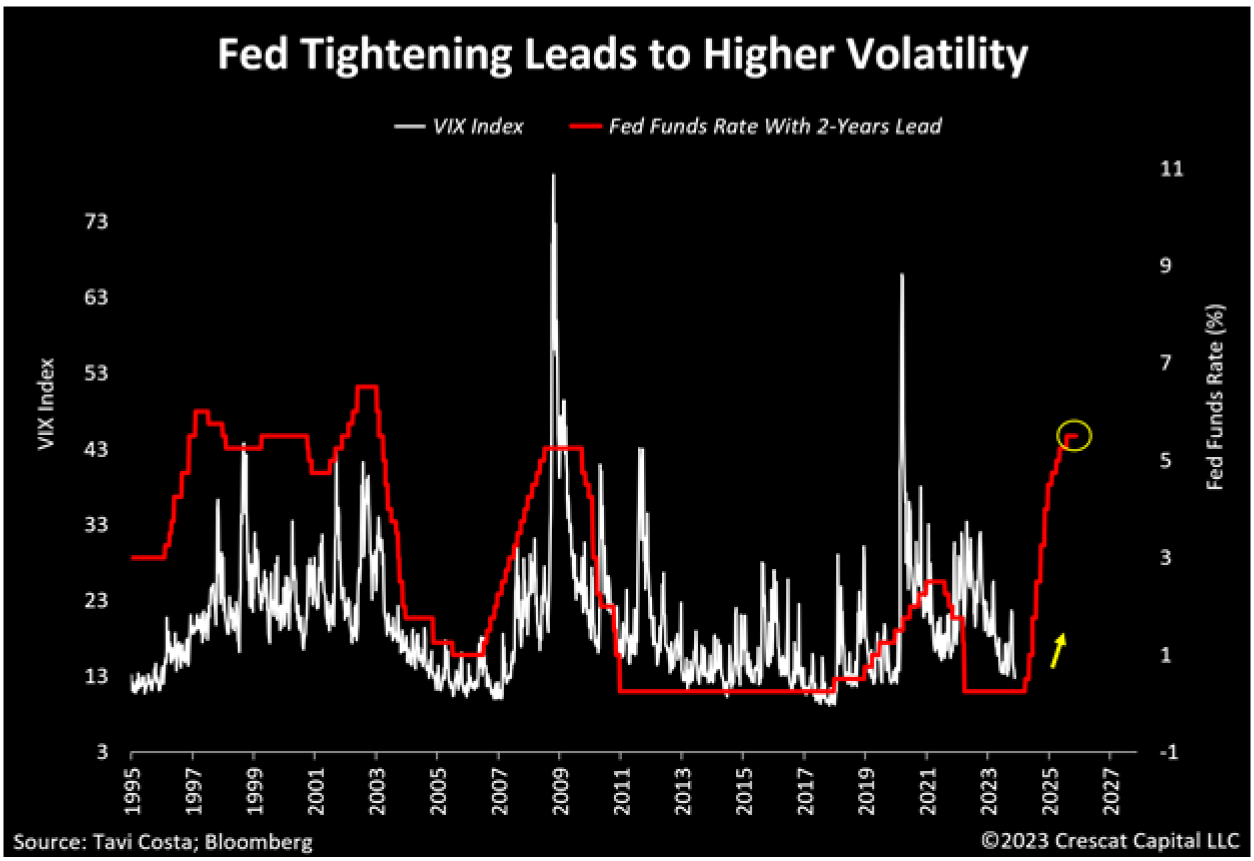
But it's plain wrong: bank reserves are not used to buy stocks, and simple math shows "liquidity" doesn't have explanatory power on future stock returns

The effects of the Fed's aggressive tightening cycle are likely only *now* beginning to be felt (from Otavio Costa via X)...

The lagging effects of monetary policy are about to start impacting financial markets.

With a two-year lead, changes in Fed funds rates have often foreshadowed significant volatility events in equity markets.

The current narrowing leadership in the stock market, coupled with numerous recession indicators sounding alarms, supports the argument that volatility is currently unsustainably suppressed.



Government money printing is creating a "cost of living crisis" (from Sam Callahan via X)...

Bloomberg shared some evidence of the cost of living crisis many Americans face today. Since 2020:

Groceries: +25%

Home Values: +42%

Electricity Bills: +25%

Natural gas: +29%

Rent: +20%

Used Car: +35%

Car Insurance: +33%

Child care: +32%

Food at restaurants

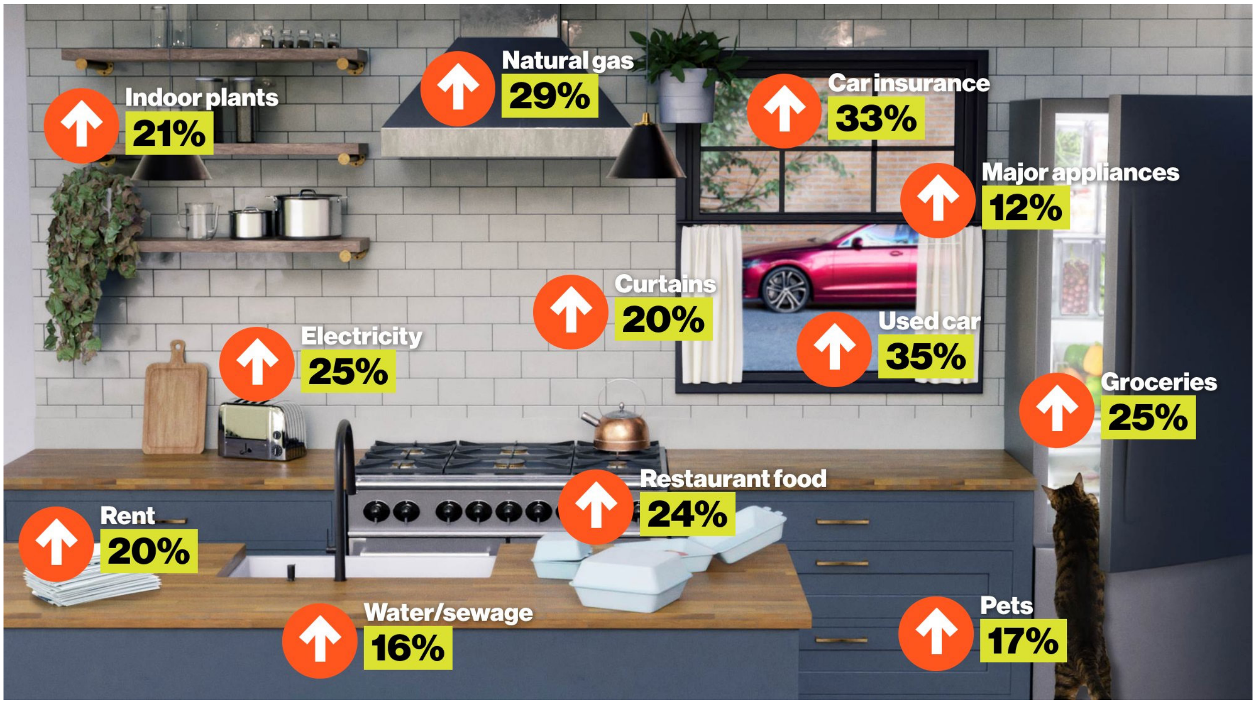
Chicken dishes: +32%

Burgers: +23%

Pasta: +14%

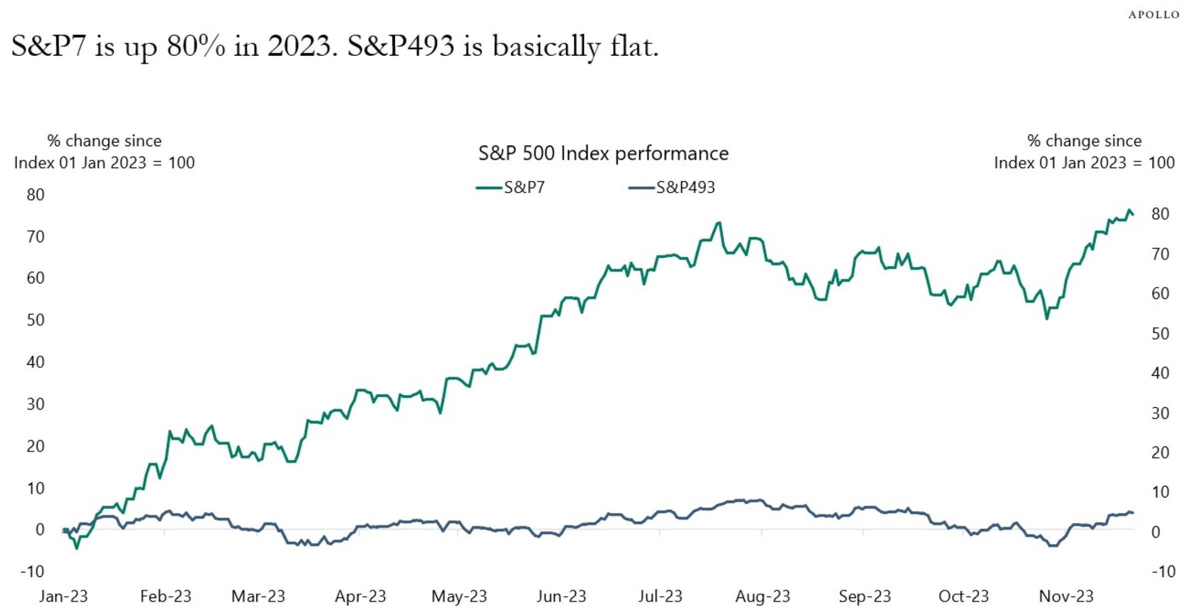
Pizza: +17%

Meanwhile, instead of addressing the problem, the government is worsening it and choosing to gaslight the public by saying this Thanksgiving was the "fourth cheapest ever."


Indoor plants
21%
Natural gas
29%
Car insurance
33%
Major appliances
12%
Curtains
20%
Electricity
25%
Used car
35%
Groceries
25%
Restaurant food
24%
Rent
20%
Water/sewage
16%
Pets
17%

Big tech stocks are historically overvalued (from The Daily Spark)...

The divergence between the S&P7 and the S&P493 continues, see the first chart below. Investors buying the S&P500 today are buying seven companies that are already up 80% this year and have an average P/E ratio above 50. In fact, S&P7 valuations are beginning to look similar to the Nifty Fifty and the tech bubble in March 2000 (see the second chart below).



Source: Bloomberg, Apollo Chief Economist. Note: The S&P7 is the Magnificent 7: Apple, Microsoft, Alphabet, Amazon, NVIDIA, Meta, and Tesla.

APOLLO

S&P7 stocks are as overvalued as the Nifty Fifty and tech in 2000

S&P7	Trailing P/E	Tech bubble	March 2000 P/E	Nifty Fifty	1972 P/E
Meta	22	Intel	41	Coca-Cola	46
Amazon	68	Cisco	100	McDonald's	71
Apple	31	Dell	57	Texas Instruments	40
Google	25	Microsoft	51	IBM	36
Microsoft	36			Xerox	46
Nvidia	115			Polaroid	95
Tesla	75				
Average P/E ratio	**53**	**Average P/E ratio**	**62**	**Average P/E ratio**	**56**

Source: Bloomberg, Apollo Chief Economist

Our "leaders" are liars or fools (you be the judge) ([from Michael Green via X](#))...

The economic ignorance is like a nightmare that won't end... so maybe not transitory...

Joe Biden
@JoeBiden

Follow ···

Let me be clear to any corporation that hasn't brought their prices back down even as inflation has come down: It's time to stop the price gouging.

Give American consumers a break.

Readers added context they thought people might want to know

As long as the inflation rate is positive, prices are increasing. The fact that inflation has come down to 3.2% in October means that prices are still going up, albeit at a slower rate than before.

imf.org/en/Publication...

eu.usatoday.com/story/money/20...

statista.com/statistics/273...

The Federal Reserve aims for a target inflation rate of 2%.
federalreserve.gov/faqs/economy_1...

Do you find this helpful? **Rate it**

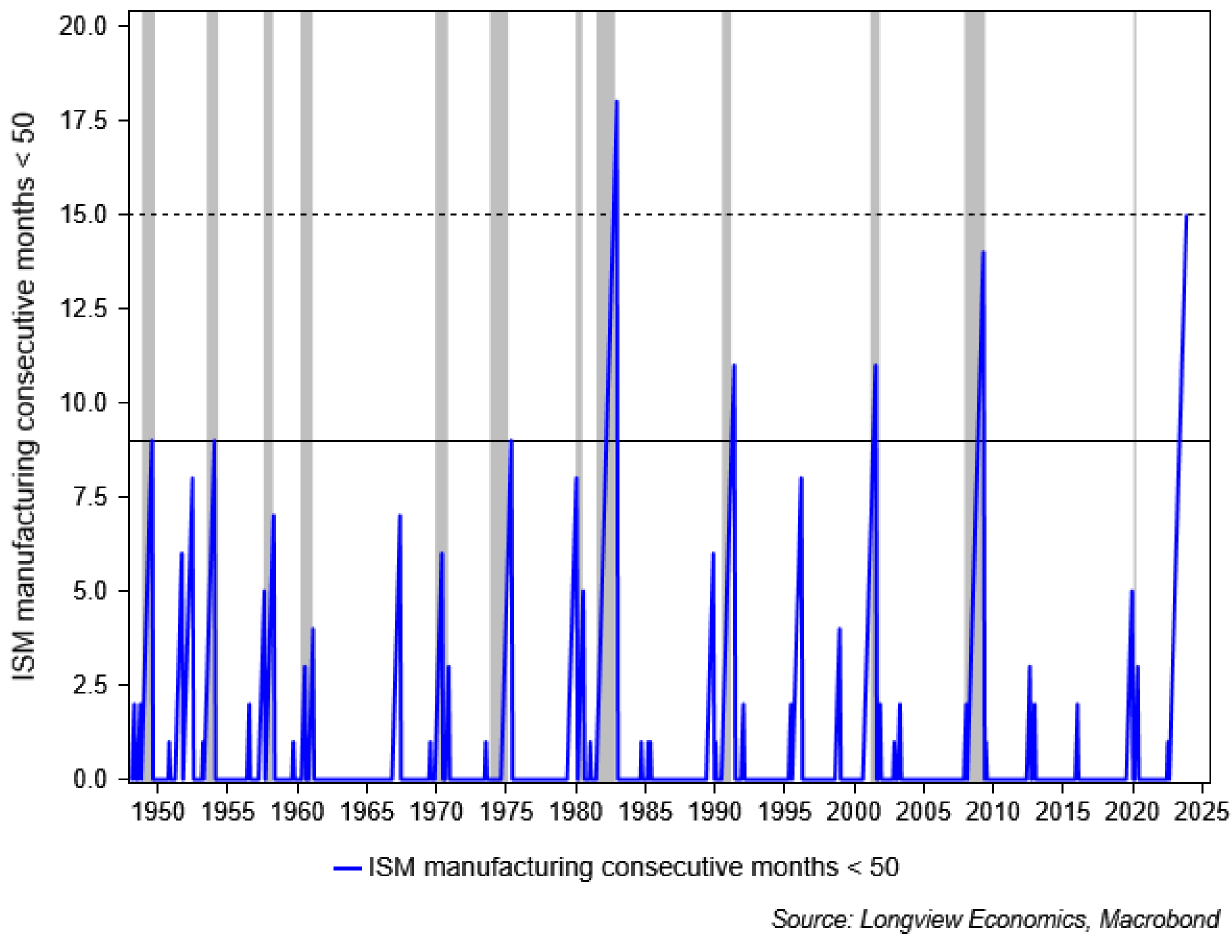
The banking system needs dramatically lower long-term rates to become solvent again (from Richard Christopher Whalen via X)...

So here's the mark-to-market for the banking industry as of Q3 2023... @ FDICgov 10-year Treasury is the toggle... @stephengandel

Total Equity Capital	**$2,357,424**	**$2,257,908**	**$2,218,286**	**$2,165,245**	**$2,207,319**	**$2,262,762**	**$2,253,341**	**$2,245,224**
Intangible assets	$404,349	$415,379	$421,498	$355,596	$430,077	$435,471	$435,999	$436,192
Total Capital (Tangible)	**$1,953,075**	**$1,842,529**	**$1,796,788**	**$1,809,649**	**$1,777,242**	**$1,827,291**	**$1,817,342**	**$1,809,032**
AOCI (AFS net of hedges)	$31,079	$170,176	$253,454	$347,851	$326,083	$283,309	$301,626	$336,936
Total Capital (Tangible-AOCI)*	**$1,921,996**	**$1,672,353**	**$1,543,334**	**$1,461,798**	**$1,451,159**	**$1,543,982**	**$1,515,716**	**$1,472,096**
Net Loans & Leases (HTM)	$11,068,770	$11,181,401	$11,592,512	$11,815,804	$12,226,876	$12,009,849	$12,089,498	$12,131,306
M2M Adjust ($)	$276,719	$894,512	$1,738,877	$2,067,766	$1,528,359	$1,801,477	$2,115,662	$2,426,261
U.S. Treasury securities (HTM)	$1,443,819	$1,481,802	$1,510,721	$1,456,722	$1,434,279	$1,326,458	$1,247,658	$1,247,123
Mortgage-backed securities (HTM)	$3,557,069	$3,522,187	$3,381,850	$3,202,320	$3,150,227	$3,032,304	$2,962,311	$2,870,131
State and municipal securities (HTM)	$423,815	$415,939	$405,028	$389,779	$384,029	$367,099	$348,528	$326,512
Total (HTM)	**$5,424,703**	**$5,419,928**	**$5,297,599**	**$5,048,821**	**$4,968,535**	**$4,725,861**	**$4,558,496**	**$4,443,767**
M2M Adjust ($)	$135,618	$433,594	$794,640	$883,544	$621,067	$708,879	$797,737	$888,753
Total Capital (Tangible-Adjusted)**	**$1,509,659**	**$344,247**	**$990,182**	**$1,489,512**	**$698,267**	**$966,374**	**$1,397,683**	**$1,842,919**
M2M Adjust (%)	**2.5%**	**8.0%**	**15.0%**	**17.5%**	**12.5%**	**15.0%**	**17.5%**	**20.0%**
10 Year Treasury Yield	**1.52%**	**2.46%**	**2.88%**	**3.83%**	**3.88%**	**3.48%**	**3.81%**	**4.59%**

The U.S. manufacturing sector is in the midst of an historic contraction ([from Longview Economics via X]())...

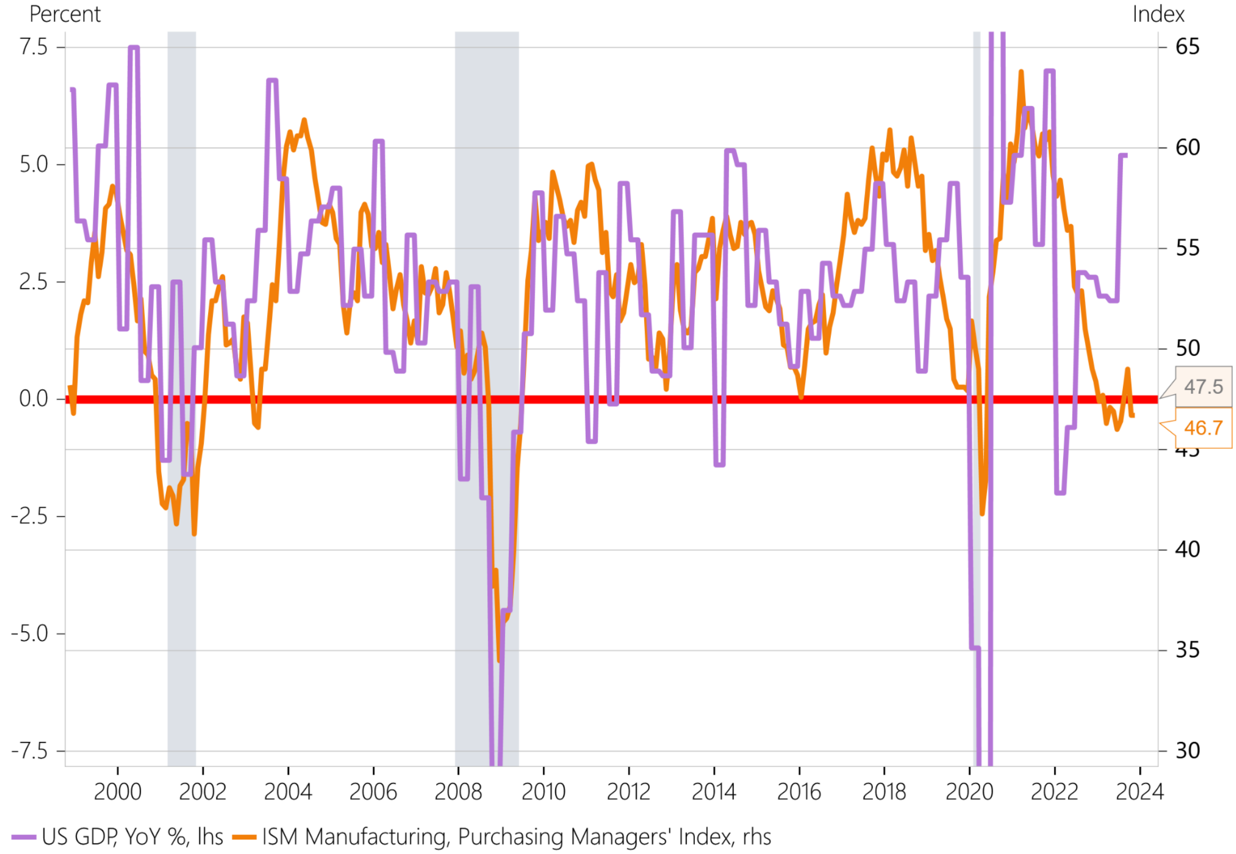
ISM manufacturing is now in contraction for 15 months straight, the longest stretch in 40 years.



History suggests the broad economy is highly likely to follow manufacturing in the months ahead (from Nik Bhatia via X)...

Recession Alert: The slowdown in ISM is unequivocal – GDP will follow after enough time and revisions.

ISM Manufacturing suggests negative GDP

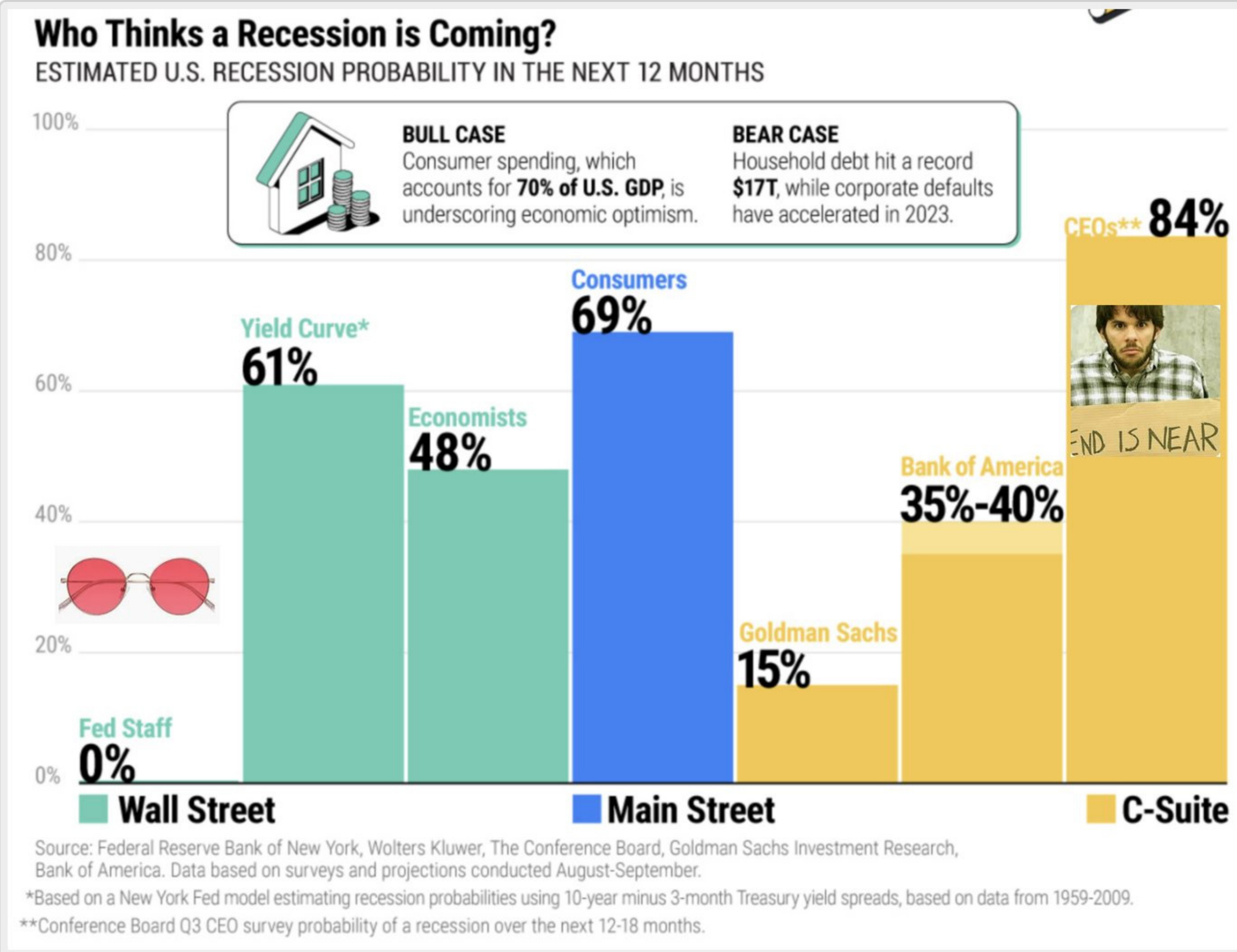


Source: The Bitcoin Layer, ISM, BEA, Macrobond

THE BITCOIN LAYER

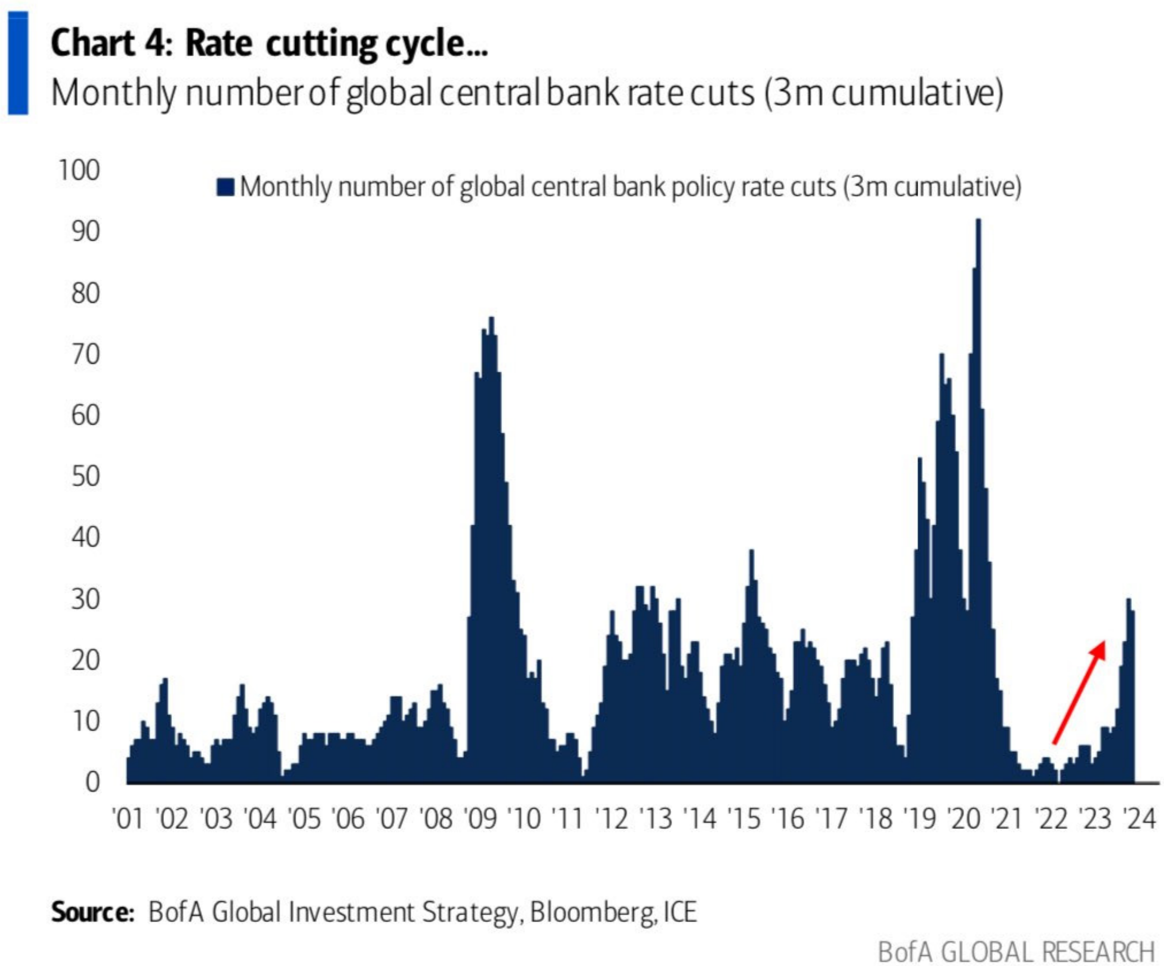
CEOs are incredibly bearish on the economy right now (from Seth Golden via X)...

The Fed may have rose-colored glasses about #recession risk, but CEOs are clearly doomsayers over the next 12-months! #economy



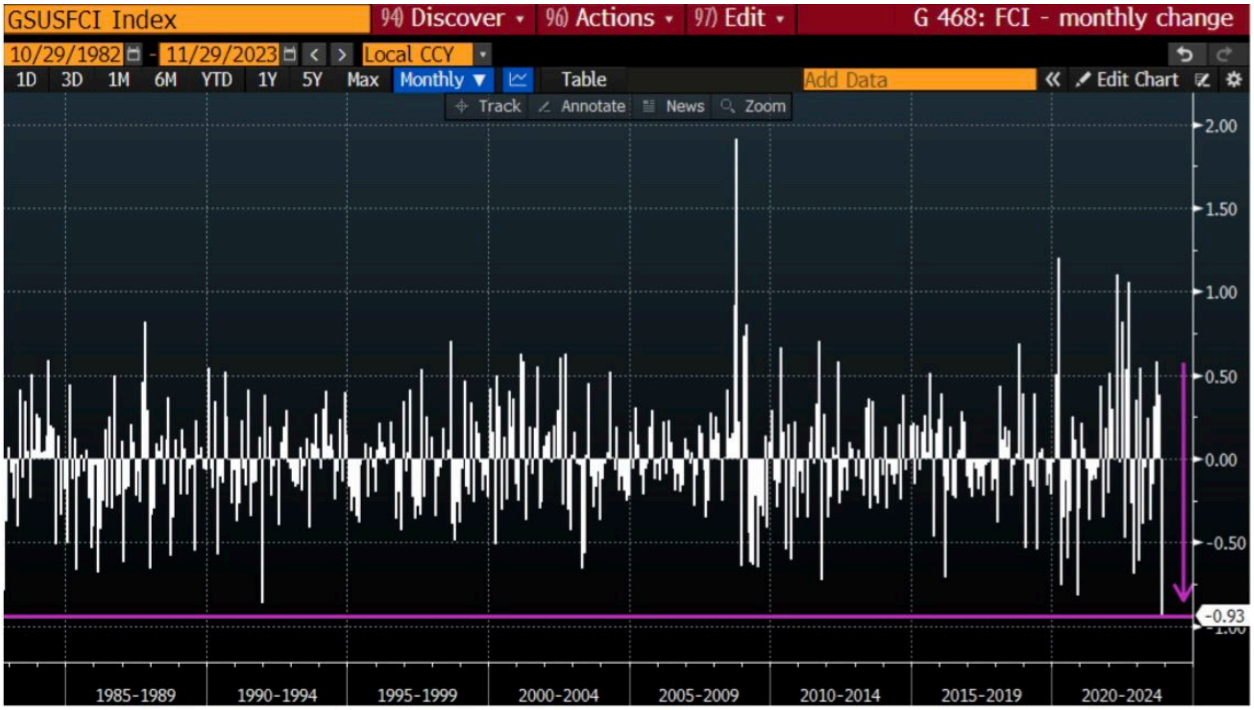
The Fed is not alone in "pivoting" (from Carl Quintanilla via X)...

Here come the global rate cuts. (via B of A / Hartnett)



Last month brought a dramatic easing in financial conditions (from David Marlin via X)...

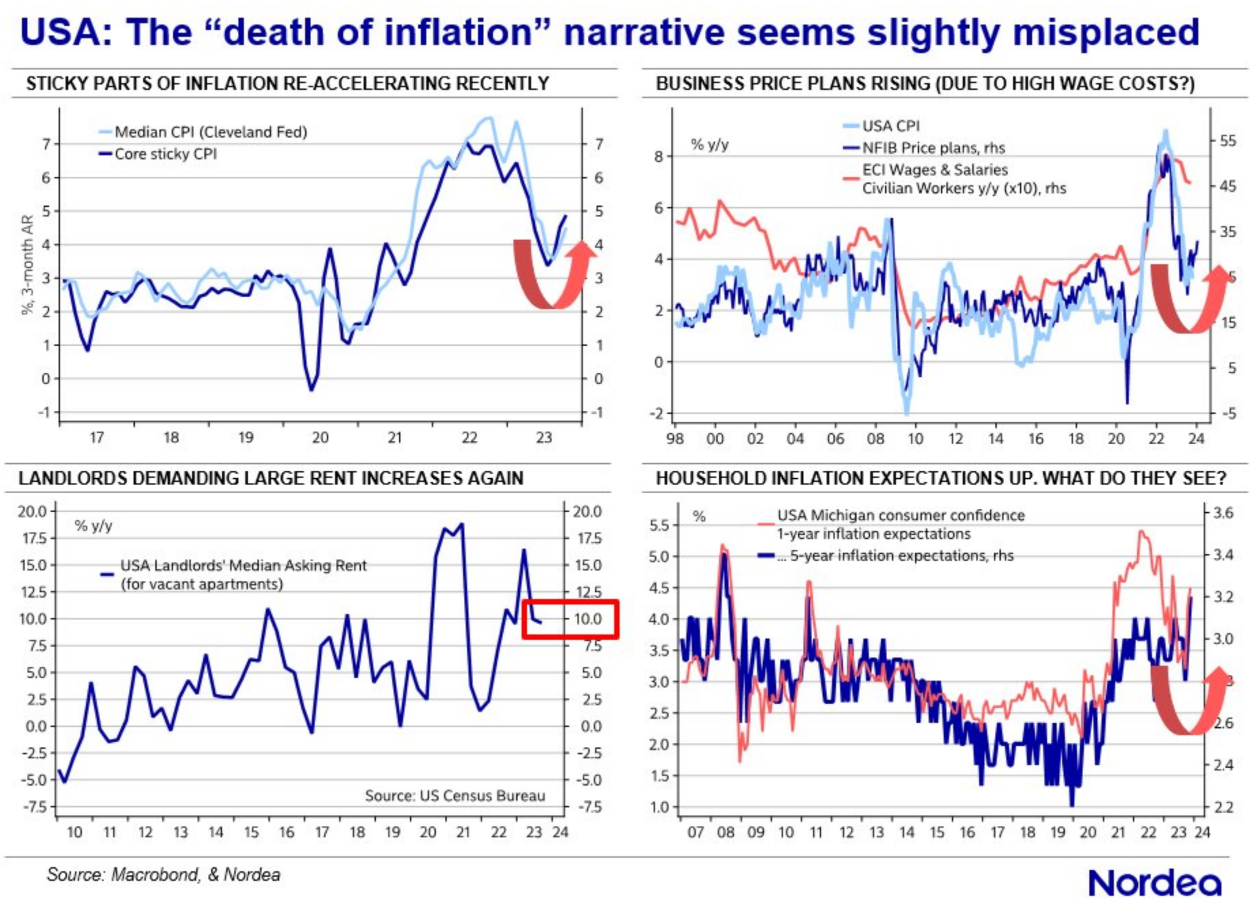
U.S. Financial Conditions eased 90 bps in November, the largest monthly easing on record (dating back to 1982). $SPY $QQQ $IWM



Source: GS GBM, as of 12/1/2023. Past performance is not indicative of future

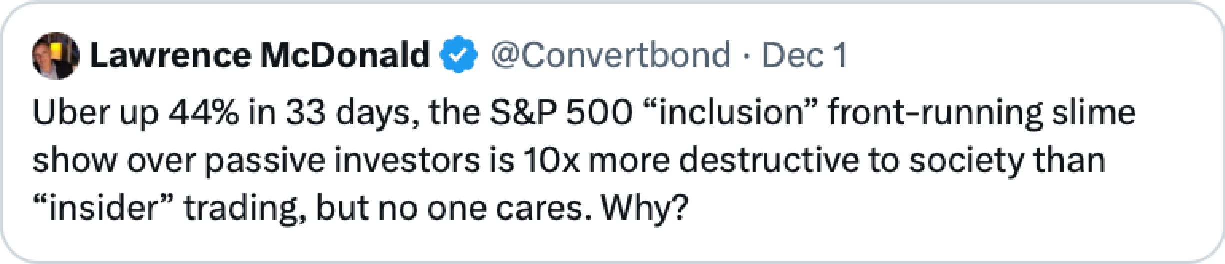
Don't dismiss the risks of inflation just yet (from Mikael Sarwe via X)...

Dear markets, I hate to break it to you but...



Passive investment flows into market-cap weighted indexes are creating huge distortions in markets (from Michael Green and Louis-Vincent Gave via X)...

Saying the quiet part out loud... bravo. FWIW, the index investor is not getting hosed, capitalism is.


Lawrence McDonald @Convertbond · Dec 1

Uber up 44% in 33 days, the S&P 500 "inclusion" front-running slime show over passive investors is 10x more destructive to society than "insider" trading, but no one cares. Why?

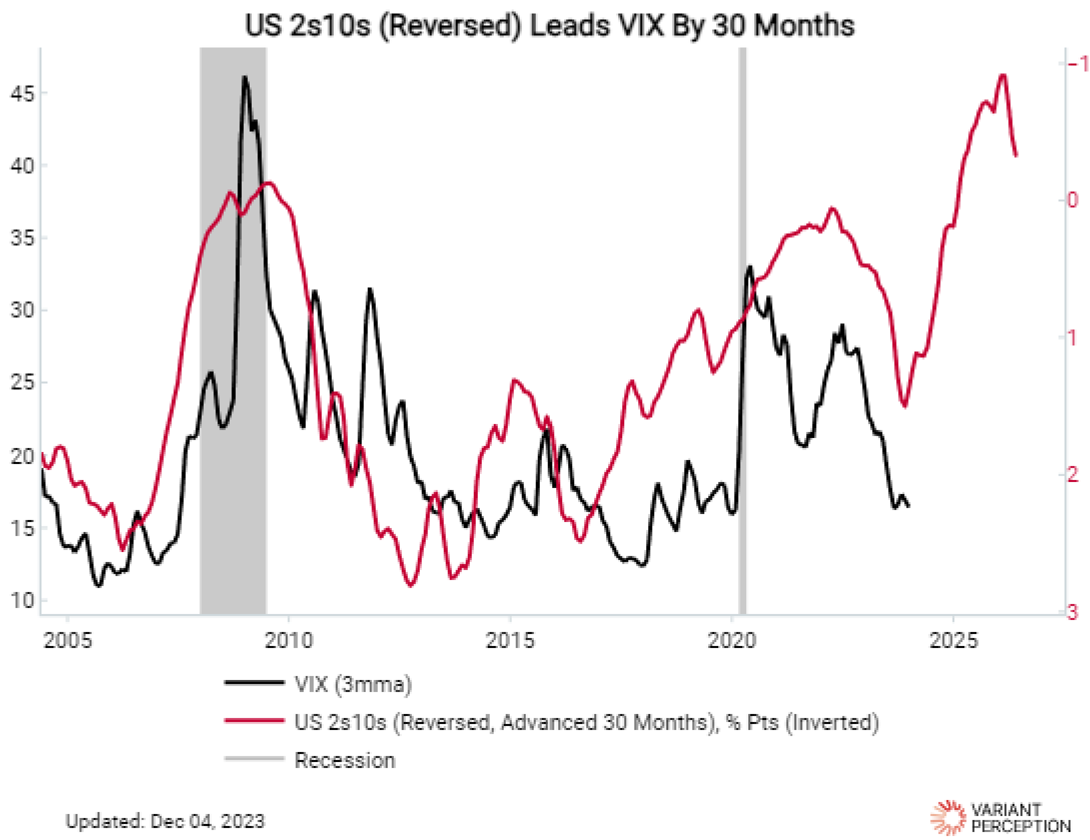
Indexing is the new form of socialism: allocating capital to whoever is BIG (like the Soviet Union used to do), whether capital is needed or not; instead of allocating capital where the marginal returns on capital will be the highest And the end result is very socialist: almost everyone gets the SAME individual outcome (index returns), but the aggregate outcome (for the broader system) over the long term ends up being massively sub-optimal. And like in every socialist country, a small minority somehow ends up with all the spoils...

The first 4x-leveraged fund launched this month ([from Eric Balchunas via X](#))...

Someone is launching a 4x S&P 500 ETN with the ticker XXXX, which would be a leveraged amt record in the U.S. We are so back. Maybe too back? h/t @Todd_Sohn

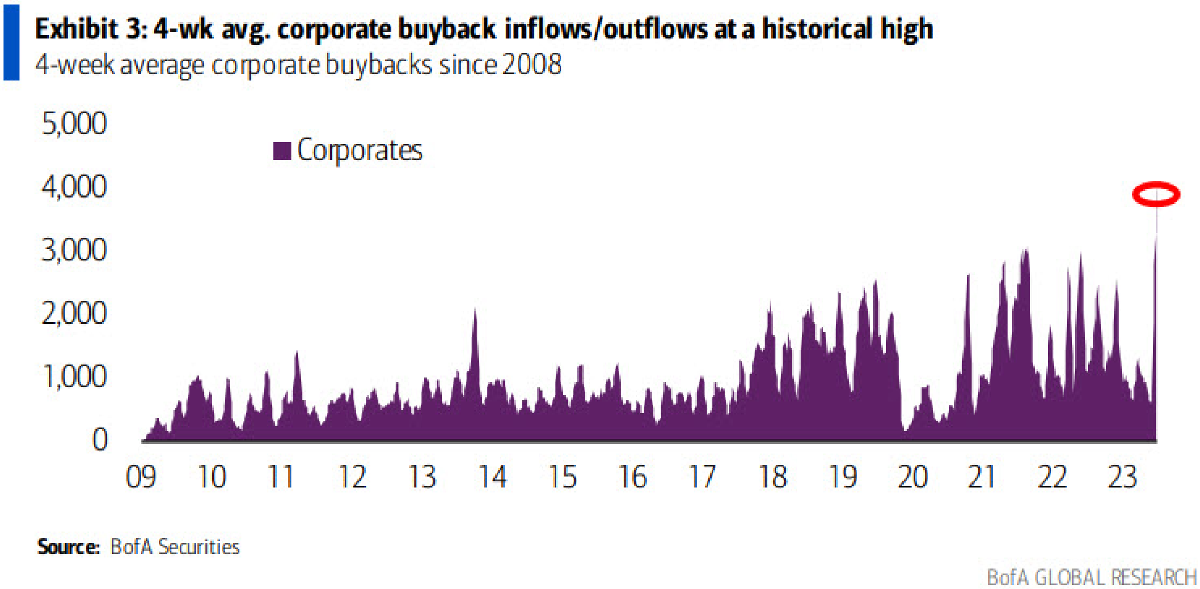
Inverted Treasury yield curves have forecasted significantly higher stock market volatility over the past 20 years (from Variant Perception via X)...

Inverted yield curves offer a very long lead on the VIX.



Last month set a new stock buyback record (from Tyler Durden via X)...

November saw the biggest amount of buybacks in history.



The tight labor market that supported a surprisingly strong economy this year is showing signs of loosening (*from The Wall Street Journal*)...

The hot labor market that underpinned a surprisingly strong economy this year is showing signs of cooling, an indication that growth could ease in 2024.

The number of available jobs at the end of October was the lowest since March 2021, the Labor Department said Tuesday. Fewer openings come as the unemployment rate has edged higher this year, Americans are taking longer to find new jobs, and wage growth is slowing.

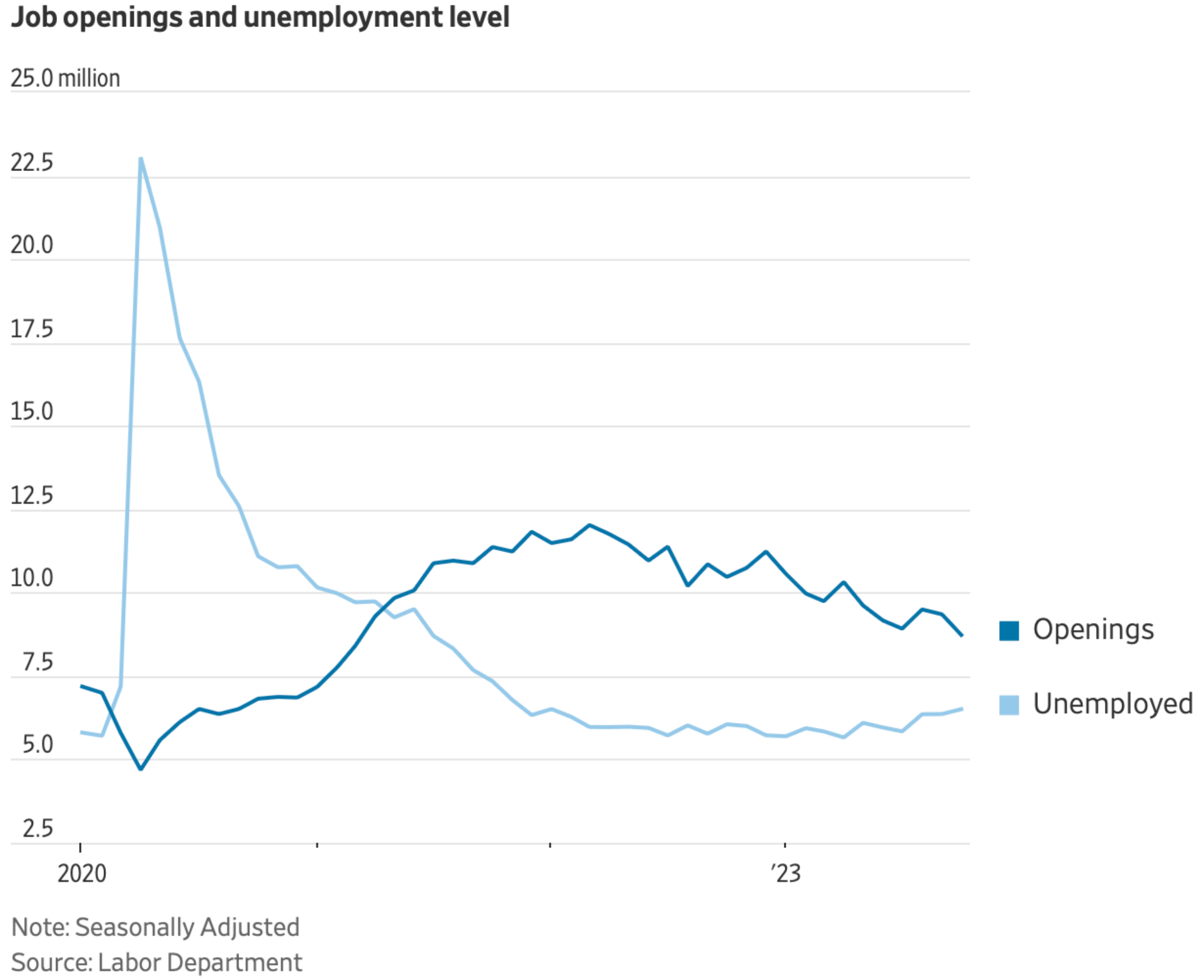
The November jobs report, out Friday, could provide additional clues about if the historically tight labor market is loosening further.

Less help wanted

Job openings fell 617,000 in October to 8.7 million. That level is well down from a record high of 12 million in March 2022, though higher than before the pandemic began.

There are still plenty of jobs available – more than the 6.5 million unemployed Americans seeking work – but that gap has narrowed. The job openings rate has trended down this year while the unemployment rate moved up. The relationship between the two readings – an economics concept known as the Beveridge curve – has moved close to pre-pandemic readings after trending well higher for the past two and half years. That adds to signs the labor market is normalizing.

The number of open jobs in insurance, real estate, and retail have all declined over the past year. One ominous sign: Businesses have said they need fewer extra workers for holiday jobs this fall.



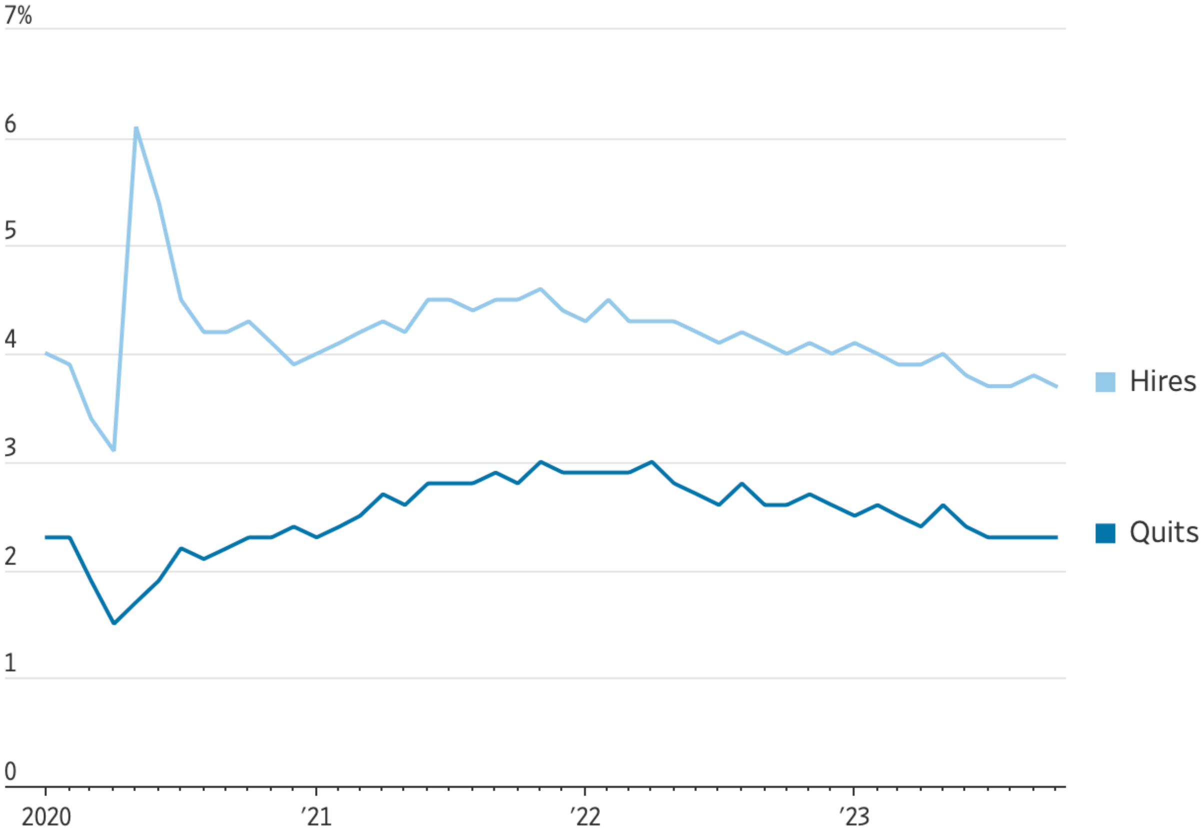
Workers quit quitting

The jump in resignations earlier in the pandemic recovery has dissipated. Economists see a declining rate of quitting as a sign workers are less certain about the labor market or that they are more satisfied with their current roles.

In October, the quits rate held steady from the prior month at 2.3%, but has trended down since touching 3% in April 2022.

Workers might have good reason not to leave their jobs without another lined up. The rate of hiring ticked lower in October from the prior month, extending a slow decline this year, suggesting employers are less desperate to fill roles.

Quits and hires rates

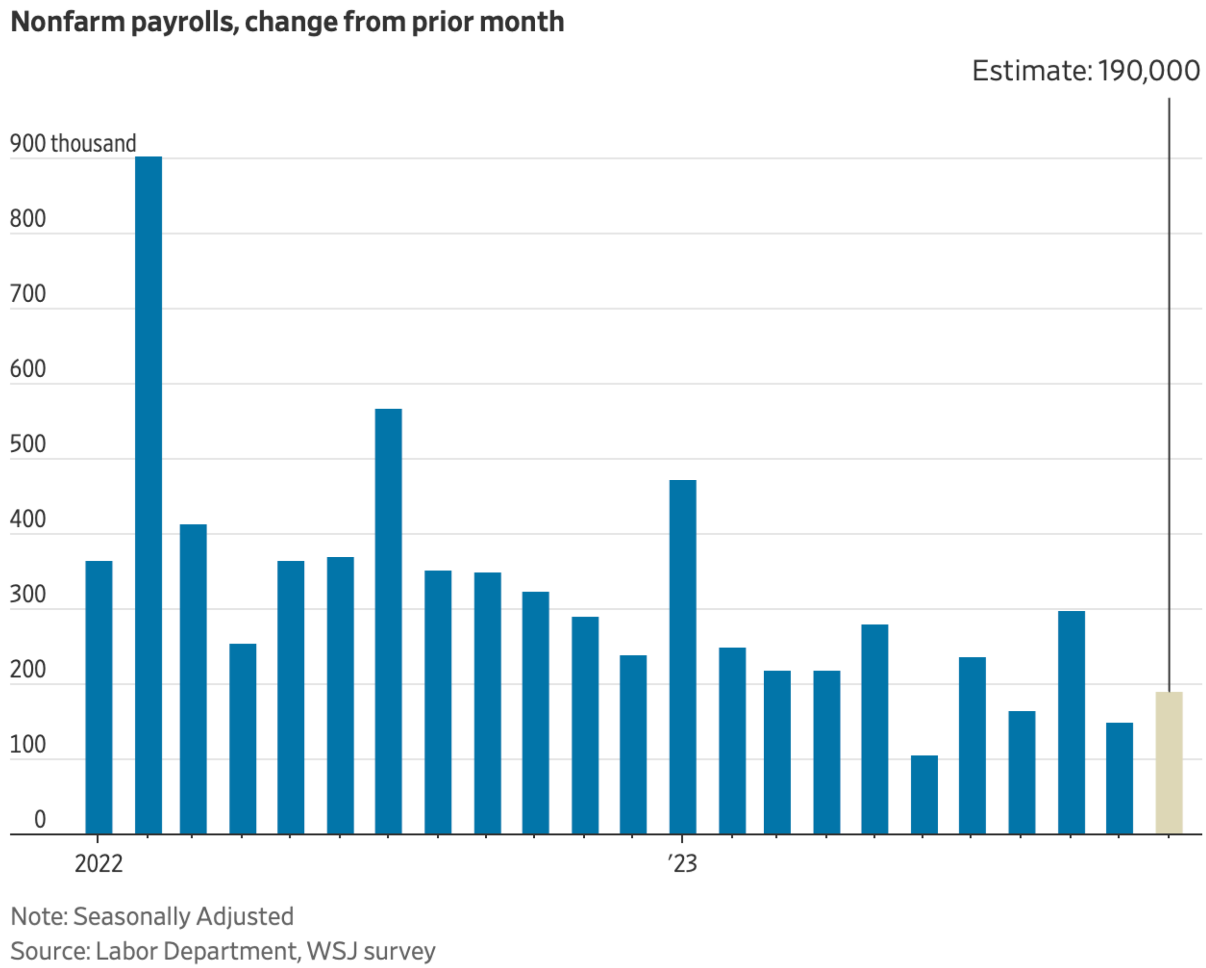


Note: Seasonally adjusted. The hires and quits rates are percentage of total employment.
Source: Labor Department via St. Louis Fed

Hiring slows down

Employers have added 239,000 jobs a month on average this year through October. That is a slowdown from nearly 400,000 a month in 2022 and more than 600,000 in 2021. Economists surveyed by *The Wall Street Journal* estimate that this cooling trend continued in November, with payrolls growing by 190,000...

Hiring has eased this year as the Federal Reserve pushed interest rates to a 22-year high this summer to combat inflation. That action has slowed the housing market and business investment, which has follow-on effects on the labor market. There are exceptions: Healthcare hiring is booming. The government and leisure and hospitality employers are also adding jobs at a solid clip.



Raises are getting smaller

When businesses were desperate to find employees in recent years, they offered workers some of the best raises of their careers. Now that companies appear less eager to hire, wage growth has cooled.

Pay gains remain above historic levels, and this year wages are rising faster than prices after falling behind earlier in the pandemic recovery. Slower wage growth can help cool inflation, especially for labor-intensive services.

Continue reading here (subscription may be required).

Liquidity may have been a boon for markets in 2023, but that may not be the case next year (from Lightman Investment Management)...

At certain times in 2023, it has felt like quantitative easing (QE) has returned. Markets have seen sudden liquidity-driven price moves where expensive equities sharply outperformed. This was particularly the case from March to May and in November.

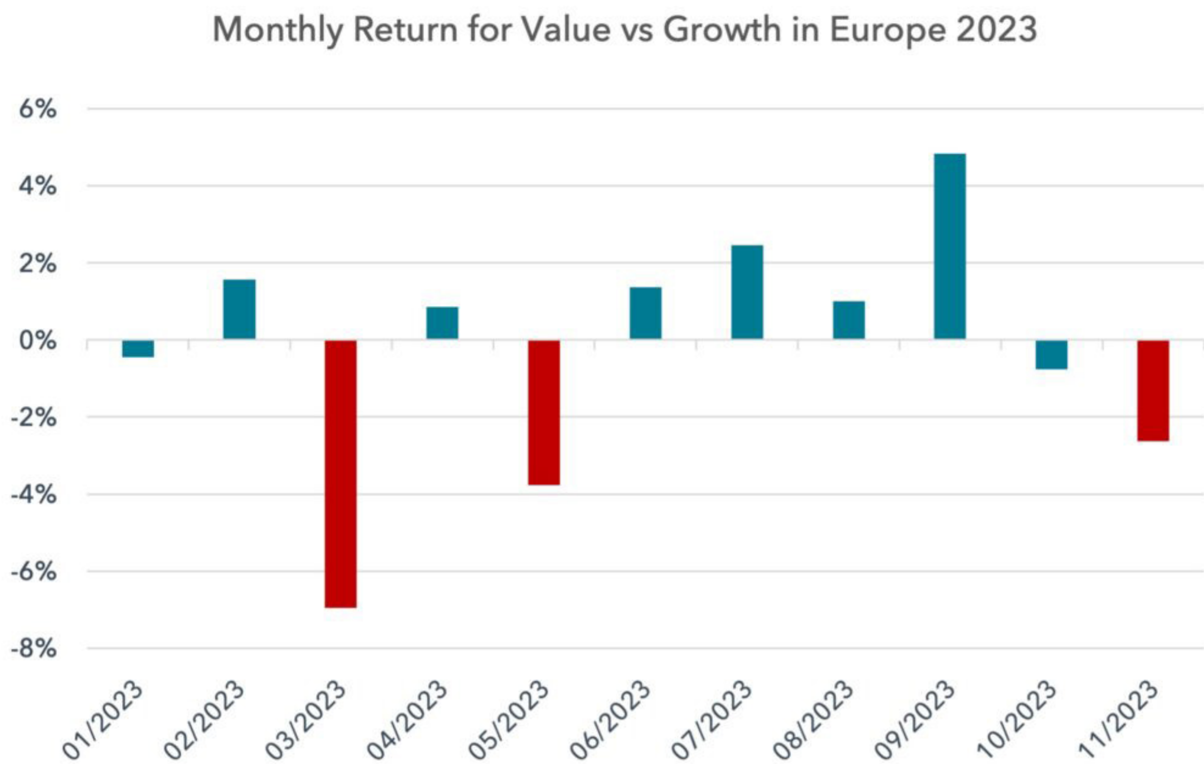
How can we have seen "QE-like" conditions with no QE? A deeper look into the Federal Reserve's balance sheet shows that at certain times this year changes in specific components of the balance sheet have indeed resulted in sharp increases in liquidity. These changes more than offset quantitative tightening (QT).

The reason it felt like QE had returned was because in some ways, for certain months this year, it had.

The good news is that this stealth or hidden QE is close to running its course and will not be present for the majority of 2024, nor likely 2025. Tighter market liquidity in 2024 should set the scene for a broader year of outperformance by value. It may also limit the scope for positive absolute returns from growth equities and, in particular, the technology sector.

A calm year for absolute returns, but volatility in relative performance

When looking at the distribution of monthly returns in 2023, value faced three very difficult months. It faced sharp relative drawdowns in March, May, and November. Whilst value may have outperformed over more months than growth so far this year, it has not felt like it.



In each of those difficult months, value securities were left behind, with expensive securities leaping higher. Markets behaved as if liquidity suddenly changed. In order to assess this, we need to look into the Fed's balance sheet.

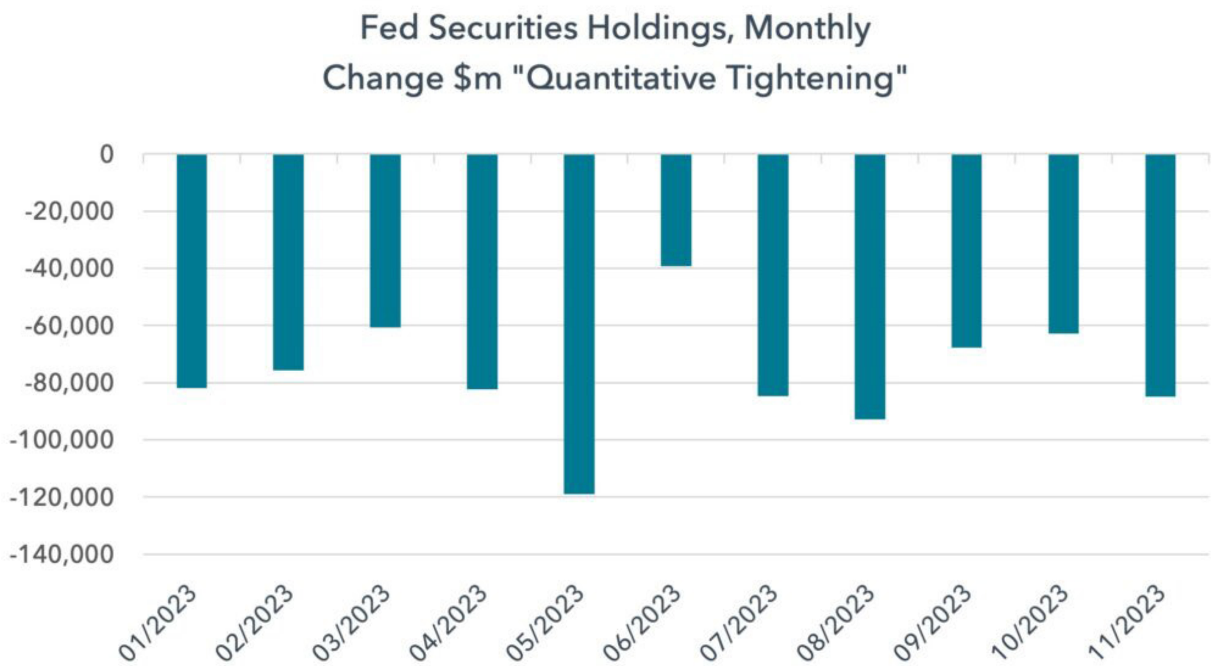
Components of the Fed's balance sheet

There are four components of the Fed balance sheet we need to focus on. It is the net change of all four added together that gives us the overall picture of market liquidity. Later in this note, we will show the net effect of these combined balances, but first we will show each individually.

1) Quantitative tightening

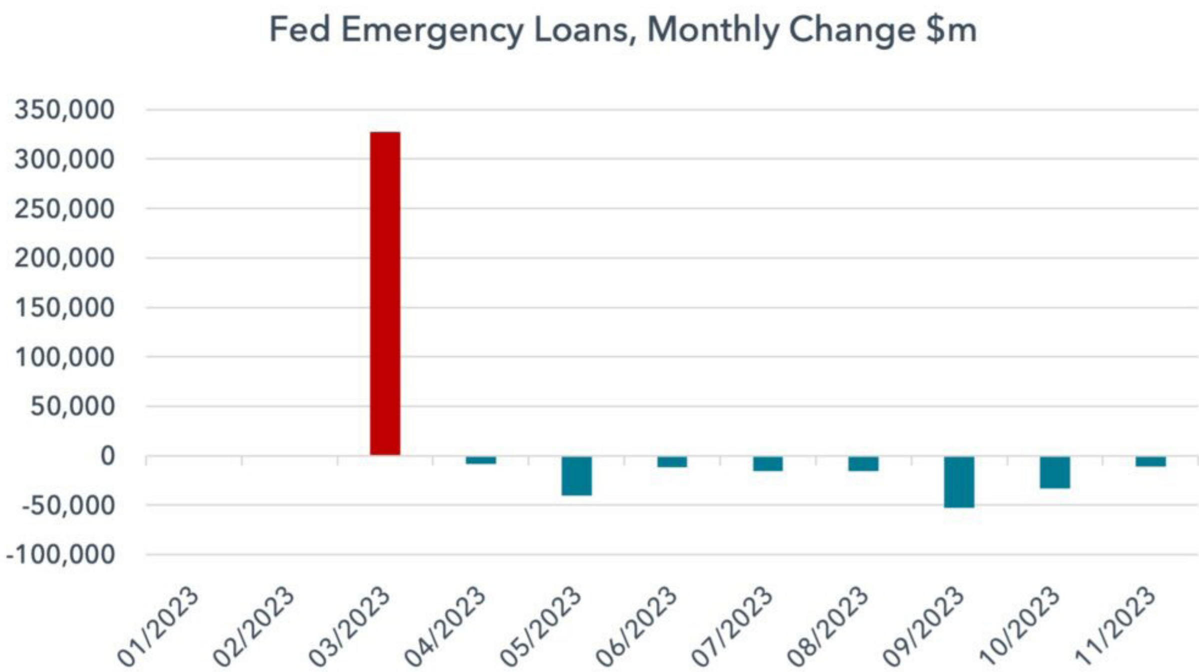
The first component that most investors monitor is the Fed's securities holdings. This includes securities bought under quantitative easing which are now running down under quantitative tightening. Quantitative tightening has continued through 2023, as we show in the chart below, averaging just under $77bn per month.

As the Fed runs down its securities holdings, new buyers need to be found for them. This acts to drain liquidity from financial markets to the tune of $75-80bn per month.



2) Fed emergency loans

During the Financial Crisis, the pandemic, and also during the Silicon Valley failure in March this year, the Fed made emergency loans to certain financial institutions. In normal times, this balance does not move much, but in times of crisis it can amount to significant liquidity creation. In March 2023 this balance jumped by $327bn. This liquidity was an important support to markets at that time. Liquidity creation, at a large enough scale, can drive markets higher, irrespective of other forces.

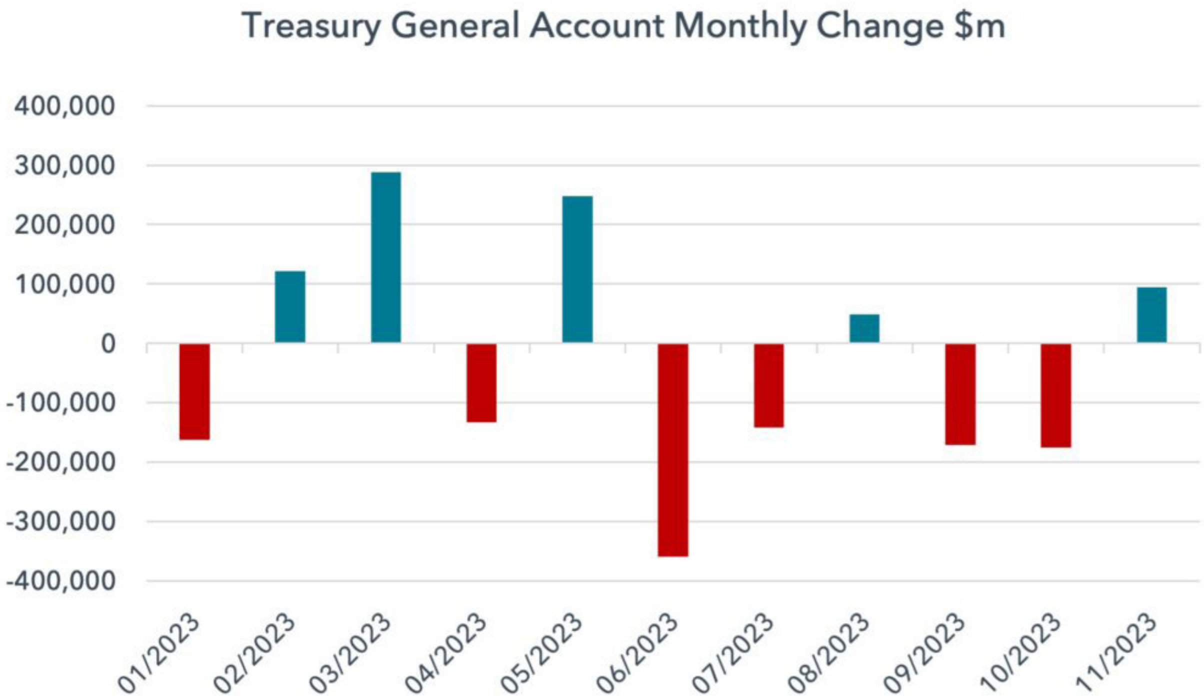


3) The Treasury General Account

The Treasury General Account (TGA) is the Treasury's checking account, where it keeps its cash, held at the Federal Reserve. The balance moves up and down according to U.S. government spending and revenue raising. Revenue can come from the receipt of tax payments or the sale of Treasury securities. Whilst the relationship is not perfect, from the point of view of market liquidity, as this balance moves higher, liquidity is broadly drained from financial markets; as it falls, liquidity is added. It can be understood like any other current account: as the balance rises, money is withdrawn from use and saved; as the balance falls, money is put to work and spent.

Earlier this year, as the debt-ceiling impasse took place, the Treasury was not able to issue debt. This forced it to run down its TGA balance to fund government spending, acting to increase liquidity – there was no borrowing and so no drain from financial markets, and there was government spending on the other side.

In the chart below, at the risk of repetition, a decline in the balance amounts to an increase in market liquidity, whilst an increase in the balance amounts to a decrease in liquidity. When bars are coloured red, it denotes an expansion in liquidity, while blue denotes a contraction.



4) The Reverse Repo Facility

The final balance to consider is the Fed's Reverse Repo Facility (RRP). This has played a big role in influencing market liquidity in 2023.

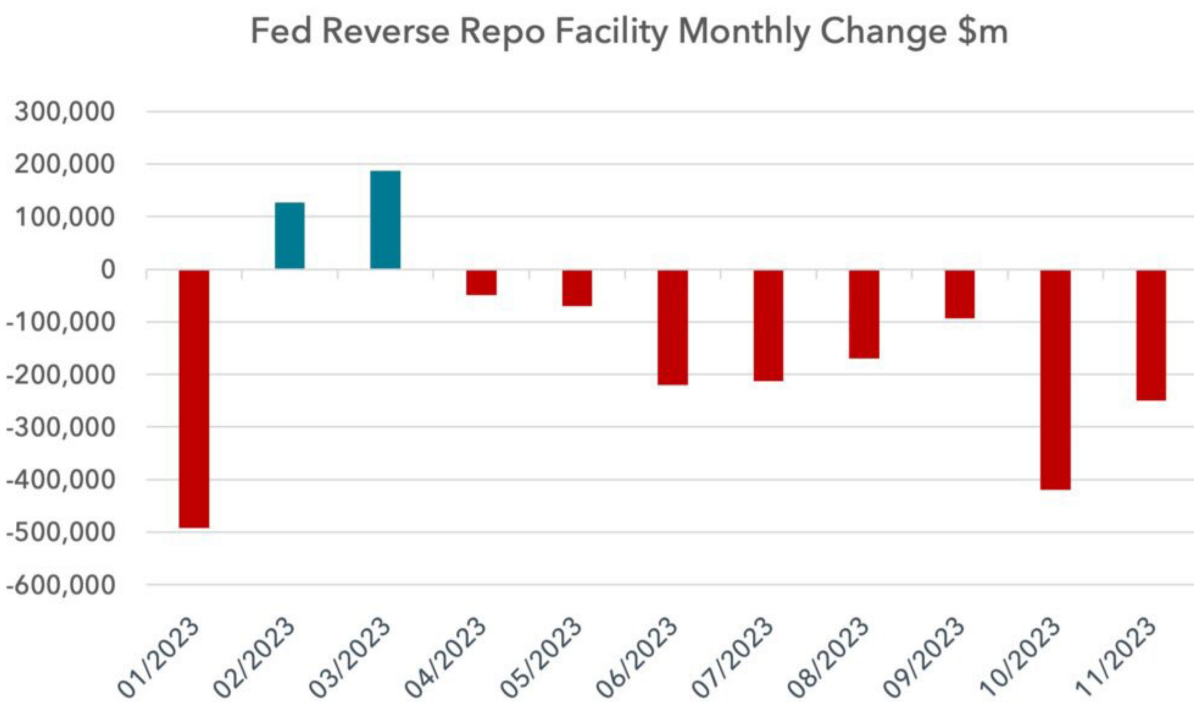
This facility is one of the Fed's tools to control interest rates. It is designed for non-bank financial institutions like money market funds, and here the Fed pays an overnight interest rate for balances deposited by these institutions.

Money market funds typically have a choice of investing in short-dated Treasuries or the RRP. As interest rates rise and are expected to rise further, money market funds tend to be incentivised to deposit money at the RRP. As rates are expected to fall, money tends to leave the RRP and go into the Treasury market.

Due to the peculiarities of the financial system post-COVID, these balances became very large in recent years. In 2021 and 2022, the RRP facility grew sharply, rising from $10bn in February 2021 to $2.5tn in December 2022. As this balance rose, it acted to drain money from financial markets. During 2023, as investors have seen rate hikes coming to an end, the RRP has fallen sharply, adding liquidity back.

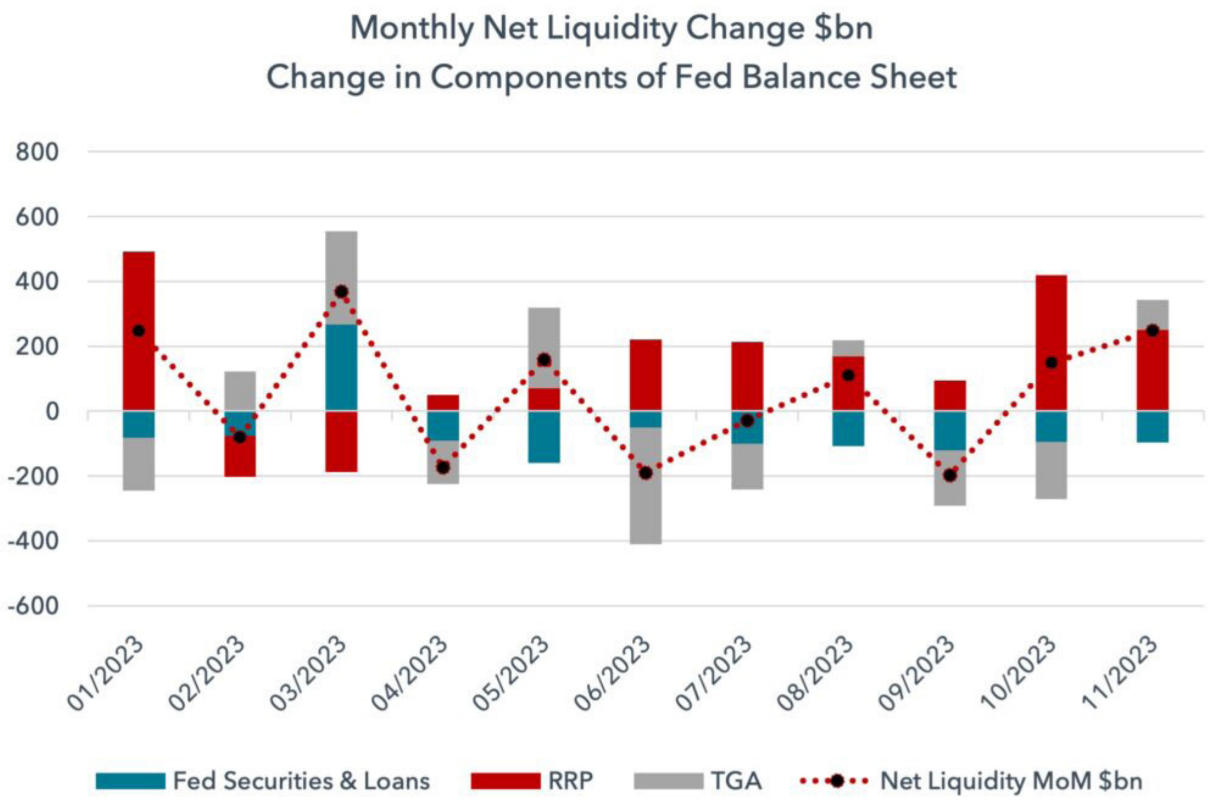
At the time of writing, the RRP is at $830bn, having started the year at $2550bn. As can be seen in the chart below, the monthly changes can be large. The average monthly liquidity increase from the RRP this year has been $150bn, with some periods seeing $400-500bn in a single month.

As with the TGA balance in the previous chart, a decline in this balance amounts to an increase in liquidity.



Aggregating all the changes in Fed balances to get a total monthly change in liquidity

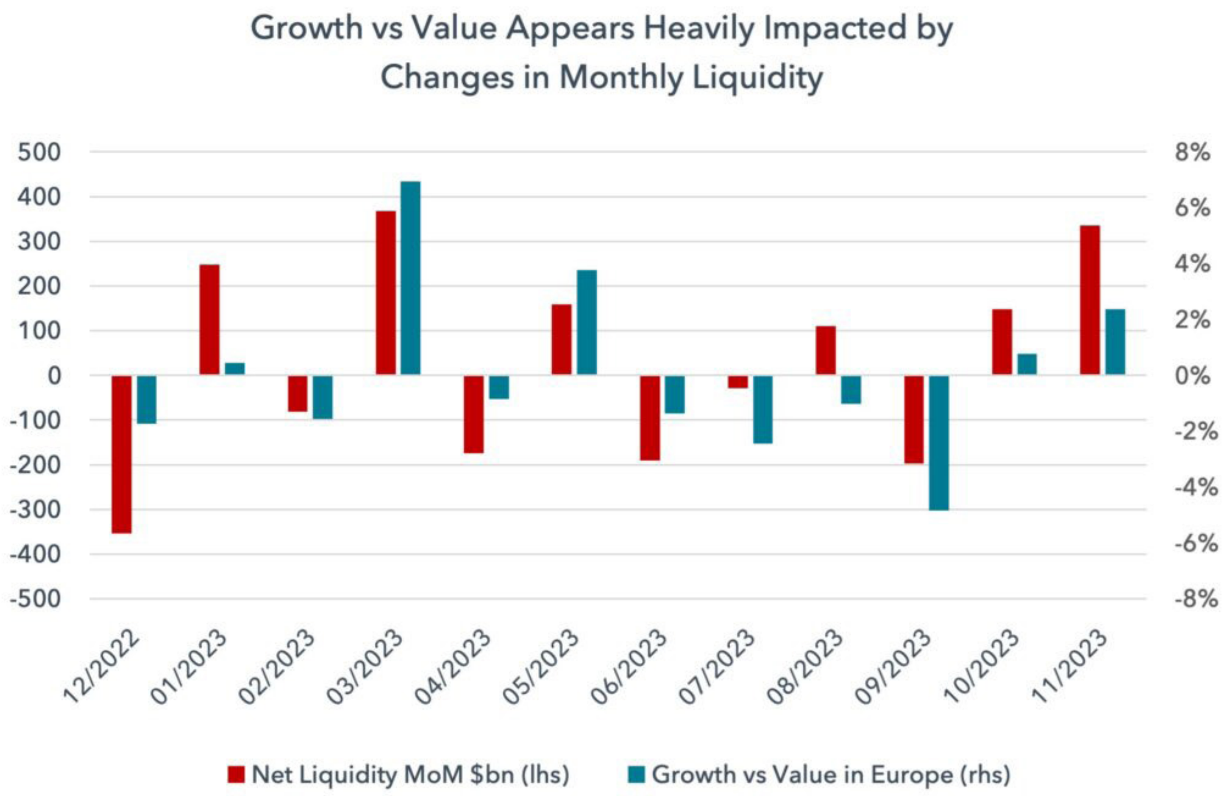
Below we show how all the components have shifted by month to impact liquidity in 2023. We have put the Fed's securities and loans into a single series. The bars show how the components changed month-on-month and the dotted line shows the net monthly change. In 2023 we saw liquidity creation in January, March, May, August, October, and November.



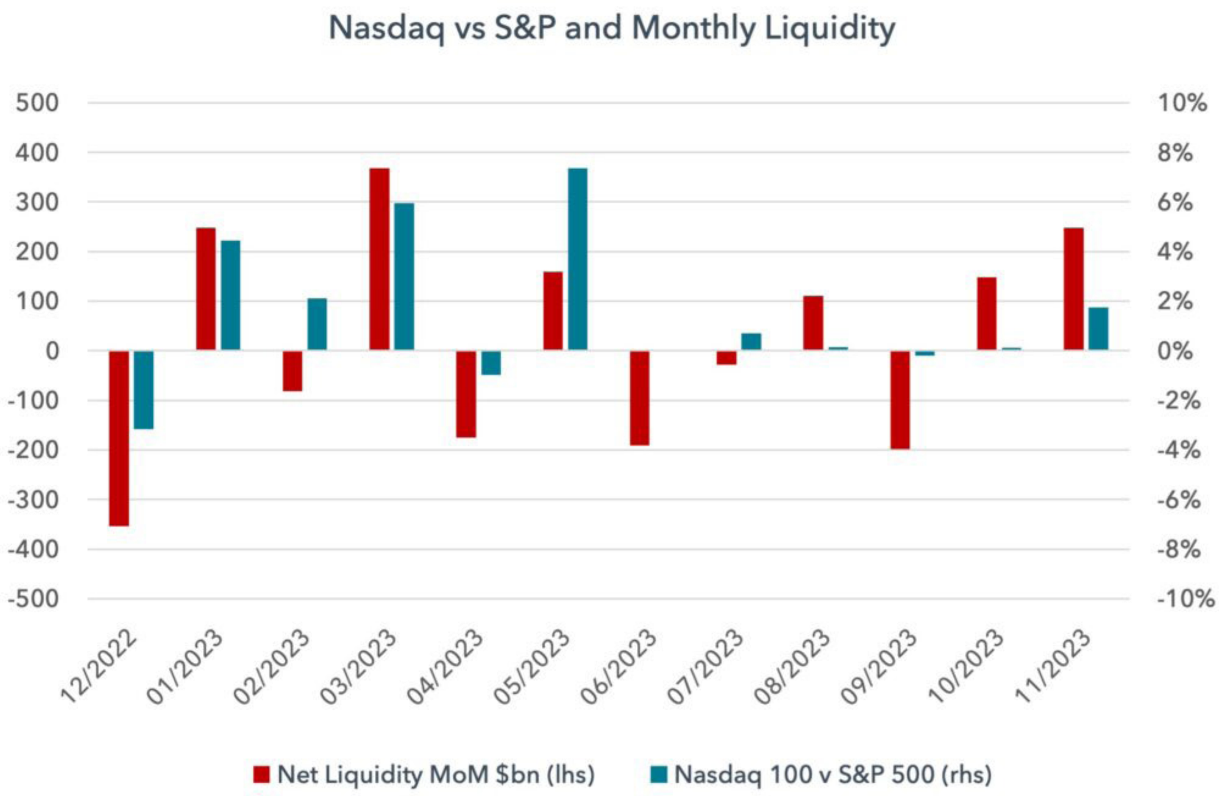
The impact of this liquidity on markets

Growth vs value appears to be heavily impacted by this liquidity over the last year. In all months where growth outperformed value, liquidity expanded by $150bn in a single month. Every time there was less than $150bn liquidity expansion, value outperformed.

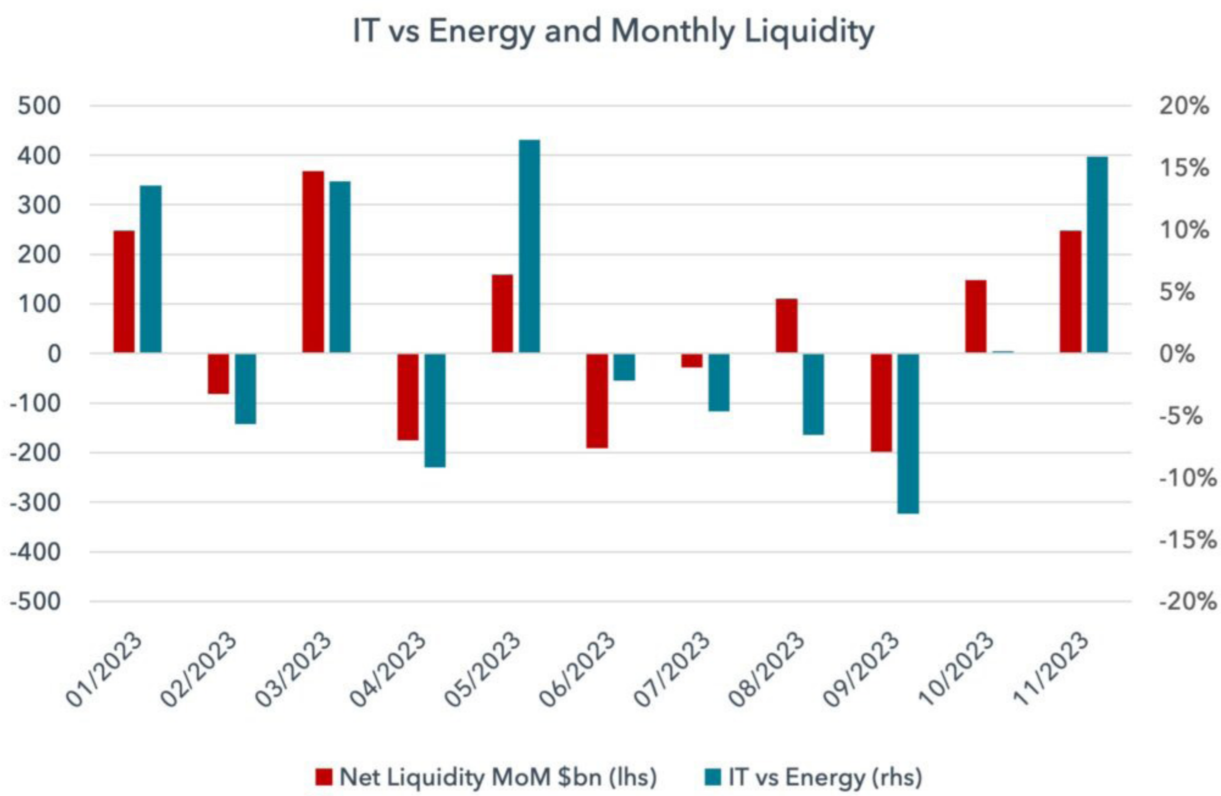
In the chart below, we show growth relative to value, where a reading above zero means growth is outperforming and a reading below zero means value is outperforming.



2023 has seen the Nasdaq outperform the S&P 500 quite consistently. But the bursts of outperformance appear strongest when there are large liquidity expansions, as we show below.



In a similar way, the IT sector appears to benefit from liquidity much more than the energy sector. When liquidity has contracted, energy has been defensive.



Within our own allocation to value, our overweights have shown themselves to be less sensitive to liquidity creation. Energy and metals & mining received no uplift when liquidity expanded. Similarly, they experienced no headwind when liquidity contracted. As these two sectors are large overweights, this has acted to hold the portfolios back in 2023.

The two most sensitive sectors to expanding liquidity are IT and consumer discretionary. We are close to zero weight in these sectors. So both in our underweights and overweights, we have low sensitivity to liquidity. This is the major reason why our funds have lagged year to date. But this attribute ought to help the funds in 2024 and 2025 as liquidity conditions become less abundant and potentially contract.

Why might these relationships hold?

There is a possibility that these relationships are spurious and simply coincidental. But the quantitative easing era saw peculiar stock market behavior relative to the last century. As we all know, value suffered significantly during QE. As soon as QE reversed and switched to QT, value decisively outperformed. This year, in the months where we have seen liquidity expand sharply, value has been held back once more.

The reason this relationship might hold could relate to mega-cap stocks capturing a higher market share of the liquidity, with growth stocks being dominant amongst mega-caps. It could also be to do with momentum and investment fashion – big liquidity creation finds itself flowing into fashionable large-caps, pushing them higher.

Why would commodity-facing equities be so insensitive to liquidity creation? It might be because commodity prices reflect the fundamentals of today, not tomorrow. They are priced off spot, reflecting the prevailing fundamental supply and demand dynamics each day. Liquidity flows ought not to be able to move underlying commodity prices in a meaningful way, and so the equities themselves should also be less sensitive.

There is also the duration argument that we have discussed before. Lower future interest rate expectations tend to lower the Reverse Repo balance, adding liquidity. But lower interest rate expectations may also lift the valuation of long-duration securities more than short-duration securities, driven by expected lower discount rates.

What about liquidity in 2024?

To come up with a picture of liquidity in 2024, we need to assess the outlook for all four Fed balances discussed above.

The Fed's securities holdings should continue to decline through next year. QT is expected to continue at $75-$80bn per month. It is expected to end only when bank reserves fall to 8-10% of GDP, and this is not envisaged until 2025 at the earliest.

What about the chances of QE returning? The Fed has stated that QE is a policy only to be used when interest rates are at the effective zero bound. This means rates must first be cut to near-zero before QE would be considered. This suggests QE may never return, or if it does, it is a long way off, likely measured in years. For this reason, we assume QT continues at the same pace for the remainder of 2024.

We do not expect any change in liquidity from the Fed's emergency loan programme.

The Treasury General Account is intended to be held at c.$750bn. This is deemed an appropriate balance for the U.S. government to hold for working-capital purposes. This balance also acts as a buffer in the event of further disputes relating to the debt ceiling. The current balance is $753bn, so we forecast no change in the TGA next year.

The major source of liquidity that remains is from the Reverse Repo Facility. From its level of $830bn today, we anticipate it moving to zero at a rate of $150bn per month, in line with what has taken place in 2023. This suggests that the RRP balance would be liquidated by early May 2024.

Below is a table of the monthly liquidity change expected over the coming eight months.

	Dec 23	Jan 24	Feb 24	Mar 24	Apr 24	May 24	Jun 24	Jul 24
QT	-80	-80	-80	-80	-80	-80	-80	-80
RRP	150	150	150	150	150	65	0	0
TGA	0	0	0	0	0	0	0	0
Total Monthly Liquidity Change	70	70	70	70	70	-15	-80	-80

Whilst we can expect an expansion of liquidity for a few more months, the amounts are far smaller than we saw in the boom months of 2023. Here we saw expansions of $150bn to $370bn. It was only in those huge $150bn-plus expansions that value underperformed. A net $70bn that we forecast from December 2023 to April 2024 should not amount to a significant threat to value. As liquidity tightens through the year, we would expect value's outperformance to accelerate.

What about interest rates in 2024?

Investors are discounting 125bps of rate cuts in the U.S. and Europe over the next year. Could this amount to a significant tailwind for growth-style investing and a headwind for value? We would say no, for two reasons.

First, the major liquidity expansion from these potential rate cuts has already hit markets and is behind us. The decline in the RRP balance has created $1.7tn of liquidity this year. This injection of liquidity took place because of the perception of future rate cuts. As we have discussed above, 2024 sees QT continuing and “only” $830bn left in the RRP. This balance is not big enough to move the needle in 2024.

Second, it is the long end of the yield curve that matters for valuation, not the short end. Whilst the Fed can cut interest rates at the short end, it cannot drive down interest rates at the long end. As we have discussed in previous notes, the supply of bonds in the coming years is so high relative to demand, that it is hard to see long bond yields falling much more, even in recession.

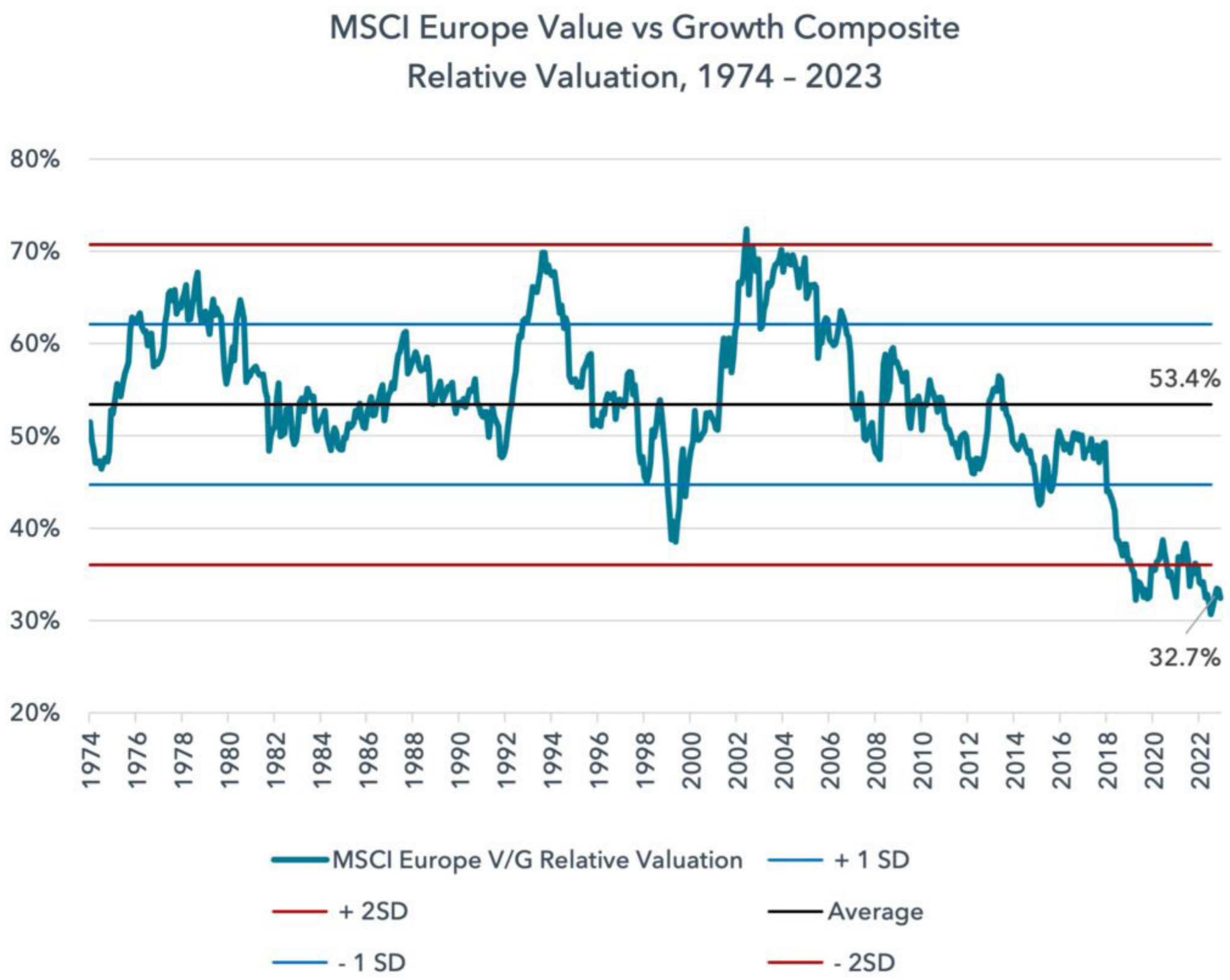
To hold value back in 2024 we need to see ultra-low bond yields and this appears unlikely.

Why does growth investing appear to require such abundant liquidity and what does it mean for value?

There are many possible theories why growth investing needs nearly $150bn of monthly liquidity creation. One could be related to the size of the fiscal deficit. The U.S. government is borrowing c.$140-160bn per month to fund its deficit. Because it needs to find new buyers to fund this debt issuance, this amounts to a drain on market liquidity that sits outside the Fed’s balance sheet. Perhaps it is not a coincidence that central bank-driven liquidity needs to expand by this much to support expensive growth equities?

But perhaps a more compelling argument is that the fundamentals for value are so strong that only a deluge of liquidity can stop it from outperforming.

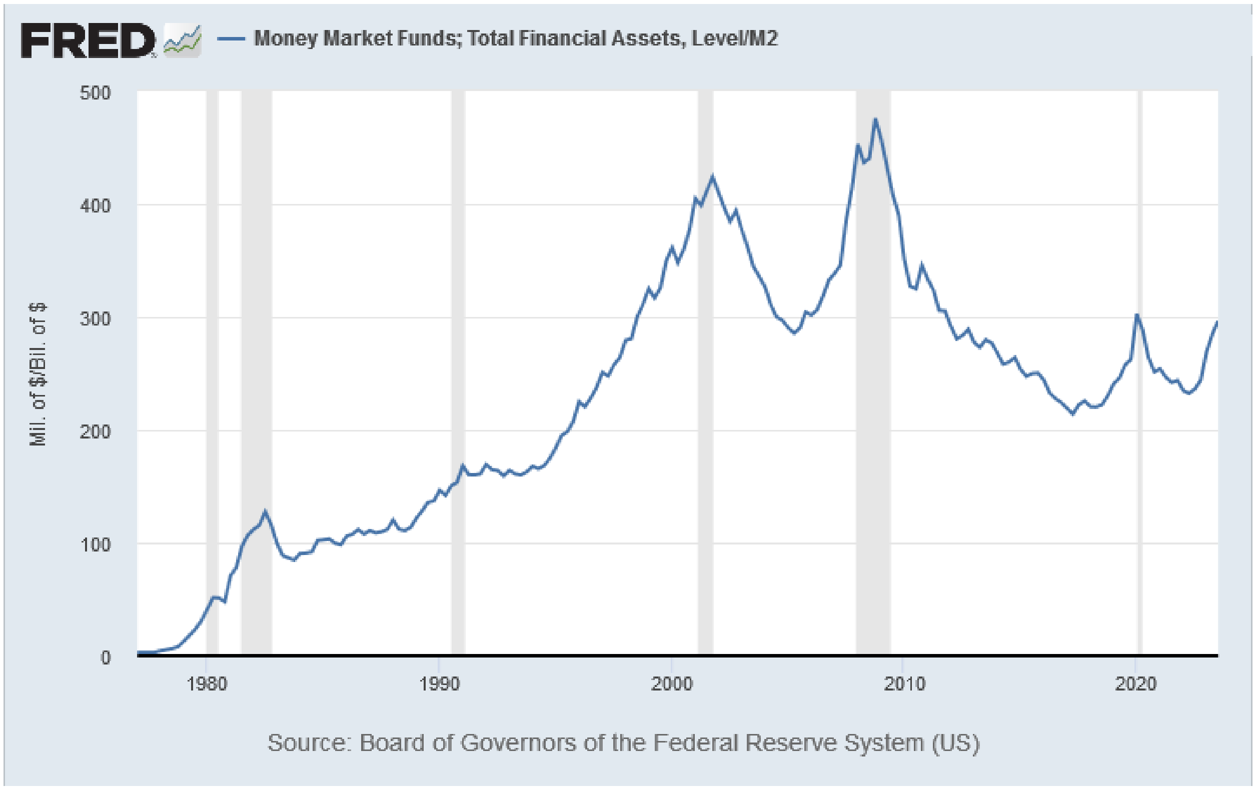
Value equities remain at a 50-year low in relative valuation compared to expensive growth equities. In the last 50 years, they have traded at an average valuation of 53% of the price of growth equities. Today the price is 33%. Returning to the 50-year average would require 60% outperformance in re-rating alone. As we have seen in recent years, many value companies are growing faster than growth companies and so earnings growth can provide more upside. The elastic band is pulled back. It does not take much for value to outperform, as we have seen in recent years.



This exercise has shown that we can put an approximate figure on what it takes to stop value outperforming. That number is $150bn per month. The good news is we are unlikely to see that level of liquidity creation in 2024, leaving us confident that value's outperformance is set to return more broadly and decisively.

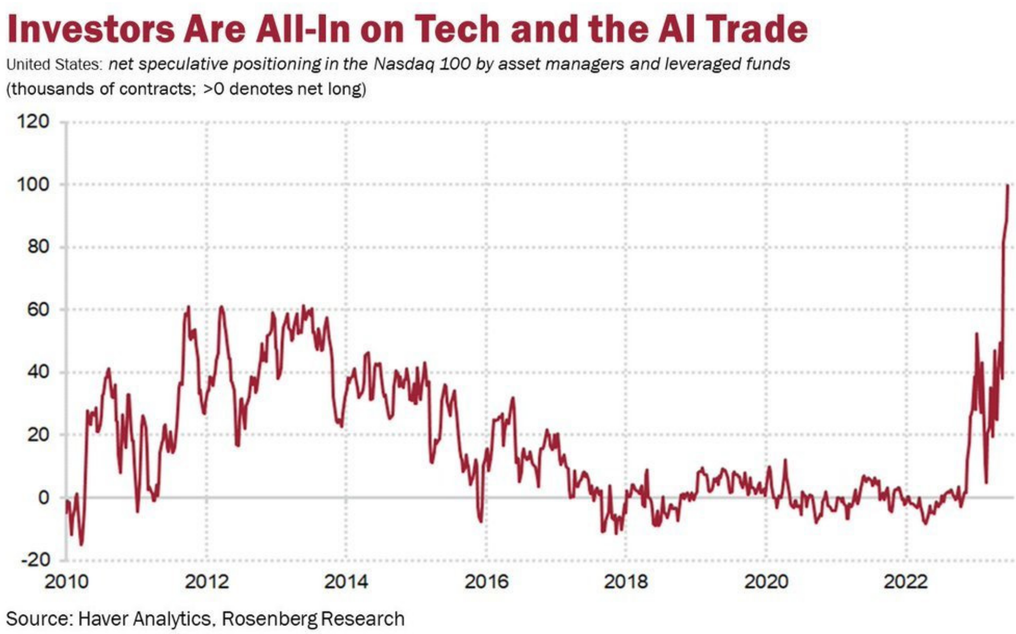
This chart suggests the bullish "cash on the sidelines" argument isn't all it's cracked up to be (from Tom McClellan via X)...

With so many analysts talking about all of the "cash on the sidelines" sitting in money market funds, I got to wondering about how it compares to the total money supply. Here is that comparison (to M2, not seasonally adjusted).



Speculative positioning in tech stocks has gone parabolic this year (from Martin Pelletier via X)...

Markets are getting very crowded here.



Dow Theory – an "old school" form of technical analysis created by *Wall Street Journal* co-founder Charles Dow and popularized by the late, great newsletter writer Richard Russell – is still sending a cautious message about stocks (from The Elliott Wave Financial Forecast)...

The Dow Jones Transportation Average has been lagging notably during the rally that started on October 27. There exists a long-term bearish Dow Theory non-confirmation between the Industrials and the Transports, as shown on the [below] chart.

While the Industrials closed at a new high, the Transports are nowhere near their closing high of November 2, 2021. A shorter-term bearish non-confirmation occurred at the Industrial's January 2022 high, which led to the decline to September 2022.

The current non-confirmation is far larger and has much bigger bearish implications for the market. The non-confirmation will turn into a bear market signal when both indexes close below their prior intermediate term closing lows on October 27.

Beware the most crowded trade on Wall Street – next year's "soft landing" (from *The Wall Street Journal*)...

At the end of last year, investors thought recession was a done deal. The year before, they thought big tech would be immune to rate increases. And a year before that, they were convinced that paying high prices for stocks popular with the wider public would make them rich.

This December, they believe, again with absolute conviction, that the economy is heading for a soft landing and lower interest rates. Maybe this time they will be right.

Then again, maybe not. Being in the crowd is always an uncomfortable place for an investor, but agreeing with such a strong consensus is especially difficult, because if it turns out to be wrong, the punishment from the markets will be painful – just as it was in each of the past three years.

The consensus that next year the Federal Reserve will be able to slash rates without facing recession was strong even before the central bank put out a dovish forecast on Wednesday. It got even stronger as a result of the Fed's new "dot plot" of forecasts, with futures traders putting a 16% probability on a rate cut as soon as next month and an 82% chance of a cut by March...

The reaction to the Fed wasn't really about what the Fed predicted, though. The median policy maker's "dot" forecast of interest rates at the end of next year dropped to 4.6%, from 5.1%. But the federal funds futures market is 100% sure that rates will be much lower, according to CME Group's FedWatch.

Instead, investors took the Fed's prediction – and Chairman Jerome Powell's answers at a press conference afterward – as evidence that they were right to think the Fed would cut rates early and often as the economy glides smoothly into that rarest of outcomes, the soft landing.

An outcome other than a soft landing would definitely be a problem for markets. But it is also that so much is riding on its happening. A soft landing isn't just priced – it is priced in and more.

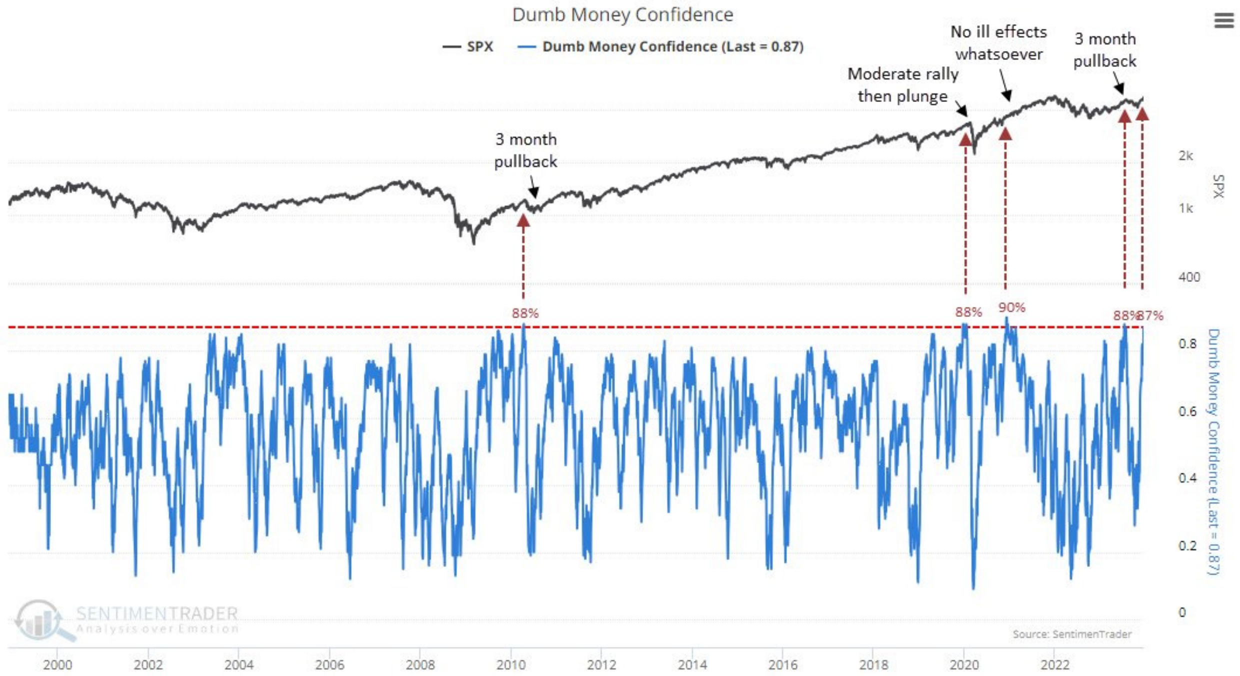
"Talk to investors and there's this strong sense that we get through this rate cycle without any major accidents," says Peter Oppenheimer, chief global equity strategist at Goldman Sachs. "It may still be a bit naive and premature to believe that." Goldman has been arguing for a soft landing since last year, but the market's rapid rally has already caught up with the bank's three-week-old S&P 500 forecast for the end of next year.

Continue reading here (subscription may be required).

Data suggest retail investors are "all in" on stocks again ([from Jason Goepfert via X](#))...

Dumb Money Confidence just jumped to the third-highest reading in 25 years.

It was no problem at all in 2021. Other than that, very high Confidence typically precedes modest gains at best until sentiment resets.



Recent poll suggests most Americans are ignorant of even basic economics (from Lawrence Lepard via X)...

I live in a country of the galactically stupid: h/t John Rubino for finding this.

The Fed is betting its reputation on an unlikely "soft landing" (from former New York Fed president Bill Dudley via *Bloomberg*)...

The U.S. Federal Reserve and its chair, Jerome Powell, are betting that they can have the best of both worlds – that they'll be able to defeat excessive inflation without forcing the economy into recession.

I hope it goes well. Unfortunately, there's still a significant chance it won't.

Powell surprised markets last week with his extraordinarily dovish comments on the outlook for interest rates. He took further increases off the table and put the prospect of cuts firmly on. This was a big shift: Only two weeks earlier, he had opined that any talk of rate reductions was premature. "Higher for longer" is now in the trash bucket. Instead, officials are expecting further declines in inflation that will make earlier and more rapid rate cuts possible, even necessary.

Powell noted that the latest consumer-price report implied that the Fed's preferred measure of inflation – the core personal consumption expenditure price index – will likely register a 3.1% year-over-year increase when the next data are released at the end of December, indicating progress toward the Fed's 2% objective. The median expectation in the December Summary of Economic Projections is for three 25-basis-point interest-rate reductions in 2024, ending the year 50 basis points below the September projections...

The pivot significantly lowers the risk of a recession and hard landing – in large part through its effect on markets. Fed funds futures are already pricing in a full 150 basis points of easing next year. Since the end of October, 10-year Treasury note yields have fallen by about 90 basis points, the stock market has increased by more than 10%, credit spreads have narrowed, and the dollar has weakened. The Goldman Sachs Financial Conditions Index has eased by about 100 basis points, and the firm's economists now expect the economic impulse to be positive in 2024. The Fed's own financial conditions index will soon tell a similar story.

Problem is, the central bank's dovishness also increases the possibility of no landing at all – that is, overheating and persistent inflation that could undermine the Fed's credibility, while requiring renewed tightening and a deeper recession to get things back under control.

Continue reading here (subscription may be required).

Here's a comprehensive list of 2024 macro outlooks from major banks and asset managers (from the Long View via X)...

U.S. BANKS

JPMorgan https://shorturl.at/eltPT

JPMorgan Private Bank https://shorturl.at/eyzHK

Goldman Sachs https://shorturl.at/gqLX2

Goldman Sachs Asset Management https://shorturl.at/mCSW1

Morgan Stanley https://shorturl.at/jlmzA

Bank of America https://shorturl.at/iuxyF

Bank of America Private Bank https://shorturl.at/ajsv7

Citi https://shorturl.at/puW07

Wells Fargo https://t.ly/2bF1E

BNY Mellon https://t.ly/BCLLT

State Street https://t.ly/p47tE

Lazard https://t.ly/ZkkUm

T. Rowe Price. https://t.ly/e9b3d

TD Securities https://rb.gy/nnjx81

Charles Schwab https://rb.gy/lzcgh4

RBC Capital Markets https://rb.gy/0guz6u

EUROPEAN BANKS

UBS https://rb.gy/r6vi0m

HSBC https://rb.gy/43mdwp

Deutsche Bank https://lnkd.in/eVsPCNVR

BNP Paribas https://lnkd.in/erFVwJKR

Barclays https://lnkd.in/ec8WyWP3

Lombard Odier Group https://lnkd.in/ePHr8mK4

Macquarie Group https://lnkd.in/enqQSUmB (Australia)

ASSET MANAGERS

BlackRock https://lnkd.in/eSxDA_bR

Amundi https://lnkd.in/ei6QXd7n

M&G plc https://lnkd.in/e_PaFDwR

Man Group https://lnkd.in/edXtr7NP

Wellington Management https://lnkd.in/exnzD8_E

Invesco US https://lnkd.in/egzQrPAu

Legal & General Investment Management (LGIM) https://lnkd.in/e7hjAkx6

Schroders https://lnkd.in/ewiRsg-t

Deutsche Bank (Wealth) https://lnkd.in/efw_cwRd

Allianz https://lnkd.in/ehuSey7i

AXA IM https://lnkd.in/e4iDZ9_M

PIMCO https://lnkd.in/eKA7hdBB

Capital Group https://lnkd.in/ehH2jW3a

Julius Baer (secular outlook) https://lnkd.in/eaN5EfJV

Pictet https://lnkd.in/eziFnGU8

Vanguard https://lnkd.in/e8Fnrs2C

Fidelity https://lnkd.in/eB6tJZb4

Cambridge Associates https://lnkd.in/eTHqAe4w

PRIVATE EQUITY FIRMS

KKR https://lnkd.in/e_m6UE5F

Apollo Global Management, Inc. https://lnkd.in/eCHMuRvV

Blackstone https://lnkd.in/edyFqR63

BlackRock (Private Markets) https://lnkd.in/eiGcGCfy

AUDIT AND CONSULTING FIRMS

Deloitte https://lnkd.in/e9Vz8dKU

PwC https://lnkd.in/ebENpssC

EY https://lnkd.in/ewKh8m9m

Boston Consulting Group (BCG) https://lnkd.in/eDsnJRfQ

This has been a "Bad Santa rally" ([from *The Financial Times*](#))...

[L]ast week's Fed pivot was a bona fide Christmas miracle. As mainFT's Katie Martin wrote this weekend:

"The only thing Jay Powell could have done to deliver a stronger impression of a festive giveaway to global markets this week would have been to conduct his press conference decked in an oversized red suit with fluffy white trimmings and a matching hat."

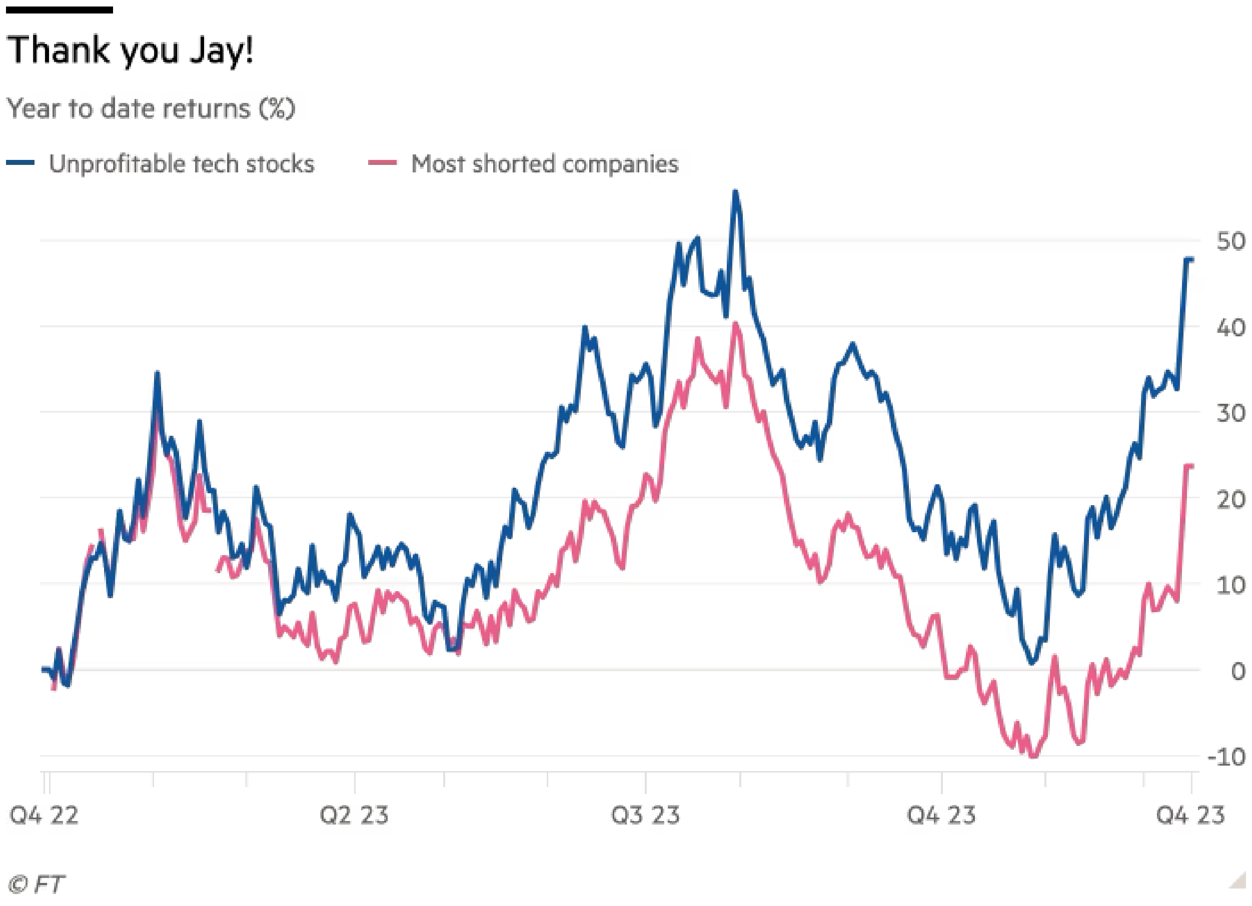
Bond yields plunged across the board, with the 10-year Treasury yield falling below 4 per cent for the first time since summer. The MSCI All-Country World Index jumped 2.6 per cent last week for its seventh consecutive week of gains – the longest streak in almost six years.

As JPMorgan's Phoebe White wrote: "Christmas came early." It has already forced Goldman Sachs's David Kostin to raise his 2024 target for the S&P 500...

However, if this is a proverbial Santa rally, it looks more like the Billy Bob Thornton version than Edmund Gwenn.

Most of the Magnificent 7 that have powered much of the U.S. stock market rally actually underperformed last week. In contrast, trashier stocks and assets ripped higher. And broadly speaking, the trashier they were the better they did.

For example, Goldman Sachs's custom indices of unprofitable technology companies and the most heavily shorted stocks rocketed 8 per cent and 12 per cent respectively last week thanks to the Fed's "dovish hold".



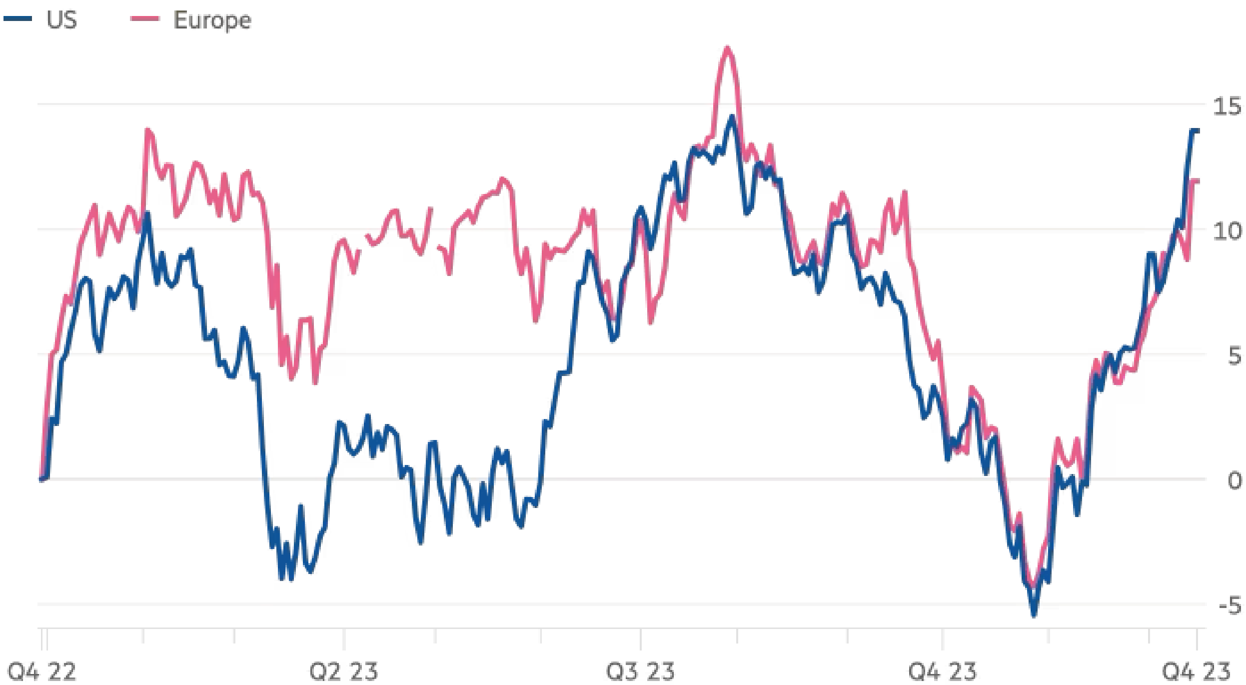
To highlight just two examples, Nikola and Carvana both jumped about 27 per cent last week.

(It's hardly the meme stock short-covering saga reloaded, but it will be interesting to see the end-of-month performance of a lot of hedge funds.)

There was a similar rally in companies with weak balance sheets in the U.S. and Europe (weak-balance-sheet stocks in Asia also bounced, but only a little, which makes sense given that many of them are Chinese real estate-related stocks for whom a Fed pivot will be scant help).

The pivot party

YTD returns for companies identified as having weak balance sheets (%)



© FT

SPACs also enjoyed last week, jumping 3.7 percent to extend the gains since October to 20 per cent and once again putting them as a group within touching distance of clawing back the 2022 losses.

IPOX SPAC index

Index points

Source: LSEG
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Fund managers are the most optimistic since the previous bull market peaked in early 2022 ([from *Bloomberg*])...

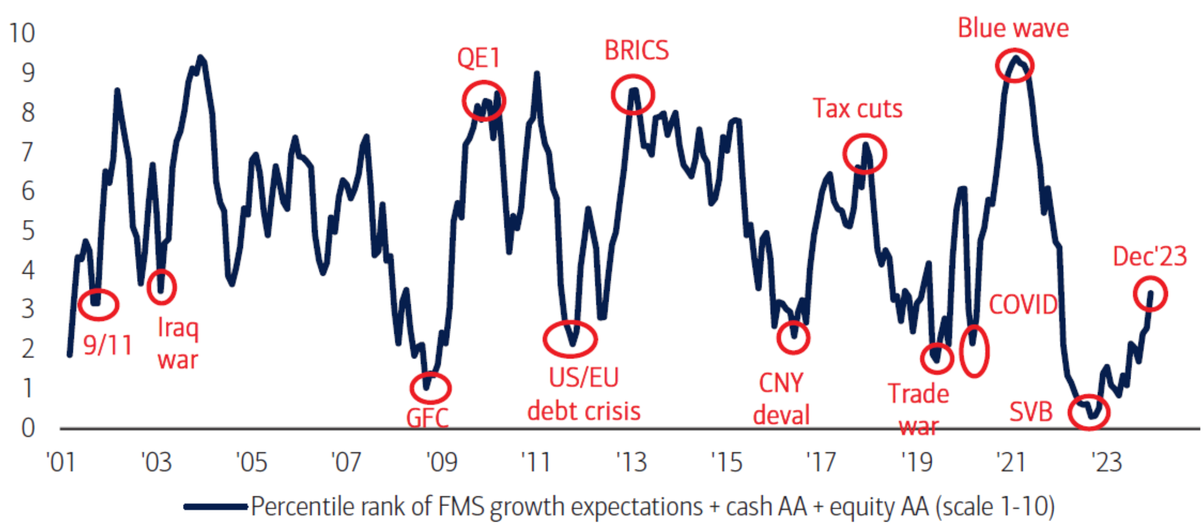
Investors are the most optimistic since the beginning of 2022 as expectations of policy easing by the Federal Reserve are fueling a rush into stocks, according to a Bank of America Corp. survey.

The sentiment of global fund managers surveyed in December was the most upbeat since January 2022 on a Goldilocks environment – a steady economy that is not running too hot or too cold – as the case for next year, a team of strategists led by Michael Hartnett wrote in Tuesday's note.

Against that backdrop, the poll showed investors are the most overweight on stocks since before the Fed started to hike interest rates, with cash allocations cut to a two-year low of 4.5% from 4.7%. Meanwhile, fund managers are the most overweight on bonds in 15 years. They are also the most bearish on commodities relative to bonds since March 2009.

"Policy, not positioning" is the new tactical driver of asset prices, Hartnett said.

Chart 2: FMS sentiment improved to highest since Jan'22
Percentile rank of FMS growth expectations + cash level + equity allocation (scale 0-10)



Source: BofA Global Fund Manager Survey; (0=bearish, 10 = bullish)

BofA GLOBAL RESEARCH

Continue reading here (subscription may be required).

This month saw the largest one-day inflow into stocks in history (from The Kobeissi Letter via X)...

This is incredible:

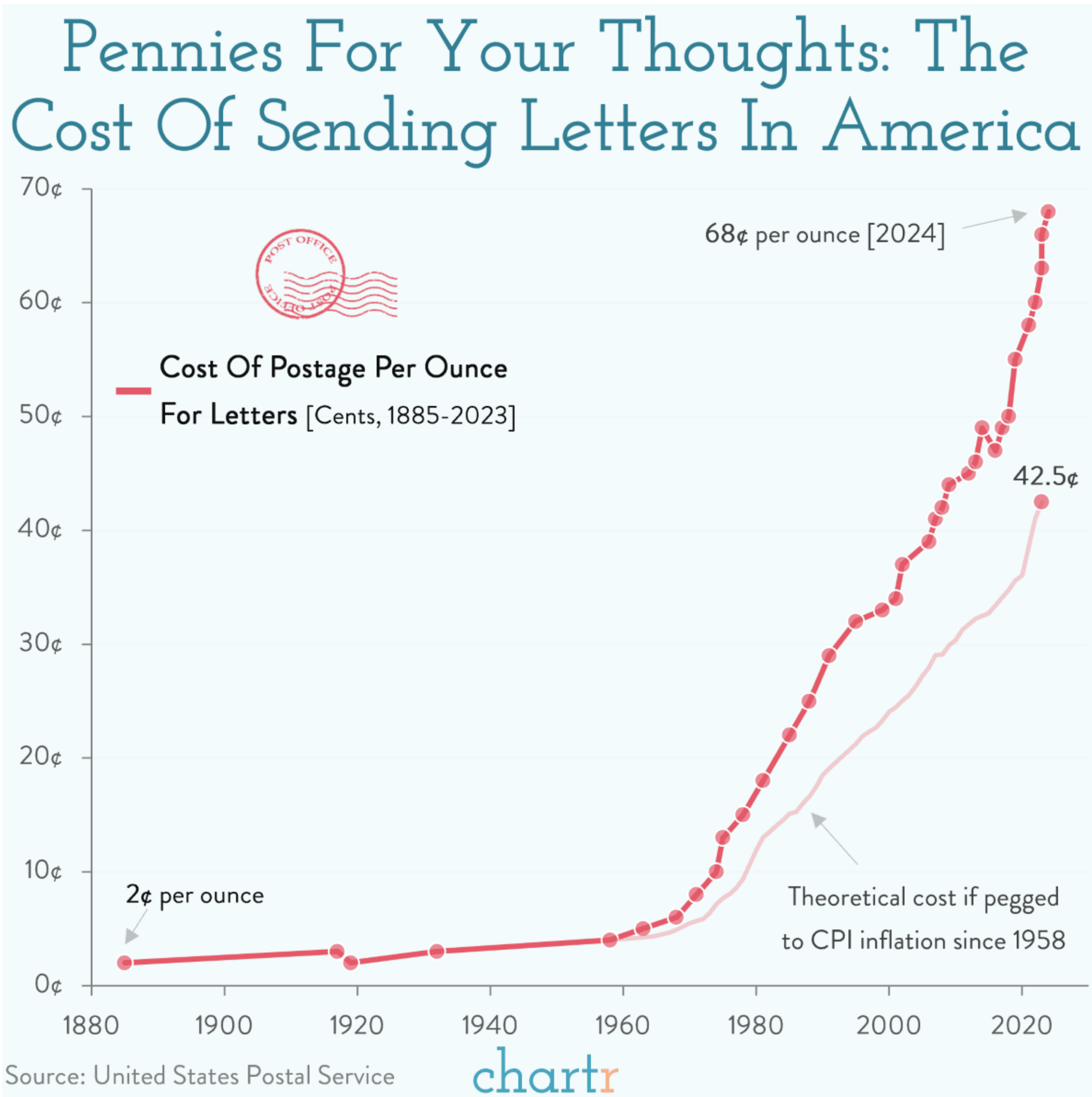
On Friday, the S&P 500 ETF, $SPY, saw its biggest single-day inflow on record, at $20.8 billion. Dating back to the ETF's inception in 1993, this has never been seen.

Total inflows last week alone hit $24 billion, also posting a new record. Yesterday, $SPY saw ANOTHER $10 billion of inflows, putting the total at nearly $35 billion since last Monday.

That's $35 billion in six trading days, or $5.8 billion PER DAY.

Santa Claus Rally is an understatement.

This chart shows the consumer price index (CPI) is nonsense (from Chartr)...



In 1885, the cost to send a letter was just two cents an ounce, today the same privilege – after two price increases this year – will set you back 66 cents, with another price increase slated for 2024. For much of the last century, any hikes have broadly mirrored inflation, however, since 1958, the price of letter-sending has outstripped the wider CPI.

Are banks now "gaming" the Fed's emergency lending program? ([from Paulo Macro via X](#))...

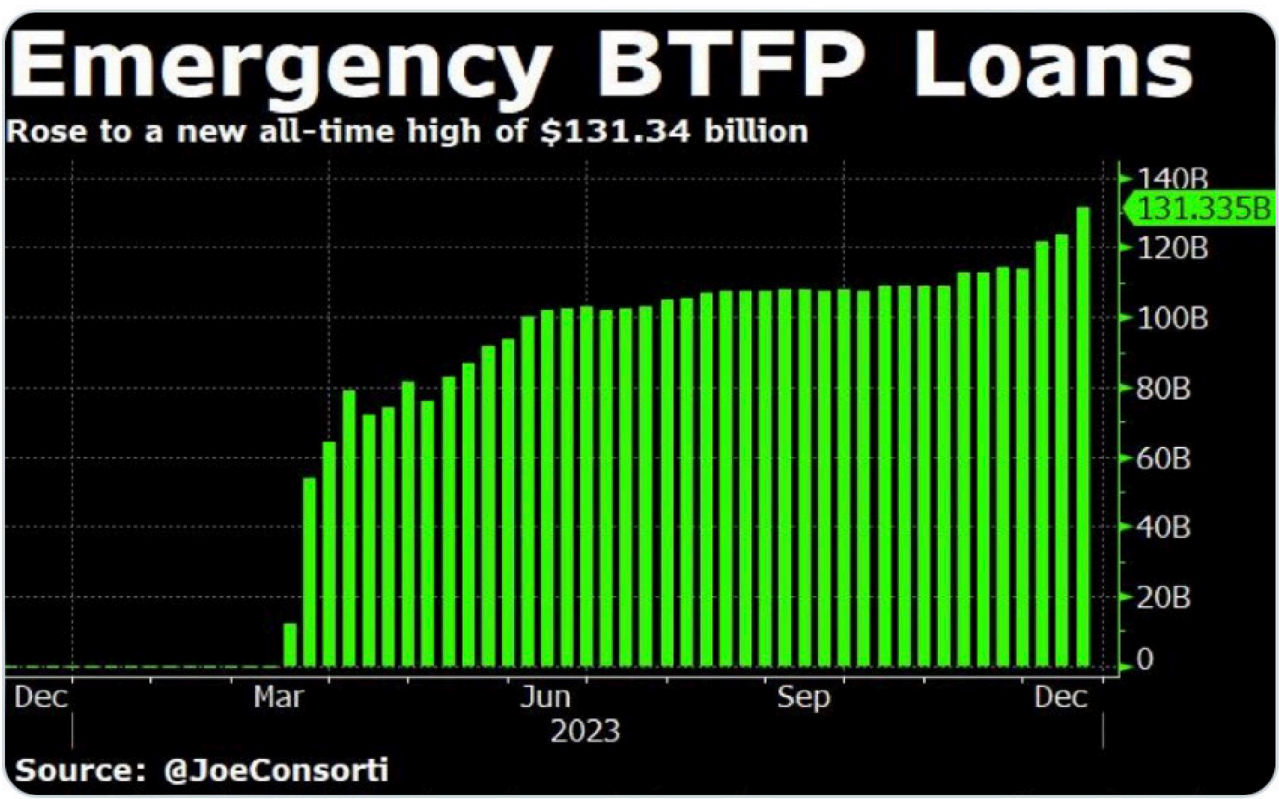
So banks can pledge USTs trading 85c for par loans with a 4.9% cost (BTFP = OIS+10bps = 4.9%), and then turn that cash right around to the Fed at 5.4% funds. Incredible. I can feel the wealth effect from here.

Geiger Capital
@Geiger_Capital

Banks are now making money by borrowing from the Fed's newest bailout facility (BTFP), which charges a lower rate, and then just parking that money into another spot at the Fed, which pays higher interest.

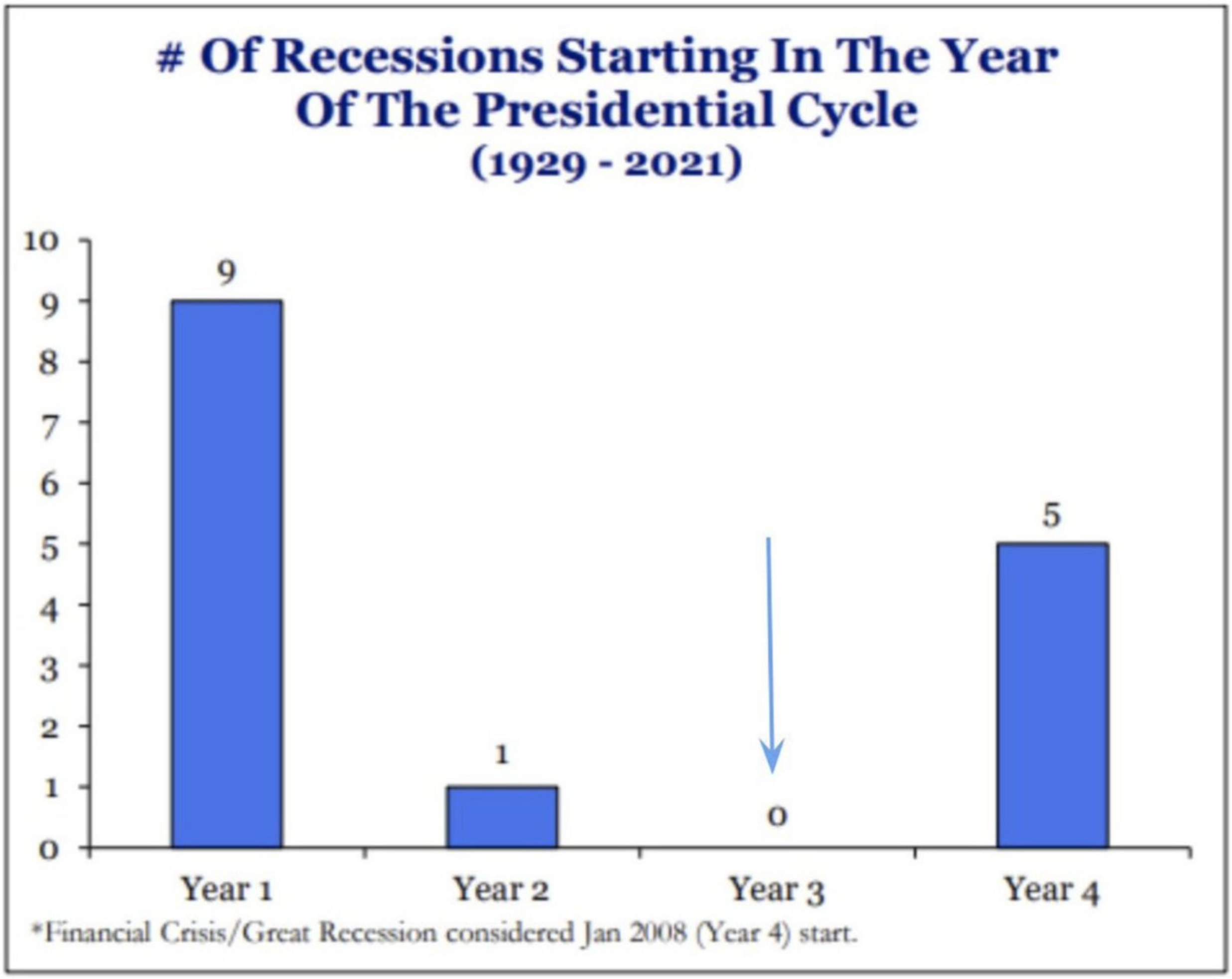
Arbitraging the Fed itself. No risk.

Absolute clown show.



Joe Consorti ⚡

The presidential cycle suggests the risk of a recession will rise significantly next year (from Seth Golden via X)...



THE LEGENDS SPEAK

Wisdom and Insight from the World's Greatest Investors

A simple three-step framework from one of the most successful investors you've never heard of (from Kyle Grieve via X)...

Pulak Prasad has soundly beat the majority of the investing competition since 2007, generating 19.1% returns annually. His high-quality portfolio is full of multi-baggers. Here is a short list of a few of his multi-baggers over the years.

Company	No. of years held	Multiple
Berger	13.3	32.2×
Mindtree	9.6	8.2×
Page	13.7	82.2×
Ratnamani	11.7	16.2×
Supreme	11.6	13.6×
WNS	13	10.6×

Now, the framework:

1. Avoid big risks.
2. Buy high-quality at a fair price.
3. Don't be lazy – be very lazy.

Avoiding big risks means... Minimizing capital destruction.

His main focus to accomplish this is to avoid making mistakes of commission. He's fine missing out on an exceptional business if it doesn't align with his rules. These rules are:

1. Be wary of criminals, crooks, and cheats

2. No aligning with unaligned owners

3. Avoid fast-changing industries

4. Ignore M&A junkies

5. Avoid turnarounds

6. Detest debt

Detesting debt is a very well-worded rule to follow, and Pulak makes a great point about major U.S. bankruptcies:

"If I were to list the 20 biggest bankruptcies in the United States, you would notice that all with Lehman at the top and LyondellBasell at number 20 were heavily indebted."

After finding a business with minimal risk Pulak wants to look for certain qualities in a business that make it exceptional. These include:

- A robust business model
- A high and sustainable ROCE
- Have wide and enduring moats
- Quality and tenured management
- Operating in less disruptible industries
- Highly fragmented customer and supplier base

Once he finds a low-risk exceptional business, he's ready to move onto acquiring it at the right price, which is... around 15x earnings.

You might be wondering when can you buy an exceptional business for these kinds of prices? The answer is rarely, which is why you must act fast when the market offers you massive discounts.

Once he owns an exceptional business, the final step is: Be incredibly lazy.

Pulak's aim is to be a permanent investor in public businesses. So he does not sell very often. Since 2007, he's averaged one sale every 1.5 years. His selling system is what you'd expect from someone who wants to hold businesses for the long term:

1. Sell when the business has experienced irreparable business damage

2. Sell when you observe egregiously bad capital allocation

And that's it! He says "We never sell on valuation..."

A rare letter from Warren Buffett many investors have never read (from Kingswell)...

At times, it can feel like everything that Warren Buffett has ever said or written has already been picked apart and examined from every conceivable angle. Buffett's annual letters – nearly 70 years' worth – remain must-reads for investors of all skill levels, while his old interviews and Q&A sessions rack up mind-boggling engagement numbers on YouTube.

But, every once in a while, we're lucky enough to stumble upon something that slipped through the cracks. I've covered a few of these "discoveries" in the past, like...

- Rediscovering Berkshire Hathaway's 1985 Annual Meeting
- Warren Buffett's 1969 Annual Letter – Yes, It Actually Exists
- Warren Buffett's Second Appearance on *Adam Smith's Money World*

(And I still haven't given up hope of tracking down Buffett's missing partnership letter from 1956, though that trail has admittedly grown quite cold.)

While digging around in the *Omaha World-Herald*'s digital archives over the weekend, I came across an op-ed that Buffett penned in 1984 about America's ballooning deficit – and its worrying ramifications on bonds, interest rates, and inflation. This plea for congressional action (and responsibility) originally appeared in the pages of *The Washington Post*, but was later syndicated to newspapers all across the country.

Up until a few days ago, I didn't even know this Buffett op-ed existed. (And, after some unsuccessful Googling, I'm guessing that's the case for most people.) So, in the Thanksgiving spirit of sharing, I've reprinted the article down below to give everyone a chance to read Buffett's warning.

(I particularly enjoy how he pokes fun at some of the popular explanations and financing "solutions" for the nation's deficit. Agree or disagree with his diagnosis of the problem, Buffett has always known how to use humor to drive home his points.)

What makes this op-ed especially timeless, though, is that its underlying theme – that nothing will really get fixed until Congress stops whistling past the graveyard and confronts the problem directly – remains as true today as it did 30 years ago.

It seems like the thorny issues of inflation, interest rates, and soaring deficits – not to mention congressional dereliction – never truly go out of style...

Financing the Deficit "Congress Must Find Will" (July 1, 1984)

The writer, of Omaha, is chairman of Berkshire Hathaway Inc. and is on the board of directors of The World-Herald. *This article was written for* The Washington Post, *which distributed it to its clients across the country.*

By Warren E. Buffett

The United States will spend about $850 billion this year and finance only 80% of that with taxes. The deficit of around $170 billion will be met by the sale of government bonds. That's a big number.

But many legislators, as well as President Reagan and Treasury Secretary Donald Regan (in their 1984 economic incarnations), are suggesting that it is not a very important number.

Certainly, they say, it is not important enough to justify the current 13% interest rate on long-term government bonds.

Supporting their position, they note that in the face of extraordinary deficits, the economy has improved and inflation has subsided. They also lean on a theory.

The theory holds that it is the method of financing deficits – not their size – that counts. The trick, this proposition says, is to avoid monetization. That is, the creation of money through purchase by the Federal Reserve system of those deficit-financing bonds.

Instead, so the argument goes, the buying must come from savings – and, in that case, the deficits will be rendered harmless.

If that proposition were truly valid, a shift in national fiscal policy would seem compelling. This new policy would seem particularly desirable because it also would instantly cure two other problems that many think impede our economic progress: the burden of excessive taxation and our lamentable national tendency to under-save.

Let's step through the looking glass and examine this remarkable cure-all.

The plan would be simplicity itself. First, abolish all federal taxes. Second, substitute for them a requirement that all present taxpayers buy a new variety of government bonds in amounts 25% higher than the taxes they now pay. Third, make it illegal for banks or the Fed to own these bonds. In that way, the bonds could not be transformed into printing-press money.

Under this system, the government would still raise its $850 billion, so spending could continue without missing a beat. Relieved of taxes, the citizenry would accumulate "the best investment you can make" – U.S. government bonds – at the staggering rate of $850 billion per year.

And, happily, the whole process would be non-inflationary since every bond purchase would be financed by savings.

Of course, a few statistical oddities would materialize. For instance, the national debt would rise at a historically fast rate. So, of course, would interest on the debt.

No problem about the interest. It would simply be paid in more bonds. (That's actually the way our government currently handles bond interest, except that we disguise things by using a borrow-from-Peter-to-pay-Paul approach. In fiscal 1983, the government's net interest payments of $90 billion were far exceeded by net sales of bonds to the public of $212 billion.)

At 10% interest rates, for example, an additional $85 billion of bonds would be issued in the second year to pay the coupons attached to bonds sold during the first year. By this procedure, the entire nation would learn the joys of pure compounding.

As old bonds annually gave birth to new bonds, the buildup in wealth would be monumental. All of this would be achieved with no reduction in consumption; after all, the $850 billion to be devoted to mandatory bond purchases – and, thus, not available for consumption – would merely equal today's sum of taxes and voluntary bond purchases (also not available for consumption).

It's interesting to contemplate the potential value of these new government bonds. If they should trade at 100 cents on the dollar, any individual could sell them off, recoup his investment, and truly feel that taxes had been eliminated.

And why shouldn't they sell at 100 cents? They would be tax-free and issued in an environment that we are told need not be inflationary. If, however, a 10% rate will not keep the bonds at par, the plan can provide that interest will be adjusted annually to reflect current rates. This would guarantee a market price of approximately face value.

The adjustable-rate provision would cause no financial strain for the government, since – whatever the rate – it must be paid in more bonds.

Skeptics may say this scheme won't work: it's too brazen, too transparent, too good to be true. Those with a mathematical bent may contend that a cascading quantity of claims on a slowly increasing quantity of goods and services must lead to accelerating debasement of the claims.

To pacify these skeptics without leaving behind all the joys of fantasy land, let's try Plan B – a variation incorporating several "improvements":

(1) Raise only part of the needed funds by sale of bonds – let's use 20% bonds, 80% taxation; (2) complicate the process by inserting pension funds and other financial intermediaries to blur who is doing what to whom; and (3) have political leaders assure the populace that large bond sales are only a one-shot proposition. That is, unending amounts of bonds are not to be forthcoming.

Prolonged usage of such assurances requires that leaders be replaced frequently. (A truly great communicator may prove an exception.)

Plan B, of course, would "work" for a much longer period than Plan A. Particularly if the country involved, like the United States, has an extended history of not materially abusing its fiscal prerogatives.

However, even the dimwitted and most trusting realize that Plan B is simply Plan A with a longer fuse. Fantasy land is still fantasy land, even when camouflaged.

And that's why financial markets, from the standpoint of policymakers, have behaved so perversely in the last few years. It's not that we've adopted Plan B. Indeed, by our words, we generally have rejected it.

But there is a pervasive apprehension in financial markets that our political system is developing a dependence on something akin to Plan B – and that, like other addictions, it will prove far easier to continue than to cure.

The market now fears the consequences of unlimited bond issuances in much the same manner as it always has feared unlimited issuances of currency.

People need no econometric models to understand that a U.S. economy with present physical output but, say, $10 trillion of government debt would be an economic world far different from the current one – even if all that debt were financed by the savings of little old ladies in Dubuque.

At a 10% rate, interest on that much debt would be $1 trillion – or 30% of today's GNP. But, of course, such a massive transfer of current output from producers to bondholders would not be allowed. The mechanism for disallowance wouldn't be repudiation.

That's not needed by governments dealing with debt denominated in their own currency. Inflation is the genteel method of diluting, or even virtually eliminating, such claims.

Given debt of $10 trillion – and real output only moderately greater than its present size – the nominal level of GNP would be enormously higher than it now is. It might be $20 trillion or $30 trillion or $15 trillion. No precision is really possible in this area.

But, in any case, a vastly increased GNP in nominal terms would have been created – in major part – by a mammoth rise in the price level. Perhaps 200%, perhaps 500%, perhaps 1,000%.

The very lack of precision about future economic relationships, once fiscal behavior gets into uncharted territory, contributes to the increased fragility and volatility of today's bond market. Of course, a mathematical case can be made that an annual combination of 8% inflation, 2% growth, and a roughly 10% increase in the national debt will produce equilibrium in the debt-GNP ratio.

The market rejects this case: it does not believe that stability can exist in any economic equation containing a high inflation component.

That's the major reason supposedly high "real" interest rates fail to entice investors.

Calculations of real rates lose all meaning in Plan B situations. What, after all, would have turned out to be the real interest rates on a long-term taxable bond issued ten years ago by Mexico, Israel, or Argentina at 5 percentage points above the inflation rate then existing?

At some point, financial markets decide that interest rate bets made with governments in fiscal disarray are a losing game – no matter how attractive the odds look on a historical basis.

The bond market does not know at what speed the bond-issuing snowball will build. It does know that, by peacetime standards, the snowball is extraordinarily large and fast-moving.

It also knows that only Congress can slow the snowball – and that the act would require great political will. The market has seen little evidence that such a will exists.

Talk by Congress about "down payments" and "out-year projections" won't work. Only action to bring down the deficit dramatically – now – will suffice. Were that to occur – and to be combined with a continuation of Chairman Paul Volcker's leadership at the Fed – long-term interest rates would drop sharply.

Such a drop will not guarantee a brighter national economic picture, but its absence will preclude that future. Unless Congress moves decisively, rates will stay up. Lots of talk and little action will leave the market scrambling to get out of the snowball's path.

Berkshire Hathaway Vice Chair Charlie Munger passed away late last month at the age of 99. Here's a remarkable story of some of the adversities he overcame to become one of the most successful investors in history (from Kevin G. via X)...

In 1949, Charlie Munger was 25 years old. He was hired at the law firm of Wright & Garrett for $3,300 per year, or $29,851 in inflation-adjusted dollars as of 2010. He had $1,500 in savings, equal to $13,570 now.

A few years later, in 1953, Charlie was 29 years old when he and his wife divorced. He had been married since he was 21. Charlie lost everything in the divorce, his wife keeping the family home in South Pasadena. Munger moved into "dreadful" conditions at the University Club and drove a terrible yellow Pontiac, which his children said had a horrible paint job. According to the biography written by Janet Lowe, Molly Munger asked her father, "Daddy, this car is just awful, a mess. Why do you drive it?" The broke Munger replied: "To discourage gold diggers."

Shortly after the divorce, Charlie learned that his son, Teddy, had leukemia. In those days, there was no health insurance, you just paid everything out of pocket and the death rate was near 100% since there was nothing doctors could do. Rick Guerin, Charlie's friend, said Munger would go into the hospital, hold his young son, and then walk the streets of Pasadena crying.

One year after the diagnosis, in 1955, Teddy Munger died. Charlie was 31 years old, divorced, broke, and burying his nine-year-old son. Later in life, he faced a horrific operation that left him blind in one eye with pain so terrible that he eventually had his eye removed.

By the time he was 69 years old, he had become one of the richest 400 people in the world, been married to his second wife for 35+ years, had eight wonderful children, countless grandchildren, and become one of the most respected business thinkers in history.

An oldie but a goodie. Thanks for sharing @joshuakennon.

Munger's advice on risk management was as simple as it was powerful (from The Long View via X)...

Simple advice on risk management: "But really, it's knowing you can have a very bad day. Do not live your life in such a fashion that a bad day can kill you."

BECKY QUICK: I think people learn more from their mistakes sometimes than their successes.

CHARLIE MUNGER: Yeah, on their bad days even. Yes. But really, it's knowing you can have a very bad day. Do not live your life in such a fashion that a bad day can kill you.

BECKY QUICK: Which means what when it comes to investing? Making sure you don't use leverage?

CHARLIE MUNGER: Well, they aim for the fences. It's like a hitter at baseball who tries to hit a home run on every pitch. The great home runners do not remotely swing at every pitch. They wait for one that they can really handle. And that's what great stock traders do too.

Here's a summary of 12 of Charlie Munger's most important insights on life and investing (from Compounding Quality via X)...

Charlie Munger's wisdom will continue to spread forever. He is a big inspiration and role model for many investors. Here are 12 insights from Charlie himself:

1. Understanding both the power of compound return and the difficulty getting it is the heart and soul of understanding a lot of things.

2. In my whole adult life, I've never hoarded cash, waiting for better conditions. I've just invested in the best thing I could find.

3. Part of the Berkshire secret is that when there's nothing to do, Warren is very good at doing nothing.

4. I didn't get rich by buying stocks at high price-to-earnings multiples in the midst of crazy speculative booms, and I'm not going to change.

5. We all start out stupid, and we all have a hard time staying sensible. You have to keep working at it.

6. I think that many CEOs get carried away into folly. They haven't studied the past models of disaster enough and they're not risk-averse enough.

7. A lot of other people are trying to be brilliant and we're just trying to stay rational. And it's a big advantage. Trying to be brilliant is dangerous, particularly when you're gambling.

8. If investing wasn't hard, everyone would be rich.

9. The desire to get rich fast is pretty dangerous.

10. Those who keep learning will keep rising in life.

11. I have made bad business decisions. You can't live a successful life without doing some difficult things that go wrong. That's just the nature of the game. And you wouldn't be sufficiently courageous if you tried to avoid every single reverse.

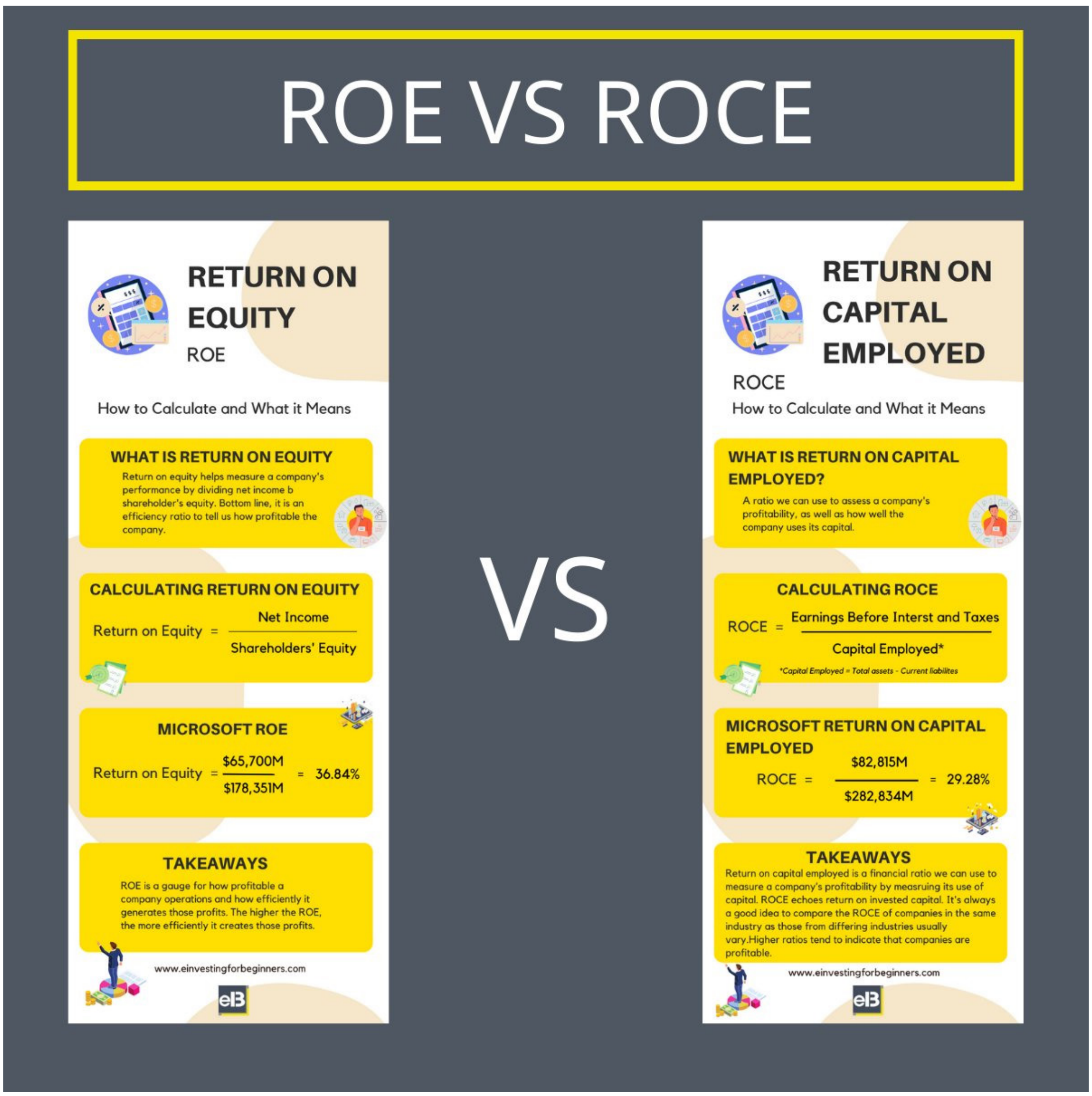
12. If you're going to live a long time, you have to keep learning. So if you don't learn to constantly revise your earlier conclusions and get better, you are – I always use the same metaphor. You're like a one-legged man in an ass-kicking contest.

Two profitability metrics every investor should be familiar with (from The Investing for Beginners Podcast via X)...

ROE vs ROCE

- ROE gauges profits relative to shareholders equity and net income
- ROCE assesses overall capital efficiency, including debt.

Buffett loves ROE > 15%; indicates possible moat. Terry Smith loves ROCE. Both worthwhile to know.



Key takeaways from the new edition of the fantastic book: *Poor Charlie's Almanac: The Wit and Wisdom of Charlie Munger* (from David Senra via X)...

1. Find a simple idea and take it seriously.
2. Good ideas are rare. When you find one, bet heavily.
3. Humans have been writing down their best ideas for 5,000 years. Read them.
4. Avoiding stupid mistakes is more important than being smart.
5. Don't work with anyone you don't admire.
6. Don't sell anything you wouldn't buy.
7. Avoiding a bad habit is easier than breaking a bad habit.
8. Work on your best idea. Don't diversify.
9. Incentives rule everything around you.
10. Never, ever, think about something else when you should be thinking about the power of incentives.
11. The most important rule in management is: Get the incentives right.
12. The storyteller is the most powerful person in the world.
13. Education is the process whereby the ability to lead a good life is acquired.
14. Be dependable for your tribe.
15. Trust is one of the greatest economic forces on Earth.
16. Don't over optimize for growth at the expense of durability.
17. Great businesses are built by going ridiculously far in maximizing or minimizing one or a few things. Think Costco.
18. The combination of scale and fanaticism is *very* powerful. Think Sam Walton.
19. Do the unpleasant task first.
20. Don't multitask.
21. Learning is changing behavior.
22. Avoiding stupidity for a long time *is* genius.
23. Many hard problems are solved best when approached backwards.

24. Think of ideas as tools. When a better tool comes along, use it.

25. Clip your business and personal expenses. Small leaks sink big ships.

26. Make friends with smart dead people. Adam Smith, Darwin, Cicero, Ben Franklin – whoever interests you. Read their writing. Steal their ideas. They don't need them anymore.

27. Only focus on great businesses, and great businesses have moats.

28. Dominating a niche can produce profit margins that make you salivate.

29. Telling people WHY increases compliance.

30. Stay in the game long enough to get lucky.

31. Stack cash to survive unexpected problems and seize unexpected opportunities.

32. Don't confuse intelligence with invincibility.

33. Panic spreads and compounds quickly.

34. If you're not winning – scale down and intensify.

35. Appeal to interest, not to reason.

36. Understanding opportunity cost is a superpower.

37. Don't confuse the map for the territory.

38. People often interpret price as a signal for quality.

39. All human systems are gamed.

40. Beating back bureaucracy is a never-ending battle.

41. The acquisition of knowledge is a moral duty.

42. Learning from history is a form of leverage.

43. Make sure your best players get the most playing time.

44. It is inevitable that bad things will happen to you. When they do get up, keep going, and remember the next maxim:

45. Self pity has no utility.
46. Find out what you are best at. Then pound away at it. Forever.
47. Envy is weakness.
48. The behavior of peer companies will be mindlessly imitated.
49. Emotion blurs judgment.
50. Only play games where you have an edge.
51. Avoid mob rule. Avoid demagogues. Avoid dogma. Avoid bureaucracy.
52. Optimize for independence.
53. Use money to buy freedom.
54. Aim for durability.
55. Keep the people who don't matter from interfering with the work of the people who do.
56. What do you have an *intense* interest in? Do that for your living.
57. Self-improvement has no end.

How Warren Buffett finds "wonderful" businesses (from Invest in Assets via X)...

Warren Buffett famously said:

"It is far better to buy a wonderful business at a fair price than a fair company at a wonderful price"

Let's break down Buffett's method of finding "wonderful" companies. Buffett's framework is four-fold:

1. Invest in businesses you understand

2. The business must have favorable long-term prospects

3. The management team must be competent

4. The price of the business must be attractive

1. Understand the business

"We don't look to jump over seven-foot bars – we look around for one-foot bars that we can step over"

Buffett follows two principles:

- He looks at simple businesses
- If he can't understand how a business makes money, he stays away

To understand the business one must ask and answer some important questions:

- How is the business making money?
- How are the unit economics?
- Does the business have a moat?
- How is the competitive landscape?

Explain these to a five-year-old.

2. Favorable long-term prospects

Investing in a business that consistently creates value will yield the best returns over time. One example is Buffett's Coke investment. Coke had a capital-light business model, with high profitability and a strong brand name.

The business quality was great, but what was even greater was the potential growth that lay ahead. Buffett noticed that every time the U.S. entered a new country, Coke would follow and end up dominating the soft-drink market. The global soft-drink market was for the taking.

A few questions that will help you determine long-term prospects:

- How consistent is the growth?
- Is the business gaining market share?
- What is the realistic total addressable market?
- How much is the market growing per year?
- Can the business expand globally?

3. Competent and high-integrity management

Competency will show up in the annual reports with a focus on return on capital, free cash flow, capital allocation, and long-term initiatives/projects. CEOs with a short-term mindset are something Buffett avoids.

Management should be aligned with shareholders, and be owners of the company themselves. If not, they might not act in alignment with what is best for the business long-term.

Integrity is hard to measure – Buffett wants someone you could marry your daughter to. Integrity is a combination of trust, reputation, and doing what you say you're gonna do.

This can be tracked over time by following a company and listening to earning calls. How is the mgmt speaking? Do they admit when they're wrong? Do they take accountability?

4. A fair price

Buffett famously wants a fantastic business at a fair price.

There are several ways to determine if a business is fairly valued, but keep in mind – it depends on future prospects. If Berkshire's valuation criteria was too strict, they would not have bought Coke and Apple, two of their best investments ever.

Price is what you pay, value is what you get. The price has to be seen in relation to the quality and the growth of the business.

That being said, after identifying a great business with long-term prospects and great management, not paying too much for such a business is key to making a great investment.

Compare the free cash flow yield to the risk-free rate (10-year treasury) and do a discounted cash flow analysis to make sure the current price is sound.

Here's a case study on the power of intelligent share buybacks (from Andrew Kuhn via X)...

Studying Henry Singleton and Teledyne should be mandatory for every public company CEO in terms of capital allocation.

From 1963 to 1990, Teledyne compounded at 20.4%, compared to the S&P's 8.0%.

He was a P/E arbitrager, using Teledyne's extremely high multiple to acquire over 130 other companies and then buying back its own stock when it was very cheap.

From 1972 to 1984, Teledyne repurchased over 90% of its shares.

Buying back stock

Singleton acted aggressively to take advantage of *Teledyne's* cheap stock during recessions for the benefit of long term shareholders. Using the company's strong cash flows, he began one of the most intensive and value creating share repurchase programs in corporate history. From 1972 to 1984, in a total of eight separate tender offers, *Teledyne* repurchased nearly 90% of its stock, always offering shareholders a premium of between 22% and 47% above the prevailing market price, yet still paying prices that proved to be low.

As further evidence of *Singleton's* market savvy, in three of the tender offers *Teledyne* issued bonds rather than used cash to repurchase stock—in each case, *Cooperman* notes, "top picking the bond market.:

The massive share repurchases magnified the benefit of the strong absolute earnings growth and the stock went from its 1974 low of around $5 to a high in 1987 of over $400.

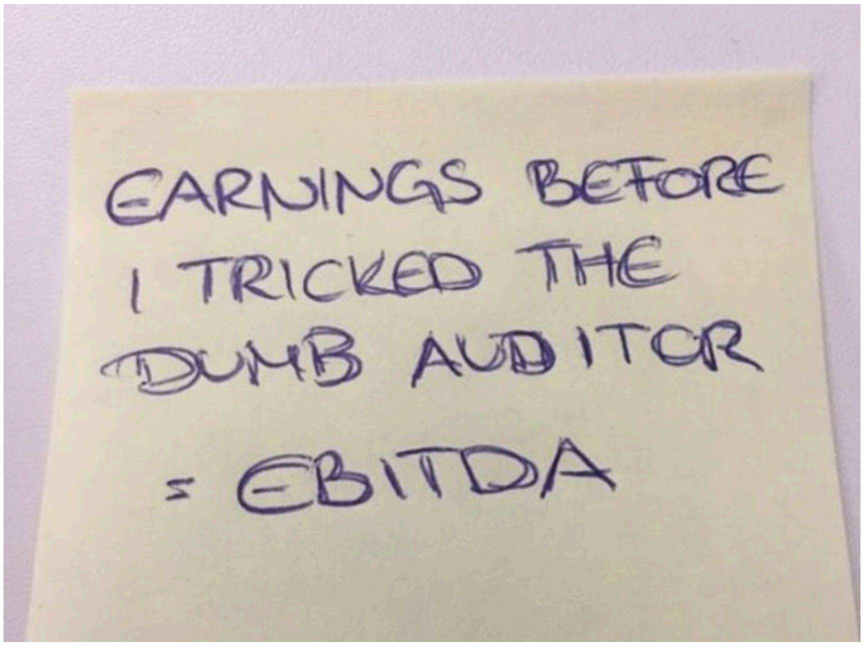
Given the benefits of aggressive share repurchases, we asked venture capitalist *Rock* why more companies haven't followed *Teledyne's* lead. "The ego of the CEO is typically focused on building a business," he says, "which isn't particularly consistent with using cash to buy back stock."

You can read more about Singleton and Teledyne here.

What every investor should know about EBITDA (from Brian Feroldi via X)...

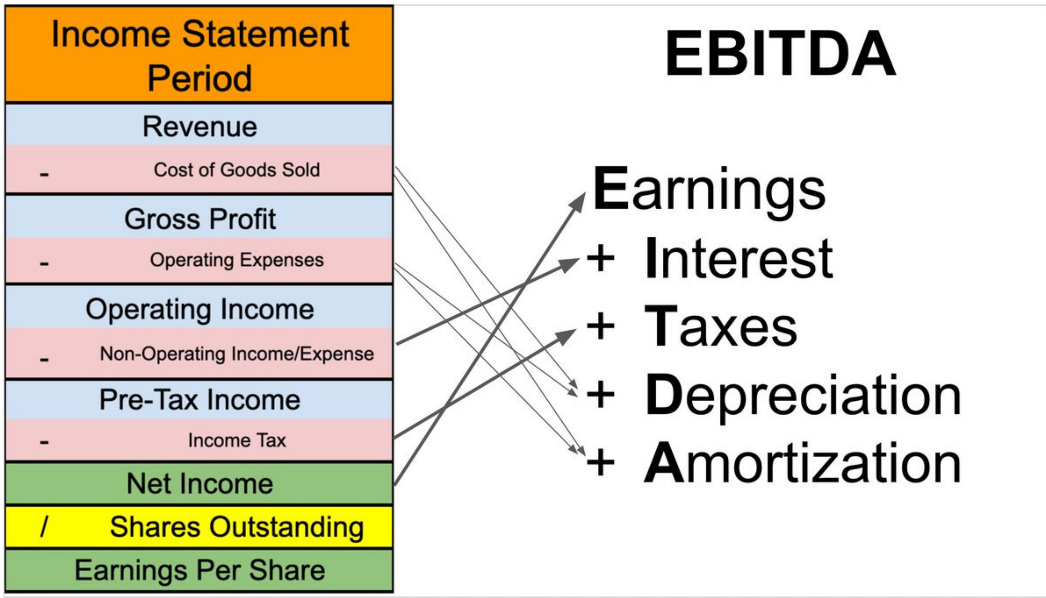
Charlie Munger called it "bullsh*t earnings." So why is EBITDA so popular on Wall Street?

Here's everything you need to know about this controversial investing term:



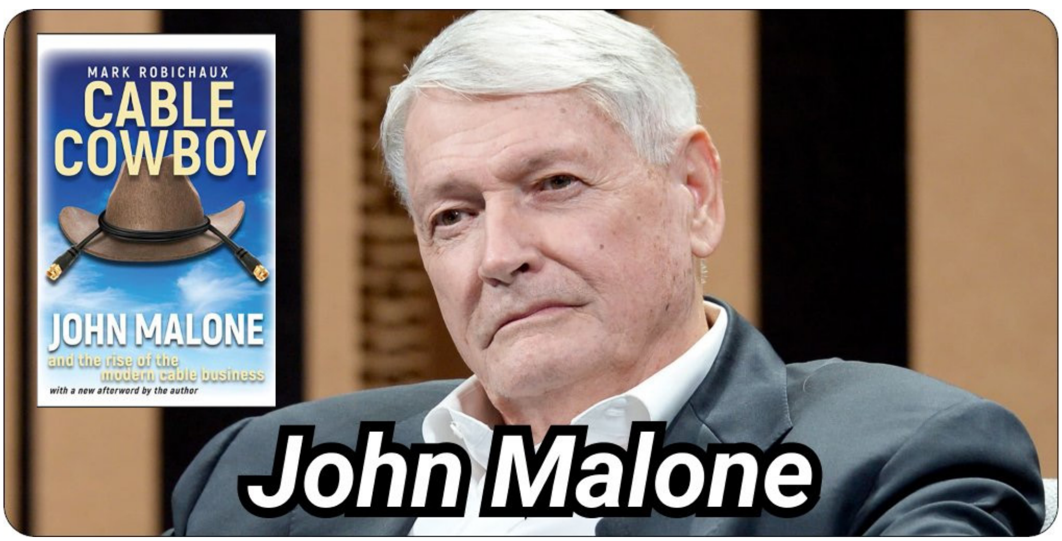
EBITDA is an alternative way to measure a company's profitability. EBITDA is simply an acronym: Earnings Before Interest, Taxes, Depreciation, and Amortization.

To calculate EBITDA, you start with Net Income (Earnings). Then you add back Interest, Taxes, Depreciation, and Amortization.

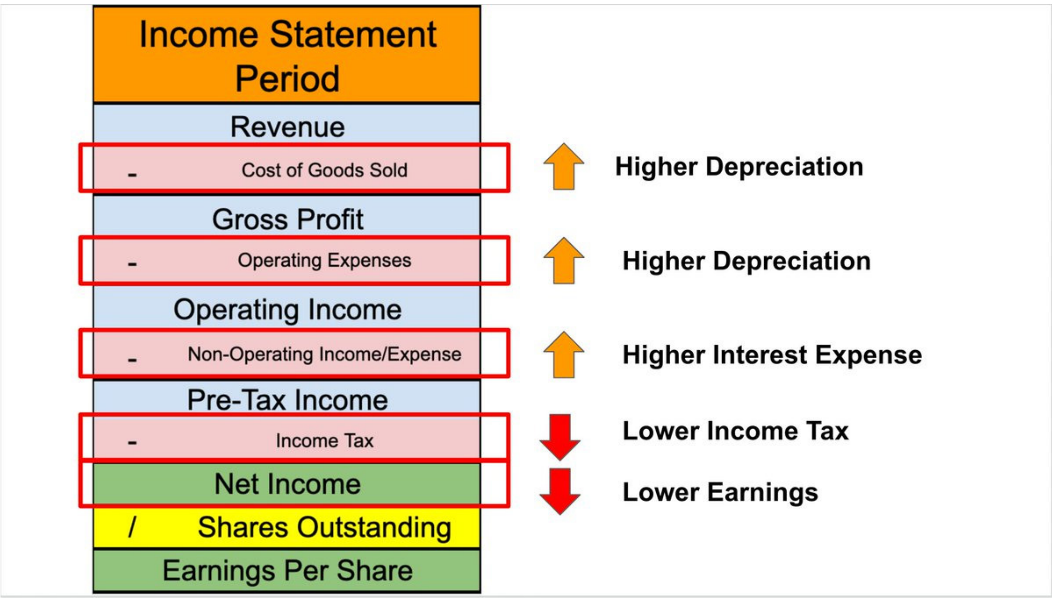


Why measure EBITDA at all?

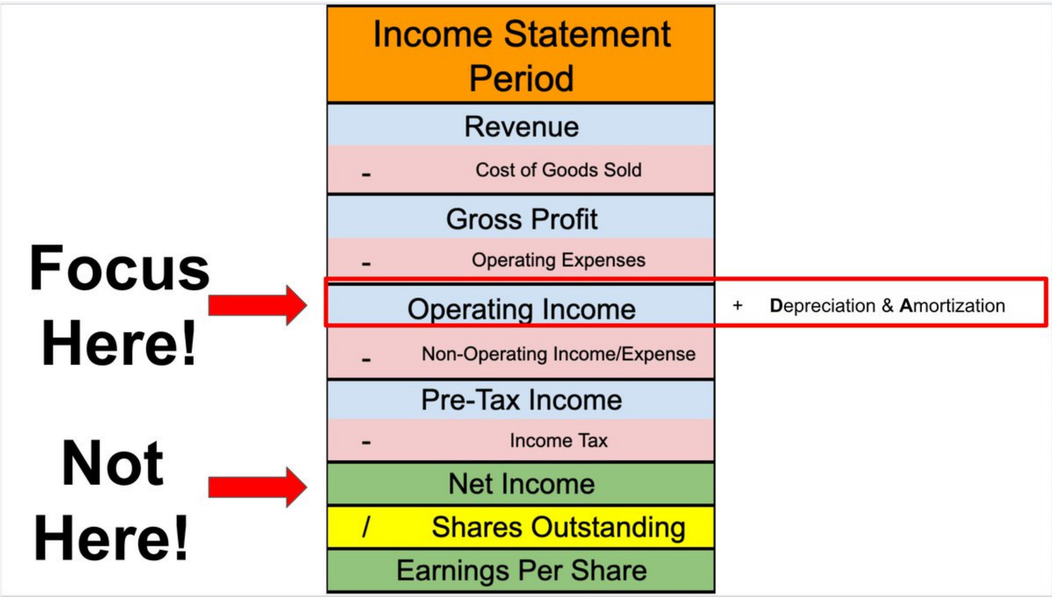
EBITDA was popularized by John Malone, one of the best owner/operators of all time. Malone became a billionaire primarily by buying and operating cable companies.



Malone LOVED using leverage (debt) to grow and HATED paying taxes. He used interest + deprecation expenses to minimize his tax bill. A side effect is that this LOWERED net income.



Lowering net income was a problem since it's an important number for investors and lenders. Malone convinced them to focus on CASH FLOW instead of earnings. EBITDA is a quick and easy way to roughly measure a company's cash flow.

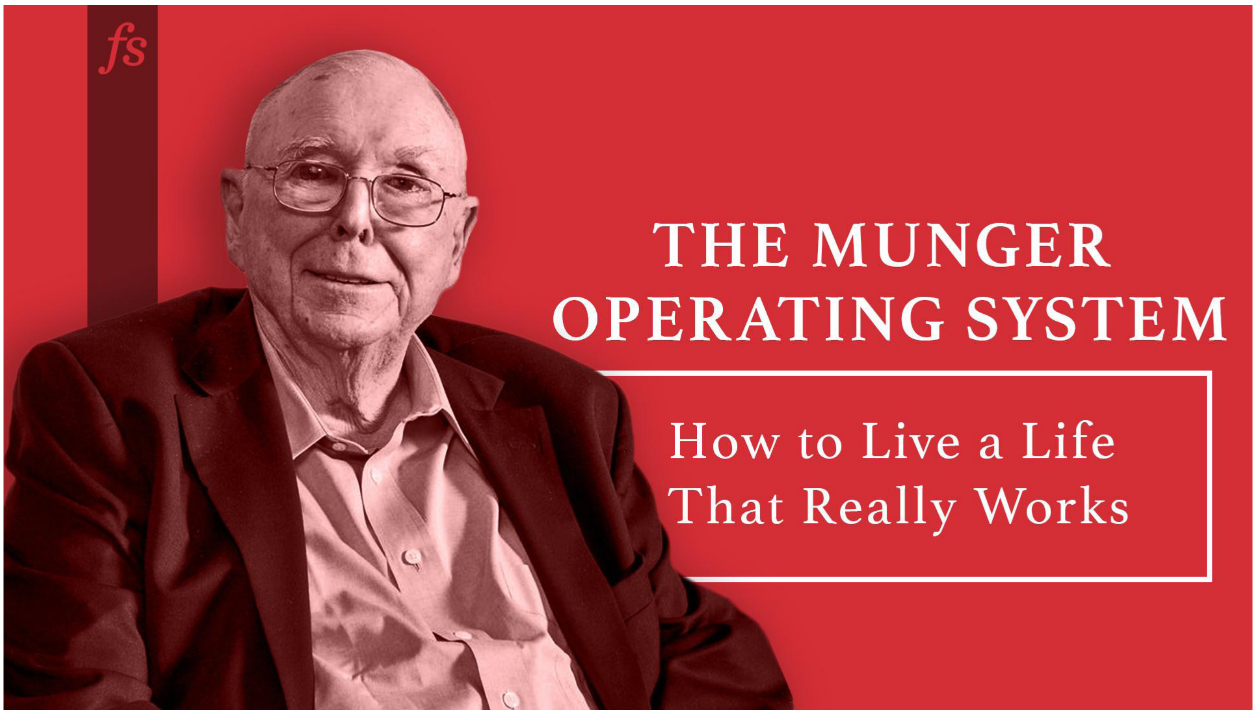


Highlights from one of Charlie Munger's most famous speeches (from Farnam Street)...

The Munger Operating System: How to Live a Life That Really Works

In 2007, Charlie Munger gave the commencement address at USC Law School, opening his speech by saying, "Well, no doubt many of you are wondering why the speaker is so old. Well, the answer is obvious: He hasn't died yet."

Fortunately for us, Munger has kept on ticking. The commencement speech is an excellent response to the Big Question: How do we live a life that really works? It has so many of Munger's core ideas that we think the speech represents the Munger Operating System for life.



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To get what you want, deserve what you want. Trust, success, and admiration are earned.

> *It's such a simple idea. It's the golden rule so to speak: You want to deliver to the world what you would buy if you were on the other end. There is no ethos, in my opinion, that is better for any lawyer or any other person to have. By and large the people who have this ethos win in life and they don't win just money, not just honors. They win the respect, the deserved trust of the people they deal with, and there is huge pleasure in life to be obtained from getting deserved trust.*

Learn to love and admire the right people, alive or dead.

> *A second idea that I got very early was that there is no love that's so right as admiration-based love, and that love should include the instructive dead. Somehow, I got that idea and I lived with it all my life; and it's been very, very useful to me.*

Acquiring wisdom is a moral duty as well as a practical one.

> *And there's a corollary to that proposition which is very important. It means that you're hooked for lifetime learning, and without lifetime learning you people are not going to do very well. You are not going to get very far in life based on what you already know. You're going to advance in life by what you're going to learn after you leave here…if civilization can progress only when it invents the method of invention, you can progress only when you learn the method of learning.*

Attain fluency on the big multidisciplinary ideas of the world and use them regularly.

> *What I noted since the really big ideas carry 95% of the freight, it wasn't at all hard for me to pick up all the big ideas from all the big disciplines and make them a standard part of my mental routines. Once you have the ideas, of course, they are no good if you don't practice — if you don't practice you lose it.*
>
> *So I went through life constantly practicing this model of the multidisciplinary approach. Well, I can't tell you what that's done for me. It's made life more fun, it's made me more constructive, it's made me more helpful to others, it's made me enormously rich, you name it, that attitude really helps.*
>
> *Now there are dangers there, because it works so well, that if you do it, you will frequently find you are sitting in the presence of some other expert, maybe even an expert that's superior to you, supervising you. And you will know more than he does about his own specialty, a lot more. You will see the correct answer when he's missed it.*
>
> *[…]*

> *It doesn't help you just to know them enough just so you can give them back on an exam and get an A. You have to learn these things in such a way that they're in a mental latticework in your head and you automatically use them for the rest of your life.*

Learn to think through problems backwards as well as forward.

> *The way complex adaptive systems work and the way mental constructs work, problems frequently get easier and I would even say usually are easier to solve if you turn around in reverse.*
>
> *In other words if you want to help India, the question you should ask is not "how can I help India?", you think "what's doing the worst damage in India? What would automatically do the worst damage and how do I avoid it?" You'd think they are logically the same thing, but they're not. Those of you who have mastered algebra know that inversion frequently will solve problems which nothing else will solve. And in life, unless you're more gifted than Einstein, inversion will help you solve problems that you can't solve in other ways.*

Be reliable. Unreliability can cancel out the other virtues.

> *If you're unreliable it doesn't matter what your virtues are, you're going to crater immediately. So doing what you have faithfully engaged to do should be an automatic part of your conduct. You want to avoid sloth and unreliability.*

Avoid intense ideologies. Always consider the other side as carefully as your own.

> *Another thing I think should be avoided is extremely intense ideology, because it cabbages up one's mind. You've seen that. You see a lot of it on TV, you know preachers for instance, they've all got different ideas about theology and a lot of them have minds that are made of cabbage.*
>
> *But that can happen with political ideology. And if you're young it's easy to drift into loyalties and when you announce that you're a loyal member and you start shouting the orthodox ideology out what you're doing is pounding it in, pounding it in, and you're gradually ruining your mind. So you want to be very careful with this ideology. It's a big danger.*

> *In my mind I have a little example I use whenever I think about ideology, and it's these Scandinavian canoeists who succeeded in taming all the rapids of Scandinavia and they thought they would tackle the whirlpools in the Grand Rapids here in the United States. The death rate was 100%. A big whirlpool is not something you want to go into and I think the same is true about a really deep ideology.*
>
> *I have what I call an iron prescription that helps me keep sane when I naturally drift toward preferring one ideology over another. And that is I say "I'm not entitled to have an opinion on this subject unless I can state the arguments against my position better than the people do who are supporting it. I think that only when I reach that stage am I qualified to speak." Now you can say that's too much of an iron discipline..it's not too much of an iron discipline. It's not even that hard to do.*

Get rid of self-serving bias, envy, resentment, and self-pity.

> *Generally speaking, envy, resentment, revenge and self pity are disastrous modes of thought. Self-pity gets pretty close to paranoia, and paranoia is one of the very hardest things to reverse. You do not want to drift into self-pity.*
>
> *I have a friend who carried a big stack of index cards about this thick, and when somebody would make a comment that reflected self pity, he would take out one of the cards, take the top one off the stack and hand it to the person, and the card said, "Your story has touched my heart, never have I heard of anyone with as many misfortunes as you". Well, you can say that's waggery, but I suggest that every time you find you're drifting into self pity, I don't care what the cause — your child could be dying of cancer — self-pity is not going to improve the situation. Just give yourself one of those cards.*
>
> *It's a ridiculous way to behave, and when you avoid it you get a great advantage over everybody else, almost everybody else, because self-pity is a standard condition and yet you can train yourself out of it.*
>
> *And of course self-serving bias, you want to get that out of yourself; thinking that what's good for you is good for the wider civilization and rationalizing all these ridiculous conclusions based on the subconscious tendency to serve one's self.*

At the same time, allow for the self-serving bias in others who haven't removed it.

> *You also have to allow for the self-serving bias of everybody else, because most people are not going to remove it all that successfully, the human condition being what it is. If you don't allow for self serving bias in your conduct, again you're a fool.*

> *I watched the brilliant Harvard Law School trained general counsel of Salomon lose his career, and what he did was when the CEO became aware that some underling had done something wrong, the general counsel said, "Gee, we don't have any legal duty to report this but I think it's what we should do it's our moral duty."*
>
> *Of course, the general counsel was totally correct but of course it didn't work; it was a very unpleasant thing for the CEO to do and he put it off and put if off and of course everything eroded into a major scandal and down went the CEO and the general counsel with him.*
>
> *The correct answer in situations like that was given by Ben Franklin, he said, "If you want to persuade, appeal to interest not to reason." The self serving bias is so extreme. If the general counsel had said, "Look this is going to erupt, it's something that will destroy you, take away your money, take away your status…it's a perfect disaster," it would have worked!*

Avoid being part of a system with perverse incentives.

> *Incentives are too powerful a controller of human cognition and human behavior, and one of the things you are going to find in some modern law firms is billable hour quotas. I could not have lived under a billable hour quota of 2,400 hours a year. That would have caused serious problems for me — I wouldn't have done it and I don't have a solution for you for that. You'll have to figure it out for yourself but it's a significant problem.*

Work with and under people you admire, and avoid the inverse when at all possible.

> *And that requires some talent. The way I solved that is, I figured out the people I did admire and I maneuvered cleverly without criticizing anybody, so I was working entirely under people I admired. And a lot of law firms will permit that if you're shrewd enough to work it out. And your outcome in life will be way more satisfactory and way better if you work under people you really admire. The alternative is not a good idea.*

Learn to maintain your objectivity, especially when it's hardest.

> *Well we all remember that Darwin paid special attention to disconfirming evidence particularly when it disconfirmed something he believed and loved. Well, objectivity maintenance routines are totally required in life if you're going to be a correct thinker. And there we're talking about Darwin's attitude, his special attention to disconfirming evidence, and also to checklist routines. Checklist routines avoid a lot of errors. You should have all this elementary wisdom and then you should go through and have a checklist in order to use it. There is no other procedure that will work as well.*

Concentrate experience and power into the hands of the right people – the wise learning machines.

> *I think the game of life in many respects is getting a lot of practice into the hands of the people that have the most aptitude to learn and the most tendency to be learning machines. And if you want the very highest reaches of human civilization that's where you have to go.*
>
> *You do not want to choose a brain surgeon for your child among fifty applicants all of them just take turns during the procedure. You don't want your airplanes designed that way. You don't want your Berkshire Hathaways run that way. You want to get the power into the right people.*

You'll be most successful where you're most intensely interested.

> *Another thing that I found is an intense interest of the subject is indispensable if you are really going to excel. I could force myself to be fairly good in a lot of things, but I couldn't be really good in anything where I didn't have an intense interest. So to some extent, you're going to have to follow me. If at all feasible you want to drift into doing something in which you really have a natural interest.*

Learn the all-important concept of assiduity: Sit down and do it until it's done.

> *Two partners that I chose for one little phase of my life had the following rule: They created a little design/build construction team, and they sat down and said, two-man partnership, divide everything equally, here's the rule; "Whenever we're behind in our commitments to other people, we will both work 14 hours a day until we're caught up."*
>
> *Well, needless to say, that firm didn't fail. The people died rich. It's such a simple idea.*

Use setbacks in life as an opportunity to become a bigger and better person. Don't wallow.

> *Another thing of course is life will have terrible blows, horrible blows, unfair blows, doesn't matter. And some people recover and others don't. And there I think the attitude of Epictetus is the best. He thought that every mischance in life was an opportunity to behave well, every mischance in life was an opportunity to learn something, and your duty was not to be submerged in self-pity but to utilize the terrible blow in a constructive fashion. That is a very good idea.*

The highest reach of civilization is a seamless system of trust among all parties concerned.

> *The last idea that I want to give you as you go out into a profession that frequently puts a lot of procedure and a lot of precautions and a lot of mumbo jumbo into what it does, this is not the highest form which civilization can reach. The highest form which civilization can reach is a seamless web of deserved trust. Not much procedure, just totally reliable people correctly trusting one another. That's the way an operating room works at the Mayo Clinic.*
>
> *If a bunch of lawyers were to introduce a lot of process, the patients would all die. So never forget when you're a lawyer that you may be rewarded for selling this stuff but you don't have to buy it. In your own life what you want is a seamless web of deserved trust. And if your proposed marriage contract has 47 pages, my suggestion is do not enter.*

Classic investment wisdom from legendary fund manager Peter Lynch (from Matt Allen via X)...

I have a college degree. But I've learned more about investing from Peter Lynch than I did in school. Here are 10 Peter Lynch quotes that will make you a better investor:

1. "Never invest in any idea that you can't illustrate with a crayon."

2. "Owning stocks is like having children – don't get involved with more than you can handle."

3. "Whenever you invest in a company, you are looking for its market-cap to rise. This can't happen unless buyers are paying higher prices for the shares, making your investment more valuable."

4. "The key to making money in stocks is to not get scared out of them."

5. "In this business, if you're good, you are right 6 out of 10 times. You are never going to be right 10 out of 10 times."

6. "Know what you own, and why you own it."

7. "If you can't find any companies that are attractive, put your money in the bank until you discover some."

8. "Stocks aren't lottery tickets. There's a company attached to every share."

9. “There's no shame in losing money on a stock. Everybody does it. What is shameful is to hold on to a stock, or worse, to buy more of it when the fundamentals are deteriorating.”

10. “As I look back on it now, it’s obvious that studying history and philosophy was much better preparation for the stock market than, say, studying statistics.”

Ten of the best investment quotes from 2023 (from Meb Faber via X)...

1. "Some people get rich studying artificial intelligence. Me, I make money studying natural stupidity." - Carl Icahn

2. "I put two children through Harvard by trading options. Unfortunately, they were my broker’s children." - @jasonzweigwsj

3. "If you put the government in charge of the Sahara Desert, in five years there’d be a shortage of sand." - Milton Friedman

4. "The art of investment is the discipline of inaction in the absence of a good opportunity, but aggressive action when one is identified." - Li Lu

5. "To others, being wrong is a source of shame; to me, recognizing my mistakes is a source of pride. Once we realize that imperfect understanding is the human condition, there is no shame in being wrong, only in failing to correct our mistakes." - George Soros

6. "The psychological mood of people changes more drastically than anything else in finance. Human nature changes least of all." - Benjamin Graham

7. "If the price is right, we are going to sell. I think that's true of everything you have, except maybe your kids and possibly your wife." - Carl Icahn

8. "A lot of people with high IQs are terrible investors because they've got terrible temperaments. You need to keep raw, irrational emotions under control." - Charlie Munger

9. "The mutual fund industry is not an investment management industry. It's a marketing industry." - David Swensen

10. "Nothing is linear. The world doesn't move toward what we think is rational a little bit every day. The best way to manage volatility is to have a strategy that you can stick with. If you believed in it, it wouldn't matter how poorly it did for a while." - @CliffordAsness

INVESTMENT IDEAS

The top 20 tech stocks with the highest free cash flow (FCF) margins (from The Future Investors)...

The FCF margin is the % of the revenue that converts directly into free cash flow. Here are the Top 20 High-Quality companies in the Tech sector with the highest FCF margins:

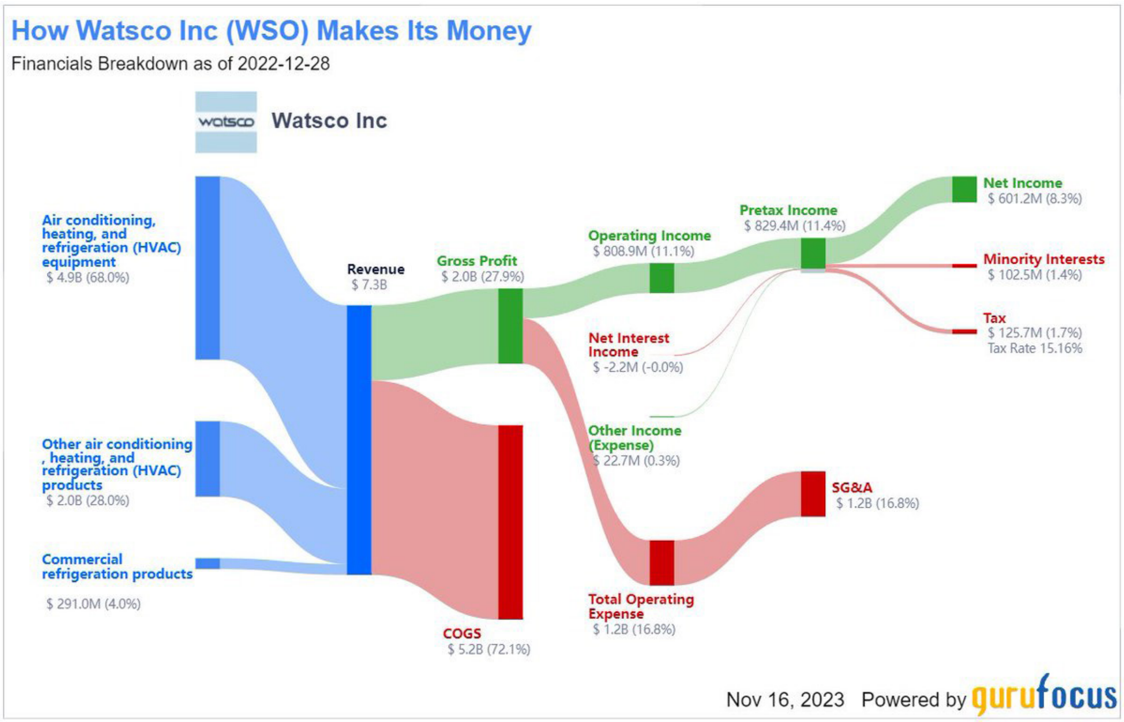
1. $QLYS - Qualys - 63.9%
2. $BESI - BE Semiconductor - 51.2%
3. $ANET - Arista Networks - 45.6%
4. $NVDA - Nvidia - 44.9%
5. $FICO - Fair Isaac - 41.8%
6. $MSFT - Microsoft - 36.6%
7. $CDNS - Cadence Design - 36.6%
8. $ADBE - Adobe - 36.4%
9. $FTNT - Fortinet - 36.1%
10. $SNPS - Synopsys - 34.6%
11. $MPWR - Monolithic Power - 31.3%
12. $NEM - Nemetschek - 28.9%
13. $OLED - Universal Display - 25.1%
14. $MANH - Manhattan Assoc. - 24.1%
15. $ASM - ASM International - 24.0%
16. $CSU - Constellation Soft. - 23.7%
17. $FN - Fabrinet - 19.5%
18. $SMCI - Super Micro Comp. - 12.6%
19. $ADSK - Autodesk - 9.5%

20 $ASML - ASML - 9.4%

Details on a "boring but beautiful" company you probably haven't heard of (from The Investing for Beginners Podcast)...

Want to find a "boring" but beautiful company?

Check out Watsco (WSO), the leading HVAC distributor. Let's learn more about the biz model and moat.



$WSO is a long-term winner, with 20% CAGR over the last 30 years. WSO began in 1956 in Florida as a manufacturer of parts, tools and components in the HVAC industry.

In 1989, WSO pivoted from manufacturing to distribution. Growing more than 100x from $64 in 1989 to current levels of $6B.

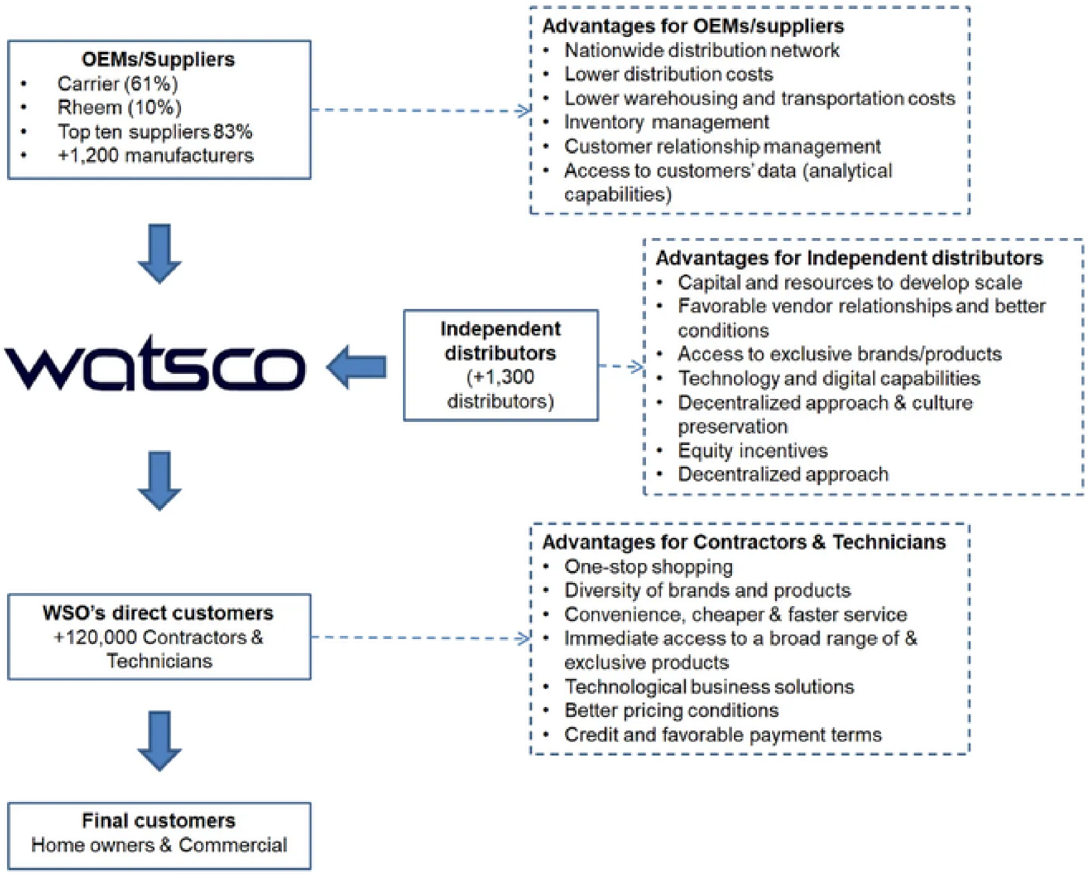
Now WSO is the largest HVAC distributor in North America. WSO operates in 42 US states thru 670+ locations, as well as Latin America.

$WSO operates as a one-stop shop for contractors. They handle all the supplies required to do the entire installation as well as just selling the equipment. WSO has a symbiotic relationship with $CARR as their leading distributor.

To put it simply, this implies offering everything else that enters the house besides the systems themselves, such as ducting, copper tubing, or insulation supplies (which means also bigger tickets and higher margins).

$WSO biz model centers around acting as a hub within the HVAC supply chain.

The HVAC industry is fragmented, to say the least, with over 120,000+ contractors and dealers servicing consumers' homes. WSO acts as a middleman between the consumer and CARR, for example.



$WSO offers advantages to two sides of the equation. For OEM/Suppliers:

- One stop shop
- Offers immediate access to nationwide system of branches
- Saves OEM/suppliers the cost of maintaining a distributor network
- Save inventory costs & mgmt

For customers (contractors)

- One stop shop
- Broad range of brands & products (1 of WSO biggest advantages)
- Extensive network makes it cheaper and faster
- Exclusive contracts with suppliers forcing contractors to use them for specific products

$WSO estimates the current TAM for HVAC around $120B annually. The distribution of HVAC/R equipment is dominated by about 6,700 organizations, although this industry's equipment manufacturing concentrates among 7 companies.

$WSO can take advantage of its scale and lower cost of capital to grow through M&A thanks to this highly fragmented state.

WSO can pick and choose to sell & capitalize on the brand recognition with exclusive trade name and contracts with Carrier, Rheem, and Mitsubishi.

$WSO utilizes a "buy and build" strategy. Watsco can purchase an established distributor and incorporate them into their huge network instead of opening new sites from scratch.

WSO can then develop these locations into even greater cash-generating units by using the cumulative investments already made in technology, customer service, and culture.

The moat exists around the organic growth they benefit from by a broader distribution network because it increases client base, contractor convenience, and network-wide customer service.

Passing along better supplier terms to customers and reinforce organic growth and obtaining the customer base from the company with a larger base. This also increases WSO's resources and capacity to reinvest in the WSO, and these investments imply steady platform growth.

Tech progress makes contractors/distributors more productive, attracting new solo distributors who see the advantages of operating under WSO's umbrella and the challenges of competing with them, fueling WSO's acquisition strategy, and the growth of its distribution network.

$WSO operates thru a "buy and build" strategy in which they buy market leaders, and then "build" them up with a growth strategy with the acquired biz by adding products and locations that best serve their customers.

The model's uniqueness lies in the decentralized nature.

$WSO has no desire to alter the cultures of acquired companies or modify their leadership; on the contrary.

At those businesses, WSO promotes a growth-oriented culture, assists the leadership teams, and invests in a wide range of technology to enable growth.

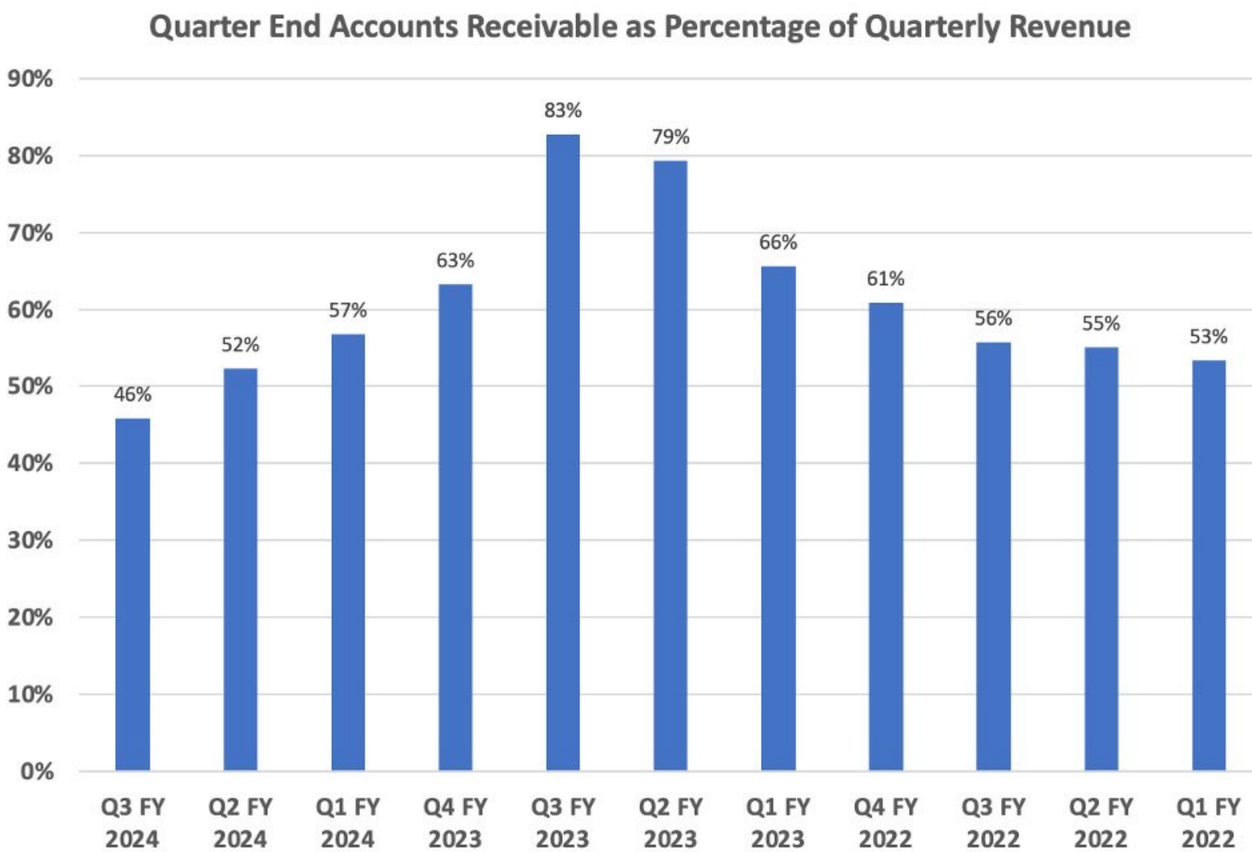
As always, long ways to go to fully understand this fantastic company, hope this short look into the biz helps.

Eight "red flags" surrounding high-flying tech stock Nvidia (NVDA) (from Kashyap Sriram via X)...

I'm gratified by the response I received on my previous thread highlighting Nvidia's $NVDA accounting tricks and buyback shenanigans. Q3 was more of the same. Let's get into it.

Rather than re-hashing the previous arguments, which the bulls will willfully ignore and the skeptics already know, I'll leave you with eight points to ponder.

(1) If demand is so strong the product is flying off the shelves, why is the company unable to collect cash from customers?



Over the last 10 quarters, revenue has increased by $12.46 billion while accounts receivable has increased by $5.28 billion. 42.4% of the incremental revenue has not (yet) translated into actual cash received from customers.

Said differently, credit to customers equals 42 days of sales in the most recent quarter. Why such generous credit terms at a time of peak demand?

License and development arrangements, cloud services, and support revenues are received upfront and booked over the contract term.

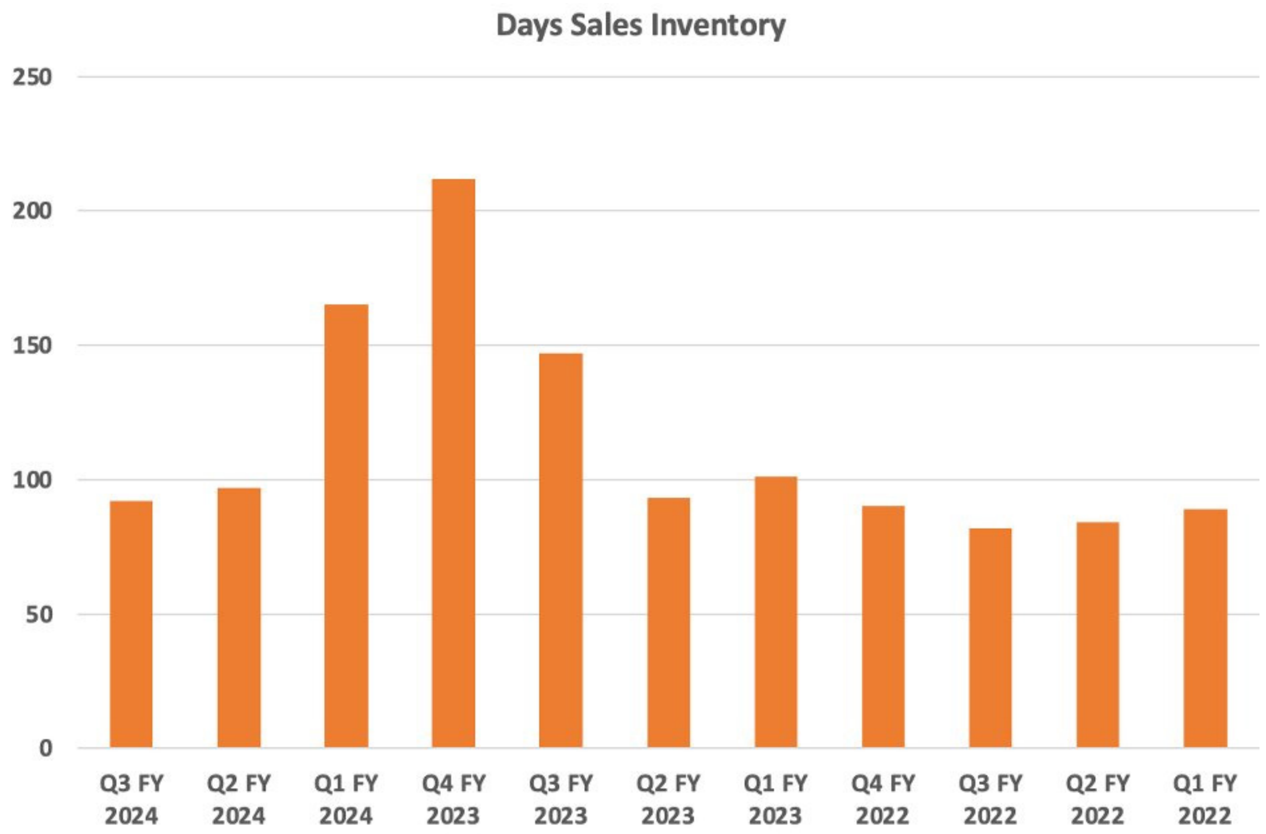
The company does not provide revenue split by product and services, but it's safe to assume days sales outstanding would be higher considering only product sales.

(2) Revenue concentration

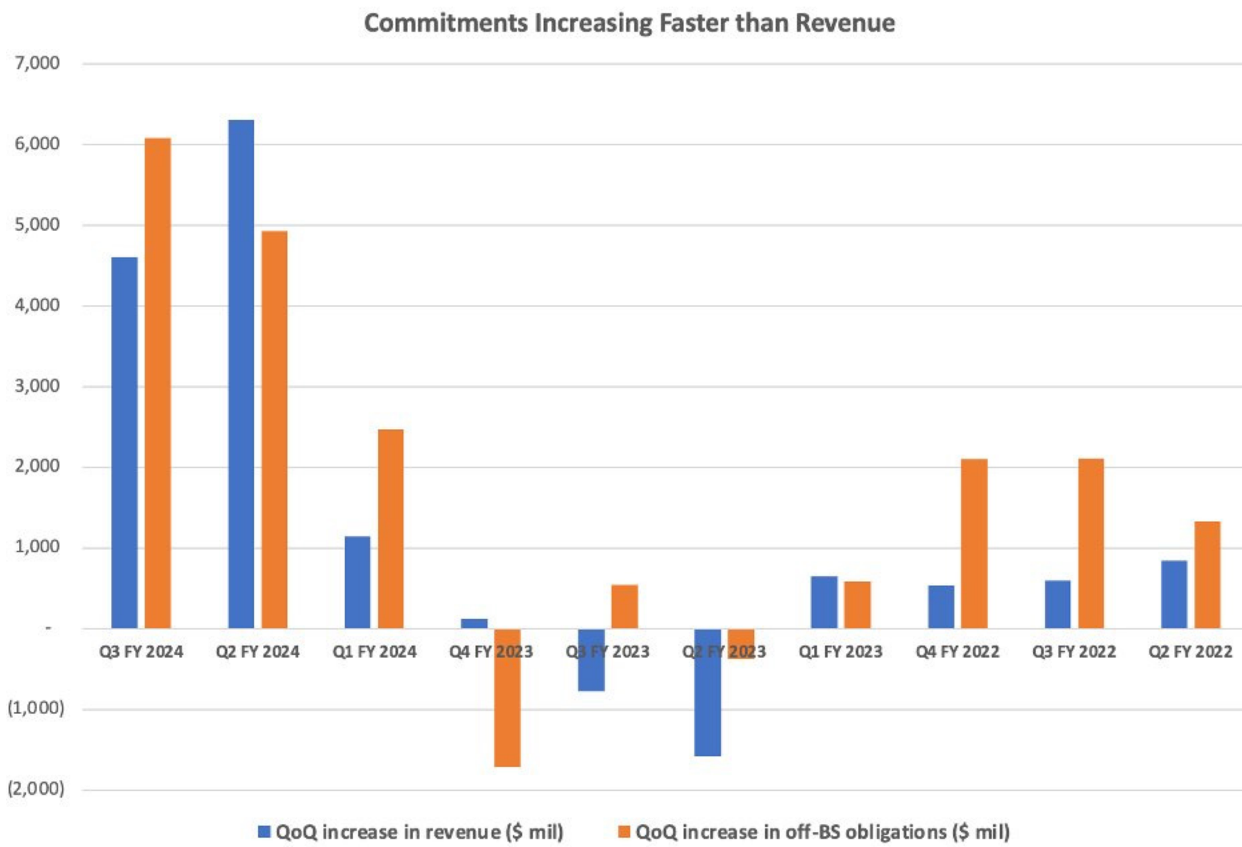
28% of last quarter revenue and 27% of last 9 months revenue is attributable to two end customers. 39% of Q2 revenue and 32% of first half revenue came from just two customers, of which one is a distributor.

(3) Excessive Inventory

The company has high inventory levels.

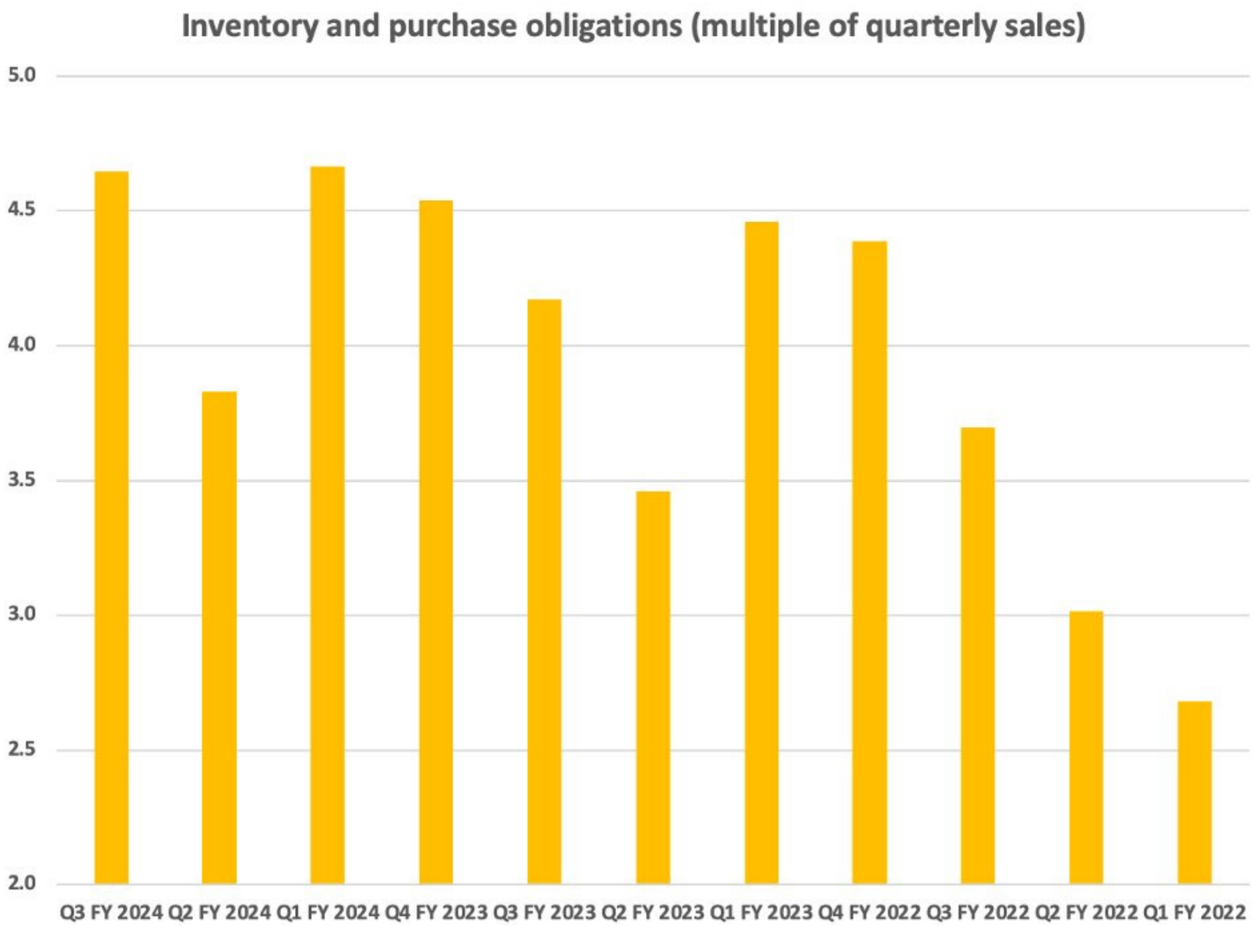


And has committed to more purchases. Off-balance sheet purchase obligations have grown at a faster pace than revenue.



The company ended the last quarter with $21.54 billion in off-balance-sheet obligations. These consist of: (1) inventory purchase and long-term supply and capacity obligations, and (2) non-inventory obligations including cloud services, primarily for R&D purposes.

Backing out the non-inventory commitments, the company has sufficient current inventory and purchase commitments to satisfy 4.65 quarters worth of demand at last quarter's revenue run rate. This inventory build-up is striking when considering the company took a $2.17 billion inventory impairment charge just last year!



The purchase commitments indicate that $NVDA has visibility into several quarters' worth of future demand. Yet, they do not provide guidance beyond the immediate quarter.

Do they deliberately withhold revenue guidance, or are they ordering inventory with no actual visibility into future demand? Either explanation is suspect.

(4) China demand has been pulled forward

Tencent says it has enough Nvidia chips to last several generations. Are they the only Chinese customer to have foreseen the chip ban?

Last quarter, Nvidia had to break out sales to Singapore as a separate line item.

Sales to Singapore customers accounted for 15% of revenue. This is widely seen as a proxy for China sales.

With sanctions in place, this source of demand is no more.

(5) Every Nvidia customer is a competitor for subsequent quarterly sales

Unlike an iPhone or a car, Nvidia's customers are not buying the GPUs for personal consumption (except for "gaming" which is a misnomer).

The GPUs remain in use for 3-5 years. After Nvidia has booked the sale, end customers can:

(1) Buy the chips outright via product resellers,

(2) Lease the use of these chips from data centers,

(3) Obtain the services of these chips indirectly through cloud service providers.

Also, chips which were erstwhile used for Ethereum mining are now trying to find a new home. Ethereum transitioned to proof-of-stake in September 2022, making this use case redundant.

There is a finite limit to how much $NVDA can grow sales even if end demand continues to grow.

While bulls like to say Nvidia has pricing power due to current high demand, this is not true. Higher prices will bring about higher supply from current holders of Nvidia's products.

The company's 74% gross margin is not sustainable.

(6) Nvidia's current business is not resilient to an economic downturn

Nvidia estimates its products cater to 30,000 global customers, of which half are start-ups. When they run out of seed funding, Nvidia's data center customers will lose revenue and demand will collapse.

When the growth stops, the inventory write-downs will start. Nvidia will also need to write down accounts receivable if its immediate customers face declining demand and go bankrupt.

Nvidia has sold at least $2.3 billion worth of chips to a customer (CoreWeave) who purchased it using a credit line. It is rumored that the customer (in which Nvidia owns an equity stake that remains undisclosed in their quarterly filings) has subsequently engaged in a sale and leaseback transaction with Nvidia.

While it is unclear to what extent Nvidia will be unable to convert receivables into cash in a downturn, this possibility exists.

(7) The curious case of the missing taxes

In the Q2 filing, $NVDA said the company will be paying $3.81 billion in deferred income taxes in Q3. According to the Q3 cash flow statement, actual deferred taxes paid amounted to $530 million. Was this part of the $3.81 billion?

Deferred tax assets on the balance sheet grew by $584 million during the quarter. Was this $530 million payment part of that growth?

The footnotes provide no explanation for this curiosity. The supplemental cash flow information shows that the company paid $4.35 billion in income taxes in Q3, but a cash walk-through from Q2 to Q3 fails to turn up that number.

(8) Inventory Accounting

The company charges provisions on inventory and inventory write-offs (non-cash expenses), and cash paid to settle off-balance sheet obligations (actual cash expenses), against cost of goods sold. This has the effect of hiding impairment charges and write-offs in both the P&L statement and the cash flow statement. It is also misleading because the company is paying cash to decrease a hidden, off the books contractual obligation while providing no context for evaluating the company's remaining obligations. If demand sinks, there is no way to know how much cash Nvidia will need to pay out to contract manufacturers when they cancel orders. With $21.54 billion in contingent liabilities, this could become a huge problem down the line.

This little known stock could be a "fat pitch" investment (from Paul Andreola via X)...

This year, in August, we found what we believe is a "Fat Pitch". It was a company that we had been following for years. Up until the pandemic they were growing revenues nicely and had just turned profitable. The pandemic hurt the company and revenues and earnings suffered.

The shares price followed their revenues and earnings, lower. Coming out of the pandemic, by August, the company regained its growth and turned nicely profitable again. It grew it's revenues by over 60% in that quarter and showed a very healthy profit.

In September the company released its year end numbers and once again revenues and earnings grew. This time revenues grew by over 80% for the quarter. The company had its second profitable quarter in years. The backlog also grew.

Recently the company announced another quarterly result and this time revenues grew over 60% over the year ago period. Profits again this quarter but they were down from last quarter as the company has started investing for further growth. Now 3 profitable quarters in a row.

Backlog continues to in size as does another KPI that indicates that this backlog will continue to grow. This company offers a product that typically generates a 2-3 year payback for its clients as well as other benefits. It's a leader in its rapidly growing vertical.

Proven management, strong moat, very large addressable market, roughly 80% of their revenue is somewhat repeat business from their existing, and very large clients. They've addressed less than 5% of their existing clients potential needs.

Company provides energy efficiency and emissions reduction solutions to Fortune 500 and other large multinational companies. It saves its customers money by reducing their fuel use and cutting their carbon emissions.

The company's "proprietary and proven solutions can recover up to 80% of energy lost in typical boiler plant and steam system operations while delivering a high return on investment with a short, compelling payback."

Yes, many of you guessed correctly. The company is Thermal Energy International, $TMG.V

We have interviewed the company several times in the past including this recent interview.

The company has a current market cap of $30.5 million and an EV of $31 million. TTM revenues are $23.2 million up 53% from the previous TTM of $15.2 million. TTM earnings of $1.39 million. Currently trades at an EV/E of 22.3 times TTM earnings.

Order backlog: $11.6-million as at Aug. 31, 2023, and $22-million as at Oct. 24, 2023. What gets really interesting is what they call PDA's or Project Development Agreements. The number of PDA's has jumped to 27. Historically they have a 75% closing rate on PDA's

The average size of these kind of orders is $2 million, so if past closing rates hold that should be another $40 million in bookings we should expect within a year. Continued growth seems well baked in here…

I would argue that is not well known in the investment community or at least very misunderstood. There is no analyst coverage and very little social media chatter on the company.

One thing to note is that there are roughly 2 million options (exercise price $0.08) that are due to expire on November 30 which may have been keeping some pressure on the share price.

The investment case for global beauty and personal care company L'Occitane International (from Clark Square Capital)...

Investment Thesis Summary

The company we are looking at today is **L'Occitane** (HK: 973) [disclosure: I own shares]. L'Occitane has an EV of EUR $3.8B and trades ~$2m USD per day.

I believe the stock is compelling for the following reasons:

- The near-term stock setup has been derisked due to the lowered margin guide for FY24 and the consequent failed take-private attempt.
- L'Occitane's top line will continue to grow at least double digits due to Sol de Janeiro, which is growing triple digits and shows no signs of slowing down.
- A recovery in Elemis + L'Occitane provides further upside to top-line growth. I model a mid-teens rate over the next two years.
- I expect L'Occitane's EBIT margin to revert above 15% by FY25.
- The low absolute and relative valuation makes the risk/reward compelling. The downside is likely capped by a takeover or a re-listing.

I see a pathway for the shares to be worth at least HKD 40 in a year or roughly double today's price.

Why this might be mispriced

- **Orphaned equity**: Despite being a predominantly French company, the stock trades in Hong Kong. This mismatch creates a conflict, as European investors might not be able to buy the stock due to fund restrictions even if they are interested in the company.
- **Failed take-private**: in August, a news story suggested that the Chairman was interested in acquiring the remaining shares of the company he does not own (he owns c. 70%). However, the Chairman ultimately decided to walk away from the deal, causing the share price to collapse.
- **IR / corporate disclosures are poor:** Transcripts of the company's calls are not on Bloomberg or other news services despite regularly mentioning critical details, including forward-looking guidance.

Trading dynamics

The average daily traded volume is roughly $2.0m USD per day, which makes this liquid enough for PAs and small funds.

Capital structure

- Please note that the company reports in EUR, while the stock price is quoted in HKD.
- The company's capital structure is simple and clean. L'Occitane has a market cap of EUR 3.4B and an enterprise value of EUR 3.8B.
- Net debt is manageable, at 1.0x net debt to EBITDA.

L'Occitane - Cap Structure	
Last update	11/24/2023
Last px (HKD)	HKD 19.74
(x) Diluted S/O	1,486
Market cap	**HKD 29,334**
HKD/EUR	HKD 8.54
Market cap	**EUR 3,435**
(-) Cash on B/S (FY23)	EUR 147
(+) Debt (FY23)	EUR 519
Total Enterprise Value (TEV)	**EUR 3,806**
Net Debt	EUR 372
Pre-IFRS 16 '23 EBITDA	EUR 379
Net debt / EBITDA	1.0 x

Business background

L'Occitane is a global manufacturer and retailer of beauty and personal care products focusing on natural and organic ingredients. The company has close to 2,800 retail outlets with 1,360 owned stores and a presence in more than 90 countries. The company was incorporated in Luxembourg, has headquarters in France, and trades on the Hong Kong exchange.

The company's major brands include L'Occitane en Provence, Elemis, Sol de Janeiro, and others. Sales are split almost evenly across retail, online, and wholesale, each taking up roughly a third of the total. L'Occitane is well diversified geographically, with sales coming primarily from Asia Pacific (APAC) at 42%, followed by the Americas at 33% and EMEA at 25%. In FY23, the company generated €2.1B in sales and €337m in adjusted operating profit at a ~16% margin.

The company's leading brands (and reporting segments) are:

- L'Occitane en Provence - fragrance, skincare, haircare, and body and bath.
- ELEMIS (acquired in 2019) - skincare.
- Sol de Janeiro (acquired in 2021) - fragrance, skincare, haircare, and body care.
- Other brands - include Erborian, L'Occitane au Bresil, Grown Alchemist, LimeLife, and Melvita.

Recent events

The last six months have been volatile for the stock price. Let's recap what has happened since the company announced FY23 results.

1. June 26, 2023 - Management reports strong FY23 results but unveils an unexpected $100m incremental investment into marketing and growth investments, primarily directed at the core L'Occitane brand, which had performed well in FY23 (+7% YoY CC) ex. Russia (divested) and China.
2. August 8, 2023 - A Bloomberg story comes out, claiming that the company's Chairman, Reinold Geiger, who owns ~70% of the company, is interested in taking the company private at HK$35 per share (a 37% premium to the last closing price.)

3. August 11, 2023 - L'Occitane confirms that the Chairman is interested in taking the company private but at a price of "no less than HK$26."
4. September 4, 2023 - The Chairman reports that he has decided not to proceed with a deal to acquire the remaining shares of the company he does not own. The stock falls ~30% to HK$20.

Thesis

The near-term stock setup has been derisked due to the lowered margin guide for FY24 and the consequent failed take-private attempt.

The recent selling has been driven by two big non-fundamental events.

First, the company lowered its margin guide on account of the Board's decision to spend an incremental EUR 100m on marketing for FY24 (which brings down EBIT margins 400bps to ~12%, as per the guide). This decision was made despite the fact that core brands have performed quite well; even core L'Occitane grew nicely in FY23 if you exclude Russia and China. I believe that this expense is more likely to prove a one-off in nature rather than an increase in the cost of doing business.

Second, the Chairman decided to not take the company private after news stories claimed he was interested in doing so, initially at a price as high as HKD 35 per share. This caused the stock to trade back down to the HKD 20 range. Deal break events such as this one can be a good hunting ground for opportunities due to the technical selling pressure that occurs.

Combined, these events have created an attractive entry point in the stock, as the company continues to execute well, but the price has come down, and the shares have de-rated significantly in the interim.

L'Occitane's top line will continue to grow at least double digits due to Sol de Janeiro, which is growing triple digits and shows no signs of slowing down.

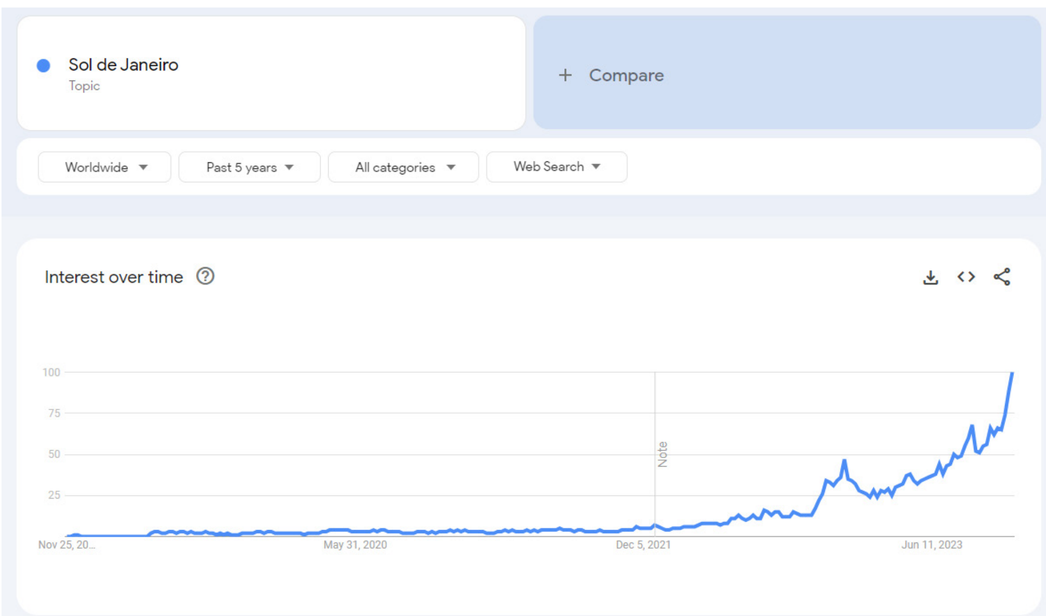
Sol de Janeiro (SdJ) has been a fantastic acquisition for L'Occitane. Over the past few quarters, the brand's growth has accelerated to triple-digits on an annualized revenue base of over **EUR 600m**, with the latest reported quarter (Q2) being particularly strong. If SdJ can maintain a similar rate of growth on an absolute "dollar" basis, the brand's growth will lead to a double-digit growth rate for L'Occitane.

	FY22 Q3	FY22 Q4	FY23 Q1	FY23 Q2	FY23 Q3	FY23 Q4	FY24 Q1	FY24 Q2	FY24 Q3	FY24 Q4		**FY22 A**	**FY23 A**	**FY24 E**	**FY25 E**	**FY26 E**
Sol de Janeiro	N/A	26	43	56	64	100	113	157	139	175		26	267	584	904	1,224
YoY %						284%	165%	180%	117%	75%			-	119%	55%	35%
CC %						268%	171%	202%	117%	75%				126%	55%	35%
Abs $						72	75	115	75	75				317	320	320

It's hard to forecast the growth of SdJ accurately. But, there are a few things here that give me confidence that SdJ can continue to, at the very least, keep growing at the same rate on an absolute "dollar" basis.

First, SdJ is expanding to new markets this year, such as Hong Kong. Second, SdJ has no presence in travel retail, an important sales channel for most BPC brands. This year, they have launched travel retail in Europe and North America. More importantly, SdJ will launch travel retail in APAC markets in the back half of FY23; these are some of the biggest markets for BPC in the world. Third, SdJ continues to launch successful new products. When SdJ was acquired, their *Bum Bum Cream* represented over 50% of sales. Less than two years in, however, SdJ's fragrance mists are now the number one selling product. Lastly, SdJ's exclusivity contract with Sephora in the US ends in FY24, allowing the brand to enter other retailers.

A Google Trends search also confirms that global search interest for Sol de Janeiro remains exceptionally high. Given the above, I see no reason why SdJ can't be a +EUR 1B brand within the next two years.



Google Search trends - Sol de Janeiro "Global" search (Nov 22, 2023)

A recovery in Elemis and core L'Occitane provides for further upside to top-line growth.

Both Elemis and L'Occitane en Provence had a couple of issues in FY23, which should prove to be temporary.

In the last few quarters, the brand Elemis has been making a move towards "premiumization". In order to carry this out, they have reduced their placement of products into e-commerce channels that had been overly promotional. This has weighed on growth in the last couple of quarters (FY24 H1: +7.6% cc), but management expects normalized growth to trend toward a mid-teens constant currency rate in the medium term.

For L'Occitane en Provence, the core band has had more hiccups. First, the brand divested its Russian operations in June 2022, which had an impact on the reported top-line numbers. This impact, however, will be lapped from Q3 (this coming quarter) onwards. Similar to other BPC companies, the core L'Occitane brand has slowed due to weakness in the Chinese market as well as in the APAC travel retail channel. The good news is that in the latest quarter (Q2 24), L'Occitane en Provence FY24Q2 saw an improvement and grew "double digits" in China. Management expects the core L'Occitane brand to grow at a mid-single-digit growth in the medium term.

L'Occitane as a whole is woefully underpenetrated in travel retail relative to peers. Once the channel recovers, there could be a meaningful upside. Moreover, the company is investing EUR 100m into marketing, with the bulk of this going to L'Occitane en Provence. This investment could also serve as a catalyst to re-accelerate sales in the company's core brand beyond MSD.

I expect L'Occitane's EBIT margin to quickly revert back above 15% in FY25.

Despite the significant investment of EUR 100m slated for FY24, I expect that the faster-growing brands Sol de Janeiro and Elemis will be able to help offset the drag due to their higher margins.

Sol de Janeiro carries an operating margin of ~25% relative to L'Occitane en Provence, which sits at a mid-teens margin. Likewise, Elemis operates with an operating margin closer to 20%. These two brands will drive the majority of growth over the next few years, and the overall margin will benefit from this positive mix shift for years to come.

Despite the talk of incremental investment, the company reiterated that its mid-term guide of ~16% operating margins was intact. To me, the whole guide seems like a good way to reset expectations (particularly if you're going to make a bid for the company). This means that there is a good chance that we will see continued margin expansion from these levels.

The low absolute and relative valuation makes the risk/reward compelling. Importantly, the downside is likely capped by potential corporate action.

L'Occitane's valuation is outrageously cheap. The stock is trading at ~14x FY24 earnings on what will be trough margins (~15x consensus numbers). On my FY25 estimates, the stock is likely trading closer to 10x earnings. Historically, 973.HK has traded at an average multiple of ~20x earnings, with an all-time low multiple of ~12x earnings.

Skincare/beauty peers (L'Oreal, Estée Lauder, Shiseido, etc.) tend to trade at >30x earnings and ~20x EBITDA with sell-side estimates that call for mid to high-single-digit top-line growth. In M&A transactions, you see similar multiples. Aesop, for instance, was recently sold to L'Oreal for ~20x EBITDA.

The downside is well protected, given the low valuation and the fact that the company is likely to pursue some corporate action to unlock the value if the value discrepancy remains. The Chairman might try to acquire the company again, or the company might try a re-listing on another exchange. This was an alternative that was being explored at the same time the Chairman had been looking to take the company private. The "bid" from the Chairman was HKD 26 per share. On FY24 earnings, that would have implied a multiple of 20x (EUR 2.5B at a 12% EBIT margin, assuming 25% tax).

Valuation & Price Target

The company's valuation is incredibly attractive.

- $973.HK is trading at a very inexpensive valuation on my estimates:
  - On FY24 estimates, $973.HK is trading at 14x EPS (trough margin)
  - On FY25 estimates, $973.HK is trading at 10x EPS.
- My **price target is HKD 40 per share**. I keep the valuation simple and value the company on a P/E multiple. I use a 20x P/E multiple on my FY25. This implies an EV of ~EUR 6.8B or a 15x EBIT multiple.
- If I roll forward my 20x PE multiple on FY26 estimates, I think the stock could be worth roughly HKD 50 per share in ~2 years.

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(+) Debt (FY23)	EUR 519
Total Enterprise Value (TEV)	**EUR 3,806**
Net Debt	EUR 372
Pre-IFRS 16 '23 EBITDA	EUR 379
Net debt / EBITDA	1.0 x

Valuation	
FY24 EBIT (CSC Est.)	**EUR 315**
TEV / EBIT on '24E	12.1 x
FY25 EBIT (CSC)	**EUR 444**
TEV / EBIT on '25E	8.6 x
FY24 EPS in HKD (CSC)	**HKD 1.37**
P/E on '24E	14.4 x
FY25 EPS in HKD (CSC)	**HKD 1.93**
P/E on '25E	10.2 x
FY26 EPS in HKD (CSC)	**HKD 2.48**
P/E on '26E	8.0 x

Price Target	**FY25E**	**FY26E**
P/E Multiple	20.0 x	20.0 x
Market value / share	**HKD 39**	**HKD 50**
Upside/downside	95%	151%
Market Cap	**EUR 6,713**	**EUR 8,618**
(+) Net debt (T-1)	EUR 136	(EUR 197)
Total Enterprise Value (TEV)	**EUR 6,849**	**EUR 8,421**
Implied EBIT Multiple on '25E	15.4 x	14.8 x
Implied EV/Sales	2.3 x	2.5 x

Risks

- There is a big risk of a take-under from the Chairman since he owns ~70% of the company.
- It's possible that we don't see a re-rating, given that the stock trades in Hong Kong. Although, it's hard to ignore growing earnings over time.
- China/travel retail weakness could continue, although L'Occitane is less exposed than most BPC companies.

Catalysts

- FY24 earnings showing a much better FY25 EBIT guide + continued trading updates showing top-line growth, particularly for SdJ.
- Possible buyout offer from the current Chairman.
- Possible re-listing the stock to another exchange.
- The mid-term (FY26) guide will have to be upgraded, as the company had set this in FY22 when Sol de Janeiro had just been acquired. Initially, they expected the brand to CAGR at ~30%, but SdJ has grown dramatically faster than management's initial expectations.

A list of mid-cap stocks that could become the next $100 billion behemoths (from All Star Charts)...

Welcome to The 2 to 100 Club.

As many of you know, something we've been working on internally is using various bottom-up tools and scans to complement our top-down approach.

It's really been working for us!

One way we're doing this is by identifying the strongest growth stocks as they climb the market-cap ladder from small- to mid- to large- and, ultimately, to mega-cap status (over $200B).

Once they graduate from small-cap to mid-cap status (over $2B), they come on our radar. Likewise, when they surpass the roughly $30B mark, they roll off our list.

But the scan doesn't just end there. We only want to look at the strongest growth industries in the market, as that is typically where these potential 50-baggers come from.

Some of the best performers in recent decades – stocks like Priceline, Amazon, Netflix, Salesforce, and myriad others – would have been on this list at some point during their journey to becoming the market behemoths they are today.

When you look at the stocks in our table, you'll notice we're only focused on Technology and Growth industry groups such as Software, Semiconductors, Online Retail, Solar, etc.

Then, like any good technician, we filter the list down to those closest to new highs. This allows the cream of these strong groups to rise to the top and helps streamline our mission to identify technical breakouts in the top-performing stocks.

Here is this week's list:

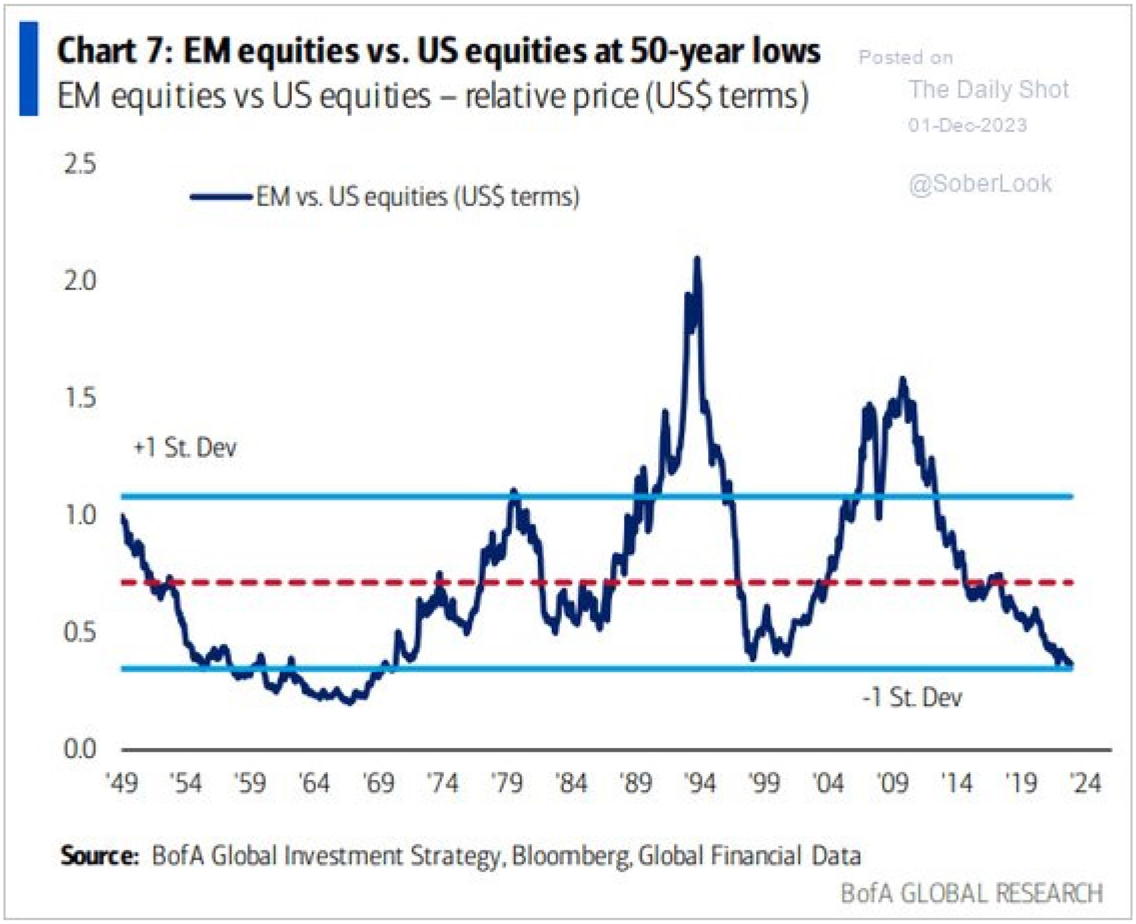
2-to-100 Club

Ticker	Company	Industry	Country	Market Cap (Millions)	Percentage From 52-Week High
NET	CloudFlare Inc	Software - Infrastructure	USA	$28,712	0.00%
SNAP	Snap Inc	Internet Content & Information	USA	$28,285	0.00%
PINS	Pinterest Inc	Internet Content & Information	USA	$25,653	0.00%
GIB	CGI Inc	Information Technology Services	Canada	$24,945	0.00%
GRMN	Garmin Ltd	Scientific & Technical Instruments	Switzerland	$24,307	0.00%
ICLR	ICON plc	Diagnostics & Research	Ireland	$23,420	0.00%
BR	Broadridge Financial Solutions, Inc.	Information Technology Services	USA	$23,179	0.00%
PHG	Koninklijke Philips	Medical Devices	Netherlands	$21,530	0.00%
EXPE	Expedia Group Inc	Travel Services	USA	$21,038	0.00%
PTC	PTC Inc	Software - Application	USA	$20,508	0.00%
FLT	FleetCor Technologies Inc	Software - Infrastructure	USA	$20,116	0.00%
ASX	ASE Technology Holding Co Ltd	Semiconductors	Taiwan	$19,749	0.00%
LH	Laboratory Corp. Of America Holdings	Diagnostics & Research	USA	$19,022	0.00%
CHKP	Check Point Software Technologies Ltd.	Software - Infrastructure	Israel	$18,187	0.00%
AKAM	Akamai Technologies Inc	Software - Infrastructure	USA	$18,127	0.00%
AFRM	Affirm Holdings Inc	Software - Infrastructure	USA	$15,225	0.00%
GDDY	Godaddy Inc	Software - Infrastructure	USA	$15,126	0.00%
PATH	UiPath Inc	Software - Infrastructure	USA	$14,865	0.00%
TWLO	Twilio Inc	Internet Content & Information	USA	$14,094	0.00%
Z	Zillow Group Inc	Internet Content & Information	USA	$13,514	0.00%
ZG	Zillow Group Inc	Internet Content & Information	USA	$13,299	0.00%
FLEX	Flex Ltd	Electronic Components	Singapore	$12,963	0.00%
HOOD	Robinhood Markets Inc	Software - Infrastructure	USA	$11,389	0.00%
GLOB	Globant S.A.	Information Technology Services	Luxembourg	$10,432	0.00%
DBX	Dropbox Inc	Software - Infrastructure	USA	$10,411	0.00%
DUOL	Duolingo Inc	Software - Application	USA	$10,141	0.00%
MEDP	Medpace Holdings Inc	Diagnostics & Research	USA	$9,407	0.00%
OLED	Universal Display Corp.	Electronic Components	USA	$9,153	0.00%
CYBR	CyberArk Software Ltd	Software - Infrastructure	Israel	$8,788	0.00%
GWRE	Guidewire Software Inc	Software - Application	USA	$8,618	0.00%
AMKR	AMKOR Technology Inc.	Semiconductor Equipment & Materials	USA	$8,305	0.00%
S	SentinelOne Inc	Software - Infrastructure	USA	$8,208	0.00%
QLYS	Qualys Inc	Software - Infrastructure	USA	$7,574	0.00%
FRSH	Freshworks Inc	Software - Application	USA	$7,218	0.00%
CVNA	Carvana Co.	Auto & Truck Dealerships	USA	$6,819	0.00%
WIX	Wix.Com Ltd	Software - Infrastructure	Israel	$6,790	0.00%
MTSI	MACOM Technology Solutions Holdings Inc	Semiconductors	USA	$6,762	0.00%
AUR	Aurora Innovation Inc	Information Technology Services	USA	$6,581	0.00%
NSIT	Insight Enterprises Inc.	Electronics & Computer Distribution	USA	$5,983	0.00%
STNE	StoneCo Ltd	Software - Infrastructure	Cayman Islands	$5,387	0.00%
MMYT	MakeMyTrip Ltd	Travel Services	India	$4,973	0.00%
VRNS	Varonis Systems Inc	Software - Infrastructure	USA	$4,953	0.00%
BLKB	Blackbaud Inc	Software - Application	USA	$4,713	0.00%
KD	Kyndryl Holdings Inc	Information Technology Services	USA	$4,627	0.00%
NVMI	Nova Ltd	Semiconductor Equipment & Materials	Israel	$3,898	0.00%
CVLT	CommVault Systems Inc	Software - Application	USA	$3,525	0.00%
WIRE	Encore Wire Corp.	Electrical Equipment & Parts	USA	$3,406	0.00%
FROG	JFrog Ltd	Software - Application	USA	$3,393	0.00%
ITGR	Integer Holdings Corp	Medical Devices	USA	$3,330	0.00%
ACIW	ACI Worldwide Inc	Software - Infrastructure	USA	$3,301	0.00%
YELP	Yelp Inc	Internet Content & Information	USA	$3,206	0.00%
GHC	Graham Holdings Co.	Education & Training Services	USA	$3,082	0.00%
ESE	Esco Technologies, Inc.	Scientific & Technical Instruments	USA	$2,963	0.00%
LSPD	Lightspeed Commerce Inc	Software - Application	Canada	$2,959	0.00%
CARG	CarGurus Inc	Auto & Truck Dealerships	USA	$2,737	0.00%
QTWO	Q2 Holdings Inc	Software - Application	USA	$2,584	0.00%
AIR	AAR Corp.	Aerospace & Defense	USA	$2,551	0.00%
NEO	Neogenomics Inc.	Diagnostics & Research	USA	$2,551	0.00%
RAMP	LiveRamp Holdings Inc	Software - Infrastructure	USA	$2,380	0.00%
XRX	Xerox Holdings Corp	Information Technology Services	USA	$2,270	0.00%

Data As Of December 19, 2023

ALL STAR CHARTS

Emerging market equities are historically cheap versus U.S. equities ([from The Daily Shot]()...



These are the only four times you should consider "averaging down" on an investment (from MicroCapClub)...

I was recently interviewed by Morningstar India and I was asked about averaging down into losers and this was my answer:

"If you personally lent someone money, and they only repaid you half of what they owed you, would you give that person more money? Of course not. Yet we continually do this with our investing, where we average down into things that have a history of disappointing us."

Averaging down can be a wonderful thing. In fact, variable pricing is the best thing about the public markets. Short-term stock prices are yanked like a dog on a leash by the madness of the crowd.

Investor sentiment is a pendulum that swings back and forth between extreme optimism and extreme pessimism and never sits still. It's on the extremes where the astute investor waits patiently buying or selling.

Even Berkshire Hathaway, one of the largest, most durable businesses in the world trades in a 30-50% trading range every year. Every. Year.

Coincidentally this is also why many successful short-term traders focus on trading the same 2-3 stocks every year. There is enough volatility in a couple things to make a living. These successful traders find the pulse of a company's stock. They know when the heartbeat becomes irregular.

Microcap stocks are inherently more volatile which means you will have even more chances to average down.

In the Art of Catching Falling Knives I wrote about how at least once per year I'll wake up to a position trading down 30% premarket. Some large holder wakes up grumpy and decides today will be the day to sell their entire position in an illiquid stock as quickly as possible.

It always feels like you'll never get another shot to buy a company you love, but almost every year the market gives you another opportunity.

This leads us to the most important question - When should you average down?

The answer is to invert the list of situations to avoid. You should only average down when:

- The business is accelerating.
- The business is profitable with no financing risk.
- The business has a sustainable growth trajectory.
- The business doesn't have a lot of debt.

Don't average down into losers. Average down into winners.

If a stock is dropping and the underlying business doesn't have all four characteristics above, let the stock drop. Let the position become a smaller portion of your portfolio. Don't catch the knife.

We all have losses in the portfolio. It's part of the game. Don't turn a loss into a mistake. Mistakes are when our actions or inaction turns a small loss into a bigger loss. It's when you are hurting your returns.

Averaging down is a skill. Done well it can be your greatest asset. Done poorly it can mean disaster.

The most gut wrenching and emotional times are when stocks fall. Remember the four characteristics you need to justify averaging down. Bookmark this article. It will help you when you need it.

Continue reading here.

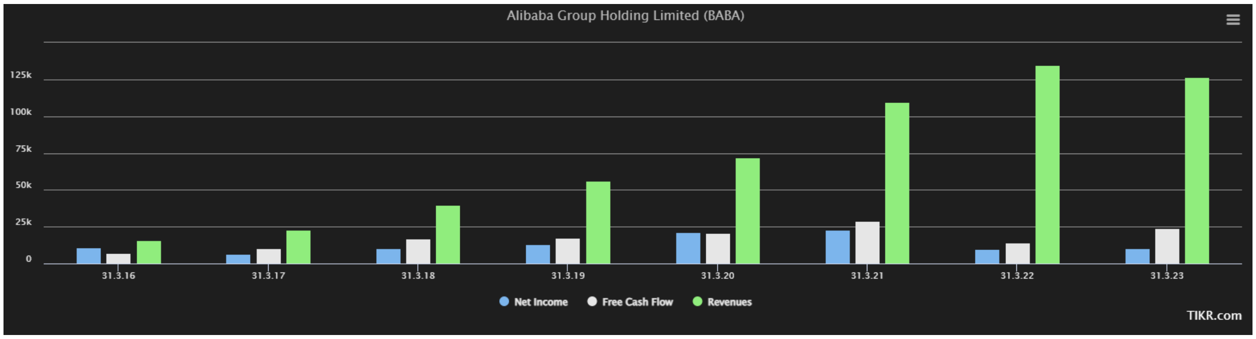
The "Chinese Amazon" is looking cheap (from Daniel via X)...

Alibaba ($BABA) is down 77% from its all-time highs. It's 24% below the IPO price in 2014.

Since then, revenues have grown over 11x and profits almost 5x.

Alibaba has a market cap of $180b and cash and short-term investments of ~ $80b plus $24b FCF per year.

There are many problems, but this is insane. If you want a closer look, here's my (very extensive) $BABA and China Deep Dive.:



A summary of the investment thesis in healthcare IT firm R1 RCM (from Voss Capital via X)...

Here is a new investment memo on a high conviction long idea $RCM.

R1: Shorts are Penny Wise, Pound Foolish

We believe the recent weakness of R1 (RCM) shares provide a unique entry opportunity into a high-quality healthcare IT franchise and that the stock could double or more over the next 2-3 years, as profitability inflects toward an eventual $1 billion in underlying FCF and the company's industry leading, technology-focused position in a secularly growing industry become more apparent.

The company has been hit by a number of headwinds in the last several months, namely a monstrous 95 page short report that questioned accounting integrity (driving 15%+ short interest), a small increase in doubtful accounts that seemed to partially validate the short report, the bankruptcy of a customer, their first ever customer loss, and a general move away from levered stocks (and healthcare services due to weaker spending cadence and utilization, not to mention fears of GLP-1's reducing demand for healthcare services longer term). We go through these issues and conclude that while highlighting some valid concerns, they are extremely short-sighted and entirely miss the forest for the trees and fail to recognize the long runway for RCM adoption and the increasing strategic value of R1. In fact, once digging under the covers, we come to the opposite conclusion of the short report and see cash flows and profitability already inflecting positively, even as R1 onboards its largest customer ever which causes a short-term profitability hit.

In short, we believe all the pieces are coming together for an attractive long term secular compounder. We see a large market opportunity paired with a terrific management team and a business that solves a real need with limited competition, trading at low absolute and relative valuations.

Summary

R1 currently has very negative sentiment. It is getting hit by both stylistic (floating debt, healthcare IT, SMID) and idiosyncratic factors (accounting, management, customer loss/bankruptcy, negative estimate revisions). While we cannot dismiss all these negatives as "nothing", it is our variant view that "under the covers" things are way better than they appear at first glance. Furthermore, our diligence suggests a very large opportunity with a strong management team that is thinking with the long term in mind.

We believe there is limited downside over the next two years as there is still latent profitability building that will show up from maturing customers and ongoing Modular growth.

Twelve months from now, we think the investment narrative will have transformed significantly as management signs new customers, earnings quality improves substantially, deleveraging begins in earnest, and hospitals become incrementally more healthy, leading to what will be viewed as a scarce high quality healthcare IT asset trading closer to fair value which should put the stock ~100% higher.

Read the full memo here.

A detailed overview of the most successful hedge-fund strategies (from Laura Kodres via the IMF eLibrary)...

Perhaps one reason why it is difficult to arrive at a definitive characterization of hedge funds is the wide variety of investment strategies they undertake. Hedge funds, as portrayed in most press reports, have been variously discussed as "gunslingers" and "swaggering buccaneers" who routinely test the resolve of authorities in various countries.1 However, in truth, the managers of hedge funds employ a vast array of investment strategies with the goal of producing profits for themselves and their investors. Their strategies include trades aimed at taking a view about the macroeconomic policies of selected countries as well as seemingly arcane movements in the pricing of the cash and futures relationship for the 30-year U.S. treasury bond: hedge funds operate both as speculators as well as hedgers. Since hedge fund investment strategies are only limited by the constraints imposed in their own prospectuses, it should not be surprising that their strategies cover a myriad of markets and instruments.

Although several data vendors classify hedge funds into as many as 28 different categories,2 for the purposes here two main types are discussed—funds using arbitrage-type strategies and funds attempting to profit from perceived discrepancies in macroeconomic policies, the so-called macro funds. An "all else" category that includes individual sectors and special strategies is discussed in general terms to convey the diversity in the mix of strategies. Some discussion of various categories of hedge funds is also presented in Section III, matching the data source used to analyze various features of hedge funds. It is worth stressing that most categorizations of hedge funds are done for the purpose of helping investors understand how the funds intend to make money. However, while hedge funds may mostly use a given strategy, undoubtedly there are variations on the theme, and hedge funds are apt to assure themselves some latitude in their prospectus as to the types of strategies they can undertake. Thus, the characterizations below should not be taken too literally.

The types of instruments used by hedge funds to implement their strategies can be quite varied. As a general rule, however, the instruments can be divided into three types: (1) spot or cash instruments; (2) futures, forwards, and swaps; and (3) options and contingent claims. The payoffs and risks inherent in these instruments are slightly different and thus it will be useful to separate them. Table 4.1 provides a very broad characterization of the types of instruments hedge funds are permitted to use, given their prospectuses. Since these data are based on the instruments that hedge funds claim they might use, the table should not be interpreted as an indication of the frequency of their use. Furthermore, some of the hedge funds do not indicate the types of instruments they use in the data set.

Table 4.1.

Proportion of Hedge Funds Using Various Instruments Ranked by Quintile of Asset Size[1]

(In percent)

Quintile	Number of Hedge Funds	Stocks	Bonds	Currency	Warrants	Options	Futures
First	161	81	68	30	42	68	39
Second	161	91	61	22	47	66	34
Third	161	90	47	22	43	72	28
Fourth	161	94	43	17	40	60	19
Fifth	161	86	41	22	36	60	27

Source: Calculated from the Mar/Hedge database.

[1]Eleven hedge funds did not have complete information on their use of various instruments, and hence, they are excluded from the sample.

Of the types of instruments hedge funds use, spot or cash market instruments are usually the simplest to understand. For the most part, a standard list of these instruments would be foreign exchange spot contracts, fixed-income, and equity securities without any special features. The management of the risks of cash market positions is relatively straight-forward in that one needs only to have historical and current information about price levels (and perhaps forecasts of future values). This is not to say, however, that the actual risk is negligible, just that calculating various measures of risk can be undertaken relatively easily. For instance a position in Russian GKO government bonds or the Hungarian forint may be straightforward to value, but the risk of loss may be quite high. Many hedge funds use only spot or cash instruments to effect their strategies. Some use mostly spot or cash instruments, occasionally combining them with futures, forwards, or options to reduce certain risks.

Futures, forwards, and swaps are all instruments that have similar payoffs to spot and cash instruments in that their values either increase or decrease more or less one-for-one with the values of the instruments underlying them—that is, they have linear payoff structures. Since these instruments mature in the future, there is often additional risk, termed “basis risk” that their movements may not exactly move with the underlying spot or cash rate until close to maturity. Thus, controlling and monitoring risks in these instruments is slightly more difficult than for pure spot or cash instruments. Hedge funds are often large users of these instruments, particularly futures and forwards, as it allows them to take positions on the movement of the underlying spot or cash market without having to hold the instrument itself (until delivery). Most funds have no particular commercial interest in owning the underlying instrument, which can sometimes entail a commodity with special storage issues (such as oil or soybeans), and prefer to offset their positions prior to the maturity of the contract. Among the most commonly used instruments are currency forwards, fixed-income futures and swaps, and equity index products.

Options and other contingent claims are very different from both of the other two types of instruments because they have payoffs that are either zero or some positive amount, depending on the value of the underlying instrument. Because options provide the “option” but not the obligation to execute the contract, the payoff from options is called “convex” and is nonlinear. This difference has several implications, the most important of which is that managing the risk in a portfolio of options is much more complicated than managing the risk of a set of spot or forward positions. Another feature of options is that while buyers are typically required to make an up-front payment of the cost of the option, if the strike price of the option3 is substantially different from the current price then a given movement in the value of the underlying instrument may lead to a larger change in the value of the option. This feature provides greater leverage, in the sense of a larger potential price move in the option than in the underlying instrument.

Strategies Used by Arbitrage-Type Hedge Funds

Analytics Behind the Strategies

Arbitrage is defined as the ability to profit from current price discrepancies in two instruments that will, at their expiry or maturity, have the same value, or a value that is different by a known (certain) amount at the time the arbitrage is initiated. The use of the term “arbitrage” has been slowly loosened to refer to various misalignments or “mispricings” of similar instruments or instruments that are thought to have similar characteristics or underlying driving factors. Despite the weakening of the original definition, generally, hedge funds that view themselves as using an arbitrage strategy utilize some type of analytical model that values various instruments and attempts to profit from the discrepancy between their “model” value and the actual market price. The key is that this type of strategy always involves two transactions: a purchase of the “undervalued” instrument and a sale of the “overvalued” instrument. An outright purchase of an undervalued equity security, for example, would not qualify as an “arbitrage.”

Many types of arbitrage strategies can be undertaken. An obvious one involves the simultaneous purchase and sale of two instruments that are expected at expiry or maturity to have the same value. Many hedge funds trade a cash instrument against its futures counterpart—a classic case for arbitrage. The most popular in the United States is the U.S. treasury bond futures contract, in which self-declared, large participant hedge funds hold about 8 percent of the open interest.4 In this case, the object is to profit from a misalignment in the futures price of the cheapest-to-deliver bond, the one bond among those qualifying for delivery that would be cheapest for the seller of the futures contract to deliver,5 and the current market price of another bond that is expected to maintain a certain pricing relationship to the cash market price of the cheapest-to-deliver bond. Similar, but less complicated, relationships exist between, say, an index of equity securities and the futures contract price based on such an index. Similarly, the strategy may be initiated for relationships between a currency spot price and its associated futures contract price. For hedge funds deemed to be large futures market participants for reporting purposes, the most popular futures contracts are the five-year treasury note contract, where hedge funds account for about 10 percent of open interest, and the S&P 500 index contract, where hedge funds account for about 8 percent of open interest.

Another "arbitrage" strategy undertaken by hedge funds is a misalignment in prices of cash market fixed-income securities. For example, a hedge fund might have a model for the levels of yields representing a number of bonds with various maturities. This model of the "yield curve" at a given time may differ from the yields of some of the maturities indicating that certain bonds may be overpriced or underpriced relative to the model. The fund would buy those bonds it thought were underpriced relative to a correctly priced bond and sell those that were over-priced relative to another correctly priced bond to gain the differences between those prices and the prices that would be consistent with their model. In principle, the hedge fund would attempt to hedge any other risks associated with such a trade. For example, the fund would enter into other transactions to make sure a shift in the entire yield curve or some other possible alteration in the slope of the yield curve would not affect the outcome of the trade, thereby allowing it to profit purely from the observed price discrepancy.

Another arbitrage would be a mispricing because of the credit quality of two instruments. For example, a corporate bond may have the same coupon and maturity as another, except that the second corporate entity has a different credit rating and the price does not appropriately reflect this credit risk difference. Perhaps the usual basis point differential between two such credit ratings is 30 basis points, but the current differential is 50 basis points (and the ratings are not expected to change). The "more expensive" bond, the one with the lower yield relative to the expected spread, would be sold and the "cheaper" bond would be purchased. These sorts of trades are routinely executed by hedge funds examining the differences in the creditworthiness of various U.S. corporate securities relative to the U.S. treasury bond yield spreads. Emerging market hedge funds (to be discussed below in detail) may attempt to arbitrage the difference between two sovereign bonds that have the same price but different credit ratings.

Combining aspects of the fixed-income market and the equity market is a strategy called convertible arbitrage. This strategy involves purchasing convertible securities, mostly fixed-income bonds that under certain circumstances can be converted to an equity security. A portion of the equity risk embedded in the bond is hedged by selling short the underlying equity. Sometimes the strategy will also involve an interest rate hedge to protect against general fluctuations in the yield curve. Thus, this trade would be designed to profit from the mispricing of the equity component of the convertible bond relative to traded equity.

Another variant that combines fixed-income securities and other securities is the mispricing of the options or other features embedded in mortgage-back securities. Often the complicated structures can be decomposed into various components that have counterparts in the market, permitting hedge funds to profit from deviations in the prices of the underlying components and the structured product. For example, the prepayment risk, the risk that the mortgage holder will prepay the mortgage prior to its maturity, in collateralized mortgage obligations may be mispriced relative to this risk embedded in other similar securities or in a portfolio of similar mortgages.

Within the equity market, a core position of purchased equities may be offset with a short equity index futures position or a put option on an equity index to mitigate the general market movements. In this case, the objective is to profit from the firm-specific characteristics of the chosen equities and to eliminate the risk of general marketwide movements. Similarly, some funds choose to buy the strong firms in an industry and sell the weaker firms, attempting to profit from the firm-specific differences within a given industry. These funds are often referred to as market-neutral funds.

The variety and complexity of various options contracts makes them fertile ground for arbitrage-oriented hedge funds. Since options valuation depends on a number of different variables, often in complicated ways, there are profit opportunities arising from better models of forecasting the underlying variables, most notably the volatility of the underlying instrument, as well as improved models for combining the underlying variables into prices. For instance, the implied volatility associated with different strike prices varies, usually with at-the-money options (those whose strike price is close to the current price of the underlying instrument) having lower implied volatility than other options with different strike prices. Analysis of the volatility relationship among strike prices may permit funds to see when specific options prices are out of line with their usual configuration.

Hedge funds also keep banks busy by arbitraging between their over-the-counter derivatives quotes. The situation may arise not just with plain-vanilla options but more complicated options. Hedge funds may compare the implied volatility in a structured product, for instance, a cap or floor structure with a barrier, or knock-out, option. A two-sided barrier option has a similar structure to a combined cap and floor but may have a different implied volatility, that is, a different price.

Strategy Determinants

Once a potential strategy looks promising, virtually all hedge funds examine whether the all-in return more than compensates for the degree of risk undertaken. Actually, many of the determinants of a viable strategy are not specific to hedge funds, but are common to many types of investors. The weighting of the determinants may differ, however, because of the compensation structures of hedge fund managers as discussed below. Three elements of this calculation are performed, with different types of hedge funds weighting their outcomes differently. The first is an examination of market risk, which usually includes some type of "stress test" to assess the downside risks of the proposed strategy. The second is an examination of the liquidity risk, that is, to see whether the hedge fund can enter and exit the markets for the instruments in a way that allows them to leave prices unaffected in normal times. Also important is whether they will be able to exit in a timely fashion during periods of market distress. The third is an examination of the timing and the cost of financing the position. If the expected duration of the trade is too long, making the cost of financing the position prohibitive, the strategy will not be undertaken.

Since hedge funds attempt to provide higher-than-normal returns to their investors and themselves, the market risk component is, in all cases, of crucial importance. Many arbitrage-related hedge funds are explicitly attempting to profit from a particular type of market imperfection and thus try to minimize the other risks associated with the strategy. To do so, they must understand these risks and they typically have invested heavily in very sophisticated ways of measuring and monitoring risk. Many of the larger arbitrage funds perform very specific and extensive stress tests to observe what happens to their trades under various scenarios. In fact, one way of testing the models on which the strategies are based is to perform such experiments. For instance, the appropriate number of bonds to sell of one maturity against another maturity to take advantage of a yield curve misalignment may be calculated by moving the yield curve by 100 basis points in both directions or by assuming a particular slope change and then using the number of contracts associated with the scenario thought most likely. In essence this is part of a stress test and would be typical of any reasonably sophisticated risk management system. Some of the larger hedge funds have daily value-at-risk models that calculate the amount of money the fund could lose assuming a certain distribution of returns of the underlying instruments held by the fund and a prespecified probability of loss. So, for example, a hedge fund's VAR model calculates that the fund could lose "x" or more dollars over a one-day horizon, on 2.5 percent of the trading days (97.5 percent of the outcomes are losses less the "x"), assuming the underlying instruments follow a normal distribution.

Liquidity risk is also very important for arbitrage-type hedge funds. The ability to make money using arbitrage-type strategies means that both legs of the arbitrage trade need to be executed together—both at initiation and at termination of the trade. Thus, the liquidity of both markets needs to be such so as to enable the fund to get in and get out without disrupting the prices: a liquid market is essential. In fact, most arbitrage-type hedge funds use only very liquid markets: the U.S. Treasury and agency markets, the U.S. and other Group of Ten equity markets, and the major currency markets (mostly the deutsche mark and the Japanese yen). This is not to say that arbitrage hedge funds never enter smaller, less liquid markets but that the potential profits have to be large enough to offset the price impact of entering and exiting the market. These types of hedge funds are reluctant to enter into trades in which either side of a trade is in a market that could become illiquid during a period of stress.

Lastly, the timing and financing of trades can be of critical concern for some types of arbitrage hedge funds. For instance, suppose there appears to be a gap between the prices of an equity index futures contract for delivery nine months hence and the underlying equity securities such that the strategy would involve selling short the equities and buying the index futures contract. Short selling U.S. equities is a trade that has a margin requirement of 50 percent (as established by Regulation T of the Federal Reserve Board) and buying the futures contract has an initial margin requirement of about 2.5 percent, depending on the contract. Holding the trade for nine months, the longest one would need to in order to assure a risk-free return in this example, means tying up one-half of the notional amount of the trade for that duration, in addition to the futures margin. This may be deemed too expensive as the opportunity cost of the capital for the short equity position may be quite high. Thus, the combination of the timing and the financing cost may mean that what initially look like profitable strategies are not.

Arbitrage hedge funds attempt to use the fact that they are using at least partially offsetting positions to obtain better financing arrangements. For instance, government dealers may be willing to finance a U.S. treasury bond position at a lower rate if taken against the 10-year bond futures contract than if the position was an outright position. Netting is commonly used as a means of lowering the cost of taking on positions as the lower risk on the netted position means that marked-to-market gains and losses will be commensurately lower. Along the same lines, hedge funds look for various instruments to profit from a given discrepancy between two markets, attempting to minimize the funding cost of the position by choosing the instrument with the lowest required margin.

Examples of Strategies

Yield curve misalignment. During January 1995, it became known that Orange County in California had incurred substantial losses associated with the purchase of some leveraged derivatives based on mortgage-backed security trades. The county was required to sell a large number of two-year U.S. treasury notes. At least one arbitrage-based hedge fund noted that this provided a classic arbitrage trade. They purchased two-year treasury notes while shorting one-year treasury bills and five-year treasury notes. Aside from making their investors a substantial profit with little risk, they viewed themselves as supplying liquidity in a period in which an aberration had forced markets out of alignment.

Equity-market-neutral investing. A classic equity market strategy is called the market-neutral portfolio. Essentially, these portfolios are constructed to eliminate the movement in equity indices, that is, general market movements. These strategies can take the form of a number of purchased individual equities expected to outperform the equity market and a passive short equity index futures position or an active short equity position. When an active short position is maintained, the strategy is often referred to as a long/short strategy, in which the simultaneously short position is maintained in stocks with poor value, earnings, or momentum characteristics. Portfolios can then be further fine-tuned to reduce both stock-specific or sector-specific exposure.

Equity derivative arbitrage. Another method of profiting from equities irrespective of the market's direction is to use derivative securities such as convertibles and equity warrants.6 For example, taking a positive view on a particular company can be expressed by buying the equity, the warrant, or the convertible. The latter two instruments provide an additional source of excess return, an element called "the derivative alpha," which is the value associated with the implicit leverage in the derivative instrument part of the security. Through these derivatives, which are both types of options, the investor "purchases" volatility in the equity. If the actual volatility experienced over the subsequent holding period is larger than the implied volatility embedded in the option's price at the time of purchase, there will be an additional return obtained from holding the equity derivative, over and above that obtained by holding the equity directly. This makes up part of the value of the derivative alpha. In addition, warrants and convertibles may appear cheap on a stock that is not borrowable (and thus has little downward pressure from short sales) or on a stock that is expensive because of other reasons.

Bond basis arbitrage. A very popular arbitrage is that between a specific U.S. treasury bond and the treasury bond futures contract traded on the Chicago Board of Trade. The futures contract specifies that a number of U.S. treasury bonds can be delivered by the seller of the futures contract to the buyer at maturity of the contract. The seller prefers to deliver the bond that is "cheapest" to purchase in the cash market. Calculating the relative cheapness of various bonds is fairly complicated (involving the "conversion factor" assigned to the bond for futures market delivery on a particular date and the overnight financing rate, or repo rate, for that specific bond), but there are a few determinants that are discretionary. Thus, when particular bonds become popular (or unpopular) because of unrelated events in the cash market, the normal relationship relative to the futures contract becomes distorted and arbitrageurs can buy or sell the bond, taking the opposite position in the futures contract, to make a profit. Rumors in the futures market on October 27, 1997 suggested that several large hedge funds bought futures and sold treasury bonds when prices of bonds responded to a "flight to quality" from the relatively large fall in equity prices on that day. That is, the cash bonds became "overpriced" relative to the futures prices as individuals flocked to buy U.S. treasury bonds and an arbitrage profit became available.

Italian tax-driven arbitrage. Until mid-1996, the Italian government imposed a 12.5 percent withholding tax on investors from countries lacking a reciprocal tax treaty with Italy. Since reclaiming the taxed amounts were considered so cumbersome, the spreads between Italian government bonds and the rate for lira interest rate swaps traded as though the 12.5 percent could not be reclaimed; this added about 100 basis points to a fixed rate government bond issue yielding 8 percent. This meant that government bond yields were driven above lira swap rates. By buying the fixed rate Italian government bonds, financing them in the lira repurchase market, and setting up a lira interest rate swap with offsetting payment streams, arbitrageurs were able to construct offsetting cash flows. The profits on the trade then stemmed from the ability of the arbitrageurs to obtain below-market rates on the repo transactions and then routinely file for the withholding tax rebate. Moreover, further gains were obtained when the spread between the Italian government bonds and the lira interest rate swaps converged as the withholding tax was eliminated.

Credit duration risk via an options convexity trade. This strategy compares foreign bonds with U.S. treasury bonds and uses options to take advantage of a differential movement in bond prices due to the market's assessment of credit risk. For example, the trade may match a Mexican government bond (UMS) with a U.S. treasury bond having the same set of cash flows (or a set of cash flows with the same duration). While changes in the bonds' prices will be the same for various interest rate changes (duration is matched), the UMS bond will respond more dramatically to perceived credit risk changes (the price is more sensitive to changes in volatility). The fund could implement this strategy by buying UMS option straddles7 and selling U.S. treasury bond option straddles. A weighting of UMS straddles to U.S. treasury bond straddles would leverage the changes in a way that the larger movements (either up or down) in the UMS bonds would make the options even more valuable relative to the U.S. treasury bond straddles, which will lose money if prices move dramatically up or down. However, the position is immune to a change in the convexity of the bonds from an interest rate change due to the offsetting options positions and their matched durations.

Strategies Used by Macro Funds

The strategies of macro hedge funds differ from those of arbitrage funds in that they are typically based on models using information on economic fundamentals. The arbitrage funds, as their name implies, use arbitrage-based models of price determination to detect profitable differences in prices rather than attempt to ascertain whether the level of prices is appropriate to begin with. There are many different types of strategies employed by macro hedge funds but they are universally known for taking a "top down" global approach to their investments, whether they are in stock markets, fixed-income securities, foreign exchange markets, or physical commodities. One macro hedge fund manager described the investment approach of macro funds as being "based on an understanding of economic cycles across a large number of countries (with particular focus on the Group of Seven nations); an assessment of where we are in these cycles; and how financial markets are likely to behave at various points in those cycles." More specifically, most macro funds purport to look for macroeconomic "imbalances" combined with changes in what might be termed "market psychology." They attempt to discern the types of events that might start a large trend or movement. When investing in foreign markets, many believe that it is important to keep track of what the local financial and industrial firms are doing as there is a feeling that when a trend is likely to change, the market psychology of the locals plays an important role in furthering the "new trend." The larger macro funds routinely send individuals to the countries to perform "on the ground" analysis.

In currency markets, the classic macro fund strategy is to examine countries that maintain a pegged exchange rate to the dollar but have little economic reason for using the dollar for the peg. Then there is an examination of the underlying macroeconomic fundamentals to see if they are consistent with an exchange rate valued at the peg. Some funds use rather detailed macroeconomic modeling techniques; others use less quantitative techniques, examining historical relationships among the various variables of interest.

As a large part of their macroeconomic assessment, hedge funds examine the safety and soundness of the banking sector and its connections to other parts of the financial sector. Excess liquidity and credit growth within the banking sector are often cited by funds as leading indicators of subsequent banking problems. Extensive use of (and dependence on) unhedged foreign-currency-denominated debt of banks and other industrial groups is also a tip-off for hedge funds. Of course, a pattern of high and rapid appreciation of various assets is also used as a signal of a financial sector awaiting a downturn. These items all point to the difficulty a country would have if it were to implement a high interest rate defense of a currency or otherwise tried to tighten monetary policy.

Another aspect to the typical macro hedge fund's strategy is an analysis of political risk and the probability that their strategy may, or may not, be implemented or that after the positions are in place, the fund may be unable to withdraw from the markets. Political risk is also part and parcel of investing in the Group of Seven countries, as political events can change the prospects of some types of trades quite substantially. For example, the country composition of the European Monetary Union is related to the behavior of various markets, perhaps with profound consequences for hedge funds. Of course, political risk continues to be a large part of sovereign risk analysis and many macro hedge funds who enter into sovereign bond markets do extensive analysis of the sovereign risk underlying these trades. The global setting in which the macro policies of various countries are decided is also of critical importance to assessing the likelihood of various macroeconomic developments that, in turn, affect the positions of hedge funds. The recent increase in global liquidity (the large number of countries pursuing relatively loose monetary policies) is thought, for instance, to be driving a number of developments in both developed and developing financial markets.

Strategy Determinants

Once a strategy looks appealing, the next step is to determine how the trade will be undertaken and the amount of leverage to be associated with it. Moreover, these two aspects of implementation are highly dependent and are critical for the returns eventually reaped by hedge funds. The decision is no different than the one an arbitrage-based fund makes except that leverage (which is synonymous with the method of financing the position) is of greater importance. Since macro hedge funds are less likely to use offsetting positions, as arbitrage funds do, they typically have positions with higher risk and the costs of financing the position will be commensurately higher.

Risk management by a large macro fund is often done on an integrated basis so that positions taken in one market can be related, through a correlation analysis, to those in other markets. Some funds perform four or five scenarios for each trading idea to explore what may happen when the assumptions underlying the trade are altered. As the technology for assessing large amounts of data improves, stress tests are becoming a common diagnostic technique. Further, there are often limits on the types of trades and the market exposures that can be taken by various traders within the fund based on a number of criteria, including the recent track record of the trader, the risk the trade would entail relative to the rest of the portfolio, and the liquidity in the market in which the trade is to be executed. It is important to remember that even the largest hedge funds have a limited number of strategies being implemented at any one time and risk management is, in most cases, much simpler than for a large money center bank. One of the largest macro hedge funds is still able to produce a report at the end of each day with a profit and loss statement and position report that fits on one letter-sized page.

After determining that the strategy fits within the portfolio of strategies and its risk characteristics are acceptable, the fund must determine the instrument. This decision is twofold: both the financing characteristics (leverage) must be meshed with the liquidity concerns. For large hedge funds, the liquidity of the instrument is often a constraint. Since they are frequently taking outright bets on the directions of various markets and are expecting to generate higher than normal returns from doing so, they need to lever themselves. This makes the established positions larger and can disturb markets when they are either initiating or terminating a trade. The “market impact cost” needs to be factored in when the trade is initiated and more often than not means that plain-vanilla or "primary" instruments are likely to be the least costly. Thus, large macro funds use spot or cash, forwards, futures, and swaps. Occasionally, they use plain-vanilla options and seldom use complex derivatives. Usually a macro hedge fund is sophisticated enough to piece together its own complex derivative if that kind of payout is desired. Forward and futures markets have leverage characteristics that are typically more appealing than spot transactions, whereby only a small proportion of the face value of the trade needs to be put up in advance.

In general, the leverage characteristics (margin requirements) of the instruments are determined in conjunction with the riskiness of the instrument and the riskiness of the hedge fund, as perceived by its counterparties. Thus, although leverage is higher for certain basic instruments—forwards greater than spot, for instance—the amount of leverage that can be obtained is generally lower for positions that entail higher risk. In some cases, the expected movement in the price of an instrument that would be necessary for a macro hedge fund to profit is not large enough relative to the costs of initiating the position to make it worthwhile. For instance, several hedge funds anticipated a fall in the Korean won but found that the costs of taking a position of a size that warranted the expected gains were too large to make the trade feasible.

Examples of Strategies

The examples below attempt to show how hedge funds use various instruments. Some of the examples could be correctly classified as arbitrage-related trades since some of the risk is transferred. However, since it is mostly macro hedge funds executing these trades they are included here. To the extent that hedge funds execute strategies in cash or spot markets, the outright purchase or sale of securities is relatively simple and is not discussed as a separate category, even though establishing short positions in some cash markets can be difficult.

Short currency strategy. A very typical strategy used by macro hedge fund is to sell a currency forward when the hedge fund expects it to depreciate. Since the forward market is an over-the-counter, interbank market, the hedge fund normally executes its sale through a bank or foreign exchange dealer. However, hedge funds could, in principle, find corporate counterparties (or even central bank counter-parties), thereby bypassing the bank intermediary.8 A bank will normally establish a credit line with the hedge fund, meaning that the bank will be willing to execute forward trades (and other instruments) of a certain size based on a credit assessment of the hedge fund. Typically, the hedge fund must post a certain amount of collateral with the bank, 5 percent is an often-quoted number, to initiate the position. While forward contracts usually do not require payment until maturity, most banks dealing with hedge funds (and other financial counterparties) require two-way collateral agreements in which a daily mark-to-market assessment of the position is done and any losses owed by the hedge fund are paid by a set time to the bank intermediary. The two-way collateral agreement also means that when the bank is on the losing side of the transaction it makes payments to the hedge fund. These strategies typically use forwards with horizons that fit those of the hedge fund's assessment of the likelihood for a depreciation. However, sometimes hedge funds use shorter-dated contracts and roll them over if the expected movement has not occurred by the time they expire. At an extreme, in five major currencies, there is a rolling spot contract traded at the Chicago Mercantile Exchange that permits a spot transaction to be rolled every day without making or taking delivery of the underlying currency.

In the Thai baht, hedge funds presumably acted through a number of counterparties to establish their short baht positions. Some hedge funds established positions early in 1997 and probably rolled them over prior to the actual decline in July. Others established their positions somewhat later and could execute trades in liquid one-month or three-month contracts without needing to roll them.

Put options strategies. Another way in which to express an opinion that a currency is likely to depreciate is to buy put options. A put option provides the buyer the right, but not the obligation, to sell at a particular price (the strike price) during the period leading up to expiration of the option. To obtain this right to sell, the option buyer must pay the seller a premium, the option's price, which reflects the probability that the currency will depreciate below the strike price (in dollars per foreign currency terms). The assessment of the probability that the option is valuable when it expires is determined mostly by the volatility of the currency's movements and the length of time to maturity. If the currency has been tightly managed and most participants expect it to remain within a narrow trading range, the volatility embedded in the price of the option will be low and consequently the option will be relatively cheap. Apparently, such was the case for options written on the Thai baht. A number of large banks allegedly sold put options on the baht to hedge funds. The hedge funds purchased the options as part of the overall strategy of shorting the baht. Put options had the advantage that implied volatility was abnormally low, making them cheap, although they had the disadvantage that the premium had to be paid up front. There are some variants to the strategy, however, such as selling puts at strike prices that are cheaper than the purchased put (further out-of-the-money). This limits the profits as the currency depreciates but also lowers the cost of the original put option.

Sovereign bond purchase. A hedge fund may decide that holding Brazilian government debt is advantageous based on an assessment of its economic fundamentals. The fund may decide that a Brady bond purchase is the best way to take advantage of such a decision. These Brady bonds may be purchased outright from a counterparty investment bank or the hedge fund may decide it does not want the risk of an interest rate move in the United States that would affect the price of the bonds, in which case the fund would short U.S. treasury bonds or notes of a similar duration against the Brady bonds. The short position could be maintained by borrowing the U.S. treasury bonds or notes by means of a reverse repurchase agreement. Alternatively, the hedge fund could simply take a short position in the U.S. Treasury futures contract with approximately the same maturity date and then tailor the number of futures contracts sold to obtain the correct duration or convexity characteristics to match the Brady bond. In this case, the hedge fund has obtained the credit risk to Brazil it desired without an outright interest rate exposure.

Credit derivatives strategies. More recently, hedge funds have found it convenient to enter into a credit derivative known as a total rate of return (TROR) swap. A total rate of return swap is structured so that the buyer swaps the "total return" on the reference asset for a regular floating rate payment (in general, based on the London interbank offered rate (LIBOR)). For example, the buyer agrees to pay the total return on an emerging market Brady bond, consisting of all contractual payments as well as any appreciation in the market value of the bond; the seller agrees to pay the buyer LIBOR plus a spread and any depreciation in the value of the Brady bond. The TROR swap protects the buyer against a deterioration of credit quality, which can occur even without a default. A hedge fund may be either a buyer or a seller depending on the credit risk they would like to take on.

A more recently developed credit derivative is the credit spread option. This option provides a payout to the buyer when the spread on two underlying assets exceeds a predetermined level. The buyer pays a premium for such protection and the seller provides a payment based on the spread. Since the credit risk of many fixed-income securities is often measured as a spread over a comparable maturity "risk-free" security, this derivative product is highly sensitive to the market's assessment of credit risk in these securities and is especially tailored to holders of emerging market debt and other high-yielding debt instruments.

Continue reading here.

Seven high-growth companies with positive free cash flow (FCF) in the U.S. and abroad (from Ryan Reeves via X)...

I can only find 2 U.S. companies that are set to grow at least 30% over the next 3 years according to analyst estimates and have positive FCF ex-SBC over the past year.

1. Celsius

2. Symbotic

And then there are a handful of international ones:

1. dLocal

2. Shelly Group

3. Li Auto

4. Kempower

5. Xvivo

Just a couple more things:

- Snowflake is actually the 3rd U.S. company if we do just FCF vs. FCF ex-SBC.
- Walmart accounted for 88% of Symbotic's revenue.

Here's a list of little-known family-owned (or influenced) companies (from Bargain Stocks Radar)...

We think family influenced businesses are an interesting niche part of the public equity markets.

If you are a coffee-can type investor this area is a great place to look for long term compounders.

There has been many studies done that highlight the longer term positive performance of family operated, or influenced, public companies.

Everyone is familiar with companies such as LVMH and Heineken who have family members controlling the company or have an influential seat on the board.

However, we wanted to find smaller less well known companies. Perhaps it's a small cap yogurt manufacturer from Greece or an Australian auto-parts distributor.

After much searching we have compiled a list of 100 family influenced public companies who are less well known to the general investing public.

I'm sure we have missed many but this is a good list to start researching.

We hope you enjoy going through the list. If you know of any companies we have missed please comment below, thanks in advance.

You can download the list here.

Share buybacks are becoming increasingly popular in Japan (from Jamie Halse via X)...

Sixty-three companies (see list below) are currently buying back more than 5% of shares outstanding - 17 of those more than 10%. 121 companies are buying back more than 3%.

Tick	Name	TSE Secto	Ratio share:	Amount to be repurchased JPY
4212	Sekisui Jushi	Chemicals	19.6%	20,400,000,000
9837	Morito	Wholesale	18.7%	600,000,000
7371	Zenken	Services	16.7%	100,000,000
6088	Sigmaxyz HD	Services	16.2%	1,200,000,000
8418	Yamaguchi FG	Banks	15.3%	10,000,000,000
4975	JCU	Chemicals	15.2%	1,000,000,000
6486	Eagle Industry	Machinery	15.1%	6,600,000,000
8002	Marubeni	Wholesale	15.1%	20,000,000,000
5076	Infroneer HD	Construction	14.3%	10,000,000,000
2371	Kakaku.com	Services	13.3%	6,000,000,000
3558	Jade G	Retail	12.6%	1,000,000,000
5011	Nichireki	Oil/Coal Prod.	12.2%	3,000,000,000
4626	Taiyo HD	Chemicals	12.2%	3,000,000,000
6706	DKK	Elec. App.	10.7%	2,500,000,000
2467	VLC HD	Services	10.5%	70,000,000
6334	Meiji Machine	Machinery	10.1%	100,000,000
8129	Toho HD	Wholesale	10.0%	6,000,000,000
7419	Nojima	Retail	9.7%	3,000,000,000
5905	Nihon Seikan K K	Metal Prod.	9.6%	100,000,000
6841	Yokogawa Electri	Elec. App.	9.3%	20,000,000,000
9628	San HD	Services	9.3%	350,000,000
1417	Mirait One	Construction	9.1%	5,000,000,000
8023	Daiko Denshi Ts	Info/Comm.	8.2%	210,000,000
3659	Nexon	Info/Comm.	8.0%	30,000,000,000
5929	Sanwa HD	Metal Prod.	7.8%	5,000,000,000
7911	TOPPAN HD	Other Prod.	7.6%	40,000,000,000
2733	Arata	Wholesale	7.2%	3,000,000,000
3591	Wacoal HD	Text/Apparel	7.1%	10,000,000,000
6134	FUJI	Machinery	7.0%	10,000,000,000
1518	Mitsui Matsushin	Mining	6.8%	3,000,000,000
6155	Takamatsu Mach	Machinery	6.6%	100,000,000
8511	Japan Securities	Other Financia	6.4%	3,300,000,000
7912	Dai Nippon Printi	Other Prod.	6.3%	100,000,000,000
6184	Kamakura Shinsl	Services	6.3%	500,000,000
9301	Mitsubishi Logisti	Warehouse/Tr	6.2%	10,000,000,000
6806	Hirose Electric	Elec. App.	6.2%	10,000,000,000
6925	Ushio	Elec. App.	6.1%	30,000,000,000
9434	Softbank	Info/Comm.	6.1%	100,000,000,000
4671	Falco HD	Services	6.0%	1,200,000,000
7459	Medipal HD	Wholesale	6.0%	10,000,000,000
1662	Japan Petroleum	Mining	6.0%	20,000,000,000
5658	Nichia Steel Wor	Iron/Steel	6.0%	210,000,000
8058	Mitsubishi Corp	Wholesale	5.9%	300,000,000,000
8358	Suruga Bank	Banks	5.9%	22,000,000,000
9948	Arcs	Retail	5.9%	5,500,000,000
8031	Mitsui & Co	Wholesale	5.8%	50,000,000,000
4041	Nippon Soda	Chemicals	5.8%	2,000,000,000
6460	Sega Sammy HD	Machinery	5.8%	10,000,000,000
6178	Japan Post HD	Services	5.8%	300,000,000,000
8359	Hachijuni Bank	Banks	5.8%	10,000,000,000
2108	Nippon Beet Sug	Food	5.8%	1,000,000,000
7989	Tachikawa	Metal Prod.	5.7%	700,000,000
6676	Melco HD	Elec. App.	5.6%	3,500,000,000
6199	Seraku	Services	5.5%	400,000,000
6135	Makino Milling M	Machinery	5.4%	1,000,000,000
6200	Insource	Services	5.4%	300,000,000
1944	Kinden	Construction	5.4%	6,000,000,000
4464	Soft99	Chemicals	5.3%	150,000,000
8012	Nagase	Wholesale	5.1%	8,000,000,000
9076	Seino HD	Land Trans.	5.0%	30,000,000,000
4826	CIJ	Info/Comm.	5.0%	300,000,000
1803	Shimizu	Construction	5.0%	20,000,000,000
5262	Nippon Hume	Glass/Ceramic	5.0%	200,000,000

Brazilian stocks may be on the verge of a massive long-term breakout (from Otavio Costa via X)...

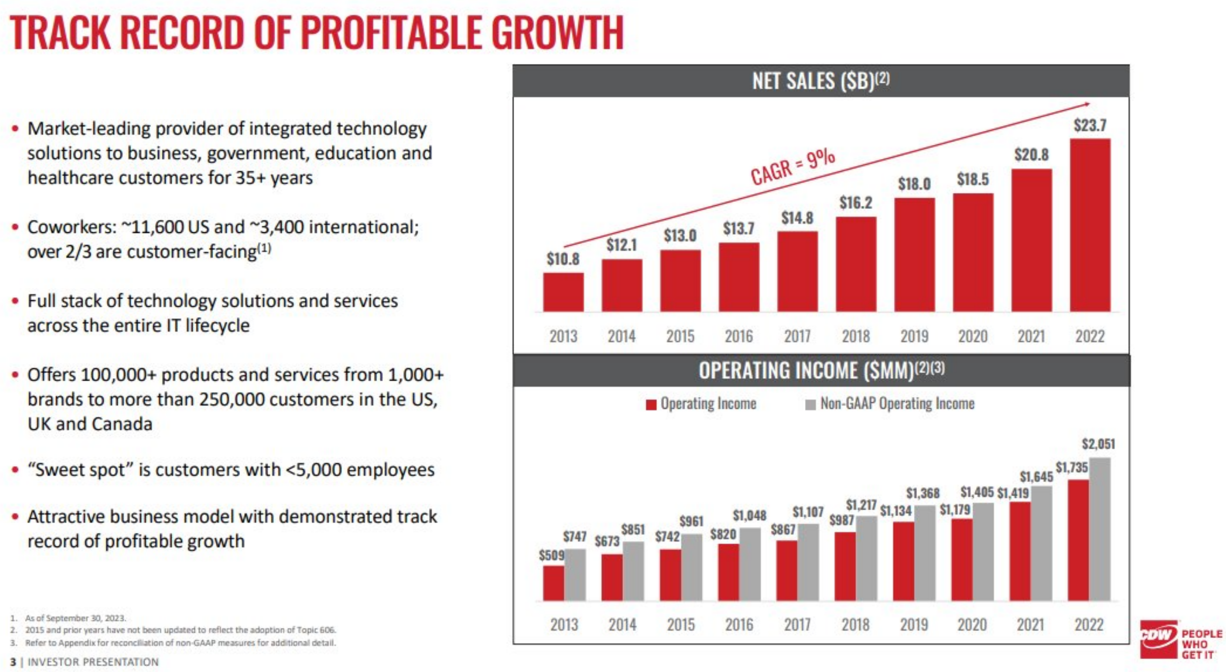
This might be one of the cleanest technical breakouts I've seen in a long time.

Brazilian equities are reviving from deeply distressed valuations, standing out as one of the few segments of the market that remain genuinely undervalued with a strong macro case propelled by the country's resource-rich economy.

Here's another "boring" business with a long history of profitable growth (from Conch Shell Capital via X)...

$CDW has been so consistent over time. Stock is up around 150% in the past 5 years.

Always surprises me it doesn't get talked about more - I've generally found "boring" business models like this just silently outperform.



Apple is looking increasingly risky at today's lofty valuation (from *Barron's*)...

Apple shares have had a historic year. The stock has rallied more than 50% in 2023 and recently closed at a record high. In terms of wealth creation, it has been the single best year for any company ever—Apple's market value grew by $1 trillion.

But the unprecedented rally comes amid one of the company's most disappointing stretches. In each of the past four quarters, Apple's sales have declined from the prior year. The slide is likely to continue in the current December quarter. Apple's most important hardware products – the iPhone, the Mac, and the iPad – still generate huge sales, but their growth is all but gone.

Meanwhile, Apple hasn't had a hit new product since its AirPods, the pioneering wireless earbuds, launched in 2016. The backdrop makes the coming launch of the Apple Vision Pro, the company's mixed-reality headset, all the more important. But success is far from certain: The promise of virtual and augmented reality has lured many entrants, including Meta Platforms and Microsoft, but there are few success stories.

This is the Apple paradox: The company's stock trades near record highs, with a market value no other company has ever attained. But its growth is gone—sales fell 3% in the latest fiscal year, and they're forecast to be up less than 4% in the current fiscal year, which ends next September—and there's no clear plan for getting it restarted.

It's possible that Apple could stick to its current script and still find a way back to top-line growth. It requires some optimistic assumptions about the upgrade rate for iPhones, an ever-rising sales price for its devices, and continued low-double-digit growth for its portfolio of services, including the App Store, Apple Music, and iCloud.

But Apple's legacy is innovation, not incremental feature creep. Apple fans—and its shareholders—have been trained to expect products that are insanely great, that think different, or that "put a dent in the universe," as co-founder Steve Jobs once said.

Denting the universe is hard, especially while preserving the strength of its current lineup. For the September 2024 fiscal year, Wall Street analysts expect Apple to generate $100 billion in net income on $397 billion in sales.

It all starts with the iPhone. Now 16 years old, the iPhone generated $200 billion in revenue in the September 2023 fiscal year—roughly the size of Microsoft's entire revenue base. On its own, the iPhone business would rank among the 15 largest U.S. companies.

But iPhone sales declined 2% in the September 2023 fiscal year—and recent hardware updates have been modest. The smartphone market is now mature. IDG sees global smartphone sales growing just 1.4% a year through 2027. The iPhone also faces intensifying competition in China – Apple's most important non-U.S. market—from Huawei Technologies and other local upstarts.

The growthiest part of the business is Apple's services portfolio, which had fiscal 2023 revenue of $85 billion, up 9%. Were it an independent company, Apple's services arm would rank in the top 50 of the Fortune 500.

There's a lot in that bucket – advertising, music, photos, financial services, podcasts, games, Apple Pay, Apple Care, and search revenue from Google, among other things. As the company has added to the mix, the company has raised prices and grown revenue. But ultimately the best way to grow services is to sell more iPhones, iPads, and Macs, since most of those services are consumed on Apple devices.

Then there's the catchall "Wearables, Home and Accessories" segment, which includes AirPods, Apple Watch, and HomePods. Revenue was down 3% in the latest year to $40 billion, about equal to Best Buy's annual sales. A current pause in watch sales due to a patent dispute won't help results in that unit.

As with the services business, Apple's hardware products largely play off the vast installed base of iPhones and other devices – there aren't a lot of Android phone owners with an Apple Watch. In 2024, Apple will add to the wearables collection with the debut of its Vision Pro headset, scheduled to launch in early 2024 at the gaudy price of $3,499. Near-term expectations are modest.

Apple's roots are in computing – the Mac turns 40 in January. (Remember the 1984 Super Bowl ad?) It isn't the happiest of anniversaries – Macs had a rotten fiscal 2023, with revenue down 27% to $29 billion. The iPad – now 14 years old – is almost the same size as the Mac, with fiscal 2023 sales of $28 billion, down 3%.

It's worth noting that Wall Street seems generally unconcerned with Apple's lack of growth. At least for now. Of the 47 Apple sell-side analysts tracked by FactSet, just three rate the stock a Sell or its equivalent.

Continue reading here (subscription may be required).

Nancy Pelosi appears to be extremely bullish on Nvidia (from TrendSpider via X)...

JUST IN: Nancy Pelosi bought $5M in $NVDA call options with a strike price of $120 that expire in December 2024. Another semiconductor bill incoming?

Amazon is planning to get into the autos business (from *The Wall Street Journal*)...

Willie Hall loves to browse and buy cars online, but he wants more options. Soon, he may turn to Amazon.com.

"I'm already a Prime member," said Hall, who lives in Colorado and bought a used Fiat 500 Abarth on Carvana in 2021. "I've been with Amazon for God knows how long and know the way they operate."

Amazon is eager to see just how many Willie Halls there are in the U.S. The company last month said shoppers next year will be able to browse, finance and complete a purchase of Hyundai vehicles on Amazon. Shoppers will only have to visit a dealership to pick up their car; the company is also working on delivering the vehicles.

Car sales represent Amazon's next bet in e-commerce dominance and come after the COVID-19 pandemic made online car purchases more popular. Amazon executives want to make buying vehicles through its website as simple as purchasing toilet paper or dog food, and the company is looking to strike broad partnerships with carmakers.

The company is set to face several challenges in expanding the program beyond a pilot phase for employees starting early next year: One is dealerships, which remain at the center of most new-car sales and depend on service revenue for profit incentives. A second will be trying to get customers who visit its website mainly for lower-priced items to turn to the platform for one of the biggest purchases of their lives. Amazon also will have to navigate different government regulations.

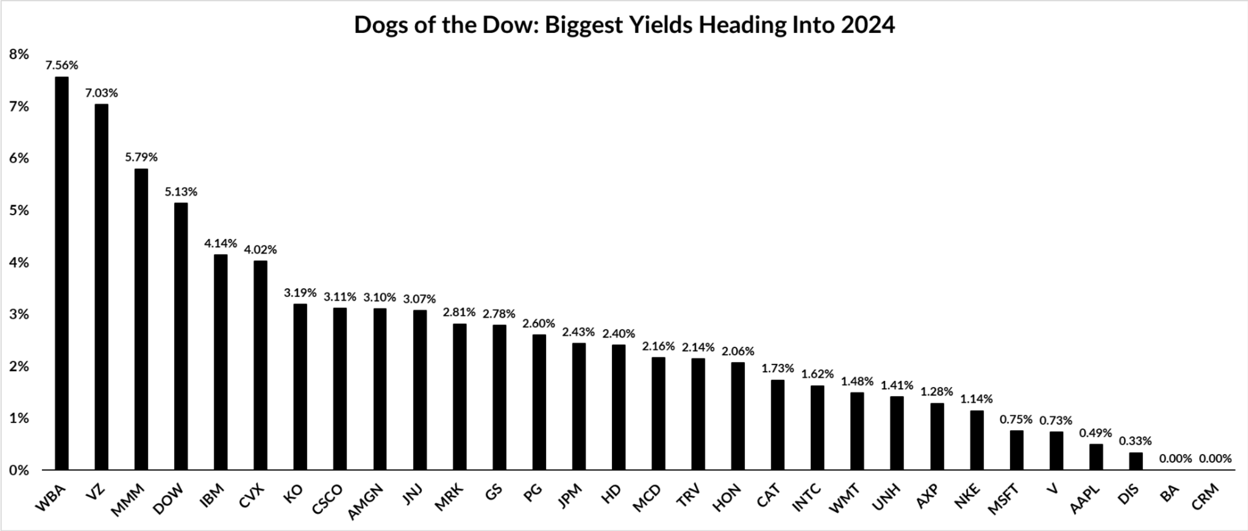
"Customers tell us it's really hard to buy a car," Fan Jin, Amazon's director of vehicle sales, said in an interview. Vehicle-buying software is fragmented, with dealers using a range of software providers. Varying regulations across states also make it difficult. "It's a process that we've heard time and again could use improvement, and we have an opportunity to go and prove it," she said.

When the new service launches later next year, Amazon said shoppers will be able to complete every step of the car-buying process through its website. Only new Hyundai vehicles will be available at the start. Consumers will have different financing options, but the company said it is still working through details. Eventually, Amazon wants to expand to trade-in vehicles and used cars.

Continue reading here (subscription may be required).

Buying the highest-yielding stocks in the Dow Jones Industrial Average each year – the "Dogs of the Dow" – has often been a market-beating strategy (from Mike Zaccardi, CFA, CMT via X)...

Dogs of the Dow worth a look?



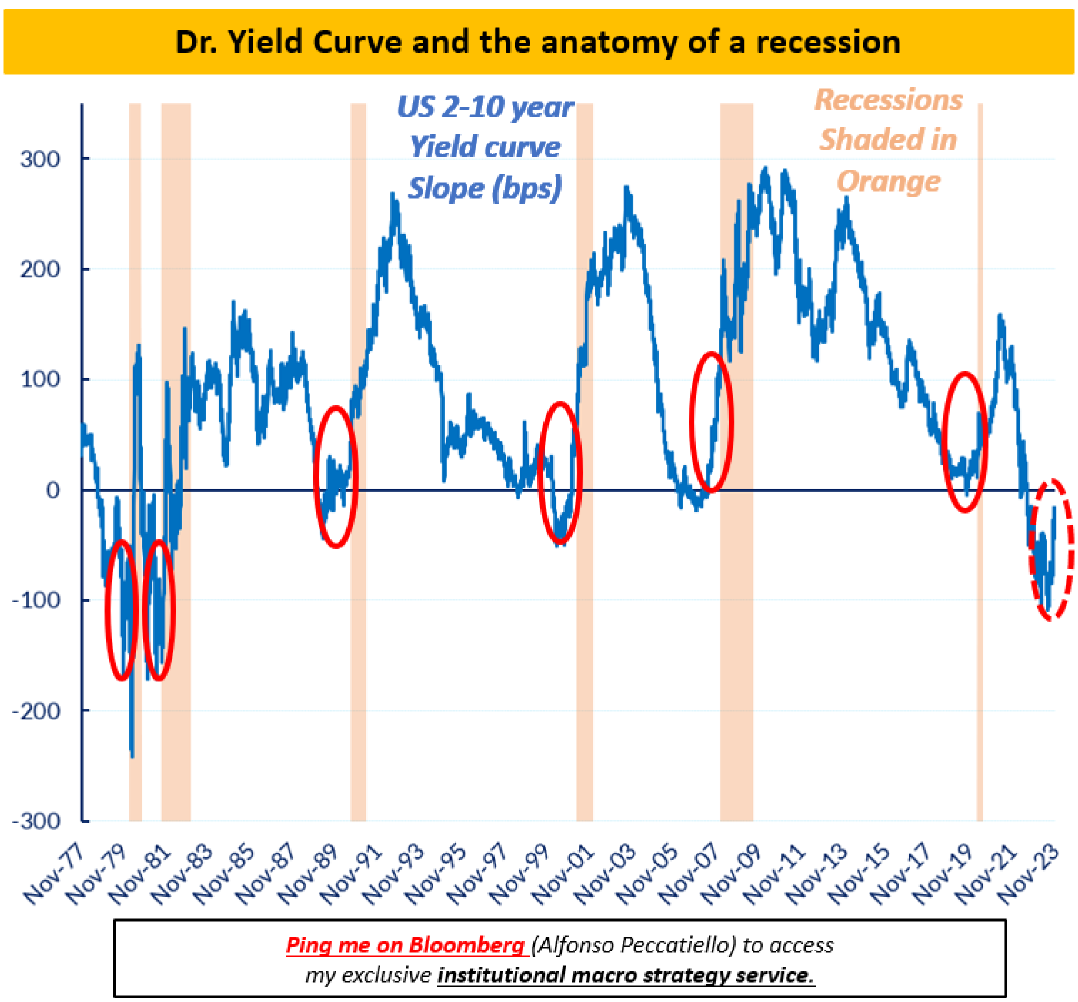
SOVEREIGN/GOVERNMENT BONDS AND CREDIT

Here's a primer on Treasury yield curve inversions (from Alf via X)...

History says that yield-curve inversions lead us into recessions.

The chart below is pretty telling: going back 50 years the track record is pretty much intact.

But why? What are the exact mechanics at play here?



Spotting empirical market behavior is a common trait of good investors, but the best macro minds out there can go a step further: they can deeply understand the very mechanics behind market behaviors.

So let's try to understand why curve inversions lead us into recessions.

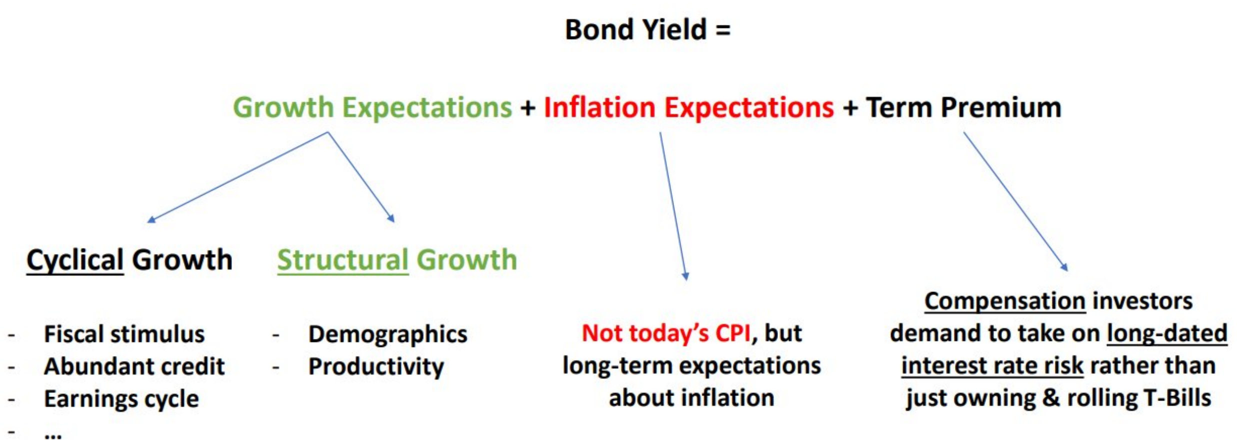
Step 1: The Fed starts hiking rates fast

2-year yields immediately move higher as they reflect the new Fed stance and future hikes that are coming.

Longer down the curve, the story is different as 10-year interest rates are driven by growth and inflation expectations (+ term premium).

There, investors start extrapolating that all these hikes will hurt future growth and inflation: 10-year yields move higher but much more slowly.

The curve inverts.

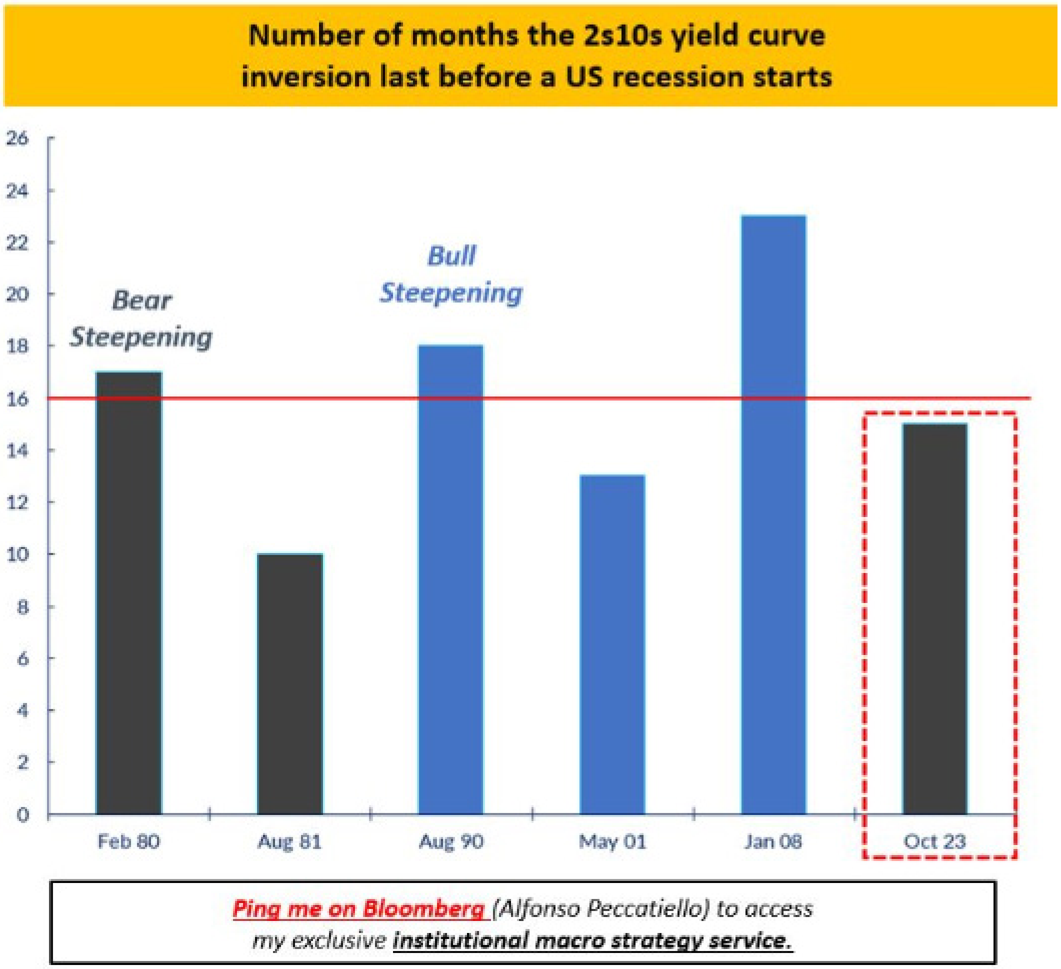


Step 2. The Fed stays the course with their hiking cycle

Even if growth starts slowing down the Fed won't bail in as they must bring inflation back to 2%: more hikes come in, and as investors face a weaker economy the curve inverts even further.

Step 3. Companies and households are under pressure

The usual macro lags last between 10-27 months: that's how long it takes for the initial curve inversion to feed into actual pain for the private sector.



The longer credit conditions are tight while the economy slows down, the more companies and households will be forced to refinance at prohibitive conditions right when their earnings stream are dwindling.

Step 4. Cut costs and investments

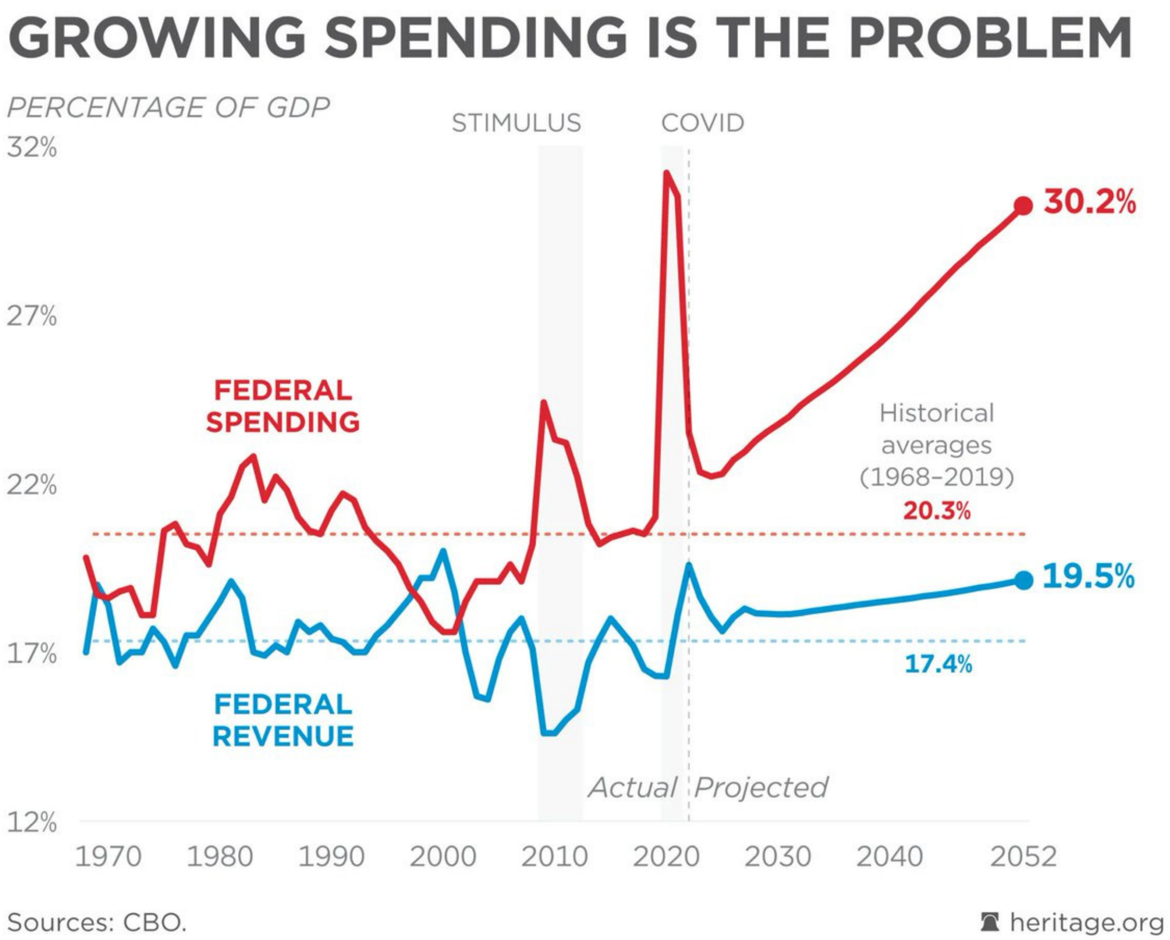
Forced to allocate a larger portion of their budget (salary, earnings etc) into higher debt servicing bills, households start spending less and companies are forced to cut labor.

Now a vicious loop unfolds: less jobs, less spending, less earnings, less jobs...

Step 5 is here: Recession

There you go: now the mechanics by which an initial yield curve inversion leads (with variable time lags) into a recession should be clear.

Don't believe the government's lies: Soaring deficits have nothing to do with taxes (from the Heritage Foundation via X)...



The Fed's recent pivot may have little to do with declining inflation (from Luke Gromen via X)...

The 2023 spike [in Treasury debt issuance] shown requires rate cuts, a weaker USD, & higher asset prices, like the 2020 spike did.

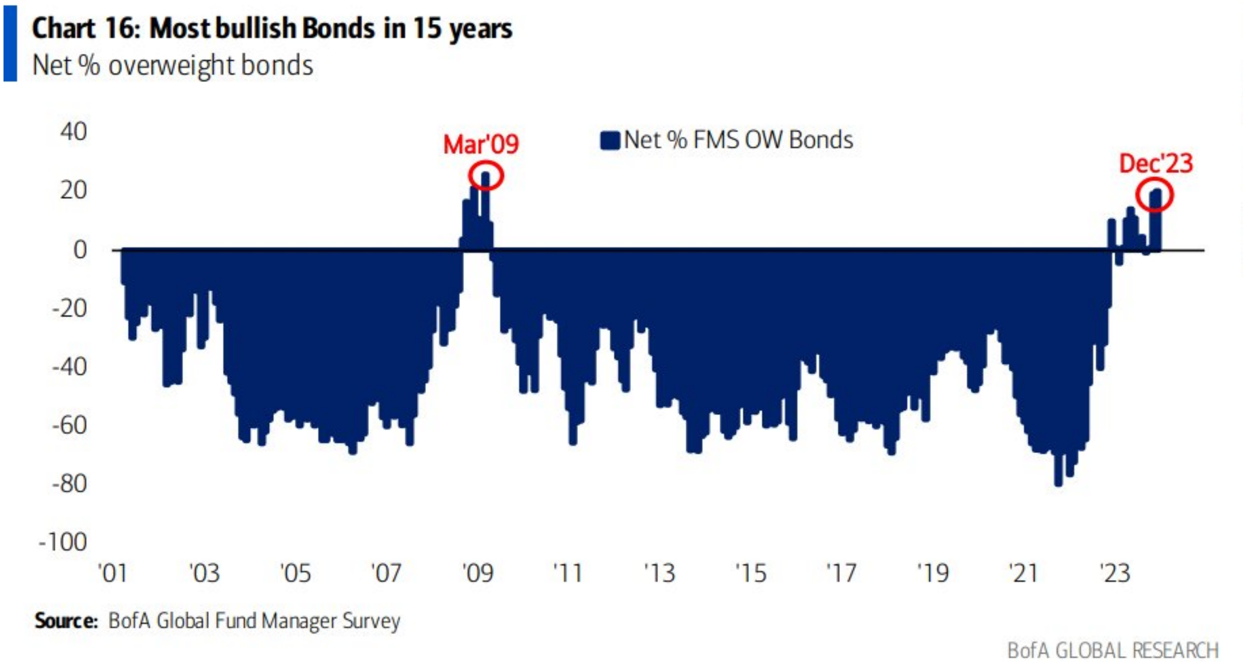
If [the Fed] doesn't want to cut rates, the other 2 options are:

a) Cut Entitlement & DoD spending by 30-35%, immediately & permanently

b) Resume Aug-Sep's 10y UST rate spiral [higher].

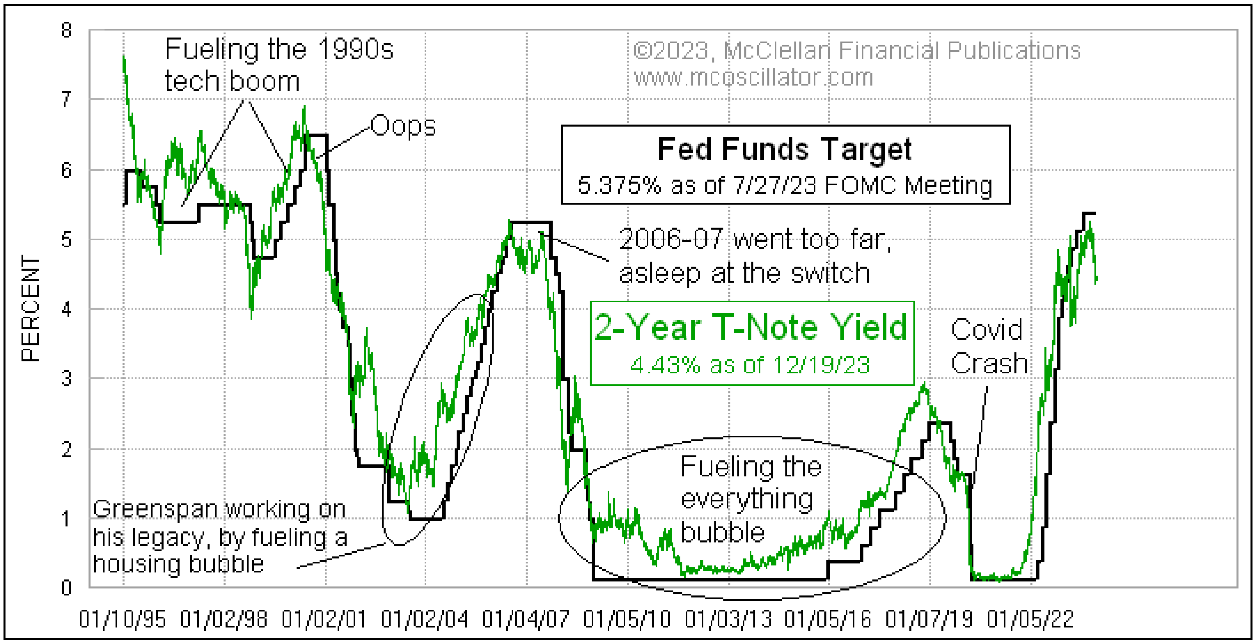
Global fund managers are extremely bullish on bonds today (from Gunjan Banerji via X)...

Investors haven't been this bullish on bonds in 15 years – according to the BofA fund manager survey.

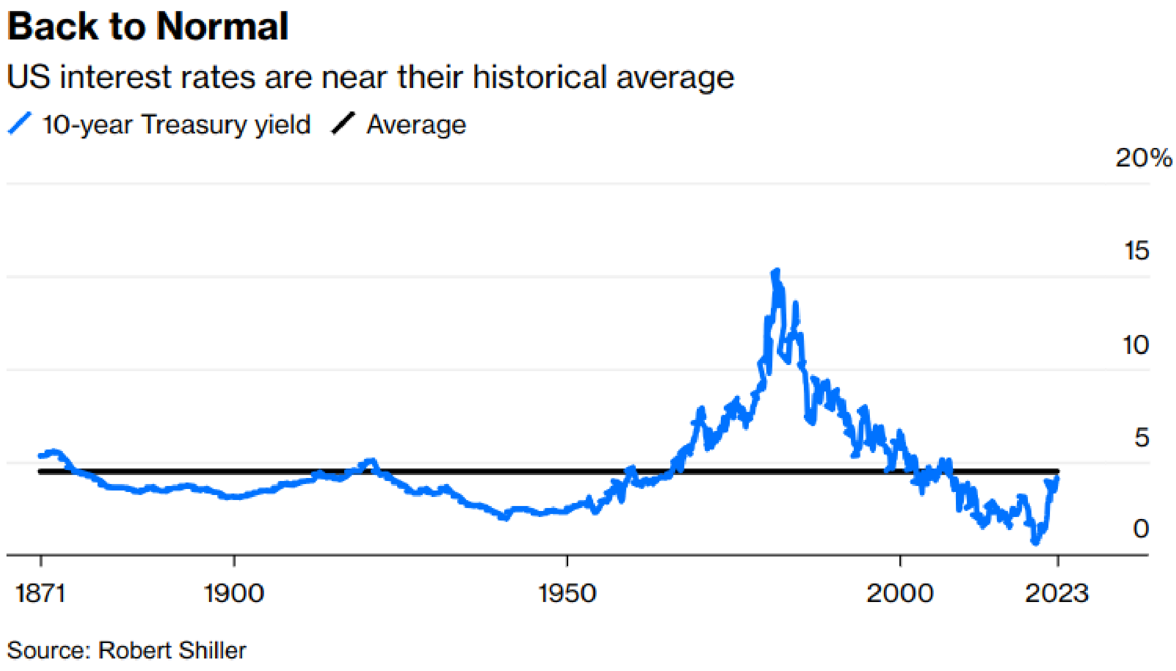


The two-year Treasury yield suggests the Fed may have already "over-tightened" (from Tom McClellan via X)...

The Fed Funds rate is now almost a full point above the 2-year yield, reflecting an immense amount of overly tight monetary policy from the Fed. They were slow to respond just like this in 2001 and 2007, and each time it caused big problems.



The dramatic increase in long-term rates over the past couple years has only brought yields back to their long-term average (from Markets & Mayhem via X)...



CORPORATE BONDS AND CREDIT

Higher interest rates have not yet increased borrowing costs for most companies (from Jim Bianco via X)...

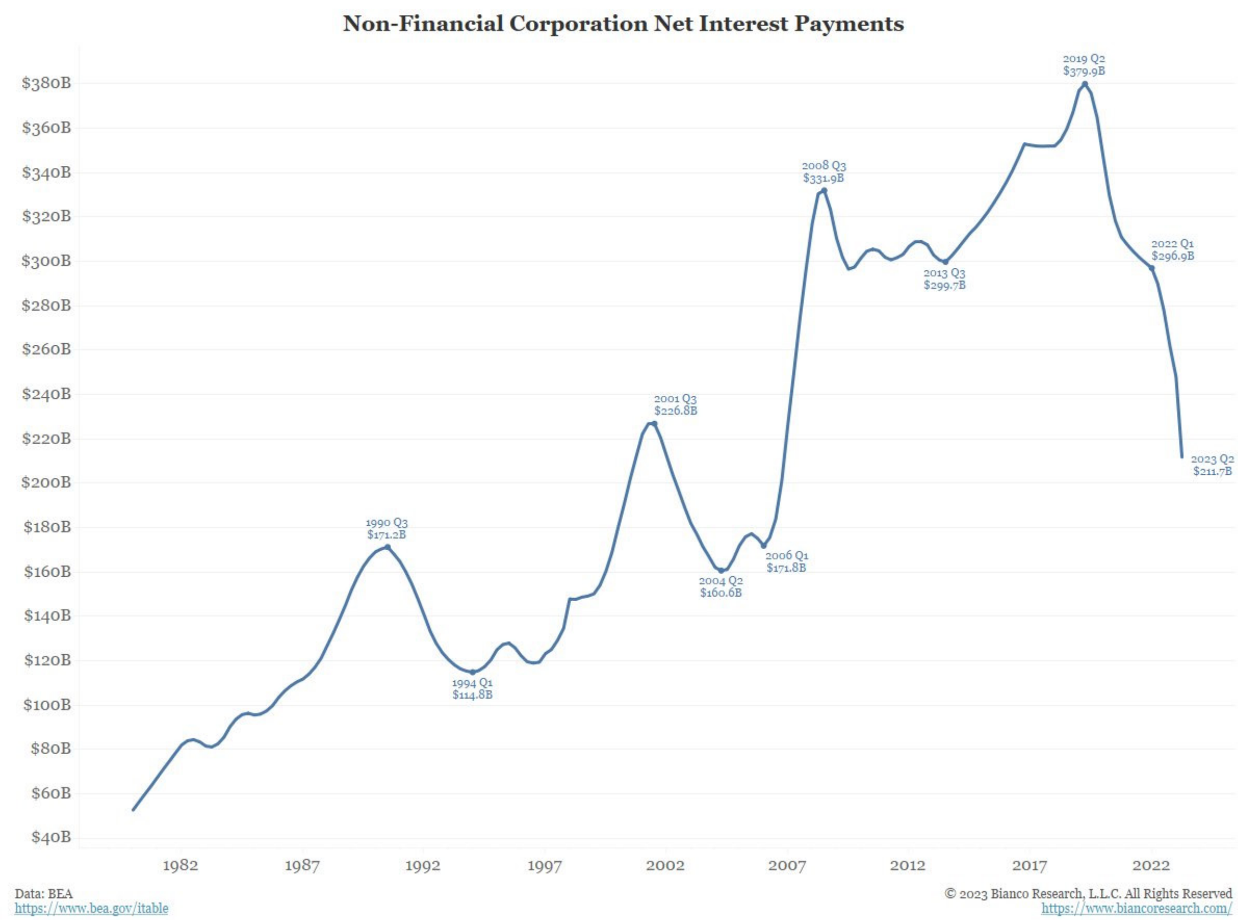
Rising rates [have caused] the government to incur higher interest costs.

This HAS NOT been the case for corporations.

Companies also have interest INCOME, while the Govt does not. This chart shows that company interest INCOME is rising faster than interest EXPENSES.

They are BETTER off because rates are moving higher.

(Net Interest = Interest Expense - Interest Income)

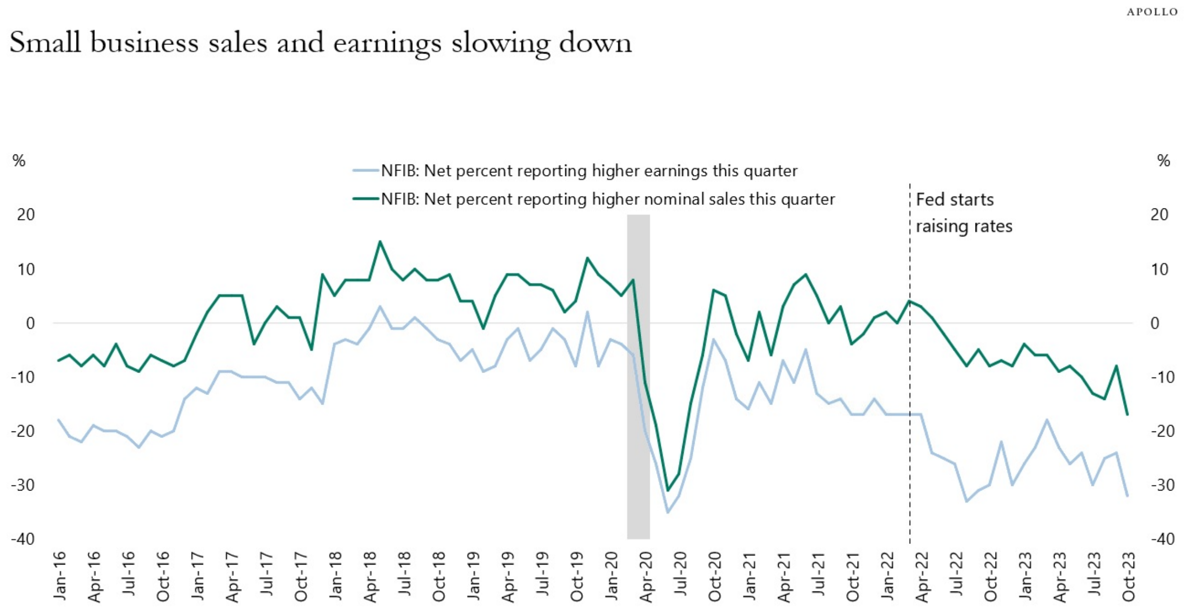


However, higher costs of capital are weighing on smaller, weaker companies (from The Daily Spark)...

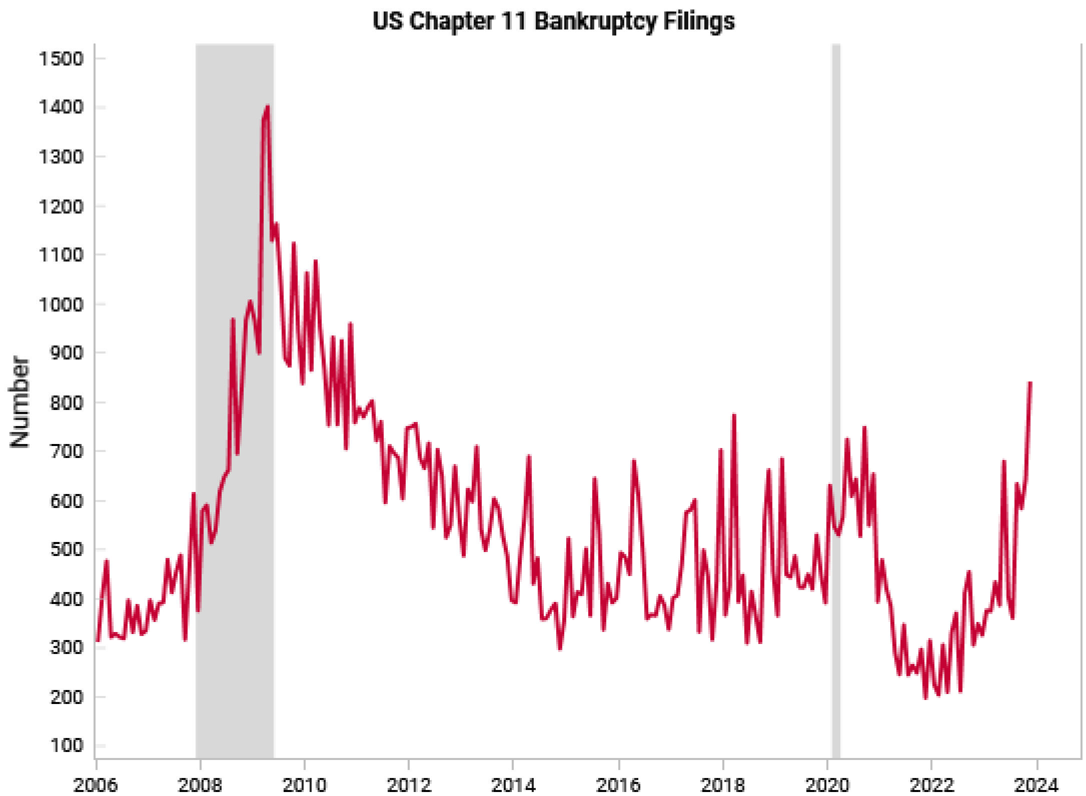
Since the Fed started raising rates, small businesses have seen a trend decline in earnings and sales, see chart below.

This is what the textbook would have predicted. Higher costs of capital weigh on small-cap companies with high leverage, low coverage ratios, and weak or no earnings.

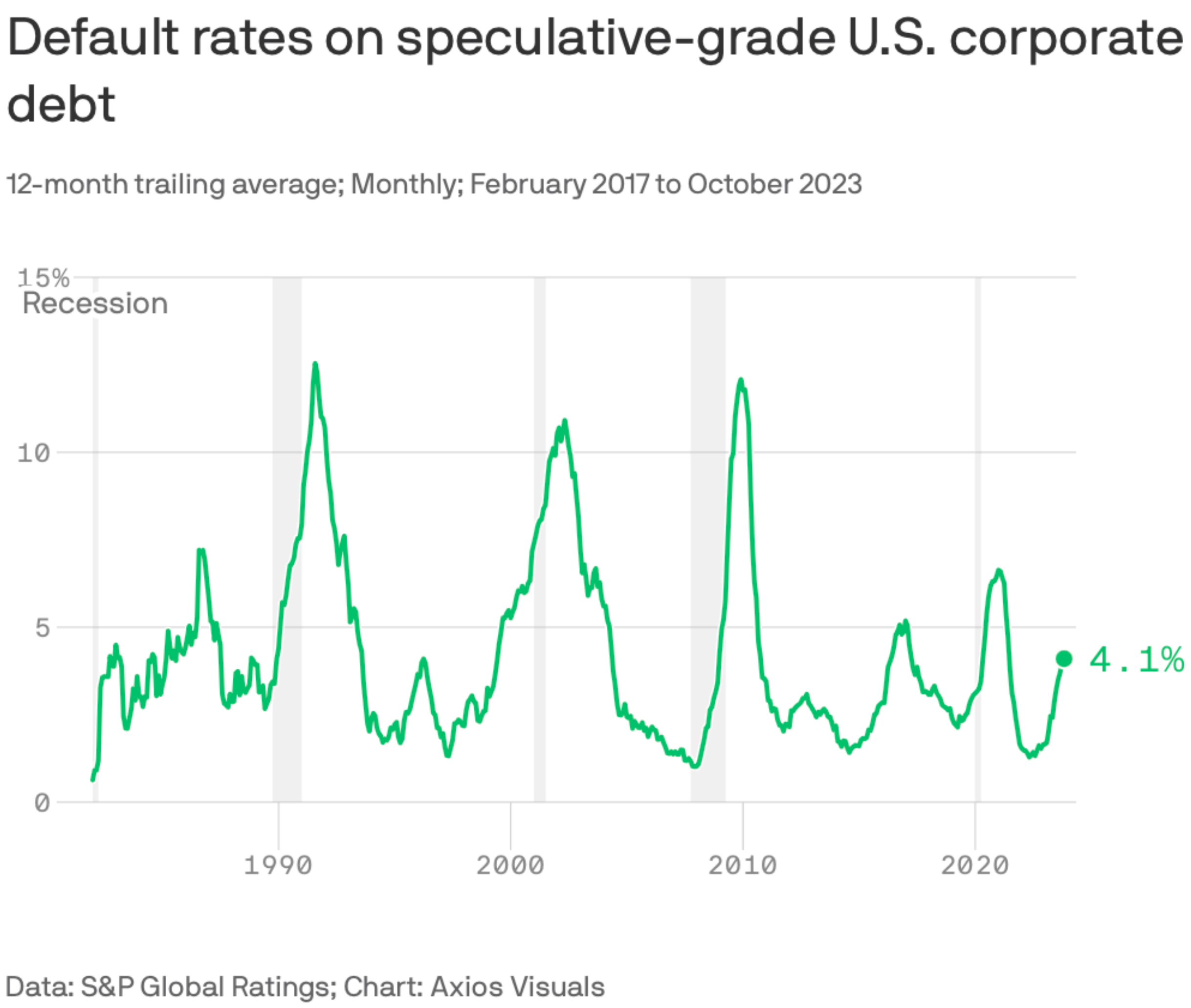
With the Fed keeping rates high at least until the middle of 2024, we should expect these trends to continue.



Chapter 11 bankruptcies are at a new post-Great Financial Crisis peak (**from Variant Perception via X**)...



Corporate default rates also continue to quietly tick higher ([from Axios](#))...



U.S. companies' debt default rates have been unusually low since 2021, but that's changing now.

What's happening: The default rate has been climbing all year, and in November it reached its historical average of 4.1%, according to S&P Global Ratings.

Why it matters: The Fed's interest rate hikes are squeezing company balance sheets. Defaults are going up as a growing number of companies can't make their interest payments, or can't afford to refinance their debt.

- And even if the Fed cuts interest rates a few times next year, they'll still be pretty high — so defaults could keep on rising.

State of play: Defaults often go hand-in-hand with bankruptcy — but defaults are a broader measure.

- This year, 43 of the 89 U.S. defaults didn't involve bankruptcies; they were what's known as "distressed exchanges."

In a distressed exchange, the lender agrees to a deal in which it won't get paid back in full, but it gets something in return, like a higher priority spot in the company's debt structure.

- The point of these types of deals is to limit the downside for the lender, while helping to create a more sustainable debt structure for the company.
- **For example:** Carvana, creator of the famed "car vending machines," did one such deal in July, which helped it avoid a full-blown bankruptcy.

Of note: The default data includes all the companies with credit ratings from S&P — that means it's mainly larger companies with bonds or loans that trade in the market. It doesn't include companies that have borrowed in the growing private debt sector.

The expected Fed pivot is unlikely to stop the coming credit-default cycle (from steph pomboy via X)...

Lost in all the excitement about a pivot is the reality that a 100bp or even 200bp cut in FED funds rate accomplishes nothing in terms of staving off the impending default cycle.

Having 4% junk rated debt roll at 7.5% (instead of 8.7%) isn't going to help. The FED would have to slash rates massively for it to make a difference.

LCD **Leveraged Loans**
@lcdnews

Maturity wall update: The amount of #leveragedloan debt due in the next 2 years is larger than ever, and roughly half of that are riskier, B-minus rated credits (better-quality borrowers have refinanced already) buff.ly/3RaVZZ0 @Kakourisr @PitchBook

CONSUMER CREDIT

Consumers are increasingly turning to Buy Now Pay Later (BNPL) to finance their spending ([from The Kobeissi Letter via X](#))...

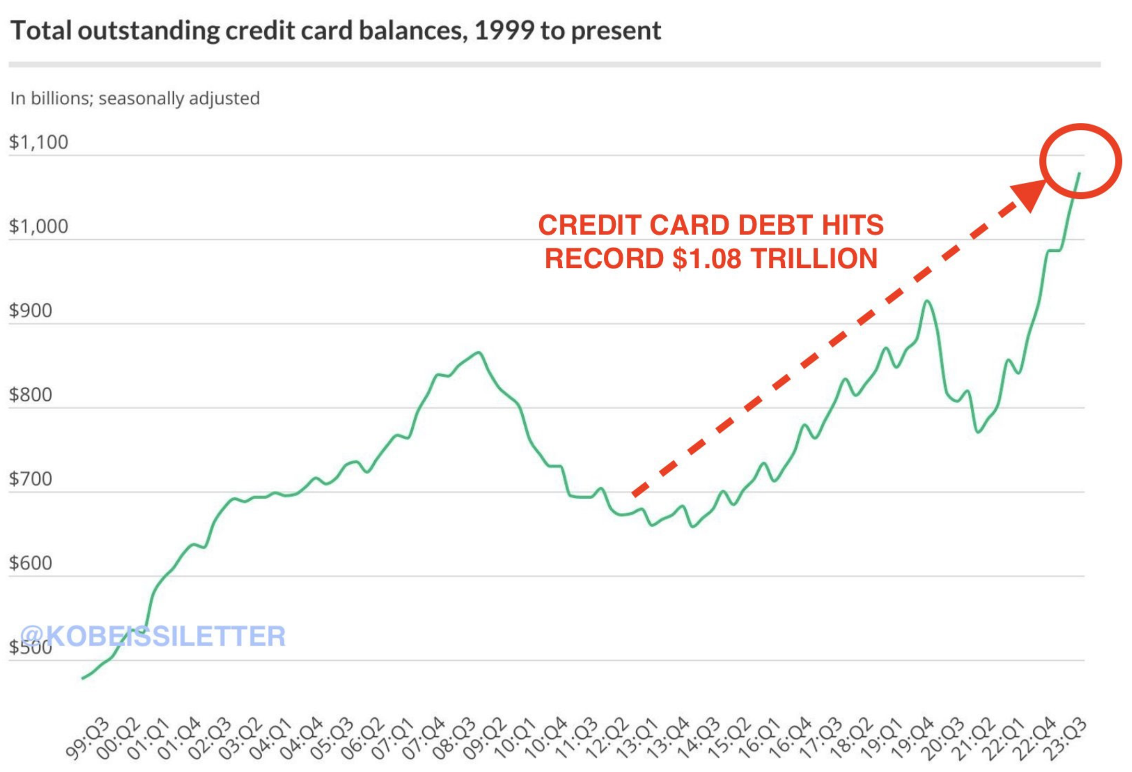
BREAKING: Buy Now Pay Later spending soars 20% compared to last year on Black Friday.

It's also expected to jump 19% on Cyber Monday to a record $782 million.

As excess savings in the US have gone from $2 trillion to zero, Americans are relying on debt more than ever.

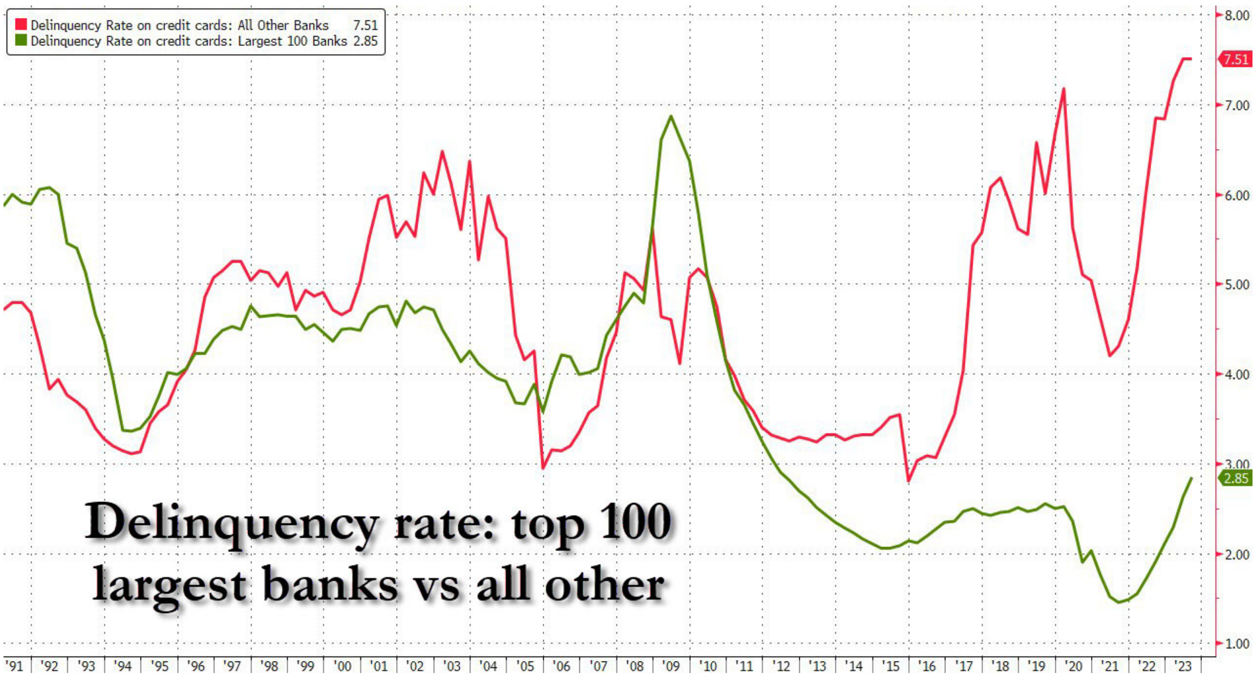
In other words, "deals" that are 20% off are being financed with credit card debt that has a 30% interest rate.

How can this end well?



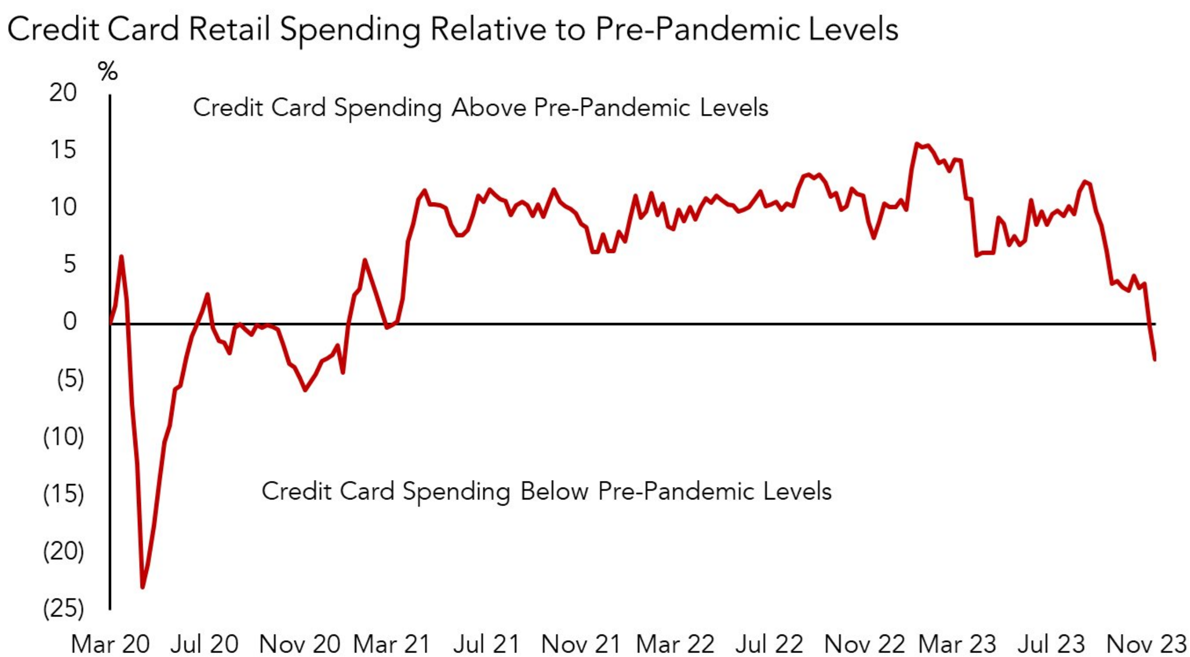
Credit card delinquencies are soaring – particularly at smaller banks ([from ZeroHedge via X](#))...

Broad bull markets take place when delinquency rates are falling. Keeping an eye on this data among others to see the end of this bifurcation-nation market. Until then, high-quality fundamentals' leadership likely persists. #macro #hope



Meanwhile new credit card spending is falling sharply (from Game of Trades via X)...

Credit card spending has collapsed. And has officially entered contraction territory.



Dates: March 2020 Through November 14th 2023.
Source: Bureau of Economic Analysis, Game of Trades.
4-week moving average. Payment cards include credit, debit and gift cards. Includes food services; excludes gas stations. Sales are adjusted for day of the week, month, holidays and broad annual trends. The data could be interpreted as changes in spending relative to expected levels prior to the pandemic.

Student loan repayments started in October, yet nearly 40% of borrowers still aren't paying (from *The New York Times*)...

Just over half of the millions of borrowers who received their first federal student loan bills in years in October – after the pandemic freeze ended – have paid the bills, the Education Department said on Friday.

Forty-three million borrowers collectively owe the government $1.6 trillion in student loan debt. In March 2020, as the coronavirus pandemic roiled the nation's economy, President Donald J. Trump's administration imposed a freeze on collections as an emergency relief measure. The moratorium was extended nine times by Congress, Mr. Trump and his successor, President Biden – until this fall, when it finally ended.

Officials had long warned that getting borrowers accustomed to paying again after such a long break would be a rocky process, especially after the Supreme Court in June overturned Mr. Biden's $400 billion plan to forgive up to $20,000 in debt per borrower. Tens of millions of people would have benefited from that relief.

Instead, 22 million people had to make their first payment in years in October as the government restarted its collection machinery. Sixty percent of them paid the bill by mid-November, according to James Kvaal, the Education Department's under secretary. (Borrowers who are still in school or recently left do not yet owe on their debts. Also, some borrowers' payment deadlines were extended because of loan servicing errors.)

That leaves nearly nine million borrowers who had payments due but have not yet made them. Many people "will need more time," Mr. Kvaal said Friday in a written statement. "Some are confused or overwhelmed about their options."

Borrowers and consumer advocates say the reasons so many people aren't paying run the gamut from administrative delays — typically caused by backlogs at the four loan servicers hired by the government to collect payments and guide borrowers through their repayment options – to an inability to afford the bill.

Continue reading here (subscription may be required).

More and more Americans are raiding their retirement "piggy banks" (from James Lavish via X)...

There will be red flags on the path to recession. Ones that we will look back on and say, of course, it was so obvious. This is one of them.

Darth Powell 🦈🇺🇸🇺🇦🇵🇱🇫🇮
@GRomePow

401k hardship withdrawals spike 300%

- Fidelity Investments

Fidelity Investments: 401K Hardship Withdrawals Spikes By 300%

11/22/2023 7:36 am

401K hardship withdrawals, used in the case of last resort due to the negative consequences it entails.

Negative consequences include an additional 10% tax, possible penalties, unable to invest in your 401K for 6 months thereafter (to name a few).

People turn to this only when their credit cards are maxed out, and are unable to find a traditional loan (due to tightening of lending standards), it's basically the definition of "tapping your retirement savings".

According to Fidelity 401K early withdrawals are up 3x what they were in 2018, here's the report:

REAL ESTATE

Existing home prices are set to rise above new home prices for the first time in decades (from The Kobeissi Letter via X)...

The median new home price is down to ~$410,000 while the median existing home prices is nearing $400,000.

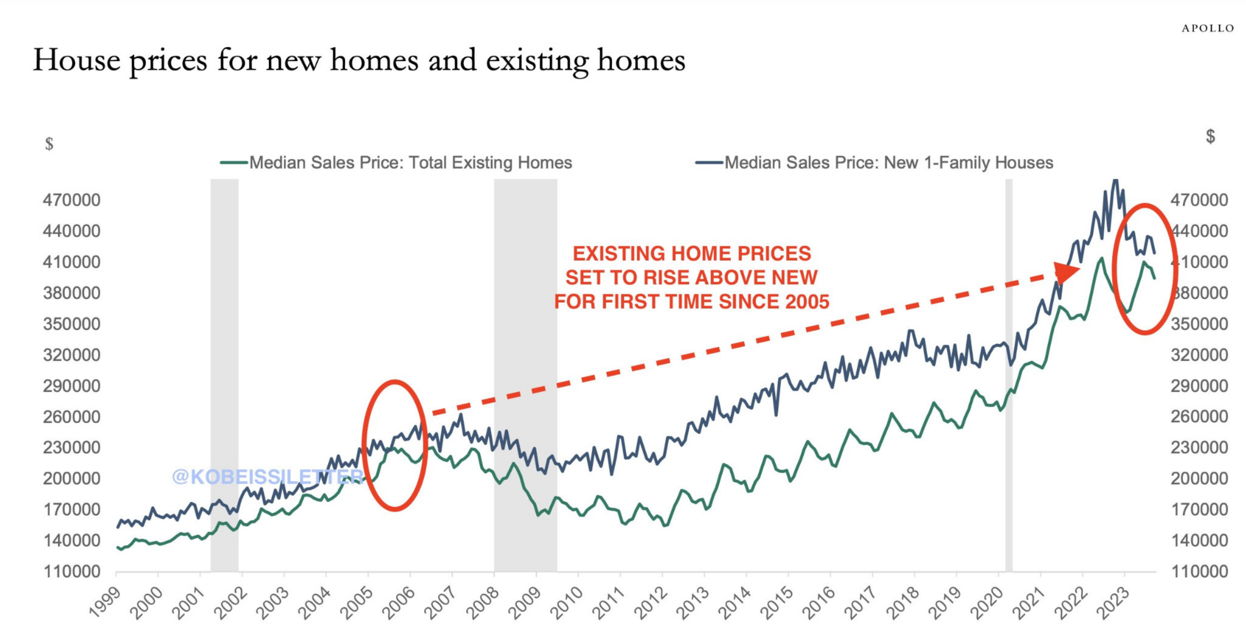
Why is this happening?

~90% of mortgages outstanding currently have an interest rate that is below 5%.

Many mortgage rates are BELOW the current inflation rate.

A mortgage issued in 2020 or 2021 is effectively an asset now.

Truly historic.



Office was the first commercial real estate (CRE) segment to become distressed. This could be the next (from KyleMatthewsCEO via X)...

Class B & C Multifamily in the Sunbelt is the next shoe to drop.

Too many of these properties were purchased between 2020-2022 at extremely low cap rates that buyers were able to make pencil by using significant rent growth assumptions and turning units, with the intention to flip out after only a couple of years in the deal..

In addition, they underwrote these investments with a 3-5 year hold with exit caps in the 4's and 5's.

Problem is, the rent growth has stopped and over the past 12 months is starting to go negative.

Markets that were crazy hot, markets like Austin, Phoenix, Vegas, Nashville, Raleigh, Orlando, etc are now experiencing YOY rent declines, while operating costs are rising rapidly, especially insurance.

Furthermore, exit cap rates are 100+ bps higher and climbing. Will likely be in the 6's and 7's, not 4's and 5's.

Almost all buyers were GPs using LP money they raised for the acquisition promising mid to high teen IRRs.

Here's the problem; on the surface it appears that they can't sell, they can't refinance, and they can't raise more money.

They will try all three, but more often than not won't be successful.

It will be difficult to sell, because cap rates have moved and they likely haven't turned enough units and pushed rents enough to compensate for the value loss from the higher cap rate.

It's challenging to refinance, because to start the lender likely doesn't want to stay in the deal. But regardless of lender, the DSCR is totally jacked up because interest rates are in the 6's and 7's, AND lenders have increased their DCR from 1.15-1.20 to 1.25-1.30.

The LTV with these numbers are so low that it will likely necessitate a capital call every time.

And it's incredibly hard via capital call to raise money because most LPs don't want to put good money after bad, so capital calls are very challenging and optically not ideal for a GP.

So all of these factors; lower values, softening rents, challenging lending environment and pessimism about values falling further are in the process of creating a surge of loans that will mature in '24 and '25 that will not be able to be refinanced or paid off via a sale.

While the culture amongst lenders and special servicers is to work it out with the existing owner as long as there is good behavior, not everything can go that way.

Not every owner behaves well when they digest the fact they worked hard for multiple years on an asset and will effectively make zero dollars.

Either because the lender has to take back the asset, or an owner throws them the keys because they have no money left in the deal and the loan is non-recourse, expect a material increase in distress in class b & c "value add" Multifamily.

There will be some fantastic buying opportunities coming down the pipe.

Having your capital and lender lined up ahead of time is paramount.

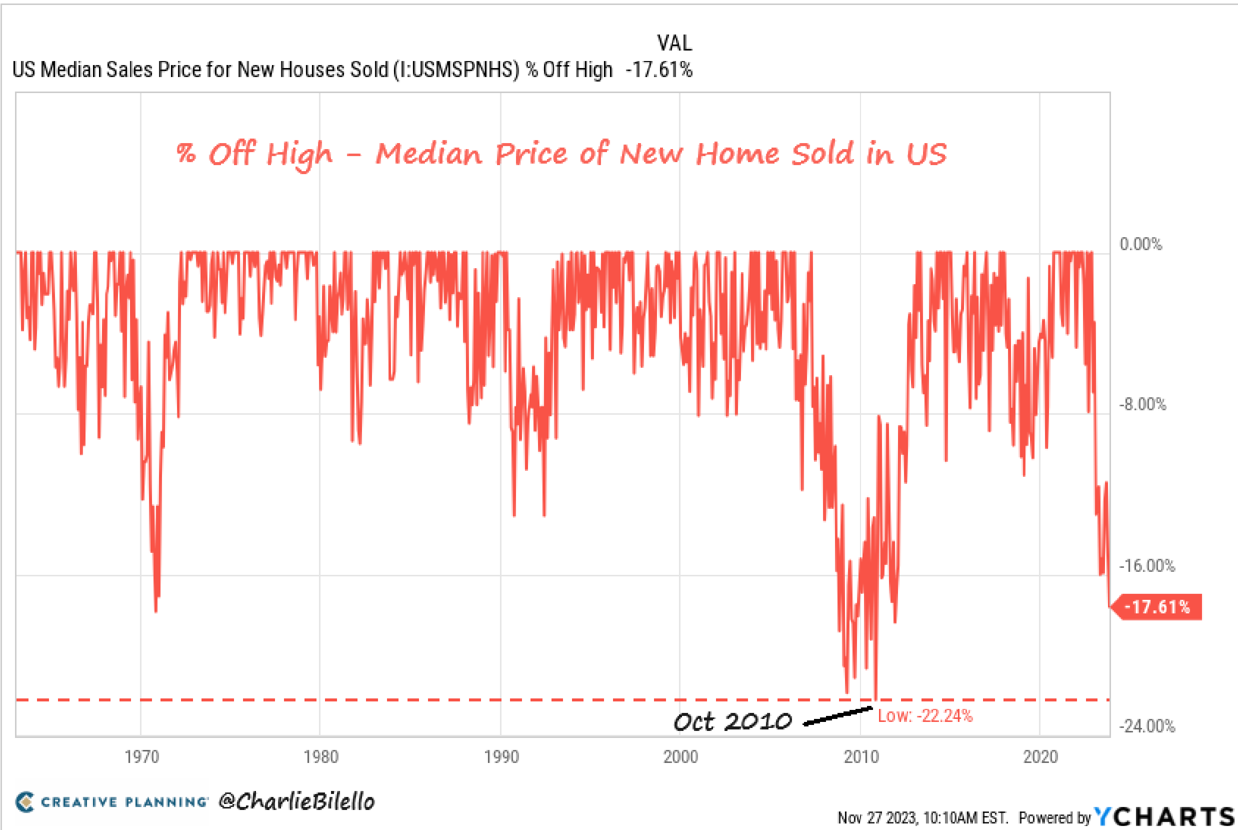
In addition, having your deal flow pipeline via the brokerage community as well as acquisition personnel is essential.

Fwiw many of these fundamental truths apply to Class A multi in these markets as well. But those deals tend to have a little more cushion to absorb loss than the pure value add deals did.

Office was the first. Multi will be the second....who wants to take a guess at the third?

New home prices have fallen almost as much as they did during the Great Financial Crisis (from Charlie Bilello via X)...

The median price of a new home sold in the U.S. is now down 18% from its peak in October 2022. After the housing bubble in the 2000s the median new home price fell 22% nationally.



Existing home prices are likely to fall significantly even if mortgage rates continue to fall ([from *The Wall Street Journal*])...

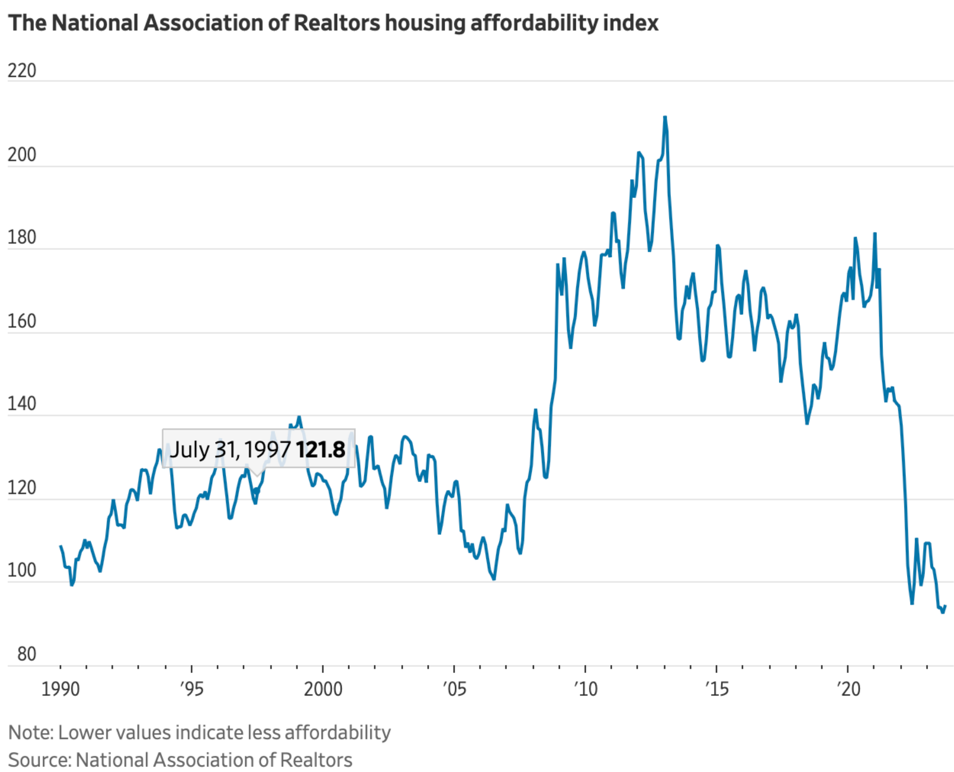
Lower rates would make U.S. houses more affordable, just not affordable enough.

The pandemic set off a flurry of demand for housing. Americans' newfound desire for space, the padding of U.S. household finances from government relief checks, and sub-3% mortgage rates were a potent mix that sent home prices skyward. Now the buying frenzy has passed and, with mortgage rates at their highest levels in over 20 years, not many homes are getting sold at all.

Yet high home prices have proved more than sticky. On Tuesday, S&P Dow Jones Indices reported that the S&P CoreLogic Case-Shiller National Home Price Index hit a new record in September, putting it 3.9% above its year-earlier level.

The big reason why home prices have stayed so high is well known: Current homeowners, carrying mortgages that are far below today's rates, are unwilling to move, and that has placed severe constraints on the supply of homes.

Absent those unusual supply constraints, it seems likely that prices would be a lot lower than they are now. Or, to put it a bit differently, equilibrium prices for homes are probably a lot lower than spot prices.



How much lower? The National Association of Realtors produces a housing affordability index, based on single-family home prices, median family incomes and mortgage rates that has lately hit its lowest levels (signifying the lowest affordability) since 1985. What is striking is that even if mortgage rates declined significantly, this measure would still suggest houses are steep.

The same goes for a similarly constructed index from the Atlanta Fed. By its lights, the threshold for an affordable house is for mortgage and other housing payments to be 30% of household income. As of September, this measure showed that for the median household, the median-priced home was nearly 50% too costly to be considered affordable.

Take mortgage rates all the way down to 5%, versus September's 7.2%, and the Atlanta Fed's measure shows that housing costs are still nearly 25% beyond affordable. One way to make the numbers work at a 5% mortgage rate would, of course, be to boost household incomes by about 25%. The other would be to drop home prices by about 25%.

Continue reading here (subscription may be required).

Veteran CRE investor warns "headlines aren't bearish enough" (from Jack Farley via X)...

When I interviewed veteran commercial real estate (CRE) investor Anthony Dilweg, I expected him to say that the bearish headlines about CRE & office were overblown.

Instead, he said the headlines weren't bearish enough, & made an analogy to the Titanic hitting the iceberg.

This shocking conversation, nearly two hours long, is now released in full.

Here are some of the key claims from Dilweg (who in a former life played quarterback for the Green Bay Packers) on how he is viewing the CRE world:

- The huge challenges CRE & office will have to contend with are WORSE than what CRE faced during the 2008 Great Financial Crisis

- Office as an asset class is "structurally broken" as remote and hybrid work has caused demand to tank

- As vacancy rates skyrocket, over a billion square feet of office asset class (20% of the asset class in the U.S.) will be obsolete over next 3-5 years

- "Return to office" trend is vastly overstated. The CEOs may say Monday - Friday is stern policy but utilization rates reveal Tuesday-Thursday is the de facto norm

- Banks are "completely overwhelmed" as CRE investors use threat of strategic default (i.e. turning keys back) to aggressively renegotiate their loans. Banks must contend with forbearance, restructuring, and extreme reduction in loan yields (350 basis point declines in loan yields are not unheard of)

- The claim that impairments to office as an asset class are just in major cities (NYC, San Francisco, LA) is an overrated narrative. I say to Dilweg (whose 5.5 million square footage portfolio is located in Southeast U.S.) "so you are not quite in the eye of the storm" (I like to support my guests) and he corrects me and says "No, I am."

- If Fed doesn't drastically cut rates, there will be tremendous pain felt throughout the entire CRE industry

- Some banks are "behaving in an interesting way" and Dilweg speculates that FDIC & OCC might still be operating behind the scenes to prevent more bank failures

- Private credit is on the margin replacing some bank financing, but terms are "very punitive"

You can watch the full interview via YouTube right here.

The problems in office CRE extend far beyond interest rates (from Randy Woodward via X)...

Office "used to seeing cap rates 5% to 7.5%, but now seeing them at 10% to 15%." A simple example of this math. The issue has less to do with the higher interest rates today but the fact that they simply can't get a loan big enough to pay off the maturing loan.

Cap Rates – Office Property Valuation
2018 – Cap rate 5% on original loan.

- NOI (net operating income) = $1mm
- $1mm/.5 = $20mm property valuation.
- 70% LTV = approved loan $14mm 5yr term.

2023 – Cap rate 10%

- NOI = $1mm (big assumption given what's going on in office)
- $1mm/.10 = $10mm property valuation.
- 70% LTV = approved loan $7mm (big assumption and more likely moving towards 50% now)
- The borrower needs to bring in $7mm cash/equity to close the old loan.

2023 – Cap rate 15%

- NOI = $1mm
- $1mm/.15 = $6,666mm property valuation.
- 70% LTV = approved loan at $4.666mm
- The borrower needs to bring in $9.33mm cash/equity to close the old loan.

Pending home sales have fallen to the lowest level on record (from The Real Deal)...

Pending home sales fell in October to the lowest level since 2001, when the National Association of Realtors started tracking the housing activity.

Contract signings fell 1.5 percent from September to October, according to NAR's monthly report. Pending deals dropped 8.5 percent year-to-year as NAR's index fell to 71.4, the lowest mark reported since the trade group began tracking the metric in 2001.

The lack of activity was due to some familiar market foes: elevated mortgage rates, high home prices and low inventory. October ushered in some of the highest mortgage rates in decades, hovering around a dreaded 8 percent threshold.

In recent weeks, however, mortgage rates have come down slightly from those Halloween highs, a small bright spot as other factors continue to hamstring the housing market.

"Recent weeks' successive declines in mortgage rates will help qualify more home buyers, but limited housing inventory is significantly preventing housing demand from fully being satisfied," NAR chief economist Lawrence Yun said in a statement.

All four regions tracked by NAR recorded year-over-year declines in pending home sales, with three of the four also reporting month-to-month drops. The exception for the latter was the Northeast, which rose 2.7 percent from September (despite dropping 6.5 percent from last year). Yun said home sales were rising in places with more inventory.

Even when homebuyers can find an acceptable mortgage rate and an available home, prices are yet another obstacle to ownership.

Continue reading here.

The Biden administration reportedly aims to address soaring home prices... by handing out free money and pushing home prices even higher (from *Newsweek*)...

The Biden administration said on Thursday that it was looking to help hundreds of thousands of households to realize their dream of homeownership, part of an effort to reduce housing costs, increase supply of affordable homes and mitigate the rising expense of paying for a house for Americans.

Through its backing of a proposal known as the Neighborhood Homes Investment Act, it would "promote homeownership for an additional 500,000 households while increasing neighborhood revitalization investments," Lael Brainard, the director of the White House's National Economic Council, said in a speech on Thursday when she urged Congress to act on the proposal.

The act will introduce a new federal tax credit to help fund "the development and renovation of 1-4 family housing in distressed urban, suburban, and rural neighborhoods," according to a draft of the bill.

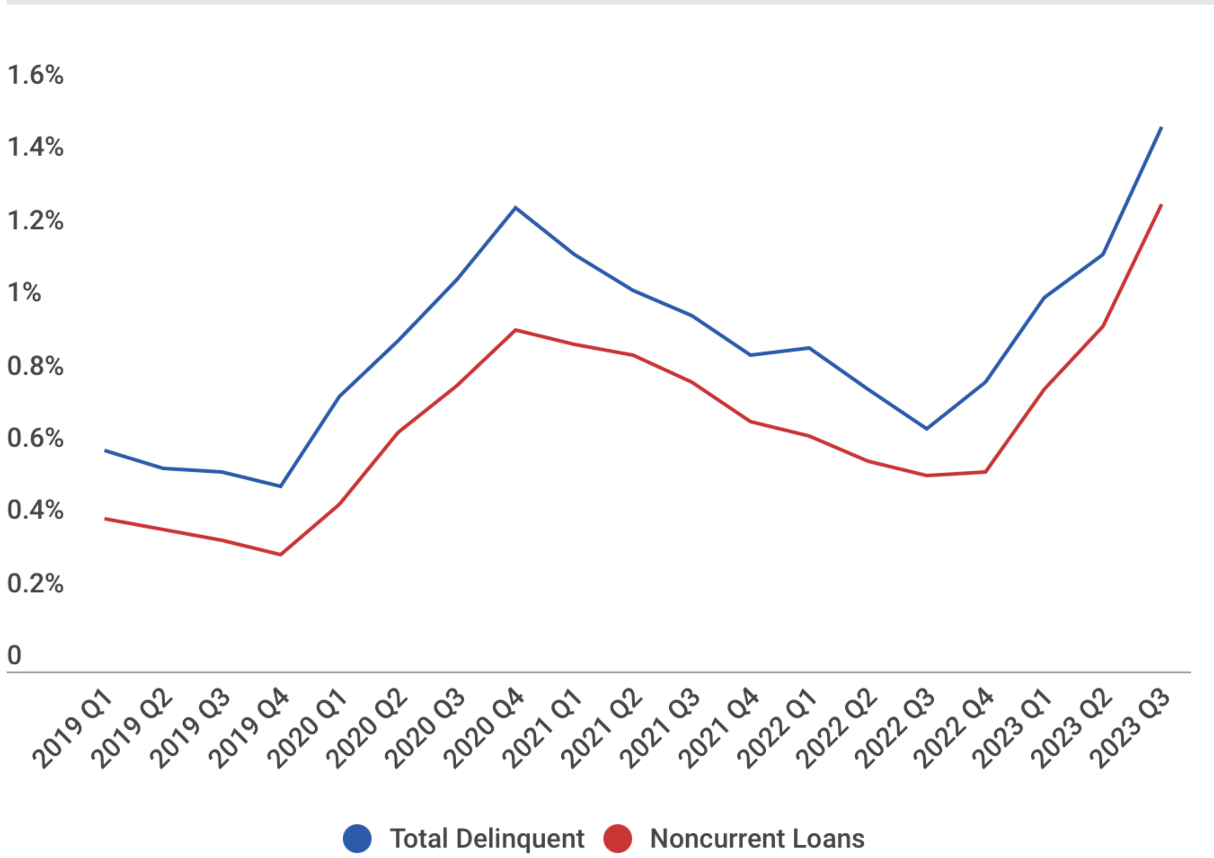
The legislation introduced by Senators Ben Cardin, a Democrat from Maryland, and Todd Young, a Republican from Indiana, could help 500,000 homes and generate $125 billion in development revenue over the next decade, the lawmakers said earlier this year.

Continue reading here.

CRE mortgage delinquencies have now surpassed their COVID-era peak (from Trepp)...

CRE mortgage delinquencies experienced another uptick, continuing the upward trend that started in Q4 2022. However, in Q3 2023, the slope of the increase steepened, with the total delinquency rising to 1.5% in Q3 2023 from 1.2% in Q2. The serious delinquency rate, or the non-current loan rate, experienced an increase to 1.3% in Q3 from 1.0% in Q2.

Q3 Bank CRE Loan Performance – Delinquencies and Defaults



SPECIAL SITUATIONS

Activist Investing, Spinoffs, Arbitrage, Mergers & Acquisitions (M&A), and More

Activist investment firm Elliott Management takes a big stake in oil refining giant Phillips 66 (PSX) (from CNBC)...

Elliott Investment Management has taken a $1 billion stake in Phillips 66 and is seeking as many as two board seats in a push to improve the company's performance, according to a Wednesday letter from the activist investor.

Phillips 66's stock rose more than 4% in afternoon trading Wednesday. The crude refining company has a market cap of nearly $52 billion. CNBC's David Faber originally broke the news.

Elliott's push for the board seats comes as Phillips has underperformed its competitors Marathon Petroleum and Valero. The activist investor said in the letter to Phillips' board that the company's performance has declined in recent years because it has shifted its focus away from its refining segment.

"Over the past three years, as Phillips 66 has fallen further and further behind, its stock has meaningfully underperformed these peers," wrote Elliott partner John Pike and portfolio manager Mike Tomkins in the letter.

Phillips shares are up about 13% year to date, while Marathon Petroleum has gained nearly 29% over the same period. Valero shares are flat year to date, but are up 124% over the past three years versus Phillips' 88% gain.

The activist investor said Phillips' operating expense per barrel has soared in recent years, "shaking investor confidence in the company's ability to run its refining operations efficiently."

Elliott backed CEO Mark Lashier's plan to improve the company's performance. Lashier is targeting $14 billion in earnings before interest, taxes, depreciation and amortization by 2025.

Continue reading here.

Here's a list of event-driven trade ideas that are potentially actionable today (from ToffCap)...

- ***S*olvay (SOLB Belgium)**. A reminder of the upcoming separation of Solvay's Essentials business (commodity products, Solvay) and specialty chemicals operations (Syensqo) on December 11. We recently posted a note on the blog discussing the separation. Interesting to keep an eye out given large differences in quality and growth of both companies.
- **Newpark Recources (NR US)**. Initiated a strategic review for its Fluid Systems business, with options including selling the entire segment or winding down its working capital. Divestment could generate $200m, and will increase the quality of the business. H/t @ ideahive for the idea.
- **Clarus (CLAR US)**. Has received bids for certain assets of the companies. Does not appear to be a high quality company, but might be interesting in case of sale given relatively high leverage.
- **Cazoo (CZOO US)**. A lot going on with this nano-cap; debt swaps, upcoming warrant distribution, reverse stock split. Should all be completed in the first week of December. Given nano-cap status, all this action could create a lot of volatility.
- **Marlowe (MRL UK)**. Shares down strongly on recent results. Strategic review ongoing; company is considering sale or spin-off of TIC. Currently trading at ~6.3x FY23e ebitda, roughly 40% below peers. H/t @ValueSituations for the idea.
- **abrdn European Logistics Income (ASLI UK)**. Launched a strategic review and is considering all options, including full sale. Trading at 30% discount to NAV. Looks like a very good chance for a deal (dividend target will have to be cut, but will reduce the already low liquidity). H/t @Estebanalbanil for the idea.
- **Enhabit (EHAB US)**. Ongoing review of strategic alternatives, including full sale of the company. Sector deals have been performed at mid-teens ebitda multiples. A similar deal valuation would suggest 50-100% upside.
- **Crescent Energy Company (CRGY US)**. Strong insider buying from the c-suite. Co trades at c. 2.5x ev/ebitda.
- **GrowGeneration (GRWG US)**. Very strong insider buying in GrowGeneration. Company seems to be hitting a rough patch, but insiders appear to love it. Net cash b/s.
- **Presidio Property Trust (SQFT US)**. Presidio (a REIT) announced a $10m buyback, on a $11m market cap. Plenty of insider buying recently.
- **Brighthouse Financial (BHF US)**. Announced a $750m buyback, >22% of the market cap.
- **Sohu.com (SOHU US)**. Chinese Sohu.com (with a net cash position of >$1bn on a $290m market cap), announced a $80m buyback program (c. 30% of market cap).
- **Battalion Oil (BATL US)**. Continues to explore strategic alternatives. Battalion is trading at ~3x TTM ev/ebitda.
- **Cambium Networks (CMBM US)**. Relatively strong insider buying. We highlighted CMBM in our interesting companies list as the stock has been under strong pressure but should have very strong tailwinds over the next few years.
- **Howard Hughes (HHH US)**. Ackman (Pershing Square) continues to buy HHH; now at almost 38%. Company recently announced it would spin off its Seaport and other related assets. ~90% upside to NAV (according to HHH).
- ***Academy Sports and Outdoors (ASO US)***. Announced a new $600m buyback program, for a total of $700m, roughly 18% of the market cap.

- ***Docebo (DCBO US)***. Odd lot tender offer (potential $1000 to be made). Keep assessed.
- ***Aware (AWRE US)***. Announced a buyback of up to $10m (almost 30% of market cap). Aware is a (unprofitable) nano-cap with ~67% of its market cap in net cash.
- ***JOYY (YY US)***. Chinese JOYY (with a net cash position of $2.7bn on a $2.3bn market cap), announced a $530m buyback program (c.23% of market cap.)
- ***Limoneira (LMNR US)***. Launched a strategic review. Options include full sale of the company. Management believes that the current market value is not reflective of the company's inherent value.
- ***Vista Outdoor (VSTO US).*** Vista to sell its Sporting Products operations for $1.9bn (or about 5x ev/ebitda on the unit's FY24e). Spin off the table. Current public stockholders of Vista Outdoor to receive shares of Outdoor Products (recently rebranded as Revelyst) and approximately $750 million in cash in the aggregate **UPDATE: Activists ColtCZ disclosed a stake and launched a bit for $30 p/s and a $900m buyback, which the company rejected. Interesting to keep assessed, could continue to see some fireworks.**
- ***Worthington Industries (WOR US)***. To spin Worthington Steel (ticker WS). Record date 21 November, 1-1 share ratio.
  UPDATE: Worthington Steel (WS) recently split from Worthington Industries (WOR). Interesting thread from @valuedontlie on spin.
- ***Renault (RNO France)***. Intends to complete the spin-off of its EV business ('Ampere') in H1 24. Renault will hold a capital markets day on 15 November.
  UPDATE: Ampere IPO targeted Q2 24, at EUR 8-10bn valuation.
- ***Lionsgate (LGF/A US)***. Spin-off of the movie / TV studio business estimated in September. Spin targeted before year end.
  UPDATE: Bondholders formed a bond group to block the spin, and appear to be succeeding.
- ***Mallinckrodt (MNKTQ US)***. Planning to emerge from bankruptcy by end of year.
  UPDATE: Recently emerged from bankruptcy.
- ***Neighbourly Pharmacy (NBLY Canada)***. Proposed take private for C$20.50 vs current price of c. $17.90 current. Exclusivity agreement extended to Jan 15 to complete negotiations. H/t @paddymcilvenna for the idea.
- ***Roivant Sciences (ROIV US)***. On the brink of sealing a $7.25bn deal with Roche for their Telavant project. Once deal closed, cash (~$7bn) + 57% stake in Immunovant (IMVT) results in roughly $12 per share - vs. current share price of $11; hence free optionality for everything else that Roivant is developing. H/t @JonathanPaxx (and VIC) for the idea.
- ***Silver Sun Technologies (SSNT US)***. Micro-cap SSNT announced a weird transaction; XPO chairman Jacobs to invest $900m in Silver Sun, Sequoia $100m, existing Silver Sun business to be spun-off. M&A shell remains (tbc QXO), setting a target of >$1bn revenues by year 1 with acquisitions is building products space.
- ***Lazydays (LAZY US)***. Continued strong insider purchases (CEO and CFO). Largest shareholder has also been acquiring shares. Stock hammered over past few months.

- ***Howard Hughes (HHH US)***. Another week, another purchase by Ackman (Pershing Square) of HHH. Company announced it would spin off its Seaport and other related assets. ~90% upside to NAV (according to HHH).
- ***Velo3D (VLD US)***. Velo3D announced that is has started a strategic review 'to maximise shareholder value'. CEO recently left.
- ***Ether Capital (ETHC Canada)***. Lots going on at cryptocurrency investor Ether Capital: CEO change, buyback announced as well as to initiate exploring strategic alternatives. Company has a strong balance sheet.
- ***InPost (INPST Netherlands)***. Advent (PE) sold another stake (5%) to PPF. PPF now owns ~22%, with option for the another 10%. Shares have reacted positively (again) as 'shareholder overhang' is reduced.
- ***Vivendi (VIV France)***. Trying (again) to figure out ways to reduce the conglomerate discount. Now exploring a split of the company into several entities (Havas, Canal+ and an InvestCo).
- ***Seadrill (SDRL US)***. Announced a new $250m buyback (~7% of s/o). Since its (re)listing, Seadrill continues to print cash and buy back shares.
- ***Seanergy Maritime (SHIP US)***. Announced a new $25m buyback, roughly 17% of market cap.
- ***Quantasing (QSG US)***. Another Chinese net cash, negative EV company announced a big buyback, $20m or ~20% of market cap.
- ***Core Scientific (CORZQ US)***. To emerge from bankruptcy in Jan. 2024 + right offering announced. Lots going on which will create volatility (hence opportunity).
- ***Capstone Green Energy (CGRNQ US)***. To emerge from bankruptcy over next week. Will trade OTC.
- ***Designer Brands (DBI US)***. Designer Brands continues to buy back shares; now roughly 30% of s/o bought back over past 12 months.
- ***SuRo Capital (SSSS US)***. Continued big insider buying in this micro-cap.
- ***African Oil Company (AOI Canada)***. Announced a 10% buyback + big insider purchases. AOI is ~25% net cash, very profitable and cash generative.
- ***G-III (GIII US)***. Announced a buyback of 10m shares outstanding, >20% of market cap.
- ***Icosavax (ICVX US)***. AstraZeneca to initiate a tender offer for all s/o at $15 p/s, incl. a contingent value right (CVR) potentially worth $5. Shares at ~$15.70.
- ***Biglari Holdings (BH US)***. Insiders purchased $2.3m in shares (>4% of s/o). Biglari now owning >60% of s/o.
- ***Spartan Delta (SDE Canada)***. Strong insider purchases. Stock decimated over past year; now ~$3 p/s vs $14 a year ago.
- ***Kodiak Gas Services (KGS US)***. Kodiak has a large upcoming lock-up expiry ahead on Dec. 26, roughly 80% of shares outstanding.
- ***Webcentral (WCG Australia)***. Recently announced the sale of core business. Stock price was up sharply, but market seems to underestimate SOTP value. Current share price ~28ct vs potentially >45ct per share SOTP. Should play out over the next few months. H/t to @TheRealDavey2 and @ClarkSquareCap for the idea. See @ClarkSquareCap for a write-up. **UPDATE: Buyback announced (10%), to commence as soon as Dec. 22, after completion of the sale of the Domains business (expected Dec. 20).**

INVESTMENT CHRONICLES

- ***Docebo (DCBO US)***. Odd lot tender offer (potential $1000 to be made). Keep assessed.
  UPDATE: Reminder that tender offer will expire on Dec. 28.
- ***Lifecore Biomedical (LFCR US)***. Strategic alternatives. Potential buy-out. Demand for similar CDMO assets is high. Large shareholders pushing for sale. Potentially 75-100% upside.
  UPDATE: LFCR recently communicated that it continues to actively evaluate strategic alternatives.
- ***Rain Oncology (RAIN US)***. Busted biotech, negative EV Rain Oncology received a buy-out offer from Concentra Biosciences (Tang Capital). Shareholders to receive (if accepted) $1.25 per share + a contingent value right (CVR). Tang already owns c.15% of the company. Current share price (27 October) is $ 1.07.
  UPDATE: Signed a merger deal with Pathos AI for $1.16 cash per share + a CVR with potential value of $0.17. Current share price $1.20.
- ***LianBio (LIAN US)***. Net cash biotech, announcing strategic review. Interest from BMS for HCM assets. BMS set to pay LianBio $350m in a one-off fee. C. 80% of market cap currently net cash.
  UPDATE: Received offer from Concentra Biosciences for $4.30 p/s in cash. LIAN rejected the offer.
- **Spirit Airlines (SAVE US)**. Merger arbitrage. Spirit / JetBlue merger uncertainty; airlines disagree with DOJ attempt to block the merger. The trial date has been set for October 16. Spirit shareholders to receive ~$ 33 / share if deal consummated (vs current share price ~$ 17). Companies confident in deal closing potential.
  UPDATE: Court decision expected by year end. Spread still wide.
- ***Yellow (YELLQ US)***. Currently in bankruptcy proceedings. Relatively valuable asset base with already some good bids; main uncertainty is pension liabilities. High risk/reward trade. H/t @AmadeusValue for idea and more info.
  UPDATE: Positive news flow regarding (pricing of assets in) auctions; strong share price reaction so far.
- ***Solvay (SOLB Belgium)***. A reminder of the upcoming separation of Solvay's Essential business (commodity products, Solvay) and specialty chemicals operations (Syensqo) on December 11. Interesting to keep an eye out given large differences in quality and growth of both companies.
  UPDATE: Spin completed. Spinco trading under Syensqo SYENS. A reminder that this was a 1-1 spin. Strong share price reaction of both shares.

Activist short seller Hindenburg Research targeted a recent IPO this month (from Hindenburg Research via X)...

Maison Solutions is a company that took six California Asian-themed grocery stores public on the Nasdaq in October.

The company also owns a 10% equity interest in a Dai Cheong Trading, a distribution company owned by $MSS controlling holder, Chairman and CEO, John Xu.

$MSS went public on 10/5/2023 at $4 per share with a valuation of $69M and closed the same day at $8.96, essentially doubling in value within hours of the IPO.

As of yesterday it had a market cap over $265M.

$MSS is a loss-making business in dire financial straits.

Grocery stores typically have razor thin margins of between 1% to 3%.

For the quarter ended July 31, 2023, $MSS posted $13.8 million in revenue and a loss from operations of ($216,745).

As of July 31, 2023, $MSS had just $1.61 million in cash and total current assets of $6.70 million vs. $8.14 million of current liabilities & loans of $2.8 million.

As of July 31, 2023, MSS was in violation of its debt service coverage ratio covenant on its bank loan.

In further signs of distress, an apparently undisclosed federal tax lien totaling $80,053 was filed on Maison International Inc. in July 2022 for prior tax periods.

According to UCC records as of Dec. 15th, there are no updates that would indicate the lien has been paid off.

Grocery stores often trade at P/S of well under 0.5x.

Ex: $VLGEA operates 34 supermarkets and trades at ~0.15x sales.

$NGVC is a regional chain based in Colorado that trades at ~0.33x sales.

$MSS trades at ~4.63x sales. At a 0.5x multiple it would trade at $1.58, 90% downside.

Pre-IPO, $MSS acquired stakes in 2 supermarkets from the wife of the CEO, valued at $2.5m and $410k respectively.

We estimate the combined total value of the company's assets to be less than $15 million.

Beyond valuation, we found multiple red flags with $MSS.

In $MSS IPO prospectus, Chairman, CEO and key holder John Xu is also listed as President of J&C International Group, LLC, “a cross-border investment firm” since 2013.

J&C’s website says it “support[s] immigration services for high-net-worth Chinese investors and institutions”.

$MSS CFO Alexandria Lopez is also listed as former CFO at J&C International. Her bio lists 10 years of financial and accounting experience, all at J&C International.

She received her B.A. in Accounting from the University of Phoenix, an online university.

J&C International, $MSS CEO John Xu and related entity Hong Kong Supermarkets were named as defendants in 2020 litigation alleging they used supermarkets as a front to defraud the EB-5 visa program.

The plaintiff alleged that J&C International took a $500k investment in Hong Kong Supermarket from him to help him get his Visa.

He alleged that $MSS CEO John Xu and J&C forged his Visa application, and listed him as a fake employee of a supermarket location now owned by $MSS.

The plaintiff alleged that when he asked for copies of his visa application, he was threatened with retaliation by J&C and John Xu.

The court found in favor of the plaintiff, and defendants lost an appeal.

The case is currently being scheduled for trial.

In a separate lawsuit from 2018, a plaintiff alleged that J&C and $MSS CEO John Xu engaged in a scheme to loot his company and turn it into an illegal visa mill.

We also believe that MSS’ recently appointed centralized vendor, XHJC Holding Inc., is an undisclosed related party.

The principal address for XHJC Holding Inc is a Japanese restaurant that is associated with $MSS CEO John Xu.

The mailing address we found for XHJC Holding on State of California corporate documents is the same as J&C International.

MSS's underwriter, Joseph Stone Capital, has 7 disclosures on its FINRA BrokerCheck page, including 4 regulatory matters and three arbitration cases.

One described "knowingly providing substantial assistance to salespeople conducting fraudulent and unethical sales practices."

$MSS is the only priced IPO that Joseph Stone Capital participated in for 2023.

In 2021, Joseph Stone was the underwriter for $EJH. Shares spiked as high as $16.60 shortly after the IPO and now trade at a spilt adjusted price of $0.041.

In 2022 Joseph Stone was the sole underwriter for Visionary Education Technology Holdings Group Inc, now trading as $GV.

The IPO was priced at $4 per share and shares now trade for $0.12 cents.

$MSS's prospectus auditor was Friedman LLP, previously charged by the SEC over failure to detect fraud at another Asian supermarket chain, iFresh.

iFresh was delisted & now trades at $0.0006 on the OTC pink sheets.

One of MSS' stores, in El Monte, was once an iFresh location.

Our investigation also revealed that $MSS is being pumped by WhatsApp chat rooms, in similar fashion to what we saw with a similar China-based pump and dump, $GDHG, which crashed ~90% in one day of trading last week.

The chatroom dialogues were nearly identical.

On Nov. 22 2023 Maison closed a private placement of 1,190,476 shares of its common stock at $4.20 per share to 2 foreign individuals.

One purchase was for 892,857 shares, representing 5.12% of the total outstanding shares and the largest holding outside of the CEO.

The closing price on the day was $10.87, giving these unnamed buyers an instant 61% discount on shares they turned around and registered for re-sale one week later.

The Prospectus filing for sale of these shares was filed on December 11th.

We believe $MSS is slated to suffer a similar fate to $GDHG and that retail shareholders will once again be left holding the bag on a massively overvalued company that has become bloated in size due to illegal and nefarious pumping/manipulation.

We are short $MSS.

Another short seller alleges fraud at recent e-commerce tech IPO Klaviyo (KVYO) (from Lauren Balik via Medium)...

Summary:

1. There is strong evidence that suggests Klaviyo (NYSE: KVYO), one of 2023's few tech IPOs, is increasingly reliant on privately owned company Retention.com and similar businesses for Klaviyo revenue generation.
2. Klaviyo's revenue model relies on "contact list size" or the number of contacts on lists that are passed through Klaviyo's email, SMS, and other offerings. Klaviyo relies heavily on contact list size growth given Klaviyo's long tail distribution with the vast majority of its over 130,000 customers spending under $50,000 annually through Klaviyo.
3. Retention.com is a service that markets directly to Klaviyo customers, promising Klaviyo customers high returns on investment through its Personally Identifiable Information (PII) data collection network. Retention.com promises to turns anonymous visitors to Klaviyo customer websites into email addresses for its customers to then pass through Klaviyo.
4. Retention.com makes no attempt to adequately explain how their process of turning anonymous visitors to e-commerce websites into email addresses it then sells to brands is legal, instead relying on gimmicky sales tactics like throwing influencer parties and operating B2B affiliate marketing tactics to land new Klaviyo customers.
5. Retention.com uses tactics such as shady payday loan advertising posted on social media to bait American consumers into giving their personal data to Retention.com's data collection network. This PII customer data generated in this process is then used as Retention.com's justification for consumer consent for emails, to which it sells access to Klaviyo customers. This data is constantly resold over and over again to Klaviyo customers to boost the sizes of lists Klaviyo customers feed through Klaviyo, increasing their Klaviyo costs.
6. There is strong evidence suggesting that in the two Klaviyo fiscal quarters leading up to Klaviyo's IPO and listing on the New York Stock Exchange, Retention.com engaged in a blitz of activity which pumped revenue to Klaviyo even though Retention.com's practices are legally questionable and outside of Klaviyo Terms and Acceptable Use Policy.

7. Klaviyo does not make mention of Retention.com in its partner materials, yet Retention.com directly targets Klaviyo customers and in fact Retention.com leads with this messaging on its website and in public-facing marketing materials.
8. Similar companies such as GoBot have also popped up and target Klaviyo customers by promising Klaviyo customers 10x email list sizes by turning anonymous site visitors into email contacts to be fed through Klaviyo, which pumps up Klaviyo revenue.

Continue reading here.

PRECIOUS METALS

Gold appears to be on the verge of a massive move higher (from Otavio Costa via X)...

Gold is back above $2,000. The next move for the metal is to break out from a triple-top formation.

Precious metals have never been this close to a third cycle.

If so, two important assets are poised to become major beneficiaries:

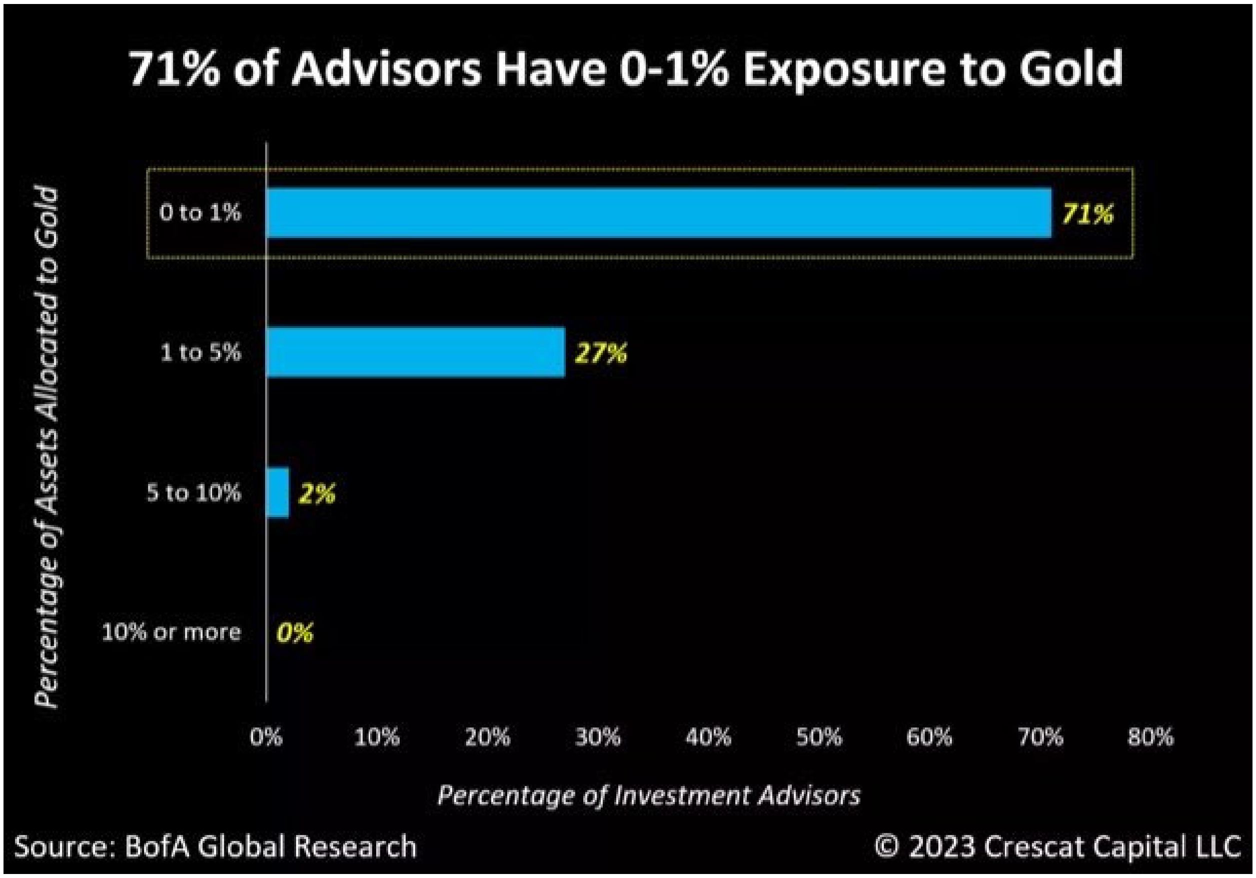
- Silver, with a historically high 83 gold-to-silver ratio
- The overlooked, underappreciated, and unloved mining industry, currently valued at a fraction of its historical valuations

Yet, most investors have virtually no exposure to gold today (from Otavio Costa via X)...

What further reinforces the undeniably strong case for gold today is the consistent neglect of the metal as a defensive alternative over the past few decades.

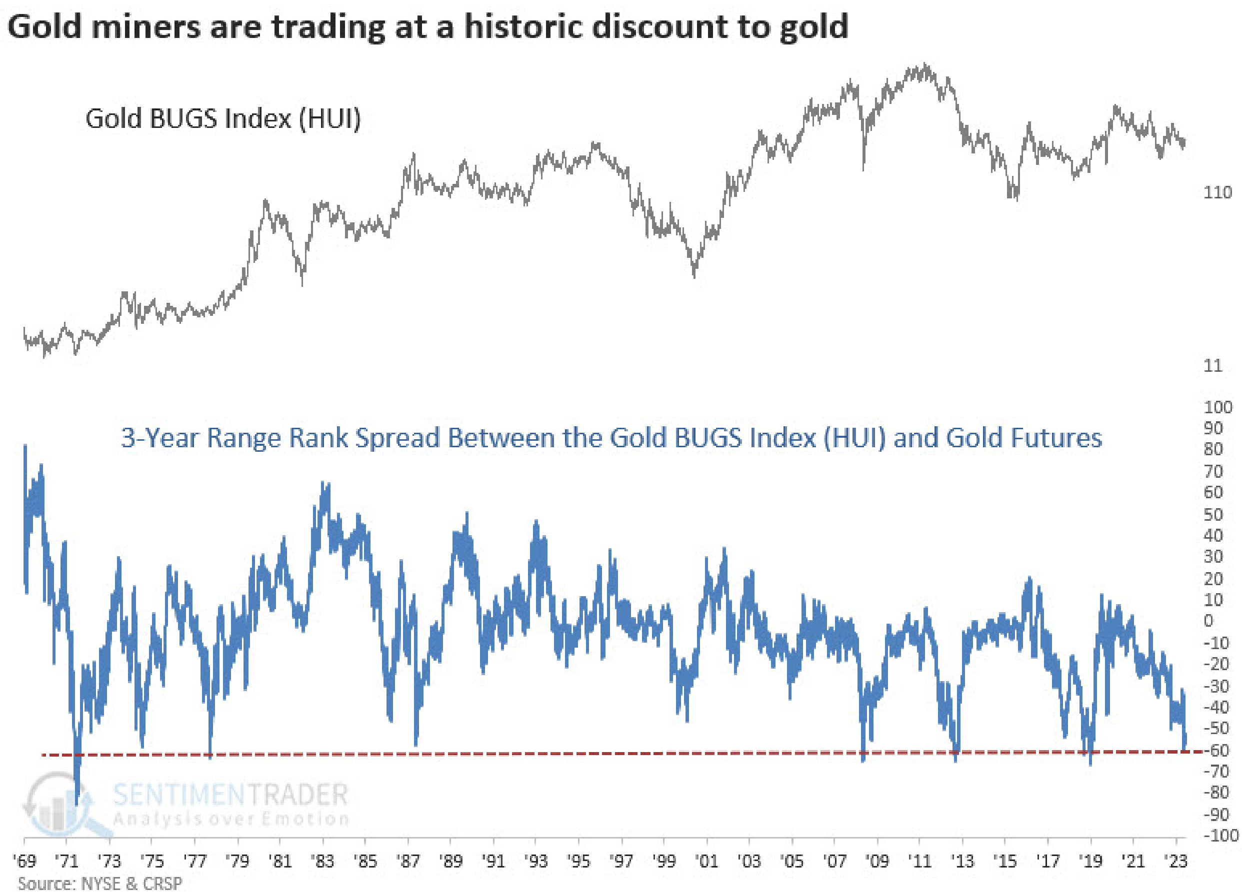
This is evident in the significant underrepresentation of precious metals among traditional investment strategists.

If traditional investment strategies and central banks undergo a substantial shift towards the metal, it could likely represent one of the most compelling investment opportunities in gold to date.



Gold mining stocks are trading at an historic discount to gold (from Dean Christians, CMT via X)...

The 3-year range rank spread between gold miners and gold recently fell to -60%, a phenomenon observed in less than 1% of cases since 1969.



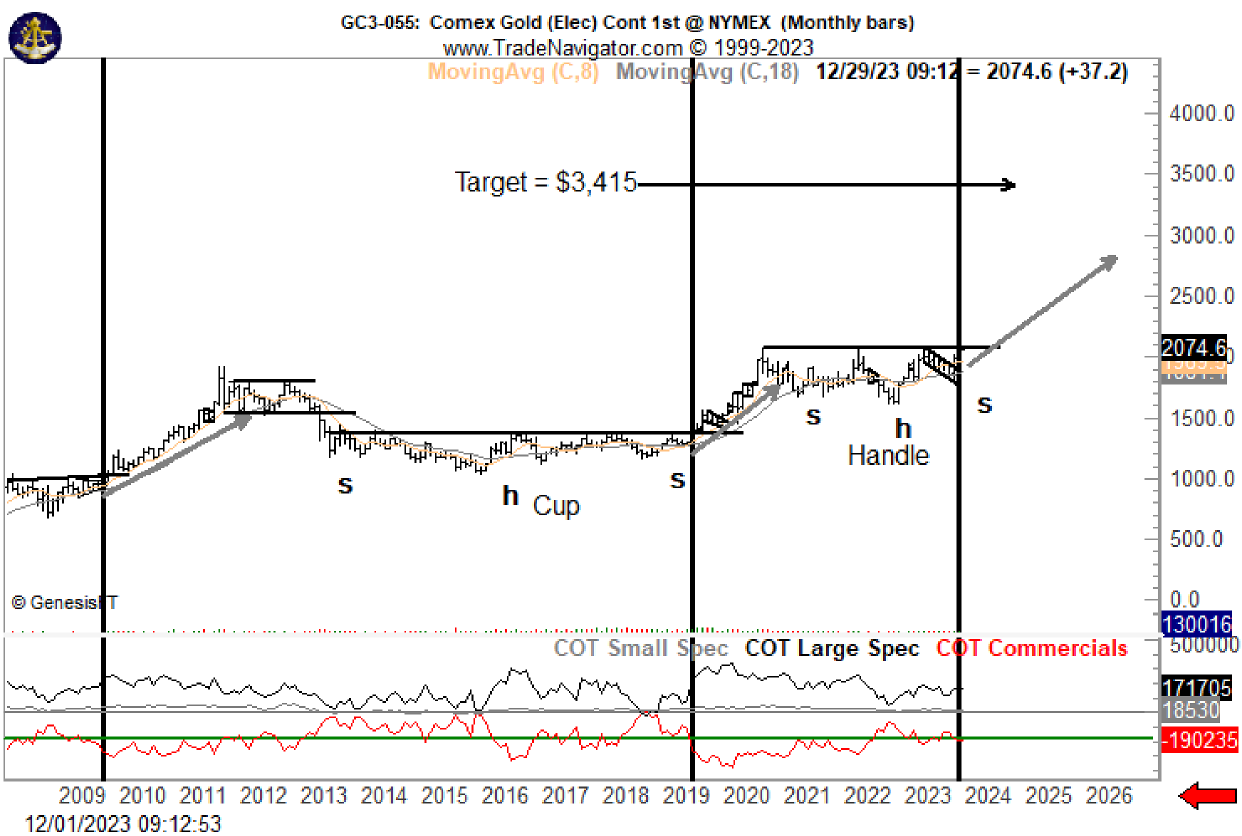
Gold has already touched new all-time highs this month with very little "fanfare" (from Lyn Alden via X)...

Futures market positioning suggest gold could move well above $3,000 over the next couple of years (from Peter Brandt via X)...

Some traders claim that the current [Commitments of Traders] profile in Gold is negative. Au contraire!!!!

Similar COT profile existed at start of 80% advance in 2009 and 50% advance in 2019.

Apply the avg of these and Gold goes to $3,415



Costco sold $100 million worth of gold bars last quarter (from Mining.com)...

Gold bars continue to be one of the hottest items at Costco ahead of the holiday season.

This week, the US retail warehousing giant revealed that it sold $100 million worth of the yellow metal during the first fiscal quarter.

In an earnings call on Thursday, Costco CFO Richard Galanti confirmed to analysts that bullion is definitely on the menu for its customers. "They're buying gold," he said when asked about consumer trends from the latest quarter.

This echoes what Galanti had said back in September — that the company's inventory of PAMP Suisse gold bars tends to sell out "within a few hours" of the products being listed online.

Continue reading here.

This gold-mining stock is a buy (*from Barron's*)...

Gold-mining stocks haven't been able to keep up with gold prices—but this may be the year that changes for Barrick Gold.

Gold miners are thought of as leveraged plays on the metal, yet Barrick shares are up just 3% this year while gold is up more than 10% to $2,036 an ounce. Blame higher costs and lower-than-expected gold production.

Barrick has several things going for it. The company has some of the world's best mines in spots like Nevada and the Dominican Republic, and it's the top gold producer in Africa. It aims to boost its mine output—mostly gold and some copper—by 30% by the end of the decade.

It has the industry's most effective leader in CEO Mark Bristow, a swashbuckling South African and hands-on manager who visits each major mine at least three times a year. He also has a knack for handling delicate relations with host countries in the developing world.

"Barrick probably has the best management in the mining business, an excellent balance sheet with virtually no net debt, and a well-covered 2.3% dividend yield," says independent analyst Keith Trauner. The stock trades for about 16 times next year's projected earnings.

Continue reading here (subscription may be required).

ENERGY

No, solar and wind cannot replace fossil fuels today (from Alex Epstein via Energy Talking Points)...

The anti-fossil-fuel agenda pretends it's not harming us by claiming, in contradiction to all evidence, that rapidly eliminating fossil fuels won't make energy more expensive and less reliable—because unreliable solar and wind can somehow replace fossil fuels.

If solar and wind could actually replace fossil fuels, they wouldn't need massive government punishments of fossil fuels plus massive government preferences of their own—mandates, subsidies, and no penalty for unreliability.12

If solar and wind could actually replace fossil fuels, China, which dominates the production of solar and wind components, wouldn't be using coal to produce these components—and wouldn't have over 300 planned new coal plants designed to last over 40 years.13

Continue reading here.

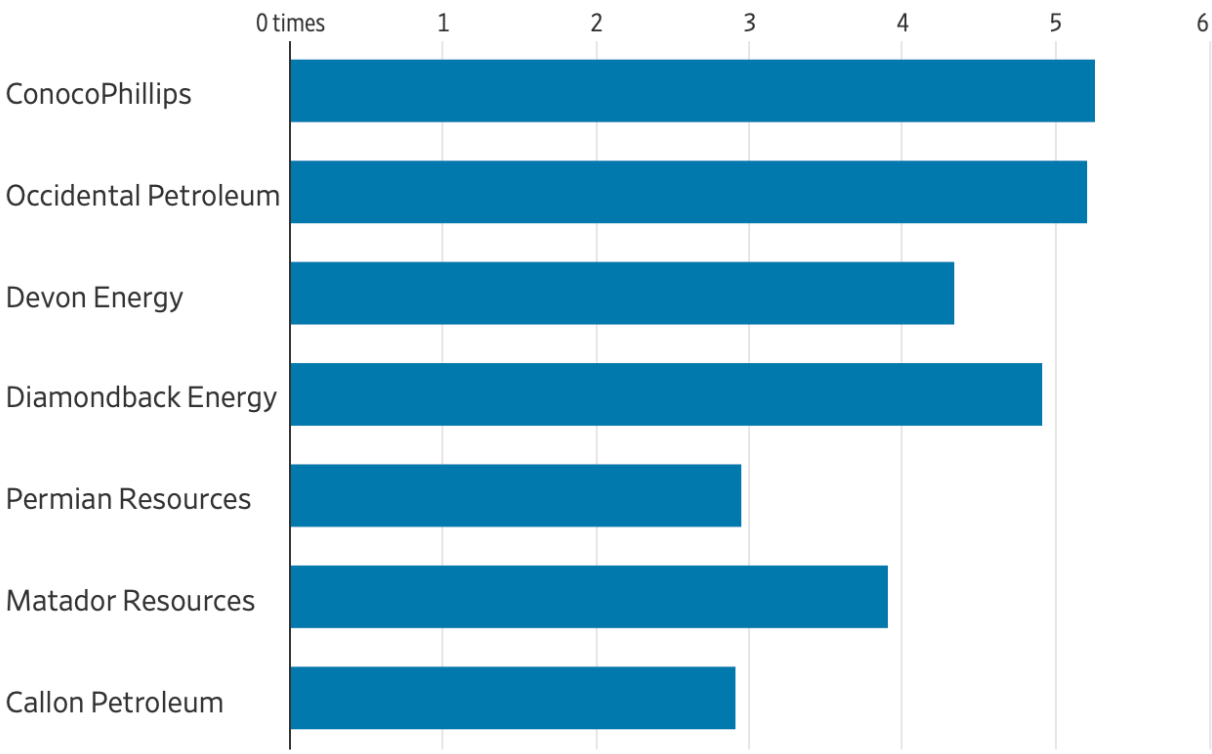
The U.S. oil "land grab" continues (*from The Wall Street Journal*)...

It's a seller's market in the U.S. oil patch.

Occidental Petroleum is in talks to buy CrownRock, one of the last remaining private companies of scale in the Permian basin, *The Wall Street Journal* reported on Wednesday. If the deal goes through, it would be the latest in a string of mergers and acquisitions this year, including Exxon Mobil's $64.5 billion purchase of Permian giant Pioneer Natural Resources.

The *Journal* report said the deal could be valued at "well above $10 billion" including debt. CrownRock produces nearly 150,000 barrels of oil equivalent a day, according to Fitch Group. Even assuming a conservative price tag of $11 billion, it implies Occidental would be shelling out at least $73,000 per flowing barrel of oil equivalent a day for CrownRock.

Producers with the largest scale also tend to command the highest valuation
Enterprise value as a multiple of forward-12-month Ebitda. Companies ordered by enterprise value, with the largest on top.



Note: As of Nov. 30, 2023.
Source: FactSet

That pricing looks steep compared with other moderately sized Permian deals inked this year. Notably, Ovintiv OVV 3.22%increase; green up pointing triangle in April agreed to pay about $65,000/boepd for Permian basin assets from private equity firm Encap, according to an estimate from Bison Interests, an energy investment firm. Civitas Resources' CIVI 2.01%increase; green up pointing triangle Permian deal from earlier this year implied a $47,000/boepd valuation, according to Bison's estimate. Exxon forked over $91,000/boepd for Pioneer, though arguably Exxon was paying up for Pioneer's vast undeveloped acreage—something the per barrel metric doesn't capture.

Not that Occidental is averse to paying up. The company famously outbid Chevron to buy Anadarko Petroleum in 2019—a deal that seemed reckless back when oil prices plunged in 2020 but has paid off handsomely. Occidental was the top performer in the S&P 500 in 2022 and the company is in a much better spot financially now, having shed some $30 billion of long-term debt since its post-acquisition peak.

The current oil market isn't particularly supportive. Prices declined even after OPEC+ announced a further production cut on Thursday. Meanwhile, investors haven't rewarded companies for making acquisitions, as evidenced by the lukewarm reception to Exxon and Chevron's deal announcements.

Still, the shrinking pool of acquisition targets and the market's discount on small producers should provide enough motivation for consolidation. An index that is heavily weighted toward Exxon Mobil, Chevron and other large producers is 43% more expensive than an index tracking smaller producers, based on enterprise value as a multiple of forward-12-month earnings before interest, taxes, depreciation and amortization. Any company that can be "bite size" for another company is in a good position, notes Dan Pickering, chief investment officer at Pickering Energy Partners. Large Permian-focused bites include Diamondback Energy, while smaller targets include Matador Resources, Permian Resources and Callon Petroleum.

This game of musical chairs is only bound to get more intense. Whoever wants the next seat will have to pay up.

Continue reading here (subscription may be required).

Uranium demand appears likely to move dramatically higher over the next couple decades (from Kuppy via X)...

Has anyone pledged to triple uranium production???

Nuclear Hazelnut 👷‍♀️
@NuclearHazelnut

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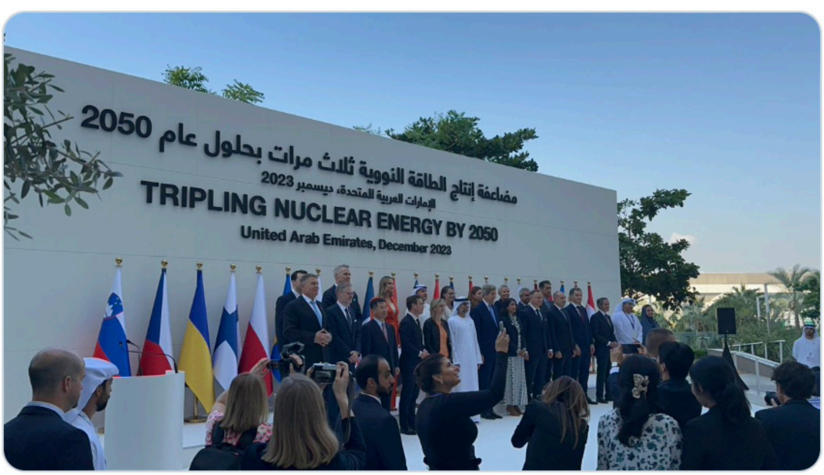
COP28 | 🇦🇪

It is official, these countries have officially pledged to TRIPLE nuclear energy by 2050.
An historic day, as nuclear energy is finally being recognized to achieve global net zero greenhouse gas emission.

Romania 🇷🇴
Finland 🇫🇮
Czech Republic 🇨🇿
Slovakia 🇸🇰
Republic of Korea 🇰🇷
Sweden 🇸🇪
France 🇫🇷
UAE 🇦🇪
Canada 🇨🇦
United States 🇺🇸
Ukraine 🇺🇦
United Kingdom 🇬🇧
Poland 🇵🇱
Bulgaria 🇧🇬
Japan 🇯🇵
Belgium 🇧🇪
WNA
IAEA



Oil could face some significant headwinds in the months ahead (from Ross Hendricks via X)...

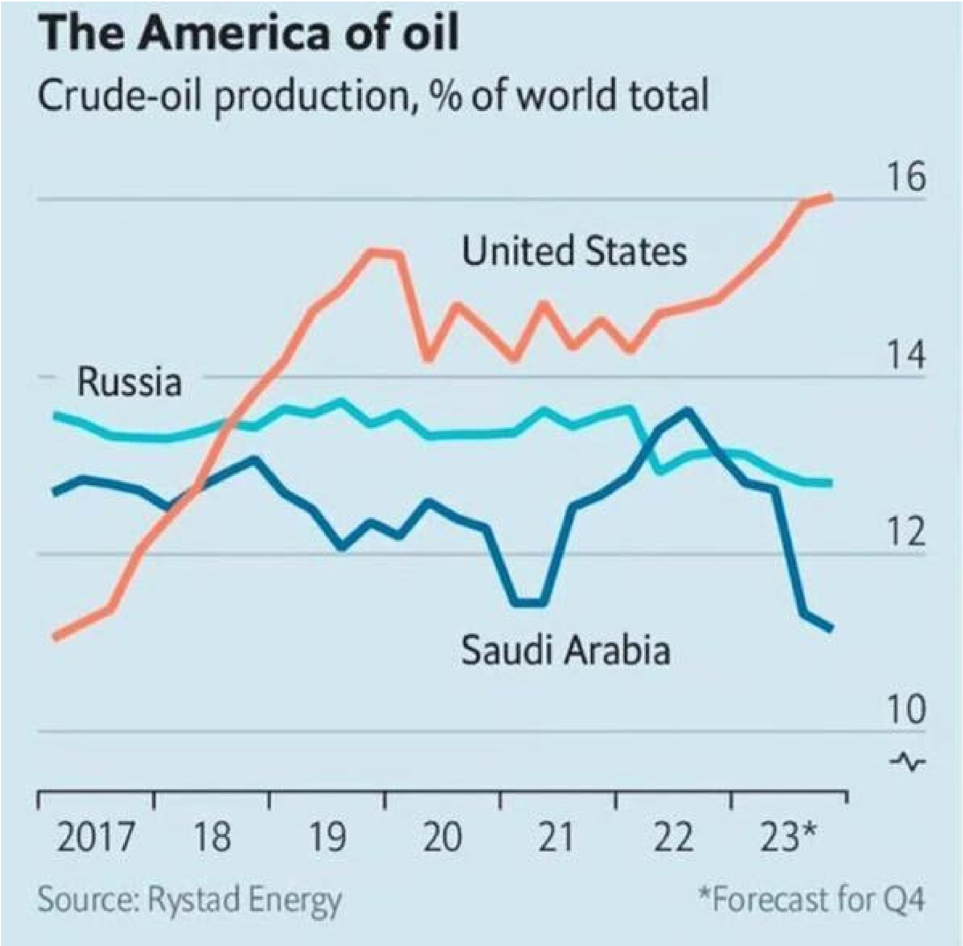
There seems to be a lot of confusion about why #oil is breaking below $70.

It's pretty simple: shale gonna shale. New record highs in US production, despite weak demand (US gasoline consumption down 2% over the last year).

Meanwhile, OPEC+ is losing cohesion on propping up the market at the expense of shale stealing their market share.

This reminds me a lot of 2014. If OPEC decides they no longer want to surrender the market to shale drillers, crude could get cut in half from here.

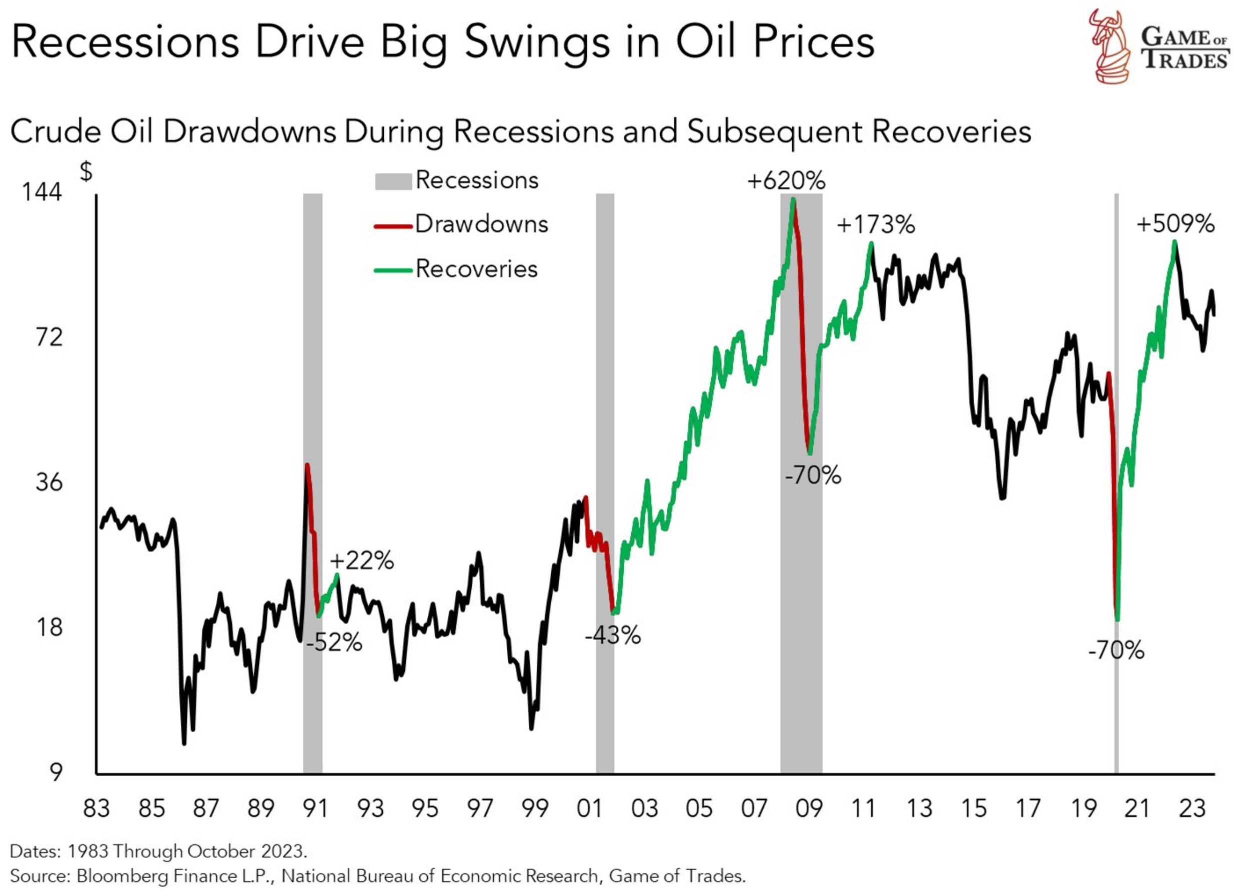
Don't shoot the messenger, just facts.



The price of oil is often extremely volatile around recessions (from Game of Trades via X)...

In a recession = oil collapses

After a recession = oil spikes



The White House's plan to refill the U.S. Strategic Petroleum Reserve (SPR) is not going well (from *Bloomberg*)...

The Biden administration may not be able to take full advantage of the recent drop in oil prices as it seeks to refill its depleted crude oil reserve, the Energy Department's No. 2 official said Monday.

The US Strategic Petroleum Reserve stands at its lowest level since the 1980s, but physical constraints and maintenance at the network of underground caverns along the US Gulf Coast have been limiting the amount the Energy Department can purchase to about 3 million barrels a month, Deputy Energy Secretary David Turk said.

"That is the physical limit of how much we can buy back," Turk said in a Bloomberg TV interview on the sidelines of the COP28 climate conference. "We hope we can bring more capacity on line at these price levels to buy as much as we can to refill. We will buy back as much as we possibly can, but there are some physical constraints."

Oil prices have posted back-to-back monthly declines as supplies from non-OPEC countries ballooned, while the outlook for demand growth has softened. West Texas Intermediate fell 0.8% Monday to $73.45 a barrel, the lowest since Nov. 16.

The more than 700-million-barrel oil reserve, constructed in the aftermath of the 1970s Arab oil embargo, currently stands at about 350 million barrels, following the Biden administration's historic 180 million barrel withdrawal to tame gasoline prices in the wake of Russia's invasion of Ukraine as well as sales mandated by Congress.

So far efforts to refill it have been at a trickle, with two of the reserve's sites in Texas and Louisiana offline for maintenance and a $1.4 billion modernization program, funded through oil sales, behind schedule and over budget.

Continue reading here (subscription may be required).

China appears to be beating the U.S. in nuclear energy technology (from Erik Townsend via X)...

EVERYONE is under-appreciating the importance of this. CHINA is in the lead on advanced nuclear energy technology. **By a lot.** Unless western governments get their shit together very soon, **China will control energy globally for the next 100 years**.

Zhao DaShuai 无条件爱国🇨🇳
@zhao_dashuai

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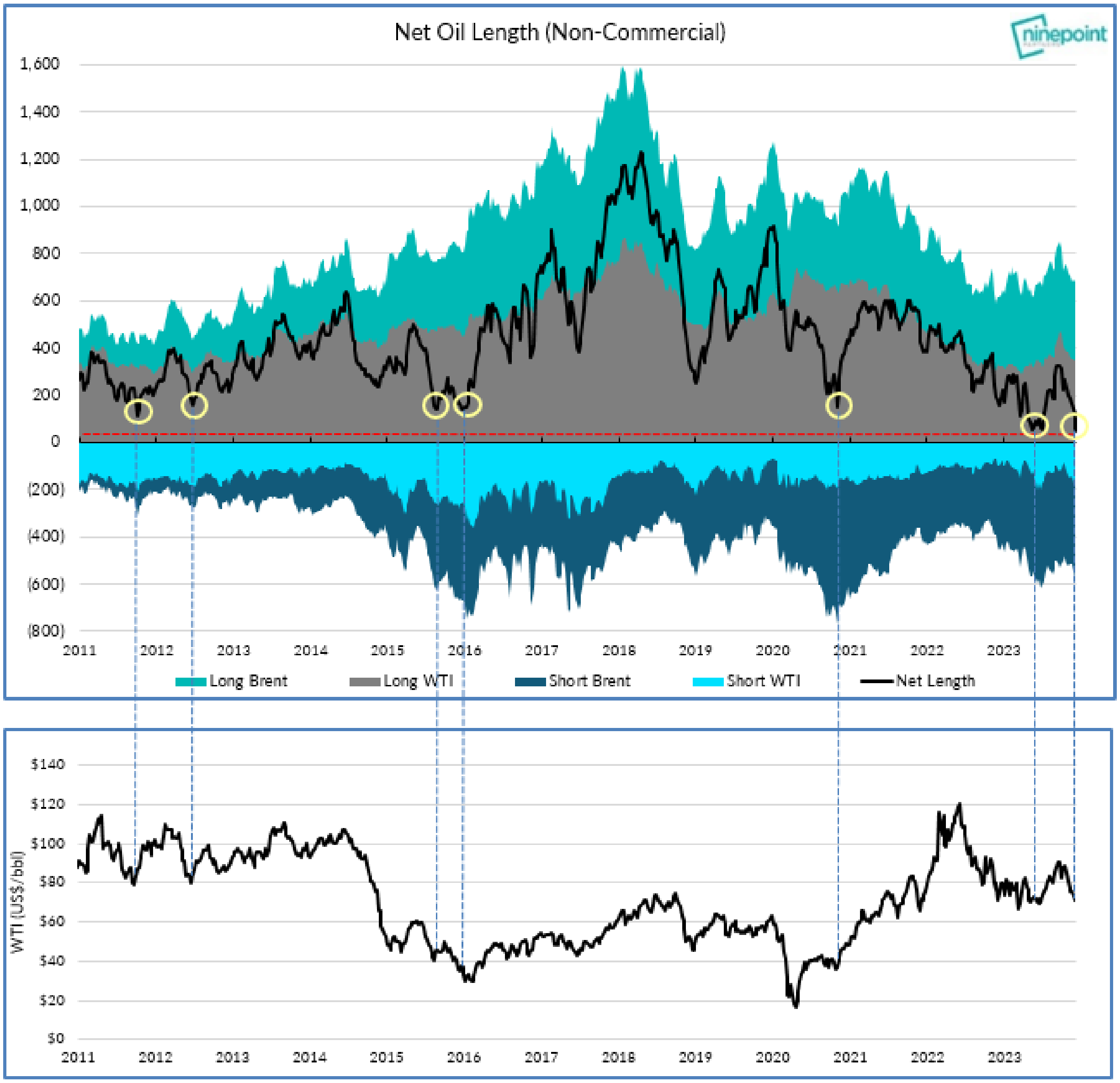
China will build nuclear powered container ships ☢️

It's powered by a Thorium Molten Salt Reactor (MSR), the significance of which is beyond shipping.

The immediate [other] application would be nuclear powered aircraft carrier.
1/3

Investor sentiment toward the oil industry is extremely bearish today (from Eric Nuttall via X)…

Sentiment has now reached its lowest level in recent history, as measured by net speculative length. Traders are now more bearish than during the COVID lockdowns that resulted in the biggest demand shock in history, and the paper market is now only net long 12 hours of oil demand! Commodities bottom when sentiment bottoms…

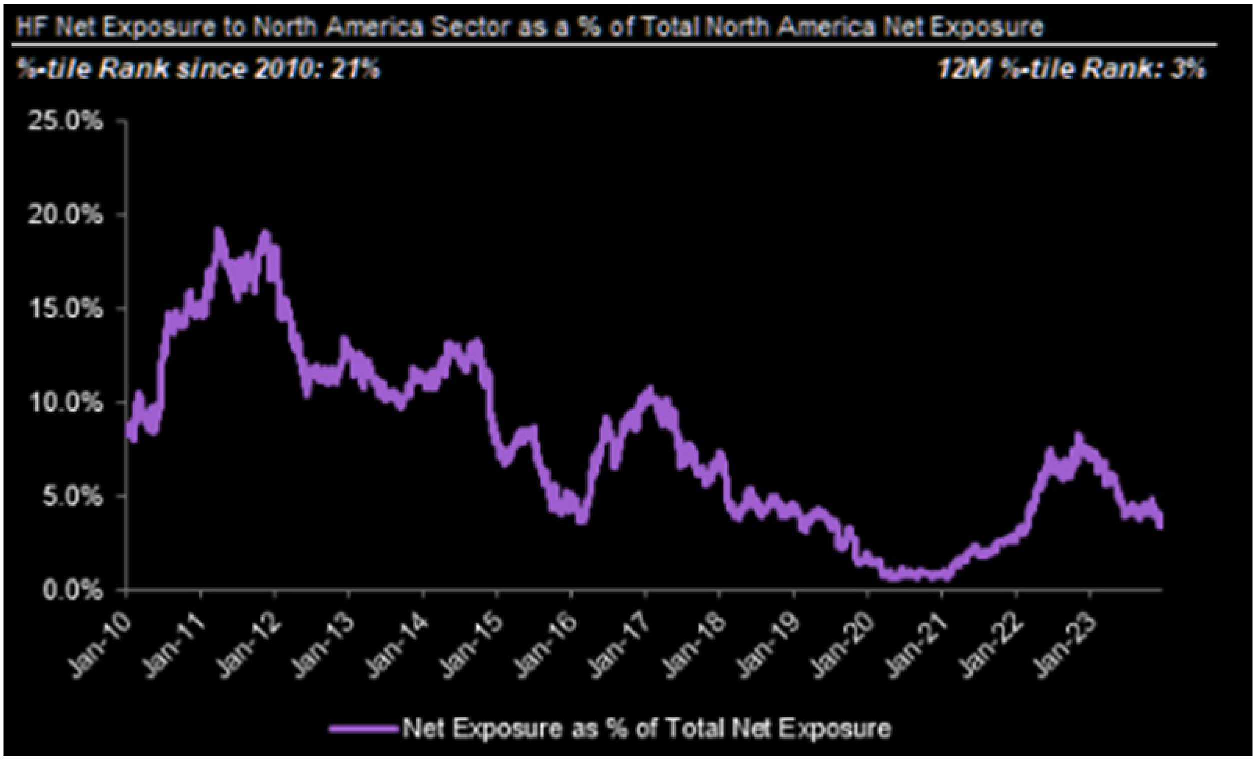


Source: Bloomberg

Despite downside risks to oil prices, the energy sector looks relatively attractive today (from Markets & Mayhem via X)...

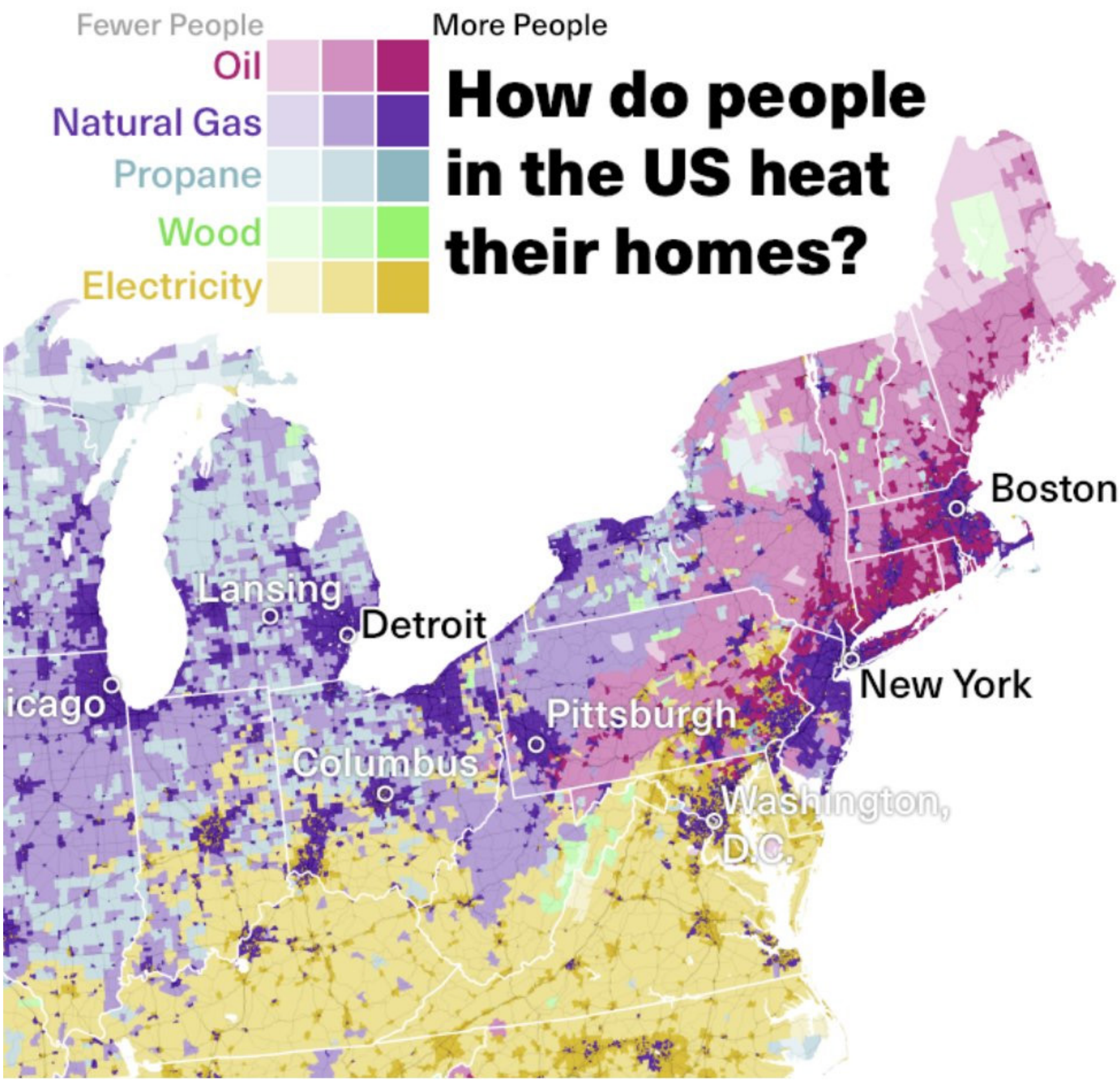
Valuations are cheap, exposure is low, and the price of oil could move higher next year.

I've been accumulating some of my favorite names in the space.



This map highlights one of our country's many energy policy failures (from John Arnold via X)...

The Northeast has fought the expansion of natural gas pipelines for decades. As a result, it is the only region in America that still heats homes using (dirty and expensive) oil despite being adjacent to one of the most prolific nat gas fields in the world.



Warren Buffett's Berkshire Hathaway continued to buy more shares of Occidental Petroleum (OXY) this month (from Energy Headline News via X)...

New Filing: Berkshire Hathaway bought 5.18 million more shares of Occidental Petroleum over the last three days.

Average purchase price of $60.22 per $OXY share for a total outlay of $312.1 million.

Berkshire now owns 27.7% of the O&G giant. $BRK.A $BRK.B

Not all the news is bearish for oil prices today (from Josh Young via X)...

Oil geopolitical risk, Red Sea + Persian Gulf edition

@calvinfroedge

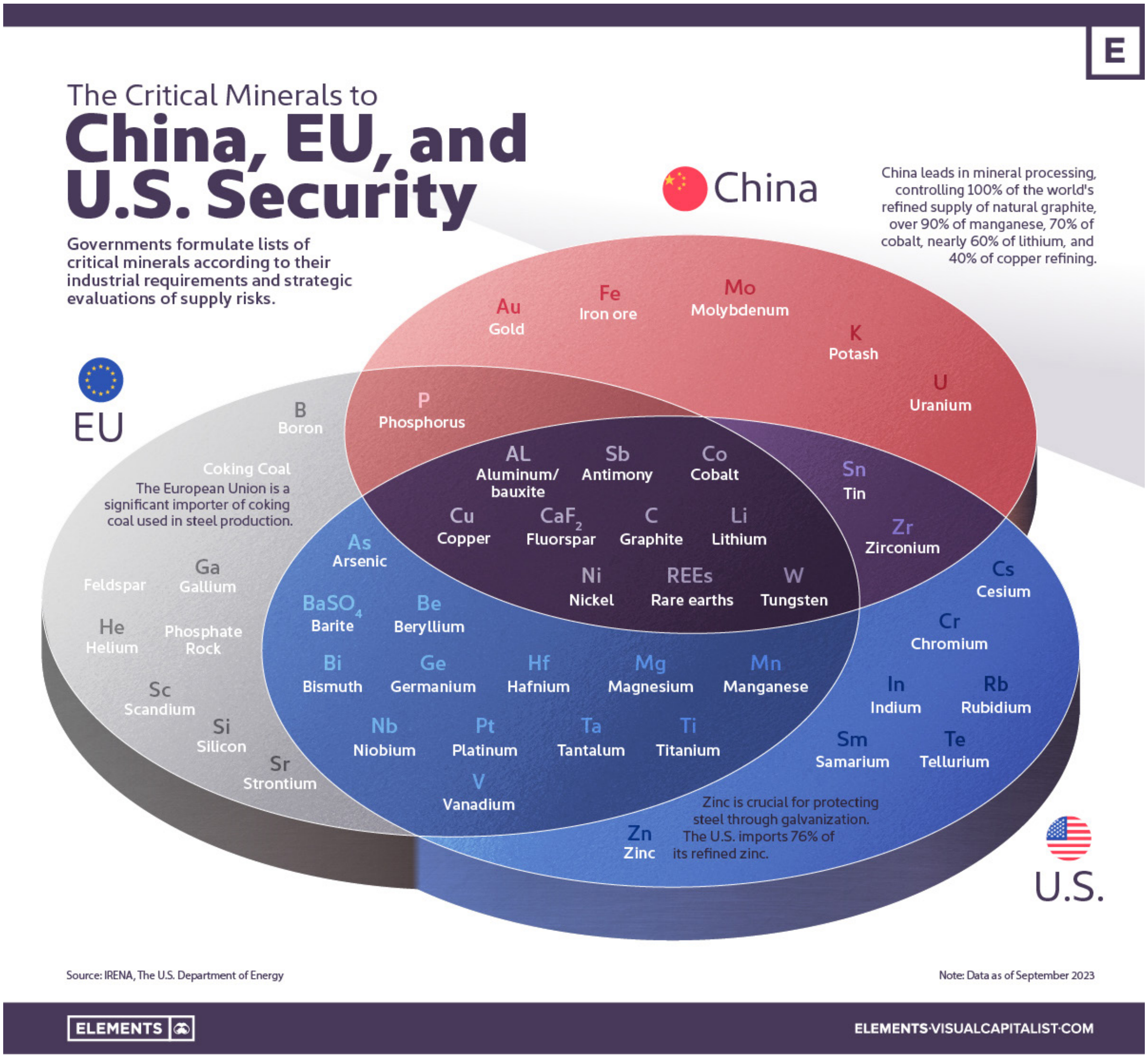
Follow

I think we may need to start considering that oil exports may be cut off via both the Red Sea and the Persian Gulf.

I expect oil markets will actually take this seriously next week. A complete shut off of this region would be catastrophic for the global economy.

OTHER COMMODITIES

These minerals are critical to national security ([from Elements by Visual Capitalist](#))...



Governments formulate lists of critical minerals according to their industrial requirements and strategic evaluations of supply risks.

Over the last decade, minerals like nickel, copper, and lithium have been on these lists and deemed essential for clean technologies like EV batteries and solar and wind power.

This graphic uses IRENA and the U.S. Department of Energy data to identify which minerals are essential to China, the United States, and the European Union.

What Are Critical Minerals?

There is no universally accepted definition of critical minerals. Countries and regions maintain lists that mirror current technology requirements and supply and demand dynamics, among other factors.

These lists are also constantly changing. For example, the EU's first critical minerals list in 2011 featured only 14 raw materials. In contrast, the 2023 version identified 34 raw materials as critical.

One thing countries share, however, is the concern that a lack of minerals could slow down the energy transition.

The Critical Minerals to China, EU, and U.S. Security

With most countries committed to reducing greenhouse gas emissions, the total mineral demand from clean energy technologies is expected to double by 2040.

Despite having most of the same materials found in the U.S. or China's list, the European list is the only one to include phosphate rock. The region has limited phosphate resources (only produced in Finland) and largely depends on imports of the material essential for manufacturing fertilizers.

Coking coal is also only on the EU list. The material is used in the manufacture of pig iron and steel. Production is currently dominated by China (58%), followed by Australia (17%), Russia (7%), and the U.S. (7%).

The U.S. has also sought to reduce its reliance on imports. Today, the country is 100% import-dependent on manganese and graphite and 76% on cobalt.

After decades of sourcing materials from other countries, the U.S. local production of raw materials has become extremely limited. For instance, there is only one operating nickel mine (primary) in the country, the Eagle Mine in Michigan. Likewise, the country only hosts one lithium source in Nevada, the Silver Peak Mine.

Continue reading here.

Here are four potential tailwinds that could push copper prices higher (from Robert Friedland via X)...

As copper rallies toward a three-month high above $3.90/lb., we're seeing the continuation of trends we identified in the past few weeks.

1/ Supply challenges

The situation in Panama continues to worsen, with the government forcing the closure of the Cobre Panama operation after banning new mining contracts, impacting approx. 1.5% of global supply.

2/ Tightening concentrate supply

Miners and Chinese smelters agree to the first drop in fees in three years.

3/ Unexpected strength in demand

Global copper demand remains robust. Over the first four months of 2023, OECD copper demand increased by a strong 3.7%. China imported 353kt of refined copper in October, the highest volume this year.

4/ Increased 'balkanization' of supply chains

US sets limits on Chinese content to receive EV tax credits under the IRA... the restrictions will include suppliers of key battery raw materials.

Copper also appears to be breaking out from a long-term consolidation pattern ([from Caleb Franzen via X](#))...

It's hard to ignore this breakout for copper from a 20-month wedge after retesting the former base from 2017 - 2020.

Copper bidding isn't congruent with a recession.

The metals and mining industry looks poised to dramatically outperform the broad market in the years ahead ([from Graddhy - Commodities TA+Cycles via X](#))...

$XME looks ready to yet again outperform $SPX up from the commodities bear market low. Above black line will see #metals & #mining sector moving very strongly I think. The 2nd inflationary wave is soon upon us.

Global fund manager positioning is sending a super bullish message about commodities today (from Otavio Costa via X)...

This is probably one of the most important charts I've seen in the last weeks.

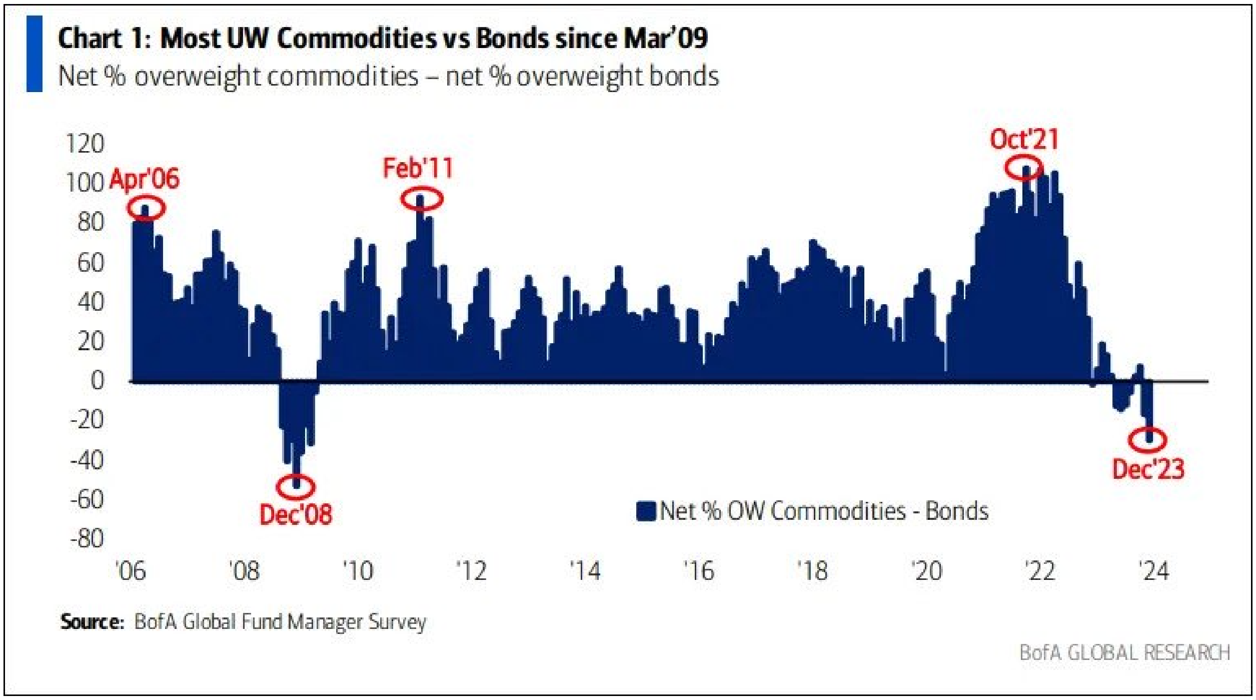
Commodities are the most underweight relative to bonds since March 2009.

It underscores the historical extremity in the valuation disparity between hard vs. financial assets.

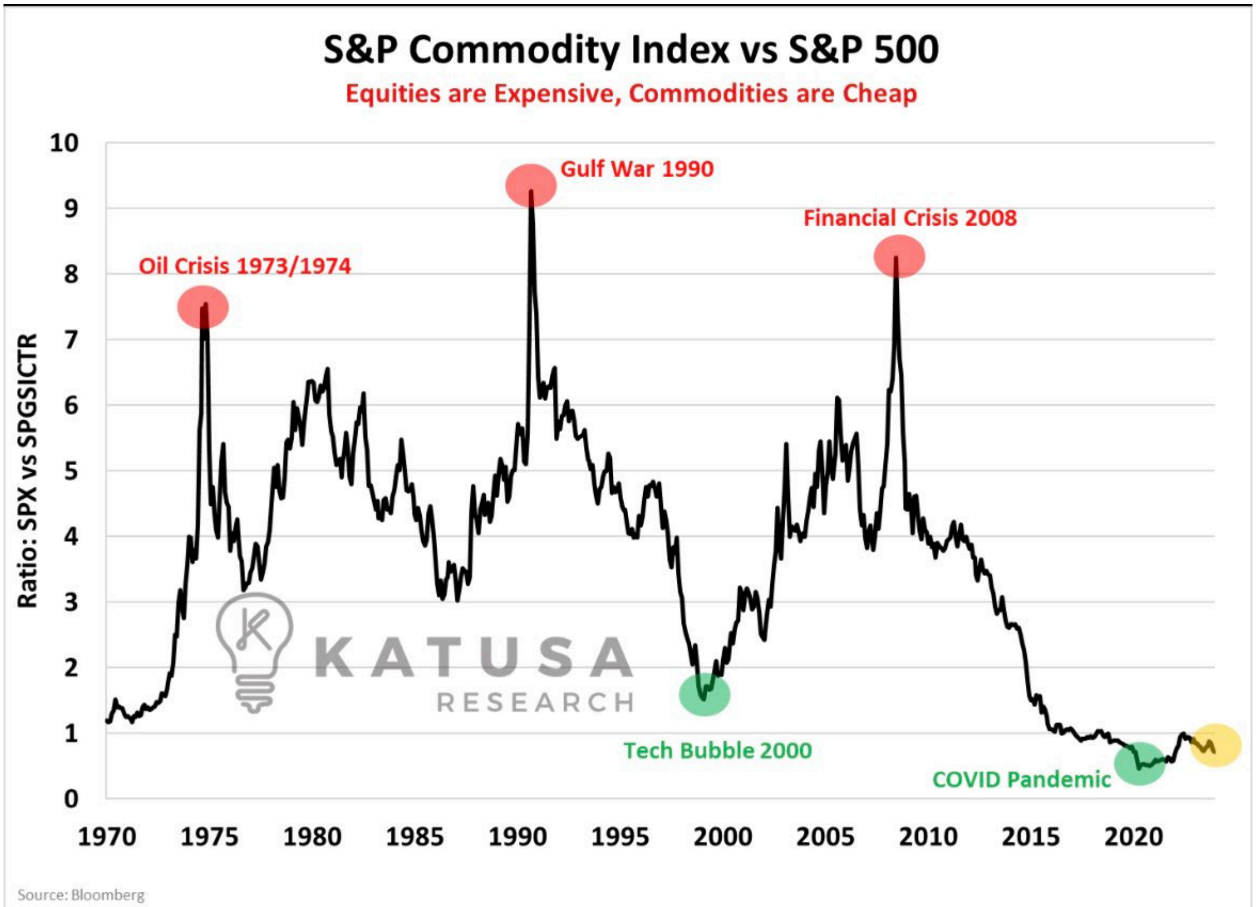
The shift back to resource industries may catch many investors off guard as valuations in crowded sectors compress.

It's worth noting that three out of the last four commodity cycles in the past 130 years coincided with inflationary periods.

Against the backdrop of deglobalization, extensive fiscal spending, and labor cost pressures, a broad increase in commodity prices would only add fuel to the inflation fire.



Commodities also appear "generationally cheap" versus stocks (from Katusa Research via X)...



BITCOIN AND CRYPTO

Is there a best time and day to buy Bitcoin for the long term? (from River Research)...

Recurring orders, often referred to as dollar-cost averaging, are a way to spread out an investment amount over time. This decreases exposure to price volatility and reduces time spent trying to time the market. It's a way to passively invest in bitcoin in the long term...

Is there a best time of the day or best day of the week to dollar-cost average bitcoin? And is there a best frequency for DCA?

Based on our research, we found that:

1. Historically, the daily high price happened within a 4-hour window 38.5% of the time, and the daily low price happened within that same 4-hour window 39.4% of the time. This pattern has shifted over time and the window has shrunk.
2. From 12-1 PM Eastern time, there is a one-hour window with over 3 times as many price bottoms than peaks in the past twelve months. This hour has a 4.37% theoretical advantage for daily recurring orders relative to any day's average.
3. Mondays have historically had the highest odds of having the weekly low price relative to the weekly high price falling on this day. This day has a 14.36% theoretical advantage for weekly recurring orders relative to any week's average.
4. The first and second days of each month have historically had the highest odds of having the lowest price relative to the monthly high price happening on those days. A monthly recurring order on these days gives a 6.83% and 3.73% theoretical advantage relative to any month's average, while on the last three days of the month, there is a 3.11%, 6.83%, and 6.21% higher chance to buy a monthly high than a monthly low.
5. Due to the variance of the exact moments when price peaks and bottoms happen, the achievable practical advantage on timing a recurring order is around 1.2%.

Continue reading here.

This chart suggests we may never see Bitcoin trade below $30,000 again (from Willy Woo via X)...

We'll probably never see BTC going below $30k again if this on-chain pattern holds true (8 for 8 so far). What you see here is #Bitcoin's price discovery across 13 yrs. It's a contour map the BTC supply according to the price HODLers paid for their coins, and how it changed over time.

DENSE HORIZONTAL BANDS:

These are price regions where much of the supply moved between investors reflecting strong agreed value.

PATTERN:

Whenever BTC had:

(a) strong bands of agreed price

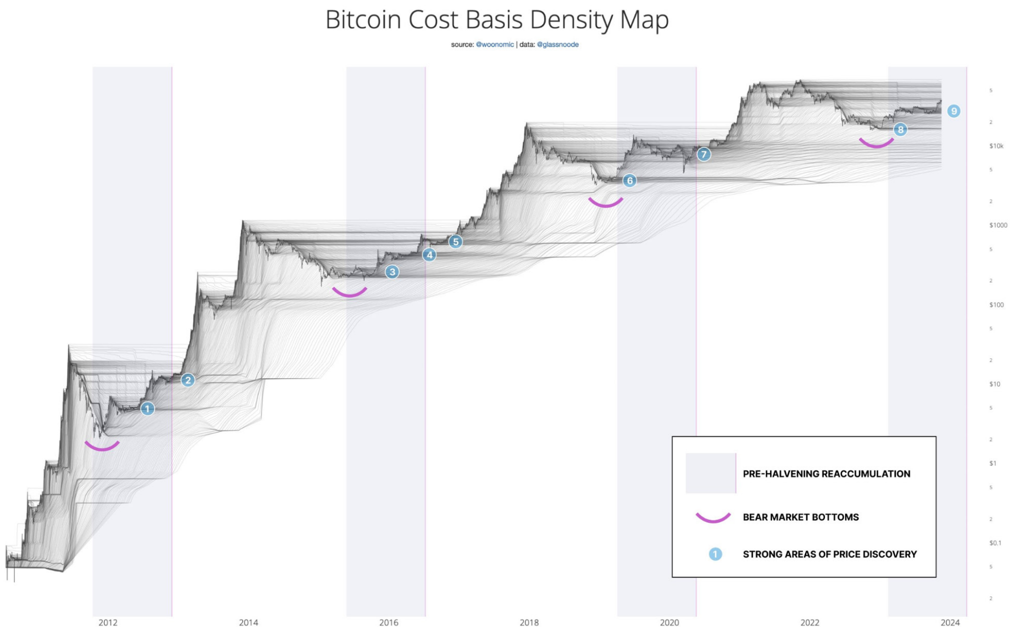
(b) coming out of a bear market

(c) and leading into the next [halving] (marked in vertical bands)

... the price never comes back to retest this band of support.

CONTEXT:

Why "up only"? #Bitcoin is far from a commodity market at saturation. What we're seeing across the 13 yrs of this chart is BTC's widespread adoption. The network had 10,000 users in 2010, today there's well over 300m people using it as a store of value technology. This is only going to climb with a spot ETF.



Twitter founder Jack Dorsey leads $6.2 million investment in a new decentralized Bitcoin mining pool (from Bitcoin Magazine Pro)...

Jack Dorsey, founder of Twitter and CEO of Block, has teamed up with several other investors to lead a round of seed funding for OCEAN, a new model of mining pool that seeks to decentralize the process, and achieved $6.2M in investment.

OCEAN is a project devised by Mummolin Inc., a Wyoming-based firm founded in 2023 by Bitcoin Core developer Luke Dashjr and others. As of yet, it's still in its earliest stages, but many of the fundamentals were outlined on November 28, when Mummolin announced the end of the seed funding round. Essentially, OCEAN will be a fundamentally decentralized mining pool, as Dashjr described it: "The role of mining pools must change for Bitcoin to exist as a truly decentralized currency. OCEAN is a new type of pool that enables miners to be truly miners again. We are launching as the most transparent pool and also the only non-custodial pool where miners are the recipients of new block rewards directly from Bitcoin."

Mining pools are a fundamental part of the Bitcoin mining ecosystem in 2023, as it has become prohibitively expensive for individual miners to have any hope of making a dent into the substantial transactions needed to create and validate bitcoins. Gone are the days that a hobbyist could have any hope of earning a few on any sort of home computer setup, now even the most rudimentary systems have substantial requirements of hardware and electricity.

So, to give these smaller miners an opportunity, there are mining pools, which allow users to pool together their resources, and get a share of the subsequent bitcoins. As OCEAN's Global Head of Sales, Bitcoin Mechanic, noted however: "Even though hashrate may be distributed globally, the reality is that the intelligent parts of mining (running a full node, sourcing transactions, constructing the block template) are performed by very few individuals and the pools that they control. This has the potential to hurt Bitcoin." In other words, all the major pools are heavily centralized, where most of the contributors are reliant on this center to actually make payouts.

Continue reading here (subscription may be required).

Bitcoin-focused tech firm MicroStrategy bought another $600 million in Bitcoin last month (from Blockworks)...

MicroStrategy continues to buy bitcoin. The company announced in an 8K filing on Thursday that it had bought roughly $593 million worth of bitcoin throughout the month of November.

From Nov. 1 to Nov. 29, the company bought 16,130 bitcoin along with its subsidiaries. The average price works out to be nearly $36,000.

The company now holds roughly 174,530 bitcoin, worth roughly $5.2 billion at a purchase price of $30,000.

Prior to the November buys, MicroStrategy disclosed a huge buy back in June when it bought 12,000 bitcoin over a span of two months at an average price of $28,136 per bitcoin.

The price of bitcoin (BTC) took a dip following the 8K disclosure, though the price is still above $37,000 at the time of publication.

Read more: Bitcoin flirts with breakout, price mirrors lead-up to 2012 halving

Back in early November, during the company's earnings call, MicroStrategy founder Michael Saylor said that the approval — then launch — of spot bitcoin ETFs would be a "catalytic event" that would benefit both his company and other entities with bitcoin exposure.

"I think we'll see more and more analyst coverage from traditional Wall Street banks as these ETPs make bitcoin exposure available," Saylor said on the earnings call. "More coverage means more education, means more awareness, and that results in more interest."

MicroStrategy would continue to allow investors to gain exposure to bitcoin through its holdings, and that's – Saylor believes – is not something that would go away if the world's largest asset manager BlackRock or any of the other entities vying for a spot bitcoin ETF get the green light from the US Securities and Exchange Commission.

While it's unclear what exactly made MicroStrategy so bullish on bitcoin in the month of November, there have been a slew of bitcoin ETF-related headlines. Additionally, the next bitcoin halving is roughly five months away – both of which have been identified as potential catalysts for positive price action.

Continue reading here.

El Salvador's Bitcoin purchases are reportedly "back in the black" today (from Nayib Bukele via X)...

El Salvador's #Bitcoin investments are in the black!

After literally thousands of articles and hit pieces that ridiculed our supposed losses, all of which were calculated based on #Bitcoin's market price at the time...

With the current #Bitcoin market price, if we were to sell our #Bitcoin, we would not only recover 100% of our investment but also make a profit of $3,620,277.13 USD (as of this moment).

Of course, we have no intention of selling; that has never been our objective. We are fully aware that the price will continue to fluctuate in the future, this doesn't affect our long-term strategy.

Nonetheless, it is important that the naysayers and the authors of those hit pieces take back their statements. The responsible thing to do would be for them to issue retractions, offer apologies, or, at the very least, acknowledge that El Salvador is now yielding a profit, just as they repeatedly reported that we were incurring losses.

If they consider themselves true journalists, they should report this new reality with the same intensity they reported the previous one. We'll see... Stay tuned!

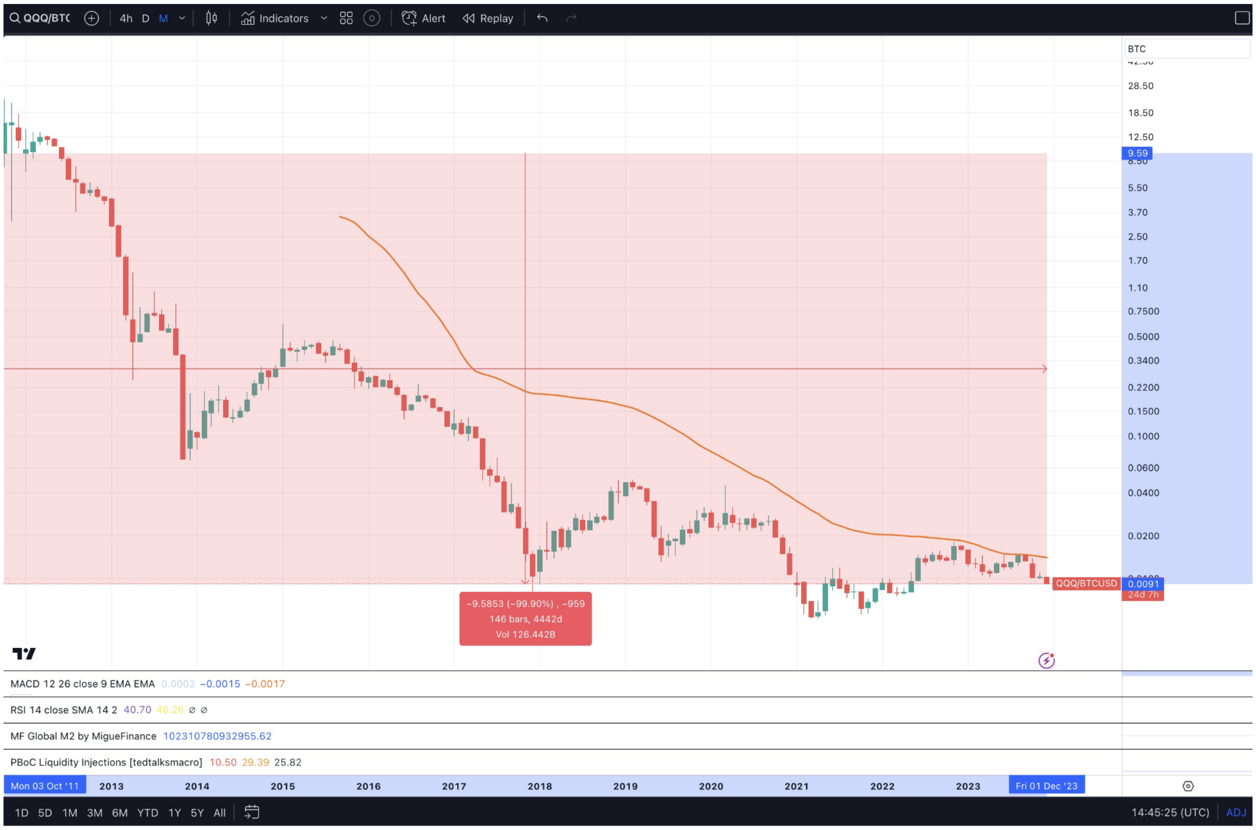
This long-term chart of the Nasdaq 100 versus Bitcoin is a must-see (from Dr. Jeff Ross via X)...

For your consideration: 👀

$QQQ is crushing it... or nah?

Relative to #bitcoin, the famous technology stock index is fairing relatively well (compared to other U.S. and international stock indices), down only -99.9% since October 2011.

Opinion: All assets trend to zero over time against bitcoin. Choose wisely.



Ten reasons the upcoming Bitcoin ETF could "change everything" (from Fred Krueger via X)...

#10. Very little money has come into Crypto since the SBF debacle in Nov 2022. Prices have climbed this year, but not based on new fiat coming in to buy BTC.

#9. Wall Street views anything down 50% from its ATH as dead. ETH is 52% from its ATH. BTC is "only" down 37%, so "almost dead". The ETF will push us much closer to where Wall Street and 10 Trillion USD of ETF money gets interested.

#8. Wall Street can't, for regulatory reasons, take massive positions held on Coinbase. They can't do self custody. They CAN buy the ETF.

#7. There are 400,000 RIAs in the US alone that advise people. They can't advise Coinbase or Self Custody. They CAN and WILL advise the ETF.

#6. Even sophisticated retail with Coinbase accounts face tax problems by buying first Bitcoin itself, then selling and rolling into the ETF. They prefer waiting.

#5. Corporate treasuries can much more easily take a small position on the ETF than deal with what MSTR and TSLA did from a governance standpoint.

#4. Many users, including myself, would prefer not dealing with keys and multisig, versus just owning the ETF. It solves the custody problem.

#3. The ETF with the imprimatur of BlackRock or Fidelity legitimizes things. 100x easier to explain to your board or your boss than "GBTC".

#2. Although the ETF doesn't explicity say Bitcoin is not a security, it implicity does at this stage.

#1. Boomers are too lazy to understand Bitcoin the asset. The ETF is a simple way to play "number go up" for an entirely new asset class.

The key point is that this a TRANSFORMATIVE event. It moves BTC into the Mainstream Financial World. It opens our favorite asset to a sales force of 400K advisers, 30+ brokerages, 100M+ investors.

This could be another massive tailwind for Bitcoin adoption in the years ahead ([from Preston Pysh via X](#))...

This is a major highlight. The FT represents the legacy narrative. If they are writing pro-bitcoin ESG material it's because the decision makers on high have finally allowed it.

I think we are about to see a lot of these shifting pro-#Bitcoin narratives happening in the coming 12 months (and not for crypto).

Daniel Batten @DSBatten

Follow ···

I just about fell off my chair.

In what is a significant shift, The Financial Times just published its first cautiously pro-Bitcoin ESG article.

Beyond COP28: A fresh look at bitcoin's ESG credentials

Could BTC be ESG? A recent rise in the price of bitcoin is reviving a debate on whether the digital currency could be considered an ESG investment. The recent growth is coming on the heels of a possible approval of a spot bitcoin ETF as early as next month.

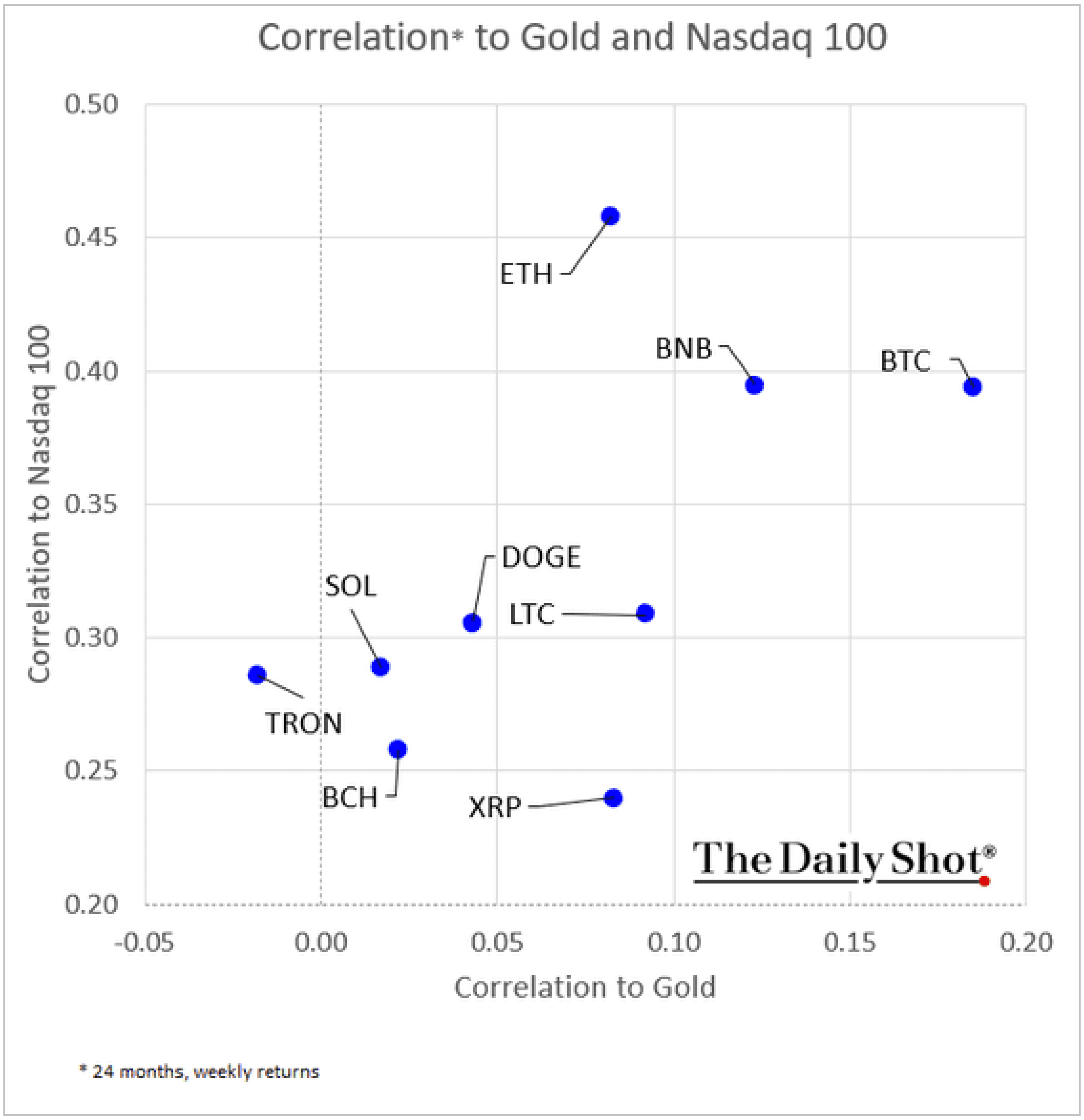
Bitcoin has often been criticised for its heavy electricity use. Yearly electricity use from bitcoin mining is 137.91 terawatt-hours, or the equivalent of the power usage of Ukraine, according to estimates by Digiconomist's Bitcoin Energy Consumption Index.

But investors such as Daniel Batten at CH4 Capital say there is potential for bitcoin to be environmentally friendly, or to push beneficial social outcomes. "Bitcoin energy consumption is high and will continue to go up. This is for certain. However, it is a mistake to say this means it is anti-ESG," he told me.

Bitcoin's large electricity usage could turn out to be a benefit in some cases, Batten argued, where it could soak up excess supply of energy generated via renewable sources such as solar or wind. A KPMG report looking at bitcoin and ESG notes potential social benefits, too. The cryptocurrency could allow previously unprofitable, small electrical grids linked to local renewable energy to become "financially viable" in developing countries and in turn improve electricity access, it said.

Of course, prices of bitcoin and other cryptocurrencies are volatile and pose significant regulatory risks. This was especially notable following the downfall of cryptocurrency platform FTX and more recently, Binance founder Changpeng Zhao pleading guilty to money laundering. It may be a long road ahead before bitcoin establishes itself as an ESG asset. (*Kaori Yoshida, Nikkei*)

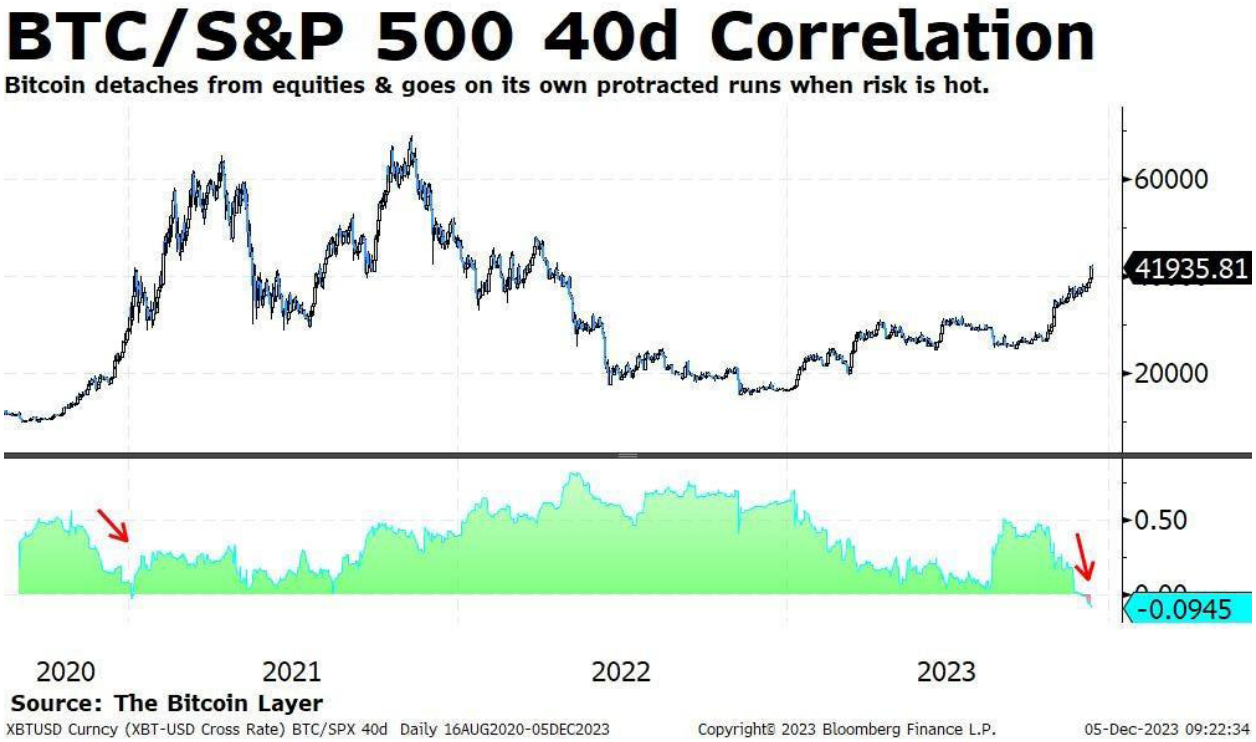
Data show Ethereum (ETH) has the highest correlation to stocks among major cryptocurrencies, while Bitcoin (BTC) has the highest correlation to gold ([from The Daily Shot](#))...



This super-bullish signal hasn't appeared since Bitcoin's 2020 bull market rally (from The Bitcoin Layer)...

Bitcoin is up 57% over the past two months since rumors of imminent spot bitcoin ETF approval began swirling. Up 172% from its cycle bottom this time last year, it crossed $42,000 on Sunday in a dominant move that feels like we never left these levels in the first place:

To further illustrate the magnitude of this rally, this is the first time since the beginning of the 2020 bull run that bitcoin's 40-day correlation with the S&P 500 flipped negative—a hallmark of BTC when it's trouncing traditional risk assets:



[Continue reading here (subscription may be required)].

Options traders are betting the recent Bitcoin rally continues (*from Bloomberg*)...

Options traders are loading up on bets that Bitcoin will surge to $50,000 by January, when many market observers expect the SEC to finally allow exchange-traded funds to directly hold the cryptocurrency.

That's the price level with the largest open interest, or the total amount of outstanding contracts, to buy Bitcoin with call options that expire Jan. 26, according to data compiled by Deribit, the largest crypto options exchange. Calls give the buyer of the contracts the right to purchase the underlying asset at a specific price within a set time period.

Bitcoin last reached $50,000 in December 2021. Digital assets were then in the midst of retreating from all-time highs with the Federal Reserve beginning to remove the record amount of stimulus added during the Covid pandemic. Now with expectations that the Fed is going to pivot on monetary policy next year and a Bitcoin ETF seen as almost a sure thing, the crypto sector is staging an eye-popping rebound.

"The bullish sentiment is thriving," said Luuk Strijers, Deribit's chief commercial officer.

Bitcoin has surged more than 60% since the middle of October, when speculation jumped that the Securities and Exchange Commission was on the verge of signing off on ETF applications from the likes of asset management powerhouse BlackRock.

Continue reading here (subscription may be required).

Despite its big rally this year, Bitcoin still appears to be "cheap" (from Dan Morehead via X)...

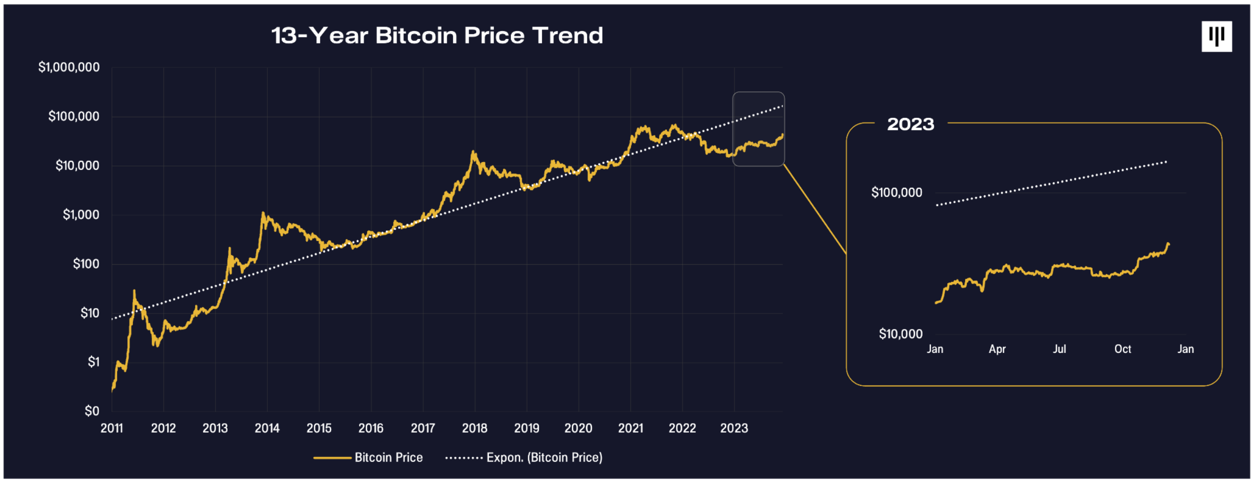
I can imagine an investor thinking: "Bitcoin is up 162% this year. Well, I missed it." and giving up.

No. That's the wrong mindset.

It's up almost that much EVERY year (on average). The 13-year trend growth rate is 117%.

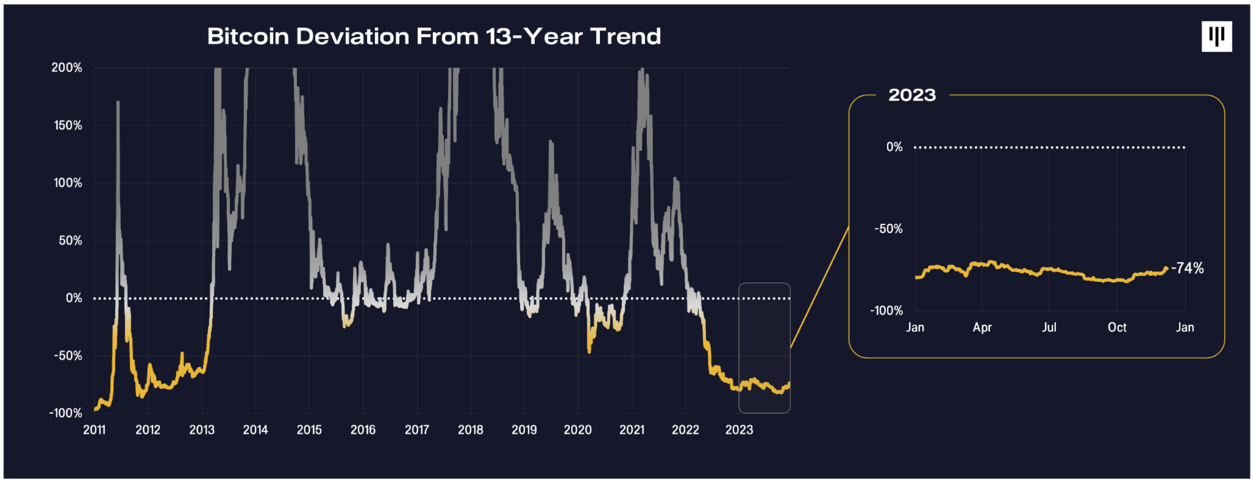
Bitcoin, as a proxy for our industry, is still very cheap relative to its 13-year exponential trend.

Zooming into the graph of the log trend of bitcoin you can see that the rally in 2023 is just normal – the gold line has barely outpaced the 13-year trend.



So, even the rally we're experiencing isn't doing much to change the relative undervaluation of bitcoin.

Here's a graph of the deviation of bitcoin from its 13-year trend growth rate. Even after the rally it's still 74% cheap to the trend.



It's only spent 13% of the last 13 years at that level or cheaper.

What you should know about the Financial Accounting Standards Board's recent rule change for Bitcoin (from Swan Bitcoin)...

This [month], FASB officially adopted Fair Value Accounting rules for Bitcoin beginning after December 15th, 2024.

The amendments in the ASU improve the accounting for certain crypto assets by requiring an entity to measure those crypto assets at fair value each reporting period with changes in fair value recognized in net income. The amendments also improve the information provided to investors about an entity's crypto asset holdings by requiring disclosure about significant holdings, contractual sale restrictions, and changes during the reporting period.

The amendments in the ASU apply to all assets that meet all the following criteria:

1. Meet the definition of intangible asset as defined in the *FASB Accounting Standards Codification®*
2. Do not provide the asset holder with enforceable rights to or claims on underlying goods, services, or other assets
3. Are created or reside on a distributed ledger based on blockchain or similar technology
4. Are secured through cryptography
5. Are fungible
6. Are not created or issued by the reporting entity or its related parties.

The amendments in the ASU are effective for all entities for fiscal years beginning after December 15, 2024, including interim periods within those fiscal years. Early adoption is permitted for both interim and annual financial statements that have not yet been issued (or made available for issuance). If amendments are adopted in an interim period, they must be adopted as of the beginning of the fiscal year that includes that interim period.

Source: FASB

Up until this point, corporations faced a challenge when attempting to put Bitcoin on its balance sheet due to the way Bitcoin was treated on balance sheets.

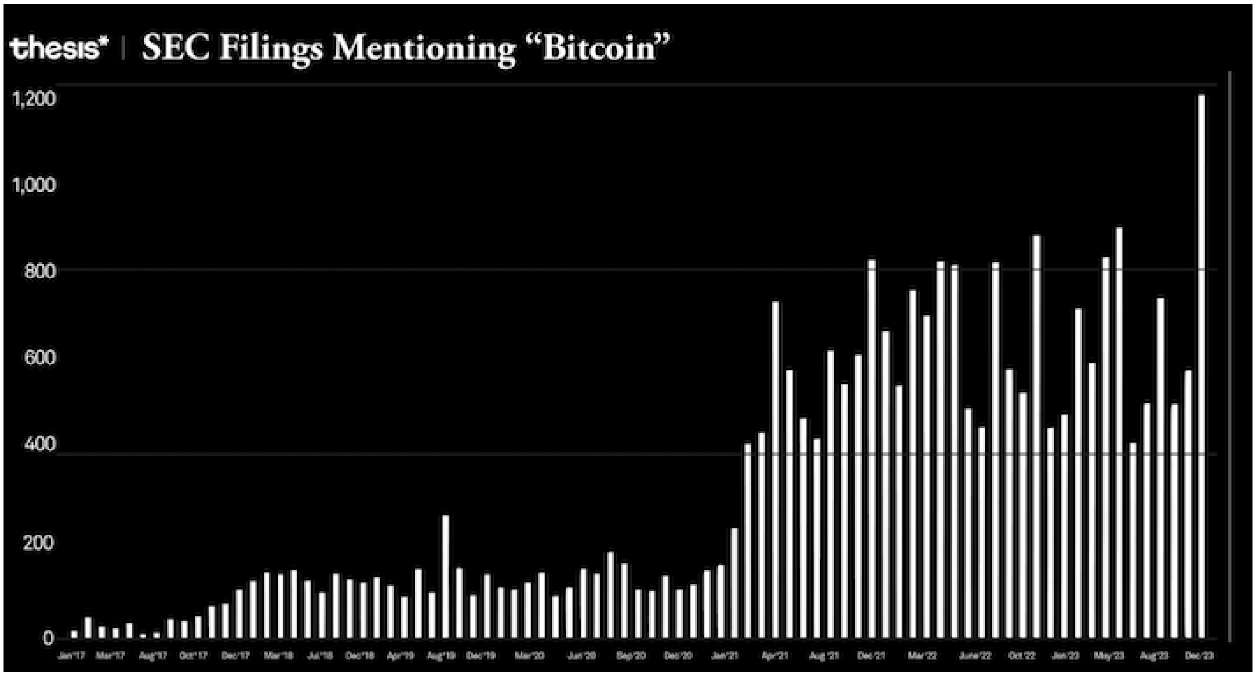
Corporations need to classify Bitcoin as an intangible asset, which means If the price of Bitcoin goes down, they have to mark the value lower on their balance sheet, and if the price goes up, they can't record the gain unless they sell the bitcoin

This creates a huge balance sheet impairment for these companies if the price of bitcoin drops. It creates a situation where a company has to potentially list the bitcoin on its balance sheet at a lower value than the current market price when it is simply holding it.

This accounting upgrade will help facilitate the adoption of Bitcoin as a treasury reserve asset at the corporate level. Industry leaders such as Former PayPal President and Lightspark CEO, David Marcus took to X to point out the significance of the rule change.

This accounting rule change comes as this recent Bitcoin rally appears to be on the radar of corporations.

In November, there were over 1,000 mentions of Bitcoin in SEC filings, an over 30% increase from the same month last year.



This is an over 30% increase from the high made last May. Corporations are paying attention, and it is about to get a whole lot easier for them to put Bitcoin on their balance sheets.

Why the upcoming Bitcoin ETF approval may not be a "sell the news" event (from Mike Alfred via X)...

The only reason Bitcoin is not already trading at $60,000-$80,000 now is because there is a 1.3% chance the spot ETF is not approved in January.

Once this slight doubt is extinguished on approval day, BTC will absolutely rip higher.

The kid analysts and traders who say this is a sell the news event have no idea how the institutional investment business works.

Godspeed.

NOTABLE INSTITUTIONAL BUYING

From SEC Form 13F Filings by Top Investment Managers and Concentrated Hedge Funds This Month

Institution or Fund	Manager	Date of Filing	Stock Purchased/Sold	Ticker	Shares Owned	Value of Holdings	% of Portfolio	Change in Shares	% Change in Shares	Average Transaction Price	Purchase Value
Decheng Capital Management III	Jessie Qiu	11/29/2023	Alpine Immune Sciences	ALPN	6,708,288	$76,809,898	25.63%	6,708,288	New	$11.45	$76,809,898
Decheng Capital Management III	Jessie Qiu	11/29/2023	Roivant Sciences	ROIV	1,459,700	$17,049,296	5.69%	1,459,700	New	$11.68	$17,049,296
Decheng Capital Management III	Jessie Qiu	11/29/2023	Aura Biosciences	AURA	1,163,123	$18,243,928	6.09%	869,790	296.52%	$15.69	$13,642,913
Euclidean Capital	Joseph Cosmai	12/1/2023	SPDR Gold Shares	GLD	1,062,500	$182,165,625	39.74%	507,500	91.44%	$171.45	$87,010,875
Chai Trust Co	Philip Tinkler	12/4/2023	Equity Lifestyle Properties	ELS	9,055,685	$576,937,691	43.07%	102,696	1.15%	$63.71	$6,542,762
RR Advisors	Robert Raymond	12/5/2023	Targa Resources	TRGP	773,000	$66,255,000	11.46%	31,000	4.18%	$85.71	$2,657,057
RR Advisors	Robert Raymond	12/5/2023	Antero Midstream	AM	6,076,000	$72,785,000	12.59%	169,000	2.86%	$11.98	$2,024,468
RR Advisors	Robert Raymond	12/5/2023	Genesis Energy	GEL	5,232,000	$53,990,000	9.34%	119,000	2.33%	$10.32	$1,227,984
Tegean Capital Management	Matthew Adonnino	12/6/2023	Qualcomm	QCOM	50,000	$5,553,000	5.85%	50,000	New	$111.06	$5,553,000
Tegean Capital Management	Matthew Adonnino	12/6/2023	Citigroup	C	300,000	$12,339,000	12.99%	75,000	33.33%	$41.13	$3,084,750
Tegean Capital Management	Matthew Adonnino	12/6/2023	Coherent	COHR	175,000	$5,712,000	6.01%	65,000	59.09%	$32.64	$2,121,600
Tegean Capital Management	Matthew Adonnino	12/6/2023	Newmont	NEM	150,000	$5,542,500	5.84%	50,000	50.00%	$36.95	$1,847,500
Tegean Capital Management	Matthew Adonnino	12/6/2023	Warner Bros Discovery	WBD	800,000	$8,688,000	9.15%	78,300	10.85%	$10.86	$850,338
Sylebra Capital	Matthew Whitehead	12/8/2023	Elastic NV	ESTC	3,924,450	$318,822,318	16.94%	3,924,450	New	$81.24	$318,822,318
Sylebra Capital	Matthew Whitehead	12/8/2023	RingCentral	RNG	8,183,003	$242,462,379	12.88%	8,183,003	New	$29.63	$242,462,379
Sylebra Capital	Matthew Whitehead	12/8/2023	Advanced Micro Devices	AMD	2,213,249	$227,566,262	12.09%	2,213,249	New	$102.82	$227,566,262
Sylebra Capital	Matthew Whitehead	12/8/2023	Impinj	PI	3,948,566	$217,289,587	11.55%	3,948,566	New	$55.03	$217,289,587
Sylebra Capital	Matthew Whitehead	12/8/2023	Purecycle Technologies	PCT	29,193,256	$163,774,166	8.70%	29,193,256	New	$5.61	$163,774,166
Sylebra Capital	Matthew Whitehead	12/8/2023	Five9	FIVN	2,013,488	$129,467,278	6.88%	2,013,488	New	$64.30	$129,467,278
Stadium Capital Management	Alexander Seaver	12/15/2023	Sleep Number	SNBR	2,002,227	$49,234,762	40.73%	1,303,001	186.35%	$24.59	$32,040,795
Stadium Capital Management	Alexander Seaver	12/15/2023	GoDaddy	GDDY	396,291	$29,515,754	24.42%	63,940	19.24%	$74.48	$4,762,251
SC US (TTGP)	Roelof Botha	12/20/2023	Maplebear	CART	39,760,537	$1,180,490,344	10.88%	39,760,537	New	$29.69	$1,180,490,344
SC US (TTGP)	Roelof Botha	12/20/2023	PDD Holdings	PDD	14,447,097	$1,416,826,803	13.05%	11,262,075	353.59%	$98.07	$1,104,471,695

NOTABLE INSIDER BUYING

From SEC Form 4 Filings by Top Executives and 10% Owners This Month

Stock Purchased/Sold	Ticker	Total Buy Value	Total Sell Value	Total Buy Filings	Total Sell Filings
OCCIDENTAL PETROLEUM CORP	OXY	$900,767,200	$0	2	0
DOLLAR TREE INC.	DLTR	$99,281,880	$0	1	0
BlackRock ESG Capital Allocation Term Trust	ECAT	$54,180,487	$0	10	0
BlackRock Innovation & Growth Term Trust	BIGZ	$49,666,652	$0	9	0
BlackRock Health Sciences Term Trust	BMEZ	$41,634,443	$0	9	0
MADRIGAL PHARMACEUTICALS INC.	MDGL	$30,065,192	$0	2	0
Howard Hughes Holdings Inc.	HHH	$24,052,913	$30,280	4	1
BlackRock Capital Allocation Term Trust	BCAT	$20,842,092	$0	7	0
Verve Therapeutics Inc.	VERV	$18,000,000	$6,343	1	1
STAAR SURGICAL CO	STAA	$13,729,960	$0	2	0
EyePoint Pharmaceuticals Inc.	EYPT	$51,874,147	$39,436,472	2	3
Liquidia Corp	LQDA	$11,000,001	$0	3	0
SHOE CARNIVAL INC	SCVL	$10,391,080	$0	2	0
Verrica Pharmaceuticals Inc.	VRCA	$10,197,908	$0	2	0
EMPIRE PETROLEUM CORP	EP	$10,054,656	$0	1	0
RumbleOn Inc.	RMBL	$9,469,042	$0	2	0
Pulse Biosciences Inc.	PLSE	$9,422,299	$0	11	0
ASA Gold Precious Metals Ltd	ASA	$9,278,150	$0	8	0
MERCURY SYSTEMS INC	MRCY	$8,229,418	$0	1	0
Hartford Schroders Private Opportunities Fund	XHFIX	$8,000,000	$0	2	0
Citi Trends Inc	CTRN	$8,128,879	$286,320	3	1
Olema Pharmaceuticals Inc.	OLMA	$8,031,280	$314,250	2	1
Elicio Therapeutics Inc.	ELTX	$7,047,530	$0	1	0
NUVEEN NEW JERSEY QUALITY MUNICIPAL INCOME FUND	NXJ	$5,738,634	$0	7	0
Cibus Inc.	CBUS	$5,470,992	$0	1	0
Wave Life Sciences Ltd.	WVE	$5,000,000	$0	1	0
OCULAR THERAPEUTIX INC	OCUL	$4,999,998	$0	1	0
ClearBridge MLP & Midstream Fund Inc.	CEM	$4,872,998	$0	4	0
HEARTLAND EXPRESS INC	HTLD	$4,695,593	$0	4	0
Astria Therapeutics Inc.	ATXS	$4,588,000	$0	1	0
ClearBridge Energy Midstream Opportunity Fund Inc.	EMO	$4,213,947	$0	4	0
Anterix Inc.	ATEX	$4,069,683	$0	1	0
Federated Hermes Premier Municipal Income Fund	FMN	$4,051,670	$0	6	0
Syros Pharmaceuticals Inc.	SYRS	$3,999,998	$0	1	0
TMT Acquisition Corp.	TMTC	$3,700,000	$0	1	0
Y-mAbs Therapeutics Inc.	YMAB	$3,530,829	$0	8	0
DIRTT ENVIRONMENTAL SOLUTIONS LTD	DRTTF	$3,401,256	$0	2	0
Lovesac Co	LOVE	$3,864,294	$469,213	1	1
Aimei Health Technology Co. Ltd.	AFJK	$3,320,000	$0	1	0
IGM Biosciences Inc.	IGMS	$3,431,464	$115,086	1	3
PIMCO Flexible Real Estate Income Fund	REFLX	$3,100,000	$0	1	0
Akero Therapeutics Inc.	AKRO	$3,677,505	$586,450	2	3
NUVEEN PENNSYLVANIA QUALITY MUNICIPAL INCOME FUND	NQP	$3,037,302	$0	8	0
Invesco Trust for Investment Grade New York Municipals	VTN	$3,026,854	$0	7	0

Stock Purchased/Sold	Ticker	Total Buy Value	Total Sell Value	Total Buy Filings	Total Sell Filings
Mallinckrodt plc	MNKTQ	$2,812,500	$0	1	0
Spectrum Brands Holdings Inc.	SPB	$2,668,700	$0	1	0
ClearBridge MLP & Midstream Total Return Fund Inc.	CTR	$2,584,205	$0	4	0
Biglari Holdings Inc.	BH	$2,530,320	$0	2	0
DWS STRATEGIC MUNICIPAL INCOME TRUST	KSM	$2,355,541	$0	5	0
PIONEER MUNICIPAL HIGH INCOME FUND INC.	MHI	$2,328,668	$0	5	0
Sight Sciences Inc.	SGHT	$2,258,429	$0	2	0
MINIM INC.	MINM	$2,244,896	$0	2	0
Invesco Pennsylvania Value Municipal Income Trust	VPV	$2,199,195	$0	8	0
HighPeak Energy Inc.	HPK	$2,162,827	$52,334	1	1
Beyond Air Inc.	XAIR	$2,088,797	$0	2	0
Allied Gaming & Entertainment Inc.	AGAE	$2,036,985	$0	3	0
Chavant Capital Acquisition Corp.	MOBX	$1,997,370	$0	1	0
Ryman Hospitality Properties Inc.	RHP	$2,040,633	$151,287	1	1
Erasca Inc.	ERAS	$1,764,444	$0	3	0
TILLY'S INC.	TLYS	$1,712,876	$48,891	3	1
Lazydays Holdings Inc.	LAZY	$1,656,864	$0	3	0
EATON VANCE CALIFORNIA MUNICIPAL BOND FUND	EVM	$1,574,620	$0	7	0
BLACKROCK CALIFORNIA MUNICIPAL INCOME TRUST	BFZ	$1,537,354	$0	3	0
Nextracker Inc.	NXT	$1,498,823	$0	1	0
UNIFI INC	UFI	$2,875,000	$1,539,113	1	1
MERRIMACK PHARMACEUTICALS INC	MACK	$1,298,472	$0	1	0
EATON VANCE CALIFORNIA MUNICIPAL INCOME TRUST	CEV	$1,285,374	$0	6	0
System1 Inc.	SST	$1,249,600	$0	1	0
SCIENTIFIC INDUSTRIES INC	SCND	$1,200,000	$0	1	0
Globalstar Inc.	GSAT	$1,264,175	$116,250	1	1
MainStay CBRE Global Infrastructure Megatrends Term Fund	MEGI	$1,129,470	$0	3	0
TILE SHOP HOLDINGS INC.	TTSH	$1,116,676	$0	4	0
DORCHESTER MINERALS L.P.	DMLP	$1,097,571	$0	3	0
AGREE REALTY CORP	ADC	$1,091,588	$0	4	0
LESAKA TECHNOLOGIES INC	LSAK	$1,064,171	$0	1	0
OmniAb Inc.	OABI	$1,010,000	$0	1	0
Calamos Long/Short Equity & Dynamic Income Trust	CPZ	$998,242	$0	4	0
GLOBAL PARTNERS LP	GLP	$993,140	$0	2	0
UNIVERSAL ELECTRONICS INC	UEIC	$990,918	$0	2	0
Generation Bio Co.	GBIO	$778,895	$0	5	0
UNION PACIFIC CORP	UNP	$999,007	$235,000	1	1
Kayne Anderson Energy Infrastructure Fund Inc.	KYN	$716,604	$0	2	0
CareCloud Inc.	CCLD	$662,594	$0	2	0
Energy Transfer LP	ET	$659,500	$0	1	0
EATON VANCE NEW YORK MUNICIPAL BOND FUND	ENX	$616,531	$0	6	0
BLACKROCK MUNIYIELD PENNSYLVANIA QUALITY FUND	MPA	$616,220	$0	5	0
First Trust Intermediate Duration Preferred & Income Fund	FPF	$603,405	$0	4	0
National Storage Affiliates Trust	NSA	$596,450	$0	2	0
BNY MELLON MUNICIPAL INCOME INC.	DMF	$592,714	$0	8	0
Chewy Inc.	CHWY	$550,511	$0	2	0
Sezzle Inc.	SEZL	$540,779	$0	5	0
ARBOR REALTY TRUST INC	ABR	$539,725	$0	2	0
Guggenheim Active Allocation Fund	GUG	$525,200	$0	7	0
Hillenbrand Inc.	HI	$523,529	$0	4	0
SinglePoint Inc.	SING	$500,000	$0	1	0
Heritage Insurance Holdings Inc.	HRTG	$499,986	$0	2	0
Black Stone Minerals L.P.	BSM	$497,232	$0	1	0
Grindr Inc.	GRND	$472,418	$0	2	0
SURO CAPITAL CORP.	SSSS	$470,478	$0	4	0
Qorvo Inc.	QRVO	$465,950	$0	1	0

Stock Purchased/Sold	Ticker	Total Buy Value	Total Sell Value	Total Buy Filings	Total Sell Filings
Westrock Coffee Co	WEST	$464,300	$0	4	0
Kimbell Royalty Partners LP	KRP	$460,856	$0	1	0
CVD EQUIPMENT CORP	CVV	$448,366	$0	1	0
Texas Community Bancshares Inc.	TCBS	$444,455	$0	2	0
CYANOTECH CORP	CYAN	$435,510	$0	2	0
PIONEER MUNICIPAL HIGH INCOME ADVANTAGE FUND INC.	MAV	$427,574	$0	5	0
Matador Resources Co	MTDR	$425,101	$0	6	0
TRIMBLE INC.	TRMB	$465,864	$48,100	1	1
Marpai Inc.	MRAI	$415,901	$0	3	0
B. Riley Financial Inc.	RILY	$404,392	$0	1	0
Elys Game Technology Corp.	ELYS	$381,710	$0	3	0
SR Bancorp Inc.	SRBK	$360,850	$0	3	0
Trinseo PLC	TSE	$360,500	$0	1	0
Crescent Energy Co	CRGY	$353,455	$0	3	0
AMREP CORP.	AXR	$344,146	$0	7	0
Burke & Herbert Financial Services Corp.	BHRB	$331,990	$0	3	0
CSP INC	CSPI	$329,767	$0	1	0
RE/MAX Holdings Inc.	RMAX	$324,807	$0	1	0
FIRST BUSEY CORP	BUSE	$552,372	$231,806	2	2
Southland Holdings Inc.	SLND	$315,755	$0	8	0
AMTECH SYSTEMS INC	ASYS	$314,760	$0	2	0
DENTSPLY SIRONA Inc.	XRAY	$314,400	$0	1	0
GoodRx Holdings Inc.	GDRX	$305,229	$0	2	0
Yoshiharu Global Co.	YOSH	$302,400	$0	1	0
Electromed Inc.	ELMD	$302,369	$0	1	0
NXG NextGen Infrastructure Income Fund	NXG	$300,375	$0	1	0
ULTRALIFE CORP	ULBI	$291,595	$0	2	0
FLOTEK INDUSTRIES INC	FTK	$286,529	$0	3	0
KEMPER Corp	KMPR	$277,758	$0	3	0
Cytosorbents Corp	CTSO	$275,001	$0	7	0
RANGE IMPACT INC.	RNGE	$267,080	$0	3	0
Immix Biopharma Inc.	IMMX	$266,919	$0	1	0
3D SYSTEMS CORP	DDD	$265,000	$0	1	0
Nuveen Core Plus Impact Fund	NPCT	$253,822	$0	1	0
agilon health inc.	AGL	$250,206	$0	1	0
BALL Corp	BALL	$249,976	$0	1	0
HUBBELL INC	HUBB	$249,860	$0	1	0
BRISTOL MYERS SQUIBB CO	BMY	$249,609	$0	2	0
CHART INDUSTRIES INC	GTLS	$248,116	$0	3	0
ILLINOIS TOOL WORKS INC	ITW	$241,790	$0	1	0
FLOWERS FOODS INC	FLO	$240,134	$0	2	0
AB INTERNATIONAL GROUP CORP.	ABQQ	$234,880	$0	3	0
OPAL Fuels Inc.	OPAL	$222,923	$0	4	0
GERMAN AMERICAN BANCORP INC.	GABC	$219,400	$0	6	0
HARTE HANKS INC	HHS	$212,867	$0	2	0
PCB BANCORP	PCB	$207,320	$0	3	0
Green Plains Inc.	GPRE	$206,763	$0	3	0
CINCINNATI FINANCIAL CORP	CINF	$205,960	$0	1	0
Texas Pacific Land Corp	TPL	$205,816	$0	22	0
SYNCHRONOSS TECHNOLOGIES INC	SNCR	$202,341	$0	1	0