Porter & Co.

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INVESTMENT CHRONICLES

Issue No. 12 | March 2024

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.

We hope you'll come to think of *Investment Chronicles* as a highlight of your subscription with Porter & Co. We think it is the most comprehensive expression of our goal as a business: to give you the information we'd most want if our roles were reversed.

Porter Stansberry
Stevenson, MD
March 2024

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

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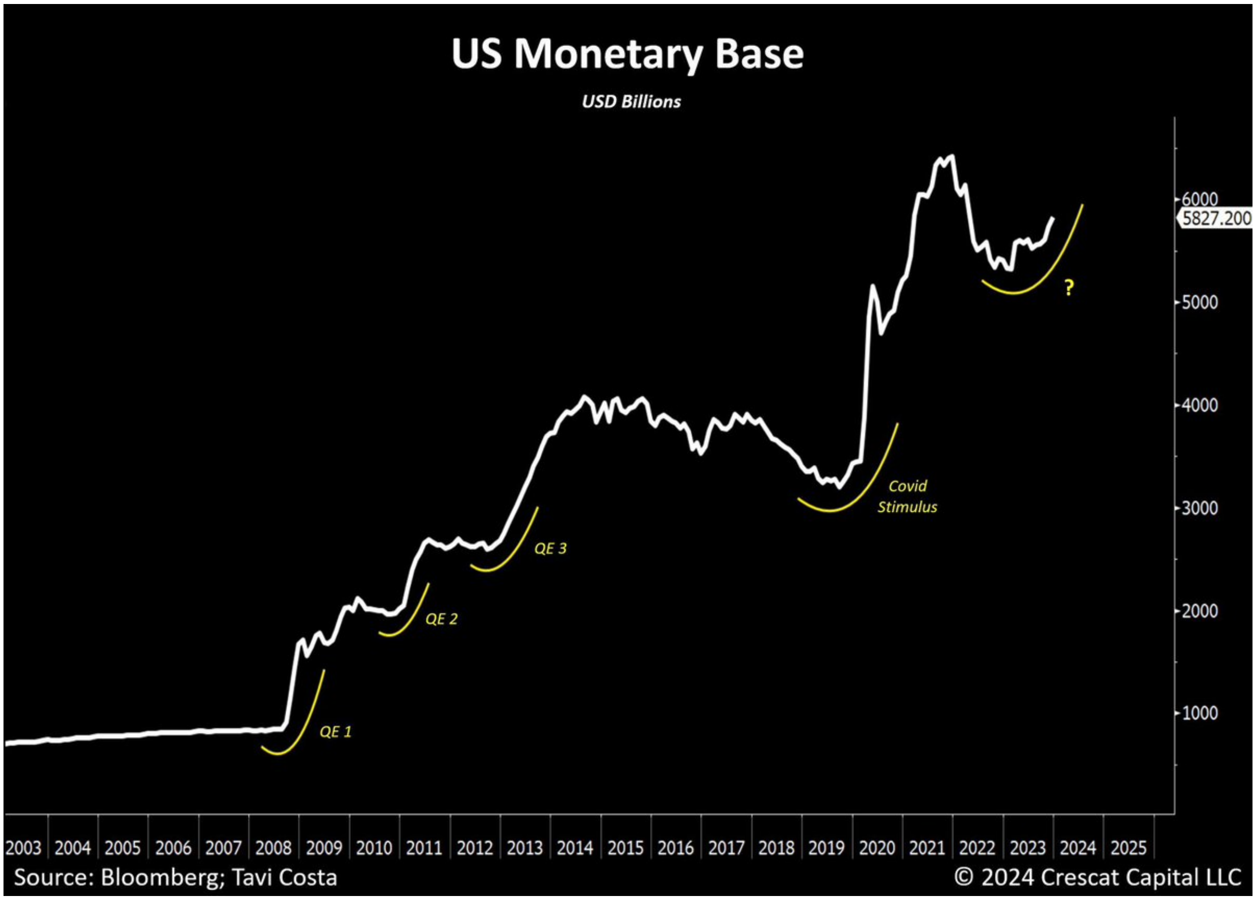
THE FIVE

The Most Important Charts We're Watching This Month

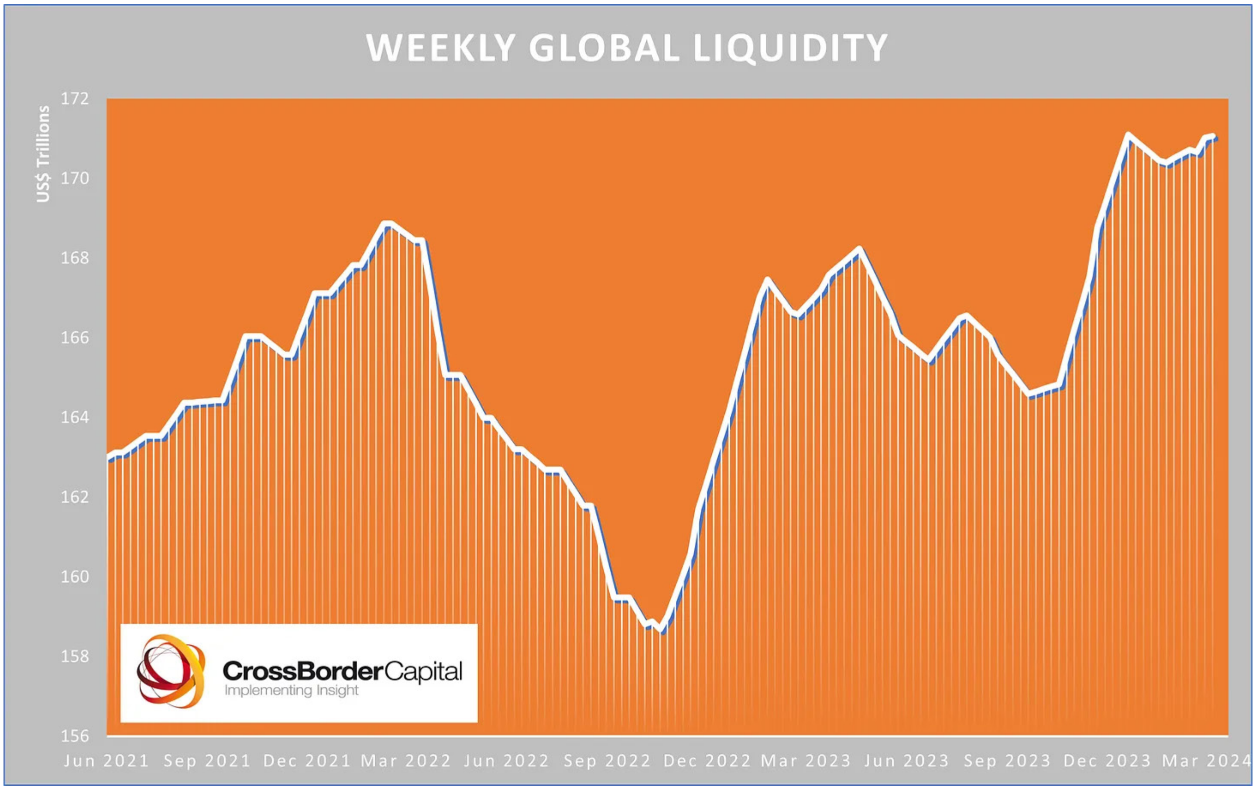
The big story this month was the breakout in "sound money" assets. Gold rallied to an all-time closing high, above $2,100 per ounce (from StockCharts.com)...

Bitcoin also closed at an all-time high, above $70,000 per coin ([from StockCharts.com](#))...

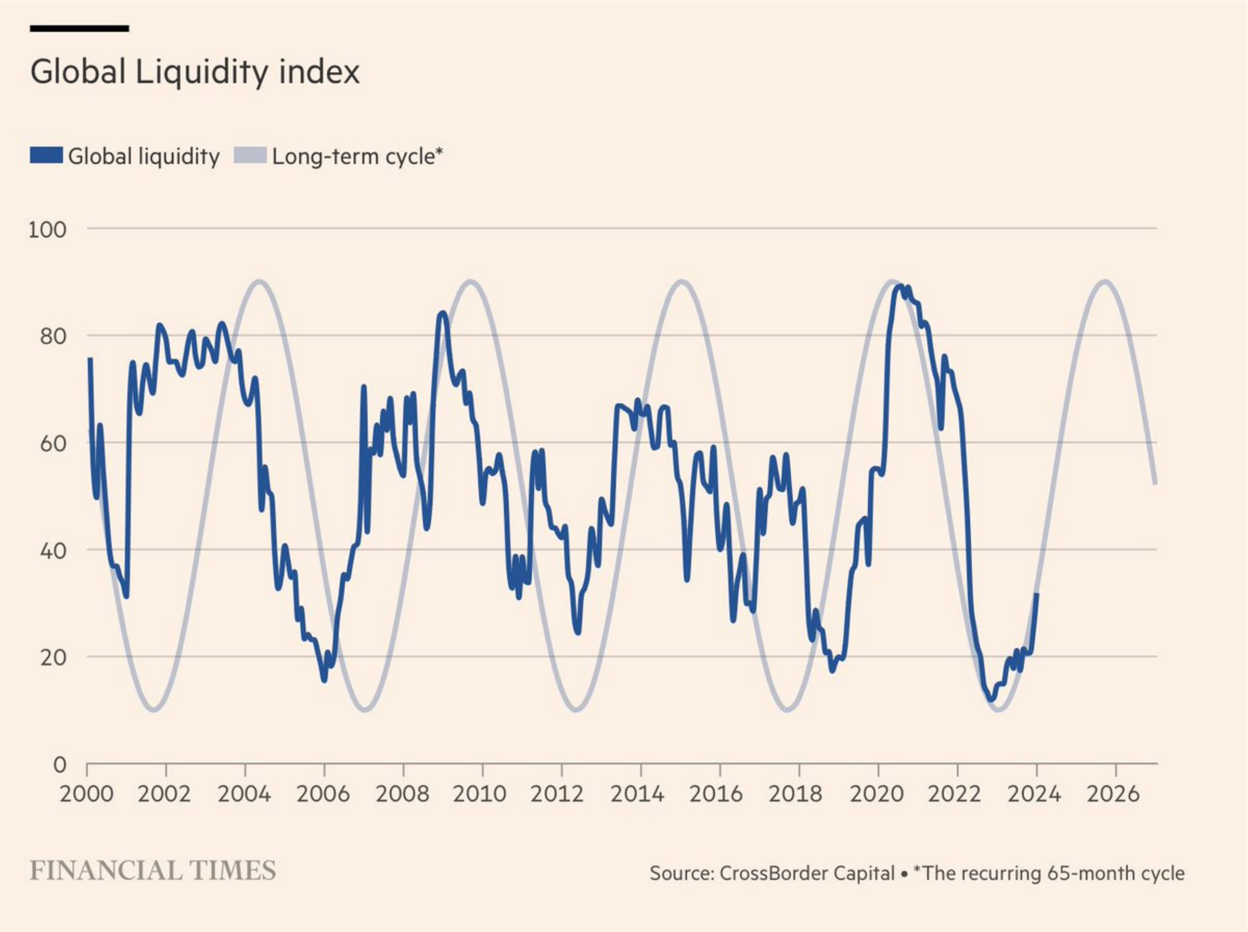
The sharp rally in these assets has followed a reacceleration in the U.S. monetary base (from Otavio (Tavi) Costa via X)...



These moves have also coincided with a surge in global liquidity to all-time highs (from Capital Wars)...



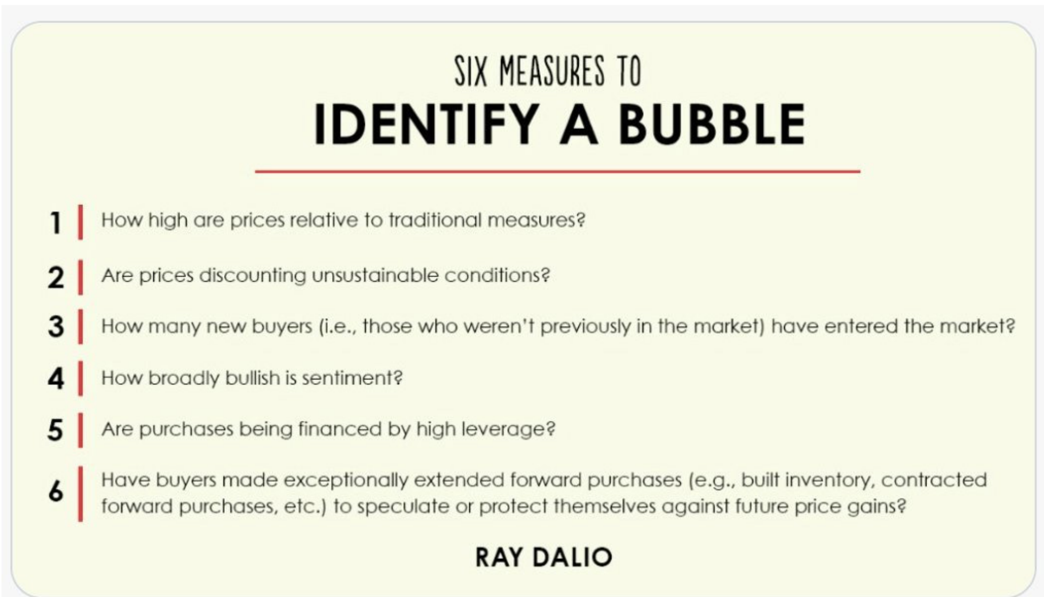
And based on historical cycles, this surge in liquidity is likely to continue well into next year (from Barchart via X)...

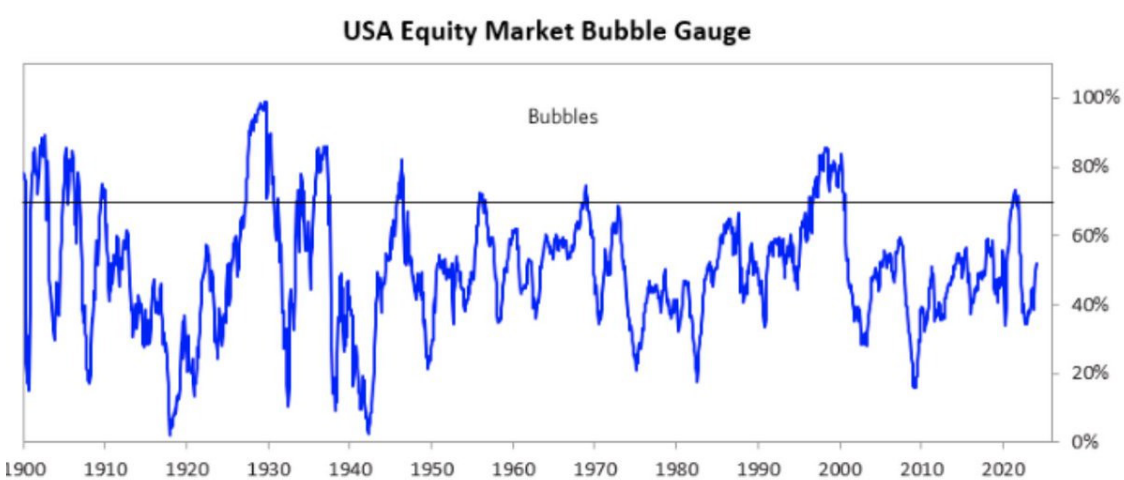


ECONOMICS AND MARKETS

According to hedge-fund legend Ray Dalio, U.S. markets are not in a bubble (yet) (from Seth Golden via X)...

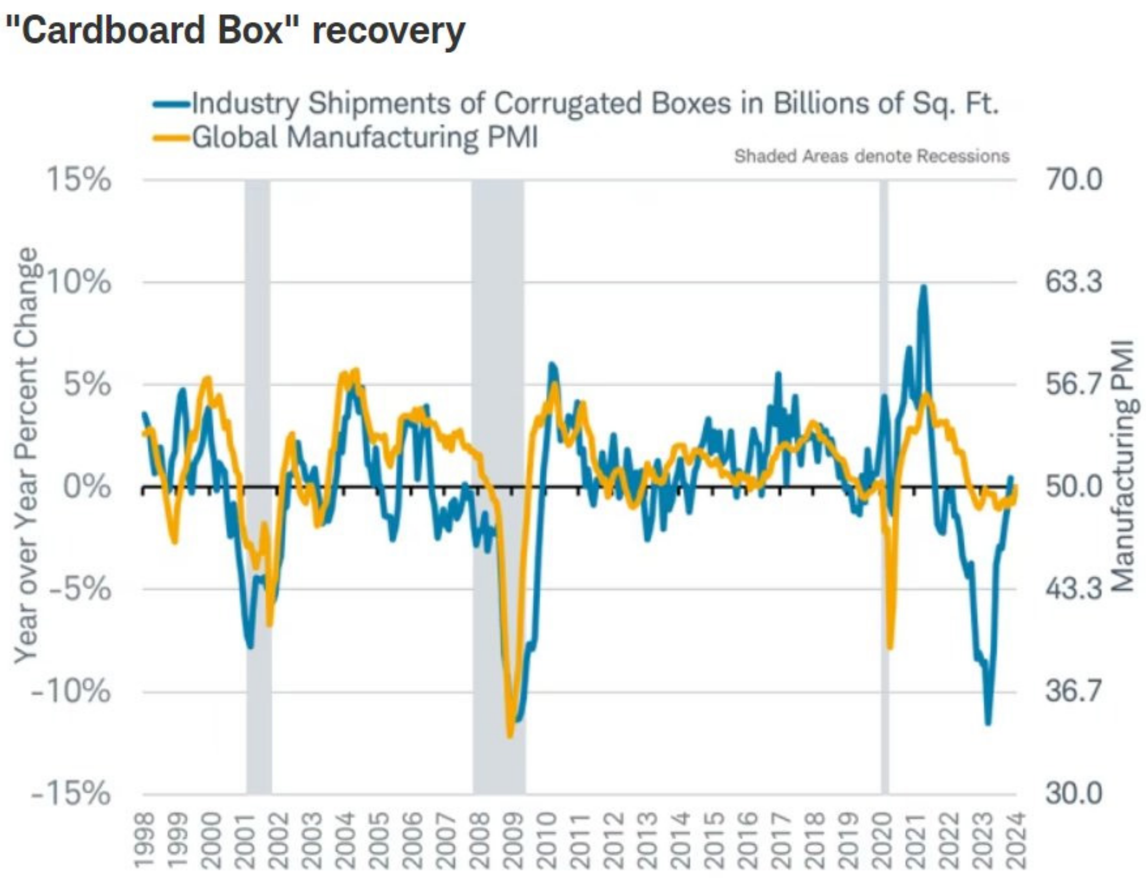
Ray Dalio: "I've seen a lot of bubbles in my time and have studied even more in history, so I know what I mean by #Bubble & I systemized it into a 'bubble indicator' that I monitor to help give me perspective... this is NOT A BUBBLE"





Source: Ray Dalio

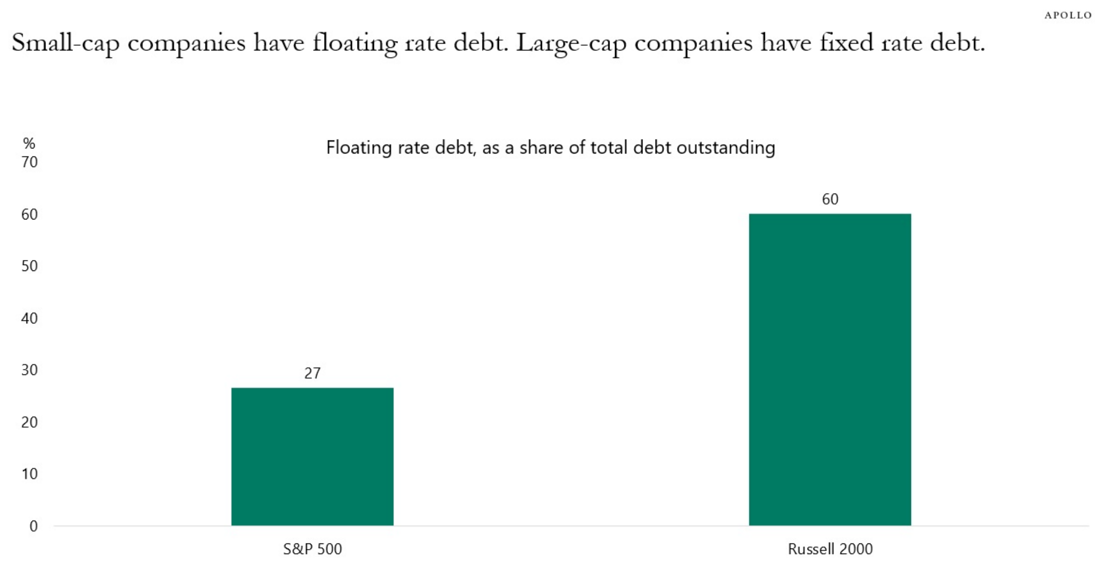
Charles Schwab says the "cardboard-box recession" is over (from Tracy Alloway via X)...

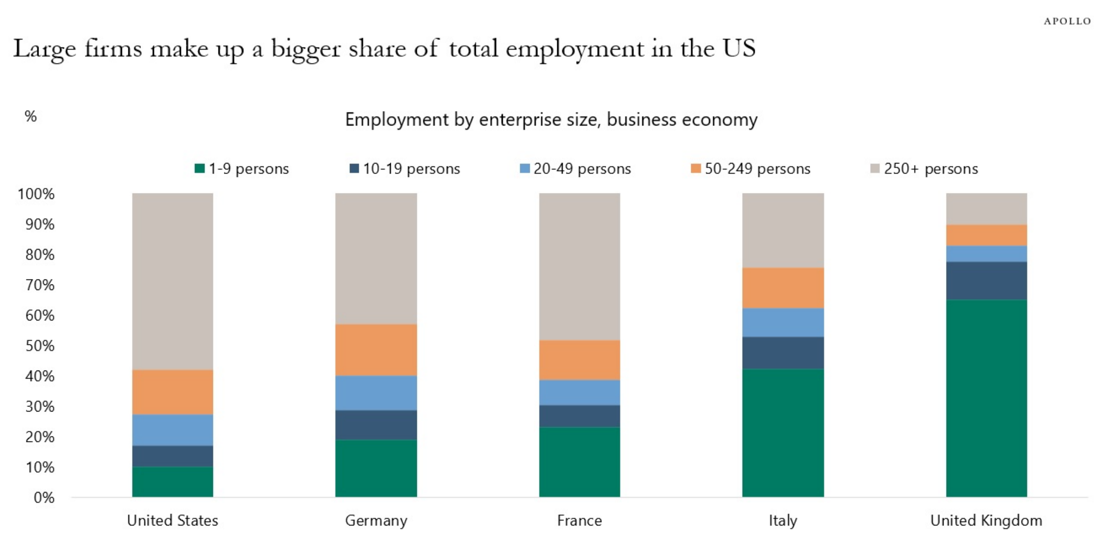


Source: Charles Schwab, Fibre Box Association, S&P Global, Bloomberg data as of 2/23/2024.

Why Federal Reserve rate hikes are having a more limited impact on the economy this cycle (from The Daily Spark)...

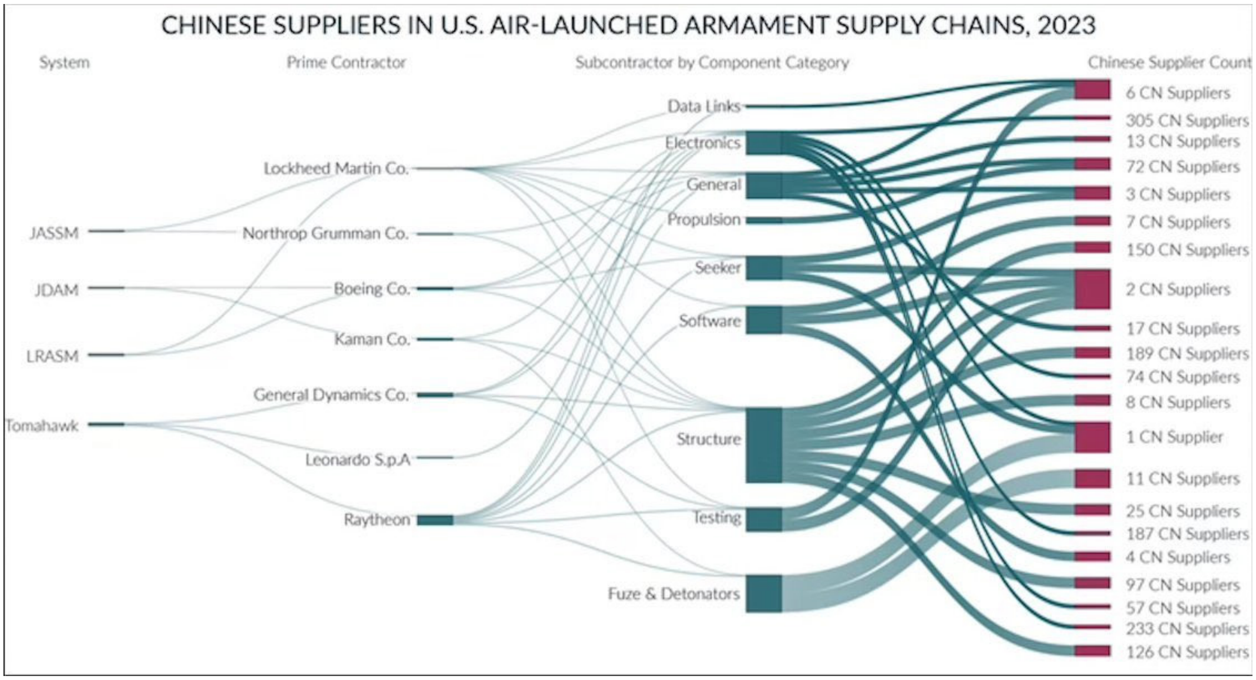
The U.S. economy is dominated by larger companies, and larger companies generally have fixed rate debt. This is likely a key reason why Fed hikes are having a more limited impact on the economy.





The U.S. military is still heavily dependent on China ([from joshua steinman via X](#))...

If you pay attention to one tech Twitter chart this week, I beg you, make it this one (not the other one).



Here's the summary, thanks to @AnthropicAI's "Claude" engine (pretty good!)


ANTHROP\C

The image shows a diagram mapping out Chinese suppliers involved in U.S. air-launched armament supply chains in 2023, based on analysis of component categories across several major U.S. defense contractors and systems.

Key observations:

- The diagram reveals an extensive network of Chinese suppliers integrated into critical U.S. weapons systems supply chains.
- Suppliers are mapped by component category, with Electronics, Data Links, and Fuze & Detonators having the highest counts of Chinese suppliers.
- Major defense prime contractors like Lockheed Martin, Northrop Grumman, Boeing, Raytheon and others all have Chinese suppliers in their armament supply chains.
- Well-known missile systems like JASSM, JDAM, LRASM and Tomahawk have significant numbers of Chinese suppliers providing key subcomponents.

The implications for U.S. defense are concerning:

- Dependence on Chinese suppliers introduces major security risks, including potential for tampering, disrupted production during conflicts, and IP theft.
- Lack of domestic sourcing for critical components could hurt readiness and impede operations if supply chains are cut off.
- There are likely many more Chinese suppliers in other weapons systems beyond air-launched armaments.
- Urgent action is needed to identify, remove and replace Chinese suppliers throughout defense supply chains to reduce risks and ensure supply chain integrity and security.

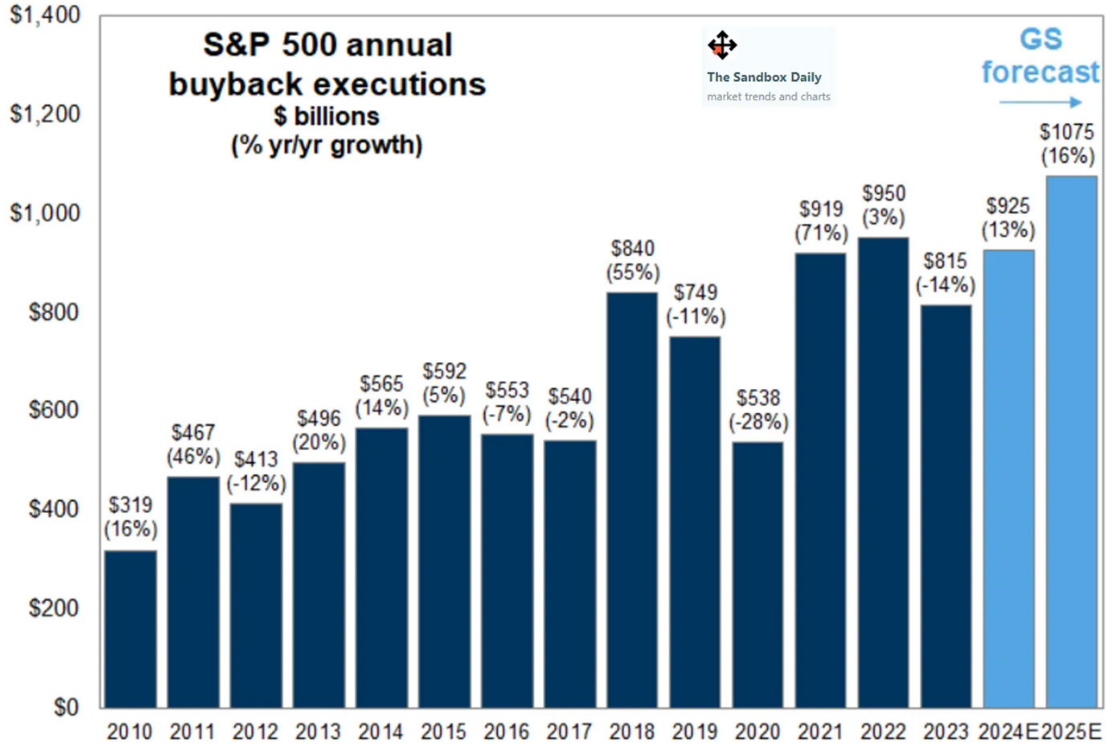
In summary, this analysis exposes an alarming level of Chinese infiltration into the U.S. defense industrial base, creating strategic vulnerabilities. Mitigating this issue should be an urgent priority for the Pentagon and the defense industry. Strengthening domestic production capabilities and supply chain resiliency is critical for U.S. national security.

Goldman Sachs expects U.S. share buybacks to grow 13% this year and exceed $1 trillion for the first time in 2025 (from The Sandbox Daily)...

Stock buybacks, the process in which a company buys back its own shares in the open market, are making a comeback now that companies are feeling more confident about the future.

After falling 14% in 2023, Goldman Sachs expects U.S. share buybacks to total $925 billion in 2024 (13% YoY growth) and exceed $1 trillion (16% YoY growth) for the 1st time in 2025, driven by strong earnings growth from technology companies and looser financial conditions as the Federal Reserve looks to cut interest rates.

S&P 500 annual buyback executions

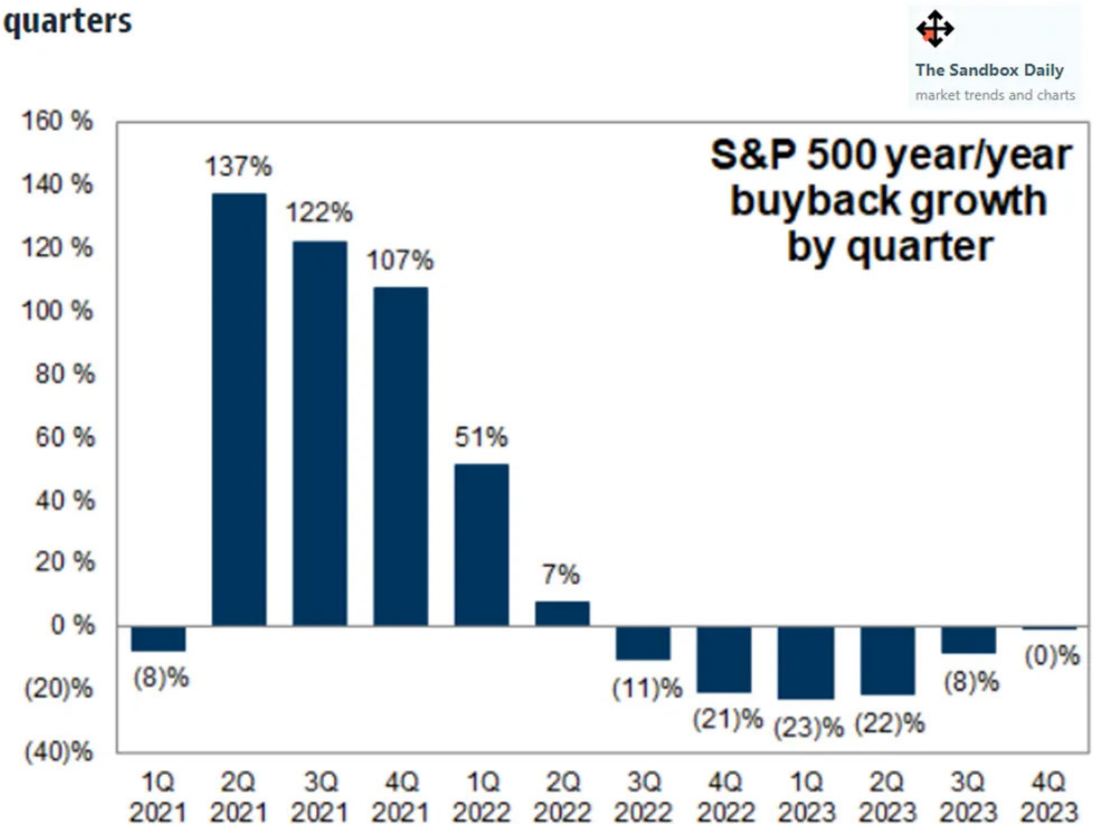


Source: Goldman Sachs Global Investment Research

Stock buybacks have been on a bit of a rollercoaster over the last couple years.

After crashing in 2020 during the onset of the COVID-19 pandemic, share repurchases exploded in growth in 2021 before leveling off and collapsing again in 2022-2023 as C-Suites across America prepared for the recession that never came.

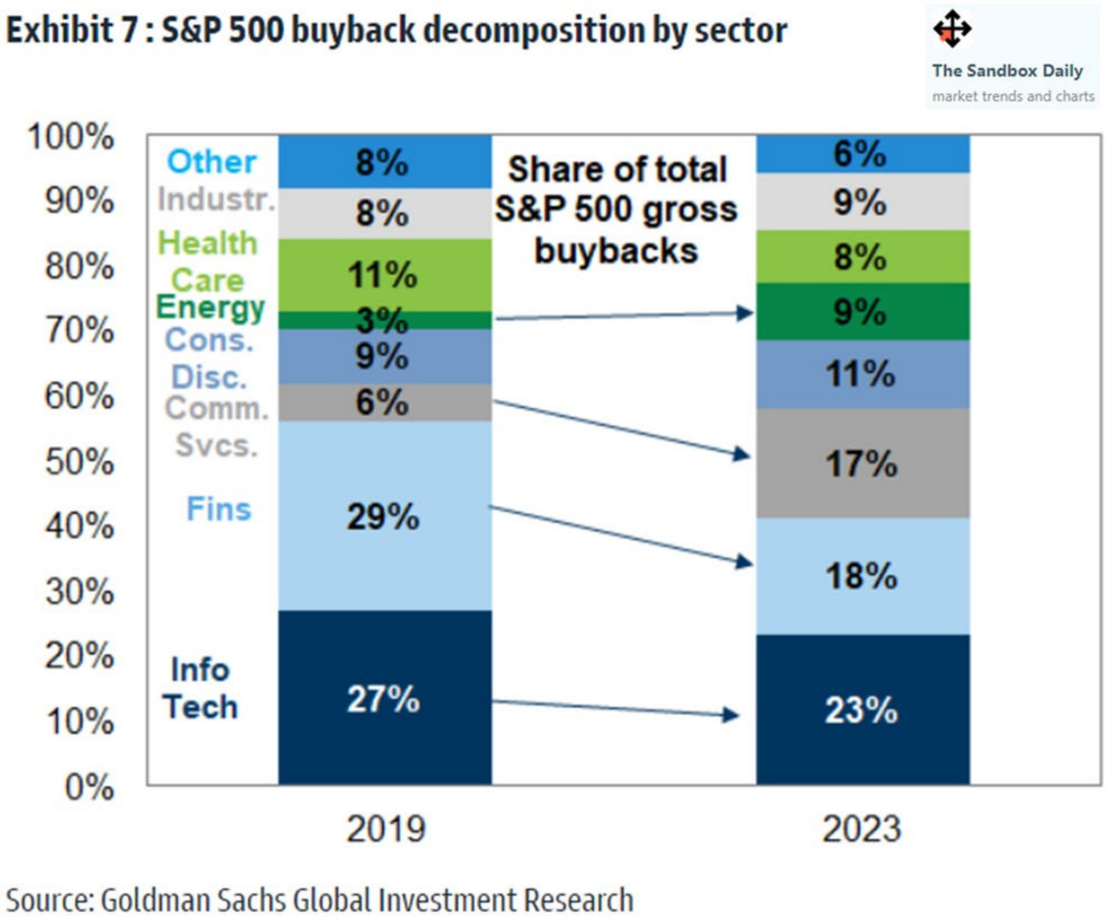
Exhibit 4 : Buybacks are were about flat in 4Q23 after shrinking for five quarters



Source: Goldman Sachs Global Investment Research

Information Technology and Communication Services will be the primary drivers of index level buyback growth.

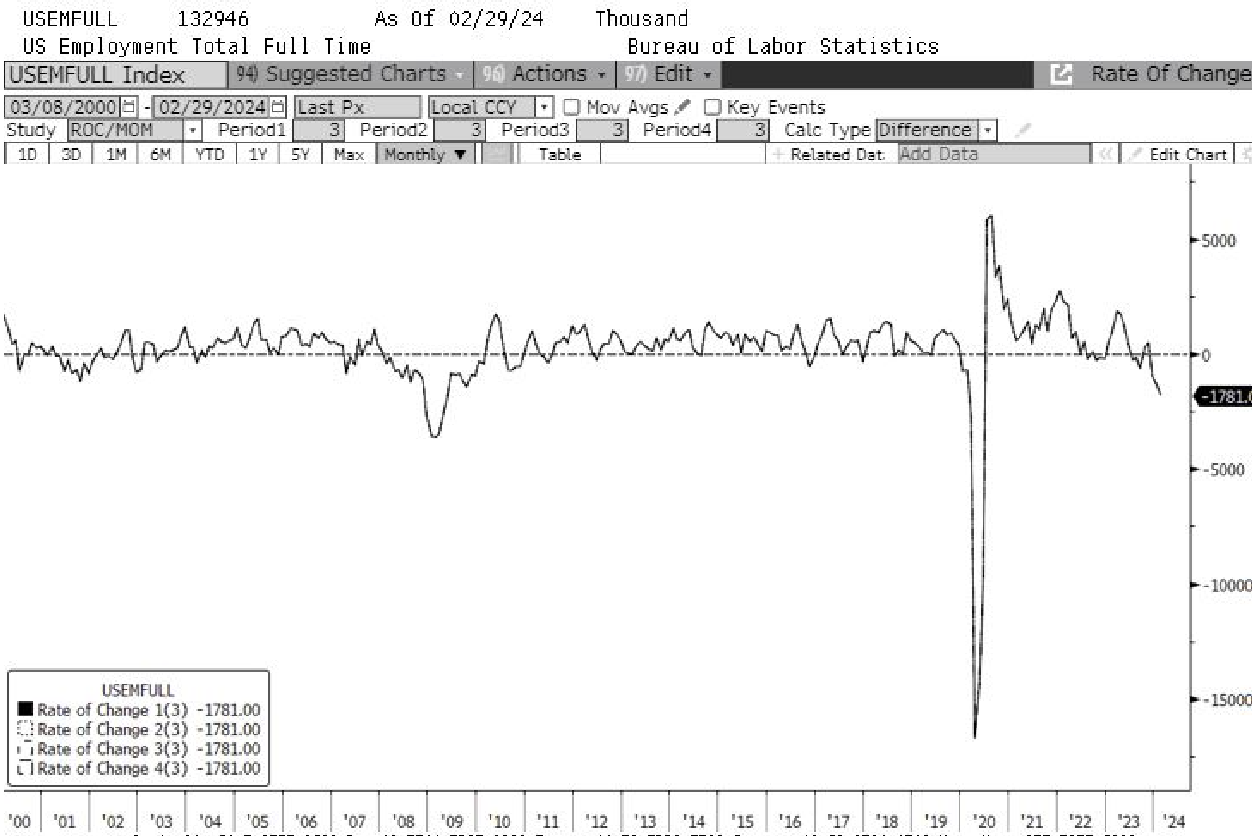
Revenue growth for these sectors will be supported by strong consumer spending and increased demand for AI-related products.



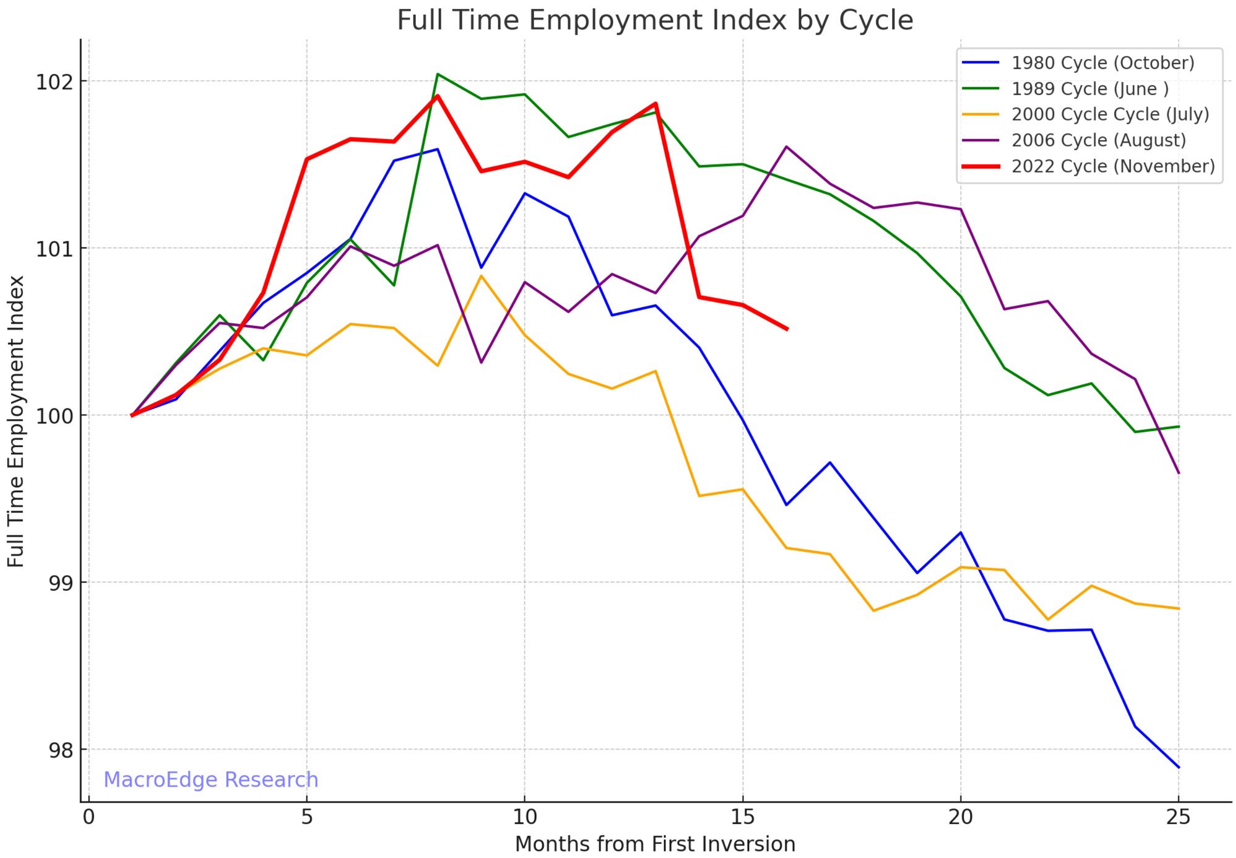
Companies enter share repurchase programs to reduce the outstanding share count, return capital to shareholders in a tax efficient manner, boost key financial ratios, bolster the stock price, and offset share dilution through employee stock option grants.

Over the last three months, the U.S. economy has shed 1.87 million full-time jobs ([from steph pomboy via X]())...

That's the largest decline since the Great Financial Crisis, outside the covid lockdowns.



This decline in employment is quietly on pace with similar cycle downturns (from Buck via X)...



What the world's leading liquidity expert is seeing now (from Adam Taggart's Thoughtful Money)...

When today's guest was on this channel back in December, he explained that rising net liquidity was responsible for the surprisingly strong performance seen in both the economy and the financial markets in 2023.

And he predicted that these net liquidity inflows would continue, leading to even higher asset prices ahead.

Well, here in the final month of Q1 2024, things so far have played out according to his script.

So where does he see liquidity heading for the rest of the year?

To find out, I sat down for another very important conversation with Michael Howell, founder & CEO of Crossborder Capital.

He still expects positive net liquidity flows to drive the economy and markets higher though 2025...but he admits it will be a rockier ride from here, starting in Q2.

Adam's Notes: Michael Howell (recorded 3.4.24)

As is customary I ask Michael what his assessment of the global economy and financial markets is. He remains optimistic, attributing most developments to liquidity trends. He observes that the liquidity cycle, which drives significant market and economic activities, turned positive in trajectory in October 2022, coinciding with the British gilt crisis and further bolstered by the failure of Silicon Valley Bank in the U.S.

Over the past 15 months, increased liquidity has been channeling into markets and is now starting to positively impact real economies, building momentum. He anticipates a peak in this liquidity cycle by the end of 2025, suggesting a robust second half for 2024 and continued growth into the following year, albeit possibly at a slower pace than in previous cycles.

Michael underscores that sluggish economies coupled with policymakers' desire to stimulate growth create an optimal environment for financial markets. He emphasizes the importance of focusing on major economies like the United States and China, rather than smaller European ones, for understanding global economic trends. The U.S. economy is showing signs of robustness, while

China appears to be gradually emerging from a period of slower growth experienced over the last 2 years. Although current growth there may not match pre-COVID levels, it's nonetheless on an upward trajectory. He also points to increasing trade volumes in the Asia Pacific region and a record month reported by the Port of LA in January as evidence of this acceleration, giving validation to his positive outlook for global economic activity.

Does he anticipate the upward trend in markets, fueled by rising liquidity, to persist? And additionally, is there a risk of markets overestimating this liquidity increase and prematurely boosting stock prices to unsustainable levels? Michael acknowledges the complexity behind market trends but affirms that we indeed remain in a bull market, which typically lasts 2 to 3 years. But as we're already about 15-16 months into this bull market, he suggests that most of the gains we can expect from it have already occurred. He expects decent returns in the next 12-18 months, though gains will come more slowly. He predicts a market rotation from the Magnificent 7, with a broadening rally moving into traditional cyclical sectors and liquidity sensitivity assets like Bitcoin.

All this said, he highlights some immediate concerns for the U.S. financial system, particularly in Q2, due to liquidity-related challenges facing the Federal Reserve and U.S. Treasury. These include the end of the Bank Term Funding Program (BTFP), the draining of the Reverse Repo Program (RRP), and coming tax receipts into the Treasury General Account. These factors will potentially constrain liquidity in the short term. That said, Michael believes the overall trend for federal liquidity is upward — although these Q2 events may cause a temporary dip before it continues to rise.

Continue reading (subscription required).

More Americans are treating their 401(k)s like ATMs (*from The Wall Street Journal*)...

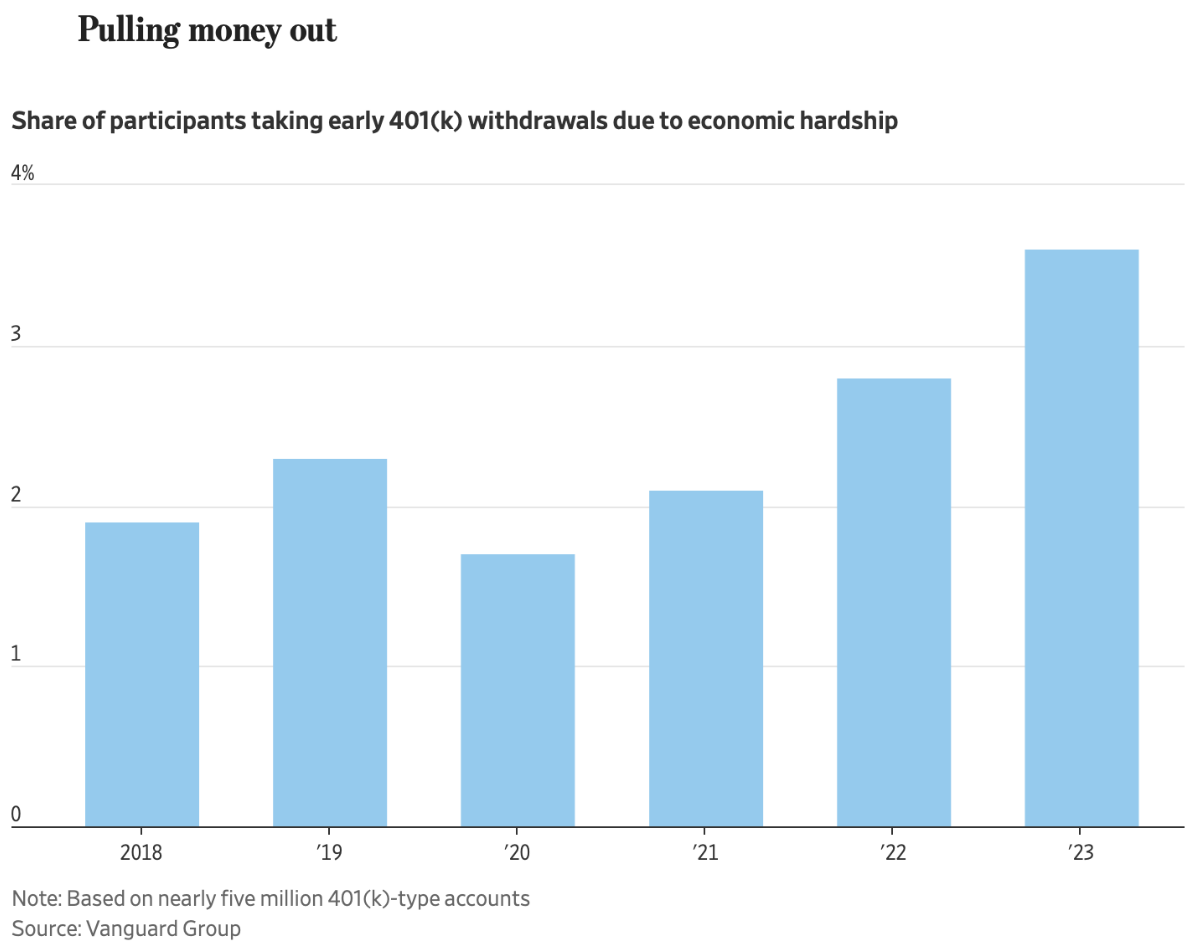
The 401(k) is doing double duty as both a retirement account and a source of emergency funds for more Americans.

A record share of 401(k) account holders took early withdrawals from their accounts last year for financial emergencies, according to internal data from Vanguard Group. Overall, 3.6% of its plan participants did so last year, up from 2.8% in 2022 and a prepandemic average of about 2%.

Retirement plans such as the 401(k) are designed to keep Americans' nest eggs out of reach until later in life. And values in these accounts have risen substantially, in part because of a strong stock market and programs that automatically funnel money from people's paychecks into their 401(k) accounts.

These surging balances, however, have helped make more people comfortable dipping into their accounts when needed.

Americans are dealing with conflicting financial forces. While hiring has been strong and workers' earnings keep rising, the cost of groceries, child care and car insurance keeps climbing. More people are carrying heftier balances on their credit cards.



Emergency distributions hit back-to-back record highs in 2022 and 2023, according to Vanguard, which administers 401(k)-type accounts for nearly five million people and published the data ahead of an annual report scheduled for June.

Continue reading here (subscription may be required).

This chart suggests the U.S. is heading toward a "financial precipice" (from Robert Sterling via X)...

This is the scariest chart I've ever made. This is what it looks like when a country is heading toward a financial precipice.

Each color shows $1T getting added to the national debt.

Not that long ago, it took six years to add a bar.

We're now adding one every 90-120 days.

The explosion of debt has been the only bipartisan phenomenon of my lifetime. For us conservatives, we can't blame it on just Biden and Obama. For you Democrats, you can't put this on just Trump. It's both parties, all presidents, and every Congress.

The acceleration started under George W. Bush. Bush went into 2002 with less than $6T of debt. Thanks to GWOT military spending and tax cuts we probably couldn't afford, $6T grew to $7T in 23 months, $8T in another 21 months, and $9T in 23 months.

Then the Great Recession hit. We added the next trillion in 13 months, crossing $10T for the first time in American history. And we haven't looked back since.

During the second Obama term, with spending reined in by the Tea Party movement, annual deficits reduced to less than $1T, and growth in the debt slowed down. At the end of Obama's tenure, it took nearly 20 months to go from $19T to $20T.

That would be the last time it took a full year to add a trillion dollars to the debt.

In 2017, a real-estate developer got inaugurated as president. And, if there's one thing we all know—and love!—about real-estate investors, it's that they understand the value of leverage.

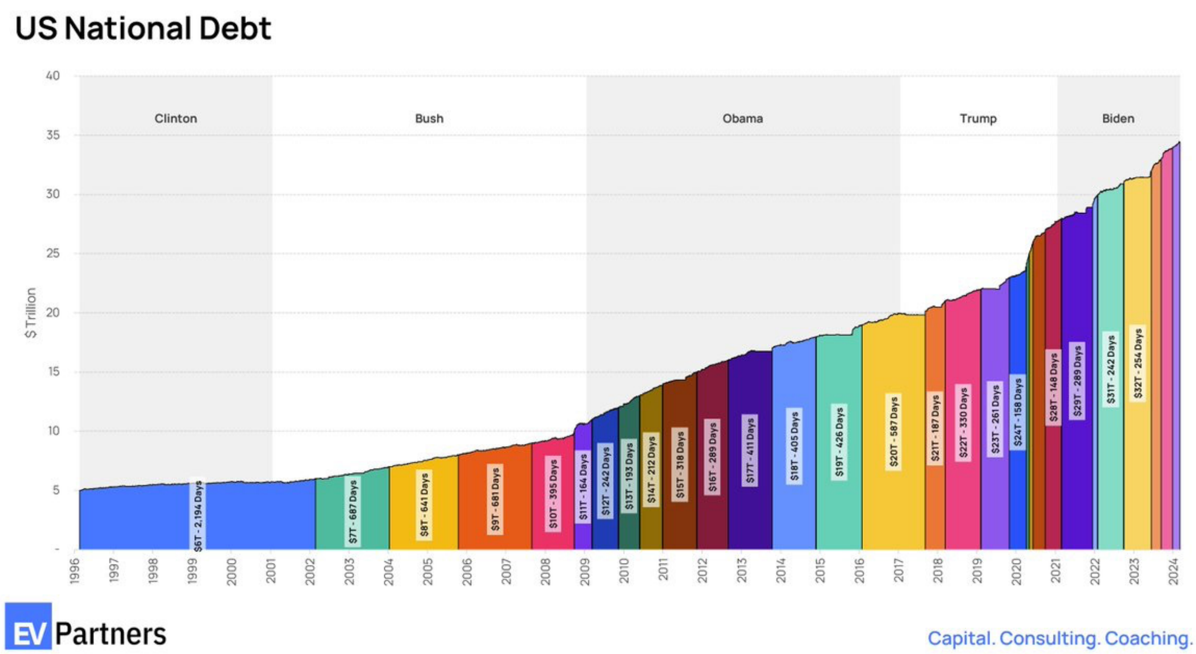
Under Trump, even as the economy surged, deficits grew, and national debt once again spiraled. We ended 2019 with a little over $24T in debt.

Then Covid hit, along with consumer stimulus, PPP loans, massive government spending, and reduced tax receipts. Over just two months in 2020—April and May—we added $2T to the national debt. Ever since, we've been adding $1T every 160 or so days.

With Biden in the White House and a narrowly divided Congress, we're now adding $1T to the debt every three to four months. It took just 91 days to go from $32T to $33T. 104 days to get to $34T.

And it's not slowing down. Biden has another 300+ days in office this term. When he or Trump enters their second respective term in office in 2025, the debt will likely be above $37T.

Where does it end? As deficits continue to pile up and borrowing costs remain relatively high compared to where they were over the previous 20 years, how is any of this sustainable?



Why it may be too late for the Fed to stop inflation now (from Luke Gromen via X)...

Fed screwed up by not letting inflation run "Higher 4 Longer" in 2022 to get debt/GDP back to 70-80% before hiking, b/c rate hikes on debt/GDP of 120% eventually start adding to inflation👇

To stop inflation at this point, the Fed would need to cut rates to 0% and balance the Federal budget, which would trigger a 7% of GDP decline.

This would be a bigger GDP drop than the Great Financial Crisis, except with no bailouts for anyone this time...just stand aside & watch it burn.

There are two major problems with this:

a) The Federal budget is NOT the Fed's purview - Fed has no say over the fiscal side.

b) A 7% drop in GDP from 7% of GDP fiscal cuts would drive the fiscal deficit to RISE >7% of GDP as receipts fell & countercyclical stabilizers rose.

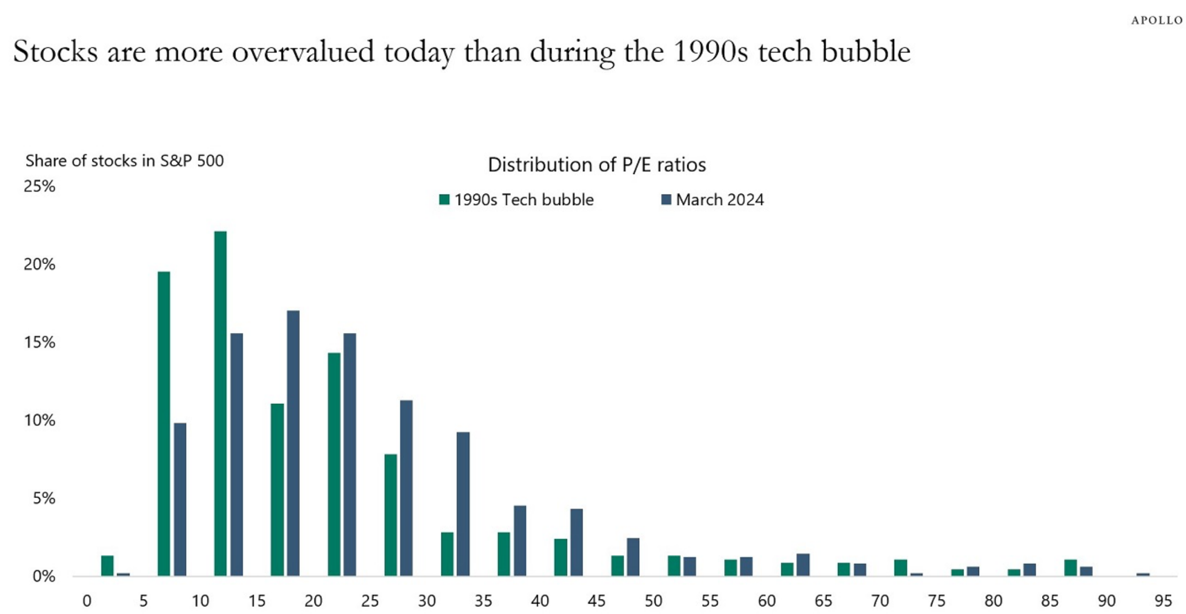
In short, failing a productivity miracle implemented ASAP, we are quickly approaching the proverbial "print the money or trigger the revolution" moment...in the GRC.

A much weaker USD & a new "everything bubble" buys time...while a stronger USD lights the match.

Let's watch.

By this measure, the AI bubble is already bigger than the 1990s tech bubble (from The Daily Spark)...

The distribution of P/E ratios for the S&P 500 shows that stocks today are more overvalued than they were in March 2000, see chart below.



The next round of quantitative easing ("QE") could look a little different than the last (from Joseph Brown via X)...

It's possible the next round of QE will not show up on the Fed's balance sheet.

Instead, it could be carried out by banks themselves.

Here's how a change to banks leverage rules could bail out the US government.

The US Government currently owes $34 trillion - not including interest. For every dollar they borrowed in the past, they have to borrow more dollars today to pay it back when it matures. And for every dollar they borrow today to pay back old maturing debt, they have to borrow even more in the future.

Basically, the debt has to grow if they don't want the whole fiat system to collapse.

But, the problem is that the economy does not have a limitless supply of dollars to loan the government. Sometimes, the dollars run out.

If we rewind the clock to the last time the dollars ran out, it was 2019. The US government had spent the last few years borrowing and spending like crazy. On the backs of the Trump tax cuts and increases in government spending, the deficit exploded.

By September of 2019, the economy did not have any dollars left to loan to the government. In fact, banks did not even have enough dollars to loan to each other.

This caused the repo market to almost collapse in September of 2019. Banks went to each other in overnight markets to get cash from each other, and realized they were all trying to do the same thing. Nobody had any cash. They all had assets (treasuries) but no cash. So the overnight cost for cash exploded, and banks were at risk of collapse. This was a liquidity crisis. Without overnight funding, banks would face overnight collapse. Obviously the Fed wanted to avoid this, so they intervened.

When the Fed intervened in the repo market, they said it "wasn't QE" because they were only buying short term government debt from banks in order to keep overnight cash cheap. But we all know the result is the same - print cash and give it to a bank in exchange for an asset. The Fed's balance sheet grew, and banks had the liquidity they needed again.

This is the path they almost always take. When liquidity dries up, when the government needs cheap financing, or when a crisis threatens "moderate long term interest rates", the Federal Reserve steps in, printing enough new money to buy the necessary treasuries from the market.

But given the fact that inflation is still so sticky, if the government were in need of a new round of QE again soon, it would be deeply unpopular for the Fed to abandon its fight against inflation, fire up the printer, and start QE again.

Lucky for them, they may be able to accomplish stealth QE with a simple rule change for banks, and it wouldn't even have to show up on their own balance sheet.

We'll come back to that in a moment. First we have to address the question of government borrowing. Is the government at risk of repeating the same thing that happened in September of 2019? Where they had borrowed all available cash out of the system, triggering a liquidity crisis?

Yes. Right now, every time the government tries borrowing long term debt, the auctions don't go well. The difference between the rate they want to borrow at and what they end up paying is called a tail. Over the last few months, the sizes of tails on treasury auctions keep making new records.

The one place the government is continuing to borrow from in order to avoid this mess is short term debt; T-Bills. The funding from this is coming from places like money market funds, who are pulling their cash out of the Fed's Reverse Repo Facility and buying T-Bills at auction instead.

Right now there is only about $500 billion left in this facility. Within the next couple of months - at current government borrowing rates - this facility will be drained. Leaving the government forced to pay higher rates to attract lenders, until all the available money to lend has been fully borrowed.

So what about this rule change?

Current leverage rules limit how much a bank can buy and hold of any assets, including US treasuries. (Remember, when you buy a debt asset, that's just another way of saying you are loaning money). Banks buy a mix of assets to optimize return while paying attention to potential risk.

The Federal Reserve could simply change this rule, so that the limits no longer apply to treasuries. They've done it before (temporarily) and they can do it again. This would allow banks to purchase a limitless amount of US treasuries, becoming a bottomless source of borrowing for the government.

But what about profitability? Banks still would have to worry about that, right? Well, not really. Treasuries are considered "risk free" which means that you are guaranteed to get your money back if you hold it until maturity.

Recently, that was a big "IF" for banks that were holding underwater treasuries while a bank run started. It didn't matter that the treasury was considered risk free if they had to sell it prior to maturity at a loss.

But the Fed has facilities in place that give banks the ability to temporarily offload underwater treasuries to the Fed in exchange for cash if they need it.

So without the need to worry about risk, and with a leverage rule change that exempts US treasuries, banks could become a source of borrowing for the government that has no end. Banks would loan money into existence to the US government, buying as many treasuries as they wanted, keeping all the upside and none of the risk.

QE through the banks, without the Fed's balance sheet ever having to change. Without the Fed's credibility being challenged. And they can keep up their facade of fighting inflation, all the while enabling the very thing that will keep it roaring higher.

The End.

Recent *Barron's* and *The Economist* covers are all you need to know about the current state of market sentiment (from Otavio (Tavi) Costa via X)...


The Economist
Time's up for TikTok
Inside Putin's Russia
Crazy rich Indians
A special report on the oil industry
MARCH 16TH–22ND 2024
AMERICA'S
PUMPED-UP ECONOMY

Retail sales have been weakening sharply (from Brian McCarthy via X)...

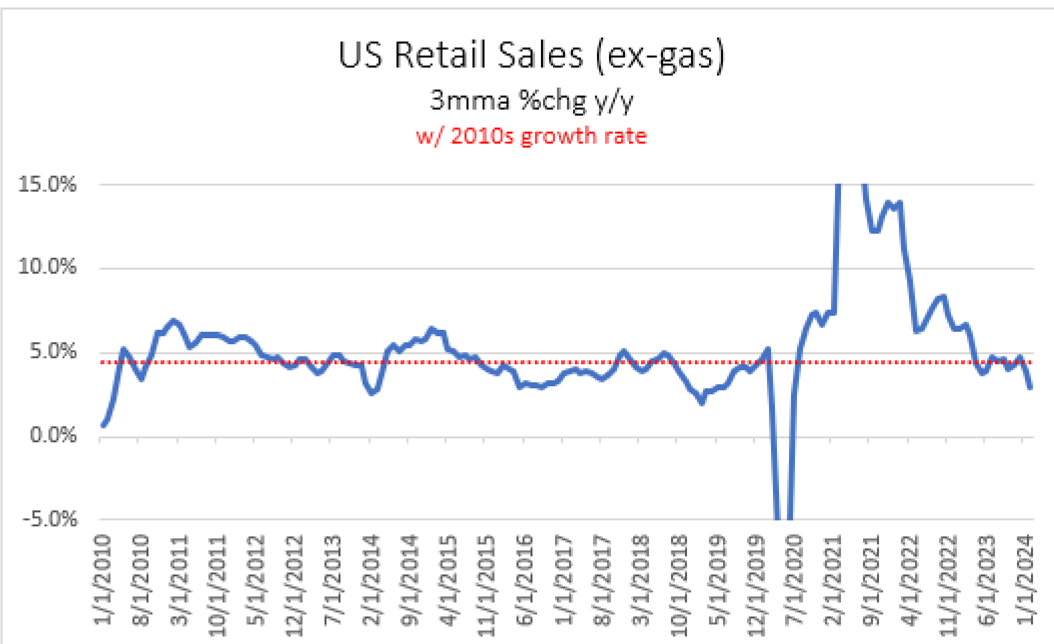
Team higher-for-longer (and their hawkish brethren at the Fed) continues to focus on badly lagging indicators like rent and services inflation, while ignoring the fact that retail sales ex-gas 3mma on-year-ago is up 2.9% (nominal), a new cycle low and well BELOW levels which were consistent w/ 2% inflation in the last economic cycle. The last 3 months were DOWN on the previous 3 months, so we are also decelerating sharply.

Noticeable labor market weakness will soon follow, in line with leading indicators like declining quits rates and NFIB hiring intentions.

Meanwhile, the misplaced H4L narrative is preventing the Fed from getting ahead of the slowdown.

This is how business cycles end in the textbooks, which apparently too few have read. I think Powell has, but he lacks either the will or the power to drag the FOMC to where it needs to be.

We'll get sufficient further weakness to push them to a June cut, but it will be too little, too late. They are already behind the curve.



Nearly one in three Americans has no retirement savings at all (*from MarketWatch*)...

Nothing. That's not much to fall back on in retirement.

As many as 28% of Americans have nothing saved for their retirement, 39% aren't contributing to a retirement fund, and another 30% don't think they'll ever be able to retire. That's according to a new GoBankingRates survey.

Between 25% and 35% of all demographics between the ages of 18 and 64 years old report having nothing saved for retirement, the survey said.

How much is needed for a secure retirement varies by person and situation, of course. But a study from Northwestern Mutual in 2022 found that U.S. adults anticipate they will need $1.25 million to retire comfortably, while a 2023 Schroders survey put the figure at about $1.1 million.

GoBankingRates, meanwhile, found that a quarter of the 1,000 people surveyed think they can retire with less than $500,000. Another quarter believes it will take somewhere between half a million and a million dollars, while another 30% expect their retirement to cost higher in the seven figure-range.

So why aren't people saving for retirement? Some don't have access to retirement-savings plans, although participation is low even when the accounts are available: The Bureau of Labor Statistics says 69% of private industry workers have access to an employer-based retirement plan but only 52% participate.

Other obstacles include inflation, debt, as well as low financial literacy, starting saving too late, being inconsistent in making contributions, and spending on wants without seeing saving for retirement as a need, GoBankingRates said.

Continue reading here (subscription may be required).

If re-elected, Biden wants to hike taxes by $7 trillion (from MishTalk)...

If Democrats win the trifecta with a clean sweep of the Senate, House, and White House in November, taxes would rise by $7 trillion over 10 years.

The House Ways and Means Committee reports The Biden Tax Hike Will Likely Exceed $7 Trillion.I believe they mean would not will.

Tax Details

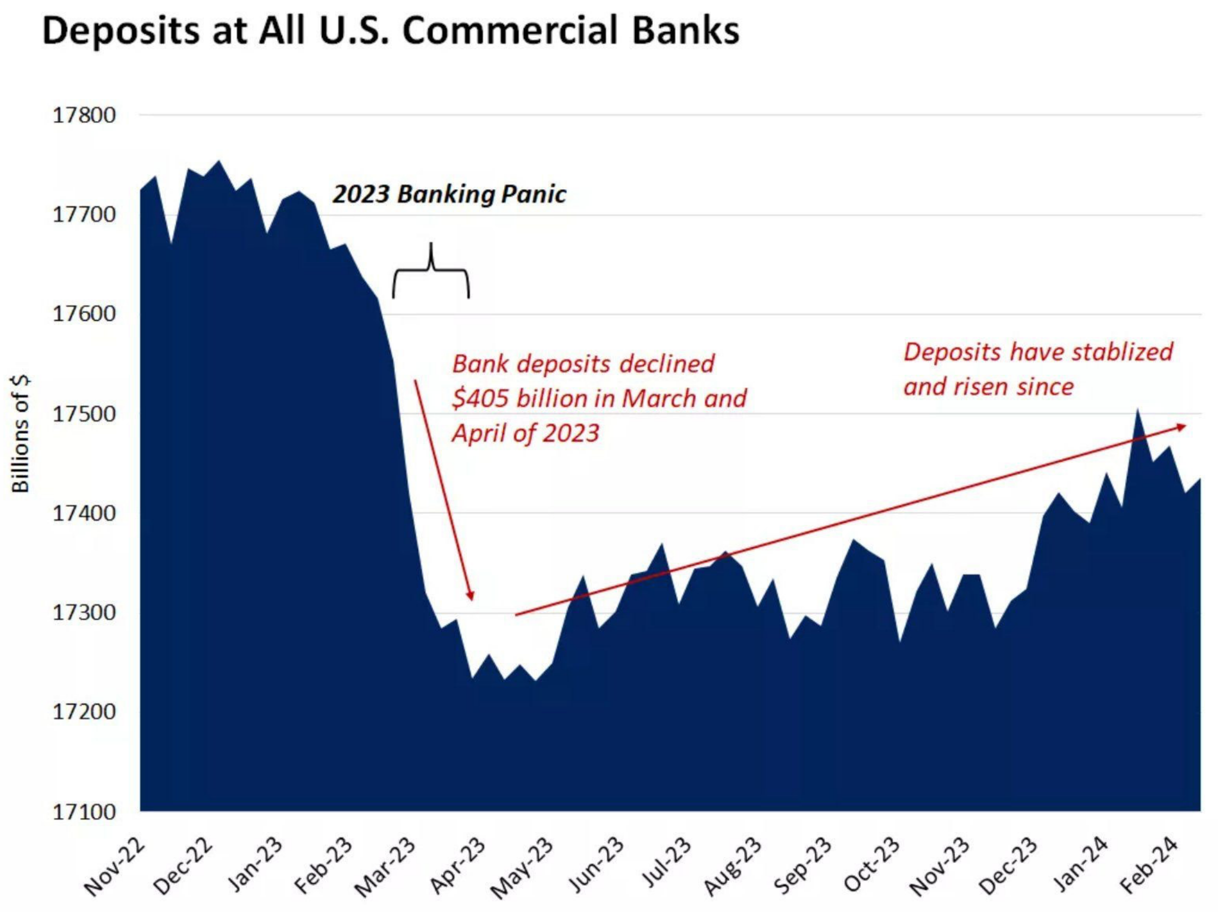
- President Biden Quietly Pledges to Let Trump Tax Cuts Expire
- Sending Jobs and Companies Overseas with Higher Business Taxes than China
- Global Tax Surrender Allows Foreign Governments to Take American Tax Dollars
- President Biden's proposal to raise the top rate to 39.6 percent goes after small business owners who pay their business taxes via their individual tax return – despite his pledge not to raise taxes on small businesses.
- A Tax on Wealth You Haven't Even Earned Yet.
- Higher Prices for Energy Bills and an Energy Insecure America.
- An IRS That Would Terrify Godzilla

A friend of mine asked when will the tax hikes cause a recession. I replied "never." I suspect my friend was confused over the title that said "will" it should say "would".

I did not total up all of those details because I don't believe it's going to happen. However, It is a warning shot as to what would happen if Democrats did win the trifecta.

Continue reading here.

U.S. bank deposits have stabilized and risen since the 2023 banking panic, showing that confidence is slowly returning ([from Charles-Henry Monchau via LinkedIn])...



Source: St. Louis Fed.

While the S&P 500 seems due for a breather, the absence of a momentum divergence suggests further upside ahead (from Mark Ungewitter via X)...

Big tech stocks have become the stock market (from The Kobeissi Letter via X)...

Stock concentration is now at Great Depression levels:

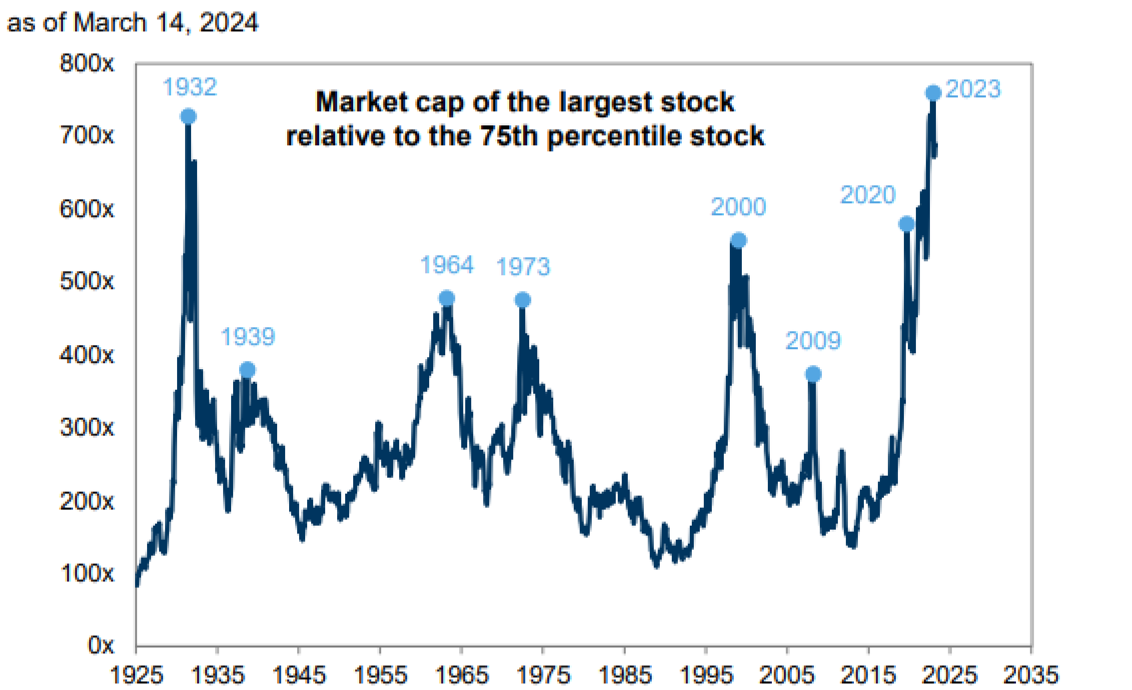
According to Goldman Sachs, the market cap of the largest stock is now 750 TIMES the market cap of a 75th percentile stock.

To put this in perspective, even at the peak of the 2000 Dot-com bubble the metric only hit 550x.

We officially have a higher stock concentration than the peak of the Great Depression in 1932.

The top 10% of stocks in the US now reflect ~75% of the entire market.

Big tech IS the stock market.



Source: Compustat, Kenneth R. French, Goldman Sachs Global Investment Research

An unsuspecting company is trading like an AI stock (from The Kobeissi Letter via X)...

Current state of the stock market:

Wingstop, $WING, a chicken wing company, is now up 84% over the last year and worth $10 billion.

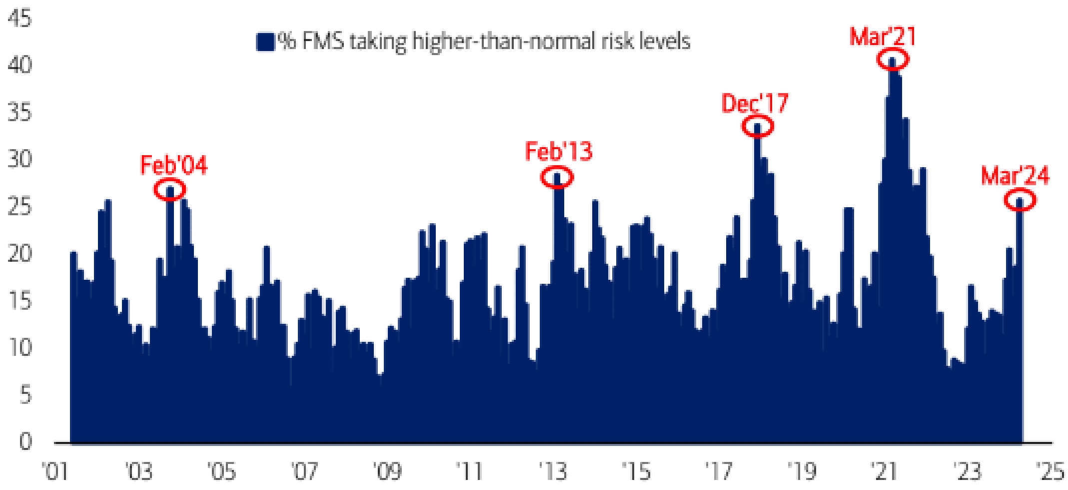
It's trading at 144x earnings and tripling the S&P 500's return.

Who needs AI when you have chicken wings?

BofA's Global Fund Manager Survey shows that risk appetite is at its highest since 2021 (from Ayesha Tariq, CFA via X)...

Chart 1: BofA Global FMS risk appetite highest since Nov'21

% FMS respondents saying they are taking 'higher-than-normal' level of risks relative to their benchmark



Source: BofA Global Fund Manager Survey

BofA GLOBAL RESEARCH

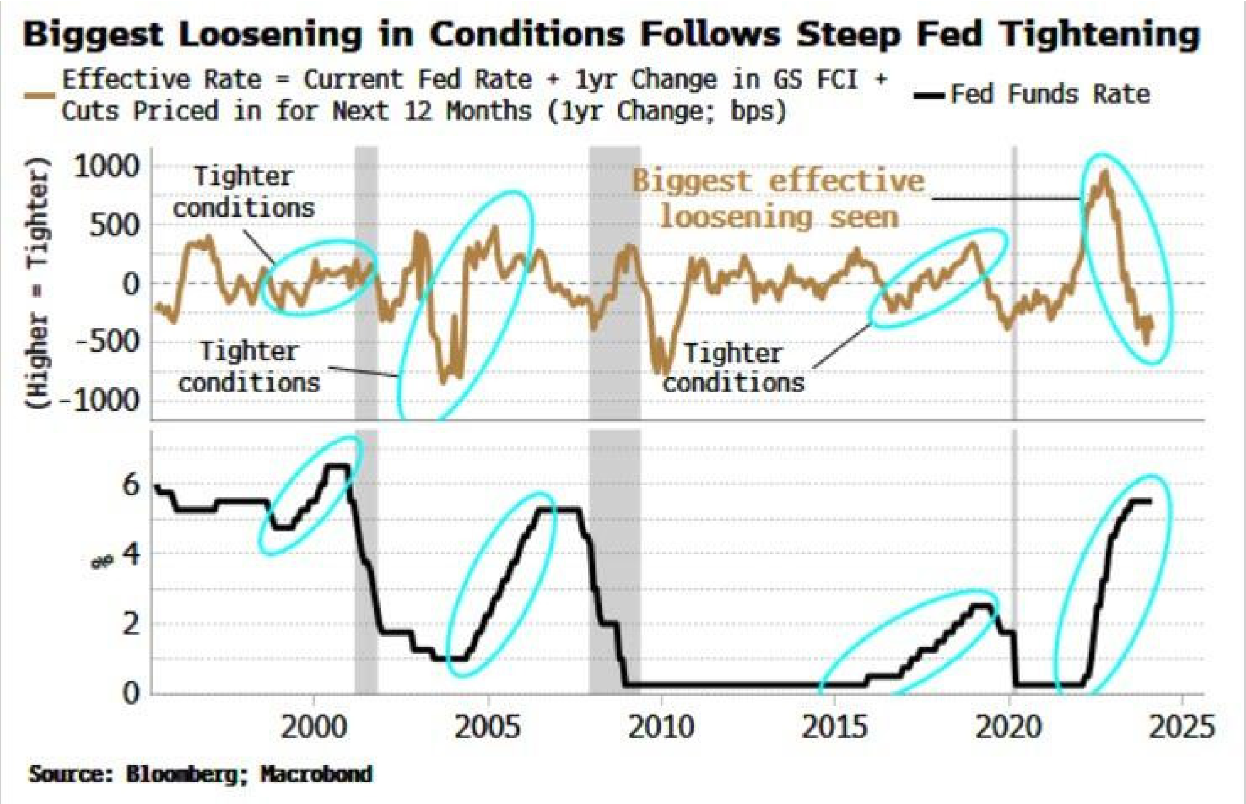
History shows this is not necessarily a reason for immediate concern (from Jason Goepfert via X)...

Fund managers are the most bulled up in 2 1/2 years, according to BofA.

This is not a good reason to sell.

The Fed wants to loosen during what has already been the largest effective easing of financial conditions that we've seen from peak to trough ([from Markets & Mayhem via X](#))...

That seems fine, right?



The next global rate-cutting cycle likely began in mid-March (from The Bitcoin Layer)...

The Swiss go first

A global rate cutting cycle has begun, and by the end of today's post you will understand why I believe investors must factor in central bankers' insistence on lowering policy rates.

Let's start with Switzerland's central bank:


Bloomberg

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Economics
Central Banks

Switzerland Surprises With Rate Cut, Moving Ahead of ECB and Fed

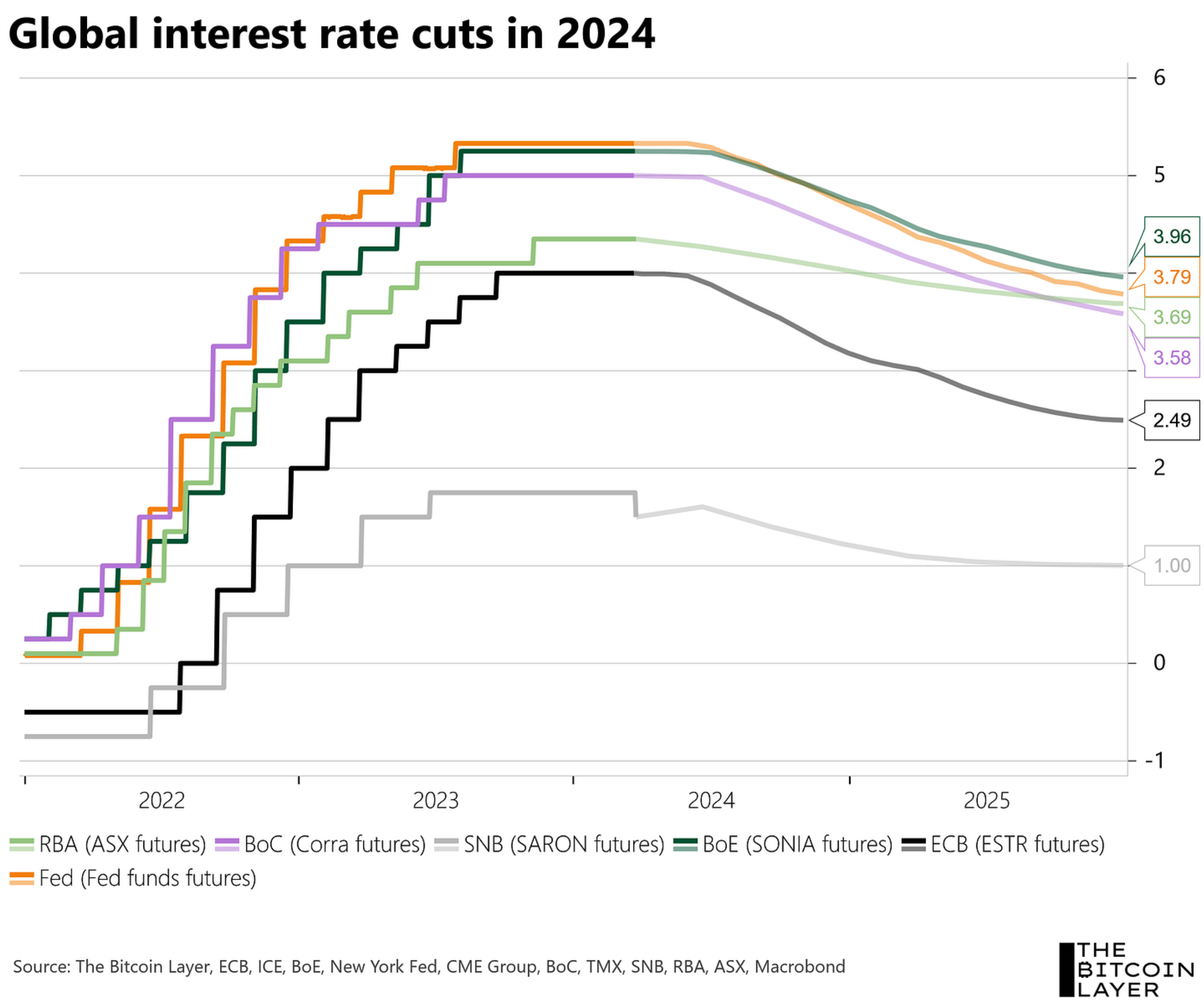
- Move is first among the world's 10 most-traded currencies
- Only a small minority of economists anticipated decision

In a very important preface, the SNB made sure to signal the reasoning for its action:

> *The Swiss National Bank unexpectedly cut its key interest rate by 25 basis points, moving months ahead of global peers as policymakers* ***try to prevent gains in the franc****.*

If the SNB is trying to prevent gains in the franc, what would cause them in the first place? As Switzerland's primary monetary concern is its pseudo-peg with the euro, the expectation of rate cuts in Europe—the EU is in terrible economic shape with Germany in recession—should drive capital, at the margin, away from the euro and into the Swiss franc. Appreciation in the Swiss franc counters the SNB's objectives, therefore requiring a preemptive interest rate cut ahead of the ECB's next move. While we made a call in December 2023 for ECB cuts by March (and Fed cuts by June), the ECB failed to deliver a cut. Now, with the SNB leading the way, we might see the European authorities capitulate.

Europe is certainly a different economic animal than the United States—the continent's economy is struggling relative to the US, with a likely explanation being fiscal dominance on which we will deliberate further today. It makes sense, then, that European central banks are having a go at monetary easing. Notice the first realized cut in silver, while other policy rate futures curves all slope in the same direction, downward:



FOMC keeps cutting outlook

What if Powell is lying to us the whole time, and the cutting outlook is simply due to the fear that the dollar will strengthen too much as everybody else cuts rates, similar to the reasoning the SNB gave early this morning?

You must consider this a possibility before getting into a verbal game of squash with the brick wall that is Fed speak.[1] People overestimate the dual mandate—that is, the market gives too much credence to the Fed being guided by inflation and unemployment. It's much more driven by the stock market and financial stability, and the only evidence you need is the Fed's behavior in each financial crisis (2007-2010, 2019, 2020-2021).

The dual mandate is all for show, and the consensus is struggling with marrying the Fed's overall positive economic outlook, healthy labor market, and persistent inflation with a large cutting cycle:

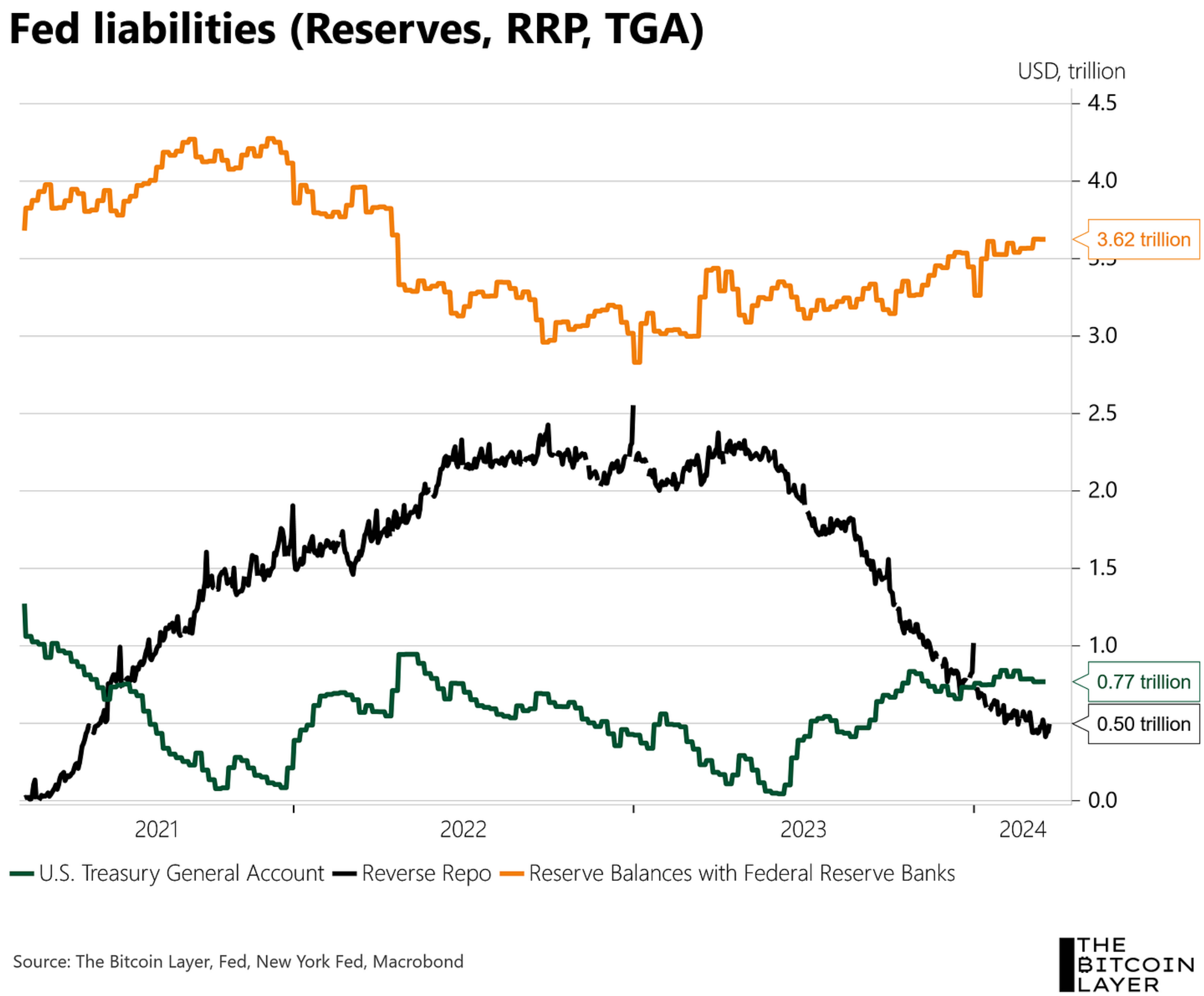
Then the double-speak started, with Powell curiously suggesting progress has continued on disinflation instead of admitting it has stalled:

> *Nevertheless we continue to make good progress on bringing inflation down.*

Really, Jerome? Or is this just a cover?

Not only is the Fed ready to cut rates despite above-target inflation and juicy economic growth, it is also ready to slow QT in order to maintain "ample reserves" and prevent any "disruption in money markets," according to Powell. And this is all a segue to my understanding of the imminent cutting cycle: funding.

As reverse repo (RRP), an emergency cash pool standing by to enter money markets, declines, money markets will need their next source:



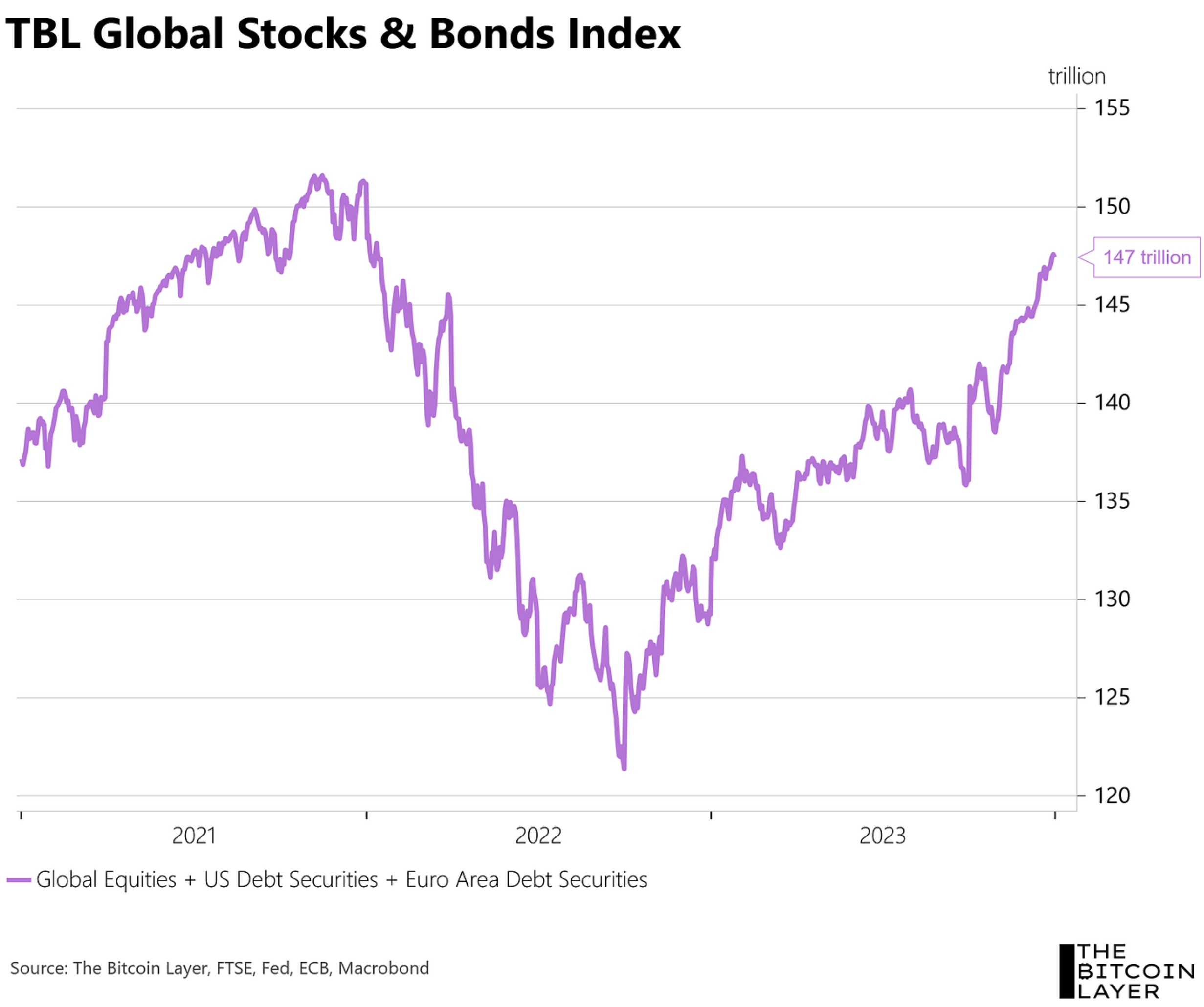
The orange line, reserves, is a potential source of funding, but banks prefer to keep their reserves for a variety of reasons instead of helping a primary dealer in need. Currently, funding is abundant, because SOFR is keeping in line with other money market rates, which means dealers are able to fund their Treasury holdings at tight market rates. Funding is also abundant when corporate bond issuance is sky-high and dealers can shuffle around inventory without headache for the repo desk. RRP still has half a trillion dollars, meaning that there is enough funding to go around still yet.

But it is the funding that will eventually run out, and I believe it is the reason why the Fed understands it has to cut rates soon and stop shrinking its balance sheet, a source of funding. And so, I respond to Lyn Alden's comment with "funding markets":

Back to fiscal dominance now—financial conditions have eased remarkably over the past several months despite high nominal rates because the economy is so strong, of which much has been attributed to the sheer size of the fiscal deficit. High rates exacerbate the deficit, reinforcing economic growth. The problem, however, with fiscal dominance is that it suggests monetary policy is ineffective, but I interpret the Fed reducing rates as an expression that monetary policy is restricting some activity, at the margin, down the road, in funding markets.

One way to think about restrictive funding is a primary dealer that must keep Treasury inventory yielding 4.5% with repo rates at 5.5%—this is a negative charge every day to the bank. While funding is clearly plentiful (RRP, issuance, SOFR rates), it must be imbalanced in its distribution. I might be giving the Fed too much credit here, but that's what *I see them seeing*.

Think about this liquid pool of assets, including 4,000 of the world's largest companies, and then the US and EU investment-grade bond markets. It now stands at around $150 trillion in size:



Many of these assets are not owned outright but are leveraged. This means those positions all have funding needs (lending) and costs (repo rates, margin rates). Five percent policy rates, in my estimation, will cripple some positions at the margins, busting a liquidity cycle clearly in expansion. Now, some of this analysis might sound similar to a Michael Howell, but I am not using his liquidity models or definitions whatsoever here. Instead, I'm suggesting that the current asset markets require a roll, and the train stops from an equity market perspective when that funding finally becomes restrictive. And I believe it eventually will, feeding back into the economy via negative wealth effect, and stopping the train.

Interestingly, we can also assume the reaction function of the Fed in such a scenario, opening the can of worms that comes with unlimited bailout culture.

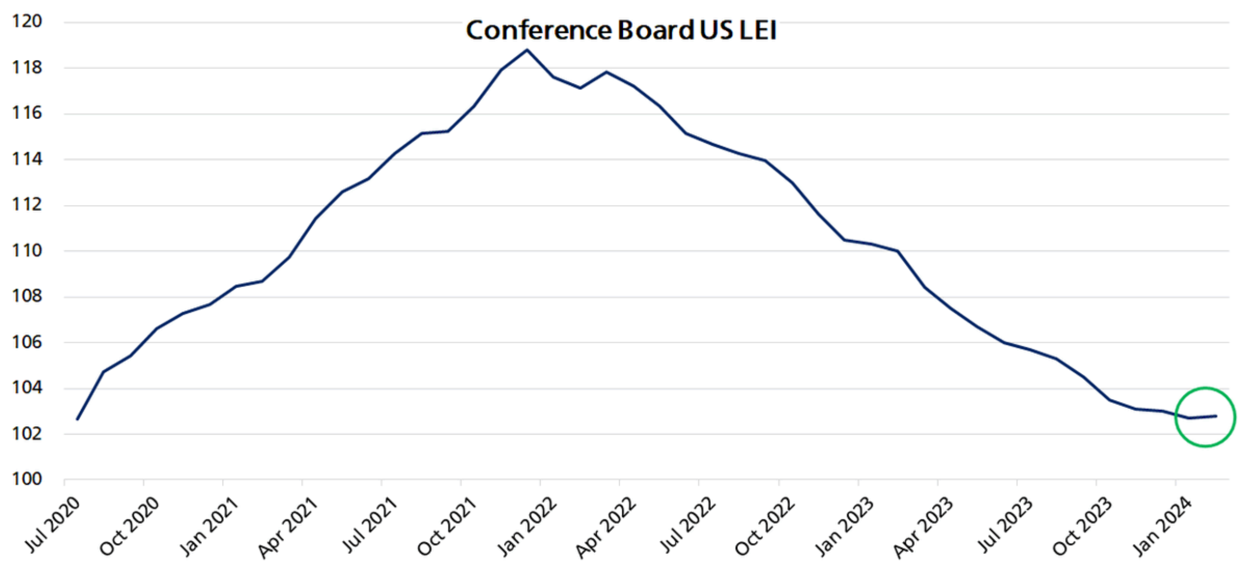
Continue reading here (subscription required).

Leading indicators suggest China's economy is re-awakening in a big way (from Andreas Steno Larsen via X)...

China is on the MOVE! Are you paying attention?

U.S. leading economic indicators also moved slightly higher in February for the first time in two years (from Timothy Peterson, CFA CAIA via X)...

US Leading #Economic Index up 0.4%, the first increase in two years. This is February's number so it has nothing to do with FOMC activity yesterday.

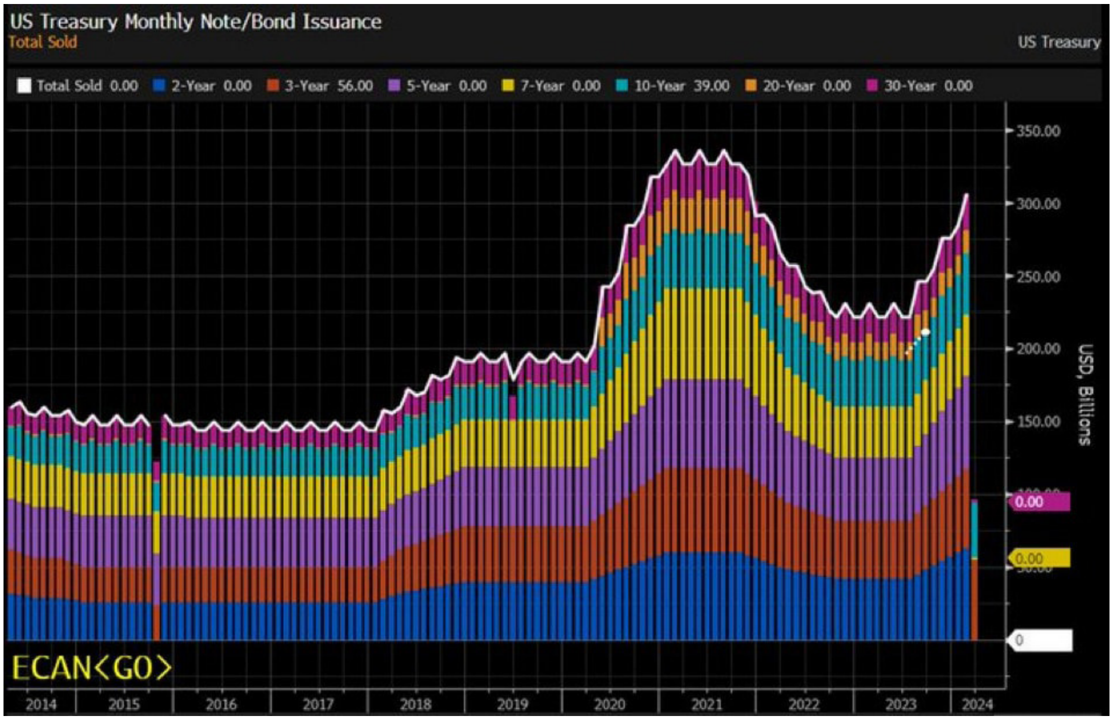


The key takeaways from this month's Fed meeting (from FFTT Tree Rings)...

Our take on the Fed's actions on Wednesday is that they are acting in support of what we have called their "shadow 3rd mandate" (UST market functioning). Check out what the UST MOVE Volatility Index did Wednesday on the Fed's move (below) – it collapsed below what had been a "support" level, suggesting a significant increase in UST market liquidity.

In the short run, all else equal, a weaker USD and more USD liquidity will reduce USD hedging costs and make FX-hedged 10y UST yields more attractive to Japanese & EU investors, as well as increase global balance sheet capacity to buy USTs. As such, we are not surprised to see 10y UST yields decline on the Fed's seemingly inflationary actions. We have repeatedly noted that increasing USD liquidity would likely paradoxically drive LT UST yields lower for a brief period.

Most market participants seem to remain in dogmatic denial about why the Fed seemed so dovish in this week's meeting, but the answer is hiding in plain sight: Monthly UST note/bond issuance is back to near post-COVID highs, despite solid US GDP growth and full US employment!



Via MM

Allow us to bluntly translate the implications of the chart above: A view that Powell is going to be hawkish on inflation in the face of the above is implicitly a view that Powell is going to force sharp cuts to US Baby Boomer Entitlements in an election year and US defense spending in a new Cold War. With respect, in our view there is no way that is going to happen.

As such, this decline in LT UST yields is likely to be a technical, short-term decline in 10y UST yields that will before long require more buying support from a much bigger balance sheet once more USD liquidity and a weaker USD manifests in higher sequential inflation and nominal GDP growth, which should not take too long – we expect it in the next few months.

One final critical point – **note in the chart above how 2021's "Everything Bubble" drove monthly UST note/bond issuance from $325B to $225B; to the extent that the Fed's actions continue to fuel a new "Everything Bubble", this should serve to once again reduce future UST issuance in 6-12 months' time. Having hollowed out our manufacturing sector and financialized our economy, this is now the Fed and Treasury's primary policy lever.**

We continue to believe the US is in fiscal dominance, having been put there by the Fed's mistake of raising rates before inflation had reduced US Federal debt/GDP back to 70-80% from 120%...indeed, US debt/GDP bottomed in 1q23 and has been rising ever since. We also continue to believe much of Wall Street is offsides because they dogmatically refuse to believe US policymakers have effectively allowed the system to evolve to an "Argentina with US characteristics" outcome.

Continue reading here (subscription required).

Congress just passed another $1.2 trillion spending bill (from The Kobeissi Letter via X)...

At the current pace, the US deficit for this fiscal year will cross $3 trillion, nearly double the $1.6 trillion deficit that Congress estimated.

Deficit spending is on track to hit nearly 28% of GDP by 2050.

Meanwhile, Federal revenue will be just ~19% as US debt levels are skyrocketing.

Over the last 100 days, total US debt is up a whopping $1 trillion, an average of $10 billion per day.

We will likely see US debt hit $36 trillion this year.

The spending spree continues.

ECONOMIC POLICY

House sends $1.2 trillion spending bill to Senate hours before deadline

About three-quarters of the federal government will shut down at midnight if the upper chamber doesn't also pass the legislation

Why Apple's anti-trust case matters (from BIG by Matt Stoller)...

Today, the Department of Justice and 16 states led by officials from both political parties filed an antitrust case against Apple, the fourth trillion dollar firm targeted by the Biden administration with an antitrust suit for unfair monopolistic behavior.

This suit is a big deal in and of itself, but it also matters beyond just Big Tech. But it's also a bit unusual, because while Google, Amazon, and Meta have their villain-esque side, Apple is beloved, with some of the strongest branding in the world, and it spends billions on its iconic 'Think Different' imagery. Its smartphones are user-friendly and often seamless, and its CEO Tim Cook talks up the firm's commitments to privacy and consumer protection.

Beyond that, it seems like there's competition, since Android phones are available. Few iPhone customers actually switch, but the point is, theoretically they can. At the very least, it seems like an odd priority to take on a corporation that people like and that makes good products, when there are so many other problems.

So what's the point of the case? On a broad level, the short story is that Apple used to be wondrous. But monopoly power, as it turns out, has poisoned the firm. Once a great innovator, Apple has decayed, moving away from its roots as a competitive technology firm, and spending its resources making it harder and harder for consumers and businesses to get out of the Apple ecosystem, and then trying to extend that ecosystem from smartphones into cars, business software, and banks. Apple has become a dangerous corporation, with designs on imposing an authoritarian vision over as much of the economy as it can get away with.

In other words, the broad allegation is about how power corrupts. The complaint may be about technology, but the story here is as old as time. Let's dive in.

It's Not Just Apple

One of the interesting questions is why Big Tech is in the cross-hairs of antitrust, as opposed to more standard industries like food, medicine, farming, or banks. One answer is that Big Tech firms are the pace-setters of commerce, so what they do, or are not allowed to do, influences every non-tech CEO. But a different answer is that those more standard industries are in the cross-hairs of antitrust. In fact, the suit against Apple must be understood as a mere part of a revolution in policymaking. And oddly enough, that revolution starts with a body most of us disdain. Congress.

In October of 2020, Democratic Congressmen David Cicilline and Republican Congressman Ken Buck released a blockbuster Antitrust Subcommittee report detailing the unfair monopolistic practices of four giant trillion dollar firms: Apple, Facebook, Amazon, and Google. The report was the culmination of a 16 month investigation in which investigators examined millions of documents, interviewed hundreds of business leaders in the industry, and put Big Tech CEOs on the witness stand. These hearings and reports generated headlines all over the world, and showed, in detail, that Big Tech firms weren't big because they were great, they were big because they thwarted rivals through specific business practices.

What kind of impact did that report have? Well, from 1998 until that report in 2020, the Department of Justice didn't file a single monopolization claim against anyone, and certainly not against any powerful firm. Since the release of that report, enforcers in government filed major antitrust suits against Facebook, Amazon, Google, and now Apple. The line from the report to the current multi-trillion dollar assault is direct; one of the key investigators on the Antitrust Subcommittee staff was a young researcher named Lina Khan. And outside of government, private plaintiffs have filed cases as well, with Google for the first time declared an unlawful monopolist in its suit against Epic Games.

The flurry of activity in the competition policy world is hardly isolated to Big Tech. Spurred by the Big Tech report and the energy it helped generate, the government has investigations or suits on meat prices, rent, drugs, epipens, ticketing, airlines, homebuying and supermarkets. Moreover, private litigants, often with support from government, are trying to reorder other areas of the economy, such as the change in commission structures announced by the realtors earlier this week.

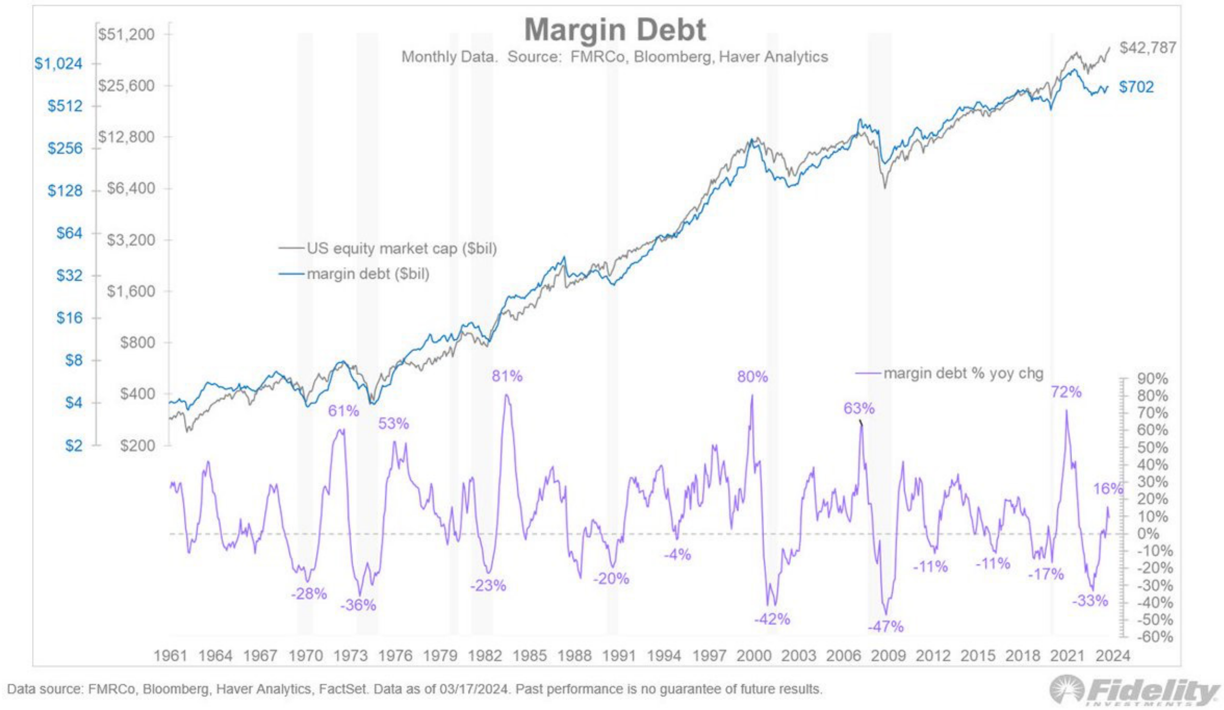
Yesterday another inhaler maker slashed prices to $35 out of pocket in response to FTC pressure. Today, aside from the Apple case, bank regulators tightened merger rules on banks above $100 billion in size, the Department of Transportation started an investigation on airline's use of data to manipulate or price-gouge consumers (with support from Senator Ron Wyden), and the government came out with the results of a major investigation on how big retailers, distributors, and food processors squeezed small businesses and consumers during the pandemic.

All of that is a way of saying that to look at the Apple suit in isolation and ask, as many are, why go after the iPhone, which most people like, instead of addressing more important things, is to miss the bigger picture. Enforcers are dealing with food, medicine, housing, and travel. But they are also going after the titans of industry, which includes Apple. And the suit explains why.

Continue reading here.

Margin debt remains below prior peak extremes (from Jurrien Timmer via X)...

As for sentiment, it doesn't appear that we are at an extreme yet. Margin debt is growing at a 16% clip, which is well below past extremes.



Small speculators are "all in" (from SentimenTrader via X)...

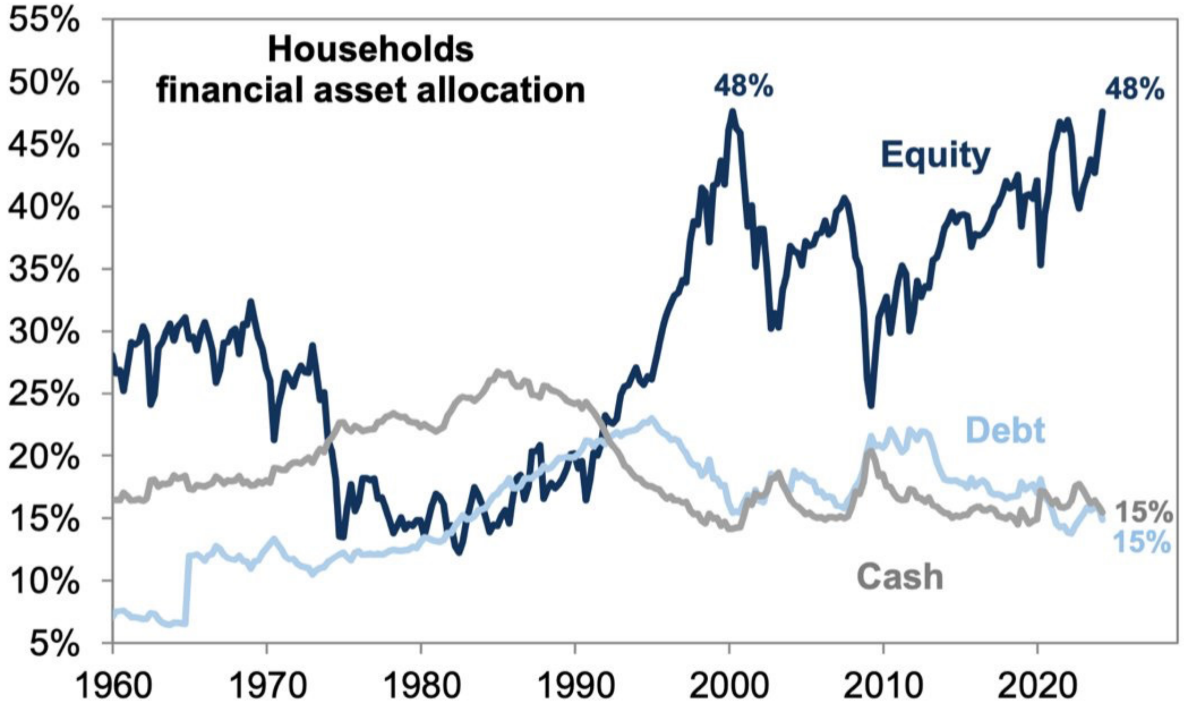
Small speculators in stock indexes have reached their most bullish net position ever.

U.S. households own the most stocks since the peak of the dot-com bubble (from Barchart via X)...

U.S. households are currently allocating 48% of their financial assets to stocks, their highest equity exposure since March 2000. Anything interesting happen in March 2000?

Exhibit 10: US household financial assets allocation

allocations as of 4Q23; asset pricing as of March 20, 2024



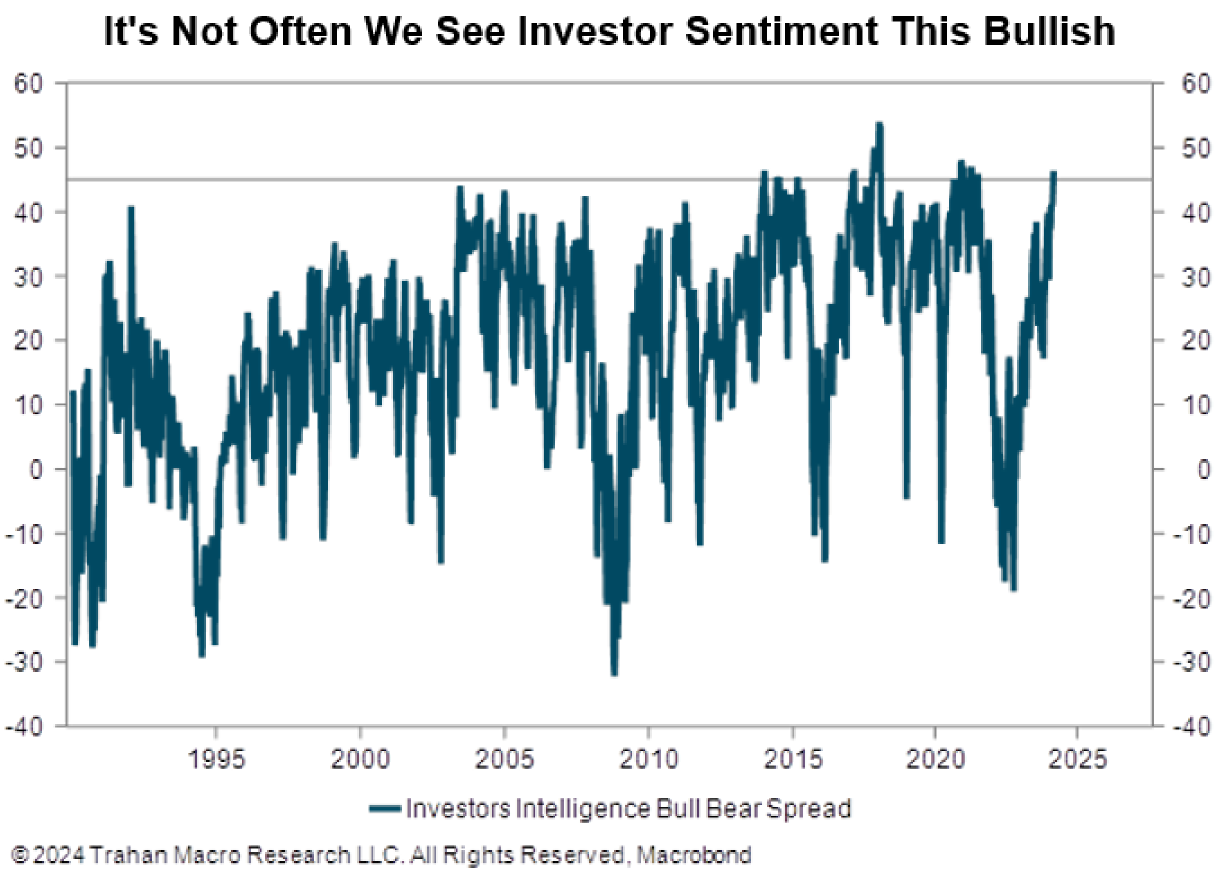
Source: Federal Reserve, Goldman Sachs Global Investment Research

This is officially the longest yield-curve inversion in history (from Barchart via X)...

The 10Y-2Y Yield Curve has been inverted for 431 consecutive trading days, the longest yield curve inversion in history, even surpassing the 1978-1980 inversion under Fed Chair Paul Volcker.

The Investors Intelligence survey shows newsletter writers have rarely been this bullish ([from Francois Trahan, M²SD via X](#))...

I've been tracking the bull/bear spread from Investors Intelligence for as long as I can remember. It's not the type of thing I look at every week or even every month, but when it feels like sentiment is extreme, I like to be able to quantify it and this is a great tool for that.



I remember using this chart in the Fall of 2022 and pointing out at the time that I had only seen such bearish sentiment once in my career at the height of the GFC. Today's bullish readings were seen twice during the great bull market of the 2010s and in the post-pandemic rally.

While this is not a precise timing tool, all three episodes were followed by major market corrections. This just tells us that consensus is very bullish and the market is vulnerable to disappointment. We shall see.

THE LEGENDS SPEAK

Wisdom and Insight From the World's Greatest Investors

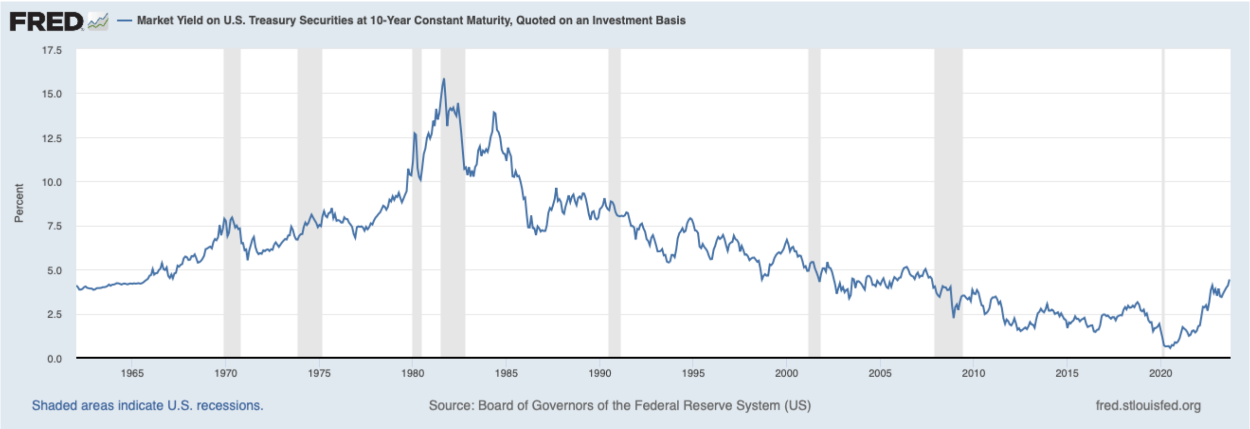
Here's a detailed look at Warren Buffett's classic wisdom on inflation (from The Rational Walk)...

The passage of time plays tricks on our memories. Agonizingly slow trials and tribulations in the present appear less extreme when viewed retrospectively.

The historical narrative of the inflation that took hold from the middle of the 1960s to the early 1980s is told knowing that Paul Volcker would have the fortitude to dispense the medicine needed to finally break the fever. However, people who actually lived through those years had no such advance knowledge and conventional wisdom was that high inflation would persist in the 1980s and perhaps indefinitely.

Long term treasuries yielded above 15% in 1981 in anticipation of years of high inflation. When the rate of inflation started to decline, interest rates remained relatively high for many years as market participants remained skeptical.

The exhibit below shows the yield on the ten year treasury since 1962. What's interesting about the chart is that the current ten year yield of around 4.5% is comparable to yields seen in the mid-1960s and remains *very low* from a historical perspective. Many charts published in the financial media seem to start around 2005 which creates the false illusion that current rates are historically high.



Source: St. Louis Fed

Double-digit inflation did not return after the spike of the early-1980s and yields began a long multi-decade decline. This decline was hardly in a straight line and those who actually lived through the upward squiggles in the chart could very well have declared the end of the bond bull market at numerous times. In the 1980s, anyone who predicted that the ten year treasury would eventually yield *under 1%* in 2020 might have been involuntarily committed to a mental institution for observation.

Even Warren Buffett was surprised by the taming of inflation during the 1980s based on comments in his shareholder letters. In early 1987, Mr. Buffett was still expecting a return to higher levels of inflation when he wrote about his distaste for long-term bonds, predicting "much higher rates of inflation within the next decade."

While I personally recall the later years of the Great Inflation, the extent of my dismay was mostly restricted to feeling cheated when comic books went from 40 cents to a shocking 75 cents over just a few years. But fortunately, reading provides a window to the past as seen through the eyes of people who lived through it.

I've read Warren Buffett's letters to shareholders sequentially many times. By doing so we can see how Berkshire Hathaway evolved over the decades in "real-time" rather than with the benefit of hindsight. My interest in reading about the Great Inflation of the 1970s and early 1980s recently inspired a return to the letters of that period.

Links to the first two articles in this series appear below. Part one covers Mr. Buffett's views on bonds and interest rates in early 1970. Part two is an overview of how Berkshire's auto insurance business was caught by surprise during the mid-1970s. In this article, I will focus on Warren Buffett's comments regarding the great advantage of owning capital-light businesses with pricing power during inflationary times.

Warren Buffett on Inflation — Part 1

Warren Buffett on Inflation — Part 2

False Comfort

"For years the traditional wisdom – long on tradition, short on wisdom – held that inflation protection was best provided by businesses laden with natural resources, plants and machinery, or other tangible assets ('In Goods We Trust'). It doesn't work that way. Asset-heavy businesses generally earn low rates of return – rates that often barely provide enough capital to fund the inflationary needs of the existing business, with nothing left over for real growth, for distribution to owners, or for acquisition of new businesses."

— Warren Buffett, Appendix to 1983 letter to shareholders

Generations of Benjamin Graham's disciples have started with the balance sheet when analyzing a business. The quest for companies trading at less than book value, or better yet, below net current asset value, has long been viewed as the cornerstone of intelligent investing. This was true for Warren Buffett for a long time and he had great success with investments such as Dempster Mill during the partnership years, and this is what led Mr. Buffett to acquire control of Berkshire Hathaway itself.

Of course, aside from liquidation scenarios, the analyst must closely examine the income statement over many years to be satisfied that the enterprise is capable of earning an adequate return on equity. A poor business incapable of earning an adequate return on equity will justifiably see its stock trade below book value since buyers will demand an adequate return on their investment. In contrast, a great business that delivers a return on equity far in excess of the average business can be expected to trade far above book value.

With Charlie Munger's help, Warren Buffett began to shift his attention toward intangible assets in the early 1970s. As Mr. Munger pointed out decades later, it is difficult to move away from an approach that had worked so well for so long:

> *"I don't love Ben Graham and his ideas the way Warren does. You have to understand, to Warren — who discovered him at such a young age and then went to work for him — Ben Graham's insights changed his whole life, and he spent much of his early years worshiping the master at close range. But I have to say, Ben Graham had a lot to learn as an investor. His ideas of how to value companies were all shaped by how the Great Crash and the Depression almost destroyed him, and he was always a little afraid of what the market can do. It left him with an aftermath of fear for the rest of his life, and all his methods were designed to keep that at bay."*

What worked so well for Ben Graham in depression-era markets, and continued working well for Warren Buffett as he started his career in the 1950s, would not work nearly as well in the inflationary environment of the late 1970s. In his 1983 letter to shareholders, Mr. Buffett contrasts asset-heavy enterprises with companies that have significant intangible assets and minimal need for tangible assets:

> *"In contrast, a disproportionate number of the great business fortunes built up during the inflationary years arose from ownership of operations that combined intangibles of lasting value with relatively minor requirements for tangible assets. In such cases earnings have bounded upward in nominal dollars, and these dollars have been largely available for the acquisition of additional businesses. This phenomenon has been particularly evident in the communications business. That business has required little in the way of tangible investment – yet its franchises have endured. During inflation, Goodwill is the gift that keeps giving."*

Economic goodwill is not an asset that can be estimated with great precision. When accounting goodwill exists on a balance sheet, it is the result of a business acquisition that was made for a sum greater than the identifiable assets of the acquired business. In 1983, accounting goodwill was subject to amortization over forty years.[1] However, as Mr. Buffett explained in the letter, the economic goodwill of an excellent business is more likely to grow over time than to shrink.

Many businesses with significant economic goodwill have no accounting goodwill on their balance sheet. A start-up that generates economic goodwill over time will not have any balance sheet account for goodwill. It is only when a business is acquired that accounting goodwill will appear on the balance sheet of the purchaser.

It seems intuitive that one would want to own businesses with a large amount of tangible assets during inflationary times based on the idea that those tangible assets should be worth more after taking the effects of inflation into account. But favoring businesses with a great deal of tangible assets just because they are visible on the balance sheet is a false comfort.

See's Candies vs. "A Mundane Business"

During my childhood in California, no holiday season was complete without at least a few boxes of See's Candies. For those who have never lived in California, it's difficult to understand the formidable brand that See's had developed by the 1970s. The only negative was that few people would eat See's year round. It was very much a candy for special occasions, but this also meant that customers were not very price sensitive.

By 1983, Berkshire Hathaway had owned See's Candies for over a decade and Warren Buffett reflected on the company's economics in the appendix to his 1983 letter to shareholders. The unexciting title of the appendix is *"Goodwill and its Amortization: The Rules and The Realities"* which probably deterred many readers from proceeding. But the appendix is really about the benefits of companies with economic goodwill during inflationary times — a far more exciting topic — with See's as a case study.

When Blue Chip Stamps acquired See's Candies in 1972 for $25 million, See's had $8 million of net tangible assets and was earning $2 million after tax.[2] When Berkshire paid $17 million over net tangible assets, this generated $17 million of accounting goodwill that was slowly amortized into expenses over many years.

Obviously, it would have been wonderful to purchase a business earning $2 million after tax for just $8 million. However, the ability of a business to earn 25% after tax on net tangible assets obviously indicated the presence of valuable economic goodwill. Although Mr. Buffett might have considered paying $25 million for a business earning $2 million to be a rich price, Charlie Munger was more willing to consider intangible assets and was strongly in favor of the purchase.

Warren Buffett explained the purchase rationale as follows:

> *"In 1972 (and now) [early 1984] relatively few businesses could be expected to consistently earn the 25% after tax on net tangible assets that was earned by See's – doing it, furthermore, with conservative accounting and no financial leverage. It was not the fair market value of the inventories, receivables or fixed assets that produced the premium rates of return. Rather it was a combination of intangible assets, particularly a pervasive favorable reputation with consumers based upon countless pleasant experiences they have had with both product and personnel.*
>
> *"Such a reputation creates a consumer franchise that allows the value of the product to the purchaser, rather than its production cost, to be the major determinant of selling price. Consumer franchises are a prime source of economic Goodwill. Other sources include governmental franchises not subject to profit regulation, such as television stations, and an enduring position as the low cost producer in an industry."*

In 1983, See's earned $13.7 million after taxes on $20 million of net tangible assets. In other words, See's went from earning 25% on net tangible assets to 68.5% over eleven years. As Mr. Buffett points out, this indicates the presence of economic goodwill far larger than the original cost of accounting goodwill.

See's produced extraordinary results during a period of high inflation, as we can see from the following table from the 1983 shareholder letter:

52-53 Week Year Ended About December 31	Sales Revenues	Operating Profits After Taxes	Number of Pounds of Candy Sold	Number of Stores Open at Year End
1983 (53 weeks) ...	$133,531,000	$13,699,000	24,651,000	207
1982	123,662,000	11,875,000	24,216,000	202
1981	112,578,000	10,779,000	24,052,000	199
1980	97,715,000	7,547,000	24,065,000	191
1979	87,314,000	6,330,000	23,985,000	188
1978	73,653,000	6,178,000	22,407,000	182
1977	62,886,000	6,154,000	20,921,000	179
1976 (53 weeks) ...	56,333,000	5,569,000	20,553,000	173
1975	50,492,000	5,132,000	19,134,000	172
1974	41,248,000	3,021,000	17,883,000	170
1973	35,050,000	1,940,000	17,813,000	169
1972	31,337,000	2,083,000	16,954,000	167

Source: Warren Buffett's 1983 shareholder letter

It is remarkable that a company that generated $31.3 million of sales in 1972 using $8 million of net tangible assets could generate $133.5 million of sales in 1983 using just $20 million of net tangible assets. We can see from the table that See's had very strong pricing power throughout this period. The implied price per pound rose from $1.85 in 1972 to $5.42 in 1983. Although physical volume of candy sales slowed toward the end of the period, price increases continued to deliver enhanced profitability.

Warren Buffett presents readers with a thought experiment comparing the purchase of See's Candies in 1972 to a hypothetical "mundane" business:

> *"… Let's contrast a See's kind of business with a more mundane business. When we purchased See's in 1972, it will be recalled, it was earning about $2 million on $8 million of net tangible assets. Let us assume that our hypothetical mundane business then had $2 million of earnings also, but needed $18 million in net tangible assets for normal operations. Earning only 11% on required tangible assets, that mundane business would possess little or no economic Goodwill.*
>
> *"A business like that, therefore, might well have sold for the value of its net tangible assets, or for $18 million. In contrast, we paid $25 million for See's, even though it had no more in earnings and less than half as much in 'honest-to-God' assets. Could less really have been more, as our purchase price implied? The answer is 'yes' – even if both businesses were expected to have flat unit volume – as long as you anticipated, as we did in 1972, a world of continuous inflation."*

The following summary shows the scenario described above in tabular form:

	See's Candies	"Mundane" Business
Net Tangible Assets	$8 million	$18 million
After-tax Earnings	$2 million	$2 million
Return on net tangible assets	25%	11%
Market value of business	$25 million	$18 million
Return on purchase price	8%	11%

It is doubtful that an investor rigidly applying Benjamin Graham's principles would buy either company, but if forced to choose, such an investor would almost certainly prefer the mundane business given that it could be purchased at book value, implying a larger margin of safety, and provided a higher initial return on the purchase price.

My initial reaction when reading this section was that the missing element is that See's could be expected to grow while the "mundane" business might not. However, Mr. Buffett explains how See's represented greater value in "a world of continuous inflation" even if both businesses were expected to have flat unit volume.

If we assume that the price level doubles, how would this affect these businesses? They would both need to double nominal earnings to $4 million to represent flat earnings in real terms. If each business could maintain the same unit volume while doubling prices, profits would also double assuming that margins stay the same.

But there is crucial difference:

> *"But, crucially, to bring that about, both businesses probably would have to double their nominal investment in net tangible assets, since that is the kind of economic requirement that inflation usually imposes on businesses, both good and bad. A doubling of dollar sales means correspondingly more dollars must be employed immediately in receivables and inventories. Dollars employed in fixed assets will respond more slowly to inflation, but probably just as surely. And all of this inflation-required investment will produce no improvement in rate of return. The motivation for this investment is the survival of the business, not the prosperity of the owner."*

In the table below, I have summarized the scenario for the two businesses following the doubling of the price level:

	See's Candies	"Mundane" Business
Original Level of Net Tangible Assets	$8 million	$18 million
Additional investment in tangible assets	$8 million	$18 million
New Level of Net Tangible Assets	$16 million	$36 million
After-tax Earnings	$4 million	$4 million
Market value of business	$50 million	$36 million
Δ Market Value / Additional investment	> 3-to-1	1-to-1

Both See's Candies and the mundane business must double net tangible assets in order to double after-tax earnings. However, See's only requires an incremental $8 million of investment while the mundane business requires $18 million. Under this scenario, we can expect that the market value of both businesses would double. **However, See's only had to invest $8 million in incremental net tangible assets to generate $25 million of incremental market value. In contrast, the mundane business invested $18 million to generate $18 million of incremental market value.**

What kind of alchemy can convert $8 million of additional investment into $25 million of market value? The answer is the presence of economic goodwill. Economic goodwill doubled from $17 million to $34 million, but this doubling required not a single dollar of incremental capital investment. **The value of the goodwill kept up with inflation but required no capital investment from the owners of the business.**

Conclusion

See's Candies was not only a dream business for Berkshire from an economic perspective but represented a real-life case study that changed Warren Buffett's approach to capital allocation in the half century that followed. Of course, Charlie Munger's insight played a major role in bringing about this transformation.

In his 2007 letter to shareholders, Mr. Buffett reported that See's generated $383 million of sales with pre-tax profits of $82 million. Remarkably, the capital required to run the business was only $40 million. Only $32 million in incremental capital had to be invested between 1972 and 2007 to handle the growth of the business. Cumulative pre-tax profits on that initial $25 million purchase totaled $1.35 billion, with all of that cash sent to Berkshire to acquire other businesses. Unfortunately, companies with the economics of See's Candies are few and far between:

> *"There aren't many See's in Corporate America. Typically, companies that increase their earnings from $5 million to $82 million require, say, $400 million or so of capital investment to finance their growth. That's because growing businesses have both working capital needs that increase in proportion to sales growth and significant requirements for fixed asset investments.*
>
> *"A company that needs large increases in capital to engender its growth may well prove to be a satisfactory investment. There is, to follow through on our example, nothing shabby about earning $82 million pre-tax on $400 million of net tangible assets. But that equation for the owner is vastly different from the See's situation. It's far better to have an ever-increasing stream of earnings with virtually no major capital requirements. Ask Microsoft or Google."*

See Candies is a tremendous business but has proven to be quite limited in terms of growth opportunities beyond the west coast. If See's had the ability to generate its returns on tangible assets while also being able to reinvest those earnings at the same rate, it would be a compounding powerhouse. Instead, it has been a cash cow for Berkshire and fueled acquisitions in totally different fields.

It seems fitting to conclude by noting that Warren Buffett did not have perfect foresight when it came to predicting the Great Inflation or the disinflation of the 1980s. In fact, he clearly expected high inflation to persist into the 1980s and beyond. But nailing a macro forecast was not required for Berkshire Hathaway to thrive.

A closer look at Warren Buffett's 2023 annual letter to Berkshire Hathaway shareholders (from Kingswell)...

Over the weekend, Berkshire Hathaway released its 2023 annual report — alongside Warren Buffett's much-anticipated letter to shareholders. (And, while I'm not exactly an impartial observer to all things Buffett, I thought it more than lived up to the hype.)

For those of us who try to use his annual writings to better understand both the man's methods and Berkshire's larger performance, it can be a bit of information overload. The complete report stretches on for over 150 pages and, as Buffett notes, "is filled with a vast amount of information — some important, some trivial".

So, in an effort to drill down past the trivial (and, also, to keep this article to a manageable length), I've picked out a few of the most significant lines from Buffett's latest letter for deeper study.

Ones that reveal the most about his current outlook on Berkshire's prospects and reinforce the timeless lessons that he has spent his life teaching to us.

"In reality, Charlie was the 'architect' of the present Berkshire, and I acted as the 'general contractor' to carry out the day-by-day construction of his vision."

Warren Buffett opens the annual report with a heartfelt tribute to his late partner, Charlie Munger. The Berkshire Hathaway vice-chairman passed away on November 28, 2023 — just a few weeks short of his centenary.

As expected, Buffett lavishes praise and gratitude on Munger here — once again crediting his late friend with steering him away from the Grahamian cigar-butt investing of his youth and towards wonderful businesses (at fair prices) instead.

To Charlie's inimitable eye, scrounging for discarded cigar butts — while undeniably profitable in the decades after the Great Depression — posed inherent limits of scale.

"[Charlie] told me — correctly! — that I had made a dumb decision in buying control of Berkshire," Buffett writes. "But, he assured me, since I had already made the move, he would tell me how to correct my mistake."

The Munger message was simple: "Warren, forget about ever buying another company like Berkshire. But now that you control Berkshire, add to it wonderful companies purchased at fair prices and give up buying fair businesses at wonderful prices."

Throughout his long life, Charlie always insisted that Buffett gave him far too much credit for this awakening. Buffett, in turn, refused to stop — never missing a chance to tell the world about Munger's pivotal role in the Berkshire story.

There's probably no better proof of their unshakeable friendship than the fact that these two men spent their entire lives falling all over each other trying to give the other one all the credit for Berkshire's success.

And, in this year's letter, Buffett gets the last word.

"Our preference [to exclude unrealized gains/losses from net income] was pretty much the rule until 2018, when the 'improvement' was mandated. Galileo's experience, several centuries ago, should have taught us not to mess with mandates from on high. But, at Berkshire, we can be stubborn."

This has, quite understandably, become a recurring theme of sorts in Warren Buffett's letters: An annual lamentation of the misguided FASB mandate to include unrealized gains and losses from stock investments in a company's net income number.

To illustrate the absurdity of this rule change, Buffett marvels at how Berkshire Hathaway's net earnings can swing from plus $90 billion in 2021 to a $23 billion loss in 2022 to, finally, a $96 billion gain last year. You're apt to get whiplash reading that.

Does this rollercoaster ride of highs and lows tell the tale of a conglomerate in crisis?

Nope, it's just the latest example of mark-to-market madness.

In truth, Berkshire's operating earnings (Buffett's preferred performance metric) have marched steadily upwards in recent years. In Q4 2023, these earnings increased by an impressive 28%.

Remember: Accounting should illuminate — not complicate.

And, for companies like Berkshire, the mandate to include paper gains and losses in net income will almost always lead to confused analysis and distorted results. (As Buffett points out in his letter, these unrealized price swings "can exceed $5 billion a day" in Berkshire's massive common stock portfolio.)

I won't belabor the point, but I do want to add one thing: No one has championed ethical accounting and consistent methods of financial disclosure more than Buffett. Which makes this whole situation all the sadder. He probably hates having to question the validity of GAAP figures in his widely-read letter.

But, in the interests of his shareholders, he cannot be expected to hold his tongue. The FASB has basically backed him into a corner and cannot complain when he notes that their mandated net income numbers are "worse-than-useless".

"[Ajit Jain's] achievements since joining Berkshire have been supported by a large cast of hugely-talented insurance executives in our various [property-casualty] operations. Their names and faces are unknown to most of the press and the public. Berkshire's lineup of managers, however, is to P/C insurance what Cooperstown's honorees are to baseball."

Berkshire Hathaway's insurance operations did a lot of the heavy lifting in 2023 — with all three segments logging successful years. GEICO, in particular, continued its rise from the dead with $3.6 billion in pre-tax earnings. Those six straight quarters in the red (during 2021 and 2022) are now just a distant memory.

The auto insurer's combined ratio clocked in at an impressive 90.7% — far below last year's disastrous 104.8%. It even bested Ajit Jain's own preliminary estimate — "just south of 100%" — given at the annual meeting back in May.

Elsewhere, earnings at Berkshire's Primary Group rocketed up 250% and Reinsurance followed with a 30% gain of its own.

Berkshire's float grew to a staggering $169 billion at year's end. And it continues to come at no cost to the company thanks to these sterling underwriting results.

Just imagine showing up at the bank and asking to borrow $169 billion at a 0% interest rate. You'd surely get laughed out of the building — and quite possibly carted off to the loony bin. But that's pretty much what Berkshire's insurance operations have managed to achieve here. Long may that continue.

"Berkshire can sustain financial surprises, but we will not knowingly throw good money after bad."

Things are not quite as rosy in other corners of Warren Buffett's fiefdom.

Here, he paints a bleak picture and sounds almost shaken by the situation unfolding at Berkshire Hathaway Energy. The utility's earnings plummeted 40.3% last year — significantly weighed down by forest fire litigation on the West Coast.

According to the 10-K: "The decline reflected an increase in energy operating expenses, including an increase in estimated pre-tax loss accruals of $1.6 billion ... for wildfires in 2020 and 2022 that arose in Oregon and California."

Buffett levels his harshest criticism at the regulatory apparatus that has seemingly put BHE in its crosshairs. "The regulatory climate in a few states has raised the specter of zero profitability or even bankruptcy," he writes. "In such jurisdictions, it is difficult to project both earnings and asset values in what was once regarded as among the most stable industries in America."

Yikes.

He then goes on to mention Pacific Gas & Electric (filed for bankruptcy in 2019) and Hawaiian Electric (seemingly on its way towards bankruptcy). Not an encouraging comparison for PacifiCorp, the BHE subsidiary on the hook for these wildfires.

Buffett goes on to say that the "fixed-but-satisfactory-return pact [of the electric utility business] has been broken in a few states". And not by BHE.

He adds that it will be many years before Berkshire "can intelligently make decisions about the desirability of future investments in vulnerable western states".

Buffett sounds incredibly frustrated. Like a guy who is re-thinking a lot of things about BHE's heavy investment in the western United States. As he says in the quote above, "We will not knowingly throw good money after bad."

If PacifiCorp is going to get hammered by regulators and juries after every natural disaster in western states, that's going to be big problem. Not just for BHE. Not just for other electric utilities operating in the area. But for the country as a whole.

"A century from now, BNSF will continue to be a major asset of the country and of Berkshire. You can count on that."

The situation at Berkshire Hathaway's railroad is not quite as happy as the above quote might suggest. Earnings fell 14.4% in 2023 due to disappointing freight volumes (led by a big drop in consumer products) and ballooning labor costs.

"BNSF's earnings declined more than I expected," Buffett admits, "as revenues fell. Though fuel costs also fell, wage increases, promulgated in Washington, were far beyond the country's inflation goals. This may recur in future negotiations."

Most worrying, though, is that BNSF's profit margins continue to slip compared to its five principal North American competitors. That needs fixing toot suite.

Buffett expects nothing less. "I believe that our vast service territory is second to none and that, therefore, our margin comparisons can and should improve."

His commentary on BNSF can certainly be read as a shot across the bow at management — but, unlike the BHE section, Buffett ends on a stridently optimistic note about the railroad's long-term place in the world.

"There remains only a handful of companies in this country capable of truly moving the needle at Berkshire, and they have been endlessly picked over by us and by others. Some we can value; some we can't. And, if we can, they have to be attractively priced."

Warren Buffett remains on the hunt for that all-too-elusive elephant. A company both large enough — and priced reasonably enough — to make an impact. As Buffett says, that leaves a very small universe of possibilities to choose from.

This dilemma has resulted in Berkshire Hathaway's cash pile soaring to $163.3 billion. And, while its staggering size rankles some who would prefer to see this money put to work, I rest comfortably knowing that Buffett has so much dry powder with which to attack the market. I'd rather that he remain patient and carefully pick out just the right pitch to swing at — because that invariably means good things for shareholders.

FYI: I don't typically include cash from "Railroads, Utilities, & Energy" in this total, so you may see a bigger cash number — like $167.6 billion — elsewhere.

"All stock repurchases should be price-dependent. What is sensible at a discount to business-value becomes stupid if done at a premium."

In all, Berkshire Hathaway repurchased $9.2 billion worth of its own stock during 2023 — with $2.2 billion of that total coming in the fourth quarter.

Here's what Warren Buffett spent each month on share repurchases:

- October — $948.8 million
- November — $1.1 billion
- December — $55.7 million

Despite buybacks coming to a screeching halt in December, they've picked right back up again in the new year. If my back-of-the-napkin math is correct, Berkshire has repurchased 995 Class A equivalents in the first six weeks of 2024.

And, based on that "price-dependent" quote above, one would assume that the lion's share of these repurchases came in the first half of January — before Berkshire's big run-up in price.

"Though we very much like our ownership, as well as the option [to increase our stake in the future by exercising warrants], Berkshire has no interest in purchasing or managing Occidental."

Here, Warren Buffett reiterates that he has no interest in acquiring a majority ownership interest in Occidental Petroleum. But, importantly, he does describe it as an investment that he "expects to maintain indefinitely".

It's always a fun little parlor game to see who does — and does not — receive shout-outs in Buffett's annual letter. And, on that score, Vicki Hollub must be feeling pretty good today.

"Under Vicki Hollub's leadership, Occidental is doing the right things for both its country and its owners," Buffett enthuses. "No one knows what oil prices will do over the next month, year, or decade. But Vicki does know how to separate oil from rock — and that's an uncommon talent, valuable to her shareholders and to her country."

Berkshire Hathaway currently owns 28.2% of Occidental Petroleum. If Buffett exercises those aforementioned warrants, it would jump up to 34.4%.

"In 1863, Hugh McCulloch, the first Comptroller of the United States, sent a letter to all national banks. His instructions included this warning: 'Never deal with a rascal under the expectation that you can prevent him from cheating you.' Many bankers who thought they could 'manage' the rascal problem have learned the wisdom of Mr. McCulloch's advice — and I have as well. People are not that easy to read. Sincerity and empathy can easily be faked. That is as true now as it was in 1863."

I'm sure I'm not the only one who read that passage and immediately thought of Berkshire Hathaway's recent legal wranglings with the Haslam family.

Berkshire paid $2.6 billion for the final 20% of Pilot Travel Centers after both sides shelved their respective lawsuits and agreed to a settlement back in January. That's quite a bit less than the $3+ billion that most were expecting. We'll never find out for sure, but it sure seems like Berkshire got the upper hand in settlement negotiations.

"Sincerity and empathy can easily be faked." Hmm, now who can he be talking about there?

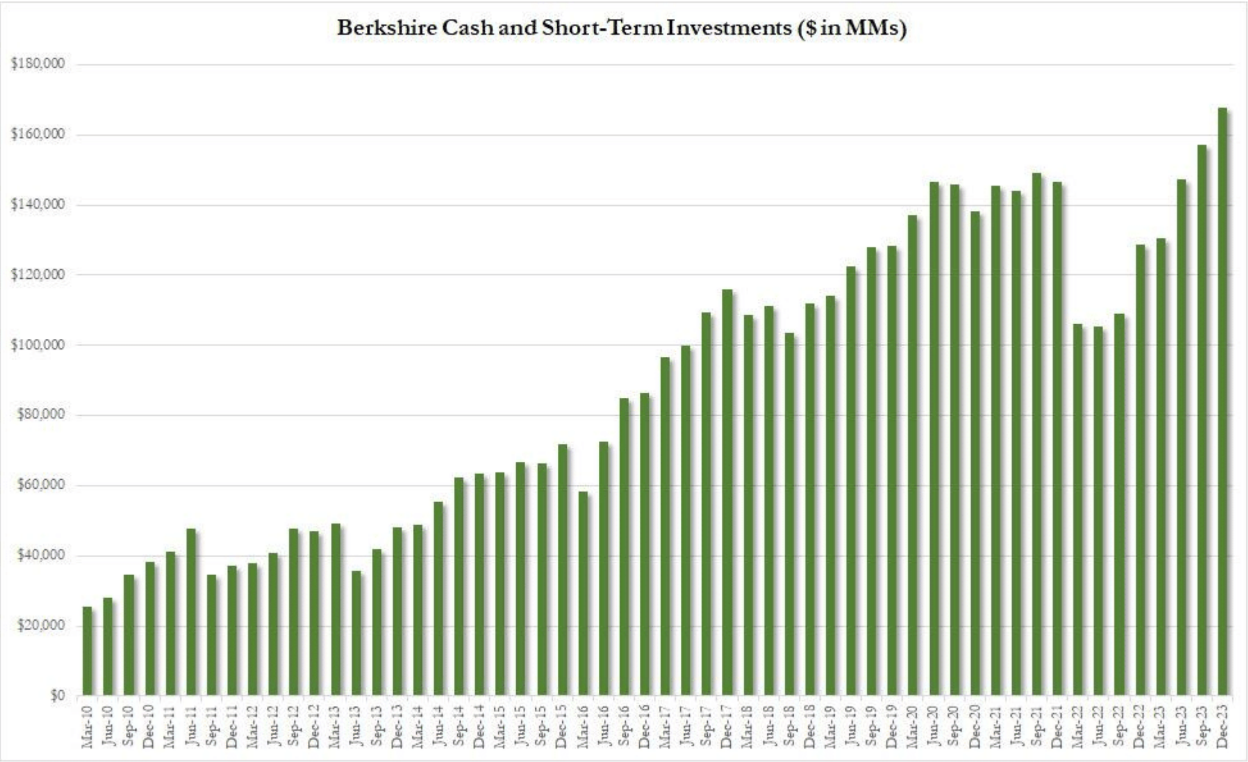
A few more great lines from the letter…

- "Over the years, Berkshire has attracted an unusual number of such 'lifetime' shareholders and their heirs. We cherish their presence and believe they are entitled to hear every year both the good and bad news, delivered directly from the CEO and not from an investor-relations officer or communications consultant forever serving up optimism and syrupy mush."
- "When you find a truly wonderful business, stick with it. Patience pays, and one wonderful business can offset the many mediocre decisions that are inevitable."
- "Though the stock market is massively larger than it was in our early years, today's active participants are neither more emotionally stable nor better taught than when I was in school … Markets now exhibit far more casino-like behavior than they did when I was young. The casino now resides in many homes and daily tempts the occupants."
- "America has been a terrific country for investors. All they have needed to do is sit quietly, listening to no one."

Berkshire's dilemma about cash and valuations (from RIA Advice)...

> *"One of the longest-running traditions in modern finance is that every year, one Saturday morning in late February, the world's financial class – from professionals to mere amateurs – sits down as they have for the past 65 or so years – for an hour and read the latest Berkshire annual letter written by Warren Buffett. In that letter, the man seen by many as the world's greatest investor, wrote down his reflections, observations, aphorisms and other thoughts which are closely parsed and analyzed for insight into what he may do next, what he thinks of the current economy and market climate, or simply for insights into how to become a better investor."* – Tyler Durden

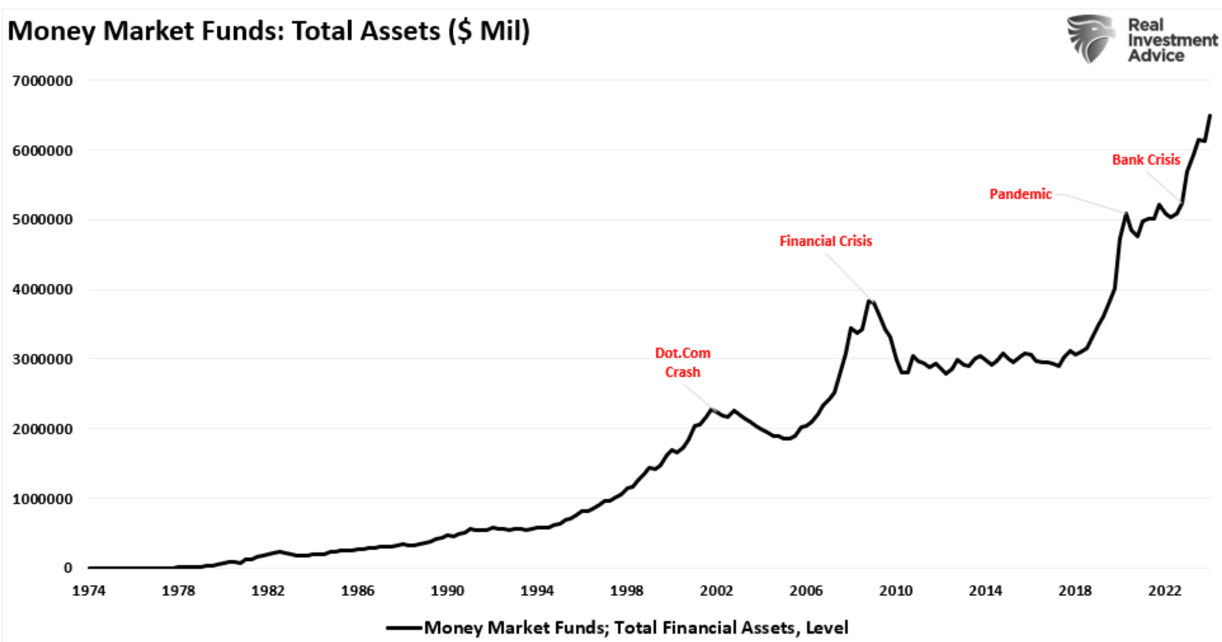
His latest letter was no different, with various tidbits for investors to digest concerning the current market and investing environment. The one thing that got most of my attention was his comments about the recent surge in cash holdings. Berkshire's cash and short-term investments *(read T-bills)* now exceed $160 billion.



To put that into context, that cash pile alone would make Berkshire the 59th-largest economy in the world, only slightly smaller than Ukraine.

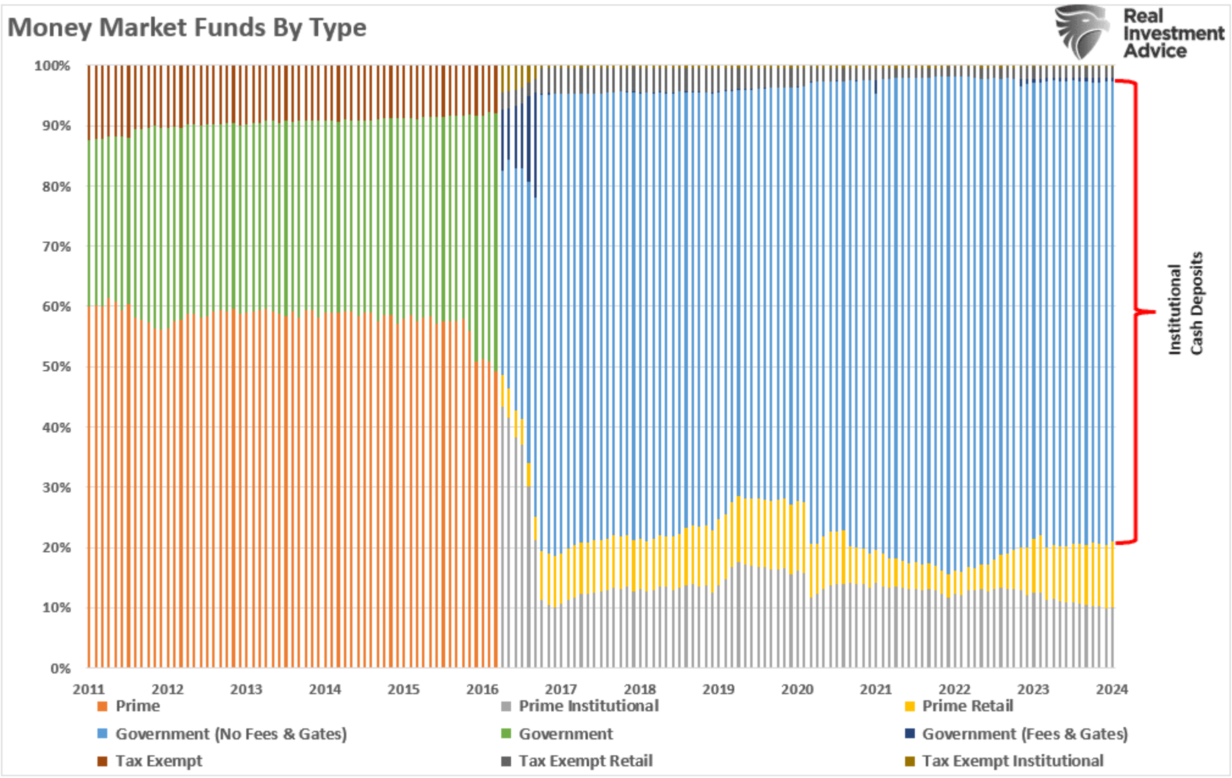
56	Algeria	Africa	224,107	2023	191,913	2022	163,473	2021
57	Hungary	Europe	203,829	2023	178,789	2022	181,848	2021
58	Ukraine	Europe	173,413	[n 6]2023	160,503	[n 6]2022	200,086	[n 6]2021
59	Kuwait	Asia	159,687	2023	184,558	2022	136,642	2021
60	Ethiopia	Africa	155,804	2023	126,783	2022	99,269	2021
61	Morocco	Africa	147,343	2023	134,182	2022	142,867	[n 7]2021
62	Slovakia	Europe	133,044	2023	115,469	2022	116,527	2021
63	Cuba	Americas	—		633,442	2022	126,694	2021
64	Dominican Republic	Americas	120,629	2023	113,642	2022	94,243	2021
65	Ecuador	Americas	118,686	2023	115,049	2022	106,166	2021

Of course, it isn't just Berkshire that holds a lot of cash. Money market funds have continued to surge, hitting a record of $6.4 Trillion as of January.

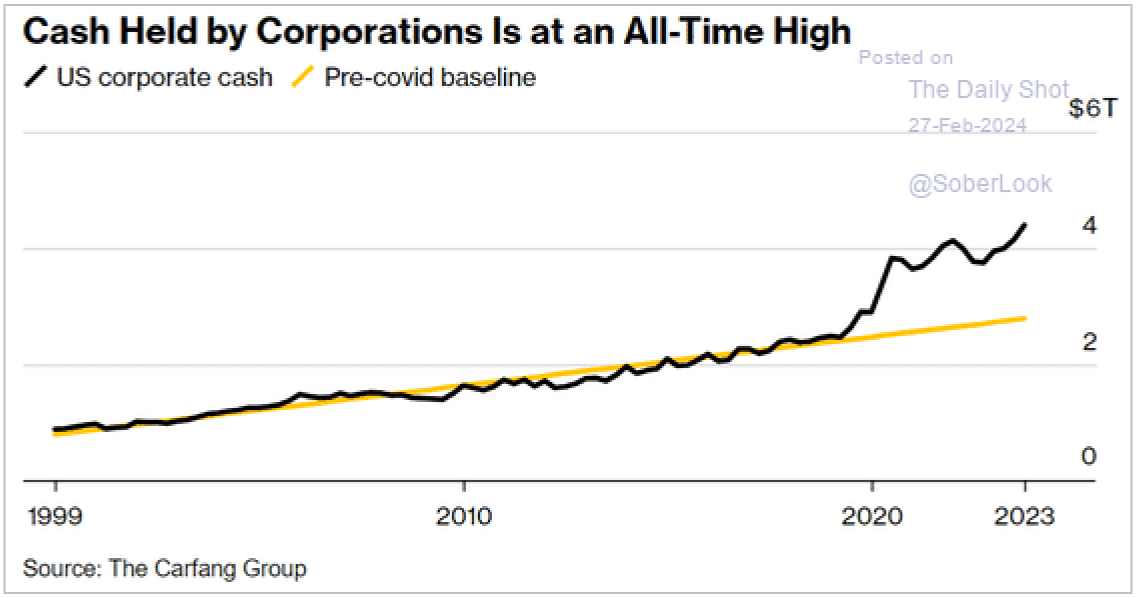


As discussed previously, most *money-market account balances belong to corporations* and other entities. To wit:

> *"You will notice the bulk of the money is in Government Money Market funds. These particular types of money market funds often have much higher account minimums (from $100,000 to $1 million), suggesting these funds are not retail investors. (Those would be the smaller balances of prime retail funds.)"*

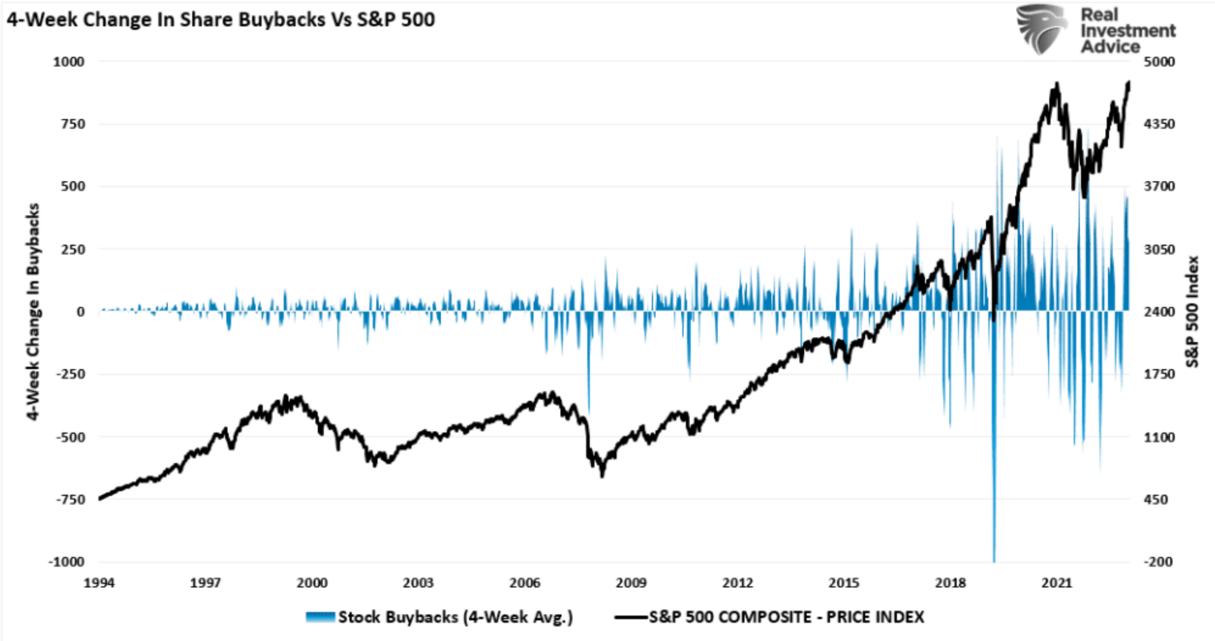


As shown below, more than $4 Trillion of that $6.4 Trillion belongs to corporations, primarily large-capitalization companies like Berkshire, Apple, Google, Microsoft, Meta, Amazon, and the rest.



While much of the media continues to hope those funds will flow into the financial markets, the reality is that these dollars are set aside for capital investments, operations, and, of course, buybacks.

> *"Since the Great Financial Crisis, one of the primary uses of corporate 'cash on the sidelines' has been for share repurchases to boost earnings. As noted previously, as much as [40% of the bull market since 2012] can be attributed to share buybacks alone."*



While Berkshire continues to execute buybacks, Buffett knows how those purchases should be made.

> *"Such repurchases increase your participation in every asset Berkshire owns. To this obvious but often overlooked truth, I add my usual caveat: All stock repurchases should be price-dependent. What is sensible at a discount to business value becomes stupid if done at a premium."*

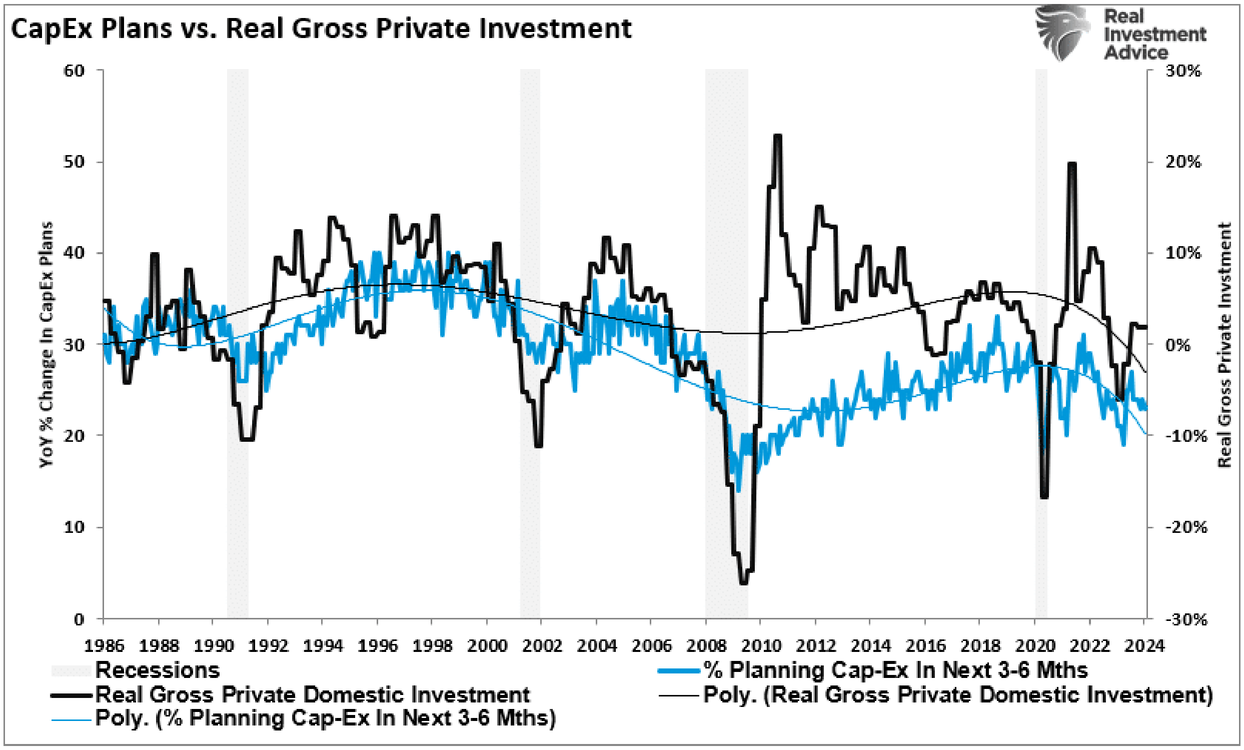
Unfortunately, following the financial crisis, most companies committed to buybacks at massive premiums to benefit insiders more than shareholders. *Such was our previous commentary on Buffett's views on buybacks.*

However, this brings us to Berkshire's real dilemma of cash.

Berkshire's Dilemma

In *"Small-Cap Stocks May Be At Risk,"* we discussed the importance of economic outlooks on a company's commitment to capital investments.

> *"Furthermore, if the economy and the underlying demand were as strong as recent headlines suggest, the business would be ramping up capital expenditures to meet that demand. However, such is not the case regarding capital expenditures and actual versus planned employment."*



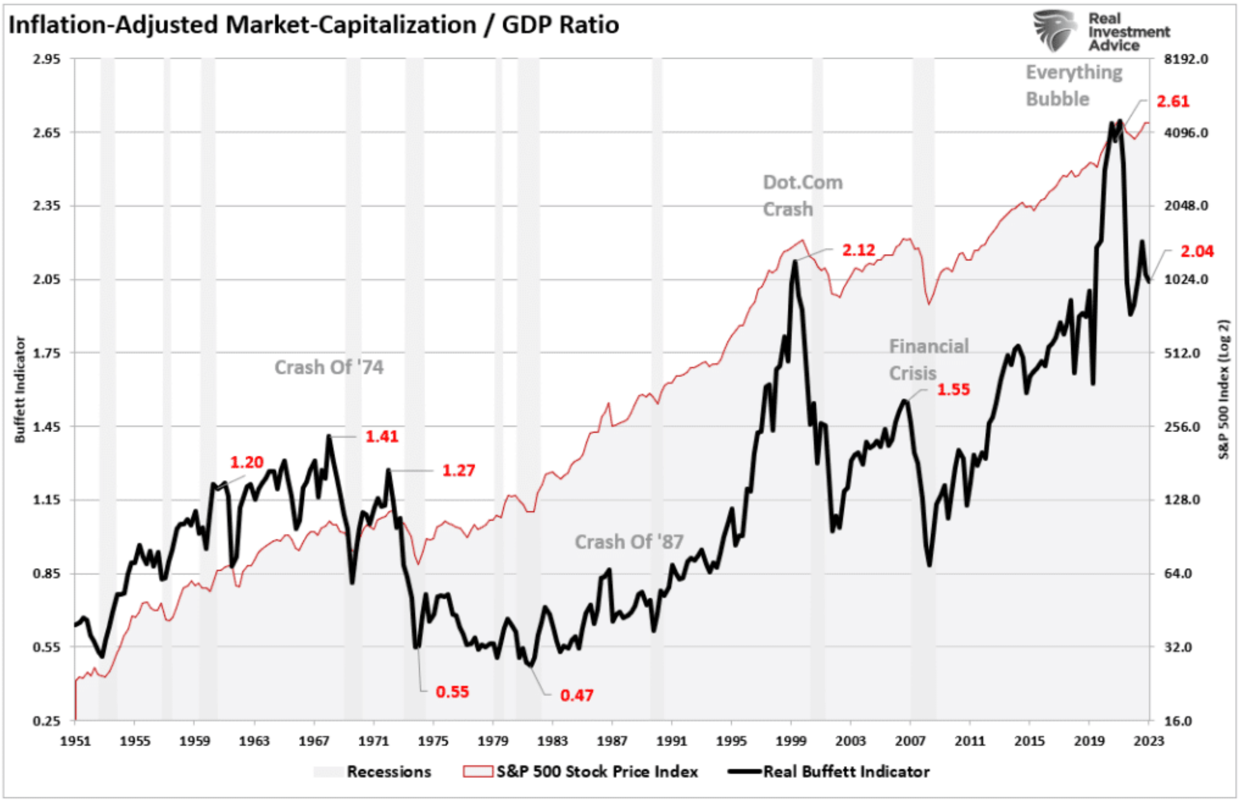
The problem with capital investments is that they take time to generate a profitable return that accretes to the business's bottom line. The same goes for acquisitions. More importantly, concerning acquisitions, they must both be accretive to the company and reasonably priced. Such is Berkshire's current dilemma.

> *"There remain only a handful of companies in this country capable of truly moving the needle at Berkshire, and they have been endlessly picked over by us and by others. Some we can value; some we can't. And, if we can, they have to be attractively priced."*

This was an essential statement. Here is one of the most intelligent investors in history, suggesting that he cannot deploy Berkshire's massive cash hoard in meaningful size due to an inability to find acquisition targets that are reasonably priced. With a $160 war chest, there are plenty of companies that Berkshire could either acquire outright, use a stock/cash offering, or acquire a controlling stake in. However, given the rampant increase in stock prices and valuations over the last decade, they are not reasonably priced.

Buffett's Favorite Measure

One of Warren Buffett's favorite valuation measures is the market capitalization to GDP ratio. I have modified it slightly to use inflation-adjusted numbers. The simplicity of this measure is that stocks should not trade above the value of the economy. This is because economic activity provides revenues and earnings to businesses.

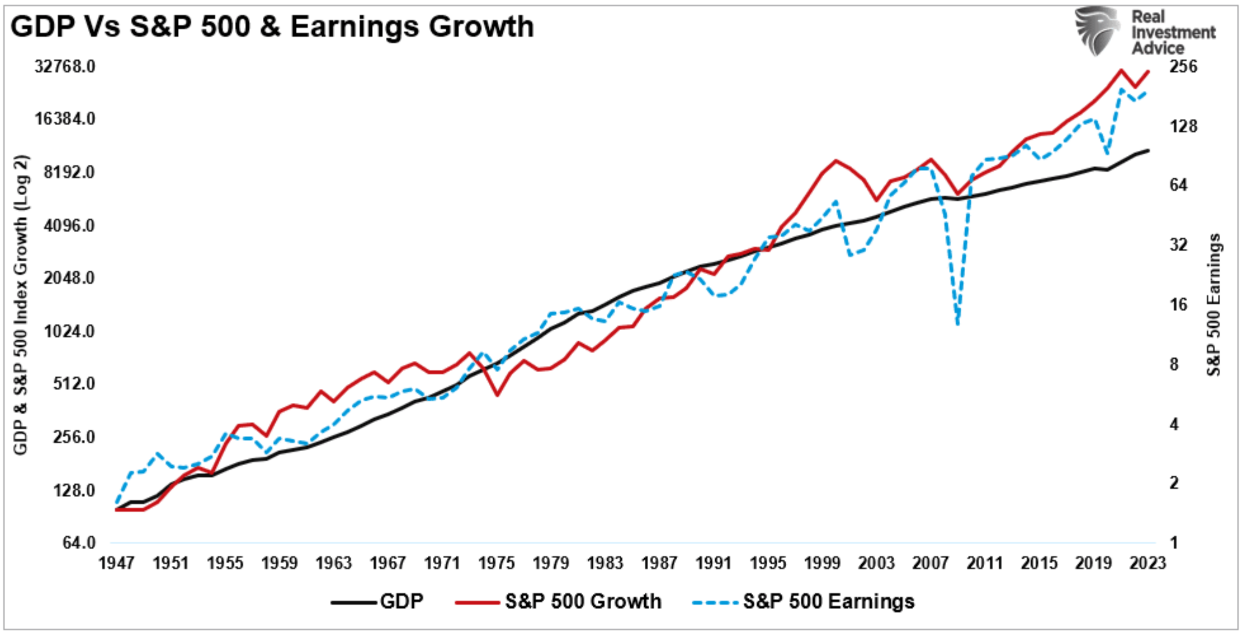


As discussed in *"Stock Markets Are Detached From Everything,"* the current environment is anything but opportunistic for a value investor like Warren Buffett. To wit:

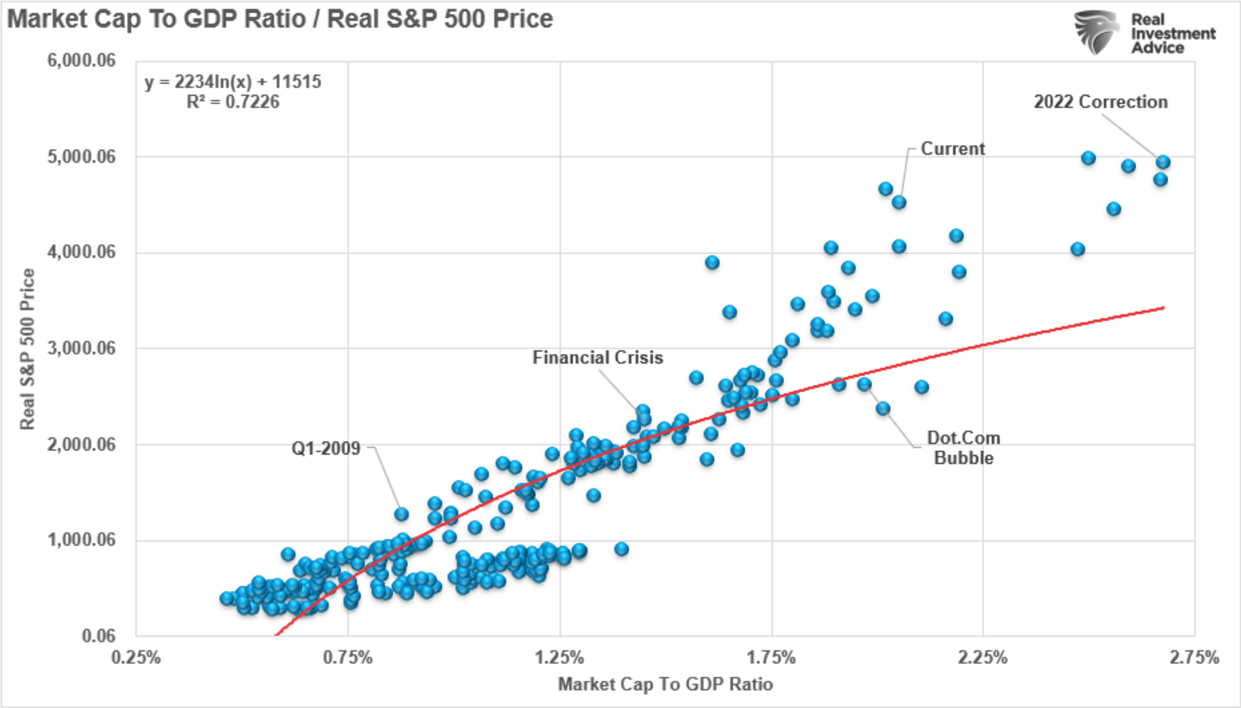
> *"While stock prices can deviate from immediate activity, reversions to actual economic growth eventually occur. Such is because corporate earnings are a function of consumptive spending, corporate investments, imports, and exports. The market disconnect from underlying economic activity is due to psychology. Such is particularly the case over the last decade, as successive rounds of monetary interventions led investors to believe 'this time is different.'"*

There is a correlation between economic activity and the rise and fall of equity prices. For example, in 2000 and again in 2008, corporate earnings contracted by 54% and 88%, respectively, as economic growth declined. Such was despite calls for never-ending earnings growth before both previous contractions.

As earnings disappointed, stock prices adjusted by nearly 50% to realign valuations with weaker-than-expected current earnings and slower future earnings growth. So, while stock markets are once again detached from reality, looking at past earnings contractions suggests such deviations are not sustainable.



With the current market capitalization to GDP ratio data point outside the historical range as economic growth slows, you can understand Berkshire's dilemma of deploying cash.

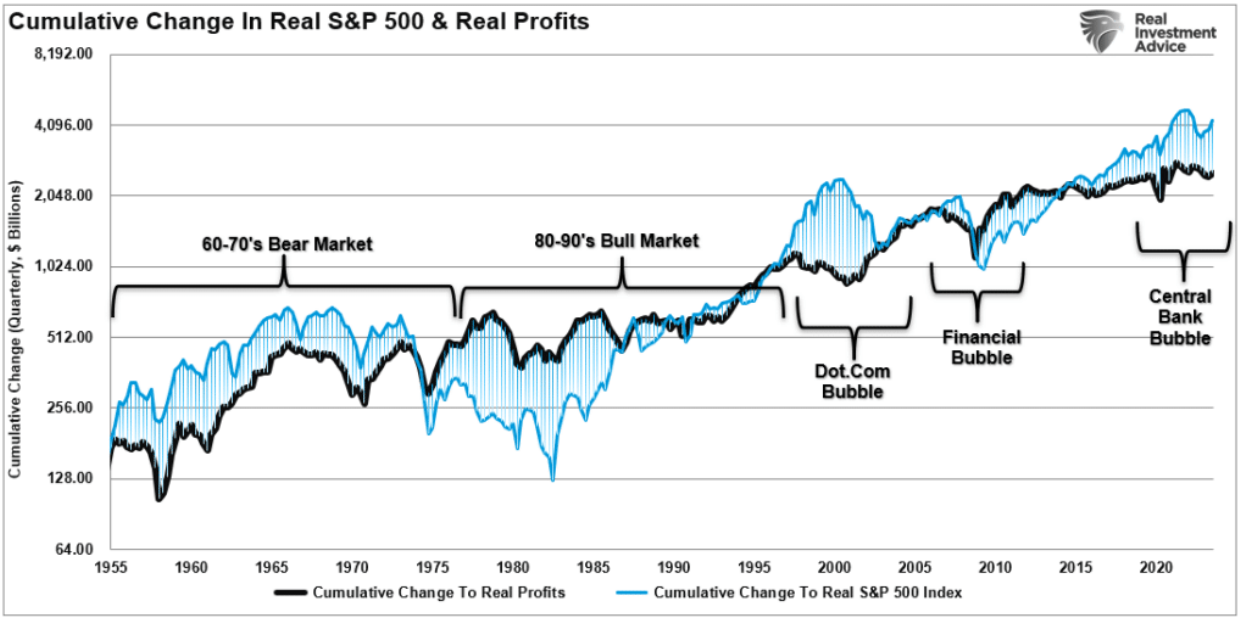


The risk of overpaying for assets comes down to sustaining current profitability.

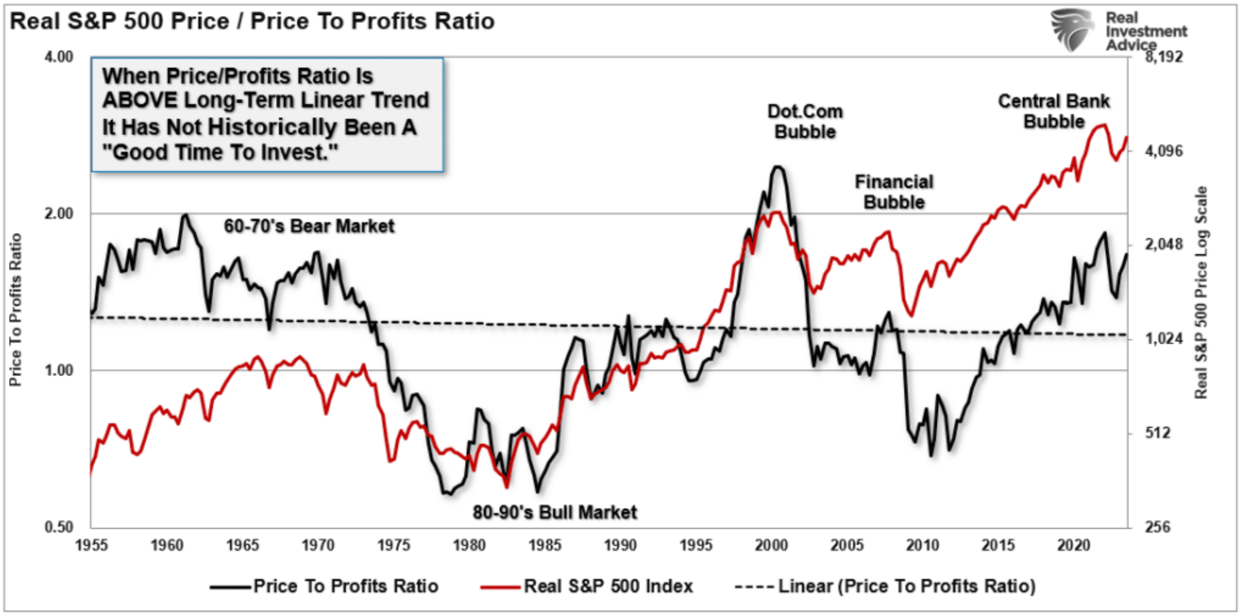
Price-To-Profits Sends A Warning

Berkshire's issue of finding *"reasonably priced"* acquisitions is not just one of being overly picky about opportunities. The reality is that after more than a decade of monetary infusions and zero interest rates, most companies are priced well beyond what economic dynamics can support. Besides Berkshire's measure of market capitalization relative to GDP, we can also look at corporate profits as they relate to economic growth. Again, this analysis is unsurprising, given that economic growth generates the revenue to provide corporate profits.

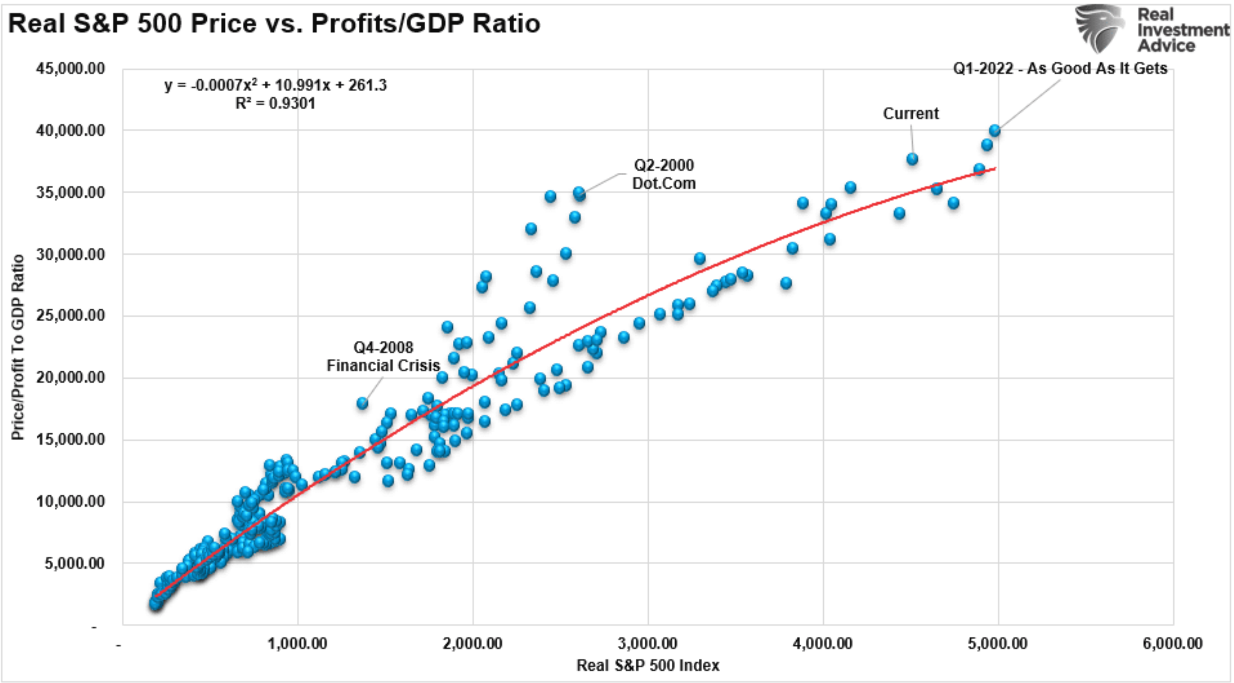
The chart below measures the cumulative change in the S&P 500 index compared to corporate profits. Again, when investors pay more than $1 for $1 worth of profits, those excesses are eventually reversed. The current deviation of the market from underlying profitability suggests that eventual reversion will be pretty unkind to investors.



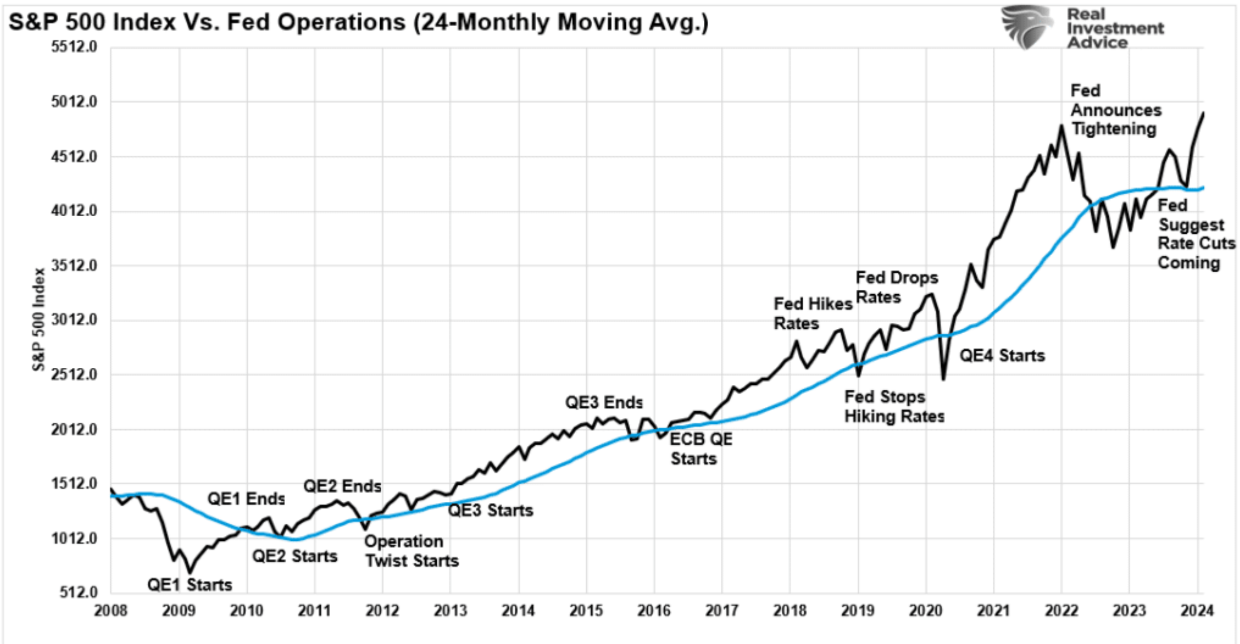
The correlation is more evident in the market versus the price-to-corporate profits ratio. Again, since corporate profits are ultimately a function of economic growth, the correlation is not unexpected. Hence, neither should the impending reversion in both series. Currently, that ratio is approaching levels that preceded more significant market reversions to realign the markets to profitability.



The high correlation, as noted, is unsurprising. Investors should expect an eventual reversal, with the market on the more extreme end of the valuation spectrum. However, those reversals can take much longer to occur than logic would assume.



To this point, it has seemed to be a simple formula: as long as the Fed remains active in supporting asset prices, the deviation between fundamentals and fantasy doesn't matter. It remains a hard point to argue.



However, the historical "mean reversion" process has yet to be completed, which has always followed bull markets. This should not surprise anyone, as asset prices eventually reflect the underlying reality of corporate profitability and economic growth.

Interestingly, this is a point Warren Buffett specifically noted in his letter.

> *"Occasionally, markets and/or the economy will cause stocks and bonds of some large and fundamentally good businesses to be strikingly mispriced. Indeed, markets can – and will – unpredictably seize up or even vanish as they did for four months in 1914 and for a few days in 2001. If you believe that American investors are now more stable than in the past, think back to September 2008. Speed of communication and the wonders of technology facilitate instant worldwide paralysis, and we have come a long way since smoke signals. Such instant panics won't happen often – but they will happen."*

It's just something to consider.

[Continue reading here](#).

Details on the cheapest stock Warren Buffett ever owned (from Dirtcheapstocks Substack)...

Warren Buffett had a net worth of $19,700 in December 1951. That's $230,000 in today's dollars. His net worth had doubled that year, thanks largely to an investment in this little company called GEICO. But in 1952, Buffett found a security he liked even better than GEICO.

Buffett was 21 years old at the start of 1952. He had just graduated from Columbia Business School and was working at a 5-person brokerage firm in Omaha. This brokerage firm received annual volumes of the Moody's manuals. These manuals were thousands of pages – packed with font out to the margins with statistics on ~10,000 businesses. Buffett said he read through each manual – twice!

The Moody's manuals served as Buffett's guide to his first $1 million. From 1952 to 1962, Buffett compounded his net worth at 48% per year. And the inspiration for most of these investments came from the Moody's manuals.

Western Insurance Overview

Sometime in early 1952, Buffett was flipping through the Moody's Bank and Finance manual when he stumbled upon Western Insurance Securities Co. Western Insurance was a holding company with two subsidiaries:

- Western Casualty & Surety
- Western Fire

Western Insurance Securities owned 92% of Western Casualty, which in turn owned all of Western Fire.

The combined entities wrote several lines of business, but automobile insurance made up more than 60% of the overall business. Premium data below is from 1953, but it's basically the same as 1952. My 1952 data is blurry, and this is easier to read.

Net Premium Volume:	Written in 1953	In Force Dec. 31,'53
Accident	$84,841	$33,049
Health	471,476	850,485
Hospitalization	124,688	96,083
Auto liability	6,802,353	6,698,935
Other liability	2,351,397	2,410,634
Workmen's comp.	2,885,660	1,500,619
Fidelity	130,458	206,891
Surety	666,310	804,101
Glass	295,144	562,692
Burglary & theft	303,552	422,422
Auto prop. dam.	4,329 957	4,257,886
Other prop dam. and coll.	608,755	418,888
Total	$19,054,592	$18,262,685

	Written in 1953	In Force Dec. 31,'52
Fire	$1,408,563	$3,149,817
Extend. coverage	599,821	1,414,262
Earthquake	561	2,099
Inland marine	191,852	287,110
Tornado, etc.	15,402	8,712
Sprinkler leakage	974	2,270
Riot, civ. com., etc.	26	237
Aircraft	6,041	5,273
Auto, phys. dam.	7,852,656	8,381,498
Glass	1,134	1,186
Burglary	2,217	3,070
Other	13,732	13,732
Total	$10,092,979	$13,269,266

INVESTMENT CHRONICLES

Revenue & Profitability

Buffett had the 1951 financial data when he began buying the stock. Here's a 10-year history of net earnings leading up to 1952. Western was booking profits every year for a decade.

Net Earnings by Year										
Year	1951	1950	1949	1948	1947	1946	1945	1944	1943	1942
Net earnings (Thousands)	940	1,300	1,212	1,130	339	319	419	344	145	142

Buffett pulled the revenue growth and market share data from the time the company was formed (1924) through the date he purchased shares. He found that premium volume and market share were progressing rapidly.

Market Share		
Year	Avergae Premium Volume	Market Share
1924-1930	838	0.05%
1931-1935	2,668	0.20%
1936-1940	3,955	0.25%
1941-1945	5,023	0.24%
1946-1950	13,959	0.33%
1951	22,055	0.38%
1952	26,006	0.41%

Young Buffett pulled at least five years' worth of combined ratios and compared those to industry standards.

Combined Ratio			
Year	**Industry Avg.**	**Western Fire**	**Western Casualty**
1948	91%	90%	75%
1949	88%	84%	92%
1950	93%	86%	91%
1951	97%	91%	101%
1952	94%	92%	97%
Average	93%	89%	91%

Western was consistently profitable. The business had a long history of growth, and management had proven its ability to underwrite well. Combined ratios at Western Fire and Western Casualty were below the industry averages. This is impressive, especially given the growth in business over time. Management was expanding the business in a safe, profitable manner.

Balance Sheet and Capital Structure

Western Insurance Securities Balance Sheet: 1951	
Assets:	
Invesments in Subsidiaries	7,262
Cash	34
Other Assets	105
Total	7,401
Liabilities:	
Federal Income Taxes	11
Dividends Payable	46
Accounts Payable	77
Total Liab	134
6% Preferred Stock	700
Class A Stock	1,400
Common Stock	628
Retained Earnings	4,539
Total Equity	7,267

Western Casualty & Surety: Balance Sheet 1951	
Assets:	
Stocks and Bonds	15,228
Cash	1,599
Collectibe Premium	2,490
Interest Receivable	83
Other	404
Gross Assets	19,804
Liabilities:	
Losses	6,163
Unearned Premiums	7,014
Payables. Taxes, Etc.	1,765
Total Liabilities	14,942
Equity:	
Capital Stock	1,200
Surplus	3,662
Total Equity	4,862

Western Fire: Balance Sheet 1951	
Assets:	
Stocks and Bonds	7,936
Cash	937
Agents' Balances	884
Other Assets	109
Total Assets	9,866
Liabilities:	
Losses	774
Unearned Premiums	5,112
Other	564
Total Liabilities	6,450
Capital Stock	1,000
Surplus	2,416
Total Equity	3,416

My numbers aren't perfect, but they're reasonably close. My data is a little blurry, so I make the best I can with what I have. It doesn't matter for our purposes -it's close enough.

Just to rehash, Western Insurance Securities (left) owned 92% of Western Casualty (middle), which owned 100% of Western Fire (right). Buffett bought common shares of Western Insurance Securities. There were three classes of stock inside Western Insurance.

1. ***6% Preferred Stock***: 7,000 shares outstanding; $100 par. Callable at $125/share. Entitled to a 6% dividend ahead of common and class A stock.
2. ***Class A Cumulative***: 35,000 shares outstanding, Callable at $60/share. Cumulative dividends of $2.50/share.
3. ***Common Stock***: 50,000 shares outstanding. This is what Buffett owned.

Valuation:

Common shares traded between $10 and $25 in 1952. It's unknown how much Buffett paid exactly, but let's be conservative and assume he paid $25/share. With 50,000 shares outstanding, Buffett was buying at a valuation of $1,250,000. ***That's 1.3× 1951 earnings***. Of course there were two classes of stock sitting ahead of Buffett, but the preferred shareholders were only entitled to $129,500 of cash flow per year (6% on $100 par for 7,000 shares of preferred = $42,000; $2.50/share on 35,000 shares for Class A = $87,500; total = $129,500). Western was generating enough earnings to cover the preferred/Class A dividends ~7x over. No matter how you slice it, Western Insurance was insanely cheap.

When considering price to book, Buffett looked at the preferred and class A shares in the most conservative way. Since these shares were callable, he valued them with the liquidation preference. In reality management would never call in these shares. Since the preferred and class A were getting such a small fraction of the earnings, and since earnings could be reinvested at high rates of return, paying off low cost capital would have a high opportunity cost. Buffett would've understood this, but just to be conservative, he valued the preferreds at callable price.

Buffett wrote about Western Insurance in "The Security I Like Best" in March 1953. By that time, the common stock was trading for $39/share. I reconstructed his narrative and backed into how he thought about book value.

Book Value Calculation: 1952	
6% Preferred Stock (Callable @ $125/share)	875
Class A Stock (Callable at $60/share)	2,100
Common Stock (Market Value $39/share)	1,950
Total Market Value of Equity	4,925
Book Value (Valuing Pref at Callable)	11,411
Price to Book	***43%***

Remember, this is price-to-book at $39/share. Buffett wasn't paying more than $25 for his shares. Based on 1952 book value, ***Buffett paid closer to 37% of book***.

Managing Its Investments

By 1951, Western had accumulated $23MM of investable assets. Buffett notes that the business followed an extremely conservative investment policy. Western relied on the growth in premiums to expand its investment empire – ***it wasn't taking big risks on the investment side to grow its business***. At year end 1951, ~$20MM of its investments were in government and municipal bonds. In 1952, Western earned $600K of investment income, which was plenty to pay preferred dividends of $130K. Buffett notes this in his memo. It seems to be the way he thought about the preferred shares. They have a small drag on the investment income, but that investment income is continuously growing, because premium volume continues to grow. It's safe to say Western wasn't overworking its investment capital to drive intrinsic value growth.

Why Was It Cheap?

Western Insurance was likely cheap for a few reasons. For starters the market cap for common shares was $1.25MM when Buffett built his stake. That's ~$14.5MM in today's dollars. ***Western was a tiny business***. Tiny businesses get overlooked. Western traded over the counter. I have never seen an annual report for Western Insurance from the early 1950's. I compiled my data by reading old Moody's manuals. I would guess the business was unknown to most of the investing community.

There were 311 shareholders of common stock in 1952. I'm not sure if shareholders were aggregated at brokerage houses in those days, but at most, the ***average shareholder owned ~$4,000 of stock***. There is no way Western Insurance was making headlines in the *Wall Street Journal*.

I think the preferred share structure may have also kept the common shares cheap. Investors may have viewed the preferreds as an additional complication in valuing the business. In the case of Western, the preferred shares significantly reduced earnings to common stock in the early days. It was only when the business grew premium volumes to an adequate level in the late 1940's that the profits became material to common shareholders.

Lessons Learned

Buffett said he felt like he was going crazy at times. He would find these insanely cheap stocks. He'd try to get his clients to buy the stocks and they'd look at him like he was crazy. He tells the story of Kansas City Life Insurance (still around on the OTC today) selling for less than 3x earnings. Buffett thought that he could surely convince the local Kansas City Life agent to buy the stock. The agent would've understood the returns implicit in buying a life insurance policy. Buffett goes to the agent's office, and says "here, why don't you buy some shares of this company you work for, that you rely on to feed your family? The implied yield is 35%, that's 10x better than the policies you sell to people!"

And the agent looked at Buffett as if he were speaking another language.

This phenomenon would continue. In the early 2000's, Buffett invested almost all of his personal money in a bunch of Korean stocks. He deployed $100MM on a Sunday afternoon just flipping through stocks and buying simple businesses at 2-3x earnings.

How It Played Out

After Buffett wrote about Western in March 1953, the stock ripped up to $65/share. Within his first ~18 months of ownership, Buffett was up 160% on the stock. We don't know when exactly he sold, but I think it's safe to say he made a fantastic return. Buffett sold his GEICO shares to buy Western shares. At yearend 1951, GEICO made up ~65% his net worth. Knowing this, I'd assume Western was a huge position – ***likely greater than 50% of his portfolio***. Western Insurance was acquired in 1984. Split adjusted common share value prior to acquisition was

$1,030/share. This is after Western had reduced its ownership stake in subsidiaries. Dividends on common shares in 1979 alone totaled $2.1MM, nearly double what Buffett bought his stake for.

These Opportunities Are Gone

I can hear you, reader. I can hear what you're saying right now. "***Dirt, those days are over. Stuff doesn't trade like that in the modern world.***"

This was the best investment Buffett had ever seen. It wasn't like he came across these sorts of ideas once a month. He found Western Insurance after looking through thousands of securities. So, there aren't going to be 100 ideas that trade at this kind of price.

But maybe I can show you one idea from recent history.

In 2016, a full-time engineer and part-time investor named Dan Schum wrote a blog post about a stock he owned called Sonics and Materials (Ticker: SIMA). SIMA made ultrasonic equipment and had been in business for 50 years. ***The business had $13.5MM of net cash, was earning ~$2MM per year, and had a book value of $22MM***.

What would you pay for that? Name a fair price. Now name a good price. Now name an egregiously good price. What did you come up with? $15MM? $13MM? $10MM?

Dan wrote about the stock when it had a market cap of $2.3MM.

Dan discovered the stock at $0.65/share. Management took the company private at $10/share five years after his writeup.

Here's a link to Dan's write up: SIMA - Dan Schum Write Up

There are fantastic opportunities available to hard workers with small wallets.

Legendary value investor Lou Simpson's eight keys to success (from Kyle Grieve via X)...

Legendary value investor Lou Simpson invested at a compound annual growth rate of 20.3%. He beat the S&P 500 Index in 18 out of 25 years. Here are 8 keys to his success:

1. Cut your weeds and water your flowers. Most people do the opposite resulting in below market-like returns.
2. Avoid leaking returns by paying excess fees like transaction costs and taxes. They seem small and insignificant, but they can add up quickly.
3. The characteristics he looked for in a business were: • High returns on capital • Consistently good returns • Run by leaders who want to create long-term value
4. Keep turnover low. Lou's turnover rates were in the 15-20 percent range. He wanted ideas he could hold onto for long periods and skipped short-term plays.
5. Sell your ideas that aren't working, and let your winner run. If you have businesses continuing to improve intrinsic value, hold them for as long as they are excelling.
6. Lou mitigated risk by asking three questions: 1. Has my business thesis stayed intact? 2. Is the price at an "overly high" evaluation? 3. Is management making short-term decisions?
7. Lou said his biggest mistake was selling outstanding companies too soon. Great businesses are hard to find. Once you own one, covet it while it remains great.
8. Do not rely on a team of people to make decisions. "If you have a lot of people involved, you tend to have the least competent person making the decision, because you need consensus."

The great paradox of the booming U.S. stock market (from Jeremy Grantham via GMO)...

1: The U.S. Market

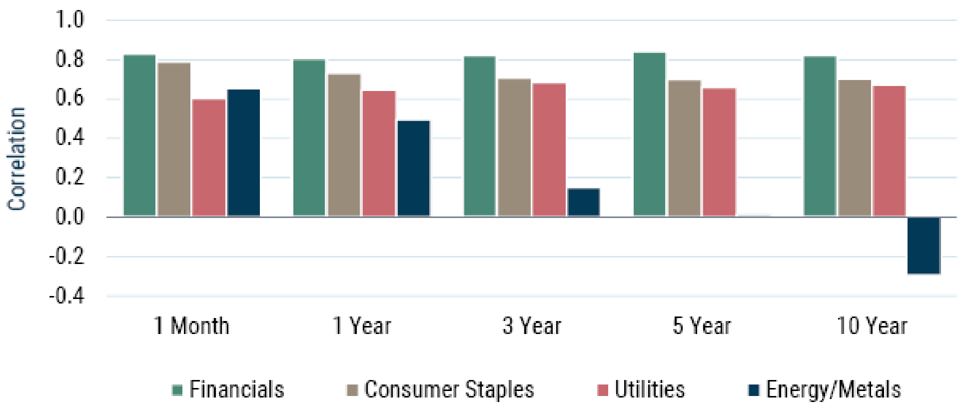
Well, the U.S. is really enjoying itself if you go by stock prices. A Shiller P/E of 34 (as of March 1st) is in the top 1% of history. Total profits (as a percent of almost anything) are at near-record levels as well. Remember, if margins and multiples are both at record levels at the same time, it really is double counting and double jeopardy – for waiting somewhere in the future is another July 1982 or March 2009 with simultaneous record low multiples and badly depressed margins.

But for those who must own U.S. stocks (most institutions) even when they are generally very overpriced, there is a reasonable choice of relatively attractive investments – relative, that is, to the broad U.S. market.

Quality: Although not spectacularly cheap today, U.S. quality stocks have a long history of slightly underperforming in bull markets and substantially outperforming in bear markets (although they did unusually well in the recent run-up). In addition, their long-term performance is remarkable. AAA bonds return about 1% a year less than low-grade bonds – everybody gets it, and always has. In bizarre contrast, the equivalent AAA stocks, with their lower bankruptcy risk, lower volatility, and just plain less risk, historically have delivered an extra 0.5% to 1.0% a year over the S&P 500 (to be precise, an extra 1.0% a year for the past 63 years, with the gains concentrated in the period since 2008). What on earth is that? Even holding their own should be inconceivable. It is the greatest aberration of all time in the market, and one I'm happy to say we at GMO realized 45 years ago, when Fama and French were still obsessing about returns to risky small cap and price to book. And while I'm bragging, I should say that GMO has added a decent long-term increment to that generic 1%, totaling 1.3% a year above the S&P 500 in our Quality Strategy for the last 10 years.

Resource equities: Not only are raw materials finite – believe it or not! – getting scarcer, and therefore certain to rise in price, but at longer horizons (10 years) resources are the only sector of the stock market to be negatively correlated with the broad stock market. They are far and away the most diversifying sector (see Exhibit 1). They are also particularly cheap today, having been whacked recently.

EXHIBIT 1: CORRELATIONS BETWEEN SECTORS AND THE REST OF THE TOP 1,000 U.S. COMPANIES: 1970-2023



As of 12/31/2023 | Source: MSCI, CRSP, GMO

Climate-related investments: With increasing climate damage and the increasing willingness of governments to take action, I believe climate investments will have top-line revenue growth that is guaranteed to be above average for the next many decades, although with no guarantees as to the smoothness of that growth. But, with all the cost of solar, wind, etc. being up front and little of the cost being operational, climate investments are exceptionally discount rate-sensitive, which has hammered them over the past two and a half years. And in its usual way, the market has overreacted to the trend of rising rates, making these investments real bargains today. Today, solar stocks are priced at over a 50% discount to the broad equity market, and some of the best clean energy companies in the world trade at levels that imply negative real growth.

Deep value: These stocks look cheap enough to be worth some investment, as the comparison with the total market is about as wide as it ever gets. The most expensive 20% of U.S. stocks are by definition always expensive, but today they are in the worst 10% of their 40-year range (compared to the top 1000 stocks). In great contrast, the cheapest 20% are in the best 7% of their range.

As for the U.S. market in general, there has never been a sustained rally starting from a 34 Shiller P/E. The only bull markets that continued up from levels like this were the last 18 months in Japan until 1989, and the U.S. tech bubble of 1998 and 1999, and we know how those ended. Separately, there has also never been a sustained rally starting from full employment.

The simple rule is you can't get blood out of a stone. If you double the price of an asset, you halve its future return. The long-run prospects for the broad U.S. stock market here look as poor as almost any other time in history. (Again, a very rare exception was 1998-2000, which was followed by a lost decade and a half for stocks. And on some data, 1929, which was famously followed by the Great Depression.)

BUBBLES AND AI

Looking backwards, what happened to our 2021 bubble? The Covid stimulus bubble appeared to be bursting conventionally enough in 2022 – in the first half of 2022 the S&P declined more than any first half since 1939 when Europe was entering World War II. Previously in 2021, the market displayed all the classic signs of a bubble peaking: extreme investor euphoria; a rush to IPO and SPAC; and highly volatile speculative leaders beginning to fall in early 2021, even as blue chips continued to rise enough to carry the whole market to a handsome gain that year – a feature hitherto unique to the late-stage major bubbles of 1929, 1972, 2000, and now 2021. But this historically familiar pattern was rudely interrupted in December 2022 by the launch of ChatGPT and consequent public awareness of a new transformative technology – AI, which seems likely to be every bit as powerful and world-changing as the internet, and quite possibly much more so.

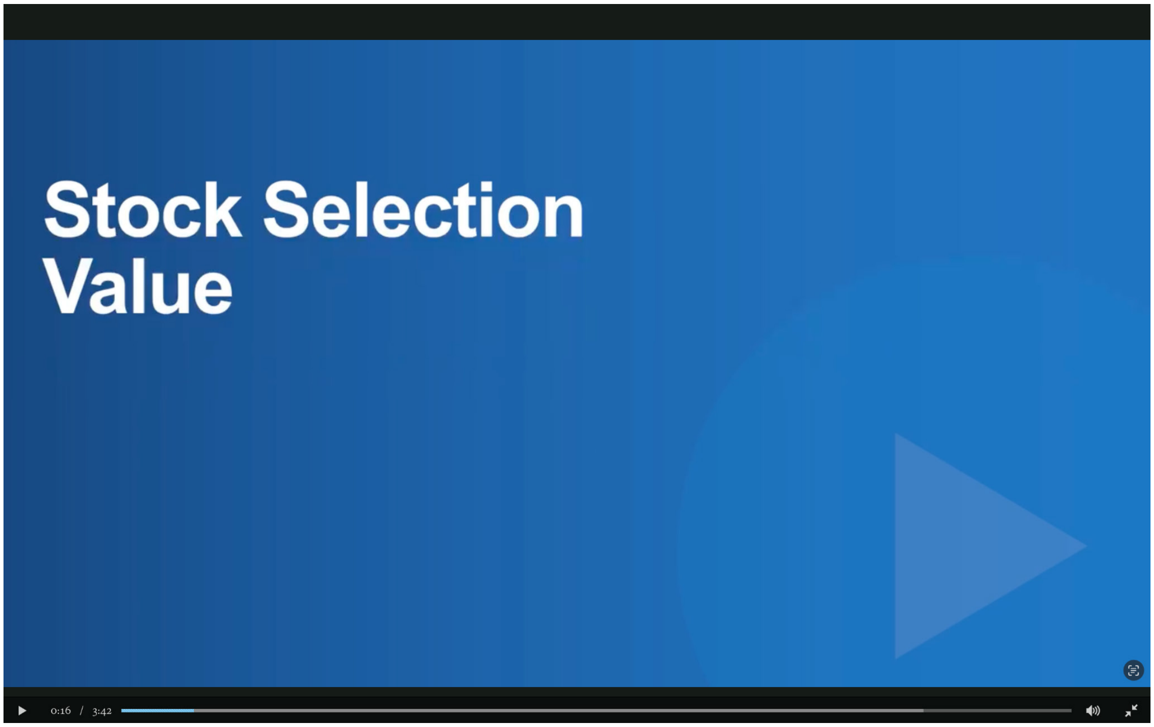
But every technological revolution like this – going back from the internet to telephones, railroads, or canals – has been accompanied by early massive hype and a stock market bubble as investors focus on the ultimate possibilities of the technology, pricing most of the very long-term potential immediately into current market prices. And many such revolutions are in the end often as transformative as those early investors could see and sometimes even more so – but only after a substantial period of disappointment during which the initial bubble bursts. Thus, as the most remarkable example of the tech bubble, Amazon led the speculative market, rising 21 times from the beginning of 1998 to its 1999 peak, only to decline by an almost inconceivable 92% from 2000 to 2002, before inheriting half the retail world!

So it is likely to be with the current AI bubble. But a new bubble within a bubble like this, even one limited to a handful of stocks, is totally unprecedented, so looking at history books may have its limits. But even though, I admit, there is no clear historical analogy to this strange new beast, the best guess is still that this second investment bubble – in AI – will at least temporarily deflate and probably facilitate a more normal ending to the original bubble, which we paused in December 2022 to admire the AI stocks. It also seems likely that the after-effects of interest rate rises and the ridiculous speculation of 2020-2021 and now (November 2023 through today) will eventually end in a recession

Continue reading here.

INVESTMENT IDEAS

Global investment manager AQR's top three investment ideas to consider for 2024 (from AQR)...


Stock Selection
Value
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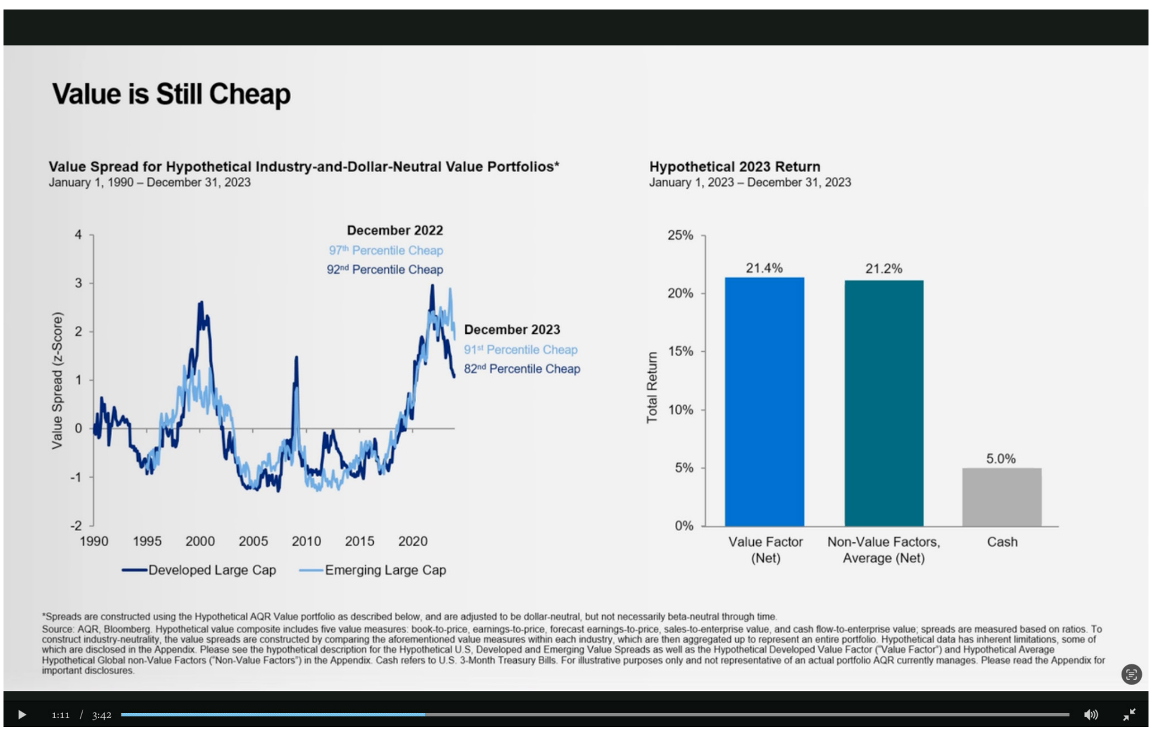
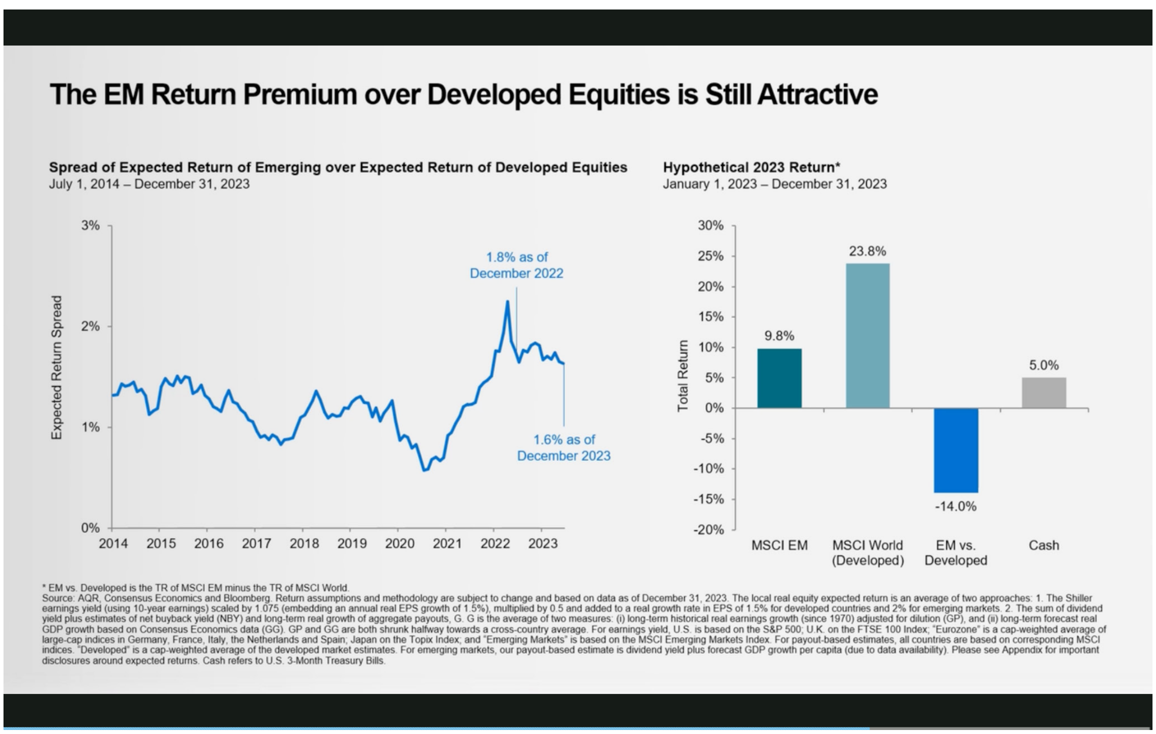
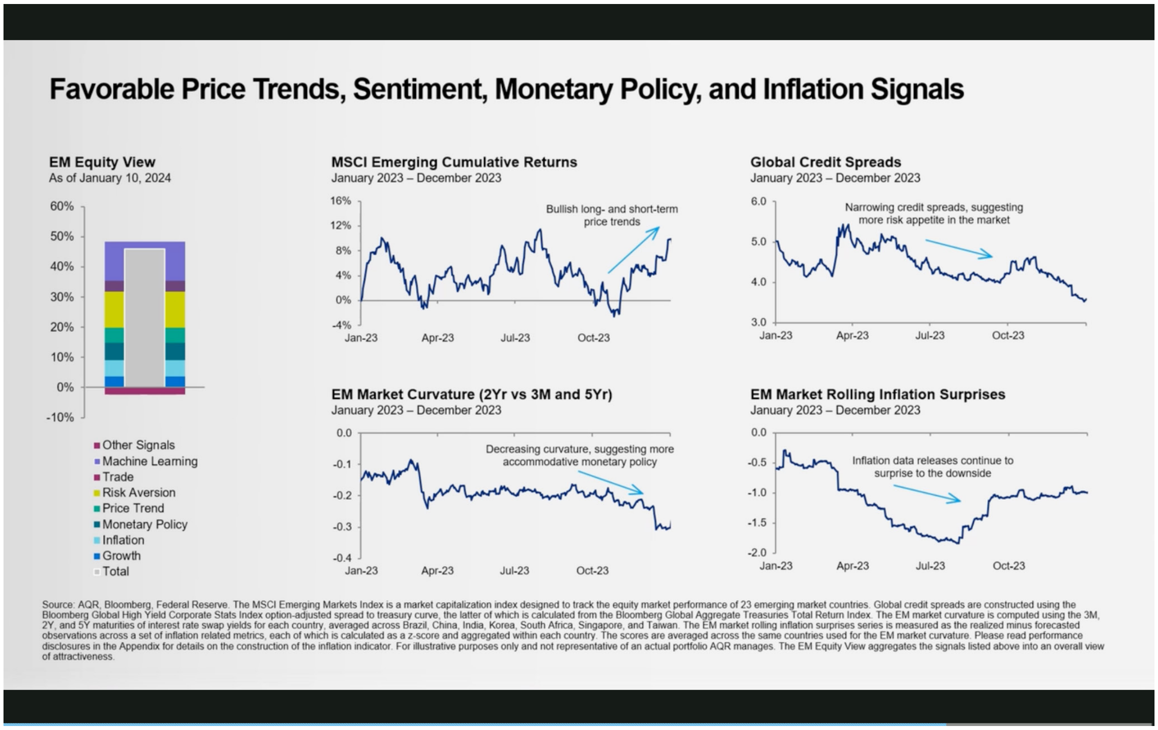

Value is Still Cheap
Value Spread for Hypothetical Industry-and-Dollar-Neutral Value Portfolios*
January 1, 1990 – December 31, 2023
December 2022
97th Percentile Cheap
92nd Percentile Cheap
December 2023
91st Percentile Cheap
82nd Percentile Cheap
Value Spread (z-Score)
4
3
2
1
0
-1
-2
1990
1995
2000
2005
2010
2015
2020
Developed Large Cap
Emerging Large Cap
Hypothetical 2023 Return
January 1, 2023 – December 31, 2023
Total Return
25%
20%
15%
10%
5%
0%
21.4%
21.2%
5.0%
Value Factor (Net)
Non-Value Factors, Average (Net)
Cash
*Spreads are constructed using the Hypothetical AQR Value portfolio as described below, and are adjusted to be dollar-neutral, but not necessarily beta-neutral through time.
Source: AQR, Bloomberg. Hypothetical value composite includes five value measures: book-to-price, earnings-to-price, forecast earnings-to-price, sales-to-enterprise value, and cash flow-to-enterprise value; spreads are measured based on ratios. To construct industry-neutrality, the value spreads are constructed by comparing the aforementioned value measures within each industry, which are then aggregated up to represent an entire portfolio. Hypothetical data has inherent limitations, some of which are disclosed in the Appendix. Please see the hypothetical description for the Hypothetical U.S, Developed and Emerging Value Spreads as well as the Hypothetical Developed Value Factor ("Value Factor") and Hypothetical Average Hypothetical Global non-Value Factors ("Non-Value Factors") in the Appendix. Cash refers to U.S. 3-Month Treasury Bills. For illustrative purposes only and not representative of an actual portfolio AQR currently manages. Please read the Appendix for important disclosures.
1:11 / 3:42

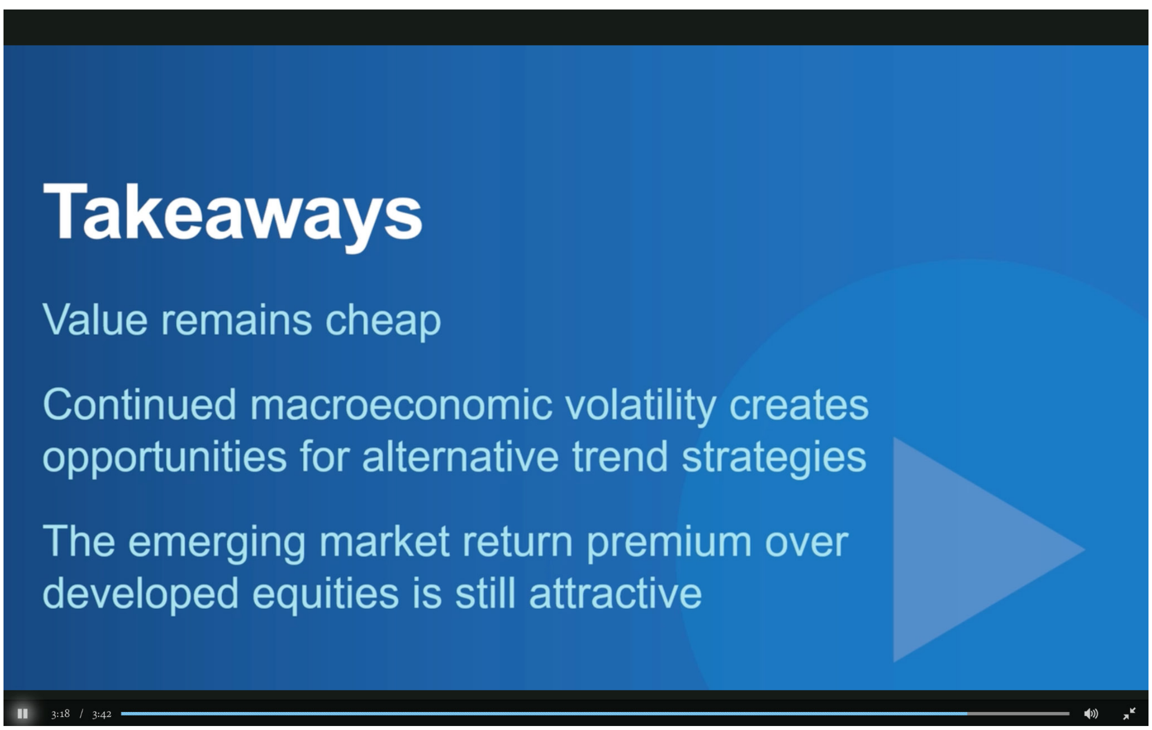

Trend Following in
Alternative Markets
1:20 / 3:42


Macroeconomic Volatility is Still Elevated
Elevated Macro Uncertainty
Larger Price Moves
More Trends
Monetary policy lags: The impact of tight policy has yet to be realized
Central bank tradeoffs: Central banks are hiking into an inflation shock for first time in decades
Disagreement: Material dispersion between market-implied and policymaker/economist forecasts, as well as across markets
Geopolitical risk: Two "hot" wars in Europe and the Middle East along with China-Taiwan tensions
Historical experience: Macroeconomic volatility tends to be persistent – economic shocks take time to wear off
Hypothetical 2023 Return
January 1, 2023 – December 31, 2023
Total Return
16%
14%
12%
10%
8%
6%
4%
2%
0%
14.3%
5.0%
Alternative Trend Following Strategy
Cash
Source: AQR, Bloomberg. Cash refers to U.S. 3-Month Treasury Bills. Hypothetical data has inherent limitations, some of which are disclosed in the Appendix. Please see the Hypothetical Alternative Trend Following Strategy description in the Appendix. For illustrative purposes only and not representative of an actual portfolio AQR currently manages. Please read the Appendix for important disclosures. Diversification does not eliminate the risk of experiencing investment losses.
2:10 / 3:42


Emerging Market
Equities
2:14 / 3:42


The EM Return Premium over Developed Equities is Still Attractive
Spread of Expected Return of Emerging over Expected Return of Developed Equities
July 1, 2014 – December 31, 2023
Expected Return Spread
3%
2%
1%
0%
2014
2015
2016
2017
2018
2019
2020
2021
2022
2023
1.8% as of December 2022
1.6% as of December 2023
Hypothetical 2023 Return*
January 1, 2023 – December 31, 2023
Total Return
30%
25%
20%
15%
10%
5%
0%
-5%
-10%
-15%
-20%
9.8%
23.8%
-14.0%
5.0%
MSCI EM
MSCI World (Developed)
EM vs. Developed
Cash
* EM vs. Developed is the TR of MSCI EM minus the TR of MSCI World.
Source: AQR, Consensus Economics and Bloomberg. Return assumptions and methodology are subject to change and based on data as of December 31, 2023. The local real equity expected return is an average of two approaches: 1. The Shiller earnings yield (using 10-year earnings) scaled by 1.075 (embedding an annual real EPS growth of 1.5%), multiplied by 0.5 and added to a real growth rate in EPS of 1.5% for developed countries and 2% for emerging markets. 2. The sum of dividend yield plus estimates of net buyback yield (NBY) and long-term real growth of aggregate payouts, G. G is the average of two measures: (i) long-term historical real earnings growth (since 1970) adjusted for dilution (GP), and (ii) long-term forecast real GDP growth based on Consensus Economics data (GG). GP and GG are both shrunk halfway towards a cross-country average. For earnings yield, U.S. is based on the S&P 500; U.K. on the FTSE 100 Index; "Eurozone" is a cap-weighted average of large-cap indices in Germany, France, Italy, the Netherlands and Spain; Japan on the Topix Index; and "Emerging Markets" is based on the MSCI Emerging Markets Index. For payout-based estimates, all countries are based on corresponding MSCI indices. "Developed" is a cap-weighted average of the developed market estimates. For emerging markets, our payout-based estimate is dividend yield plus forecast GDP growth per capita (due to data availability). Please see Appendix for important disclosures around expected returns. Cash refers to U.S. 3-Month Treasury Bills.


Favorable Price Trends, Sentiment, Monetary Policy, and Inflation Signals
EM Equity View
As of January 10, 2024
Other Signals
Machine Learning
Trade
Risk Aversion
Price Trend
Monetary Policy
Inflation
Growth
Total
MSCI Emerging Cumulative Returns
January 2023 – December 2023
Bullish long- and short-term price trends
Global Credit Spreads
January 2023 – December 2023
Narrowing credit spreads, suggesting more risk appetite in the market
EM Market Curvature (2Yr vs 3M and 5Yr)
January 2023 – December 2023
Decreasing curvature, suggesting more accommodative monetary policy
EM Market Rolling Inflation Surprises
January 2023 – December 2023
Inflation data releases continue to surprise to the downside
Source: AQR, Bloomberg, Federal Reserve. The MSCI Emerging Markets Index is a market capitalization index designed to track the equity market performance of 23 emerging market countries. Global credit spreads are constructed using the Bloomberg Global High Yield Corporate Stats Index option-adjusted spread to treasury curve, the latter of which is calculated from the Bloomberg Global Aggregate Treasuries Total Return Index. The EM market curvature is computed using the 3M, 2Y, and 5Y maturities of interest rate swap yields for each country, averaged across Brazil, China, India, Korea, South Africa, Singapore, and Taiwan. The EM market rolling inflation surprises series is measured as the realized minus forecasted observations across a set of inflation related metrics, each of which is calculated as a z-score and aggregated within each country. The scores are averaged across the same countries used for the EM market curvature. Please read performance disclosures in the Appendix for details on the construction of the inflation indicator. For illustrative purposes only and not representative of an actual portfolio AQR manages. The EM Equity View aggregates the signals listed above into an overall view of attractiveness.


Takeaways
Value remains cheap
Continued macroeconomic volatility creates opportunities for alternative trend strategies
The emerging market return premium over developed equities is still attractive
3:18 / 3:42

Dollar General (DG): A value buy or a value trap? (from The Rational Walk)...

Introduction

I often engage in “rubbernecking” when I come upon the scene of a debacle causing a company’s stock price to plummet. Last week, Dollar General’s precipitous decline following its earnings release caught my attention. After falling 12.2% on Thursday, August 31, the stock declined an additional 5.9% on Friday, September 1. The stock, which closed at $130.27 on Friday, has been cut roughly in half since October 2022. The company’s market capitalization is $28.6 billion.

Dollar General is not a company that I have followed in the past. However, a quick look at the annual report led me to believe that I am capable of understanding the business. I noted that the company posted earnings per share in excess of $10 in each of the past three years and has an attractive long-term growth story. My interest increased when I looked at dataroma.com to see who owns the stock. I’m against blind coat tailing, but when investors I highly respect not only own the stock but were *adding* to their positions recently at much higher prices, I can’t help but take notice!

Ownership | Activity | Buys | Sells | Insider

Portfolio Manager	% of portfolio	Recent activity	Shares	Value
Christopher Bloomstran - Semper Augustus	5.86	Add 76.92%	146,025	24,792,000
AKO Capital	1.16	Reduce 55.99%	450,666	76,514,000
Thomas Gayner - Markel Asset Management	1.03	Add 82.36%	509,250	86,460,000
Seth Klarman - Baupost Group	0.74	Buy	242,000	41,087,000

Source: Dataroma.com

After spending an hour on the situation, it was obvious why the market punished the stock. The business has performed very poorly this year and management has cut its guidance for the rest of the year. If you’re trying to beat the S&P 500 this year, who wants to be in a company that’s likely to post ugly results three months from now? However, what if the company can get back on track? Management continues to open new stores and, if past profitability and unit economics can be restored, perhaps this is a company that could earn $15 per share in five years and again trade at twenty times earnings. That scenario could produce an annual compound return of ~18%.

I caution the reader that I am not making predictions that this rosy scenario will happen and my background with the business is literally just three days old. This article is **not** a comprehensive business profile comparable to the series I wrote last year which was discontinued in January. Each of those profiles was the product of several weeks of work. However, I thought that the information I have gathered so far on Dollar General might be useful for readers who are not yet familiar with the company and interested in a starting point for their own research.

Overview

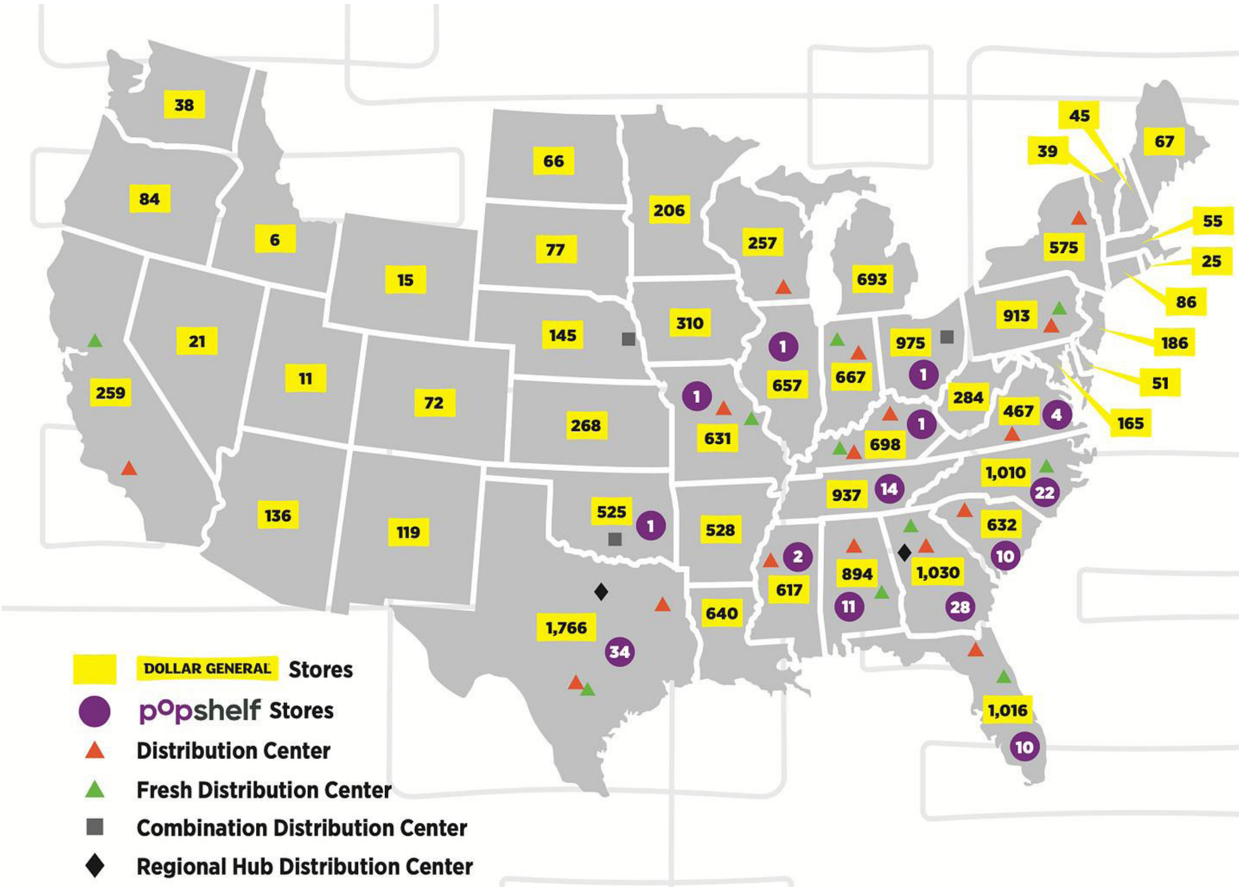
The retail landscape in the United States is intensely competitive. Consumers are aware of the importance of seeking the best value for their money in all economic environments but this need becomes acute during economic downturns and times of high inflation. There are no one-size-fits-all retail strategies in a vast country of 330 million consumers with a diverse mix of urban, suburban, and rural communities that have unique needs and face very different economic pressures.

I spent a couple of years living in a rural community more than twenty years ago. At that time, the only local retail option was a convenience store next to a small restaurant and gas station. Those of us who commuted to the nearest city had access to all of the typical retail options on a daily basis, but people who worked locally would not necessarily want to drive long distances more than once a week. The local "mom and pop" store served their needs for purchases during the week.

Dollar General specializes in serving the needs of small towns and rural communities with over 80% of its 19,488 stores located near towns of 20,000 or fewer people. The company operates more stores than any other retailer in the United States and has locations within five miles of 75% of the U.S. population. Dollar General stores are typically bare-bones small-box formats which average 7,500 square feet. A typical grocery store has about four to five times as much space while the average size of a Wal-Mart Supercenter is a whopping 178,000 square feet.

With its extensive store footprint, Dollar General benefits from economies of scale that allow for vertical integration. The company operates nineteen distribution centers for non-refrigerated products, ten cold storage distribution centers, and two distribution centers for both refrigerated products and general merchandise. The company more than doubled the size of its private tractor fleet in 2022 and anticipates having more than 2,000 tractors by the end of 2023. The distribution centers and transportation fleet provide significant control of the supply chain.

The following exhibit from Dollar General's 2022 annual report shows the locations of the 19,104 stores in 47 states that it operated as of February 3, 2023 along with the location of its distribution centers. In addition to the Dollar General brand, the company operated 190 pOpshelf locations selling non-consumable products.



Source: Dollar General's 2022 annual report

The store base is geographically concentrated in the south, southeastern, and midwestern United States and management has been adding locations rapidly over the past decade. The exhibit below shows the growth in store count since 2014:

	8/4/23	7/29/22	2/3/23	1/28/22	1/29/21	1/31/20	2/1/19	2/2/18	2/3/17	1/29/16	1/30/15	1/31/14
Number of Stores												
Stores at beginning of period	**19,104**	**18,130**	**18,130**	**17,177**	**16,278**	**15,370**	**14,534**	**13,320**	**12,483**	**11,789**	**11,132**	**10,506**
Stores opened	384	436	1,039	1,050	1,000	975	900	1,315	900	730	700	650
Stores closed			65	97	101	67	64	101	63	36	43	24
Net store increase	384	436	974	953	899	908	836	1,214	837	694	657	626
Stores at end of period	**19,488**	**18,566**	**19,104**	**18,130**	**17,177**	**16,278**	**15,370**	**14,534**	**13,320**	**12,483**	**11,789**	**11,132**
Increase in total store count	*5.0%*		*5.4%*	*5.5%*	*5.5%*	*5.9%*	*5.8%*	*9.1%*	*6.7%*	*5.9%*	*5.9%*	

Source: Dollar General 10-K and 10-Q reports

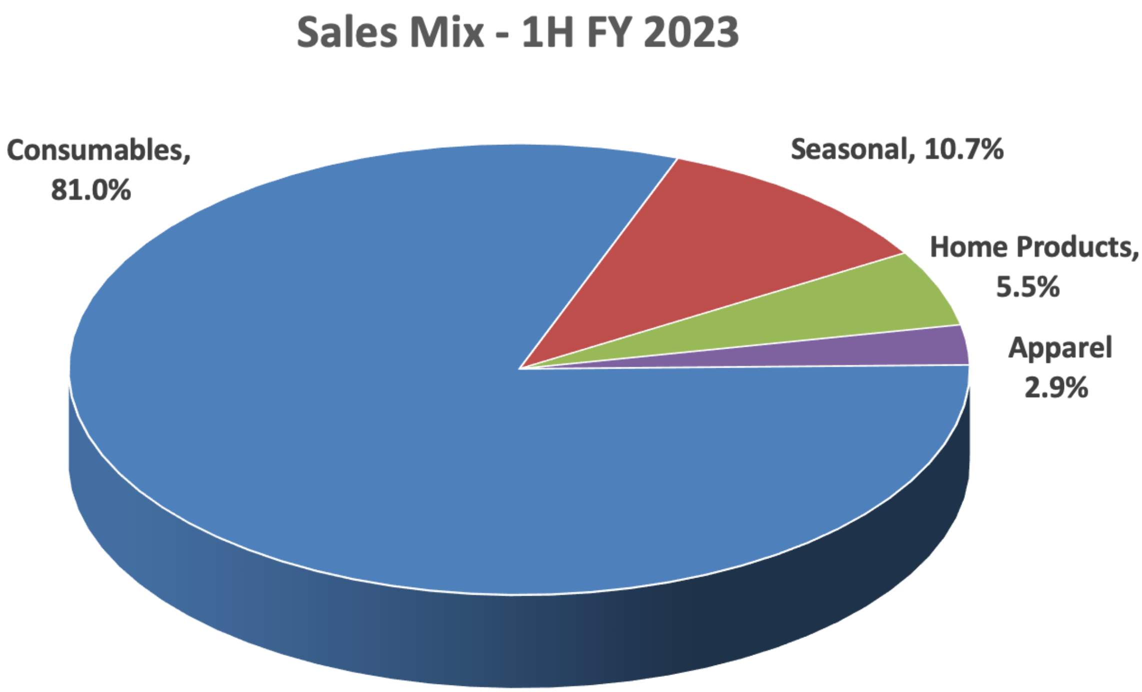
Even during a challenging year, store growth has not stopped and it appears that there is room for many more store openings in the years to come. To understand why Dollar General has an opportunity to make headway in more rural locations, I recommend a Wall Street Journal article published in 2017 that describes the customer base.

Of course, the devil is in the details, so let's take a closer look at some key metrics over the past decade with a focus on how the company has hit turbulence this year and whether management is likely to get back on track.

Sales Mix

Before delving into Dollar General's key metrics in more detail, it is important to understand the sales mix. Stores sell a mix of consumable and non-consumable products. Consumable products include shelf-stable foods as well as a growing emphasis on refrigerated and frozen foods. In addition to selling branded consumer products, Dollar General also has a private label brand named Clover Valley that sells goods similar to branded products at a lower price point.

Non-consumable products include seasonal assortments along with home products and apparel. Dollar General's business is somewhat seasonal with higher sales in the fourth quarter due to the Christmas season. Generally, non-consumable products carry a higher gross margin than consumables, although margins on a product line basis are not provided by management.



Source: Dollar General's Q2 2023 10-Q

Consumables accounted for just over 75% of sales a decade ago. The mix has been shifting toward consumables for several years and breached the 80% level during the first half. As consumables account for a larger percentage of sales, gross margins will be under more pressure. The company has attempted to shift the mix toward non-consumables, both in Dollar General branded stores as well as the new pOpshelf concept, but so far the unfavorable mix situation has persisted.

As we can see from the exhibit below, apparel has been particularly weak, with seasonal and home product sales stagnating even as store count has increased. As the company's core consumer has faced increasing pressure due to high inflation, it is natural to expect spending to gravitate toward basic necessities of daily life.

Figures in thousands	1H 2023		Fiscal Years									
			2022 *(53 weeks)*	2021 *(52 weeks)*	2020 *(52 weeks)*	2019 *(52 weeks)*	2018 *(52 weeks)*	2017 *(52 weeks)*	2016 *(53 weeks)*	2015 *(52 weeks)*	2014 *(52 weeks)*	2013 *(52 weeks)*
	8/4/23	7/29/22	2/3/23	1/28/22	1/29/21	1/31/20	2/1/19	2/2/18	2/3/17	1/29/16	1/30/15	1/31/14
Net Sales:												
Consumables	15,504,504	14,436,340	30,155,218	26,258,605	25,906,685	21,635,890	19,865,086	18,054,785	16,798,881	15,457,611	14,321,080	13,161,825
Seasonal	2,038,842	2,048,282	4,182,815	4,182,165	4,083,650	3,258,874	3,050,282	2,837,310	2,674,319	2,522,701	2,344,993	2,259,516
Home Products	1,047,834	1,099,588	2,332,411	2,322,367	2,209,950	1,611,899	1,506,054	1,400,618	1,373,397	1,289,423	1,205,373	1,115,648
Apparel	547,833	592,855	1,174,419	1,457,312	1,546,554	1,247,310	1,203,621	1,178,254	1,140,001	1,098,827	1,038,142	967,178
Total Net Sales	**19,139,013**	**18,177,065**	**37,844,863**	**34,220,449**	**33,746,839**	**27,753,973**	**25,625,043**	**23,470,967**	**21,986,598**	**20,368,562**	**18,909,588**	**17,504,167**

Source: Dollar General's 10-K and 10-Q reports

The effect of the pandemic stimulus programs is also clear when examining recent results. The company posted unusually strong sales across the board in 2020, but as the stimulus effect has waned and inflation has wreaked havoc among those with little disposable income, discretionary spending has stalled even as sales of consumable necessities have continued to grow.

Operating History: 2013 to 1H 2023

When I learn about a business, I find it useful to look at a minimum of ten years of data so I can spot long term trends. The exhibit below shows the operating results of the past decade along with the first half of fiscal 2023 (click to expand image):

Figures in thousands	1H 2023		Fiscal Years									
			2022 *(53 weeks)*	2021 *(52 weeks)*	2020 *(52 weeks)*	2019 *(52 weeks)*	2018 *(52 weeks)*	2017 *(52 weeks)*	2016 *(53 weeks)*	2015 *(52 weeks)*	2014 *(52 weeks)*	2013 *(52 weeks)*
	8/4/23	7/29/22	2/3/23	1/28/22	1/29/21	1/31/20	2/1/19	2/2/18	2/3/17	1/29/16	1/30/15	1/31/14
Net Sales:												
Consumables	15,504,504	14,436,340	30,155,218	26,258,605	25,906,685	21,635,890	19,865,086	18,054,785	16,798,881	15,457,611	14,321,080	13,161,825
Seasonal	2,038,842	2,048,282	4,182,815	4,182,165	4,083,650	3,258,874	3,050,282	2,837,310	2,674,319	2,522,701	2,344,993	2,259,516
Home Products	1,047,834	1,099,588	2,332,411	2,322,367	2,209,950	1,611,899	1,506,054	1,400,618	1,373,397	1,289,423	1,205,373	1,115,648
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Total Net Sales	**19,139,013**	**18,177,065**	**37,844,863**	**34,220,449**	**33,746,839**	**27,753,973**	**25,625,043**	**23,470,967**	**21,986,598**	**20,368,562**	**18,909,588**	**17,504,167**
Cost of goods sold	13,138,853	12,390,479	26,024,765	23,407,443	23,027,977	19,264,912	17,821,173	16,249,608	15,203,960	14,062,471	13,107,081	12,068,425
Gross Profit	**6,000,160**	**5,786,586**	**11,820,098**	**10,813,006**	**10,718,862**	**8,489,061**	**7,803,870**	**7,221,359**	**6,782,638**	**6,306,091**	**5,802,507**	**5,435,742**
Selling, general and administrative expenses	4,566,988	4,127,003	8,491,796	7,592,331	7,164,097	6,186,757	5,687,564	5,213,541	4,719,189	4,365,797	4,033,414	3,699,557
Operating profit	**1,433,172**	**1,659,583**	**3,328,302**	**3,220,675**	**3,554,765**	**2,302,304**	**2,116,306**	**2,007,818**	**2,063,449**	**1,940,294**	**1,769,093**	**1,736,185**
Interest expense	167,375	82,774	211,273	157,526	150,385	100,574	99,871	97,036	97,821	86,944	88,232	88,984
Other (income) expense	-	-	415	-	-	-	1,019	3,502	-	326	-	18,871
Income before income taxes	1,265,797	1,576,809	3,116,614	3,063,149	3,404,380	2,201,730	2,015,416	1,907,280	1,965,628	1,853,024	1,680,861	1,628,330
Income tax expense	282,582	346,122	700,625	663,917	749,330	489,175	425,944	368,320	714,495	687,944	615,516	603,214
Net Income	**983,215**	**1,230,687**	**2,415,989**	**2,399,232**	**2,655,050**	**1,712,555**	**1,589,472**	**1,538,960**	**1,251,133**	**1,165,080**	**1,065,345**	**1,025,116**
Weighted average diluted shares outstanding	220,029	228,533	226,297	235,812	250,076	258,053	266,105	273,362	282,261	295,211	305,681	323,854
Diluted earnings per share	4.47	5.39	10.68	10.17	10.62	6.64	5.97	5.63	4.43	3.95	3.49	3.17
Dividends per share	1.18	1.10	2.20	1.68	1.44	1.28	1.16	1.04	1.00	0.88	-	-
Effective tax rate	22%	22%	22%	22%	22%	22%	21%	19%	36%	37%	37%	37%
Gross Margin	31.4%	31.8%	31.2%	31.6%	31.8%	30.6%	30.5%	30.8%	30.8%	31.0%	30.7%	31.1%
Operating Margin	7.5%	9.1%	8.8%	9.4%	10.5%	8.3%	8.3%	8.6%	9.4%	9.5%	9.4%	9.9%
Net Margin	5.1%	6.8%	6.4%	7.0%	7.9%	6.2%	6.2%	6.6%	5.7%	5.7%	5.6%	5.9%

Source: Dollar General 10-Q and 10-K reports

Despite the unfavorable changes to product mix, gross margin has held up better than I would have expected. As a point of reference, I looked at my Costco research last year and noted that Wal-Mart ran at a gross margin of 24.4% in fiscal 2022 and Target ran at a gross margin of 28.3%. Obviously, Costco's gross margin of 10-11% is in an entirely different league serving a totally different member-based demographic.

The fact is that the economics of big box stores is very different from Dollar General's small box format. Rural consumers could access lower priced merchandise by shopping at Wal-Mart, but if the closest Wal-Mart is 40 miles away and gasoline costs almost $4 per gallon, such trips will be infrequent. Dollar General clearly provides a good value proposition for rural consumers compared to other convenient options.

The main source of Dollar General's recent problems is apparent when we look at the operating margin. At 7.5% during the first half of 2023, this metric is, by far, the worst showing over the past decade. SG&A as a percentage of sales came in at 23.9% during the first half compared to 22.4% in 2022 and 22.2% in 2021. Looking back further, SG&A as a percentage of sales was 21.1% in 2013.

During the company's earnings call, management provided several reasons for poor performance this year. In particular, inventory shrinkage has become a major problem. Management expects "$100 million of additional shrink headwind." In addition, management refers to an "acceleration of investment in retail labor" of ~$150 million, which I take to refer to higher labor costs due to wage inflation.

Inventory turnover has been under pressure recently. Turnover was 3.7 times at the end of the second quarter on a trailing four-quarter basis. Turnover was 4.0 times in fiscal 2022 and ranged from 4.4 to 4.9 between fiscal 2013 and 2021.

Store Unit Economics

Dollar General's rapid expansion in recent years makes it important to look at store unit economics which have been very attractive historically. Prior to 2021, the company boasted of a multi-decade record of growth in same-store sales. Here are some key metrics that I calculated on a per-store basis along with the company's reported same-store sales and sales per square foot statistics:

Figures in thousands	1H 2023		Fiscal Years									
	8/4/23	7/29/22	2022 (53 weeks) 2/3/23	2021 (52 weeks) 1/28/22	2020 (52 weeks) 1/29/21	2019 (52 weeks) 1/31/20	2018 (52 weeks) 2/1/19	2017 (52 weeks) 2/2/18	2016 (53 weeks) 2/3/17	2015 (52 weeks) 1/29/16	2014 (52 weeks) 1/30/15	2013 (52 weeks) 1/31/14
Average stores open during period	**19,296**	**18,348**	**18,617**	**17,654**	**16,728**	**15,824**	**14,952**	**13,927**	**12,902**	**12,136**	**11,461**	**10,819**
Sales per store (thousands)	992	991	2,033	1,938	2,017	1,754	1,714	1,685	1,704	1,678	1,650	1,618
Ending inventories per store (thousands)	390	378	363	318	314	296	274	259	253	253	243	236
Operating profit per store (thousands)	74	90	179	182	213	145	142	144	160	160	154	160
Average sales per square foot (TTM for 1H 2023)	**272**	**263**	**273**	**262**	**273**	**237**	**231**	**227**	**229**	**226**	**223**	**220**
Same-store sales growth	**-0.1%**	**4.6%**	**4.3%**	**-2.8%**	**16.3%**	**3.9%**	**3.2%**	**2.7%**	**0.9%**	**2.8%**	**2.8%**	**3.3%**

Source: Dollar General's 10-K and 10-Q reports

It is typical in retail for new stores to post weaker results than established stores during the first few years, so it is impressive that Dollar General was able to post the record shown in the exhibit while nearly doubling the store count. As stores mature, their financial profile begins to resemble the company-wide average.

When we look at same-store sales growth, 2020 obviously appears as an aberration due to the pandemic. Dollar General's customer demographic benefited from stimulus payments as well as other programs that have since phased out or ended. The 16.3% increase in same store sales in 2020 was bound to reverse to some degree, which resulted in the 2.8% decline in 2021 that broke a multi-decade record of same-store sales growth. Growth resumed in 2022 before showing a small decline in the first half of 2023. However, it is important to realize that these figures are in nominal dollars. The 4.3% growth of same-store sales in 2022 is nothing to write home about since this represents a *decline* in real terms given the elevated level of inflation.

Dollar General typically leases locations for its stores. In addition to the capital required to build out the store, the company must invest in inventory. I have not found reliable data on the capital expenditures required to open a Dollar General store, but we can determine the inventory per store. We can also see the operating profits, although new locations will lag the company-wide average for the first few years. Still, the figures seem encouraging regarding the unit economics of new store openings.

Balance Sheet

When we look at the balance sheet data over the past decade, it quickly becomes apparent that leverage has increased dramatically since the end of fiscal 2021. Debt has increased from $4.2 billion at the end of fiscal 2021 to $7.3 billion at the end of the first half of fiscal 2023. Debt as a percentage of total capital increased from 40% to 56% while the Debt to EBIT ratio increased from 1.36x to 2.88x.

This exhibit shows the balance sheet data over the past decade (click to enlarge):

		Fiscal Year									
	1H 2023	2022	2021	2020	2019	2018	2017	2016	2015	2014	2013
Figures in thousands	8/4/23	2/3/23	1/28/22	1/29/21	1/31/20	2/1/19	2/2/18	2/3/17	1/29/16	1/30/15	1/31/14
ASSETS											
Current Assets:											
Cash and cash equivalents	353,018	381,576	344,829	1,376,577	240,320	235,487	267,441	187,915	157,947	579,823	505,566
Merchandise inventories	7,531,459	6,760,733	5,614,325	5,247,477	4,676,848	4,097,004	3,609,025	3,258,785	3,074,153	2,782,521	2,552,993
Income taxes receivable	151,730	135,775	97,394	90,760	76,537	57,804	108,265	11,050	6,843	-	-
Prepaid expenses and other current assets	377,772	302,925	247,295	199,405	184,163	272,725	263,121	220,021	193,467	170,265	147,048
Total current assets	8,413,979	7,581,009	6,303,843	6,914,219	5,177,868	4,663,020	4,247,852	3,677,771	3,432,410	3,532,609	3,205,607
Net property and equipment	5,624,129	5,236,309	4,346,127	3,899,997	3,278,359	2,970,806	2,701,282	2,434,456	2,264,062	2,116,075	2,080,305
Operating lease assets	10,755,172	10,670,014	10,092,930	9,473,330	8,796,183	-	-	-	-	-	-
Goodwill	4,338,589	4,338,589	4,338,589	4,338,589	4,338,589	4,338,589	4,338,589	4,338,589	4,338,589	4,338,589	4,338,589
Other intangible assets, net	1,199,700	1,199,700	1,199,750	1,199,870	1,200,006	1,200,217	1,200,428	1,200,659	1,200,994	1,201,870	1,207,645
Other assets, net	63,988	57,746	46,132	36,619	34,079	31,406	28,760	20,823	21,830	19,499	35,378
TOTAL ASSETS	**30,395,557**	**29,083,367**	**26,327,371**	**25,862,624**	**22,825,084**	**13,204,038**	**12,516,911**	**11,672,298**	**11,257,885**	**11,208,642**	**10,867,524**
LIABILITIES AND SHAREHOLDERS' EQUITY											
Current Liabilities:											
Current portion of long term obligations	-	-	-	-	-	1,950	401,345	500,950	1,379	101,158	75,966
Current portion of operating lease liabilities	1,331,433	1,288,939	1,183,559	1,074,079	964,805	-	-	-	-	-	-
Accounts payable	3,681,634	3,552,991	3,738,604	3,614,089	2,860,682	2,385,469	2,009,771	1,557,596	1,494,225	1,388,154	1,286,484
Accrued expenses and other	1,013,594	1,036,919	1,049,139	1,006,552	709,156	618,405	549,658	500,866	467,122	413,760	368,578
Income taxes payable	7,261	8,919	8,055	16,063	8,362	10,033	4,104	63,393	32,870	59,400	59,148
Total current liabilities	6,033,922	5,887,768	5,979,357	5,710,783	4,543,005	3,015,857	2,964,878	2,622,805	1,995,596	1,962,472	1,790,176
Long-term obligations	7,295,215	7,009,399	4,172,068	4,130,975	2,911,993	2,862,740	2,604,613	2,710,576	2,969,175	2,623,965	2,742,788
Long-term operating lease liabilities	9,409,193	9,362,761	8,890,709	8,385,388	7,819,683	-	-	-	-	-	-
Deferred income taxes	1,119,114	1,060,906	825,254	710,549	675,227	609,687	515,702	652,841	639,955	626,858	635,821
Other liabilities	240,408	220,761	197,997	263,691	172,676	298,361	305,944	279,782	275,283	285,309	296,546
Commitments and contingencies											
Shareholders' equity:											
Preferred stock	-	-	-	-	-	-	-	-	-	-	-
Common stock	192,039	191,718	201,265	210,687	220,444	227,072	235,141	240,811	250,855	265,514	277,424
Additional paid-in capital	3,724,200	3,693,871	3,587,914	3,446,612	3,322,531	3,252,421	3,196,462	3,154,606	3,107,283	3,048,806	3,009,226
Retained earnings	2,380,451	1,656,140	2,473,999	3,006,102	3,162,660	2,941,107	2,698,352	2,015,867	2,025,545	2,403,045	2,125,453
Accumulated other comprehensive loss	1,015	43	(1,192)	(2,163)	(3,135)	(3,207)	(4,181)	(4,990)	(5,807)	(7,327)	(9,910)
Total shareholders' equity	6,297,705	5,541,772	6,261,986	6,661,238	6,702,500	6,417,393	6,125,774	5,406,294	5,377,876	5,710,038	5,402,193
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	**30,395,557**	**29,083,367**	**26,327,371**	**25,862,624**	**22,825,084**	**13,204,038**	**12,516,911**	**11,672,298**	**11,257,885**	**11,208,642**	**10,867,524**
	-	-	-	-	-	-	-	-	-	-	-
Common shares outstanding	219,470	219,105	230,016	240,785	251,936	259,511	268,733	275,212	286,694	303,447	317,058
Change in common shares outstanding	0.2%	-4.7%	-4.5%	-4.4%	-2.9%	-3.4%	-2.4%	-4.0%	-5.5%	-4.3%	

Source: Dollar General's 10-K and 10-Q reports

Although management has halted repurchases, a subject that I will discuss in the next section, the share count has been reduced by over 30% since the end of fiscal 2013.

Capital Allocation

Dollar General has historically generated significant cash flow. I prefer to look at cash flow and capital allocation over a long period of time and I gathered data for the past ten fiscal years plus the first half of fiscal 2023.

Over this period, Dollar General generated $21.2 billion of operating cash flow and spent $8.3 billion on capital expenditures. If you subtract capex from operating cash flow, you end up with $12.9 billion of "free cash flow" although with the store count nearly doubling, it is obvious that a significant amount of capex is expansionary in nature. Additionally, much of the inventory buildup over the past decade, which depressed operating cash flow by $5.9 billion, was needed to support new stores.

Dollar General has been an enthusiastic buyer of the company's stock, as noted in the previous section. Over the past ten and a half years, management allocated $14.3 billion toward repurchases. A dividend was introduced in 2015 which returned $3 billion to shareholders. The return of capital over this period was in excess of free cash flow with the difference made up by an increase of $4.3 billion of debt.

The entire cash flow statement is too large to display here so I have condensed the data into the following exhibit that shows selected sources and uses of cash over the period. We can see that the sum of free cash flow and net issuance of debt is a nearly perfect match against cash returned to shareholders.

Figures in thousands	1H 2023 8/4/23	Fiscal Years 2022 2/3/23	2021 1/28/22	2020 1/29/21	2019 1/31/20	2018 2/1/19	2017 2/2/18	2016 2/3/17	2015 1/29/16	2014 1/30/15	2013 1/31/14	CUMULATIVE FY 2013 to 1H FY 2023
Free cash flow	(37,980)	429,209	1,800,254	2,851,249	1,455,513	1,411,947	1,157,080	1,054,105	888,303	943,045	963,087	**12,915,812**
FCF as % of Net Income	*NMF*	*18%*	*75%*	*107%*	*85%*	*89%*	*75%*	*84%*	*76%*	*89%*	*94%*	*73%*
Selected sources and uses of cash												
Free cash flow	(37,980)	429,209	1,800,254	2,851,249	1,455,513	1,411,947	1,157,080	1,054,105	888,303	943,045	963,087	12,915,812
Net change in debt	271,569	2,815,398	45,630	1,050,901	55,160	(145,510)	(222,944)	236,362	240,828	(78,467)	17,073	4,286,000
Repurchases	-	(2,748,014)	(2,549,669)	(2,466,434)	(1,200,376)	(1,007,494)	(579,712)	(990,474)	(1,299,613)	(800,095)	(620,052)	(14,261,933)
Dividends	(258,885)	(493,726)	(392,188)	(355,926)	(327,568)	(306,523)	(282,931)	(281,135)	(258,328)	-	-	(2,957,210)
Total selected sources and uses of cassh	**(25,296)**	**2,867**	**(1,095,973)**	**1,079,790**	**(17,271)**	**(47,580)**	**71,493**	**18,858**	**(428,810)**	**64,483**	**360,108**	**(17,331)**

Source: Dollar General's 10-K and 10-Q reports

Readers will also note that repurchases halted entirely in the first half of fiscal 2023. According to management's comments during the earnings call, there are no plans to resume repurchases despite the precipitous decline in the stock price.

Management stated that the need to maintain an investment grade credit rating precludes the possibility of repurchases in the near term, yet the dividend remains intact. The impulse of management to treat a dividend as sacrosanct while halting repurchases in times of trouble is disturbingly familiar.

Drilling down to the past few years, we can see that management became aggressive and took on considerable debt to fund repurchases of stock at much higher prices. Over the past three and a half years, free cash flow was $5 billion but management chose to return $9.3 billion to shareholders with the vast majority returned via repurchases. Simple math makes it unsurprising that debt increased by over $4 billion.

Hindsight is 20/20, but I can understand if shareholders are annoyed by management taking on debt to fund repurchases at much higher prices only to halt the repurchase program when shares are depressed. Of course, this type of behavior is not unique to Dollar General. Taking on leverage to fund repurchases at high valuations is common.

Conclusion

I can claim no special expertise or insight into Dollar General at this point given that I have spent less than thirty hours on the company over just a few days. However, I am intrigued by the strong history of store growth and the attractive unit economics even as I shake my head in frustration at management's capital allocation record.

Will management succeed in restoring operating margins to prior levels or will the dismal 7.5% operating margin of the first half of 2023 become the new normal? It seems highly unlikely that management will totally fail to restore operating margins. In the long run, the economic fundamentals that produced a strong record over a decade have not suddenly evaporated. Inventory and wage pressures are likely to eventually abate although it is hard to predict the timing of a turnaround.

Store growth continues even in the current difficult environment and it seems clear that there is more room to grow. The vast geography of the United States and the company's current geographic footprint makes it clear that there are still growth opportunities to displace less competitive small retailers in locations where there is insufficient population density to support big box Wal-Mart Supercenters.

I am not sure what to think of the pOpshelf initiative or the company's nascent entry into Mexico that began this year. Given that I am unimpressed with management's capital allocation, I would prefer to see a laser focus on margins and growing the Dollar General format rather than taking on the potential distractions of an international expansion. However, I cannot rule out Mexico as a growth opportunity.

While Dollar General's cash generation record makes the current debt load manageable, I would prefer to see management deleverage to ratios that prevailed prior to 2022. I would also halt the dividend and redirect those funds toward repurchases if the stock remains depressed in the coming months. Management is guiding for earnings per share of $7.10 to $8.30 for the current fiscal year and it is likely that third quarter results will be ugly.

Continue reading here (subscription may be required).

A short thesis on online real-estate marketplace firm Zillow (Z) (from Spruce Point Management)...

After conducting a forensic review of Zillow, an operator of real estate-related websites and mobile applications, Spruce Point believes Zillow's core business has matured and new growth initiatives will come with significant near-term and long-term headwinds which will likely ultimately curtail its diversification and growth efforts. Based on our investigation, we estimate a 40% to 60% downside risk, or $23.00 -$35.00 per share.

The report highlights several key concerns with the Company, including:

- Zillow's core business model is under pressure from declining web traffic and growing industry litigation and regulatory risks that are poised to disrupt the real estate commission structure
- Evidence of additional business pressures against Zillow from Homes.com – now owned by the CoStar group – which represents an underappreciated threat to Zillow's market position
- We believe Zillow uses various aggressive accounting and financial policies that can enable premature revenue recognition and margin enhancement
- Questions regarding Zillow's governance, including Board entrenchment, the lack of a formal clawback policy, and compensation schemes devoid of firm financial targets

Continue reading here.

A Mexican blue-chip bargain (from Exploring With Alluvial Capital)...

Recently, and for the first time in a while, I took a dive into Mexican stocks. The Mexican stock market is much like those of many other emerging markets economies. Trading is concentrated in a short list of leading conglomerates, banks, infrastructure companies, telecoms, and other "investable" stocks. Beneath, there are several dozen other companies that get reasonable attention from locals but rarely attract the notice of foreign investors. Bringing up the rear are another few dozen small, thinly-traded stocks of interest only to the truly deranged. My focus is, of course, on these neglected companies.

I am long-term bullish on Mexico. The country's problems with lawlessness, corruption, and the illicit drug trade are well-documented. Less well-known is the fact that despite these issues, Mexico's per capita GDP is up 53% this century. Millions of Mexicans have achieved middle-class status in the last decade, and Mexico itself is now a "middle-income" economy. The population is both young and better-educated than ever, and this will translate to continued growth in discretionary income.

While I see positive trends at work in the economy, the Mexican stock market is another story. For years, the exchange has suffered from a dearth of new listings, declining volumes, and some notable departures from buyouts and mergers. The ten-year (price only) annual return for the main Mexican stock index is a woeful 2.2%. While the Mexican government and the exchange are working on initiatives to encourage IPO activity and make it easier to raise capital, it could be a while before any positive impact is felt. Interest rates are another confounding factor. With no point on the Mexican yield curve offering less than 9.5%, it is difficult to convince investors to come off the sidelines and buy equities.

Still, I am excited by the value that Mexican equities offer. Today, I would like to present a family-owned consumer packaged goods manufacturer with incredible brands, multiple partnerships with blue chip American food companies, solid capital allocation, and a bright outlook.

Grupo Herdez, founded in 1914, is a major Mexican food company. Herdez has a dominant position in several different grocery store categories, including mayonnaise and pre-made salsas. The company's market capitalization is MXN 15.2 billion, or USD $900 million.

Grupo Herdez is led by Héctor Hernández-Pons, grandson of the company founder. CEO Magazine did a brief profile of Mr. Hernández-Pons in 2021. The interview touches on one of Mr. Hernández-Pons' signature achievements: the 2009 establishment of MegaMex, now a significant contributor to the company's earnings. Here's another interview in Spanish in *Forbes México*.

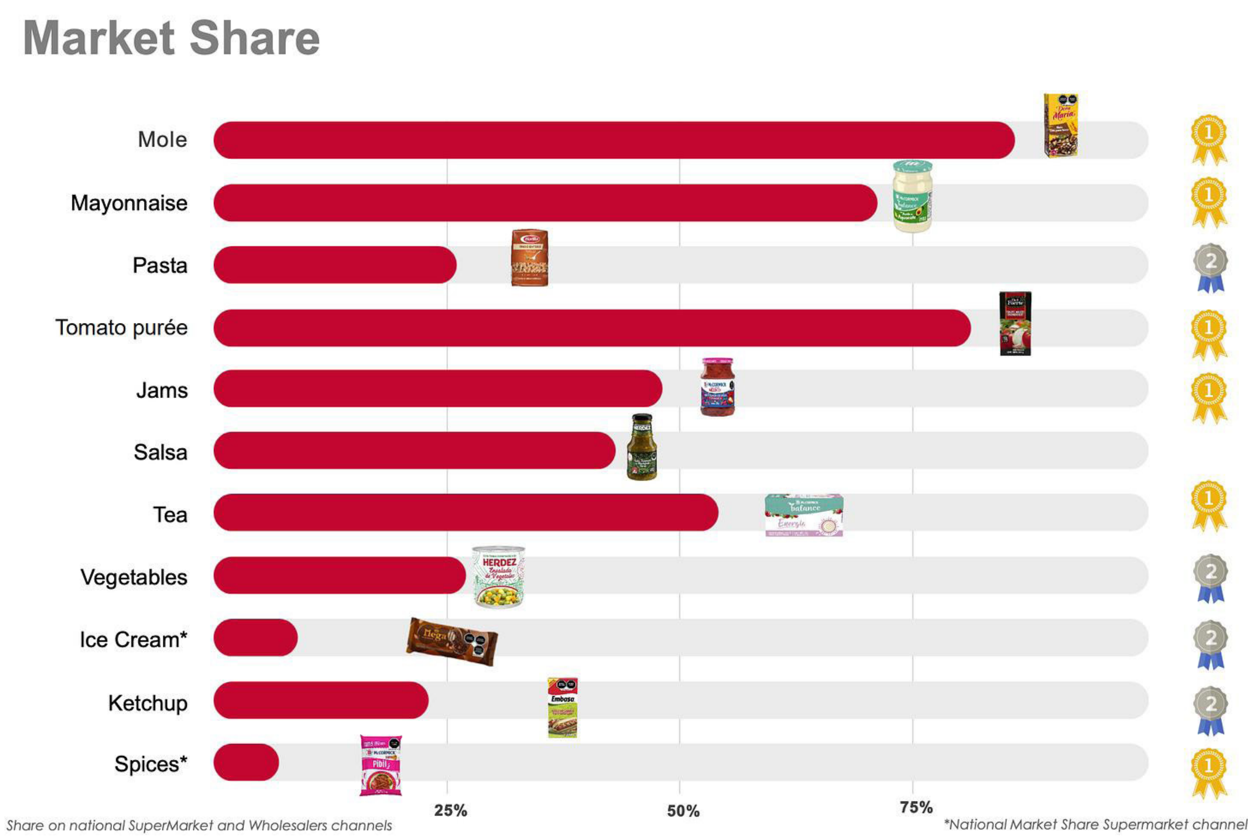
Grupo Herdez conducts its business mostly through partnerships. The company's major earning assets are:

- A 50% interest in McCormick Mexico. The remaining 50% is owned by who else but McCormick & Company, the stalwart spice and seasoning company. The partnership was established in 1947.
- A 50% interest in Barilla Mexico. Barilla is the ubiquitous blue-boxed pasta brand. Barilla is privately-held by the founding Barilla family.
- A 25% indirect interest in MegaMex, a 50%/50% joint venture with Hormel. MegaMex exports Mexican foods to US markets. Pre-prepared guacamole is a major product of theirs, as are tortillas and many other Mexican specialties.

Besides these top-flight joint ventures, Grupo Herdez has a wholly-owned "Impulsos" division that operates retail storefronts offering ice cream and other frozen treats. Unfortunately, this business was severely impacted by COVID and is still struggling to regain its former profitability. Grupo Herdez is working on a number of pricing and product strategies to improve results, and it is making progress. As is, Impulsos is something of a call option. The division operates just under breakeven but could be worth a substantial figure if it manages to restore margins to prior levels.

Here's a look at just some of the brands that Grupo Herdez offers in the United States and Mexico, from a company presentation. Recognize any? I bet you do!

It's difficult to overstate just how dominant Herdez's brands are. The company has huge market share in Mexican supermarkets. Herdez is number 1 or 2 in 10 different categories of popular, frequently-purchased items.



Clearly, Grupo Herdez occupies a strong competitive position. Grupo Herdez's products are household names. Most of these brands are past their high-growth eras, but they will be reliable sellers for a long time to come. Consumer staples businesses like Grupo Herdez usually trade at some premium to the market in general, based on the perception of strong and predictable profitability and defensive characteristics. Customers may opt for cheaper items in a downturn, but everyone needs food.

Grupo Herdez's partners are valued highly by the market. McCormick & Company trades at 27x trailing earnings and 18x EBITDA. Hormel trades at 24x earnings and 16x EBITDA. The 500-pound gorilla that is the Kraft Heinz Company is a comparative bargain at 15x earnings and 10x EBITDA, but Kraft's troubles with tired brands and consumer pushback on pricing are well-known.

McCormick has a 5-year revenue growth rate of 4.7% and EBIT margins averaged 16.9% over the period. Hormel's revenue growth was 4.9% and its EBIT margin averaged 10.4%. Kraft Heinz's revenue was essentially flat, but at least its EBIT margin averaged a healthy 21.0%.

For its part, Grupo Herdez recorded five-year annual revenue growth of 11.5% and an average EBIT margin of 12.5%. This EBIT margin figure includes the losses of the Impulsos division. Excluding Impulsos, the 2023 EBIT margin was 16.9%.

Despite much better revenue growth and comparable profitability, Grupo Herdez shares trade at only 11.6x earnings and 5.8x EBITDA. For both ratios, I have adjusted the figures for the non-owned portions of McCormick Mexico and Barilla Mexico. MegaMex is equity-accounted, so the actual EV/EBITDA ratio would be lower using proportional consolidation. Return on equity hovers in the mid-20s despite a significant corporate cash buffer.

Here is Grupo Herdez's fourth quarter 2023 report. It was a great year for Herdez, despite the continued losses in the Impulsos segment. Every segment saw increases in revenue and operating results. The company paid down debt and benefited from the late 2022 acquisition of Mediterraneo, a producer of Lebanese snacks and dips. Free cash flow generation was excellent. Both strong earnings and normalizing working capital levels contributed.

I also recommend checking out this English language presentation which gives a more qualitative overview of the company's product line, operations, and strategy. The company also conducts its quarterly earnings calls in English.

I think Grupo Herdez shares are way, way too cheap. A more reasonable price/earnings ratio of 18x would put shares at MXN 71, 55% higher than today's MXN 46. An 8x EBITDA multiple would put shares at MXN 75.

My valuation assumes no change in the status of the loss-making Impulsos segment. If this segment's profitability improves or Grupo Herdez chooses to wind it down, the benefit to earnings would be substantial.

I know what you may be thinking. The financials might look good and the valuation may be compelling, but this is an *emerging markets company*. And emerging markets companies are *notorious* for mistreating shareholders, particularly when they are controlled by a single person, family, or entity, like Grupo Herdez is. Cash flows, profits, assets, they're all wonderful. But they may as well not exist if shareholders don't see the benefits. Just ask anyone who has sent their money to languish on the Hong Kong or Singapore stock exchanges, myself included.

Fortunately, Grupo Herdez has a long history of treating shareholders well. The company rewards its owners with steady dividends and share repurchases. Acquisitions and investments are performed only when they conform to sound financial logic, not out of vanity or for empire building. Since 2013, Grupo Herdez's share count is down 24%. Recently, the company has hit the pause button on repurchases, opting instead to pay down debt. Entirely sensible when doing so earns a risk free pre-tax return of 10%. If and when interest rates decline, the company will return to buying back shares.

Now for the risks. I don't think it's right to discuss a stock without mentioning the negatives and the risks, whether actual or merely possible. Among them are:

- Currency fluctuations. The Mexican Peso has been very strong against the US Dollar lately. This reduces the profits that Grupo Herdez earns from exports and from the MegaMex segment. On the other hand, a weaker Mexican Peso would increase these profits. Herdez's substantial US-derived revenues and earnings provide a natural hedge for USD-denominated investors.
- Commodities fluctuations. Grupo Herdez may have difficulty passing through increases in input costs. Additionally, some segments are particularly sensitive to changes in the cost of agricultural products. The company identifies avocados as a large input cost for MegaMex, causing profits to decline when avocado prices surge.
- Changing consumer behavior. Marketers and economists have long pointed out how Mexican consumers are unusually loyal to national brand names, preferring them over store brands or generic label products. If this were to change, it would be to Grupo Herdez's detriment.

- Political risk. Mexico is a relatively well-functioning Western democracy, but its politics can be “colorful.” The election of an anti-corporation and/or “anti-elite” populist government would be a negative.
- Controlled company. Insiders own about 70% of Grupo Herdez shares. They call the shots. They have called them well over time, but shareholders have little recourse if management goes off the rails.

Despite these risks, I think Grupo Herdez represents a compelling opportunity. Buying dominant consumer franchises with healthy balance sheets, good growth potential, and capable management at <12x earnings typically works out well over a reasonable time frame. Grupo Herdez shares trade at low volumes but relatively consistently on the Mexican Stock Exchange. It could take time for investors to rediscover “off the run” Mexican equities. As I noted above, it is difficult to make the case for Mexican equities when Mexican bonds are yielding 10%. But Grupo Herdez will continue growing its earnings, making the occasional smart acquisition, and returning capital to shareholders. At some point the market will take notice.

Continue reading here.

Fifteen "cannibal stocks" you should know about (from Compounding Quality)...

Everyone wants to own the best companies in the world.

Have you ever heard about **cannibal stocks**?

These are companies that are heavily buying back their own shares.

Cannibal stocks can be very interesting as **your ownership in the company increases every single year without doing anything.**

What are cannibal stocks?

Cannibal stocks are companies that are heavily buying back their own shares.

If you own a business that earns $10 per share and the company buys back 50% of its outstanding shares, EPS will increase from $10 to $20.

As a result, the stock price should also double.

Here's an overview of the magic of buybacks by Mohnish Pabrai:

The Magic of Buybacks

Shares Bought Back	Return Without a Change in Earnings or PE Multiple
50%	2x
67%	3x
80%	5x
90%	10x
95%	20x
98%	50x
99%	100x

- It only starts becoming magical after 80%.
- Robust earnings growth and multiple expansion delivers huge home runs.

It is important to highlight that **share buybacks only create value when the stock is undervalued**.

This is very logical as buying back your own shares can be seen as an investment in your own company.

As an investor, you also only want to buy stocks when they are undervalued.

🏆 15 Cannibal Stocks You Should Know

We used the following criteria to screen for High-Quality Cannibal Stocks:

- ROIC > 15%
- Profit margin > 10%
- EPS growth past 5 years > 10%
- Decrease in shares outstanding past 10 years > 30%

1. Domino's Pizza ($DPZ)

Domino's Pizza is the largest pizza company in the world. They operate a network of **company-owned and franchise Domino's Pizza stores**, located throughout the United States as well as other countries.

- FCF Margin: 8.6%
- ROIC: 56.9%
- FCF Yield: 3.7%
- Expected FCF Growth (next 3 years): 6.3%
- Decline in outstanding shares since 2010 (%): 41.1%

2. Ameriprise Financial ($AMP)

Ameriprise Financial operates as a financial planning and services firm. The Company provides **financial planning** and products and services that are designed to be utilized as solutions for its clients' financial needs.

- FCF Margin: 31.5%
- ROIC: 28.6%
- FCF Yield: 10.6%
- Expected FCF Growth (next 3 years): 18.2%
- Decline in outstanding shares since 2010 (%): 57.3%

3. Discover Financial Services ($DFS)

Discover Financial Services operates as a **credit card issuer and electronic payment services** company. The Company issues **credit cards and offers student and personal loans, as well as savings products**.

- FCF Margin: 51.8%
- ROIC: 19.2%
- FCF Yield: 9.1%
- Expected FCF Growth (next 3 years): 7.5%
- Decline in outstanding shares since 2010 (%): 51.0%

4. Dollarama ($DOL)

Dollarama is a Canadian company that operates as an online marketplace. The Company offers cleaning, school, office, home, kitchen, food, health, beauty, hardware, electronics, toys, and pet products.

- FCF Margin: 14.6%
- ROIC: 21.6%
- FCF Yield: 3.7%
- Expected FCF Growth (next 3 years): 12.1%
- Decline in outstanding shares since 2010 (%): 32.9%

5. HCA Healthcare ($HCA)

HCA Healthcare offers health care services. **The Hospital provides diagnosis, treatments, consultancy, nursing, surgeries, and other services**, as well as **medical education, physician resource center, and training programs**.

- FCF Margin: 6.9%
- ROIC: 18.3%
- FCF Yield: 5.9%
- Expected FCF Growth (next 3 years): 8.3%
- Decline in outstanding shares since 2010 (%): 35.1%

6. Williams-Sonoma ($WSM)

Williams-Sonoma operates as a home furnishing store. The Company retails cooking and serving equipment, home furnishings, and home accessories through retail stores, mail-order catalogs, and e-commerce.

- FCF Margin: 8.1%
- ROIC: 36.2%
- FCF Yield: 7.1%
- Expected FCF Growth (next 3 years): -3.6%
- Decline in outstanding shares since 2010 (%): 32.7%

7. Grand Canyon Education ($LOPE)

Grand Canyon Education provides online post-secondary education services. The Company offers **graduate and undergraduate degree programs in disciplines of education, business, and healthcare.**

- FCF Margin: 20.4%
- ROIC: 23.6%
- FCF Yield: 5.7%
- Expected FCF Growth (next 3 years): 10.3%
- Decline in outstanding shares since 2010 (%): 32.1%

8. Winmark ($WINA)

Winmark develops, franchises, and operates value-oriented retail concepts for stores that **buy, sell, trade, and consign used and new merchandise**. The Company operates in the United States.

- FCF Margin: 53.6%
- ROIC: 95.9%
- FCF Yield: 3.0%
- Expected FCF Growth (next 3 years): 10.4%
- Decline in outstanding shares since 2010 (%): 31.1%

9. Visa ($V)

Visa is a great quality business with a wide moat and incredible profitability margins. When you invest in Visa, you invest in a strong secular trend.

- FCF Margin: 61.0%
- ROIC: 28.2%
- FCF Yield: 5.6%
- Expected FCF Growth (next 3 years): 15.7%
- Decline in outstanding shares since 2010 (%): 43.4%

10. O'Reilly Automotive ($ORLY)

O'Reilly Automotive retails and supplies **automotive aftermarket parts, tools, supplies, equipment, and accessories.** The Company **sells its products to do-it-yourself customers, professional mechanics, and service technicians**.

- FCF Margin: 17.9%
- ROIC: 41.2%
- FCF Yield: 3.8%
- Expected FCF Growth (next 3 years): 10.0%
- Decline in outstanding shares since 2010 (%): 55.8%

11. Autozone ($AZO)

AutoZone is a retailer of automotive replacement parts and accessories. The Company offers an extensive product line including **new and remanufactured automotive hard parts, maintenance items, accessories, and non-automotive products.**

- FCF Margin: 15.6%
- ROIC: 41.4%
- FCF Yield: 4.9%
- Expected FCF Growth (next 3 years): 16.5%
- Decline in outstanding shares since 2010 (%): 57.6%

12. PulteGroup ($PHM)

PulteGroup Inc. sells and constructs homes, and purchases, develops, and sells residential land, and develops active adult communities. The Company also provides **mortgage financing, title insurance, and other services** to home buyers.

- FCF Margin: 3.4%
- ROIC: 25.2%
- FCF Yield: 10.5%
- Expected FCF Growth (next 3 years): 15.5%
- Decline in outstanding shares since 2010 (%): 40.9%

13. Dillards ($DDS)

Dillard's operates retail department stores located primarily in the United States. The Company offers products like tops, pants, swimsuits, shorts, skirts, jeans, jackets, tees, shirts, blazers, sandals, sneakers, slippers, and much more.

- FCF Margin: 11.9%
- ROIC: 38.2%
- FCF Yield: 12.4%
- Expected FCF Growth (next 3 years): 20.1%
- Decline in outstanding shares since 2010 (%): 74.4%

14. Applied Materials ($AMAT)

Applied Materials is **active in semiconductor wafer fabrication equipment**. They are **a market leader in materials engineering solutions used to produce virtually every new chip** and advanced display in the world.

- FCF Margin: 17.9%
- ROIC: 35.3%
- FCF Yield: 3.9%
- Expected FCF Growth (next 3 years): 2.6%
- Decline in outstanding shares since 2010 (%): 36.5%

15. MSCI (MSCI)

MSCI Inc. provides investment decision support tools to investment institutions worldwide. The Company produces indices and risk and return portfolio analytics for use in managing investment portfolios.

- FCF Margin: 48.1%
- ROIC: 27.9%
- FCF Yield: 2.7%
- Expected FCF Growth (next 3 years): 15.5%
- The decline in outstanding shares since 2010 (%): 33.1%

Continue reading here (subscription may be required).

"PayPal stock has fallen far enough. It's time to buy" (from *Barron's*)...

PayPal Holdings has gone from being one of the market's most expensive stocks to one of its cheapest—and it's now cheap enough to buy.

The name PayPal used to be ubiquitous in online payments, and the company had the growth to prove it. Its Venmo service, for example, was especially popular with younger users, while using its namesake service was the default choice for many while shopping online. But Apple and Alphabet's Google ramped up their own payment options and other companies ventured into the space. As online shopping cooled following the pandemic, that growth evaporated. PayPal was forced to pivot to less-profitable products, such as providing white-label payment services to online companies.

That pressured PayPal's gross margins, which dropped to 45.8% in the fourth quarter of 2023 from 55.9% in 2020. Its shares have plunged 80% since peaking in 2021, leaving it with a market cap of $66.9 billion—and leaving investors wondering what the future holds for the increasingly beleaguered company.

The bad news is that PayPal will never return to the growth of old. The good news is that it doesn't need to. With a new CEO, Alex Chriss, leading the charge, change is coming—change that should help reverse the recent weakness. The company is becoming leaner and more focused, with new initiatives aimed at stemming the decline in profit margins and boosting earnings. With the stock trading in line with regional banks, it wouldn't take a lot of good news—just less bad news—for shares to start bouncing back.

"PayPal is trading like a coal mine that has a finite life," says David Rolfe, chief investment officer at Wedgewood Partners. "It won't take a whole lot to get it rerated."

Pay It Forward

PayPal trades too much like a bank and not enough like a fintech.

Company / Ticker	Recent Price	YTD Change	Market Value (billion)	Valuation*
PayPal Holdings / PYPL	$62.50	1.9%	$64.3	11.5
PNC Financial Services Group / PNC	152.68	-1.5	60.1	11.9
U.S. Bancorp / USB	43.69	1.0	67.3	10.9
Block / SQ	85.96	11.0	50.3	23.9

*12-month forward price/earnings ratio
Sources: FactSet, Dow Jones Market Data

The company does have work to do—and it knows it. At its "innovation day" on Jan. 25, management said it "would shock the world." It fell far short of doing that. Chriss laid out steps to address PayPal's big issues, including making it easier for people to use it to make purchases, increasing profits on its white-label offerings, and focusing on innovation in core products. Most of these were expected, however, and the company didn't cite numbers along with the initiatives. The stock fell 3.7% that day.

Still, PayPal did offer some initiatives that could yet pay off. J.P. Morgan Securities analyst Tien-Tsin Huang notes that the company is focused on innovating at a faster pace. Its new Fastlane service can autofill personal information and credit card data, Huang writes. PayPal said this could significantly increase the completion rate for transactions. Huang has a $70 price target on the stock, up 12% from Wednesday's $62.45 close.

Continue reading here (subscription may be required).

An under-the-radar gold producer with a great dividend (from Mining Charts)...

Mineros S.A. has 2 gold projects in production right now, one is located in Colombia and the other is Nicaragua. The company produced 250k ounces between the two last year. Each of these jurisdictions would be considered high risk, which I think explains some of the valuation here. The current market cap is $275 million Canadian, the company trades at a P/E ratio of 2.78 and trades at a massive discount to book value at 0.60, the balance sheet is in a very healthy position as well.

Mineros came onto my radar a few weeks ago, when the stock broke out on it's bullish earnings report which coincided with the gold price breaking out. Here is the weekly chart below you can see the massive volume that has been pouring into the stock. It's one of the most bullish charts I have come across recently.

Here are some of the highlights from the Q4 Earnings report:

-AISC is currently at $1300 between the two projects, which means the company is a cash making machine at the current gold price, which I expect can go much higher this year.

-The company was able to increase the dividend by 11% in 2023, the current annual dividend yield is still over 10%.

-There was large increases year over year across the board in many of the important financial metrics. This will continue to increase at current gold prices.

Financial and Operating Highlights.

	Three Months Ended December 31,		Change		Year ended December 31,		Change	
	2023	2022	$	%	2023	2022	#	%
Financial								
Revenue	130,427	105,059	25,368	24%	447,290	414,937	32,353	8%
Cost of sales	(82,663)	(70,677)	11,986	17%	(301,888)	(282,918)	18,970	7%
Gross Profit	47,764	34,382	13,382	39%	145,402	132,019	13,383	10%
Profit for the period from continuing operations	22,808	18,136	4,672	26%	74,538	56,097	18,441	33%
Basic and diluted earnings per share from continuing operations	$0.08	$0.06	$0.02	26%	$0.25	$0.19	$0.06	33%
Loss for the year from discontinued operations	(1,043)	(38,130)	37,087	(97)%	(57,324)	(51,610)	(5,714)	11%
Basic and diluted earnings per share from continuing and discontinued operations	$0.07	$(0.07)	$0.14	(209)%	$0.06	$0.01	$0.04	284%
Adjusted EBITDA[1]	53,364	40,117	13,247	33%	172,146	156,156	15,990	10%
Net cash flows generated by operating activities	52,932	36,602	16,330	45%	89,908	82,607	7,301	9%
Net free cash flow[1]	36,761	32,210	4,551	14%	49,202	35,611	13,591	38%
ROCE[1]	30%	25%	5%	21%	30%	25%	5%	21%
Net Debt [1]	(24,316)	17,517	(41,833)	(239)%	(24,316)	17,517	(41,833)	(239)%
Dividends paid	5,228	4,862	366	8%	20,519	22,990	(2,471)	(11)%

There are 2 large institutional shareholders that own over 40% of the company currently, one is a large player in Colombian banking/business sector and the other is an asset management company out of Colombia. It's always a positive to see shares in strong hands.

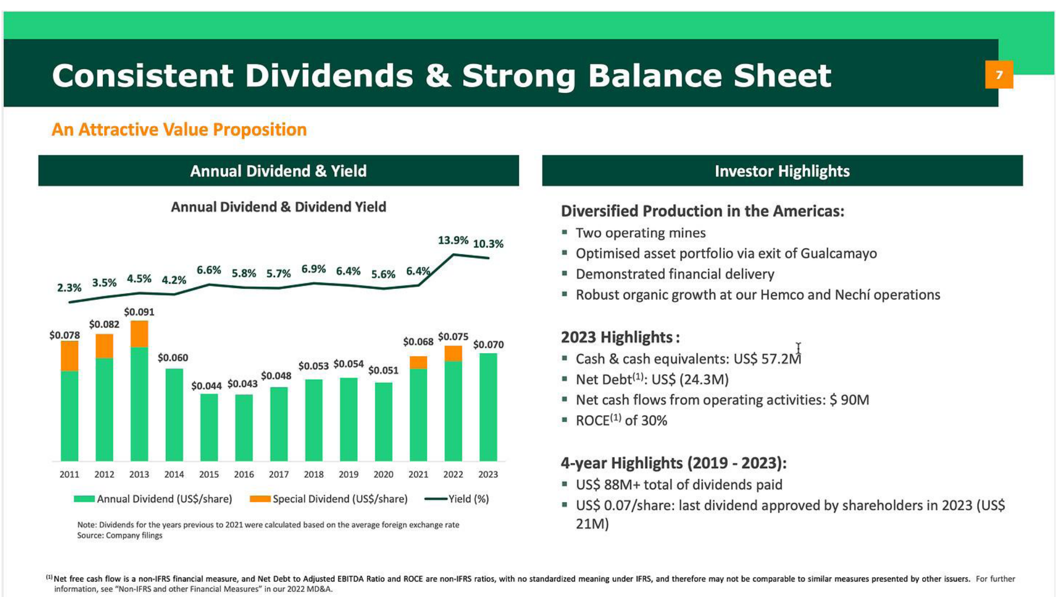
Top Shareholders (as at Dec 31, 2023)

Shareholders	Shares Held (M)	% of Shares O/S
Mercantil Colpatria S.A.	91.1	30.4%
Negocios y Rep. S.A.S.	33.7	11.3%
Total Mineros >10% Shareholders	124.8	41.7%

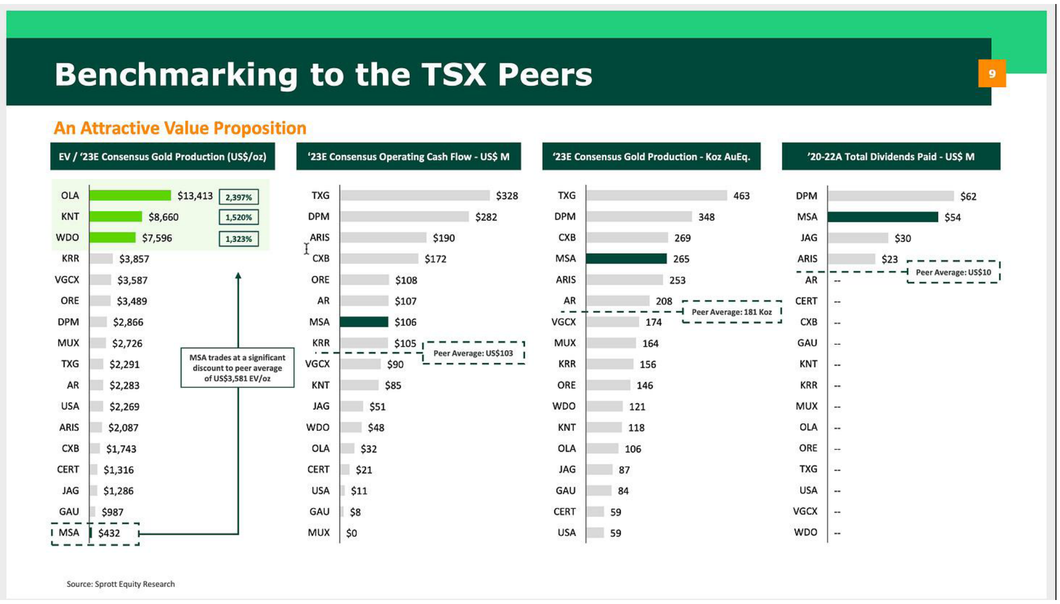
Mercantil Colpatria S.A.

- Leading player in the Colombian banking and business sector
- Founded by the Pacheco family in 1955, Grupo Colpatria has grown into one of the largest conglomerates in Colombia
- A supportive major shareholder of Mineros since 1977

I really like the strong history of the dividends here and the balance sheet is very healthy compared to some of the other producers. The next quarterly dividend is set to be paid out April 18, at .03 cents a share, with the ex-date being April 12.



When compared to similar gold producers on the TSX, the company trades at a massive discount even with much better metrics than many of the other projects. Once again I believe the jurisdictions probably have lots to do with this.



It's also important to mention the company still has over a decade of reserves at the Colombia asset and the company has been able to extend the life of the Nicaraguan asset into the 2030's through effective drilling.

In summary the investment thesis is simple here, you have to believe the gold price stays at least relatively steady here with the possibility of much higher prices. Mineros is in a great fiscal position and is very extremely undervalued right now. The company has proven they can execute and margins will continue to increase at $2100 gold with the potential for the dividend to increase significantly. I believe this is a solid place to park some money for the next while.

Copper looks likely to outperform stocks over the next several years (from Otavio (Tavi) Costa via X)...

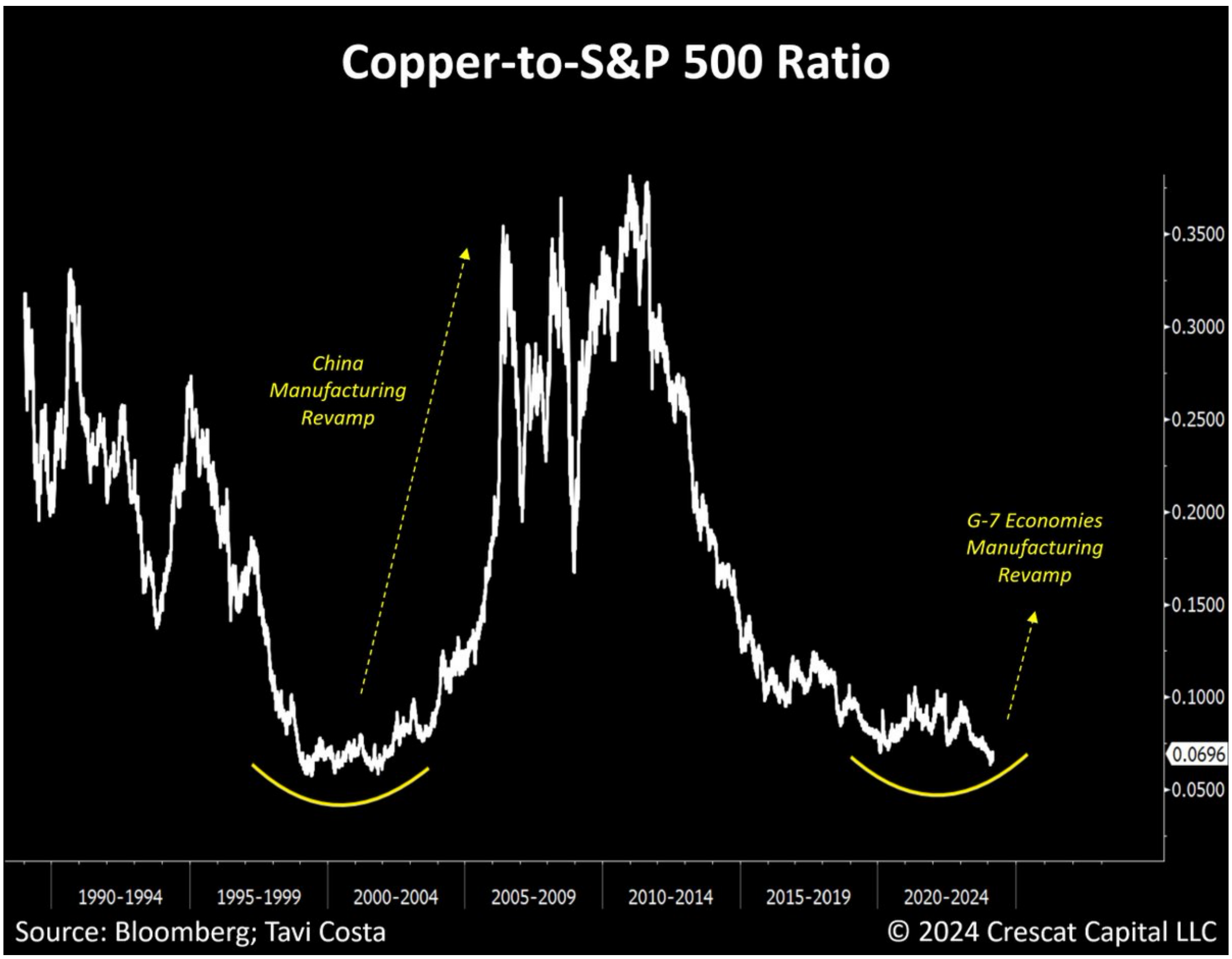
intriguing potential double bottoms in markets today.

While the green revolution and electrification efforts are set to provide a significant boost in demand for the metal, a more compelling argument lies in the reshoring of developed economies.

For over seven decades, the US and other G-7 nations have neglected significant infrastructure enhancements.

The burgeoning deglobalization forces are expected to vigorously bolster these construction undertakings.

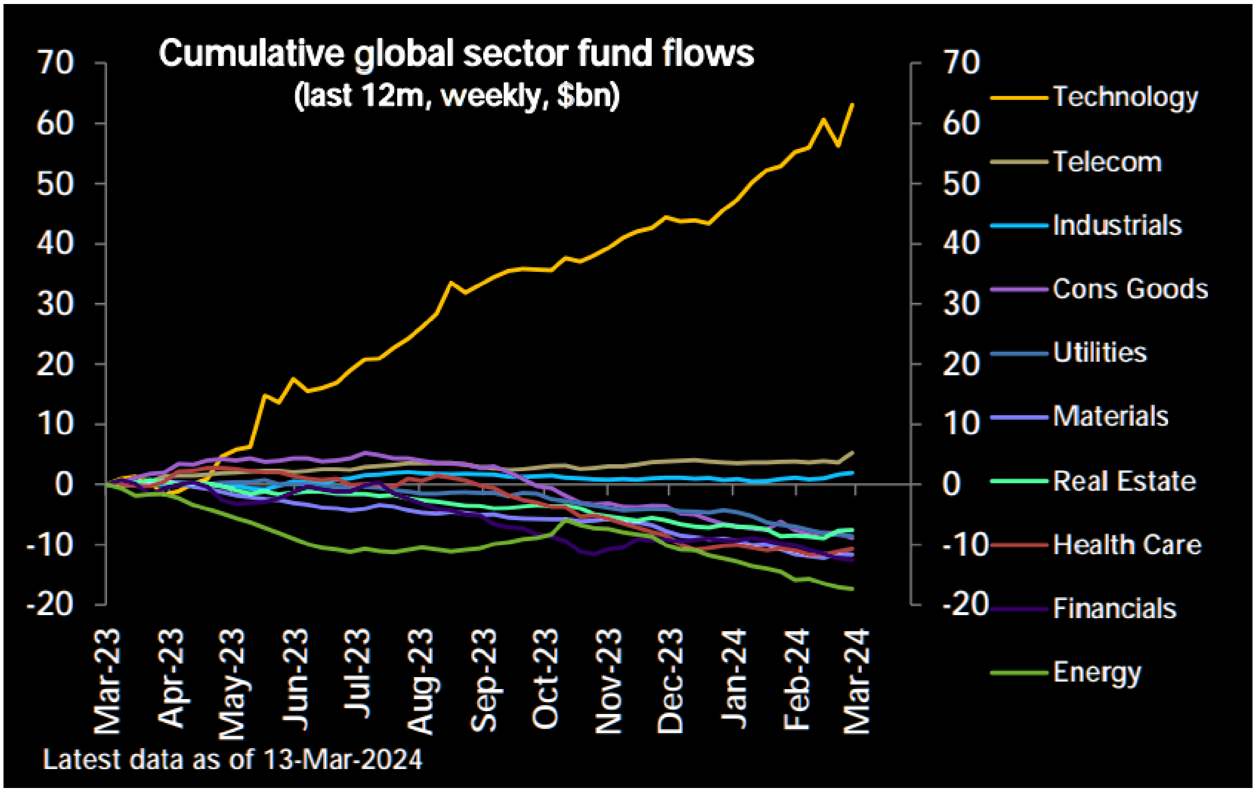
Copper is likely to emerge as a major beneficiary of these evolving trends.



The energy sector looks great from a contrarian perspective (from Markets & Mayhem via X)...

Flows to other sectors have been quite subdued outside of tech, with strong outflows from energy.

Yet energy stocks remain attractively valued and oil prices are rising... Seems like a nice contrarian setup to me.



Meanwhile, energy sector stocks (XLE) are on the verge of a multi-year breakout (from Caleb Franzen via X)...

How to invest for a weaker U.S. dollar (from Morgan Stanley Wealth Management)...

Key Takeaways:

- A strong dollar has helped lower U.S. inflation and boost stock multiples.
- But recent developments indicate that the greenback's 16-year bull run may be coming to an end.
- Investors may consider increasing exposure to commodities and international stocks.

The mighty U.S. dollar has helped exemplify a post-COVID business cycle of high yields and stronger economic growth in the U.S. relative to other parts of the world—but signs are emerging that the buck may be headed for bear territory.

The strong greenback has helped the Federal Reserve's inflation fight by muting pricing pressures from American imports and critical commodities. By lowering certain costs, it has also helped keep financial conditions relatively loose, offsetting some of the tightening impact of Fed rate hikes. This, in turn, has supported recent U.S. equity gains.

But recent market developments suggest that the dollar's 16-year secular bull run that emerged from the 2007-2008 financial crisis may finally be losing steam. Indeed, the dollar has started to weaken even as the market now appears to expect that rates may remain higher for longer, which would typically lend support to the dollar.

Could the dollar be poised for its next secular bear market? Morgan Stanley's Global Investment Committee believes it's a possibility that's at least worth considering, given the following.

1. Commodity signals:

Commodities, which tend to be negatively correlated to the dollar, have been advancing recently. Gold, for one, has hit an all-time high of $2,183 per ounce, up 18% since last October, which may suggest investors think that economic growth is slowing. What's more, Bitcoin, often considered digital gold, is up more than 150% over the same period. These trends appear in line with more-recent rebounds in cyclical commodities, such as oil and copper.

2. Bank of Japan's policy shift:

Since early 2021, the Japanese yen has depreciated against the U.S. dollar by about 50%. That was largely a function of widening interest-rate differentials, as the U.S. Fed raised rates aggressively while the BoJ held fast to a program of yield-curve control in an effort to keep yields lower. But given improvements in Japan's real growth, inflation and wages, odds are rising that its central bank will shift its policy to allow rates to rise, helping strengthen the yen. In turn, this may drive repatriation flows out of U.S. securities, including Treasuries, of which Japanese investors have been key buyers for more than 25 years.

3. U.S.-China dynamics:

Tensions between the world's two largest economies are already high around technology access and generative AI semiconductors. Legislation moving through Congress that could ban a major Chinese-owned social media platform from operating in the U.S. could be a further incentive for China to accelerate its efforts to reduce reliance on the dollar for trade.

The idea of "American exceptionalism" is broadly valued in global markets but it is also underpinned by a strong dollar. A weakening in the U.S. currency may create headwinds for equity multiples, in which case investors may benefit from asset and geographic diversification in their portfolios.

We encourage investors to keep an eye on the U.S. Dollar Index (DXY), which tracks the dollar's value relative to a basket of foreign currencies. Investors may also want to consider increasing exposure to real assets, such as commodities, gold, energy- and power-related infrastructure, and real estate investment trusts (REITs). Also look to international stocks, especially in Japan, India, Mexico, and Brazil.

Continue reading here.

This precious metals miner could be a backdoor bet on uranium (from Brandon Beylo via X)...

Looks like Sibanye-Stillwater $SBSW is getting serious about monetizing its uranium assets.

As a reminder, the company has ~32Mlbs of uranium in on-surface tailings.

That's roughly the entire market cap of the company assuming $80/lb uranium.

Sibanye-Stillwater appoints Head of uranium to drive realisation of substantial value

Johannesburg, 20 March 2024: Sibanye-Stillwater (Tickers JSE: SSW and NYSE: SBSW) is pleased to announce that it has appointed Greg Cochran as Executive Vice President (EVP) Head of uranium, effective 1 June 2024. Greg will be responsible for developing and driving strategies to realise and optimise the inherent value of the Group's substantial uranium resources, as well as for leveraging his significant experience and track record of value creation in the uranium industry to capitalise on other opportunities that may arise.

Greg is a respected international mining executive with over 30 years of experience in a diverse range of commodities and in various leadership positions globally and in uranium.

Three bullish opportunities in the energy sector (from Special Situation Investing)...

Texas Pacific Land (TPL)

It's been a while since we wrote about Texas Pacific Land Corporation. For our newer readers and listeners, TPL is the owner of 868,466 surface acres in the Texas Permian Basin. The $13 billion company's revenues come from royalties energy producers pay to use its land and from its water business, where it provides and recycles water used in fracking. It's a fantastic company with massive margins and an amazing asset portfolio. You can read all our previous pieces on the company for more details (link, link, link, link).

Our two last updates on TPL highlighted the on-going legal spat between the company's management and two of its largest shareholders. The dispute arose when the large shareholders did not vote in lockstep with management in support of increasing the company's authorized shares from roughly 8 million to 46.5 million. Our piece, *TPL's Governance Battle*, goes into detail on the issue, but suffice it to say, the whole deal has been a dark cloud hanging over TPL for more than a year.

Since our last update, the legal proceedings concluded. Both the Delaware Court of Chancery and Supreme Court ruled in favor of TPL's management. This means the company is clear to authorize up to 46.5 million shares. Since both hosts of this show dislike shareholder dilution, and we believe it's challenging for managements to use shares in such a way that doesn't result in dilution, this was not the outcome we wanted. But it's the one we got.

With the ruling finalized, TPL announced a 3-for-1 stock split on March 7th. Owners of the stock will receive 2 additional shares for every one they own on March 18th. The new shares will be distributed March 26th. Given that there are currently 7,668,422 shares of TPL outstanding, after the split, there will be 23,005,266 shares outstanding.

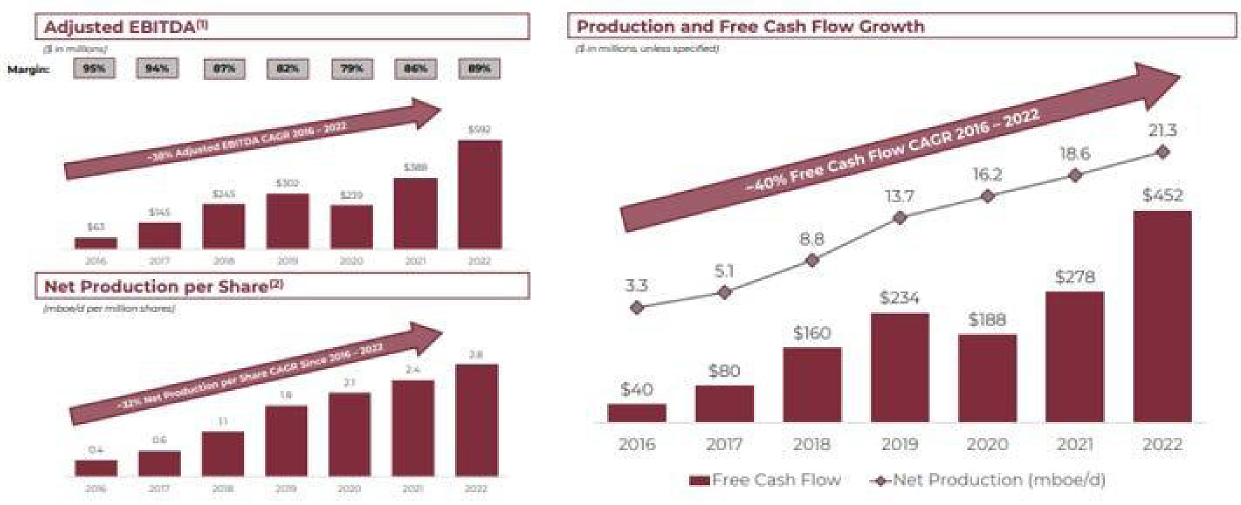
This leaves an additional roughly 23 million shares authorized that management can determine how to use. Non-dilutive share splits are fine and can increase liquidity which could benefit a thinly traded stock such as TPL. If management chooses to use the remaining shares to fund non-value adding acquisitions or worse, to pay themselves, shareholders could see their ownership in the company significantly diluted.

In an apparent effort to ease the mind of concerned shareholders, during its latest earnings call on 22 February, TPL's CEO waxed lyrical about the factors to consider when deciding how to allocate capital. Organic investments, buybacks, acquiring external assets, and dividends were all discussed but no ranking of priority was given. He did seem to suggest that TPL's shares were not cheap and thus buybacks were not top of the list.

Even though the litigation didn't conclude the way we hoped, we remain bullish on TPL's long-term prospects.

Like Buffett reportedly said of Coca-Cola, we believe a ham sandwich could run TPL. (We aren't implying that one currently does.) Regardless of the current uncertainty concerning authorized shares, TPL remains a simple, high quality company.

Check out the image below snagged from the company's latest investor presentation. They show that since 2016 through 2022, the company's adjusted EBITDA grew at a CAGR of 38%, net production per share grew at a CAGR of 32%, and free cashflow had a CAGR of 40%.



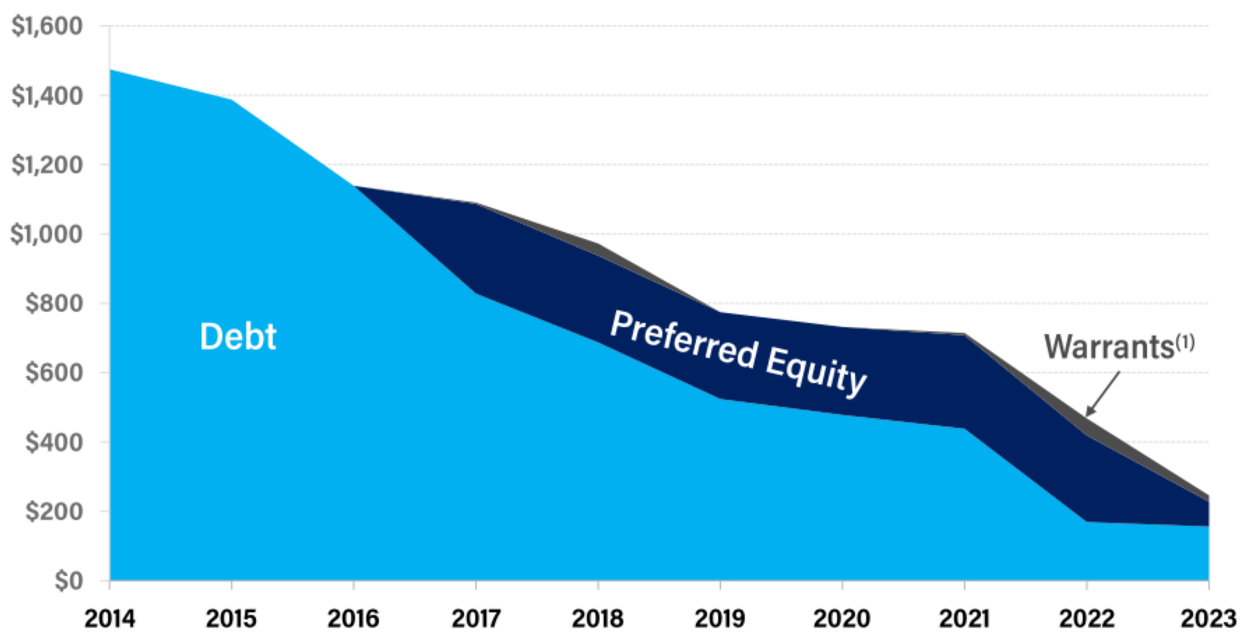
texaspacific.com

We are encouraged to see insiders buying of TPL shares lately. In addition to Murray Stahl, who buys TPL almost every day, two other directors have recently bought large amounts of TPL stock. In the last two weeks, Eric Oliver bought approximately $1 million worth of stock and Robert Roosa bought $500,000 worth. Both Stahl's continued purchases, and Oliver's recent purchases are particularly of note since both were among the party that just lost the court battle against the company. On a number of occasions, Murray Stahl said the litigation hasn't broken the relationships between the opposed parties and they still agree on most everything...including TPL's bullish prospects.

Natural Resource Partners (NRP)

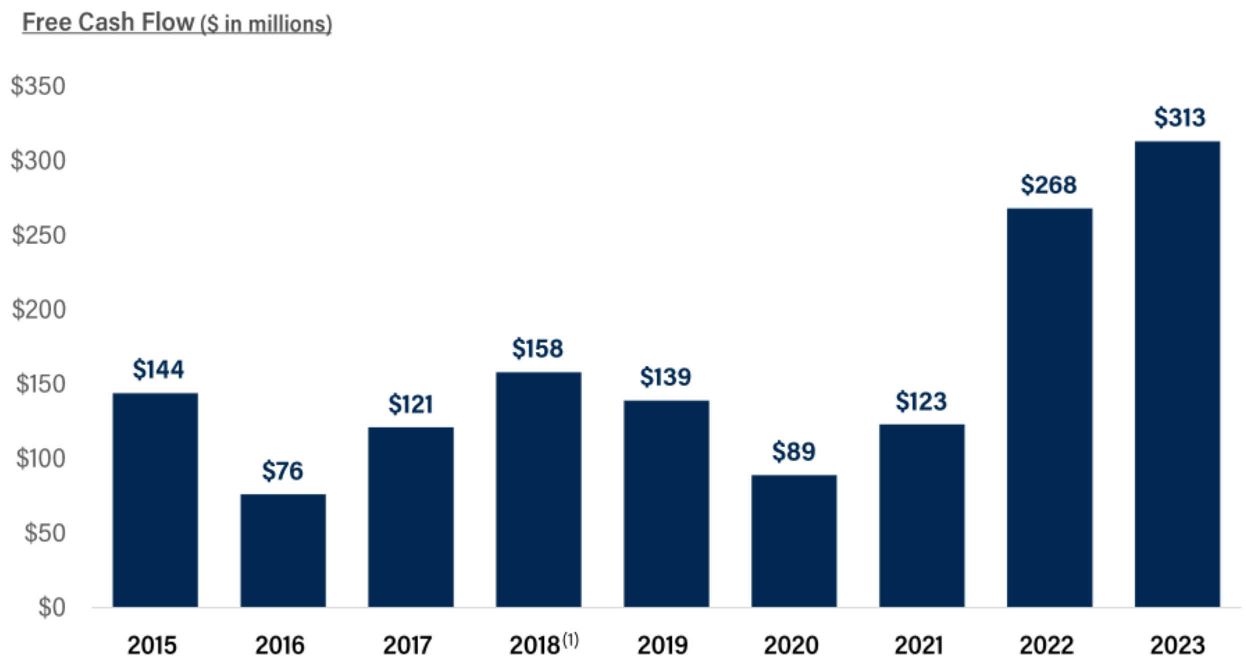
Our thesis with NRP remains in tact. The company continues to pay off debt obligations, remaining laser-focused on the goal it set back in 2015—become debt free and free up cashflow for unit holders.

Total obligations—warrants, preferred equity and debt—which were $1.5 billion in 2015, are only about $270 million today.



nrplp.com

This dramatic reduction is supported by robust cash flow, depicted in the chart below. The company produced record free cashflow in 2023 of $313 million. Yes, that's $313 million from a $1.1 billion market cap company. We'll let you do the math.

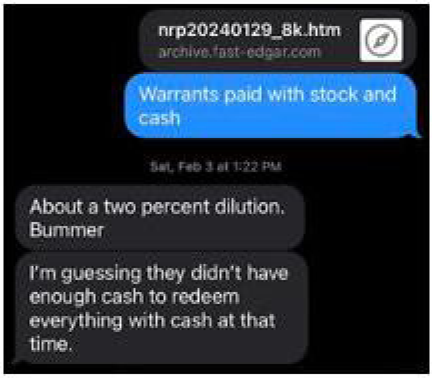


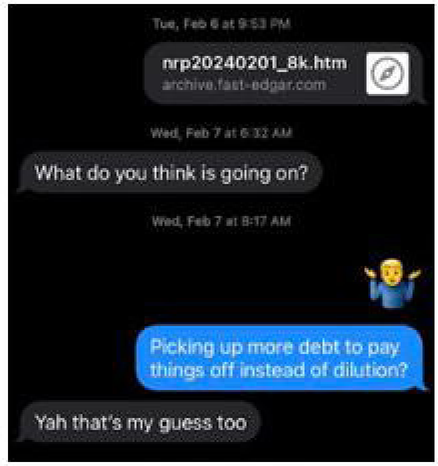
nrplp.com

Depending on the price of coal, natural gas, soda ash, and the amount of production by its lessees going forward, NRP will be extremely close to its goal within the next eighteen months.

The company kicked off the new year by settling 462,165 warrants with $10 million in cash and 198,767 common units. This was the first time we'd seen the company issue units. Then on February 1st, the company announced an increase to its total aggregate commitment under the credit facility from $155 million to $185 million. At first, these two developments—dilution and more debt—could appear negative.

Our assumptions at the time were, first, the company didn't have the cash on hand to settle all the warrants in cash (as had been its recent habit) and so it issued shares, and second, the increase to the credit facility was to avoid further dilution. The texts below show our thoughts in real time.





Below-average texting

On March 7th, during the company's latest earnings call, NRP's CEO, confirmed our suspicions by stating:

> There are two factors we consider when deciding whether to settle warrants with cash or common units: First, do we have ample liquidity, which we define quite conservatively, I might add; and second, is the market value of the common units less than our estimate of intrinsic value? If the answer to both of those questions is yes, we settle with cash.
>
> While we will not comment specifically directly on our view of intrinsic value, I will say that it was our inability to answer yes to the liquidity question that caused us to issue units to settle a portion of the warrant exercises early this year. We continue to add additional bank revolver capacity that will provide financial flexibility to settle warrants with cash and accelerate redemptions of preferreds.

As an infection point for NRP approaches, we remain confident in management's competence and shareholder-centric focus. We'll end this section of today's piece with the CEO's response to a question regarding how the company would allocate its cashflow today if it were debt free. He replied:

> Well, right now, we are still a bit out from getting to that point where the obligations are completely paid down. You are right in what you

summarized initially that at our current run rate that it's not too long before we get to the point where we're obligation free.

But I don't want to speculate now on what we would do in 1.5 years, 2 years from now if we had excess cash. I can tell you at this point in time, we don't see opportunities in the market.

If we were in that theoretical situation where we had excess cash today, there are not on the horizon overly attractive opportunities to deploy capital. That being said, I will point out that we are focused on the task at hand right now, and we're not out beating the bushes for places to deploy capital.

I think you can rest assured that we are going to be quite thoughtful about anything we do with respect to deploying capital in any manner other than distributing it out to unit holders.

Permian Basin Royalty Trust (PBT)

Another situation we're following closely is Permian Basin Royalty Trust. The short-sightedness of the market is creating an opportunity for long-term investors. Within the next couple years, cashflow available to the Trust's unit owners will likely explode.

The Trust is a pass-though vehicle for oil and gas royalties. Over the last few years, the operator on the Trust's Waddell Ranch property invested massive capex to increase production. Because the Trust has a net profits/overriding royalty, it is responsible for covering a portion of the capex. As a result, it paid out $3 million toward CAPEX in 2019, $10 million in 2020, $66 million in 2021, $124 million in 2022, and finally $120 million in 2023. This investment increased royalties from the Waddell Ranch six times, up from $39 million to $251 million.

	Year Ended December 31,									
	2023		2022		2021		2020		2019	
Gross Proceeds of Sales From the Underlying Properties:	Waddell Ranch Properties	Texas Royalty Properties	Waddell Ranch Properties	Texas Royalty Properties	Waddell Ranch Properties	Texas Royalty Properties	Waddell Ranch Properties	Texas Royalties Properties	Waddell Ranch Properties	Texas Royalty Properties
Oil Proceeds	$213,356,229	$16,423,167	$195,554,348	$20,665,465	$66,328,817	$12,799,649	$22,745,332	$10,093,604	$31,769,427	$13,325,221
Gas Proceeds	17,428,482	1,159,111	37,108,451	1,357,568	17,259,346	906,335	4,584,768	595,961	7,655,763	1,169,754
Other	20,293,769	—	$ 31,318,921	—	—	—	—	—	—	—
Adjustment(1)	—	—	(20,315,365)	—	9,423,956	—	8,583,304	—	—	—
Total	251,078,480	17,582,278	243,566,355	22,023,033	93,012,119	13,705,984	35,913,404	10,689,565	39,425,195	14,494,975
Less:	—	—								
Severance Tax	—	—								
Oil	9,678,938	632,418	8,915,016	792,637	3,057,598	380,409	1,056,855	414,326	1,457,033	489,096
Gas	933,225	49,117	4,481,839	83,552	194,140	48,894	164,243	32,666	269,932	36,693
Other	21,715,807	134,222	$ 15,427,633	—	173,640	—	726,596	—	—	—
Lease Operating Expense and Property Tax Oil and Gas	79,628,562	960,000	43,673,061	800,380	23,026,783	849,824	19,635,387	738,915	23,371,924	1,103,052
Capital Expenditures	120,462,603	—	124,283,888	—	66,559,957	—	10,314,532	—	3,306,832	—
Total	232,419,135	1,775,757	$196,781,437	$ 1,676,539	$93,012,118	$ 1,279,127	$31,897,613	$ 1,185,907	$28,405,719	$ 1,628,841
Net Profits	18,659,345	15,806,521	$ 46,784,918	$20,346,494	$ 0	$12,426,857	$ 4,015,791	$ 9,503,658	$11,019,476	$12,866,134
Net Overriding Royalty Interest	75%	95%	75%	95%	75%	95%	75%	95%	75%	95%
Total Royalty Income for Distribution	$ 13,994,509	$15,016,195	$ 35,088,618	$19,329,169	$ 0	$11,805,514	$ 3,011,843	$ 9,028,475	$ 8,264,606	$12,222,827

pbt-permian.com

We believe at some point the operator will decrease CAPEX and milk the rewards of its years of investment. This will free up a massive amount of cashflow for Trust unit owners. For a deeper dive into the situation, check out our previous piece.

Over the last year, the Trust's shares traded down 50%. Since we wrote our piece on the Trust in September, the shares are down about 33%. So a situation we thought was good back then appears even better now.

morningstar.com

Timing remains the question. Over the last month, the Trust released both its 2023 10K and a 8K that gave insight into what to expect in 2024.

On Thursday, February 29th, PBT released its 10K. We were hoping to get insight into what the operator (Blackbeard) expected for its 2024 capex budget. Any hint at a decrease in capex would be great news. The filing reported:

> Blackbeard [the operator] has advised the Trustee that the proposed budget for 2024 has not been finalized; however, it has provided the Trustee with a preliminary capital expenditure budget of approximately $301 million (gross).

At first our assumption was that the Trust's portion of the budget would be approximately 75% of the gross, about $225 million, almost double the amount it paid in 2023.

We were incorrect.

Perhaps it was a similar misunderstanding that led other investors to dump the stock the following Monday causing the stock to crash 17%. That day we were buyers, not sellers.

On March 18th, the Trust released its 8K announcing April's cash distribution. The filing revealed more details concerning the planned capes budget. Here's what it said:

> Blackbeard has advised the Trustee that the proposed budget for 2024 has not been finalized; however, it has provided the Trustee with a preliminary capital expenditure budget of approximately $301 million (gross) $106.11 million (net) and development plan reflecting that the 2024 budget will include amounts to be spent on 83 (gross) horizontal wells and 12 (gross) vertical wells along with 24 (gross) recompleted well prospects to be worked over and completed as well as infrastructure and plugging and abandonment costs. Blackbeard has advised the trustee that approximately 7% of that preliminary budget has been incurred related to January 2024 activity.

So the "net" amount of $106 million is the portion for which the Trust is responsible. This is a decrease of about $15 million from what it paid out in 2023. It appears that Blackbeard expects a decrease in capex of about 10%.

Blackbeard Operating, LLC

Year	Budget (1) Gross ($M)	Net ($M)
2023	325.12	121.92
2024	301.43	106.11

pbt-permian.com

Interestingly, the stock has recovered above were it was prior to its flash crash.

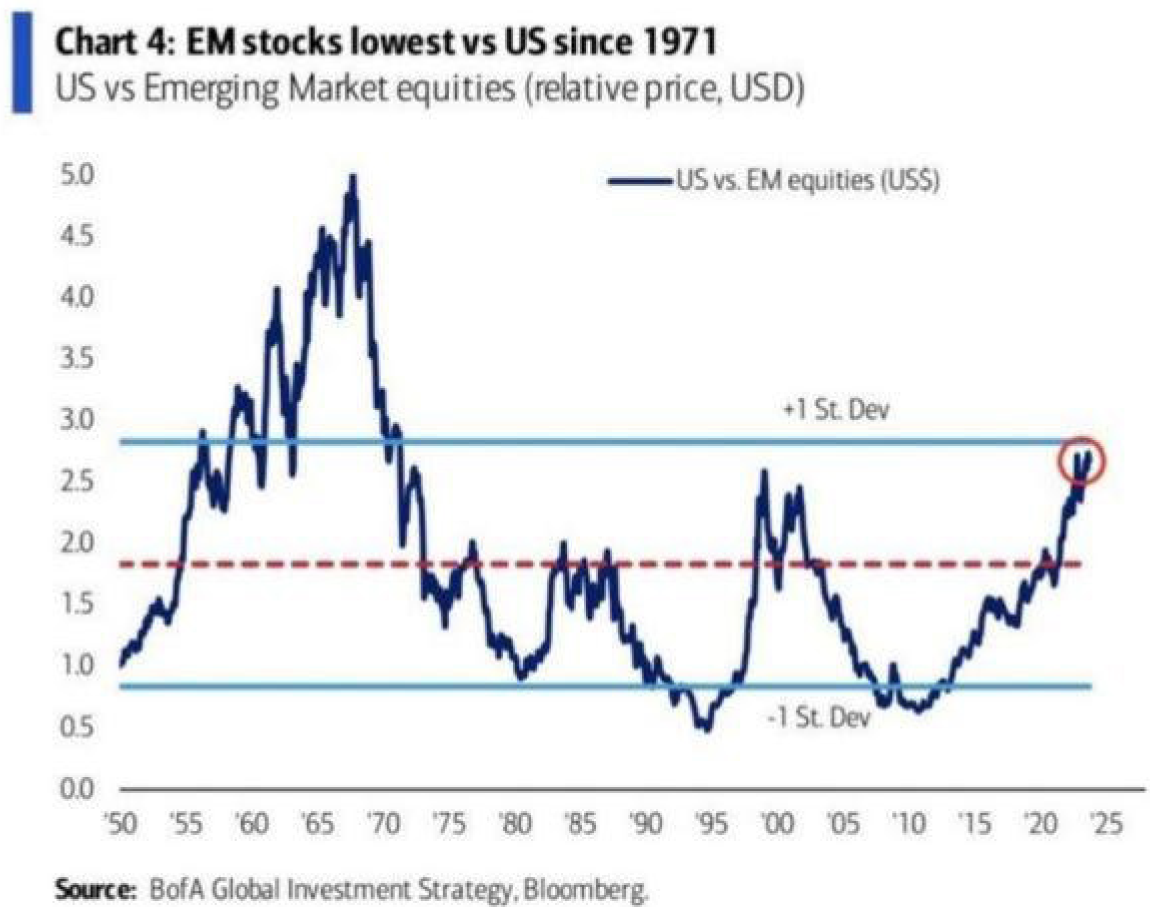
So, in conclusion, although it appears 2024 will not contain the massive decrease in capex we hoped for, the thesis remains intact. The catalyst has moved to the right but still well within sight of long-term investors such as ourselves.

Continue reading here.

Three emerging markets to consider now (from The Macro Compass)...

If you have been around for the last 10 years as a global macro investor you have experienced a situation where the US stock market was pretty much the only game in town.

Since 2010 US stock markets largely overperformed Emerging Markets:



In the investment world, recency bias is strong and people assume this has always been the case.

Yet taking a 70+ years historical perspective the evidence is much more mixed: for instance, the chart above shows the impressive EM outperformance in the 70s-80s or the early 2000s.

The next decade is likely to see a multi-polar world with geopolitical fragmentation, a bigger role for commodities, ongoing demographics and political shifts and increased US inflation and growth volatility.

All these factors point to same conclusion: owning Emerging Market exposure in a long-term macro portfolio is a sensible thing to do.

Yet Emerging markets were (and still are) seen only as an exotic addition to portfolios: a 2020 survey by Morningstar shows only 7% of global portfolio allocations are dedicated to Emerging Markets.

For reference, EMs represent about 15% of the MSCI All Country World Index (ACWI) and account for almost 40% of global GDP!

In other words: suffering from recency bias, global investors are largely under-allocated to EMs despite reasonable valuations and macro conditions in place for solid returns over the next decade.

Ok, but which Emerging Markets to invest in and why?

This article provides you with a framework to approach long-term EM investing, and it points to three of my favorite Emerging Markets to own for the next decade.

We assess the most palatable Emerging Markets to invest in through fundamentals and valuations: countries with the best fundamental score and cheapest valuations make it to the shortlist.

The focus is on EMs where sufficiently accurate data is available.

The scoring model on fundamentals is based on 4 main pillars:

- Economic growth (25% weight)
- Institutional credibility (25% weight)
- Leverage (25% weight)
- External vulnerabilities (25% weight)

Here is the summary table on fundamentals:

	Growth			Leverage		Institutional Credibility		External Vulnerabilities		
Country	Productivity % GDP	Working Age 10y FC - Now (%)	GDP per Capita PPP (USD)	Private Credit % GDP	Public Credit % GDP	Political Stability (%-ile)	Inflation Volatility	Current Account % GDP	NIIP % GDP	Reserves # Months
Argentina	-0.6%	2.0%	-0.7%	21.9%	88.0%	37.4	24.1%	-0.6%	17.5%	4.8
Brazil	-0.5%	-6.1%	-0.2%	86.4%	83.1%	38.0	2.8%	-0.2%	-40.7%	8.2
Chile	-0.5%	-0.9%	1.0%	138.7%	36.3%	68.6	3.1%	-7.0%	-17.2%	3.1
China	2.4%	-1.4%	5.8%	227.1%	79.4%	46.6	1.0%	0.5%	13.9%	11.3
Colombia	0.3%	0.5%	1.9%	59.5%	63.1%	43.0	3.2%	-5.7%	-52.1%	6.0
Czech	1.1%	-3.6%	2.1%	79.7%	44.5%	82.1	4.9%	-4.8%	-18.5%	6.8
Greece	1.0%	-1.1%	1.1%	97.1%	168.7%	60.7	3.4%	-8.8%	-145.9%	1.1
Hungary	1.1%	-0.1%	3.6%	96.1%	71.7%	66.2	6.6%	-6.6%	-48.7%	2.6
India	0.5%	-6.4%	4.5%	90.3%	83.2%	48.5	1.7%	-2.0%	-11.7%	7.0
Indonesia	0.5%	-7.7%	3.2%	38.7%	38.9%	50.0	1.8%	0.9%	-19.5%	5.2
Mexico	-0.5%	-4.8%	0.4%	39.1%	41.8%	32.9	1.7%	-1.3%	-44.6%	3.3
Malaysia	-0.4%	1.5%	2.7%	153.7%	61.8%	68.0	1.7%	3.4%	4.5%	4.3
Poland	1.3%	-2.3%	3.8%	64.9%	48.1%	65.6	5.2%	-0.1%	-33.5%	4.3
Thailand	0.9%	-3.9%	1.5%	177.8%	53.9%	50.7	2.1%	-10.4%	1.9%	7.1
Turkey	0.4%	-4.4%	3.9%	63.4%	31.1%	34.4	20.8%	-5.7%	-28.6%	3.7
South Africa	-0.8%	-7.8%	-0.3%	68.0%	72.7%	41.6	1.2%	-1.5%	20.0%	4.9

Structural growth is a function of productivity and labor force growth – both are used in our analysis. We also look at the last 10-year average realized GDP per capita as a concrete measure (not a forecast) of recent economic performance in each EM – remember take the Chinese number with a pinch of salt.

Eastern Europe (Poland, Hungary) and some Asian countries look good, while an ageing population and uneven allocation of resources in Brazil and South Africa don't look promising for growth.

Countries can grow organically but they can also make productive use of leverage to boost growth: for this reason private and public debt are both part of our assessment.

China is pretty much tapped out on leverage, and some other Asian countries (Thailand, Malaysia) also score poorly – recency bias again as the 1997 crisis seems to have been quickly forgotten?

On the other hand Indonesia, Mexico, Poland, and Turkey have leverage space to boost growth going forward.

Now a crucial point: investors hate volatility and unpredictability.

Organic or credit-driven growth matters, but institutional credibility is key for investors: a 2015 paper from Lehkonen shows how political instability is negatively correlated with long-term EM returns.

To assess institutional credibility we have blended four relevant World Bank indicators (government effectiveness, regulatory quality, rule of law, and political stability) into one index and ranked EM countries.

ELSEVIER

Journal of International Money and Finance

Volume 59, December 2015, Pages 77-99

Democracy, political risks and stock market performance

Heikki Lehkonen, Kari Heimonen

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Abstract

This study examines the impacts of democracy and political risk on stock market. Using annualized panel data for 49 emerging markets for 2000–2012 we find evidence that democracy and political risk do have impact on stock market returns and the relationship between democracy and political risk is parabolic, i.e., there is a threshold level of democracy after which political risk begins to decline. Also our results suggest that decreases in political risk lead to higher returns.

	Institutional Credibility	
Country	Political Stability (%-ile)	Inflation Volatility
Argentina	37.4	24.1%
Brazil	38.0	2.8%
Chile	68.6	3.1%
China	46.6	1.0%
Colombia	43.0	3.2%
Czech	82.1	4.9%
Greece	60.7	3.4%
Hungary	66.2	6.6%
India	48.5	1.7%
Indonesia	50.0	1.8%
Mexico	32.9	1.7%
Malaysia	68.0	1.7%
Poland	65.6	5.2%
Thailand	50.7	2.1%
Turkey	34.4	20.8%
South Africa	41.6	1.2%

Additionally, we reckon investors also assess policymakers' credibility by their ability to keep inflation in predictable ranges – countries with the highest inflation volatility tend to be penalized by investors.

We have therefore also ranked countries by their 10-year average standard deviation of CPI prints.

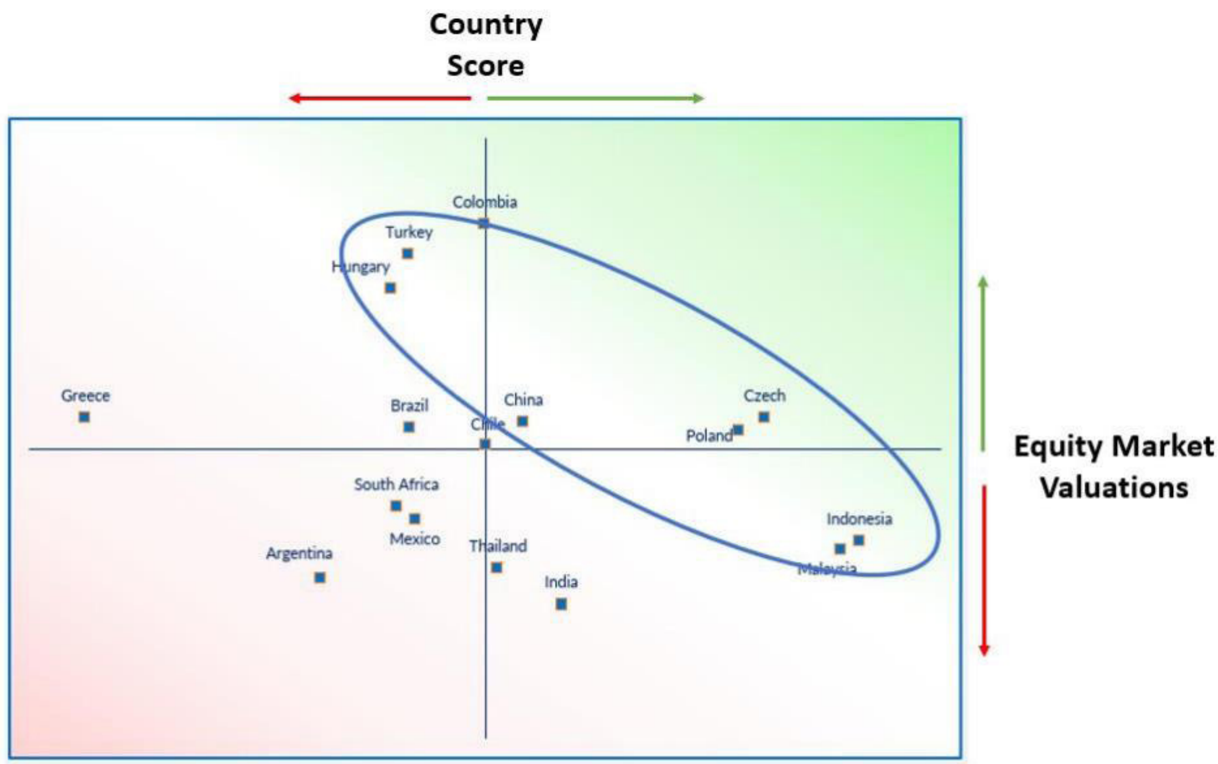
Combining these two metrics the worst performing countries are (unsurprisingly) Turkey and Argentina, while ex-China Asian countries rank well – particularly Malaysia and Indonesia given their predictable inflation ranges and good institutional frameworks.

Finally, it's important to recognize that most EM countries have external vulnerabilities: either they owe to the rest of the world through a negative current account or through a net negative investment position (NIIP).

Against this backdrop, EM countries will own a buffer of foreign exchange reserves (mostly USD and EUR) they can use to balance out their external vulnerabilities: we measure how many months of imports can be covered by the amount of net FX reserves each country has.

Turkey is notoriously vulnerable to external shocks, while China has amassed a gigantic amount of net FX reserves – actually even more than publicly disclosed.

It's now time to blend together the fundamentals and valuations so we can derive actionable conclusions.



The x-axis represents the country fundamental score: right is good, left less so.

The y-axis looks at equity market valuations: up means cheaper valuations, down = more expensive.

The top-right quadrant is the place where to look for bargains.

Remember: the EM complex is under-owned and it's overall a cheap and sensible exposure to have.

From a relative perspective, EMs look fairly priced against our fundamental models yet the blue circle highlights some interesting opportunities in this universe.

My final shortlist includes 3 countries: Poland, Malaysia, and Indonesia.

Indonesia is home to over 20% of global nickel reserves (essential in the EV-making process) and it has effectively banned the unprocessed export of nickel hence trying to force companies to set up plants locally and boost the country's long-term growth perspectives.

Even if this protectionist tactic could somehow backfire, it goes to show how Indonesia could attract more investments going forward.

Malaysia is also a net commodity exporter and the new government is keen on applying structural reforms too.

We are talking about a country with 10 years of positive current account balance and a credible policymaking mix which has now lured Tesla to engage in business relationships.

Finally my darling Emerging Market: Poland.

Over the last 5 years Poland has managed to beat most of its European peers in GDP per capita growth, and its potential long-term growth has also been boosted by a large influx of Ukrainian immigrants.

Poland is a productive economy with a long-standing and specialised manufacturing sector which will be increasingly targeted for "friend-shoring".

The country has also emerged as the 5th world largest producer of EV batteries.

The cherry on the cake is a newly elected coalition government led by Donald Tusk (former President of the European Council) which will replace the former European-critic government: a more friendly stance towards Europe will unlock further inflows of direct and portfolio investments towards Poland.

Turkey also is a high-potential investment trading at super cheap valuations and with strong demographics fundamentals, but policymakers credibility remains too low.

Concluding: investors suffering from recency bias can't see beyond US equity markets but macro conditions and cheap valuations favor a long-term allocation to EMs.

The entire space is interesting with Poland, Indonesia and Malaysiathe most compelling countries.

Continue reading here.

SOVEREIGN/GOVERNMENT BONDS AND CREDIT

Treasury markets are losing their "shock absorber" (*from The Wall Street Journal*)...

Participation is dwindling in a Federal Reserve program that has helped the U.S. government limit its borrowing costs, a development that many investors say presages higher interest rates and larger swings in the $26 trillion Treasury market.

The overnight reverse repurchase facility, known on Wall Street as reverse repo, enables large financial firms such as money-market funds to briefly swap extra cash for high-quality securities on the central bank's balance sheet and pocket some interest. The Fed program has been used heavily in recent years, at one point hitting $2.5 trillion of daily balances, but that number has shrunk steadily and recently fell below $500 billion.

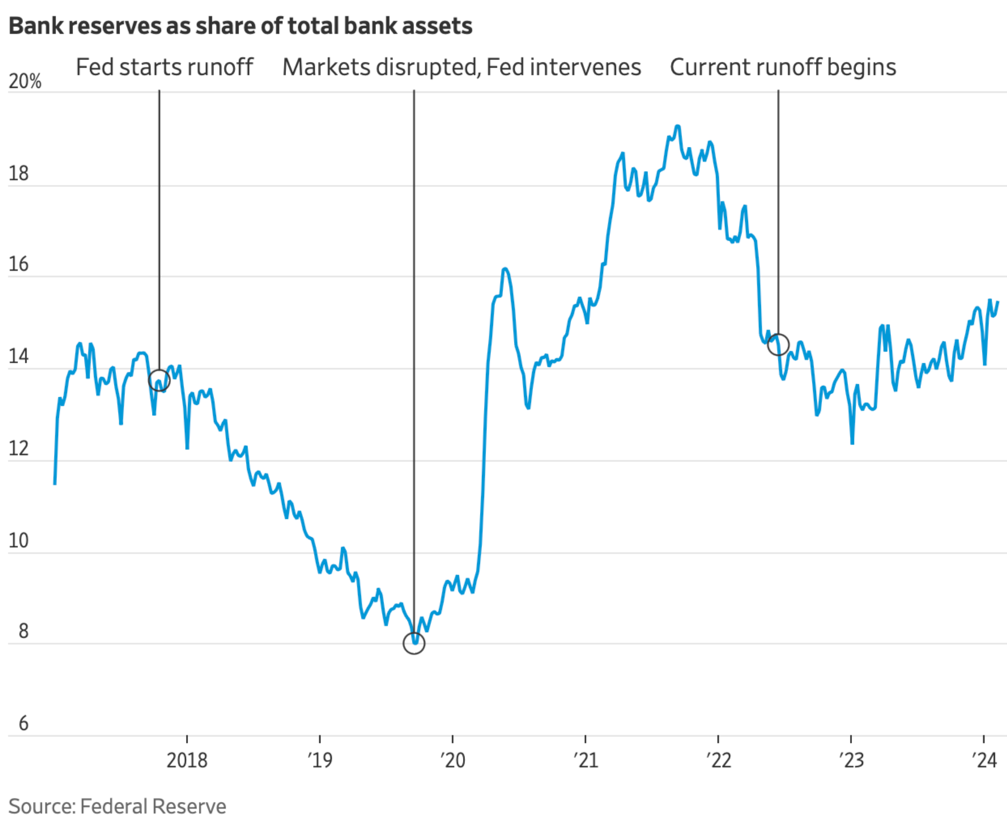
Overnight reverse repurchase transactions at Federal Reserve

Source: Federal Reserve

Many analysts and portfolio managers expect use of the program to continue to decline, which they say is likely to constrain the functioning of an important shock absorber in the market for U.S. Treasury securities. The government is facing higher interest costs as it attempts to fund a growing deficit, and observers say lower balances in the program could mean higher volatility and a fresh rise in interest rates in the market that underpins the global financial system.

"It is undoubtedly easier for the market to absorb bill supply if you have a large amount of cash in an overnight facility waiting to be deployed," said Michael de Pass, global head of rates trading at Citadel Securities.

Though obscure, reverse repo has long been at the center of the operation of the financial system and the U.S. economy. A committee that advises the Treasury suggested last fall that the heap of money-market fund cash sitting at the Fed could finance a flood of short-term bill issuance—an unusual shift that in recent months has enabled the government to keep long-term interest rates relatively low despite the quickening drumbeat of U.S. debt issuance.



Sales of Treasury bills, which mature in a year or less, surged during the pandemic and then again in 2023. There is now nearly $6 trillion of T-bills in the market, up from less than $2 trillion at the end of 2017.

That might seem like a technical development, but it is anything but for players in the global bond market. All this short-term debt will need to be refinanced at higher rates at the same time the Fed has been lifting benchmark interest rates. While selling bills allows the government to raise cash quickly, the bills soon come due, forcing difficult decisions on how to raise funds again.

Many bond investors say the Treasury Department will eventually have to come to grips with how it plans to pay its bondholders over the long haul, as interest payments become one of the largest expenses in the federal budget.

Continue reading here (subscription may be required).

Dwindling global savings is another tailwind for higher rates (from *Bloomberg*)...

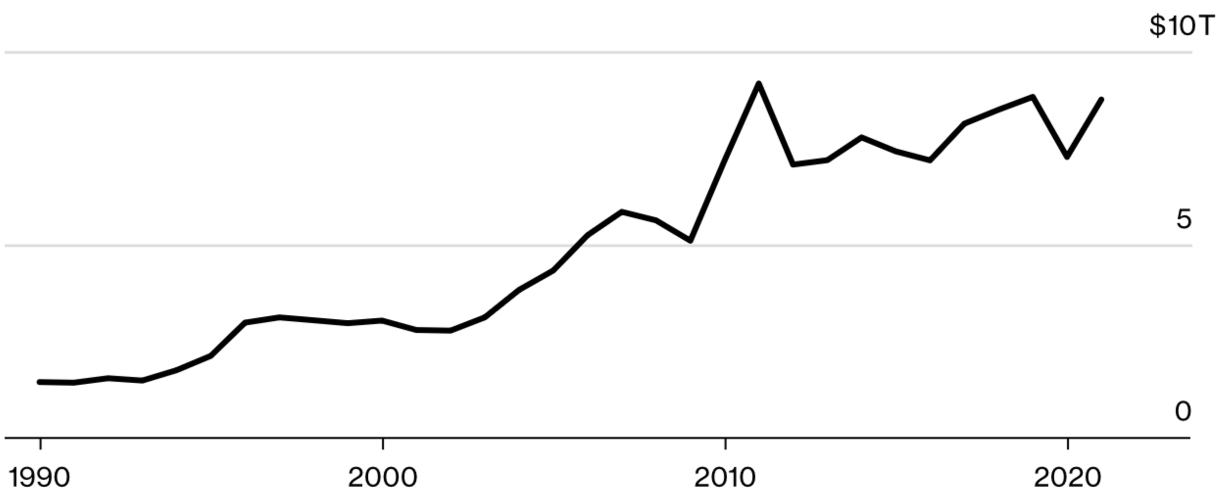
Ben Bernanke's global savings glut is drying up. Long-term interest rates worldwide may be heading higher as a result.

Aging populations, an embattled Chinese economy and an increasingly fragmented global one are among the factors threatening to turn the surplus of savings the former Federal Reserve chair identified almost 20 years ago into a shortfall.

The result, according to some economists: A reversal of the decades-long trend toward lower interest rates as borrowers from Washington on down are forced to pay up for a dwindling supply of excess cash.

Global Savings Flattens Out

Adjusted net savings in current dollars



Sources: World Bank, Hanover Provident LLC, Bloomberg
Note: Excluding particulate emission damage

In 2005, Bernanke argued the world was awash with savings because China and other emerging markets were deliberately building up foreign-currency reserves as insurance against future financial crises. Oil exporters also had more money to invest, thanks to a surge in energy prices.

The result: Downward pressure on long-term interest rates around the world, including in the US. (Bernanke declined to comment for this article).

Continue reading here (subscription may be required).

Bond giant PIMCO sees a much higher term premium for Treasury bonds (from PIMCO Perspectives)...

Common sense holds that investors should get paid more for taking more risk. This tends to be true in the bond market: The further you extend the maturity of bonds you hold, the more uncertainty you are underwriting and the more you should get compensated. Think about it simply. If you own a two-year bond, your principal will be returned after two years (absent default) and you can decide how to reinvest. The problem with a 30-year bond is that after two years, you still have to wait another 28.

Currently, the U.S. bond market doesn't follow this logic. The yield curve is inverted, with cash yielding more than longer-dated bonds. The odds are that this trend will not continue.

The most common way an inversion corrects is when the Federal Reserve cuts its short-term policy rate, which both markets and Fed officials expect to happen this year. However, there is the possibility of a much bigger shift ahead: that the curve will also correct as the term premium comes back.

Since the financial crisis, the term premium – a gauge of how much more it pays to hold longer-dated debt instead of repeatedly reinvesting in short maturities – has averaged only about 50 basis points (bps), even turning negative at times (see Figure 1). But what if we are heading back to the future, to a market resembling prior decades when higher term premiums prevailed?

Figure 1: The 10-year term premium has been in decline since the 1980s

Source: Federal Reserve Bank of New York, as of 20 February 2024. Term premium estimates are shown for 10-year U.S. Treasuries, according to the New York Fed's ACM (Adrian, Crump, and Moench) model.

The term premium has gradually declined since rising well above 400 basis points (bps) in the 1980s – when strategist Ed Yardeni coined the term "bond vigilantes" for investors who discipline government spending by demanding higher yields, and when the movie that inspired this column's title was released.

We are at a moment when the term premium could start to reverse the 40-year downtrend. January's hotter-than-expected consumer price index (CPI) reading, along with the Congressional Budget Office's latest estimates in February of the rising trajectory of U.S. debt (and the presumable increase in Treasury issuance needed to fund that debt), are recent signs of forces that could help rebuild the term premium.

If the term premium returned even to levels common in the late 1990s to early 2000s – around 200 bps – that would likely become the defining feature of financial markets during this era. It would not only affect bond prices but also prices of equities, real estate, and any other asset that is valued based on discounted future cash flows.

Spent stimulus

How far back to the future could we go? Consider that the U.S. hasn't run a balanced budget in more than two decades. This hasn't mattered because interest expenses held steady despite soaring debt. Thank falling interest rates (and term premium) for that – partly a function of the extended post-financial crisis period that PIMCO in 2009 dubbed "The New Normal."

Then COVID-19 changed everything. Massive pandemic-era fiscal spending helped U.S. households build excess savings, but it contributed to the spike in inflation that shocked the U.S. economy away from the zero lower bound of interest rates.

U.S. consumers have since shown greater resilience than those in other developed market (DM) countries, but that durability is fading everywhere. U.S. and euro area households are back to pre-pandemic levels of real wealth, and the U.K. is well below those levels, while inflation has cooled but remains sticky.

Borrowing costs are now higher, as are ongoing deficits. Therefore we know with near-certainty that interest expenses will keep rising.

Privilege and discipline

Markets call this type of profligacy "fiscal dominance" – and the conventional reaction for governments is to stop spending! Recall the U.K.'s fiscal issues in September 2022 – when the British pound lost almost 15% of its value following unfunded government spending proposals – and countless emerging market (EM) examples to boot.

The important point is that markets are a disciplining mechanism for governments, keeping them from straying too far down this spending path. Well, that is the case for nearly every DM and EM country – but it does not necessarily apply to the U.S. as the custodian of the world's reserve currency.

Indeed, the U.S. is leaning very hard on this exorbitant privilege. But privilege can tip into profligacy, slowly at first and then all of a sudden.

In the U.S., the last instance of this was in the 1980s, when the market – led by those bond vigilantes – demanded higher borrowing costs in what became a vicious spiral. It took a disciplined, coordinated approach by policymakers to short-circuit this spiral, first with tight monetary policy in the 1980s, followed by tighter fiscal policy throughout the 1990s.

And here is the crux of our concern: There is not the political will to do today what was ultimately required then. Sadly, more deficits are in the cards.

Investment implications

To be clear, we do not think we are traveling straight back to the 1980s – even if "Back to the Future" has recently reappeared as a Broadway musical. The Fed remains independent and will seek to keep a lid on inflation. But even a return to term premium levels of later decades would have material asset price implications.

In the third quarter of 2023, the term premium climbed as bond yields rose globally amid concerns about debts, deficits, higher-for-longer rates, and Fitch's downgrade of the U.S. credit rating. Shortly thereafter, we noted our overweight view toward duration – a gauge of interest rate risk – saying yields looked high relative to our near-term expectations. In the ensuing months, yields fell.

We could get a second bite at the apple. As we said in our January Cyclical Outlook, "Navigating the Descent," fiscal concerns will likely persist and could produce further episodes of long-end yields rising. We cited a curve-steepening bias in our portfolios, with overweight positions in the 5- to 10-year area globally and underweights in the 30-year area.

There is a very real possibility that the curve could kink following the first Fed rate cut, with shorter-term yields declining, intermediate rates not moving much, and longer-term yields rising as the term premium stages a comeback. In the meantime, investors do not have to take excessive duration risk to capture the lion's share of income and potential return.

Continue reading here.

Why soaring debt could derail the next U.S. administration ([from *Fortune* via Yahoo Finance](#))...

Among the illustrious nameplates adorning the offices of Ivy League business schools is one Joao Gomes. A Wharton Business School finance professor, Gomes is issuing a warning cry many of his peers so far have chosen to ignore: America's burgeoning public debt mountain.

Professor Gomes is what some might call up-and-coming: He was appointed senior vice dean of research in 2021, adding University of Pennsylvania's Marshall Blume Prize to his CV in 2018.

But the fresh-faced expert isn't afraid to step away from the pack if it means pushing presidential hopefuls for some answers. Gomes admits he's "probably" more worried than his colleagues about government debt, but refuses to stay silent on a broiling issue he believes will throw the global economy into disarray.

Gomes predicts America's $34 trillion debt burden may upset the world's financial markets as early as next year—should a president-elect announce a raft of expensive policies.

And remember the UK's mortgage meltdown following a disastrous premiership under Prime Minister Liz Truss? That's on the cards as well, as Gomes said rates could spiral to 7% "or higher" if the topic is swept under the rug by Washington.

The warning isn't chiming alone. Since the beginning of the year an increasing cacophony of alarm bells has been ringing out: JPMorgan Chase CEO Jamie Dimon says there will be a market "rebellion" over the issue while Bank of America CEO Brian Moynihan says it's time to stop "admiring" the problem and instead do something about it.

This fear is echoing outside of Wall Street, too. The Black Swan author Nassim Taleb says the economy is in a “death spiral,” while Fed Chairman Jerome Powell says it’s past time to have an “adult conversation” about fiscal responsibility.

But despite this, presidential candidates likely won't be getting on stage with promises of how they'll wrestle down the debt-to-GDP ratio to a more palatable figure (experts are currently predicting it will reach 190% by 2050.)

"I wish it was a big issue but I'm not sure it's in the interest of either party to make it a big issue," Gomes told Fortune. "As we discuss promises about: 'What we're going to do with tax and programs' it's going to be important to put it in the context of: 'Can we afford that?'"

"It's a really obvious moment in history for us to say: 'OK, what are our choices, what can we feasibly do, who has the better plan?' I suspect neither party is interested in that and it might all be pushed under the rug."

Indeed, while one party will have to make some unpopular decisions to tackle the issue, it's a problem created by both of them. Bank of America Research's Flow Show team, led by investment strategist Michael Hartnett, calculated in February that the deficits run up under the tenures of Presidents Trump and Biden are the greatest since Franklin D. Roosevelt in the 1930s.

Trump and Biden both dealt with a crisis-struck economy trying to navigate a global pandemic. FDR, of course, was firefighting the Great Depression and then oversaw the American entry into World War II.

Gomes believes that irrespective of who contributed to the mess, one party is going to have to shoulder the responsibility for unpicking it: "Toward the latter part of the decade we will have to deal with this."

"It could derail the next administration, frankly. If they come up with plans for large tax cuts or another big fiscal stimulus, the markets could rebel, interest rates could just spike right there and we would have a crisis in 2025. It could very well happen. I'm very confident by the end of the decade one way or another, we will be there."

Continue reading here.

Japan officially ends the era of negative interest rates (*from Bloomberg*)...

The Bank of Japan scrapped the world's last negative interest rate, ending the most aggressive monetary stimulus program in modern history, while also indicating that financial conditions will stay accommodative for now.

The bank's board voted 7-2 to set a new policy rate range of between 0% and 0.1%, shifting from a -0.1% short-term interest rate, according to a statement at the conclusion of its two-day meeting Tuesday. The BOJ also scrapped its complex yield curve control program while pledging to continue buying long-term government bonds as needed, and ended purchases of exchange-traded funds.

The lack of signaling on any future rate hikes weighed on the yen — which slid past the closely watched 150 mark versus the dollar — while benchmark government bond yields edged lower. The weaker currency supported Japanese equities, helping the Nikkei 225 Stock Average reclaim the key 40,000 level.

"We judged that achieving the goal of sustainable 2% inflation has come within view," Governor Kazuo Ueda said at a post-decision press conference. "The large-scale monetary easing policy served its purpose."

Continue reading here (subscription may be required).

The Fed is playing a dangerous game with the bond market (from Jim Bianco via X)...

Some thoughts about the bond market treading water since the Fed meeting while risk markets rally...

The Fed cannot randomly pick some day and cut rates. If they do and the market thinks it is not serious about inflation, it will sell bonds.

In 2022, the Fed hiked 75bps at four consecutive meetings. While they were doing this, inflation hit 9%. But the Fed was "on the case," and the 10-year yield peak was just 4.22%.

Contrast this with 2023. The Fed stopped hiking in late July 2023, when the 10-year yield was 3.95%. Even though inflation had declined from 9% to 4%, the market was "unsure" about the Fed's commitment to fighting inflation. Ninety days later, the 10-year yield jumped to over 5%, peaking in October 2023.

If the Fed is not serious about fighting inflation, when the market thinks it is a problem, it is not serious about owning the 10-year notes.

Fed dovishness only works if the market is convinced inflation is not a problem. Right now, it is unsure.

I long thought inflation was a problem (3% to 4% problem), and the economy is "no landing." So I think the market will resolve that inflation is at least an issue and that the Fed is not acting seriously about it, and it will start selling bonds.

How to choose between short-term Treasury bills and longer-term bonds (from Meb Faber via Cambria Investment Management)...

For the first time in a long time, fixed income investors have yield.

As of this writing in February 2024, short-term Treasuries yield over 5%, and long-term Treasuries around 4%.

Gone are the days of 0%, or even negative yielding bonds. (How weird was that?)

Retirees and fixed income investors are rejoicing, many acting like they just won the retirement lottery. For now, we'll ignore the bond declines of 10%, 20%, or even 50% to get here.

Thus, the most popular financial phrase of 2023: let's just "T-bills and Chill".

Now that investors have reawakened to fixed income as an asset class; it opens the doors to all types of other bonds. Outside of US government bonds there are corporate bonds, junk bonds, mortgage backed bonds, TIPS, foreign bonds, and even Bowie Bonds.

How is an investor supposed to go about choosing between all of the various choices available? Many don't, and they simply choose one of two allocations: either they invest purely in Treasuries and money market funds, or they buy a diversified bond strategy like the Bloomberg US Aggregate Bond Index, which is roughly 50% Treasuries, 25% corporate bonds and 25% mortgage-backed bonds.

Generally, as an investor moves away from what everyone considers to be the risk-free asset, T-bills, they accept some additional risk for the additional prospect of return. Two of the most well-known risks are the term premium and the credit premium.

- Term Premium – Instead of investing in short term T-bills, an investor could choose to invest in longer maturity Treasuries such as 30-year Treasury bonds. Additional compensation is expected for an uncertain future and additional volatility associated with the path of interest rates. Usually, if T-bills yield 5% then long-term bonds may yield 6% or 7%, in what would be described as an upward sloping yield curve.

- Credit Premium – Instead of investing in government bonds, and investor could allocate to corporate bonds issued by companies. These credits can vary in quality from AAA (not so many anymore) all the way down to high yielding junk bonds. Likewise, an investor would expect additional compensation for the default risk posed by bonds as they moved lower on the quality spectrum.

Anyways, there are lots of different types of bonds with different features, and generally, the riskier they are, the higher the spread these bonds will have to be to compensate the investor for the additional risk. Investing in bonds in countries like Turkey or Brazil could have yields north of 10% or even 20%. Japan and Switzerland? Still close to zero.

Pretty basic Investing 101 stuff here but stay with us for a second.

Just like the Buffett and Graham tales about the emotional Mr. Market showing up at your door to transact in stocks, the same is true for the bond world too.

For example, and these numbers are hypothetical for example's sake, but let's say T-bills yield 5%.

And let's say Mr. Market shows up and offers you junk bonds for 5%. Does that make any sense? Probably not. What about at 2%? No way!

Now what if he changes his mind and decides to come back tomorrow and offer the same bonds at 8%? Might that be attractive? Probably so. Now how about 15%? More likely!

When evaluating an investment, you won't know if it's a potentially good or bad investment without knowing the price.

Howard Marks said it best when he explained, "There's no such thing as a good idea or bad idea in the investment world. It's a good idea at a price, it's a bad idea at a price."

Value and price are tied at the hip.

Marks has also talked about this as well, saying, "Good investing is not a matter of buying good things but buying things well. And if you don't know the difference, then you shouldn't be doing much investing."

Bonds can be just as emotional as stocks. It has always been a bit puzzling to us to buy risky bonds when you are not receiving a margin of safety. If you can chill in T-bills at 5%, why take the risk to buy other bonds yielding less? It doesn't make much sense but plenty of index investors do just that.

Could we create a strategy to only invest in riskier bonds when the opportunity was favorable?

Devising a strategy here is straightforward. One could let the yield spread between risky bonds vs. T-bills dictate how you invest. When the spread is sufficiently wide, invest in risky bonds. When the spread is narrow, sit in T-bills.

How wide or narrow should the spread be to change from T-bills to risky bonds (or vice versa)? It could vary based on how opportunistic an investor wants to be vs. how much time they want to spend in the market, along with other considerations such as tracking error and volatility.

An investor's portfolio could sit in T-bills and rotate into the 10-Year Treasury Note when the yield was in the top half (50%) of history. You could also run the same strategy but only when the spread reaches the top 33% or 20%, etc.

We make sure we don't include a look forward bias into models. It's easy to invest in markets when you know how the future plays out! So, we're only going to use data up to the date examined in the below simulations.

Let's start with a simulation of investing in T-bills or the 10-Year Treasury Note. We'll use a tactical system that rotates into the 10-Year based on the yield spread being in the top 50% of history. It will move back into the safety of T-bills when the spread narrows to the bottom 50% of history.

Below is a table with risk and returns metrics for this simple system.

Compared to T-bills, the 10-Year had higher returns, higher volatility, and a typical Sharpe Ratio for a buy and hold investment during the period (most buy and hold assets tend to be around a 0.2 to 0.3 Sharpe Ratio over time.)

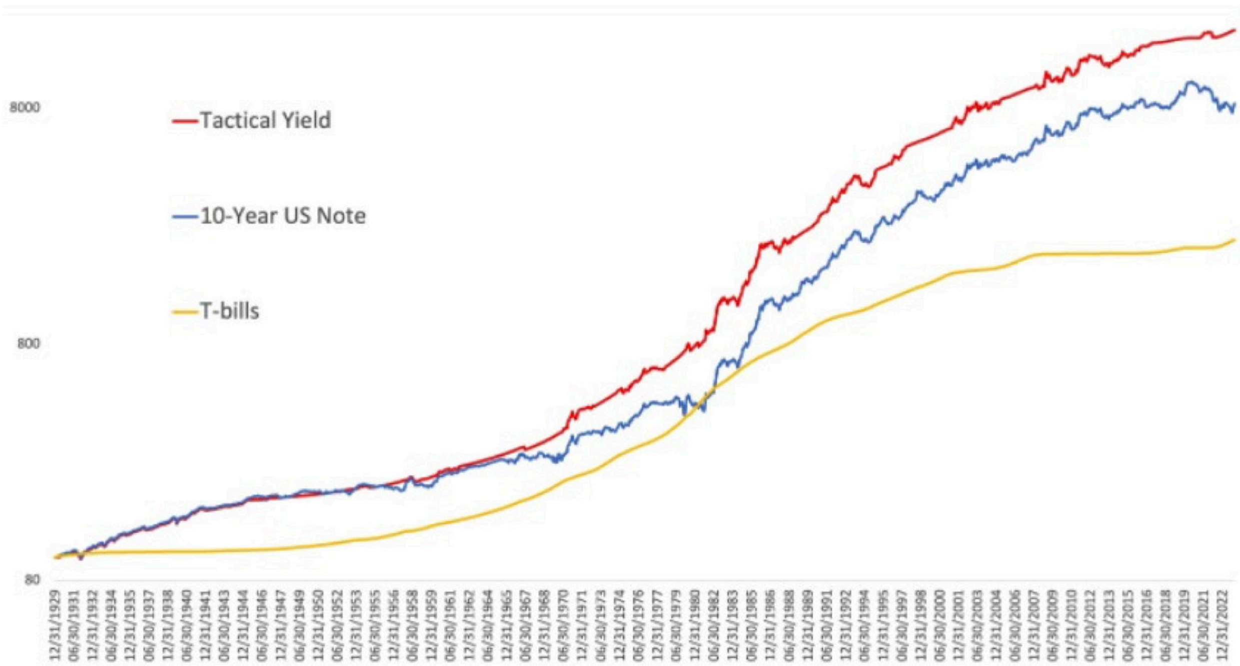
The tactical system both increased returns and lowered volatility and max drawdowns. We do not include transaction costs or slippage in the simulations but do note this tactical system has a low turnover.

Exhibit 1 - Risk and Return Statistics for T-bills, 10-Year Treasury Note, and Tactical System

1930-2022	T-bills	10-Year	Tactical Yield 10-Year or T-bill
Returns	3.35%	4.82%	5.62%
Volatility	0.89%	6.66%	5.16%
Sharpe Ratio	0.00	0.22	0.44
Max Drawdown		-26.19%	-10.66%

SOURCE: Global Financial Data

Exhibit 2 - Equity Curves for T-bills, 10-Year Treasury Note, and Tactical System



SOURCE: Global Financial Data

What if an investor decided to do the opposite - only invest in the 10-Year Treasury Note when the spread was in the bottom 50% of history and T-bills otherwise? This tactical system would have lower returns than T-bills – a decidedly poor idea. The lesson - when the spread isn't compensating the investor, it doesn't make much sense to take that risk.

We can look at a different fixed income sectors with different risk and return characteristics and run the same simulation.

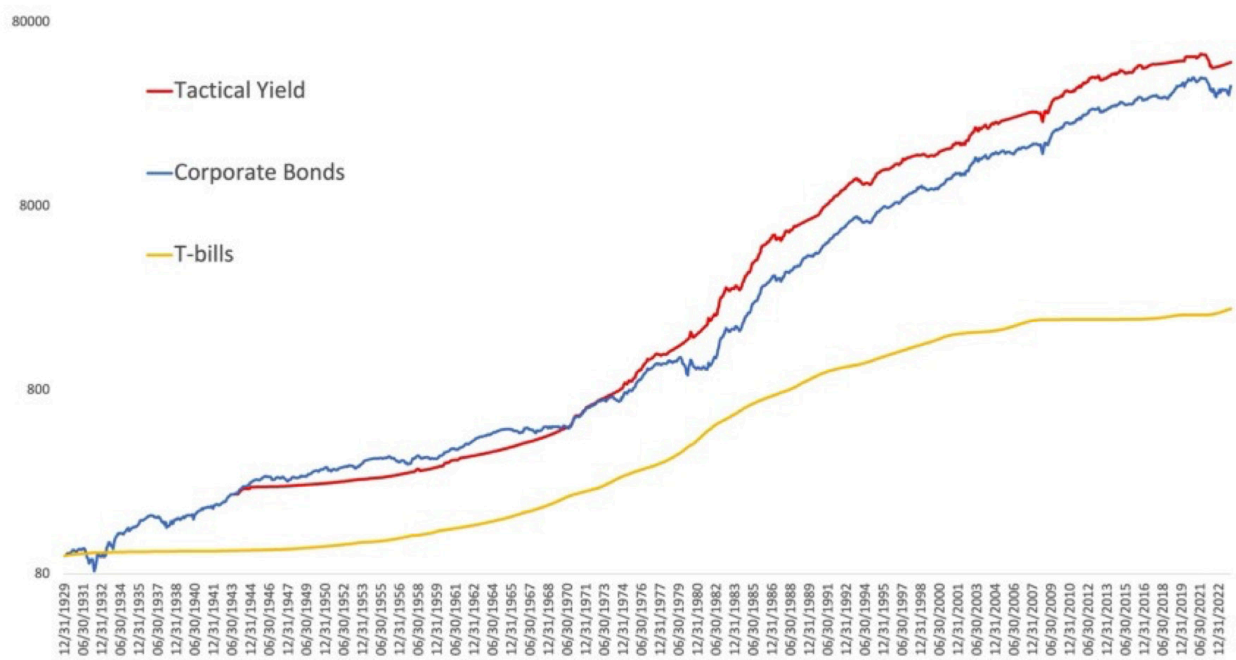
Below is a similar table for a strategy that considers investment grade corporate bonds. Again, you find a slightly higher return for the tactical system coupled with a little lower volatility and the same drawdowns. Unlike today, it was difficult to buy an index of corporate bonds 100 years ago, but the simulation below is meant to be instructive.

Exhibit 3 - Risk and Return Statistics for T-bills, Corporate Bonds, and Tactical System

1930-2022	T-bills	Corporate Bonds	Tactical Yield Corporates or T-bill
Returns	3.35%	6.46%	6.79%
Volatility	0.89%	6.32%	5.34%
Sharpe Ratio	0.00	0.49	0.65
Max Drawdown		-24.90%	-24.90%

SOURCE: Global Financial Data

Exhibit 4 - Equity Curves for T-bills, Corporate Bonds, and Tactical System



SOURCE: Global Financial Data

And what if you combined the two? Invest in T-bills until corporate bond spreads or 10-Year Treasury spreads enter the top 50% of their respective historical ranges.

Exhibit 5 – Risk and Return Statistics for T-bills, 10-Year Treasury Note and Corporate Bonds, and Tactical System

1930-2022	T-bills	Buy and Hold 10-Year & Corporates	Tactical Yield Corporates / 10-Year / T-bill
Returns	3.35%	5.68%	6.24%
Volatility	0.89%	5.83%	4.61%
Sharpe Ratio	0.00	0.40	0.63
Max Drawdown		-22.62%	-13.96%

SOURCE: Global Financial Data

There are numerous ways you can run these types of simulations:

- An investor could run this simulation across the entire series of Treasuries, including longer dated bonds such as the 30-Year, or even other types of US Government bonds such as TIPS, or agencies.
- An investor could run this simulation across the various levels of credits, from highly rated AAA all the way out to junk bonds.
- An investor could run this simulation across other more esoteric bonds with shorter histories, including emerging market sovereigns or corporate bonds, mortgage backed securities, and even high income equity products such as REITs.

In our simulations, we have found consistent results across all the assets above, albeit across varied and shorter time horizons.

What if you expanded the opportunity set to include more potential investments? In addition to the 10-Year Treasury Note and corporate bonds, below we layer in the 30-Year Treasury Bond, REITs, junk bonds, mortgage backed bonds, emerging market debt, and 10-Year TIPS as index data becomes available.

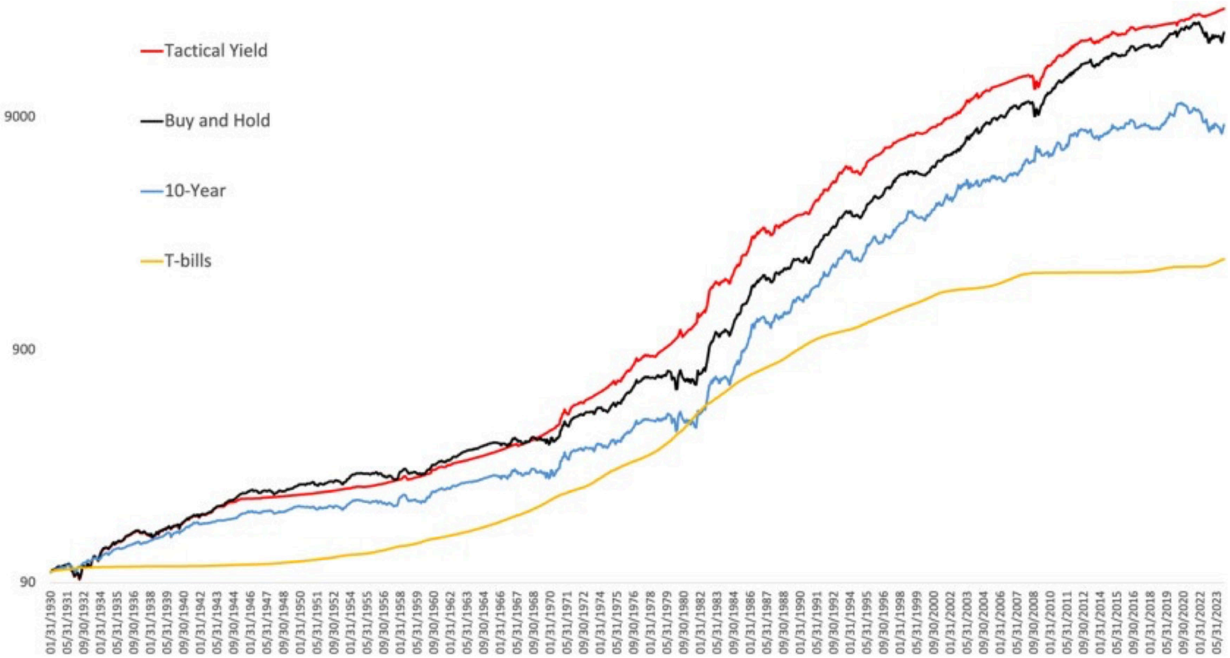
We equal weight the positions as they are introduced into the portfolio. Initially this would potentially be 50% each in the 10-Year Treasury and corporate bonds. Once we include all eight assets above, each would have a position size of roughly 12%.

Exhibit 6 – Risk and Return Statistics for T-bills, 10-Year Treasury Note, Diversified Portfolio and Tactical System

1930-2022	T-bills	10-Year	Everything Buy and Hold	Tactical Yield
Returns	3.35%	4.82%	5.84%	6.11%
Volatility	0.89%	6.66%	5.77%	4.38%
Sharpe Ratio	0.00	0.22	0.43	0.63
Max Drawdown		-26.19%	-18.29%	-13.96%

SOURCE: Global Financial Data

Exhibit 7 - Equity Curves for T-bills, 10-Year Treasury Note, Diversified Portfolio and Tactical System



SOURCE: Global Financial Data

These results largely agree with academic research on the subject. The simply titled 2016 paper "Carry" by Koijen et al is a good overview on the topic.

As investors rejoice at the opportunity to earn yield once again, many may opt to just hang out in T-bills and chill. For many this is a safe and simple choice.

Many investors are tempted to seek even higher yields, and the menu of choices is limitless.

Those that move away from T-bills tend to add other bond categories on a buy and hold basis, and with that, introduce a variety of risks to their portfolios, including the potential for increased volatility and nominal drawdowns.

Unfortunately, and despite the current drawdown many bond investors are experiencing, some bonds categories still have even lower yields than T-bills. The traditional yield curve is still inverted, and many, if not all of the assets examined in the paper do not have a yield spread over T-bills that would place them in the favorable top half of history. If those bonds don't compensate you with a reasonable margin of safety, is that a wise decision to allocate?

We don't think it is, but we do think there's a better approach. With this paper, we attempted to illustrate the effectiveness of implementing a tactical approach to fixed income investing based on the evaluation of yield spreads across a variety of fixed income sectors. We think the power lies in its ability to guide investors over time based on objective rules that have historically shown the ability to earn potentially higher returns than a simple buy-and-hold approach, but with lower volatility and drawdowns.

This simulation helps to answer the question, "When does it make sense to take on extra risk, and when might it not be prudent?"

Right now this system is signaling: "T-bills and chill." But at some point in the future, it will signal a potential green light to take on the additional exposures once again.

With that said, we think this dynamic approach to fixed income can serve as a core approach for investors looking for a strategy with an emphasis on the safety of Treasury bills, but systematically takes risk when opportunities and sufficient margins of safety present themselves.

Perhaps we will need to expand the phrase in the coming years to: "Let's just T-bills and chill.... most of the time."

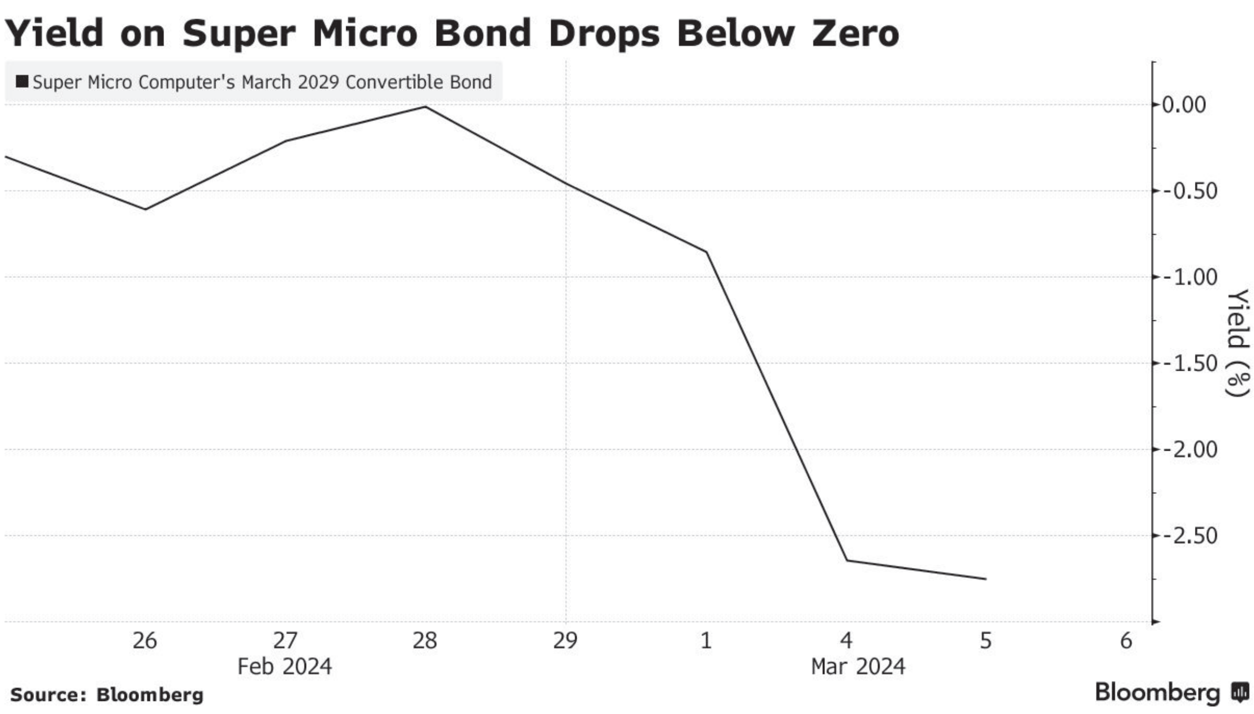
CORPORATE BONDS AND CREDIT

Negative yields are back with investors chasing AI exposure (*from Bloomberg*)...

The hype around artificial intelligence has revived a market oddity that many presumed dead with the global rise in interest rates: investors are once again paying for the privilege of owning certain bonds.

Yields on debt issued by a raft of firms in the semiconductor and microchip sectors, including Hynix and Camtek Ltd, have dropped below zero in recent weeks as money managers clamor to gain exposure to a rally that's driven the S&P 500 to a record high this year. All of the bonds in question are convertible, meaning the holder can swap them for equity on maturity at a specified conversion price.

"It's a hot sector for sure and there is a lot of demand for companies that are direct beneficiaries," said Makeem Asif, a money manager at Jupiter Asset Management, who bought convertible bonds of chipmaker Super Micro Computer Inc., which were sold with zero coupon last month. The notes have rallied since they were issued and now have a yield of around -2.75%, according to CBBT pricing compiled by Bloomberg.



For investors betting that the rally in AI stocks has further to run, buying a bond that is likely to turn into equity is a no-brainer. But recent history shows the strategy comes with risks, particularly if money managers don't have the safety net of a coupon to fall back on.

Continue reading here (subscription may be required).

Legendary distressed-debt investor Howard Marks says many companies are still "swimming naked" with debt maturities yet to arrive ([from *Bloomberg*](#))...

The test for credit arrives in 2025

Warren Buffett has a famous saying that Howard Marks riffed on this way: "When the tide goes out, we find out who's been swimming naked."

Plenty of companies are likely looking around for some clothes after an abrupt end to a decade-plus of 0% interest rates and easy-money policies globally. Analysts spent years talking about corporations that had struggling business models, kept alive by cheap leverage. So why haven't we seen them in their birthday suits yet, we asked Oaktree Capital Management's Marks on Surveillance.

His answer: "The tide hasn't gone out."

On a morning full of talk from monetary and fiscal policymakers, including the European Central Bank's Christine Lagarde, it was refreshing to get a reset on the current market cycle with Marks, who co-founded the world's biggest distressed-debt investment firm. Marks sees a benchmark rate of 3% to 3.5% at the Federal Reserve, returning to something he called a bit more normal than the free-money era.

"Today's rates are not high historically, but they're certainly higher than we had from '09 through 2021," Marks said. This "means the return on credit investing, fixed-income investing, bond investing, loan investing will be higher than those in that period, which were really paltry."

The question is, when do we see the consequences of those higher rates? This has been an increasingly pertinent question at a time when a lot of good news has been priced in for both stocks and bonds.

Invesco's Kristina Campmany pointed out markets' resilience even as the Fed's rate cuts keep getting pushed back.

"There's a lot of turmoil, and it's been this brutal repricing of Fed policy from 125 to 140 basis points of easing to this now swing of people talking about not easing at all," she said. "Yet risk assets have traded exceptionally well and have lived in their own world."

Marks noted that for credit markets, next year may be the true test. Many corporations have debt maturities coming due in earnest in 2025. If rates stay close to where they are now, some of these firms will inevitably struggle, said Marks.

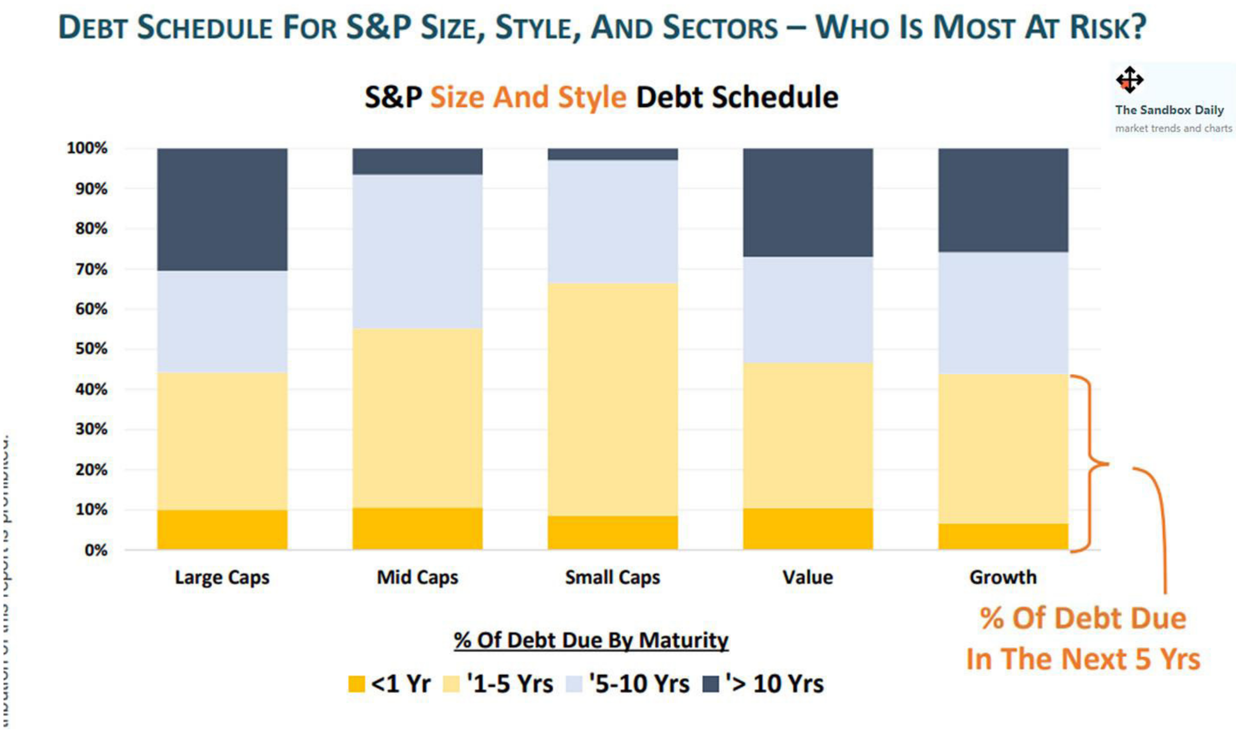
For now, it's hard for many to see why the Fed funds rates would ever return to zero again, let alone drop at all this year from the current range of 5.25% to 5.5%.

Continue reading here (subscription may be required).

Here is the corporate-debt schedule for the S&P 1500 (from The Sandbox Daily)...

Market rates remain at elevated levels amidst uncertainty on the timing and pace of the upcoming Fed easing cycle. At this point, the level of interest rates is the common thread amongst top investor concerns.

The chart below identifies the debt maturity wall for companies across the S&P 1500 – a composite of the S&P 500 (large-caps), S&P 400 (mid-caps), and S&P 600 (small-caps) – which covers 90% of the market capitalization of U.S. stocks, so it represents a broad swath of the domestic market's exposure to the path of interest rates ahead.



Nearly a third of all debt is coming due in every sector within the next five years.

S&P 1500 Sector Debt Schedule

The Sandbox Daily
market trends and charts

	Debt ($ Mil)	<1	1-5	5-10	10-15	15-20	20+
Comm Svcs	724,822	3%	29%	27%	7%	8%	27%
Disrectionary	713,327	6%	44%	32%	3%	3%	11%
Staples	497,317	6%	35%	30%	5%	8%	17%
Energy	350,909	4%	36%	34%	5%	5%	16%
Financials	2,611,006	20%	39%	23%	7%	3%	9%
Health Care	934,728	7%	30%	25%	6%	8%	24%
Industrials	757,616	6%	39%	27%	5%	6%	18%
Technology	705,579	6%	33%	26%	6%	6%	22%
Materials	289,475	6%	42%	29%	3%	6%	14%
Real Estate	389,443	5%	42%	43%	2%	1%	8%
Utilities	663,962	6%	27%	24%	6%	8%	29%

The longer rates remain elevated, the bigger the impact that the debt refinance wall will have on earnings and growth.

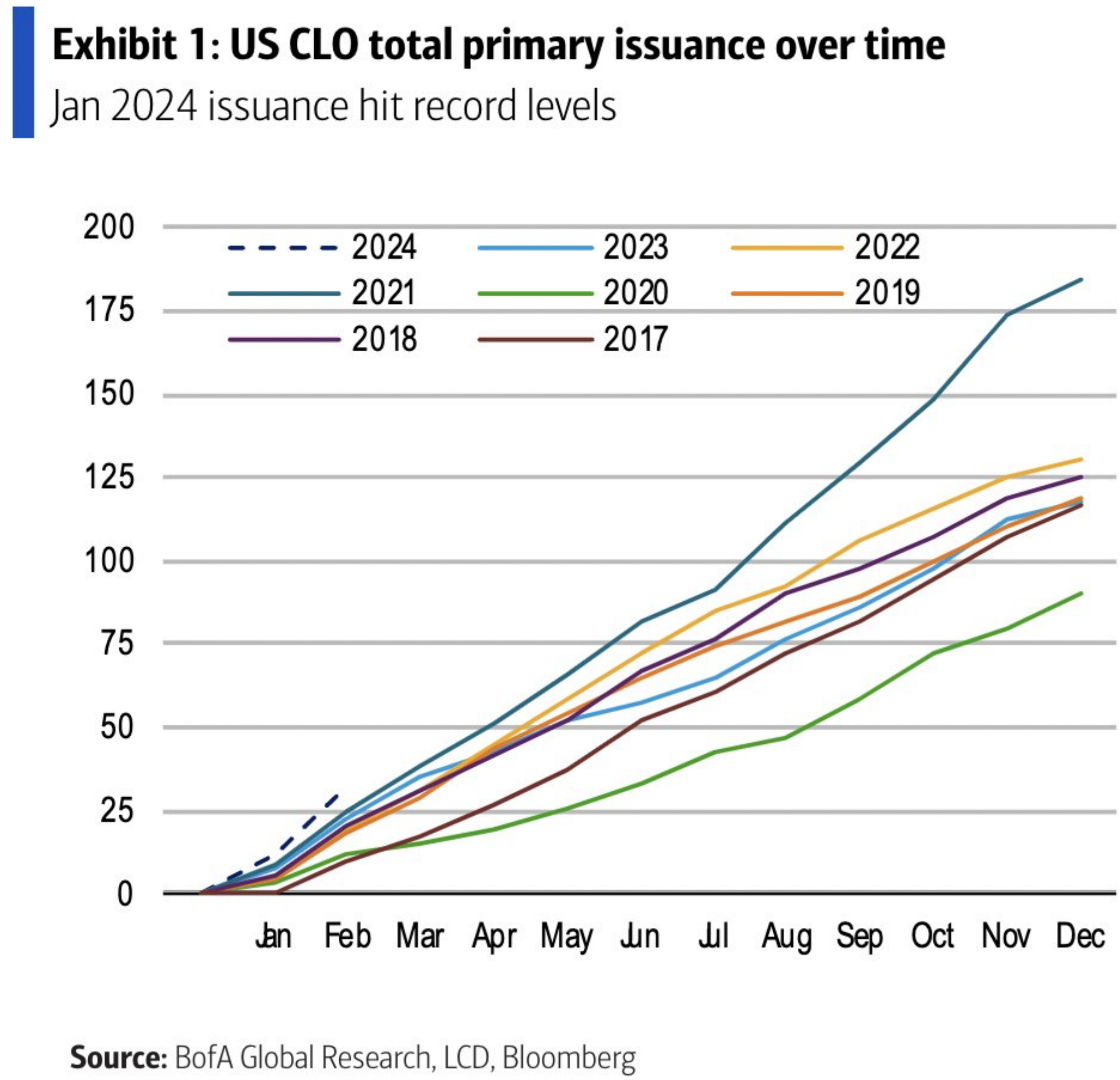
Continue reading here.

Issuance of U.S. collateralized loan obligations ("CLOs") is on pace to hit an all-time record this year (from Jack Farley via X)...

Issuance of U.S. CLOs (collateralized loan obligations) is at a record - above 2021 levels (!)

$28 Billion Year-to-date of broadly syndicated loan (BSL) primary issuance, with $7 Billion of Private Credit issuance (!!)

These private credit CLOs are getting very large.



Corporate defaults are happening at the fastest pace since the Great Financial Crisis (*from The Financial Times*)...

More companies have defaulted on their debt in 2024 than in any start to the year since the global financial crisis as inflationary pressures and high interest rates continue to weigh on the world's riskiest borrowers, according to S&P Global Ratings.

This year's global tally of corporate defaults stands at 29, the highest year-to-date count since the 36 recorded during the same period in 2009, according to the rating agency.

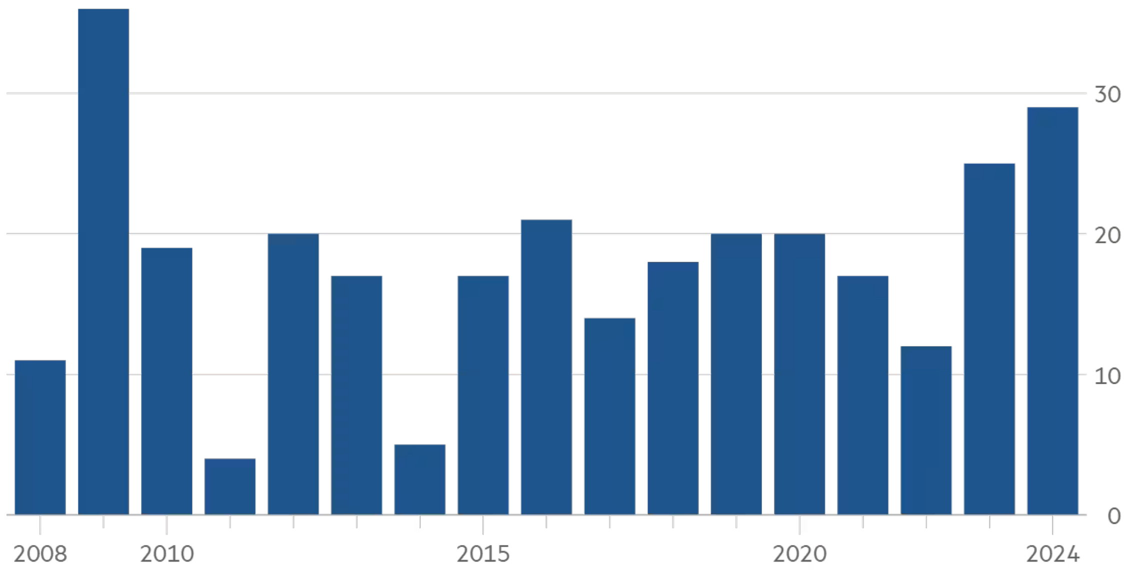
Subdued consumer demand, rising wages and high interest rates, which hurt more indebted companies, had all contributed to the increase in the number of companies struggling to repay their debt, S&P said.

"What's going on is exactly what's been going on since the [Federal Reserve] began to raise interest rates" in March 2022, said Torsten Slok, chief economist at investment group Apollo. "Default rates are rising…because higher interest rates continue to bite harder and harder on highly levered companies."

Companies to have defaulted in February included US ferry and cruise operator Hornblower, US software group GoTo and UK cinema group Vue Entertainment International.

Global corporate default tally at highest since 2009

Year-to-date default count



Source: S&P Global Ratings Credit Research & Insights
© FT

Although the majority of defaults were in the US, Europe's eight since January is twice as many as in any year since 2008, and more than double the number seen in the same period of 2023.

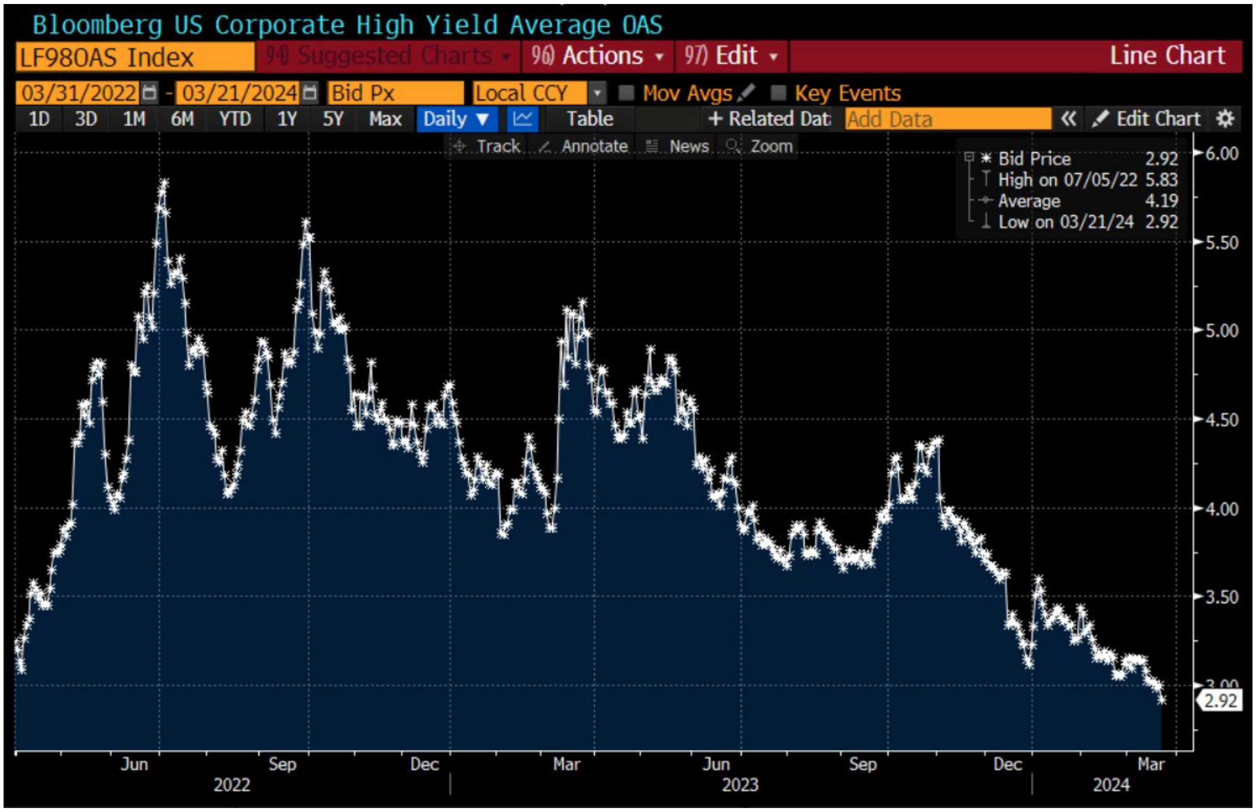
Three US healthcare companies — Radiology Partners, Pluto Acquisition and Cano Health — defaulted last month, in part due to the implementation of the No Surprises Act, which came into force in 2022 and caps the amount that providers can charge for treatments that patients did not choose and for which they are not insured, S&P said.

Fourteen, or roughly half, of the companies that have defaulted across the globe this year were classified by S&P as "distressed exchanges" — agreements that typically involve creditors receiving assets worth less than the face value of their debt, in a scenario that can help borrowers and private equity sponsors avoid expensive bankruptcy proceedings.

Continue reading here (subscription may be required).

A record amount of money has flooded into U.S. corporate bond markets this year (from Lisa Abramowicz via X)...

Inflows into credit funds have reached $22.8bn so far in 2024, the first positive start to a year since 2019.



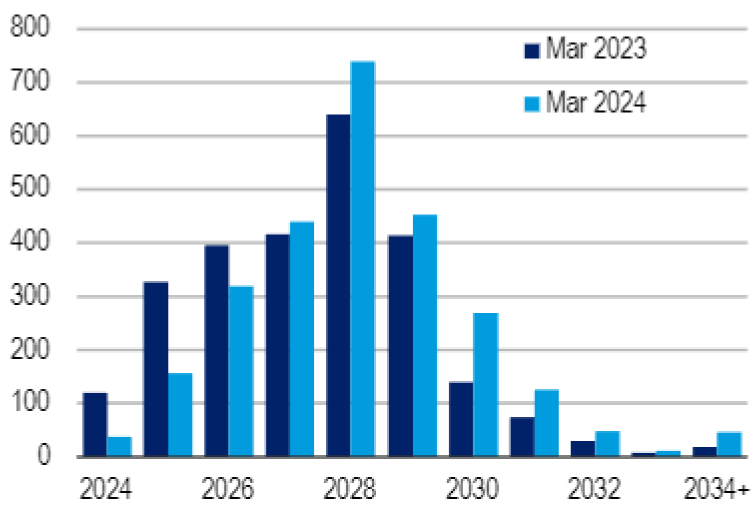
A significant percentage of the high-yield maturity wall has been extended (from Tracy Alloway via X)...

Junk bond and leveraged loan issuers have cut their 2024-2026 maturity wall by 40% from a year ago, according to BOA estimates.

"This episode represents one of the most aggressive instances of maturity extension in the history of leveraged finance."

Exhibit 1: HY/BSL debt maturities by year

Latest vs one year ago



Source: BofA Global Research

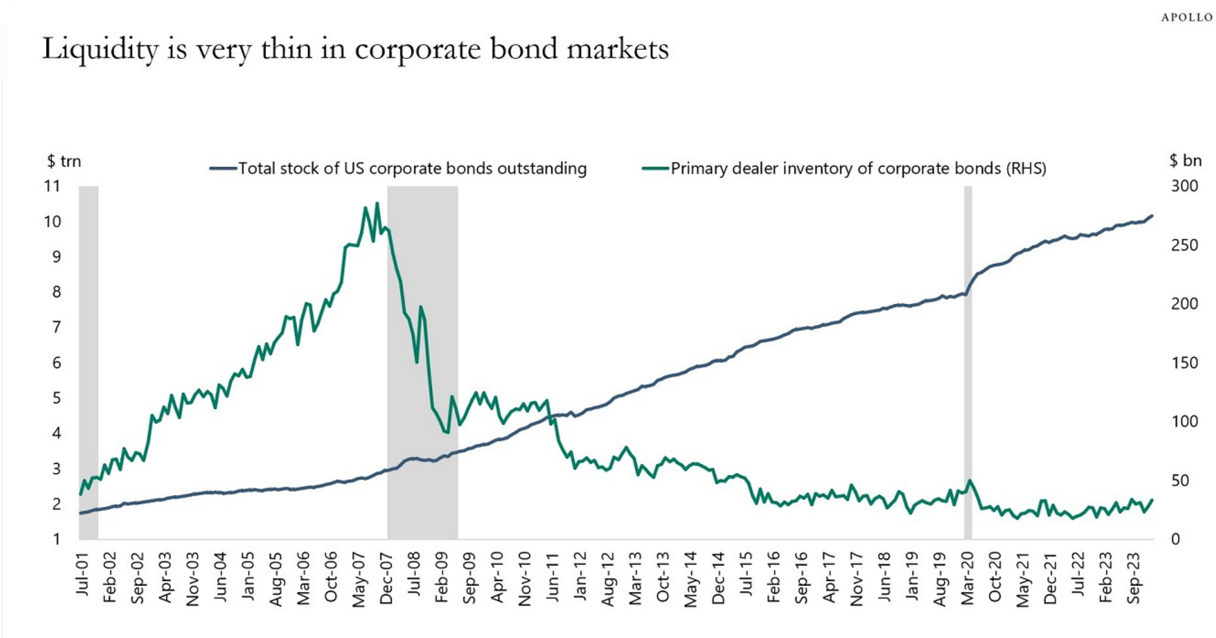
BofA GLOBAL RESEARCH

Liquidity is very thin in corporate bond markets (from The Daily Spark)...

The total amount of corporate bonds outstanding is now over $10 trillion, and the primary dealer inventory of corporate bonds is $33 billion, see chart below.

This is not a liquid market. When credit markets are quiet and calm, it gives the impression that liquidity is fine, but if many holders of credit suddenly want to sell, liquidity will disappear. Even in quiet markets, finding a bond can take several days.

With more evergreen funds with monthly and quarterly liquidity in private credit, the reality is that the liquidity situation in public and private credit is converging, and in some cases, if you want to buy or sell a big amount of public credit without moving the price, private credit may be more liquid.



CONSUMER CREDIT

Americans are paying nearly as much interest on credit-card and other debt as they are on their mortgages (from Business Insider)...

According to the US Bureau of Economic Analysis, non-mortgage interest payments soared to a record $573.4 billion annually in January, narrowly trailing the $578.3 billion spent on mortgage interest in the fourth quarter of last year.

Personal interest payments from 1960 to 2024

Source: U.S. Bureau of Economic Analysis

The almost equal amount US borrowers are shelling amount to service mortgage and non-mortgage debt is a phenomenon that hasn't been reflected in any of the data going as far back as the 1970s.

The shift has taken place as Americans secured bargain home loans in the 15 years following the 2008 crisis, particularly during the pandemic when interest rates fell to historic lows and mortgages could be locked in at 3% for 30 years.

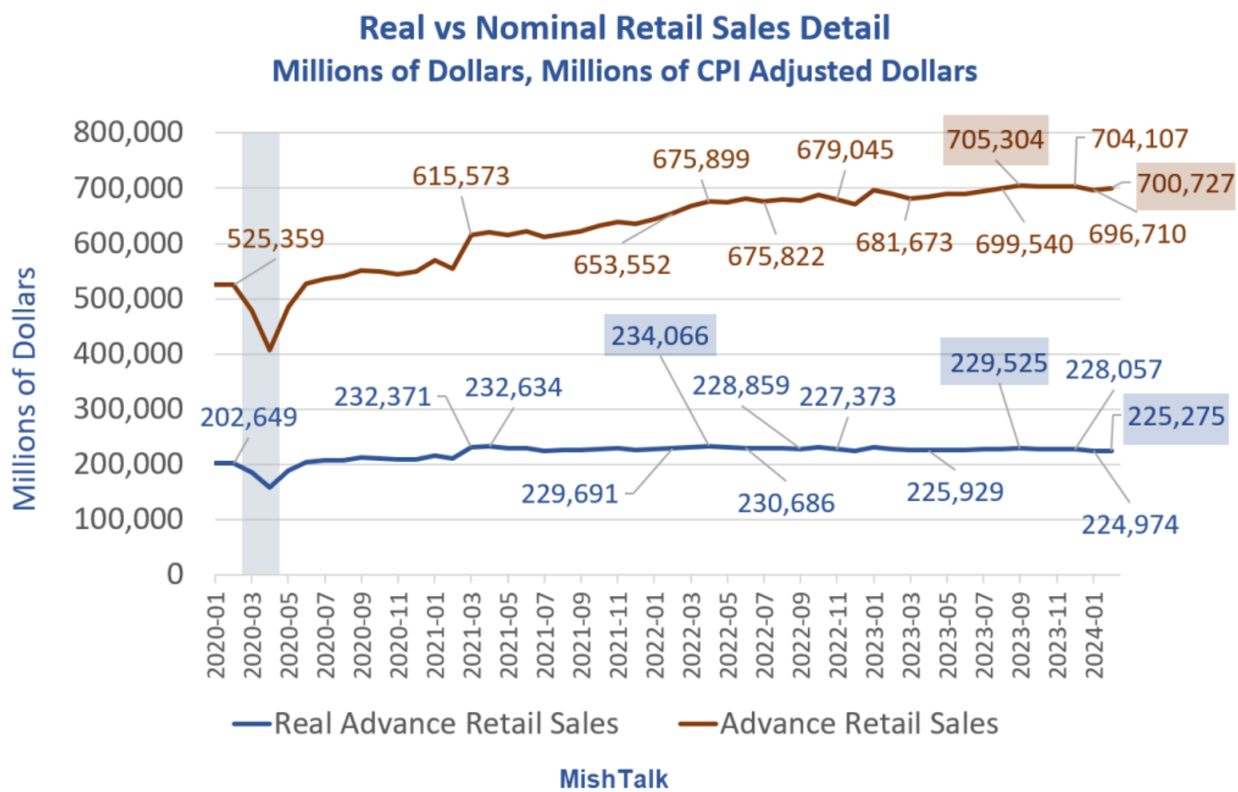
Yet other types of consumer credit, the growth of which has outpaced the growth of mortgage debt since the 2008 recession, has become much more expensive since 2022.

Fitch Ratings notes that the effective rate on US mortgage debt was 3.7% in the third quarter of last year. Meanwhile, interest on credit cards was 21.19% during the same period, raising concerns that Americans could soon run into trouble staying current on all of their debt, especially as millions of borrowers resumed paying student loans in the fourth quarter of last year.

Continue reading here.

Is the U.S. consumer finally tapping out? (from MishTalk)...

The answer to the question appears to be yes, starting October of 2023. Six pictures of real vs nominal advance retail sales tell the story.



Real and nominal advance retail sales. Real sales are inflation-adjusted by the CPI. Every month the commerce department reports Advance Retail Sales.

> Advance estimates of U.S. retail and food services sales for February 2024, *adjusted for seasonal variation and holiday and trading-day differences, but not for price changes*, were $700.7 billion, up 0.6 percent from the previous month, and up 1.5 percent above February 2023. Total sales for the December 2023 through February 2024 period were up 2.1 percent from the same period a year ago. The December 2023 to January 2024 percent change was revised from down 0.8 percent to down 1.1 percent.

I highlighted the key line “*adjusted for seasonal variation and holiday and trading-day differences, but not for price changes*.”

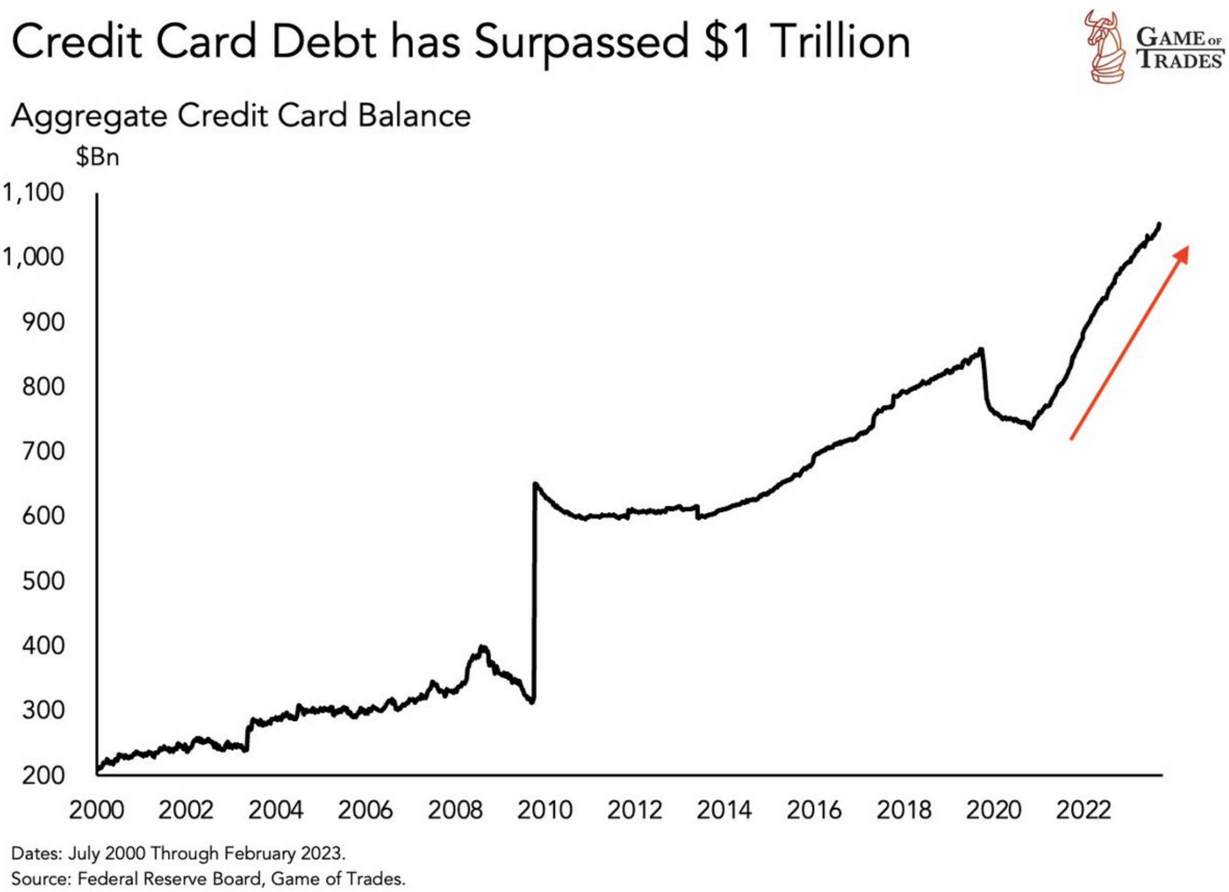
GDP depends on real (inflation adjusted) sales, not nominal sales. Also note the negative revision. “The December 2023 to January 2024 percent change was revised from down 0.8 percent to down 1.1 percent.”

Continue reading here.

Against all odds, credit-card debt continues to rise rapidly (from Game of Trades via X)...

People are spending more than they can afford at this point.

This can get very ugly.



Americans' credit-card fees have surged 50% since Biden became president (*from The Financial Times*)...

US consumers paid almost 50 per cent more in credit card expenses last year than in 2020, the year before President Joe Biden took office, putting pressure on family budgets and firing up an election issue about what Republicans say is a cost of living crisis.

Credit card interest and fees increased by $51bn in that time to $157bn, according to data provided by US banks to the Federal Deposit Insurance Corporation.

Delinquencies on credit card loans are also running at their highest level in almost 13 years, according to data from Moody's Analytics, even as banks have reported record profits from credit card lending.

The rise in credit card costs has come as the US Federal Reserve raised interest rates to a 23-year high but lenders have pushed consumer borrowing rates higher still. The central bank, which meets on Wednesday, is not expected to begin cutting rates until this summer.

Republicans have seized on credit card debt as an example of how Biden's economic policies have triggered what they say is a cost of living crisis for low-income Americans, while his administration has sought to show it is clamping down on credit card companies charging excessive fees.

The debt concerns come amid polling showing Americans remain gloomy about the Biden economy despite a surging stock market, healthy gross domestic product growth and low unemployment, posing a big threat to his re-election bid this year.

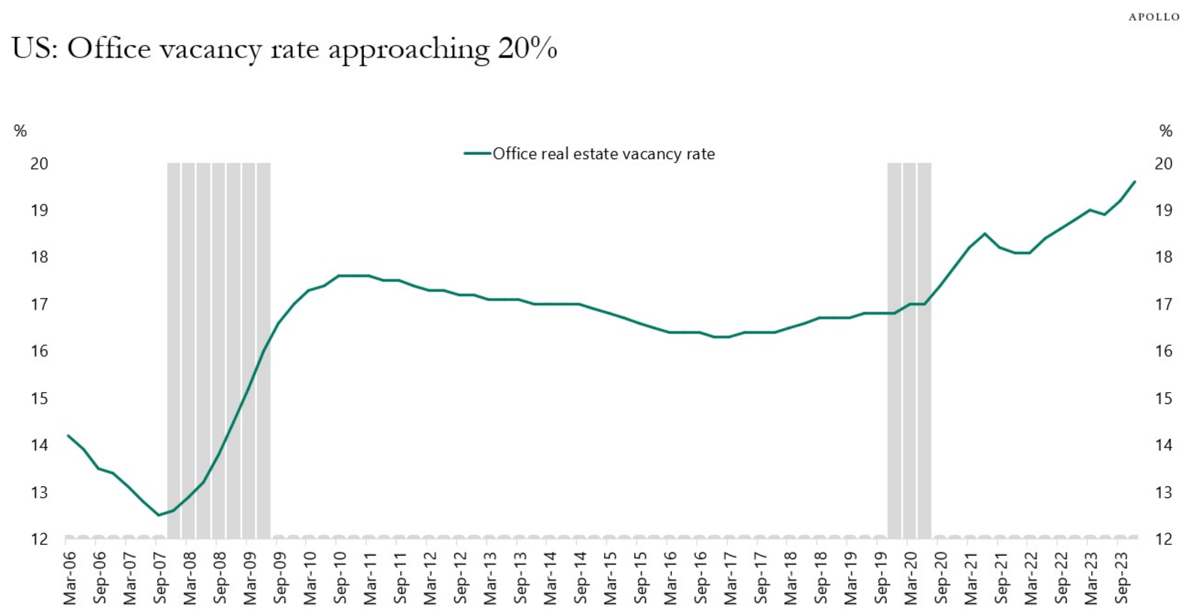
Half of Americans feel worse off than four years ago under Donald Trump and rate the former president's economic performance far higher than Biden's...

Continue reading here (subscription may be required).

REAL ESTATE

The U.S. office vacancy rate is still rising (from The Daily Spark)...

The vacancy rate for US offices is approaching 20%, see chart below. And this is in a strong economy with a strong labor market. If the unemployment rate starts rising because of the lagged effects of Fed hikes, the office vacancy rate will increase even more.



Homebuyers need to earn 80% more now than in 2020 to afford a house (from CNBC)...

Factors beyond high mortgage rates are affecting housing affordability for many Americans, according to experts.

Almost four years ago, a household earning $59,000 annually could afford a new mortgage without spending more than 30% of their monthly income and with a 10% down payment, according to a recent report by Zillow Group.

That is no longer the case today.

While the typical household in 2024 makes about $81,000 a year, up from $66,000 in 2020, wages have not kept up with housing costs.

"Since January of 2020, the typical mortgage payment on the typical home in the U.S. has nearly doubled," said Orphe Divounguy, a senior economist at Zillow.

Nowadays, potential homebuyers need to make about $106,500 a year in order to afford the typical home today, an 80% increase from January 2020, according to Zillow.

The connection between housing costs and wages has been gradually separating over the years, according to C. Kirabo Jackson, an economist and member of the White House Council of Economic Advisers.

"Around the mid-'90s, you start to see housing prices sort of separate from median wages in a way that kind of made housing less and less affordable for people who are in the market," Jackson said.

More supply 'helps keep prices down'

Tight supply is another reason behind unaffordability. Fewer homes available on the market for would-be buyers keeps real estate prices elevated and, in some local markets, the shortage makes prices climb higher.

The number of new housing units built throughout the years has been declining, and the low supply is rooted in restrictive land-use and zoning regulations, according to experts.

"If we have a supply problem, we really need to have a supply solution," Divounguy said.

Land-use and building regulations across the country make it difficult in some markets to build new homes, Divounguy said.

Continue reading here.

Under a $418 million settlement, home buyers and sellers to be spared standard broker commissions (from NBC News)...

The National Association of Realtors has agreed to a landmark settlement that would eliminate real estate brokers' long-standing commissions, commonly of up to 6% of the purchase price.

Instead, home buyers and sellers would be able to negotiate fees with their agents upfront. If the $418 million legal agreement is approved by a federal court, consumer advocates predict the ranks of real estate agents will thin, further driving down commission prices.

"For years, anti-competitive rules in the real estate industry have financially harmed millions," said Benjamin Brown, managing partner at the Cohen Milstein law firm and one of the settlement's negotiators. "This settlement bring sweeping reforms that will help countless American families."

The NAR acknowledged the pending settlement in a statement Friday and denied any wrongdoing.

"NAR has worked hard for years to resolve this litigation in a manner that benefits our members and American consumers," said Nykia Wright, interim CEO of NAR, whose previous chief stepped down late last year amid fallout from a federal lawsuit.

"It has always been our goal to preserve consumer choice and protect our members to the greatest extent possible. This settlement achieves both of those goals," Wright said in the statement.

Continue reading here.

Half of office space in downtown Pittsburgh could be empty in four years (from MishTalk)...

The CRE implosion is picking up steam. Check out the grim stats on Pittsburgh. Unions are also a problem in Pittsburg as they are in Illinois and California.

Downtown Pittsburgh Implosion

The Post Gazette reports nearly half of Downtown Pittsburgh office space could be empty in 4 years.

> Confidential real estate information obtained by the Pittsburgh Post-Gazette estimates that 17 buildings are in "significant distress" and another nine are in "pending distress," meaning they are either approaching foreclosure or at risk of foreclosure. Those properties represent 63% of the Downtown office stock and account for $30.5 million in real estate taxes, according to the data.
>
> It also calculates the current office vacancy rate at 27% when subleases are factored in — one of the highest in the country.
>
> And with an additional three million square feet of unoccupied leased space becoming available over the next five years, the vacancy rate could soar to 46% by 2028, based on the data.
>
> Property assessments on 10 buildings, including U.S. Steel Tower, PPG Place, and the Tower at PNC Plaza, have been slashed by $364.4 million for the 2023 tax year, as high vacancies drive down their income.
>
> Another factor has been the steep drop — to 63.5% from 87.5% — in the common level ratio, the number used to compute taxable value in county assessment appeal hearings.
>
> The assessment cuts have the potential to cost the city, the county, and the Pittsburgh schools nearly $8.4 million in tax refunds for that year alone. Downtown represents nearly 25% of the city's overall tax base.

In response Pittsburgh City Councilman Bobby Wilson wants to remove a $250,000 limit on the amount of tax relief available to a building owner or developer as long as a project creates at least 50 full-time equivalent jobs.

It's unclear if the proposal will be enough. Annual interest costs to borrow $1 million have soared from $32,500 at the start of the pandemic in 2020 to $85,000 on March 1. Local construction costs have increased by about 30% since 2019.

But the city is doomed if it does nothing. Aaron Stauber, president of Rugby Realty said it will probably empty out Gulf Tower and mothball it once all existing leases expire.

"It's cheaper to just shut the lights off," he said. "At some point, we would move on to greener pastures."

Continue reading here.

An interesting proposal that could help "thaw" the housing market (from Graham Stephan via LinkedIn)...

Nobody wants to sell their house because 99% have a mortgage less than the current rate. Here's a crazy solution:

Let people take their mortgage with them to the next house.

Let me explain:

In the UK and Canada, there's this concept called a "portable mortgage".

When people move from one house to another, they can take their loan with them.

They just need to pay the remaining balance of the loan but they can keep the same interest rate.

This works in the UK and Canada for two reasons:

1. Loans are paid out over 25 to 30 years, but rates aren't locked in for that long. Rates are renewed every 5 to 6 years.

2. So lenders compete among themselves to give the best rates. Portable mortgages are a good alternative to variable-rate mortgages.

In the US, loans are fixed for 30 years, and refinancing is usually a more attractive option for homebuyers, because they could get a cheaper rate.

Portable mortgages don't fit in neatly with the mortgage securities market in the US, because they have to be custom-made for specific buyers, and there's no tax credit like refinancing.

But here's why lenders in the US could benefit from offering portable loans:

1. It's a unique niche in a rising interest rate environment.

2. Many millennials and GenZ-ers want mobility, so a lender who facilitates portable loans would capture that market.

3. They could charge a transfer fee that is cheaper than getting a new loan at a higher rate, making it a better option for people looking to sell and buy.

4. They could provide slightly higher rates that are lesser than the current market rate if they had a good way of assessing the customer risk.

5. Then they could also upsell and cross-sell other products like insurance, savings accounts, refinancing, and other financial services.

This would free up so much inventory and let people downsize because they could profit off of their current homes without losing their attractive mortgages.

If any lender takes the lead on this when interest rates are high, they could capture a lot of loyal customers for a long time.

Continue reading here.

The new normal for mortgage rates will be higher than many hope (*from The Wall Street Journal*)...

Interest rates are likely to come down later this year, with the Federal Reserve on track to start cutting rates. But mortgage rates might not follow as quickly.

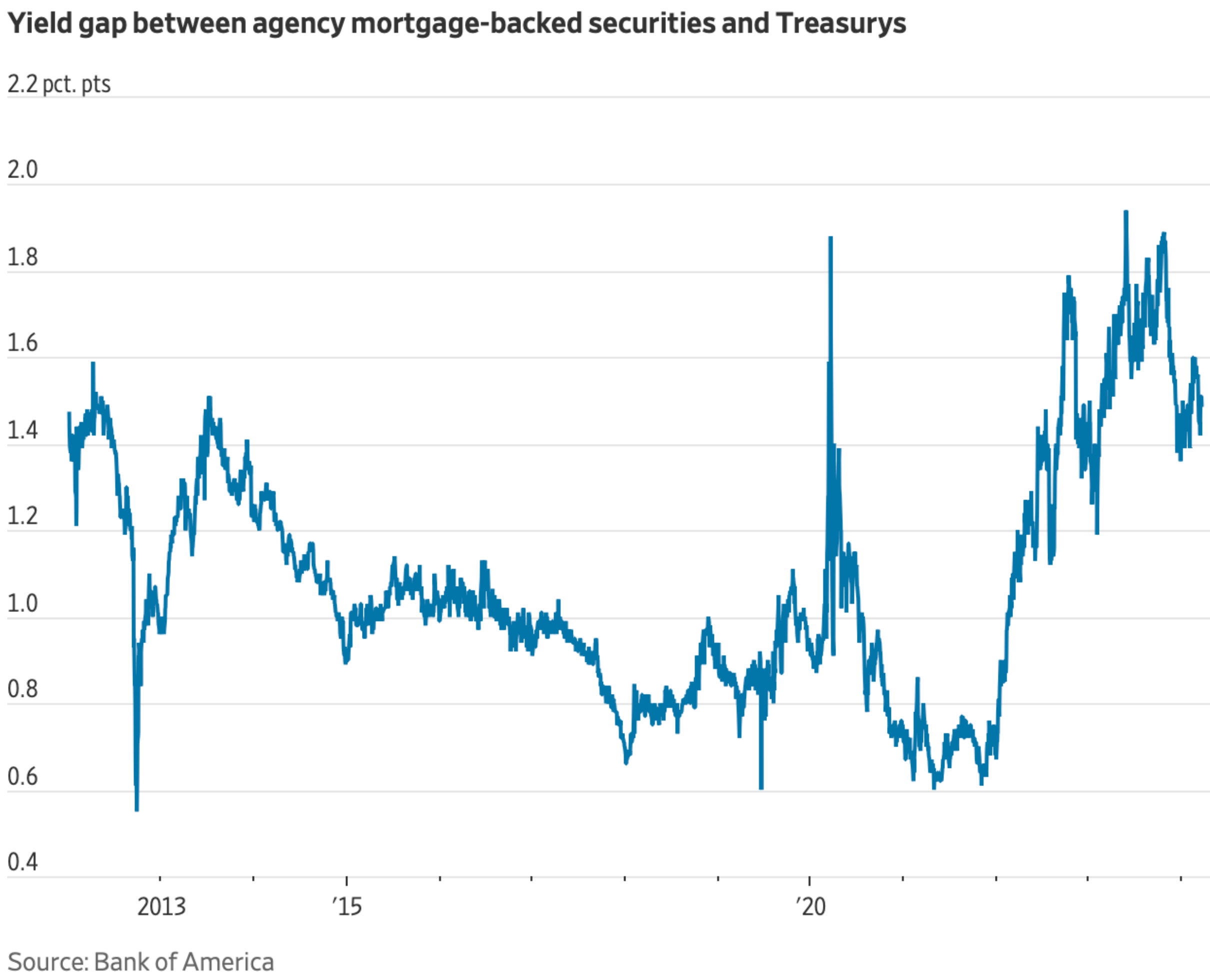
That is because mortgages, and mortgage-backed bonds, just aren't as in demand in financial markets as they were in the years before the Fed began to start to tighten in 2022. And they might not be for a while.

The extra yield over Treasurys—or spread—demanded by investors to own mortgage-backed securities issued by government-sponsored enterprises such as Fannie Mae or Freddie Mac, known as agency MBS, has come down a bit from the highs touched last year. But it still hasn't narrowed back to historical levels. Wider spreads appear to be a new normal for the mortgage market. That in turn means homebuyers for now can expect to keep paying relatively higher rates.

The yield gap between mortgage bonds and Treasurys is still around 1.5 percentage points, according to figures compiled by Bank of America. The typical spread a few years ago was around 1 percentage point.

"There is further room for tightening spreads," says David Finkelstein, chief executive and chief investment officer of Annaly Capital Management, a real-estate investment trust that invests in mortgage bonds and other strategies across residential mortgage finance. "But we don't believe we're going back to pre-2022 levels."

One crucial driver of a new baseline is that the Fed seems increasingly unlikely to return to the market as a buyer of agency MBS. Even if the Fed does end quantitative tightening sooner than anticipated, many observers expect it to continue to allow mortgage bonds to mature or pay off and leave the balance sheet at the same pace, while adjusting how quickly the Treasurys part of the portfolio declines.



One Fed governor, Christopher Waller, said in a speech at the beginning of March that he "would like to see the Fed's agency MBS holdings go to zero," alongside a desire to shift the Fed's portfolio to have a larger share of shorter-term Treasury bills.

"The historical [spread] level is from an environment in which the Fed was buying mortgages," says Jeana Curro, head of agency MBS strategy at Bank of America. "We've had to recalibrate what is normal."

Continue reading here (subscription may be required).

SPECIAL SITUATIONS

Activist Investing, Spinoffs, Arbitrage, Mergers & Acquisitions (M&A), and More

This left-for-dead company has seen historic insider buying (from Undervalued Shares)...

It's not often that you see a CEO carry out insider buys in the tens of millions.

The CEO of American software firm Asana has hovered up shares worth a lot more: USD 166m, last year alone.

Once you factor in prior years, his insider buys amount to well over USD 1bn – most likely the largest ever stretch of purchases made by a corporate insider.

The company's CEO has made ample use of the stock's weakness since the cooling of the "work from home" hype. The stock is currently down 88% since its 2021 peak, even though the company's product has been showing solid growth and holds much promise for the future.

Are these insider buys a sign that now is a good time to build a position?

Pay attention to backdoor listings

My ears perk whenever I find a company that came to market using a non-conventional way of listing.

Asana (ISIN US04342Y1047, NYSE:ASAN) is one such case. The company went public through a so-called direct public listing, a rare form of going public in which no new shares are created. Instead, only existing, outstanding shares are sold with no underwriters involved.

Apart from Asana, I am aware of only three other notable companies with such a direct public listing in recent years: Spotify, Slack, and Palantir Technologies.

Why do I take an interest in such companies?

When a company is quietly admitted to trading, fewer investors keep the stock on their radar. These direct public offerings can lead you towards real gems. I know one investor who landed his first 100-bagger thanks to a software company that did a direct public listing.

Asana is not a secret-secret company, due to its high-profile founders and its globally successful product. With a USD 4bn market cap, some analysts are already following it.

However, a sleugh of insider purchases were made last year, and the company is going to release an earnings report on 11 March 2024.

The mission to make work more efficient

Asana was set up by two prominent former Facebook employees: Dustin Moskovitz, co-founder and first CTO, and Justin Rosenstein, the engineering lead. Moskovitz held more shares of Facebook than anyone but Mark Zuckerberg himself.

As Facebook grew from a nimble start-up, the firm's early employees witnessed how it became much more of a typical large corporation. Both Moskovitz and Rosenstein allegedly became fed up with the amount of inefficient, annoying task management their team members had to do.

Large corporations typically comprise an endless number of everyday workplace struggles that keep employees from focusing on their actual work:

- Endless (and often unproductive) meetings.
- Lack of access to vital information.
- Duplication of work.

As Rosenstein once said: "When I ask people how much time they spend not doing their job – time spent on 'work-about-work' or phone calls or e-mails – people regularly tell me 60%, or even 90%."

Moskovitz and Rosenstein decided to leave Facebook to focus on creating a software that would make collaboration and communication more efficient. They wanted to reimagine communication in the workplace and link together email, data, and project updates. In effect, they envisioned a software that would become the "team brain", enabling teams to work better, smarter, and more cohesively.

Using their network and reputation in Silicon Valley, the duo quickly secured an initial USD 1.2m of angel funding before raising a further USD 9m Series A funding the same year. Three years and a successful public product launch later, they raised USD 28m Series B funding based on a valuation of USD 280m. Further details are laid out in Nira Blog's epic article "Asana's Rise to a $1.5 Billion Valuation".

Asana was off to the races, and it's grown impressively since then. It now provides a platform that helps teams orchestrate work, from daily tasks to cross-functional strategic initiatives, and tries to eliminate the need for constant meetings, email updates, and memos. This platform is currently used by about 140,000 customers that paid USD 547m in subscription charges in 2022/23. While notable clients include Airbnb and UBER, 40% of Asana's paying customers reside outside of the US, and there are millions of free users around the world.

Taking the middle road of offering both a freemium and an enterprise version was one of the key ingredients for Asana's success. "A guide to Asana, the workplace management tool that helps streamline communication across teams" by Business Insider explains more about the product and what it offers. Alternatively, watch Asana's brief introductory video linked to below.

The success of its first decade of operating culminated in Asana's direct public listing on the New York Stock Exchange in September 2020. This was the ideal moment for going public, given the prevalent remote working hype at the time. The stock debuted at a price of USD 27, only to climb to USD 142 just a year later. At its peak, the company was worth USD 30bn.

How times change!

A short three years later, the hype about "WFH" has been replaced by a new sense of realism about humans having to come together in real life to coordinate work, build relationships, and close sales. Additionally, large US tech companies had to lay off significant numbers of staff for the first time, and rising interest rates have led to multiple contraction among software companies.

Asana stock is currently down 88% from its peak.

Still, Moskovitz keeps loading up with insider purchases.

Why does he do so? Should you load up as well?

The truth about the insider purchases

Moskovitz owns 1% of Facebook, which regularly makes him pop up in rich lists with an estimated net worth of currently USD 25bn.

His Facebook wealth enabled him to become a massive buyer of Asana stock. Moskovitz last made headlines in October 2023 when he purchased 2.7m shares at prices of around USD 18 for a total investment of USD 48m. Up to that point, his purchases in 2023 alone amounted to 8.5m shares worth USD 166m, which made for an average price of USD 19.5 per share.

Insider buying, especially by a founder or CEO, is usually a bullish signal: smart money believes that a stock is undervalued. Given that Asana stock is currently trading slightly below Moskovitz' average purchase price of these transactions, should you rush out and buy the share?

Following insider purchases is an imperfect science, and one that comes with its own set of pitfalls.

Moskovitz had already purchased stock worth USD 1.02bn in 2021 and 2022. At the time, he paid an average price of USD 64, i.e. well over three times the current price. From that perspective, you could even argue that Moskovitz is a counter-indicator. His positive bias towards his own firm made him waste a record amount of cash on purchasing shares that he could have bought for a third of the price a year later.

This particular case of large-scale insider purchases demonstrates how important it is to not view these purchases in isolation, but to consider them within the broader context.

Like many other Silicon Valley companies, Asana heavily depends on compensating staff with stock. Over time, this leads to significant dilution of the share. It also means that a company has a strong interest in projecting optimism or its share price, as otherwise it might see key staff defecting to other firms.

One can argue that Moskovitz has been doing these purchases to keep his company's stock-based compensation plan attractive. His public persona (and possibly ego) will now be tied up in Asana's success. Given his enormous Facebook wealth, Moskovitz can afford to waste a billion (or two, or three) on buying back Asana stock for reasons other than making a good short-term investment.

When you spot large-scale insider buying, always keep in mind there may be reasons that are not immediately apparent from the outside. In the case of Asana, this could be a combination of Moskovitz' ego and the company's compensation plan – at least, to some extent. Had you followed Moskovitz' massive insider purchases in 2021 or early 2022, your investment would currently be down by two-thirds.

Moskovitz may have done these purchases despite multiple worries about the company's (and stock's) short-term performance.

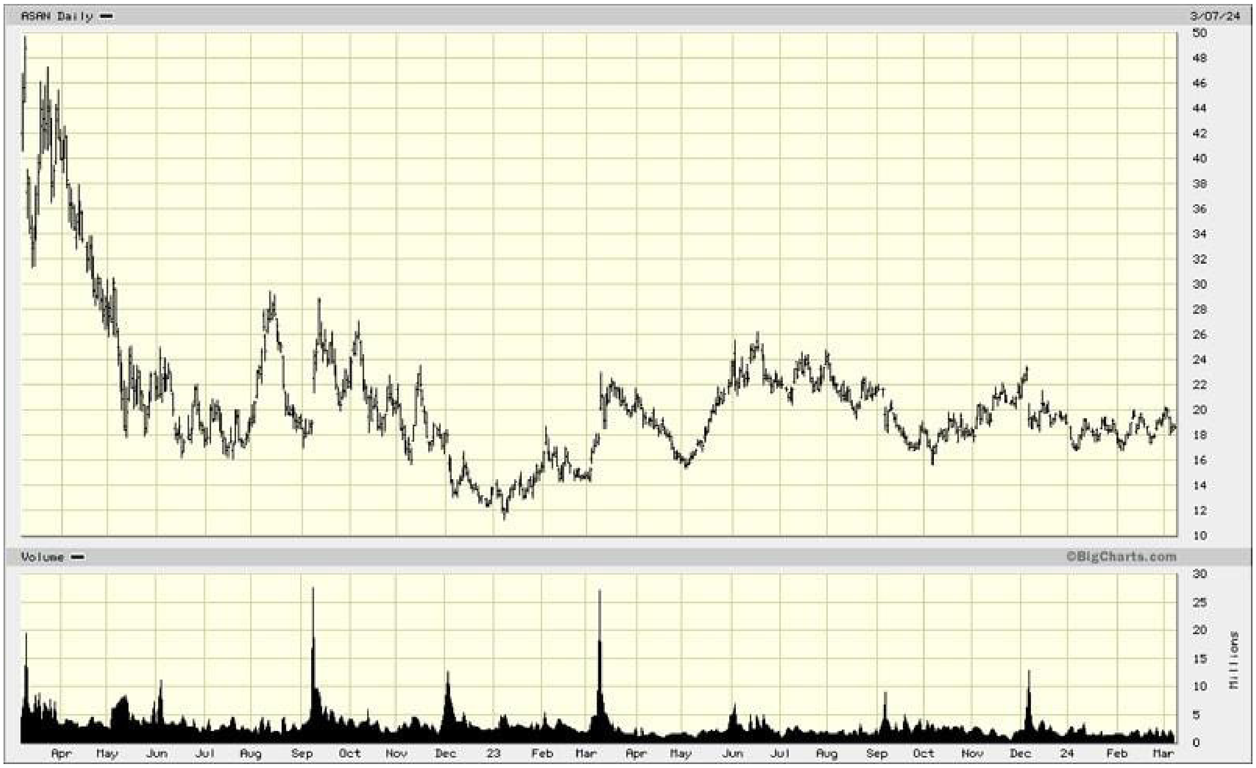
E.g., much as Moskovitz and Rosenstein are celebrated entrepreneurs, they are not the only smart people out there. The market has recently become more conscientious of the fact that there is no shortage of competitors in the space. Market leader Atlassian (ISIN US0494681010, Nasdaq:TEAM) is several times larger than Asana, and there is stiff competition from Israel's Monday.com (ISIN IL0011762130, Nasdaq:MNDY) and Slack, the platform that was taken over by Salesforce (ISIN US79466L3024, NYSE:CRM).

This sector of the software industry is currently predicted to grow at about 15% p.a. over the next few years. That's decent growth, but a massive slowdown compared to the years of the pandemic lockdowns. Also, growth investors tend to only get excited once a company or an industry achieves 20% annual growth. Add to it the fact that Asana is still losing money, even though it's already been operating for over a decade.

With all that in mind, it's easier to appreciate why the market hasn't gotten overly excited about Moskovitz' large-scale insider buys.

Not all is lost, though.

After two years of going sideways and forming a bottom, there are also good reasons for keeping the stock on your watch list.



A story that will come good eventually

Asana is one of the highest-margin software companies in the market. It has pro forma gross margins in the range of 90%, which means that as the company grows larger, 90 cents out of each dollar of incremental revenue will flow through to the bottom line. While the company isn't profitable today, that gross margin profile gives Asana plenty of leeway to scale profitably once it has become larger.

The question is, when will Asana become big enough for that to have an effect on its stock price?

In 2021, the market overestimated the company's growth potential. Right now, it may well be underestimating its potential. During this period of lower expectations, it's worth taking a closer look at factors that could eventually catalyse a recovery of the stock.

Asana's reporting include a few noteworthy yet hidden gems of information:

Large companies that have already purchased the Asana software for some of their team members are extending its use to more users within their firm. Put another way, existing customers are satisfied and happy to buy more. Asana customers that contribute over USD 100,000 of annual revenue reportedly have a so-called net revenue retention rate of over 100%.

Asana's large enterprise customers have 80m employees, but only 3m of them have been put on a subscription of the Asana software yet. There is significant growth potential by having the software spread deeper into the staff of Asana's existing clients, never mind winning new clients.

Source: [Asana Investor Day Presentation, October 2023](#).

The workplace issues that Asana's software addresses exist in nearly unlimited quantity, which makes me believe that the adoption of such software around the world will only grow further. All the more so since Asana (and its competitors) are developing ever more tools that are worth looking at, such as those powered by AI.

Here is a serious question – who can afford not to have such software to manage their teams? Researching this article has made me realise that such project management software has matured to a point where almost every team, in every industry, could benefit from using it.

Sooner or later, this should see Asana grow to a size where it breaks even – ahead of producing huge amounts of profit from each incremental dollar of revenue.

Which leads back to the same question, when to jump in?

The stock is not at the right level – yet!

Over the last five years, Asana has grown its revenue more than sevenfold, representing a 66% compound annual growth rate.

For its fiscal year 2025 (= the year ending in January 2025), Wall Street analysts currently estimate revenue growth to USD 725m, representing 12% year-on-year growth – a notable slowdown compared to prior years.

Asana has about USD 450m of net cash, leaving it with an enterprise value of USD 3.6bn. With a current share price of USD 18.50, the company is trading at 5x revenue.

As a rule of thumb, a US-based software company with a combination of 15% revenue growth, 20% long-term net margins, and a 1.5x price/earnings to growth ratio should normally be trading at about 4.5x revenue. Based on the current set of metrics, Asana stock remains slightly too high to qualify as a true bargain. It looks like Moskovitz was buying way too early when he picked up stock in 2022.

However, if the company managed to get back to 20% revenue growth and generated 30% net margins over the long term, it would deserve a valuation closer to 9x revenue. That's far from an unrealistic prospect once Asana leaves the current lull behind and achieves better economies of scale.

The kind of software that Asana is offering should stay in a secular growth trend, with Asana bound to remain in the top five of companies globally who offer this kind of service.

Moskovitz has vowed to not take the company private, and he would be unlikely to sell even if there was an offer on the table.

I'll keep this stock on my watch list, in case any general market turbulence ever makes it fall a lot further. The product is convincing, and it's a company that genuinely enhances its customers' lives. Along the way, it should eventually make heaps of money, once it has reached critical mass.

Continue reading here.

A cheap microcap poised to receive a huge legal payout (from Under the Radars via Toff Cap)...

In short: why invest in Ambase now?

- Legal Payout: If the court finds a verdict in Ambase's favor, the company could rake in up to $160m (before tax and litigation funding agreements) relative to Ambase's market cap today at only $9m.
- Low collection-related risks: Collection-related risks may be mitigated by the sale of US assets and the relative ease of collecting legal payouts from US entities vs foreign entities. All parties involved are well-established NY real estate players.
- High insider ownership: Litigation has been funded by personal capital from Ambase CEO Richard Bianco, who supported the early rounds of litigation with over $7m of his private capital. He owns 40% of shares and has gifted Ambase shares to his grandchildren, demonstrating his unwavering belief in Ambase's litigation potential.
- Timeline: A discovery order was filed on November 3, 2023. This order laid out the roadmap for information gathering. The timeline covers the period from December 2023 to the expected judgment in September 2024.

ORDERED that the discovery schedule shall be as follows:

Event and Deadline	
Parties to substantially complete document productions on or before:	December 31, 2023
All parties' affirmative expert designations with the information detailed in Commercial Division Rule 13 on or before:	February 14, 2024
All parties' rebuttal expert designations with the information detailed in Commercial Division Rule 13 on or before:	March 6, 2024
Fact depositions to be completed on or before:	April 15, 2024
End of fact discovery:	May 15, 2024
Affirmative expert reports to be served on or before:	May 31, 2024
Rebuttal expert reports to be served on or before:	June 26, 2024
End date for all disclosure:	August 7, 2024
Note of Issue on or before:	August 21, 2024
Summary Judgment Motions:	September 27, 2024

Background to the Litigation

The lawsuit is centered on claims of contract violations by the developers that resulted in significant financial damages to Ambase's shareholders.

In 2013, Ambase joined JDS Development Group and Property Markets Group to purchase the former Steinway Hall building and its ground lease for $132m. Ambase provided $65m equity – or 50% – of the acquisition price.

The developer secured a $725m construction loan from Apollo Global Management and AIG, but amid delays and cost overruns, the group ultimately defaulted on loan repayments. As loan payments approached in March 2017, Apollo sold a junior mezzanine stake to Spruce Capital Partners, who swiftly foreclosed on the project. Ambase equity value was whipped out to near zero.

Ever since, Ambase has sought to reclaim its stake in the building, while the developers JDS and PMG were brought back into the project to complete the tower.

Ambase argues that there are undisputed breaches of contract law by the developers. Violations include 1) Failing to provide timely and accurate budgets, 2) Inflating the 2015 construction costs to invalidate the Equity Put Right, and 3) Withholding information from Ambase, which allowed Spruce Capital to foreclose on the project.

> However, a crucial provision secured by Ambase CEO Bianco during initial negotiations could offer a lifeline to Ambase shareholders. Bianco secured an Equity Put Right clause in the contract. This clause allows Ambase to sell its initial $65m investment back to the developers, plus a 20% annual rate of return if the project's development costs rose by 10% or more. The true value of this equity put right is the centerpiece of this investment.

Valuation and Expected value

The trigger for Ambase to exercise the put right depends on "hard costs" increasing by 10% or more from the 2015 budget to the proposed budget in 2016. Ambase and the developers disagree on the budget-to-budget hard cost growth in 2016.

Ambase claims the developers inflated the contingencies for the budget in 2015 to avoid triggering the equity put right. The developers believe the contingency amount agreed in 2015 was $33,887,860.

However, public information from a payment notice issued by Apollo in 2017 indicates that the construction contingency agreed in 2015 was $28,219,120. See below:

FILED: NEW YORK COUNTY CLERK 06/28/2018 09:09

NYSCEF DOC. NO. 34

Schedule A

111 West 57th Street
Total Direct & Soft Costs

Budget Item	Borrower 06/30/2015	Borrower 12/2016 Update
Total Hard Costs	$258,349,730	$312,104,409
Construction Contingency	$28,219,120	$8,000,000
Total Hard Costs	**$286,568,850**	**$320,104,409**

Apollo's 2017 Borrower's Shortfall Demand Notice

Using the construction contingency amount implied from the project's primary lender, Apollo's 2017 notice above would trigger the exercise of the equity put right. In the table below, "Hard Costs" increased by 11.7%, according to information from Apollo - the JV's largest lender!

	Developers Proposed Trade Cost	Ambase and Apollo Trade Cost
Total Hard Cost - Agreed	258,349,730	258,349,730
Construction Contingency - Disagreed	33,887,860	28,219,120
Implied project Hard Costs in 2015	**292,237,590**	**286,568,850**
2016 Budget Update		
Developer Proposed Total Hard Cost	312,104,409	312,104,409
Construction Contingency	8,000,000	8,000,000
Implied project Hard Costs in Dec 2016	**320,104,409**	**320,104,409**
% Change in Hard Cost	9.54%	11.7%

Using Apollo's Construction Contingency from Shortfall Notice in 2017

% Implied Change in Hard Cost from 2015 to 2016

The value of the Equity Put Right, if exercised and upheld in court, is straightforward to calculate. If Ambase can put its $65m investment in the project back to the developer for an amount equal to a 20% annual return from 2013 through 2017, then the payout is roughly $161,740,800 (65*(1+0.2)^5). Ambase's market cap today is $8.5m (06/03/24).

Assuming a 25% probability of an +$89m payout (assuming a 45% payout for litigation financing payouts, equity offerings and tax), which are very conservative estimates, and a 75% probability of losing -$8.9m, the expected value of the equity is still positive, at $16m. 1.8x the current market cap.

Payout ($ million)	**$161.7**
Assuming a 45% payout for financing and tax	$89.0
Expected Value	**$15.6**
Market Cap	8.9
Value Per Share	**$1.05**
Current Share Price	**$0.22**
Upside %	381%
Downside %	-100%

Assigning probabilities to events is difficult, but the point is that the market is currently pricing in less than a 30% probability (using conservative assumptions) that Ambase can prove "hard costs" increased by 10%. Despite public information from related court cases showing construction contingencies that trigger the Equity Put Right, and undeniable evidence that the developers failed to provide timely and accurate budget cost. I think Ambase has a higher probability of proving its claim than the market is currently pricing in.

Risks

- Bianco's loan and litigation agreement dilute shareholders' interest in the final litigation payout. Ambase launched an $8.8m equity offering on 28 February 2024 at $0.2/share, with Ambase's CEO guaranteeing to buy any unsold shares. The CEO acting as the backstop investor could be seen as a sign of the CEO's optimism about the litigation outcome, as it further aligns his interests with those of the minority shareholders.

- Under the terms of the equity offering Ambase will issue 44m shares and also mentioned it will continue to consider litigation funding agreements with third party litigation funders for up to $5m of funding. In general, litigation funding agreements are structured so that the litigation funder would receive back their initial funding amount first (i.e. before any recovery is received by the company), plus an additional multiple of 1.0 times to 3.5 times the amount funded. This would equal ~14% of the total $160m payout and has been factored into the value per share above.

- Collection-related risks: the ability to collect legal payouts from JDS and Property Markets Group is unknown.
- Ambase has no additional asset or business model other than the Equity Put Right. If the claim is dismissed, Ambase equity would be worth zero.

Summary

If the courts uphold Ambase's Equity Put Right and the counterparties pay the debt, the total proceeds could be $160m relative to Ambase's market cap of c. $9m at the time of writing. The net payment to Ambase could exceed $89m (or $1.05 per share v ~$0.21 share price today), tax-sheltered at least in part by NOLs, and following a split of proceeds with the CEO's earlier litigation funding agreement.

Ambase shareholders may receive additional proceeds if the other claims against the foreclosing lender and the Senior Mezzanine lender are successful in court. There is also the possibility for pre-judgment interest. The statutory rate in NY state is 9% and is mandatory in breach of contract cases. Despite the additional upside, the asymmetry is attractive at today's prices.

Simply put, Ambase represents a unique opportunity with a timeline- passionately backed by its CEO, Richard Bianco.

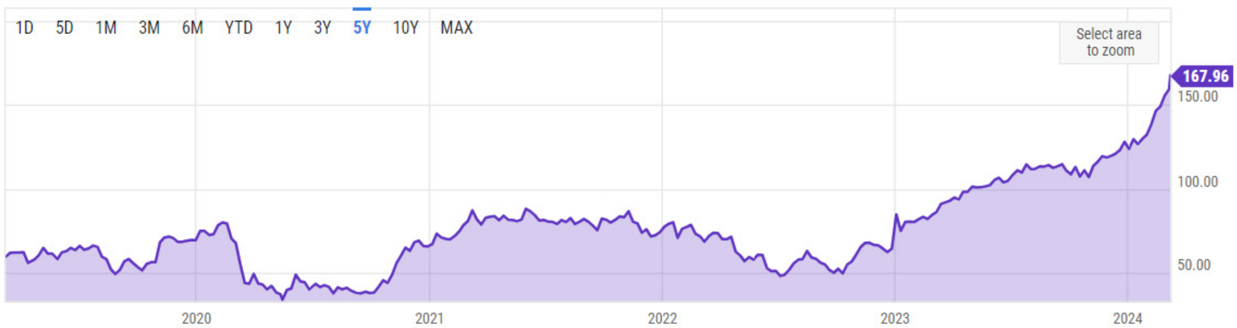
Continue reading here.

A closer look at the upcoming GE spin-off (from Value Don't Lie)...

This one was recently profiled in *Barron*'s but I wanted to take a closer look to see how to play the upcoming spin-off. GE is wrapping up their break-up with the spin-off of the Vernova power gen business and Aerospace business. Let's take a look at each piece and what they might be worth...

Quick Value

GE Vernova (GEV)



$GE 5yr chart (pre-spin)

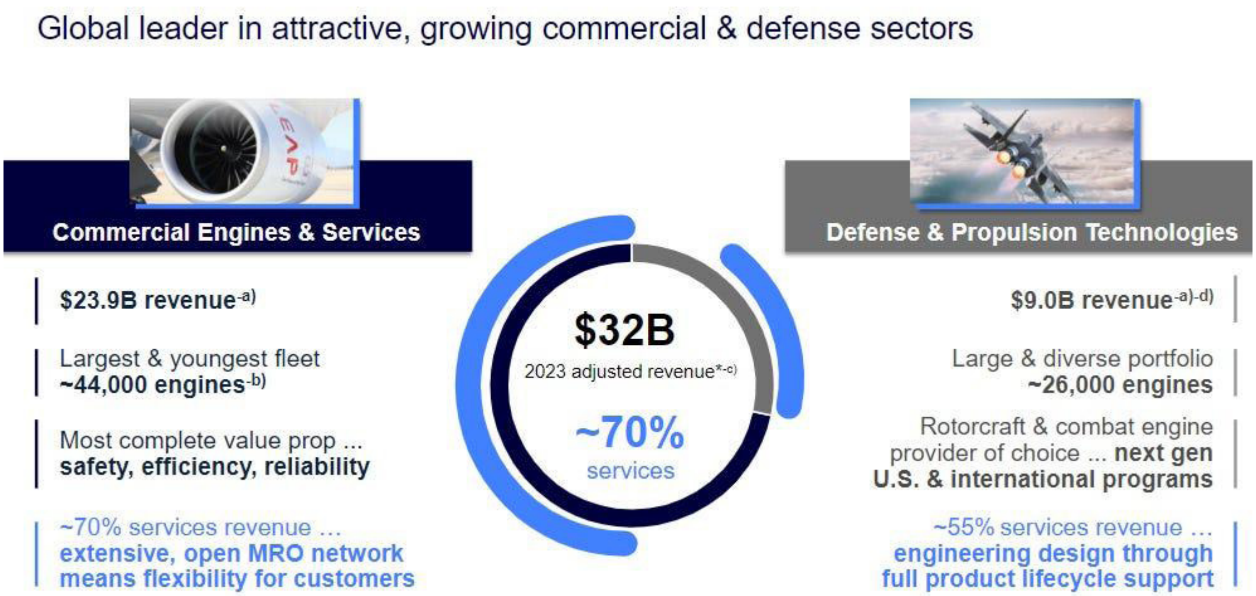
I'll try to keep this as concise as possible but for my own notes I prefer to look at both RemainCo and SpinCo to reference at the time of spin. I won't be able to cover every aspect of each company so be sure to check into them further.

As a starter, GE has 1.09bn shares outstanding x $168/share = $183bn market cap. (Also pretty wild this was a $140bn market cap just a few months ago.)

RemainCo (GE Aerospace)

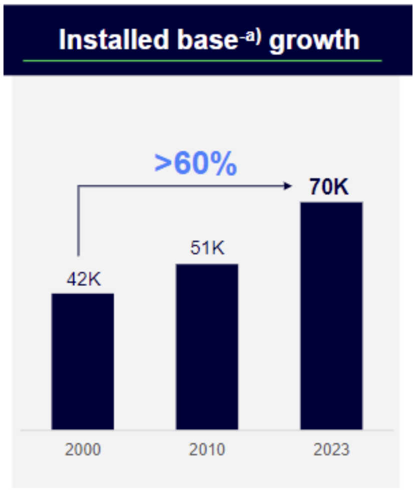
What they do...

Most will perceive this as the crown jewel. GE Aerospace makes engines for commercial and military aircraft. They also provide aftermarket parts and services. Services make up roughly 70% of total revenue making it a pretty stable business.



GE Aerospace segment overview

It's also a business with tremendous long-term tailwinds with the growth of commercial air travel and ever-expanding defense budgets. The installed base of GE engines has grown >60% since 2000:



GE Aerospace engine installed base

What do the financials look like?

Aside from the pandemic-induced dip in 2020-2021, results have historically been stable and growing. This segment has yet to eclipse the revenue/profit high watermark set in 2019 but they're closing in fast.

($m)	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Aerospace											
Revenue	21,911	23,990	24,660	26,261	27,375	30,566	32,875	22,042	21,310	26,050	31,770
Profit	4,345	4,973	5,507	6,115	6,642	6,454	6,812	1,229	2,882	4,775	6,115
margin	*19.8%*	*20.7%*	*22.3%*	*23.3%*	*24.3%*	*21.1%*	*20.7%*	*5.6%*	*13.5%*	*18.3%*	*19.2%*

Aerospace segment financials 2013-2023

Here is management's financial model through 2028...

Pretty impressive figures really... a business growing top-line at HSD/DD, operating profit that will nearly 2x to $10bn by 2028, and FCF converting around 100% of net income.

GE Aerospace financial model

From a capital allocation standpoint they plan to return >100% of FCF to shareholders over the next 3 years.

What it's worth...

RemainCo should command a high multiple... it's growing, generates a lot of cash, has very long-run tailwinds, etc.

I'll use operating profit which is guided $6-6.5bn in 2024 and $7.1-7.5bn in 2025 as a starting point. Well-run industrial peers trade at 15-20x EBITDA but may not have this level of organic growth. Using 20-25x $6-7bn operating profit = $120-175bn EV.

GE (pre-spin) has ~$22.7bn cash & investments and $21bn debt (there are some liabilities that could be considered debt-like but I'm ignoring those for a moment). Vernova will take ~$4bn cash so perhaps Aerospace is left with net debt of around $3bn.

That $120-175bn EV estimate less $3bn net debt and 1.09bn shares = $107-158 per share.

You could argue this undervalues the future potential of the business if they achieve those 2028 targets. Let's say they repurchase $25bn of stock from now until 2028 and hit the $10bn operating profit target. At 20x ($200bn) and zero net debt (by then) we have a $150bn market cap… say share count falls to 0.9bn and you have $222/share by 2028… (though that feels a little blue sky to me)

SpinCo (GE Vernova)

What they do…

Vernova sells equipment, services, and software to the power generation industry (mainly utilities and grid operators). They break it into 3 groups:

1. Power — Equipment and services for power generation. Largest installed base of gas turbines in the industry.
2. Wind — Turbines, blades, services, etc. for onshore and offshore wind generation.
3. Electrification — Equipment and services for electricity transmission & distribution.

The long-term need for additional power generation is significant (Form 10 highlights a 50% increase required by 2040) and Vernova sits in that value chain working directly with large scale utilities and grids.

At its core, this looks and feels like an E&C (engineering & construction) company with solid service businesses to support new-build backlogs. Results can be erratic at times if projects are underwritten poorly (as has been the case with Vernova for many years). Only ~45% of revenue comes from services.

What do the financials look like?

As a segment within GE, Vernova has been losing money for years, and 2023 was the first taste of a successful turnaround.

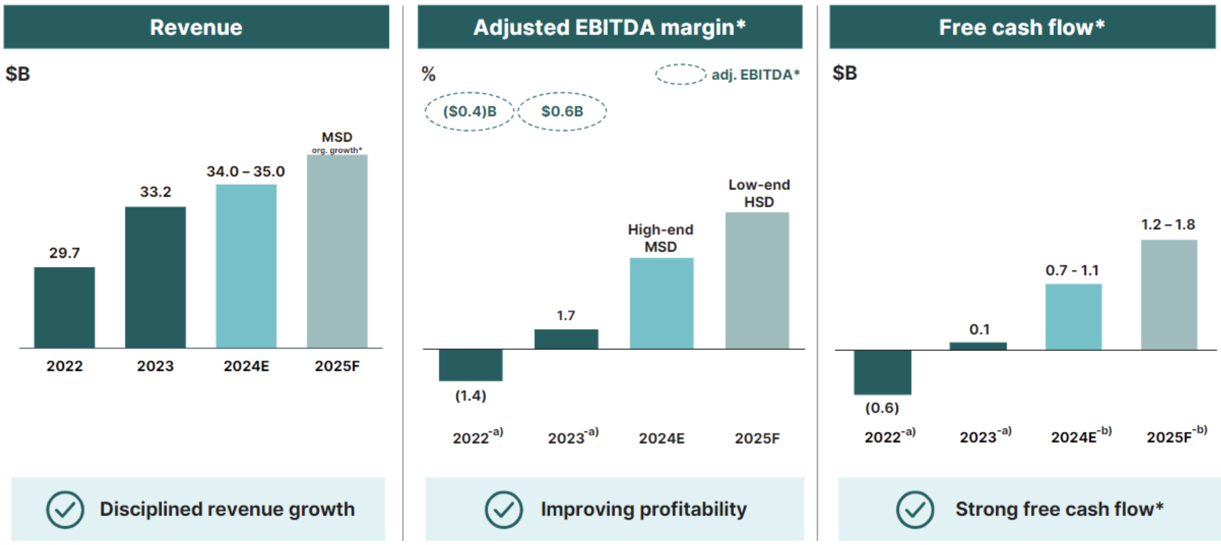
($m)	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Power											
Revenue	26,770	27,746	28,903	36,795	35,990	22,150	18,625	17,589	16,903	16,262	17,731
Profit	4,437	4,731	4,772	5,091	2,786	-1,105	291	274	726	1,217	1,449
margin	*16.6%*	*17.1%*	*16.5%*	*13.8%*	*7.7%*	*-5.0%*	*1.6%*	*1.6%*	*4.3%*	*7.5%*	*8.2%*
Renewables											
Revenue	4,824	6,399	6,273	9,033	10,280	14,288	15,337	15,666	15,697	12,977	15,050
Profit	485	694	431	576	727	140	-791	-715	-795	-2,240	-1,437
margin	*10.1%*	*10.8%*	*6.9%*	*6.4%*	*7.1%*	*1.0%*	*-5.2%*	*-4.6%*	*-5.1%*	*-17.3%*	*-9.5%*
Combined											
Revenue	31,594	34,145	35,176	45,828	46,270	36,438	33,962	33,255	32,600	29,239	32,781
Profit	4,922	5,425	5,203	5,667	3,513	-965	-500	-441	-69	-1,023	12
margin	*15.6%*	*15.9%*	*14.8%*	*12.4%*	*7.6%*	*-2.6%*	*-1.5%*	*-1.3%*	*-0.2%*	*-3.5%*	*0.0%*

Power & renewable (Vernova) segment financials 2013-2023

Segment operating margins were in the mid-teens from 2013-2016 before dropping to zero/negative. As a reminder, GE acquired the Alstom power gen and grid business in late 2015 for $13.5bn — the estimated $3bn cost synergies never materialized and actually went in the other direction.

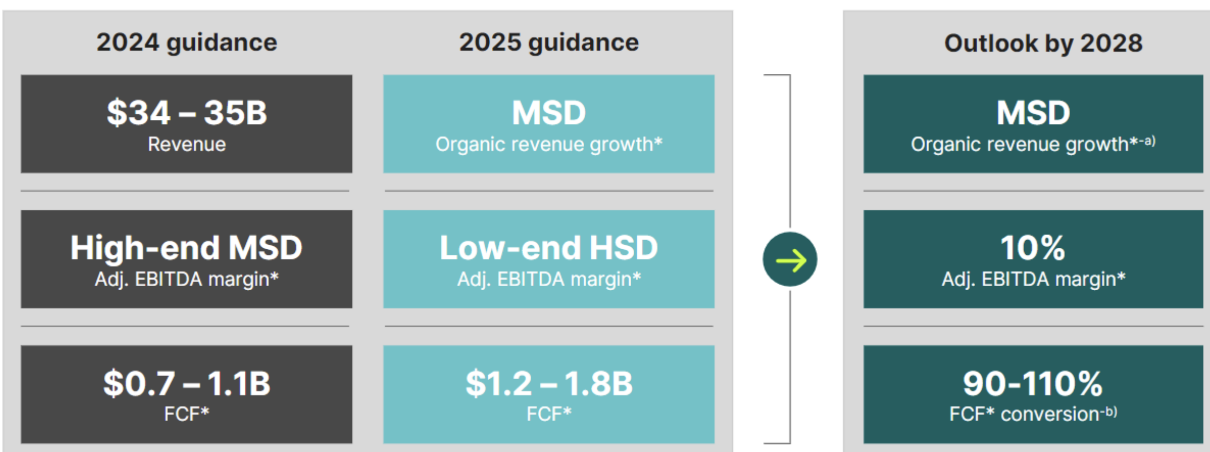
The 2017-2018 period kicked off a dramatic downturn in for large scale equipment. GE also sold a few power businesses in 2017-2018 to raise cash. Aside from that, the business has not recovered to 2013-2015 margin levels.

Fast forward to today — the business is recovering from losses to earnings and set to generate meaningful cash flow for the first time in a while.



Vernova financial summary

Here is where they plan to take the company through 2028:



Vernova financial outlook 2024-2028E

What it's worth...

Well-run industrials like Dover, Ametek, Fortive, etc. trade at premium 15-20x EBITDA multiples but most of those have 30% or better margins. Global conglomerates like Siemens, Mitsubishi, Schneider, and Hitachi trade at 10-12x EBITDA but they too have better margins (15-18%).

So what's a good comp group for this lumpy and optimistically 10% EBITDA margin business?

I think a group of engineering & construction peers makes sense here. The margin profile is similar and the "new build construction" element overlaps with Vernova well. Historically, companies like MasTec, Dycom, and Quanta traded around 8-8.5x EBITDA but lately it's more like 10-12x or more.

Ticker	Name	Last Price	Market Cap	EV/Sales (NTM)	P/E (NTM)	EV/EBITDA (NTM)	↑ EBITDA - Est Avg (NTM)	EBITDA Margin % (LTM)	Net Debt / EBITDA (LTM)
• MYRG	MYR Group Inc.	162.06	$ 2.71B	0.7x	25.2x	12.7x	$ 217.22M	5.05%	0.2x
• DY	Dycom Industries, Inc.	142.83	$ 4.16B	1.1x	19.0x	8.9x	$ 555.68M	11.64%	1.4x
• KBR	KBR, Inc.	61.66	$ 8.33B	1.3x	19.3x	12.2x	$ 828.56M	8.34%	2.1x
• MTZ	MasTec, Inc.	92.38	$ 7.19B	0.8x	33.5x	10.7x	$ 952.96M	6.32%	1.9x
• ACM	AECOM	91.73	$ 12.48B	0.9x	20.2x	12.9x	$ 1.11B	6.70%	1.4x
• J	Jacobs Solutions Inc.	146.93	$ 18.46B	1.3x	18.5x	13.5x	$ 1.60B	8.87%	1.5x
• PWR	Quanta Services, Inc.	242.06	$ 35.28B	1.7x	28.9x	17.5x	$ 2.20B	8.17%	1.1x
+ Add Ticker	+ New Group								
MEDIAN		142.83	8.33B	1.1X	20.2X	12.7X	952.96M	8.17%	1.4X
AVERAGE		134.24	12.66B	1.1X	23.5X	12.6X	1.07B	7.87%	1.4X

E&C peer multiples

If we give Vernova credit for 6-8% EBITDA margins ("high end of mid and high single digits") on $35bn revenue = $2.1-2.8bn EBITDA. Net cash will be ~$4bn at the time of spin and using a 10-12x EBITDA multiple and the old GE share count of 1.09bn = $23-34/share price target (that's $92-138/share using the 4:1 spin ratio).

Some factors that could make it more/less attractive than that:

- Revenue growth at MSD rate... 2024 outlook just now eclipsing 2019 sales levels
- Expanding EBITDA margins... from "high end MSD" to "low end HSD" to 10% is quite a leap on top of MSD revenue growth... i.e. EBITDA could be growing 15% per year
- On the other hand, this is still a very cyclical business with potential for poor project underwriting (E&C has occasional blow ups)

Summing it up…

I've got the 2 pieces pegged at:

1. RemainCo (Aerospace) valued at $107-158/share
2. SpinCo (Vernova) valued at $23-34/share ($92-138/share post-spin)

Sums up to $130-192/share vs. the current price of $168. The play would be current GE shareholders dumping the lumpier SpinCo business and ascribing a ton of value to the Aerospace behemoth. I'd be pretty interested in picking up Vernova at a price tag that heavily discounts the success of those future targets…

Continue reading here.

Here's a list of event-driven trade ideas that are potentially actionable today (from ToffCap)...

SPIN-OFFS (and related)

- ***3M (MMM US).*** Will spin its health care business into an independent public company ('Solventum'). Spin effective April 2.
UPDATE: Solventum to trade under SOLV. An investor day is scheduled for March 19 to provide an overview of Solventum's business and value creation opportunities.

- ***General Electric (GE US)***. GE is set to spin its energy business ('Vernova') on April 2. Will trade under 'GEV'.
UPDATE: GE dove deep into the medium-term expectations of the upcoming spin-offs during the recent investor day.

- ***MDU Resources (MDU US)***. After the recent spin of Knife River, MDU now also plans to spin its construction services business. Remaining company will be a pure-play energy delivery business.
UPDATE: MDU provided an update of its intended spin of the construction business 'Everus'. Link here. Spin expected 'late 2024'.

STRATEGIC ALTERNATIVES (potential take-outs, asset sales, M&A, etc.)

- ***Summit Midstream Partners (SMLP US)***. Ongoing strategic process. Sale looks most likely outcome. Announcement could be imminent as update on strategic review will be provided on March 15. H/t @AndrewRangeley for the idea.
UPDATE: Strategic review entered 'critical phase with high interest'.

- ***Sharecare (SHCR US)***. Evaluating strategic alternatives. Sharecare is actively engaging with parties interested in acquiring the company. Sharecare has a strong net cash b/s (though relatively high cash burn). Little share price reaction so far.

- ***Kineta (KA US)***. Kineta is exploring strategic alternatives, looking to sell itself. Roughly $6m net cash (remaining) as of Q3. Very recent presentation on IR site. Seems like Kineta might have some interesting assets.

- ***GrowGeneration (GRWG US)***. GrowGeneration is exploring strategic opportunities for its benching, racking, and storage business, MMI. Screens like an interesting play given (under the radar) ramp of distribution and e-commerce business.

- ***Gyrodyne (GYRO US)***. Evaluating strategic alternatives and liquidation contingencies. The company recently successfully closed a rights offering "to supplement its cash on hand to ensure it is operating from a position of strength through the duration of the liquidation process...". As of Q3, Gyrodyne had $54m in assets held for sale on the b/s and roughly $26m liabilities (incl. estimated liquidation costs) on a market cap of $13m (15/03).

- ***Xperi (XPER US)***. Rubric Capital (7.6% owner) pushing for strategic alternatives for the company's AI unit. Officially announced to be evaluating strategic alternatives (of Perceive business). Based on Bloomberg ccs, XPER will grow very quickly over the next few years and is trading at <3× 25e ev/ebitda. Co has a solid balance sheet (net cash).
UPDATE: Activist Rubric Capital nominated two independent Directors. Rubric also taking increasingly strong stance. Very interesting action going on.

NOTICEABLE LARGE BUYBACKS

- ***Victoria's Secret (VSCO US)***. Announced a $250m buyback, roughly 17% of the market cap (15/03). The share price recently dropped >30% following horrible earnings.

- ***Patterson (PDCO US)***. Approved a $500m buyback program, roughly 20% of current market cap (15/03).

- ***Eventbrite (EB US)***. Announced a $100m buyback program, on a current market cap of $560m (15/03). According to BB, Eventbrite has $280m net cash and operating earnings are on the verge of inflecting positively, with strong growth ahead. EB is trading at c. 5x ev/ebitda on 2024e.

INTERESTING INSIDER PURCHASES

- ***AMN Healthcare (AMN US)***. Strong insider buying by the CEO and CFO. Shares recently dropped almost 30% on earnings miss.

- ***FMC (FMC US)***. Strong insider buying action. If you follow us you'll know we keep close tabs with chemicals. Agri had (in our opinion) a classic cyclical downturn; markets seem to be moving in the right direction. Might be interesting to keep FMC assessed as earnings inflect.

- ***Innovid (CTV US)***. Quite some insiders buying activity. Innovid is a classic busted SPAC, but has a net cash balance sheet and seems to be inflecting on earnings. Based on street estimates. Innovid is trading at ~10x ev/ebitda on 2024e for ~30% ebitda growth over the next few years.

- ***AerSale (ASLE US)***. We note the relatively large insider purchases in this battered stock.
- ***NanoXplore (GRA Canada)***. Continued (very) strong insider purchases in this very interesting company. After years of losses, NanoXplore seems on the verge of strong profitability growth. Might be interesting to keep this one assessed.

MISCELLANEOUS (liquidations, merger arb., out-of-bankruptcy, uplistings, etc.)

- ***Signature Bank (SBNY US)***. Very attractive liquidation, with many assets already liquidated and CRE portfolio remaining. Significant upside to equity (as in, multiples). Will take some years to play our, but seems nice IRR potential.
- ***Olink (OLK US)***. Merger Arb. Olink is being acquired by Thermo Fisher. Seems to be an 'easy' deal. Roughly ~9% spread for a few months. H/t Jason (TMM comments section) for the idea.
- ***Paul Mueller (MUEL US)***. Launched a tender offer to repurchase shares at a purchase price of $80 per share (up to $10m). PM shares closed at $70 on Friday. Tender will expire May 7.
- ***JAMF (JAMF US)***. Jamf hosted an Investor Day on March 13 reviewing the company's business, strategy, and long-term financial targets. The company seems ready to scale profitability targeting accelerating top-line growth, and resp. 25% and 26% operating income margin and unl. FCF by 2026. If achieved, JAMF will trade at c.12x ebit and plenty of growth potential left (>80% GMs).
- ***Veradigm (MDRX US)***. Recently delisted, with strongly pressured stock price. Growth has been declining but stability looks ahead. Strong share price potential if Veradigm can indeed get back to growth (and uplist again). Good cash flow generation. H/t @EgweneAlVer for the idea.
- ***Bally's (BALY US)***. Merger arb. Takeover bid from Standard General at $15 p/s. Set up a special committee to evaluate the offer. Roughly 13% spread (15/03).
- ***HashiCorp (HCP US)***. Looking to sell itself. Held exploratory talks with several players (according to BB).
- ***Parkin (PARKIN UAE)***. We note (again) the upcoming IPO of Parkin, which manages parking lots in Dubai. While not extremely cheap, Parkin is massively profitable. Multiple should reflect solid and very visible cash flow generation and returns. Good dividend stock. IPO date March 21.
- ***Modern Mills (MODERNMI Saudi Arabia)***. We flag the upcoming listing of Modern Mills, another SA privatisation. Final offer price SAR 48. Might be interesting.

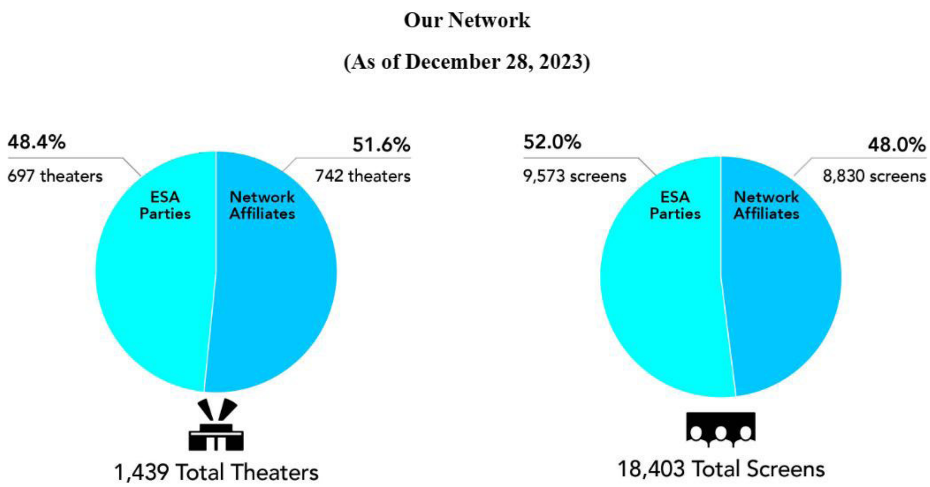
- ***WonderFi (WNDR Canada)***. Interesting action at this crypto trading platform. WonderFi is (finally) starting to show some revenue generation. Might be interesting to keep assessed as crypto moons once again. Also, decent insider purchases.
- ***Lincoln Educational Services (LINC US)***. Lincoln Edu will hold its first (we believe) investor day tomorrow (19/03). Might be interesting to keep an eye on.
- ***Turtle Beach (HEAR US)***. Looks like an sale might be imminent. Company created a 'value enhancement committee' and hired Jefferies as a financial advisor . Also, Donerail Group (who previously bid $32.86 / share and $36.50 / share), now has 5/7 of the BOD seats and 2/3 seats on the value enhancement committee.
  UPDATE: Announced a very interesting deal (DPD). Company 'incredibly optimistic on 2024 prospects'.
- ***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. 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.
  UPDATE: Recently rejected a bid from MNC Capital. Share price moved >$30.
- ***Surgepays (SURG US)***. Getting VERY close to the shut-down of ACP finding (funding depleted by April). Company recently raised $15m, probably as a defensive move in order to fund the growth of its wireless mobile product. This one will remain volatile (which means opportunity; check our blog for background on the thesis)
  UPDATE: Shares (finally) back down to earth after company acknowledged that ACP funding is drying up. Expect horrible Q2 and Q3.

Continue reading here.

A post-bankruptcy opportunity in National CineMedia (NCMI) (from Junk Bond Investor)...

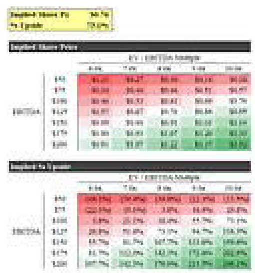
Situation Overview:

Established in 2006, National CineMedia, Inc. ("NCMI") is the largest cinema advertising network in the US. The company operates through its subsidiary, National CineMedia, LLC ("NCM"), which specializes in offering advertising services alongside managing third-party cinema circuits through network affiliate agreements. Based in Colorado, NCMI holds a 70% market share with access to 18,403 screens across 1,439 theaters around the US.



Chapter 11 Bankruptcy:

For those unfamiliar, NCM (the operating subsidiary) filed for Chapter 11 bankruptcy protection on April 11, 2023, largely due to the COVID-19 pandemic which negatively impacted the business, resulting in an estimated $850 million to over $1 billion in lost revenue. Despite efforts to increase liquidity, NCM's existing capital structure became unsustainable, leading to the decision to file for bankruptcy. You can read more about the leadup to the bankruptcy in the first day motions here and find my original write-up below.



National Cinemedia filed bankruptcy...and the equity looks interesting $NCMI

NCM quietly emerged from bankruptcy in 2023, after successfully restructuring its balance sheet and eliminating ~$1.2 billion of debt and ~$90 million of annual fixed charges. The company also eliminated certain non-profitable exhibitor contracts and restructured/eliminated office leases, which resulted in a combined $8.3 million in annual cost savings. Further, the restructuring simplified the ownership structure through which NCM Inc. now owns 100% of NCM LLC and continues to serve as its manager.

Since nearly a year has passed since my original post, I figured it was worthy of an update and a more comprehensive re-underwrite, especially since the company just posted their earnings results last week and saw its stock rip over 30%. Despite the more recent rally, the stock saw most of its price action in the last week and is only up ~25% over the last year. Nevertheless, the equity is still arguably cheap, particularly since the situation has largely been de-risked in many ways.

Note NCMI effectuated a one-for-ten (1:10) reverse stock split on August 3, 2023

Post-Emergence:

Post-emergence, NCMI has been focused on capitalizing on the ongoing recovery in theatrical attendance, growing its advertising revenue, and exploring new opportunities within the broader digital out-of-home ecosystem. The company's improved financial profile and liquidity have allowed it to invest in strategic initiatives aimed at enhancing its network capabilities, diversifying its advertising client base, and driving long-term growth.

On March 18, 2024, NCMI reported its 4Q'23 and FY'23 earnings results that exceeded both management guidance and consensus estimates. This better-than-expected performance was fueled by a robust cinema advertising market and higher pricing, offset by film slate changes due to the Hollywood strikes which resulted in attendance declines. That being said, the company reported a record high in revenue per attendee and a 43% increase in active national advertisers.

Looking ahead, NCMI guided 1Q'24 revenue to be between $34.5-$35.5 million, which is roughly flat compared to the prior year. The company expects Adj. OIBDA to be in the range of -$7.5 million to -$6.5 million in the seasonally-weak 1Q'24 compared to -$10.9 million in 1Q'23. The company did NOT provide guidance for the full year.

In a separate announcement, NCMI's Board of Directors authorized a new $100 million share repurchase program, set to run through April 1, 2027. The company will use operating cash flow for opportunistic buybacks at market prices. The announcement of a $100 million share buyback, representing a whopping ~25% of the company's market cap, combined with better-than-expected earnings, led to the stock surging by nearly 30% in the days after the announcement.

Remaining Legal Overhang:

Post-emergence, NCMI has faced some legal challenges with AMC and Cinemark appealing the confirmation of NCM's plan and the approval of its settlement agreement with Regal Cinemas. This follows a multi-year extension announced in June 2023 of its exhibitor service agreement with Regal Cinemas (~30% of NCM's total attendance).

AMC and Cinemark argue that NCM's new advertising contract with Regal triggered "most favored nation" rights in their existing agreements with NCM. However, NCM contends that the requested relief cannot be granted without "dismantling" the now-effectuated plan. NCM has moved to dismiss the appeal as equitably moot, contending that granting the requested relief would unravel the substantially consummated plan and undermine the reliance interests of numerous stakeholders.

Following NCM LLC's emergence from bankruptcy, neither AMC nor Cinemark holds any membership units in NCM LLC, but are eligible to be issued additional units pursuant to the terms of the Common Unit Adjustment Agreement. We are uncertain how the lack of ownership interest in NCM LLC and limited ownership at NCM, Inc. may affect their cooperation with us under the ESAs or otherwise going forward. Additionally, following the approval of the bankruptcy court authorizing NCM LLC's entry into the Regal Advertising Agreement and the Regal Termination Agreement (the "Regal Order") and approval of the Confirmation Order approving NCM LLC's disclosure statement on a final basis and confirming NCM LLC's Plan (the "Confirmation Order"), AMC and Cinemark filed notice of appeal of the Confirmation Order and the Regal Order. Subsequently, AMC and Cinemark sought a stay of the Confirmation Order and Regal Order in the Bankruptcy Court, the District Court for the Southern District of Texas, and the Fifth Circuit Court of Appeals, all of which denied the request. The consolidated appeals of the Confirmation Order and the Regal Order on the merits are pending in the District Court for the Southern District of Texas. We are uncertain how this litigation will impact AMC and Cinemark's willingness to cooperate under the ESAs or how long the litigation may last.

In summary, NCMI has successfully emerged from bankruptcy and is now focusing on stabilizing its business and financial performance. While the company faces ongoing challenges related to theater attendance and legal disputes with key partners, management remains optimistic about NCMI's long-term prospects and has initiated a share repurchase program to demonstrate its confidence in the company's future.

Continue reading here.

This software company may be on the verge of a long-awaited growth and profitability inflection (from Voss Capital)...

Elevator Pitch

We believe PAR Technology Corporation (PAR) is worth more than $80/share today based on our expectation of margin expansion and growth acceleration becoming evident in the next couple of quarters, combined with the scaling of acquisitions that are both profitable and strategic while also expanding PAR's total addressable market (TAM). Software platform winners with large TAMs, low churn and concurrently accelerating revenue growth and rising margins at scale deserve to be valued at premium multiples and we believe PAR is at a tipping point in demonstrating all those things. Our $84 base case price target is based on 27× 2026 EBITDA and 5.5x EV/Sales—which is a conservative discount to other vertical, scaled software platform winners.

Key Thesis Points:

1. Accelerating organic ARR from large new wins and rapidly expanding ARPU
2. Significantly expanding margins from underappreciated cost discipline
3. Profitable and strategic M&A expands TAM while strengthening software platform
4. Divestiture of Government (finally) creates a pureplay
5. Gigantic RFP pipeline of large Tier 1 QSR restaurant chains
6. Competition at an all-time relative low

Introduction

We exited PAR Technologies throughout 2021 after years of it being a core long when it became apparent to us that the true growth and profitability inflection was going to take much longer than we had originally anticipated and buyside expectations got way ahead of themselves. While we loved newly appointed CEO Savneet Singh (whom we pushed to get appointed to the board in 2018), we knew he was a very long-term thinker and was making investment/capital allocation decisions that would position the company ten years out, not one or two, and yet an immediate operational inflection point had already been more than priced into the stock.

With each passing quarter we were hopeful we would see signs of a growth/profitability inflection, yet each quarter there seemed to be some new issue that delayed that inflection. First there was a ton of R&D debt that had to be cleaned up to make customers happier. Then there were acquisitions that added upfront costs which obscured underlying progress (most recently the MENU acquisition). Following that, there were seemingly some delays in getting growth drivers off the ground (Payments and Table Service). A bizarre legacy contract with Arby's involving an ARR stepdown had also obfuscated growth. In all cases it seemed like there was a strong pipeline of large new wins just waiting to be realized, along with costs stabilizing, but it just was not quite showing up on the P&L, and there were no tangible customer wins to latch onto. PAR's big inflection was like "waiting for Godot" – it was always just around the corner.

We believe the wait is finally nearing an end and there are several significant tangible signs that the long-awaited upward inflection is about to occur. This inflection may begin in conjunction with the beginning of **the Burger King rollout, which we believe starts in earnest in Q2 of 2024 and continues through mid-2026**. However, there are several additional positive catalysts of note between now and then.

Over the next year we believe the company will simplify operationally (by selling their unrelated Government business, ***finally***), revenue/ARR growth will begin to accelerate on the back of known contract wins (Burger King and others), and significant upfront investments will be harvested to show burgeoning margin expansion. In this scenario we would get "Voss Sauce™" - accelerating revenue growth with concurrent rising margins - which usually leads to valuation multiple expansion, particularly when a company is going from unprofitable to profitable. Pair that with the recently announced acquisitions of Stuzo and Task, and we believe you will have a more fully scaled, profitable pure-play company emerging that will begin getting the valuation credit that enterprise pure-play software companies like AGYS, APPF, MANH, GWRE, TYL, and others currently enjoy.

The competitive landscape is starting to get weaker just as demand gets stronger. In our view, competitive risks are now at an all-time low with Toast losing their largest customer (Jamba Juice) and Oracle/NCR still struggling, providing a bit of a tipping point whereby PAR could be a "winner take most." This coincides with larger restaurant chains considering moving away from "do it yourself" POS and many other Tier 1s realizing they desperately need to upgrade their technological infrastructure. In other words, competition is weaker, and demand is stronger. Additional burgeoning growth drivers for PAR like Table Service, Payment attach rates, and the long-hyped international expansion should further add building blocks of credibility to justify a premium multiple.

Obvious trading comp Agilysys (AGYS), which has a similar revenue base and does what PAR does but for hotels, trades at 8x sales, 12x Gross Profit, and 45x NTM EBITDA (~34× 2026 EBITDA). We believe PAR's profile over the next 12-18 months will make them look much more like AGYS (15% EBITDA margins with 20%+ sales growth), and thus the stock could garner a similar multiple (this can be corroborated with other similar companies like APPF, TYL, etc.). In a Bull Case, PAR actually looks far more attractive than AGYS as instead of one giant customer win (Marriott for AGYS), PAR could likely be talking about several (Burger King, Popeye's?, Wendy's?, Chipotle? Subway?).

PAR's path to $80+ is straightforward to us. We derive it by forecasting $125 million in EBITDA in 2026 with a 27x EBITDA multiple, based on adding $138 million in ARR (25.5% CAGR) organically with ~60% incremental margins based on well telegraphed expense discipline combined with the EBITDA from the two recently announced acquisitions. This EBITDA multiple implies around an 8x ARR multiple, a 5.5x sales multiple and 10x EV/gross profit, still materially below the comp group.

Continue reading here.

PRECIOUS METALS

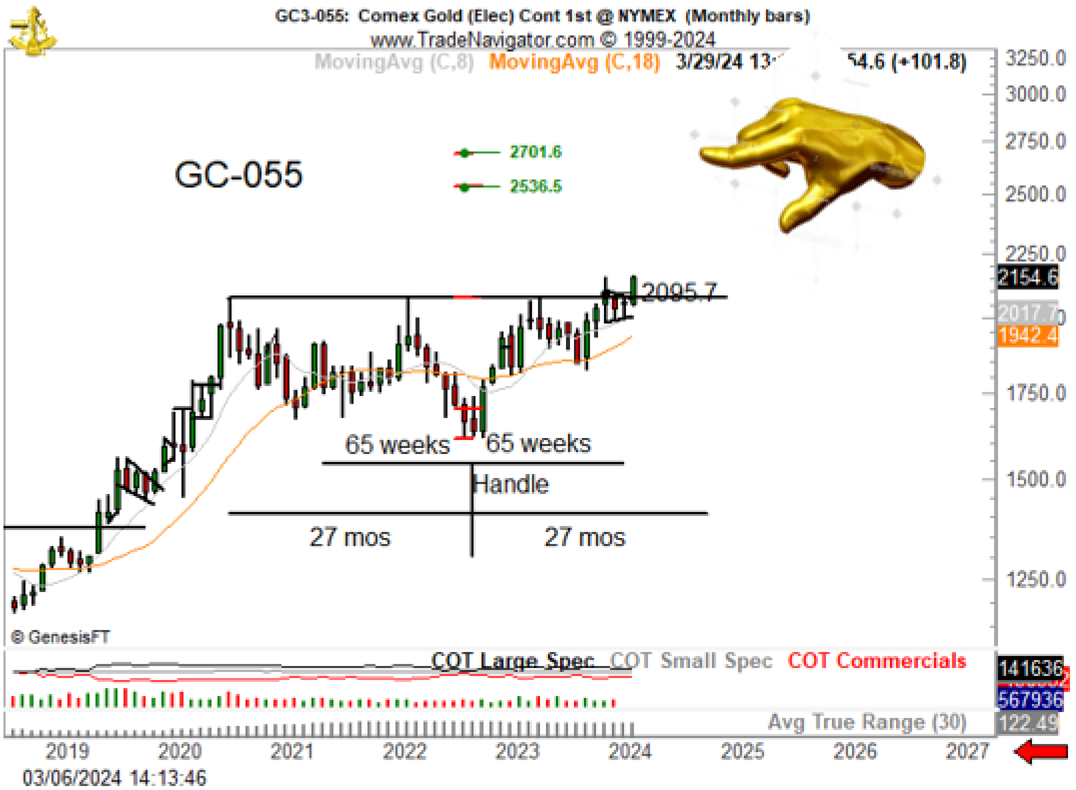
A new precious metals bull market may now be underway (from Otavio (Tavi) Costa via X)...

Sentiment in the toilet, miners completely distressed, overall capital spending at unprecedented low levels, historically suppressed implied volatility, gold-to-silver ratio at 90, central banks accumulating the metal at record pace, overwhelming levels of debt worldwide, marginal new gold discoveries, quality of existing reserves deteriorating, etc.

Gold is showing the way, but silver and miners should take the leadership.

Veteran commodities trader: This is where gold is headed ([from Peter Brandt via X](#))...

This is a FOR REAL breakout in Gold. Goldfinger points to a target range of 2530 to 2700 $GLD $GC_F



Why the mainstream view of gold and the Fed could be dead wrong (from FFTT Tree Rings)...

Gold Rally: The Fed Isn't Gonna Carry That Weight – Bloomberg

A sustained rally above $2,100 would need rate cuts. But there are increasingly sound reasons why they might not happen.

Bloomberg Intelligence's Mike McGlone suggests upward gold prices are likely, but adds that investors combine it with some Bitcoin or otherwise risk falling behind potential paradigm-shifting digitalization trends. As it is, gold's rally in recent days points toward general optimism over monetary loosening.

The resilient US stock market, strong currency, and 5% interest rates are headwinds for gold; so a further rally would be helped by an equity bubble and subsequent burst, and rate cuts. Now, how likely are they?

We found this article of note. Most investors and analysts continue to seemingly focus on gold through a singular lens: *What is the Fed going to do?*

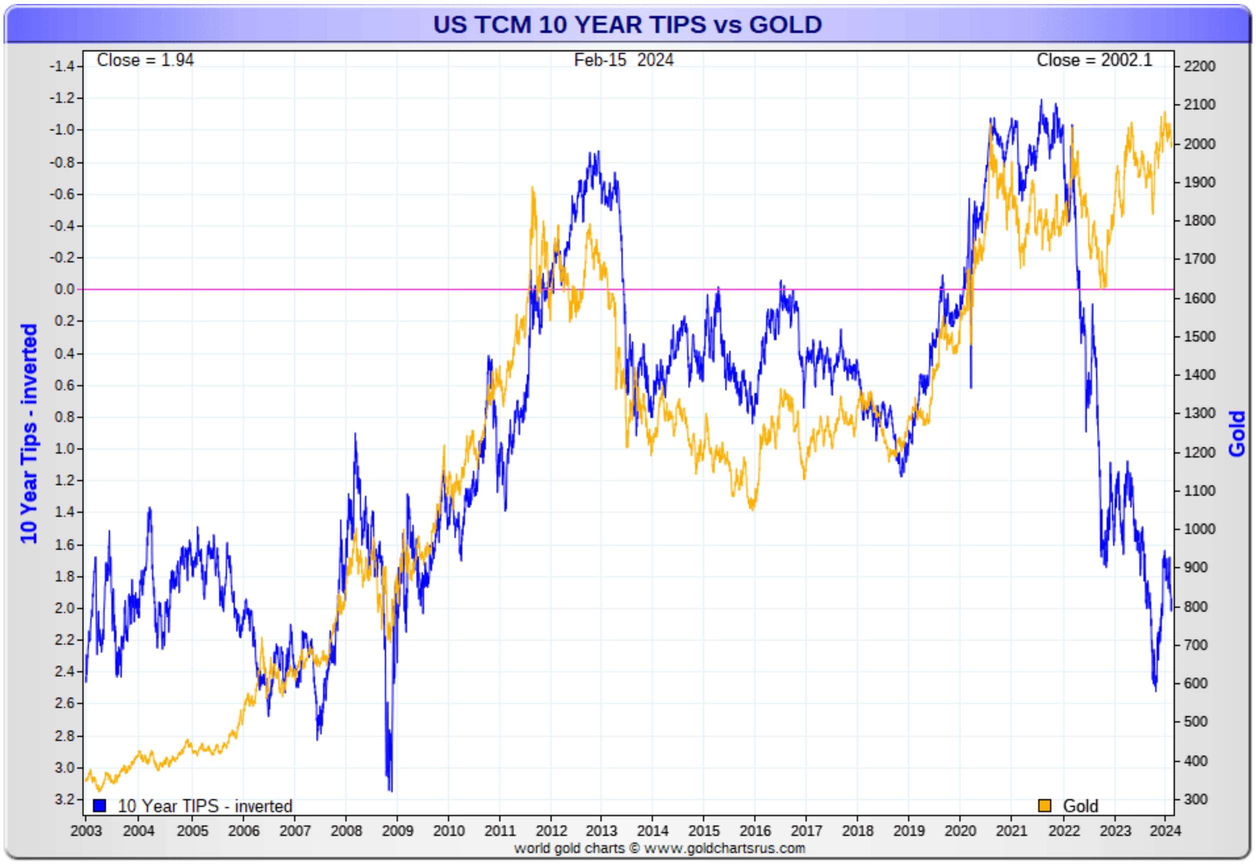
The article, like most investors and analysts at the moment, fails to note that it doesn't matter if the Fed hikes or cuts – either will drive more inflation.

It also fails to consider whether the USD is actively being weakened for both cyclical trade and strategic national security reasons, as appears to be the case...even though gold is acting like this is the case.

It also fails to consider whether more Russian or Chinese sanctions could be forthcoming, which would only further discredit the safety of USTs as a primary reserve asset, in favor of gold.

It also does not consider the possibility that oil has "re-become an oil currency" and is now being used in the BRICS bloc as a net settlement asset for non-USD oil, which given oil's 12-15x size relative to gold and BRICS secular oil demand growth would serve as a relentless bid for gold over time.

It does not consider any of these possibilities of a "correlation break" regarding gold, even though we have already seen a "correlation break" between US real rates and gold *(below).*



We are pleased that gold is at an all-time high in USDs. However, we are even more pleased that gold is at an all-time high and yet **most analysts and financial media are not even aware of, much less actively discussing, any of the factors above, all of which are significantly bullish for gold.**

If we are right, we suspect that by the time most analysts and financial media are discussing the elements above vis a vis gold, gold will likely be much higher in price. Let's watch.

Continue reading here (subscription required).

Silver could soon follow gold with a big breakout of its own ([from Otavio (Tavi) Costa via X]())...

Silver just poked its head above a 15-year resistance on the quarterly chart.

This is probably one of the most compelling macro opportunities that I have seen, particularly with the gold-to-silver ratio still near 90.

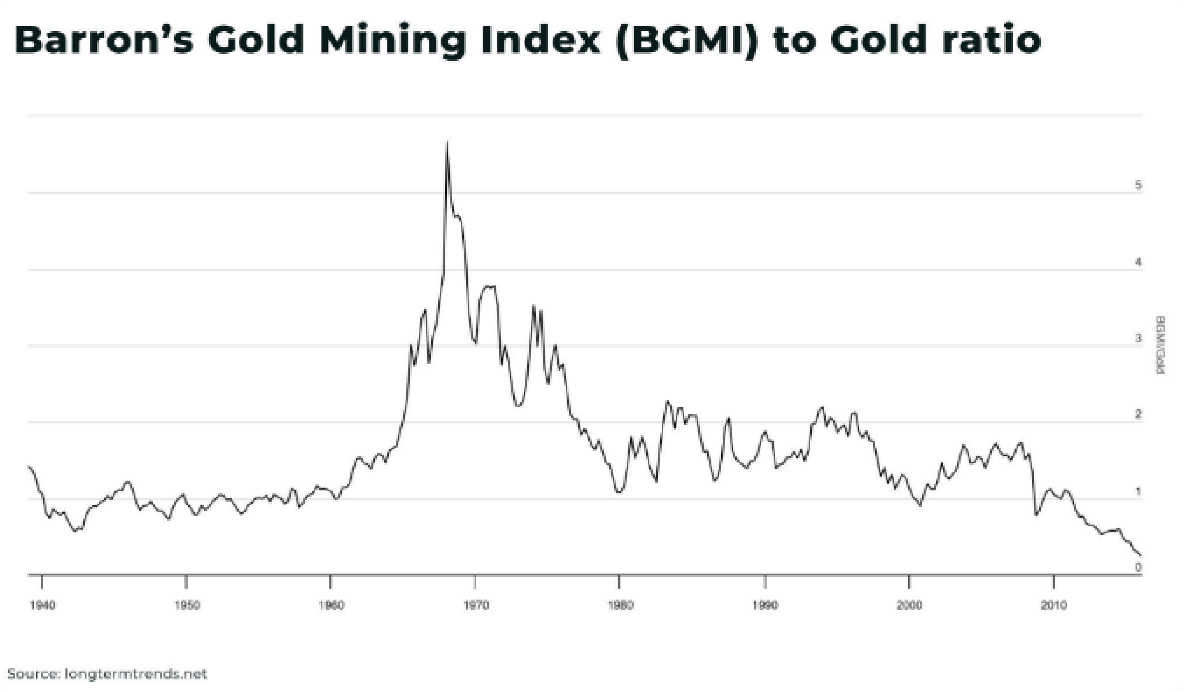
Gold-mining stocks are their cheapest versus gold in nearly 90 years (from Brandon Beylo via X)...

Barron's Gold Mining Index to Gold ratio is at its lowest point since 1940.

Something has to give.

Either gold prices pull back sharply.

Or gold miners start ripping higher.



The simplest reason to be bullish on gold today (from Jay Kaeppel via X)...

Gold is arguably the easiest market of all right now.

ABOVE RED LINE = GOOD

BELOW RED LINE = BAD

(PRO TIP: It doesn't have to be rocket science)

Why we still need gold today (from GoldFix)...

Why is this happening? Why is gold relentlessly climbing?

Why is Bitcoin, other than the ETF, resilient in its march upward? Why is silver now, possibly, we want to knock wood on these things, catching fire?

It's one word, trust. The world does not trust each other anymore.

We can get into why and where that happens.

It's pretty obvious to all of us here.

But this lack of trust manifests in deglobalization.

It manifests in an inability to look forward and say,

“It's okay you can get it back to me 60 days from now.

There is no “future” in a society where trust is lacking. There is only cash and carry. There is only collateral in the here-and-now. There is only the present-tense if you wish to keep doing trade.

If you wish to keep living civilly as neighbors— even though you don't like each other— yet still recognize you depend on each other; you need collateral.

- Clean Collateral.
- Collateral not indebted to anyone else.
- Collateral not encumbered by some clause or risk or ability to be manipulated or created or destroyed by the issuer of said collateral.

There is no other collateral on earth that fits this bill as good as precious metals.

You can argue that Bitcoin fits this bill as well, and it may fit the bill. But: They all have gold. They all have silver. They don't all have Bitcoin.

And so, as we move towards an era where trust is no longer taken for granted, where the money has to be exchanged right there and no credit lines are given, you need collateral that's clean, that everyone owns some of.

Collateral that everyone trusts and can be universally valued. That will be gold and silver.

Who is doing this?

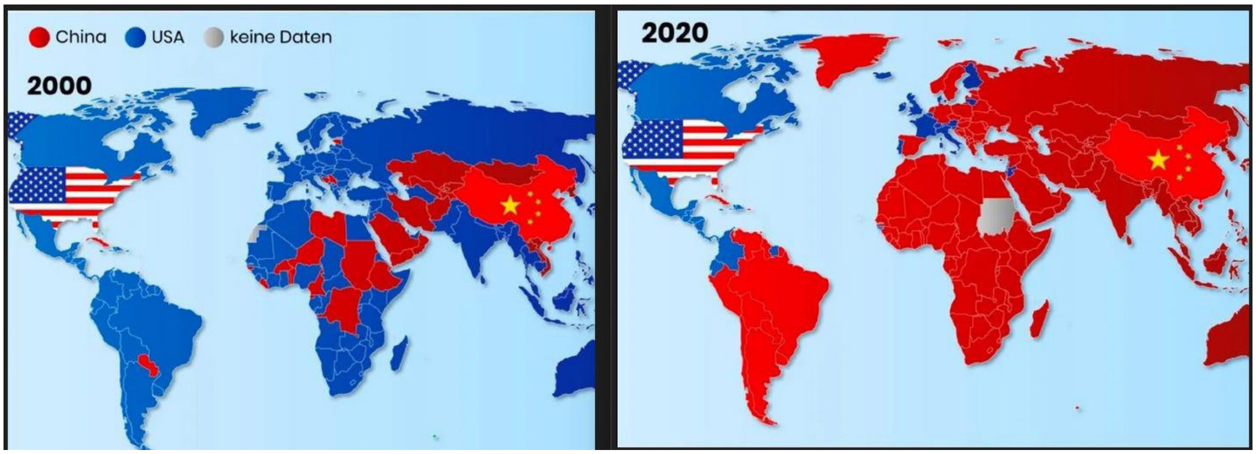
Well, everyone is doing this.

They're all in on it.

However, China is a big driver here.

China is as important, if not more important in global trade than the US considering they are the world's manufacturing engine and they are a potential consumption engine given that they have so many people.

World Trade Dominance in 2000 and 2020...

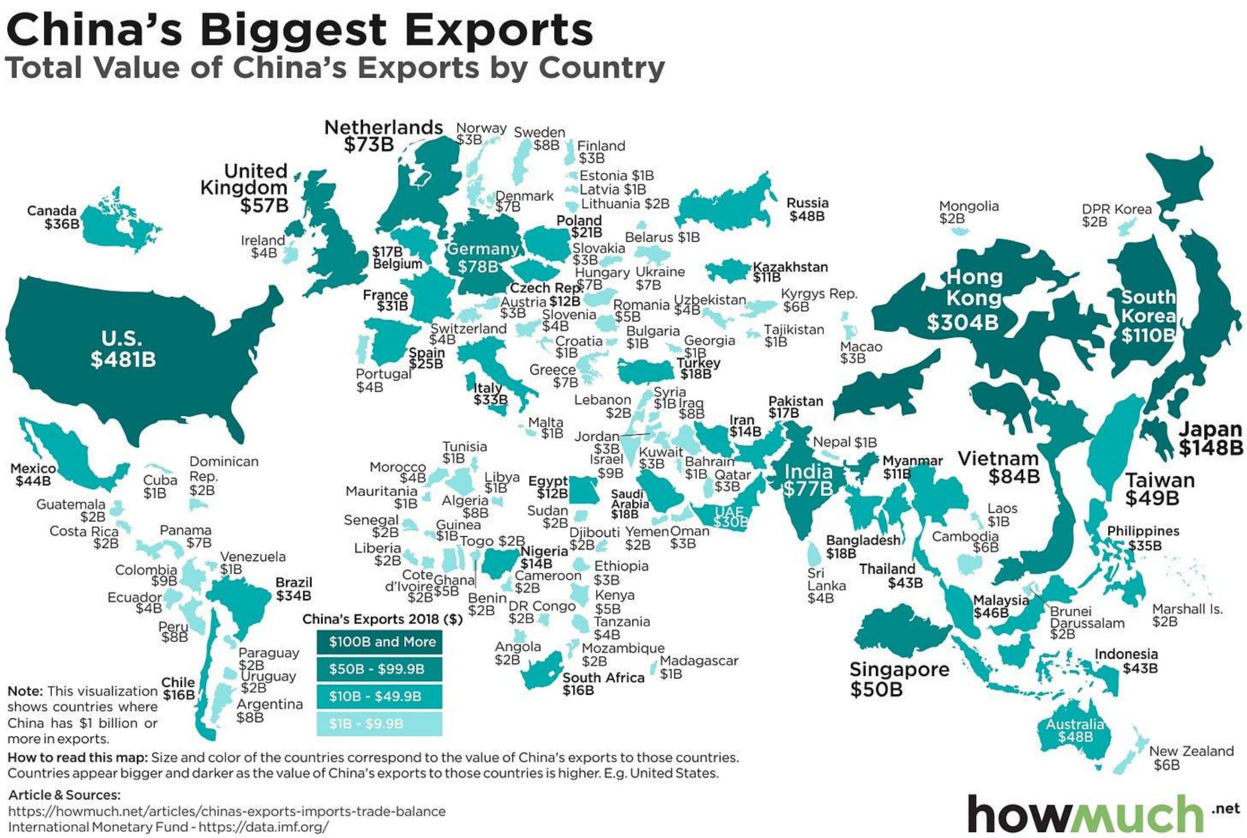


When you put these things together if nobody trusts anybody then you have to have good collateral, and China says well "we're going to use gold"

Thus, if you want to trade with China you have to have gold.

Soon you're going to start seeing world leaders talk about things like "collateral" in the context of Basel 3. That is a distraction. Basel 3 is not a cause of this. Basel 3 is a result of this.

But China and the US still need each other...



Make no mistake about it. Basel 3 exists because of the changing world. They've been planning for this eventuality since 2009, when Basel 3 was first floated. This is Mercantilism manifest.

Mercantilism, where everybody goes to their neutral corners and all trade is intermediated in part with the only objective go-between left. Gold and Silver.

This is the Mercantile temporary fix towards dealing with a lack of trust. If it works we won't have an all-out World War three.

There's a world war right now but it's being kept to a minimum. How it ends we don't know; But right now they need unencumbered collateral to avoid killing each other.

From: [Birth of the Mercantilism Thesis - Jan 2022]

> Either way, things are shaping up as a closing of the global network in what is fast becoming a mercantilist system.... If the US and China do not get on the same page now; Some real military instability might happen down the road.

We think China and the US are on the same chapter of this book now, if not the same page. They have also agreed the new collateral added to the mix will be Gold.

The WEF is Worse Than Mercantilism

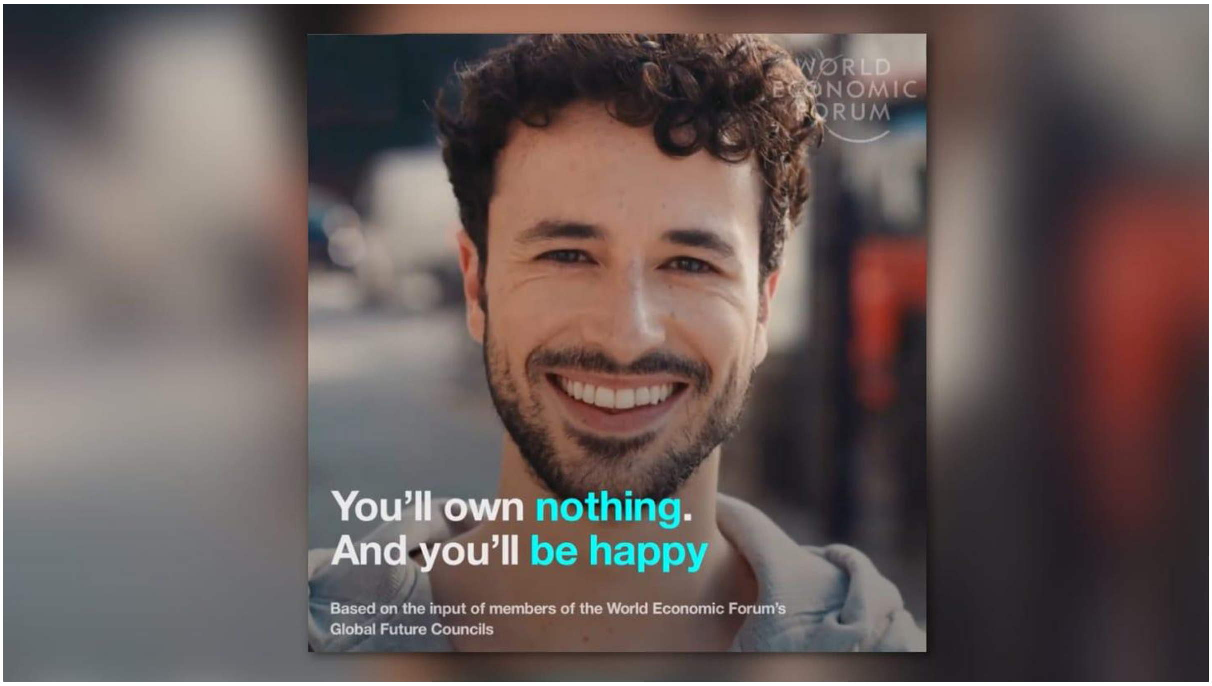
What comes after Mercantilism if it fails and the world splits even more in war? Feudalism.

There are some already planning for Feudalism with their calls for reductionism, 15 minute cities, CBDC, and other means to keep pleb servants captive on the plantation to keep their own status as lords of the European Manor. They are the enemy.

The opportunist wanted to lock in a caste system and saw his chance...

They are the ones who hope for the worst. If neokeynesian ideologues are the dogmatic remains of Europe's Liberal Democracy ideal which created tremendous prosperity over70 years, the WEF and its adherents are opportunists interested in selling you on an idea that protects their status up as feudal lords for another millennium. They hope for disaster. They are the true cynics.

They will tell you less is more, and if there is no real problem, they will make one up to get you to comply and keep them in power...



Verify Now, Trust Later

Therefore, Mercantilism has to work until trust is restored or the next step may be far worse. For mercantilism to work, trade collateral has to be unencumbered, unimpeachable, and not controlled by man.

Europe invented it and it saved them once before. Mercantilism is happening again between the US and China. The EU will be serfs for Klaus after the next World War if it fails this time. Trust will return, but not until everyone has earned it again.

Gold Has to Work, Bonds Will Not Yet.

Who has unencumbered collateral? Anyone who has gold. Gold is unencumbered collateral. So is silver, a trickier one for sure, but nonetheless it will also be called upon to serve as collateral.

What about Bonds as collateral?

“I don't want as many US bonds because of the debt. I don't want Chinese Bonds because they aren't as liquid enough. I don't want Brazilian bonds.”

The world wants something that is universally accepted. I need to buy your wheat. You need to buy my oil.

The world needs impartial money.

That means Gold and soon Silver.

Collateral is what will be needed.

Bitcoin is no joke. But central banks aren't going to buy Bitcoin. Not for a primary asset.

Continue reading here.

ENERGY

Shale oil production declines much quicker than traditional oil production, but the rate of decline is less than many investors fear (from RIA Advice)...

In a recent article, geologist Ted Cross of Novilabs eases investor concerns about the rapid depletion rate of shale oil wells. He claims investor fears are comparable to The "Red Queen Effect," a concept from Alice in Wonderland: "It takes all the running you can do to keep in the same place." Investors worry that new shale oil production will decline so quickly that new wells can't offset the declining production of existing wells. Therefore, total production increases are evermore challenging to achieve. Ted acknowledges the sharp decline in new shale oil wells but notes:

> *"Yes, shale wells decline rapidly early in life, but those declines moderate as they age, settling in somewhere between 5% and 10% per year. As the collective population of shale wells gets older and older, the "base decline" gets lower and lower."*

The graph below shows total oil production keeps rising with less production, as a percentage, attributed to new shale oil wells.

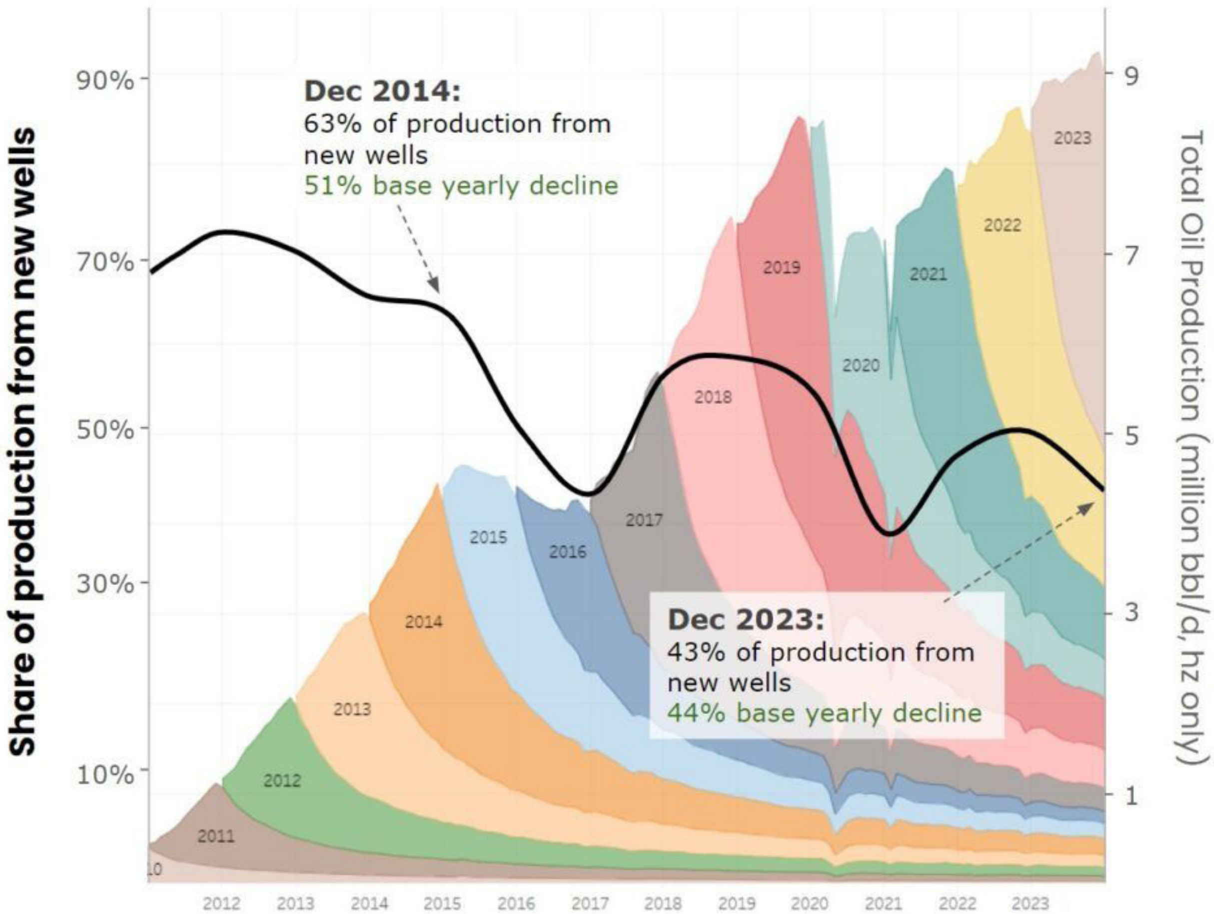
In 2014, shale oil production hit about four million barrels per day, with almost two-thirds coming from new wells. Ten years later, total production is more than double that rate. However, only 43% is from the output of new wells. He also adds that the rate of decline of older shale oil wells moderates even further.

To wit: *"The Bakken was able to post impressive growth in 2023 in part because wells in the play from 2022 and prior only declined 33% in aggregate."*

The bottom line is that shale oil production declines much quicker than traditional wells, but the rate of decline is less than investors fear.

Shale's Shrinking Red Queen?

Each year the base decline rate of US shale gets **milder** as the wedge of **older**, lower-declining wells gets **larger**



Data source: production data collected by Novi Labs from various state agencies and proprietary sources. Data has been filtered to horizontal wells only. For total oil production, each wedge represents production for wells put online that year. Share of production from new wells calculated in December of each year. For more information, visit https://novilabs.com/

novilabs.com

[Continue reading here](#).

The "Great Reset" is dying with electric vehicles ("EV") leading the way down (from Peter St Onge, Ph.D via X)...

Ford just slashed production of its much-hyped electric F-150 after losing $5 billion on EV's.

Volvo's cutting off its EV division.

Apple just announced they're giving up on EV's after plowing $10 billion into unicorn farts.

Sadly, governments are doubling down, with Biden pouring $800 billion of your money into new green projects.

Meanwhile, utilities keep installing "renewables" that drive up rates. Because, unlike EV's, you can't opt out. Until you vote.

Tech companies are going "all in" on nuclear (from *Forbes*)...

In a noteworthy move, Amazon Web Services (AWS) recently acquired Talen Energy's 960MW data center campus in Pennsylvania, which draws power from the neighboring 2.5GW Susquehanna nuclear power station. The $650 million deal is not only a significant investment for AWS but also a clear indicator of a broader trend in the tech industry: companies are increasingly turning to nuclear and renewable energy sources to power their data center operations.

AWS is not alone. MicrosoftMSFT -0.1% has taken a step toward nuclear power as well, signing a deal last year with Helion Energy, a private U.S. nuclear fusion company. Helion is expected to provide Microsoft with electricity after about five years, marking the first such power purchase agreement for fusion energy. While it remains to be seen whether Helion will be able to follow through on its ambitious promise to deliver reliable fusion energy in five years, the mere fact that such a reputable company as Microsoft was willing to sign on to the agreement gives reason to be optimistic.

The trend toward exploring cutting edge energy sources to power their operations extends beyond these two tech giants. Cryptocurrency mining companies, often criticized for their high energy consumption, are also making strides in procuring electricity from nuclear and renewable sources.

Continue reading here.

How to invest in the nuclear renaissance (from MarketWatch)...

Uranium is used as fuel for nuclear power plants and nuclear reactors that produce electricity, and the nuclear industry continues to "build momentum and is, once more, a growth sector," said BCA Research's Peloso, in a note released last week.

"Not a single week goes by without a positive development on the nuclear energy front — from additional nuclear reactors planned and lifespan extension of existing ones, to milestones on taxonomy," he said, with the Declaration to Triple Nuclear Energy signed at the COP28 in Dubai last December standing as one such example. Major countries, including the U.S., pledged to triple nuclear energy capacity globally from 2020 by 2050.

"All the momentum in the nuclear industry keeps fueling the bull case for uranium and the actors along the nuclear fuel cycle or those contributing to it," said Peloso.

In terms of how to approach uranium investing and how much exposure to take depends on the investment horizon and the mandates of investors, he said. The good news, however, is that it has become "somewhat easier for investors to gain exposure to the sector than it was even a few years ago."

'Nuclear renaissance'

Among the different investment vehicles and opportunities available to participate in what Peloso referred to as a "nuclear renaissance" is physical uranium, he said.

"Getting exposure to physical uranium has the best risk-adjusted reward in the nuclear space," partly because the likelihood of seeing much lower uranium prices is "small, but the upside potential is very high," said Peloso.

The current supply deficit and rising demand provide a "floor for uranium prices and make it a lower volatility options bet on the nuclear renaissance," he said.

Still, uranium prices are "fairly sensitive" to geopolitical risks, he said, with countries involved in the uranium supply chain, such as Russia and Kazakhstan, and "tail-risk events" such as the Fukushima Daiichi nuclear power plant disaster in March 2011.

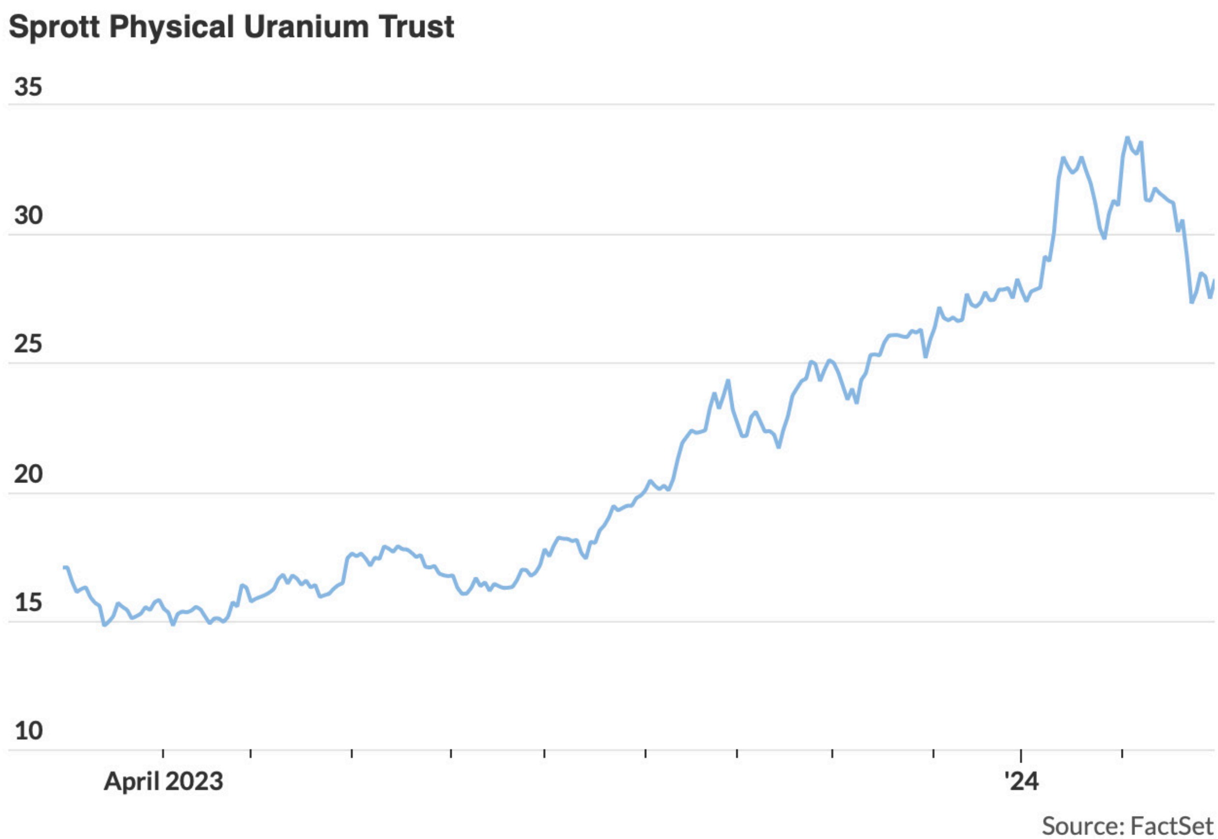
Read: Fukushima's disaster led to a 'lost decade' for nuclear markets. Russia, low-carbon goals can help power a comeback.

While rare, a Fukushima-type disaster could "potentially ruin the positive momentum that the sector is enjoying right now," Peloso told MarketWatch.

Uranium investing

Uranium, given its properties and potential uses, is probably the "most regulated element you can think of," he said, making physical ownership impractical for individual investors.

Instead, investors can gain exposure to the underlying commodity through uranium futures, exchange-traded funds, or publicly-listed companies that invest in the physical metal.



Broadly, ETFs represent an "excellent investment vehicle to gain exposure to uranium or to the nuclear energy theme," said Peloso.

The Sprott Physical Uranium Trust is a physical uranium trust that buys and holds uranium, and it's a highly liquid vehicle, he said.

Sprott Uranium Miners URNM focuses on uranium miners and physical uranium, while the Global X Uranium ETF URA includes companies involved in uranium mining and the production of nuclear components, said Peloso.

He pointed out that there are also roughly 65 publicly-listed uranium miners, made up of three types: explorers, developers, and producers.

“Miners that can bring more supply online and fill the current supply deficit should be massive beneficiaries of the recent jump in demand,” he said, and developers putting new mines into production in the coming cycle will “enjoy big upside as they go from cash consumers to cash producers.”

The most “established and well-known” miners, he said, include Cameco Corp., which is among the largest uranium producers globally, Uranium Energy Corp., which is involved in exploration, extraction, and processing of uranium, and Denison Mines Corp., a Canada-based exploration and development company.

Given its size, and how “integrated” it is to the nuclear fuel cycle,” there is reason to believe Cameco will come out as one of the main beneficiaries of the nuclear renaissance, said Peloso.

Uranium miners, generally “face less risks than other actors in the industry since there is a deficit of uranium supply,” he said.

Meanwhile, he said that Yellow Cake PLC, which specializes in the purchase and storage of uranium oxide, offers exposure to the spot uranium price without the risks attached to exploration, development, or mining, while Uranium Royalty Corp. UROY, -1.62% manages a portfolio of diversified uranium interests, including royalties and streams.

Separately, Constellation Energy Corp, which calls itself America’s largest producer of carbon-free energy, through its mix of nuclear, wind, solar and hydro resources, was among the top stock gainers for the month of February.

Outside of gaining exposure to physical uranium or the nuclear fuel cycle, there aren’t many options for investors, said Peloso. Among the few are NuScale Power Corp. SMR, -7.00%, which to date is the only company with a small modular reactor design approval from the Nuclear Regulatory Commission, he said.

Continue reading here (subscription may be required).

Europe's mild winter has left natural-gas supplies at a record high (from Reuters)...

Europe is on track to end the winter with a record volume of gas in storage, which has pushed futures prices back to pre-crisis levels once inflation is taken into account.

The supply picture has been transformed from two years ago, when traders and policymakers were worried about possible gas shortages following Russia's invasion of Ukraine.

Storage facilities across the European Union and the United Kingdom were 62% full on March 5 compared with an average of 41% full on the same date between 2011 and 2020.

Inventories amounted to 707 terawatt-hours (TWh), which was 277 TWh (+64% or +2.14 standard deviations) above the prior ten-year seasonal average.

The surplus had swelled from 167 TWh (+18% or +1.70 standard deviations) at the start of the winter heating season on October 1.

Winter 2023/24 has mostly been characterised by a strong positive North Atlantic Oscillation, directing strong westerly winds from across the Atlantic into Northwest Europe.

Pressure differentials between the Greenland-Iceland low-pressure area and the Bermuda-Azores high-pressure area have been greater than normal, accelerating warm, moist air into Northwest Europe.

The result has been higher temperatures and wind speeds than average, reducing heating demand and at the same time boosting wind generation, creating a double cut to gas consumption.

So far this winter, heating demand has been 14% below the long-term average in London and 25% below the average at Frankfurt in Germany.

Inventories are on track to end winter around 664 TWh, setting a record and beating previous highs of 629 TWh at the end of winter 2022/23 and 609 TWh at the end of winter 2019/20.

Northwest Europe is about 80% through the heating season so any cold snaps are unlikely to make a significant difference to the outcome at this point.

Continue reading here.

Amid explosive demand, America is running out of power (*from The Washington Post*)...

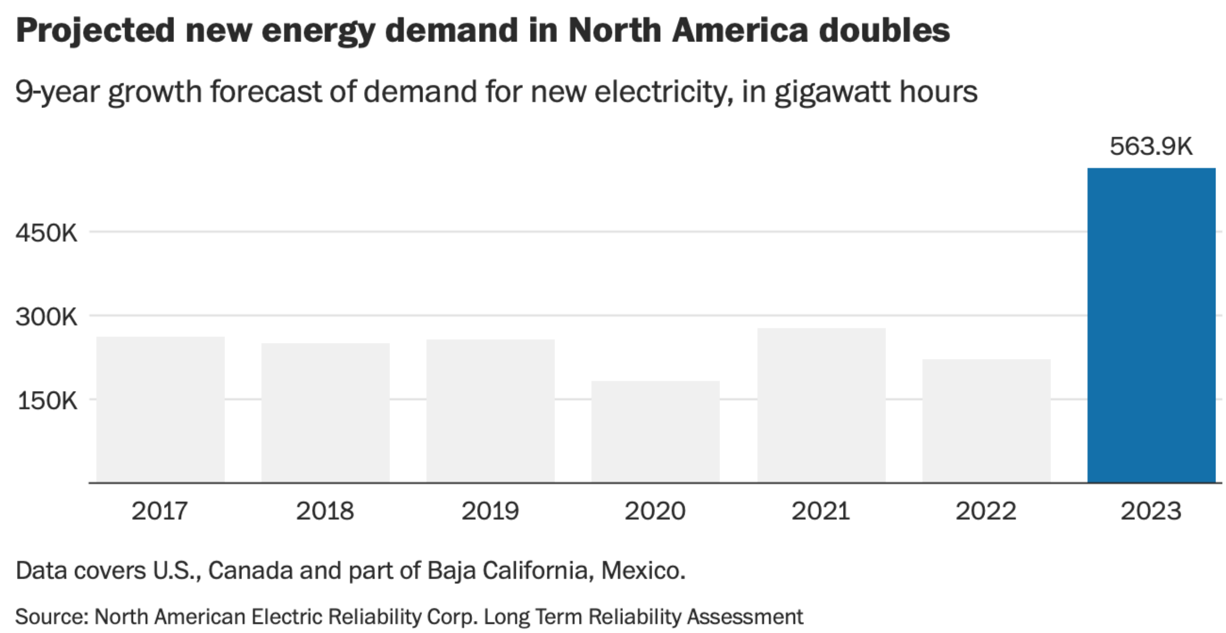
Vast swaths of the United States are at risk of running short of power as electricity-hungry data centers and clean-technology factories proliferate around the country, leaving utilities and regulators grasping for credible plans to expand the nation's creaking power grid.

In Georgia, demand for industrial power is surging to record highs, with the projection of new electricity use for the next decade now 17 times what it was only recently. Arizona Public Service, the largest utility in that state, is also struggling to keep up, projecting it will be out of transmission capacity before the end of the decade absent major upgrades.

Northern Virginia needs the equivalent of several large nuclear power plants to serve all the new data centers planned and under construction. Texas, where electricity shortages are already routine on hot summer days, faces the same dilemma.

The soaring demand is touching off a scramble to try to squeeze more juice out of an aging power grid while pushing commercial customers to go to extraordinary lengths to lock down energy sources, such as building their own power plants.

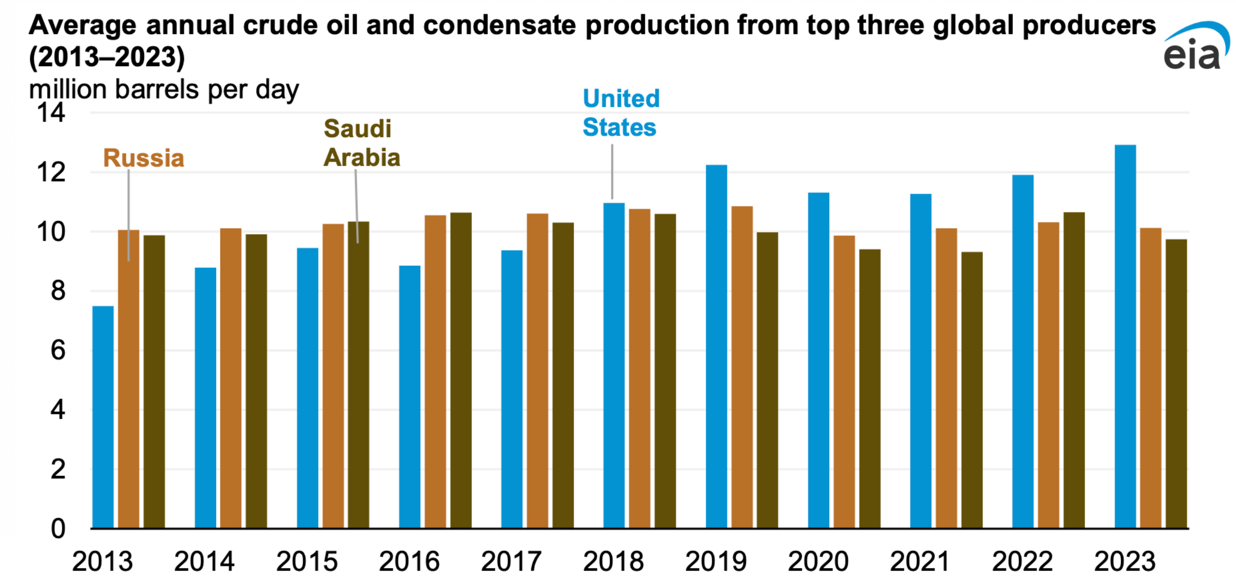
"When you look at the numbers, it is staggering," said Jason Shaw, chairman of the Georgia Public Service Commission, which regulates electricity. "It makes you scratch your head and wonder how we ended up in this situation. How were the projections that far off? This has created a challenge like we have never seen before."



A major factor behind the skyrocketing demand is the rapid innovation in artificial intelligence, which is driving the construction of large warehouses of computing infrastructure that require exponentially more power than traditional data centers. AI is also part of a huge scale-up of cloud computing. Tech firms like Amazon, Apple, Google, Meta and Microsoft are scouring the nation for sites for new data centers, and many lesser-known firms are also on the hunt.

Continue reading here (subscription may be required).

The United States now produces more crude oil than any country, ever (from the U.S. Energy Information Administration)...

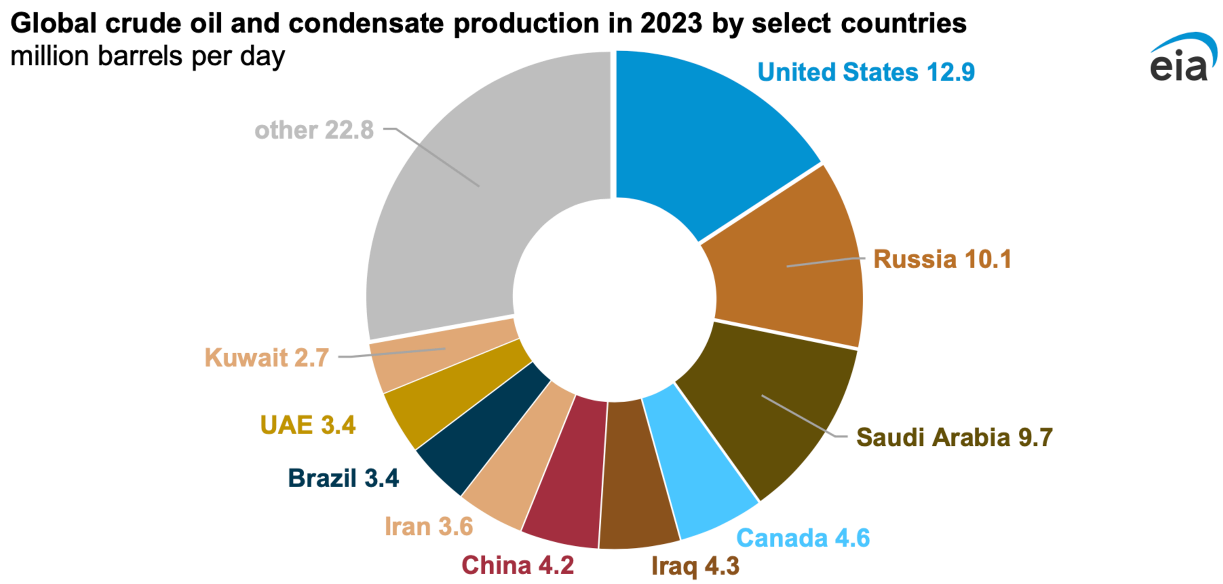


Data source: U.S. Energy Information Administration, International Energy Statistics

The United States produced more crude oil than any nation at any time, according to our International Energy Statistics, for the past six years in a row. Crude oil production in the United States, including condensate, averaged 12.9 million barrels per day (b/d) in 2023, breaking the previous U.S. and global record of 12.3 million b/d, set in 2019. Average monthly U.S. crude oil production established a monthly record high in December 2023 at more than 13.3 million b/d.

The crude oil production record in the United States in 2023 is unlikely to be broken in any other country in the near term because no other country has reached production capacity of 13.0 million b/d. Saudi Arabia's state-owned Saudi Aramco recently scrapped plans to increase production capacity to 13.0 million b/d by 2027.

Together, the United States, Russia, and Saudi Arabia accounted for 40% (32.8 million b/d) of global oil production in 2023. These three countries have produced more oil than any others since 1971 (counting production in the Russian Federation of the Soviet Union prior to 1991), although the top spot has shifted among them over the past five decades. By comparison, the next three largest producing countries—Canada, Iraq, and China—combined produced 13.1 million b/d in 2023, only slightly more than what was produced in the United States alone.



Data source: U.S. Energy Information Administration, International Energy Statistics

Continue reading here.

A fantastic (and *free*) resource for energy investors (from Dalius - Special Situation Investments via X)...

One of the best sources on energy markets "The Palgrave Handbook of International Energy Economics".

Book includes everything from the replacement value of different energy facilities to detailed discussions on S&D dynamics.

Freely available here: https://link.springer.com/content/pdf/10.1007/978-3-030-86884-0.pdf

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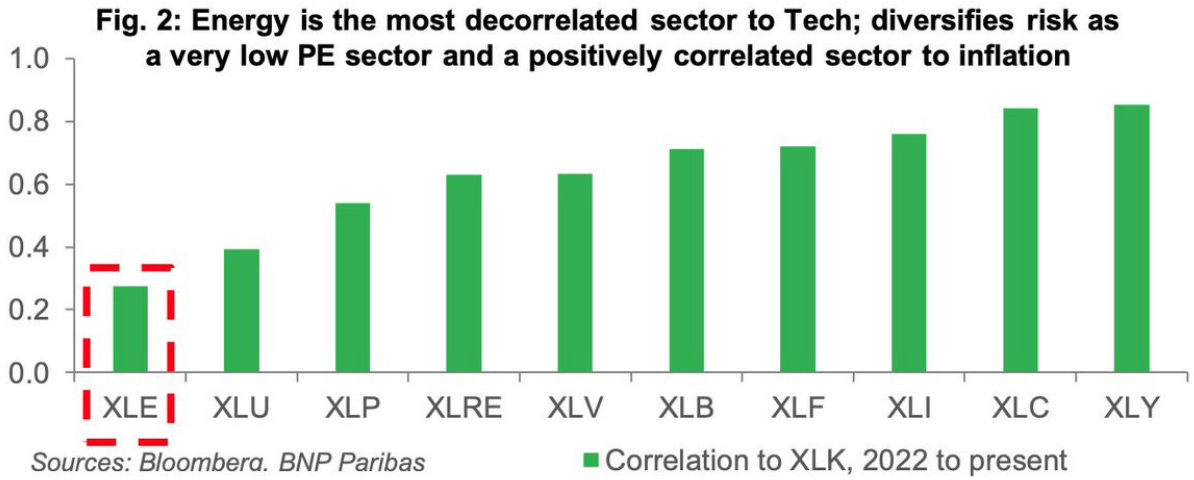
xi

Energy remains an ideal hedge for tech stocks (from Tyler Durden via X)...

"We continue to suggest investors consider diversifying Tech exposure with its least correlated sector, Energy."

BNP Paribas



Energy stocks could ultimately be a huge beneficiary of the AI boom (from John Mihaljevic via X)...

While investors trip all over themselves to get into $NVDA, Sam Altman makes a fascinating point:

"Energy is the hardest part."

Now think about how the market values AI darlings versus energy companies.

Am I the only one who smells opportunity?

EQT CEO Toby Rice warns lack of gas storage will trigger price gyrations (*from Bloomberg*)...

The chief of the largest US producer of natural gas has warned that a lack of pipelines and storage facilities will trigger dramatic price swings in the years ahead, causing them to surge as much 350%.

Gas demand in the US has jumped 50% since 2010, while pipeline and storage capacity have increased just 25% and 10% respectively, EQT Corp. Chief Executive Officer Toby Rice said during an interview at the CERAWeek by S&P Global energy conference in Houston. That leaves the market prone to wild price swings, ranging from today's level of about $1.75 per million British thermal units to as high as $8, Rice said.

"This is the world we live in unless we get serious about getting more infrastructure built," said Rice, whose company last week agreed to buy Mountain Valley Pipeline developer Equitrans Midstream Corp.

Rice is a long-standing and vocal critic of the US regulatory framework and permitting process that he says holds up the construction of new pipeline infrastructure. In November, he warned that a pipeline crunch threatened to trigger an energy crisis. Rice also said in December that falling prices will lead to a slowdown in drilling, and that prices were well below the break even cost of production.

US gas prices have undergone a dramatic collapse this year, plummeting to the lowest in four years and prompting several producers including EQT to slash production.

Another factor threatening to send prices swinging in the other direction is the dozens of coal plants that have closed in the US in recent years. Coal plants have traditionally helped keep gas prices in check because when it gets too expensive, electricity generators turn to coal for more of their power.

"That's no longer an effective lid on prices," Rice said. "So you can see prices run through that and unfortunately start seeing industrial demand destruction driving price. That's sort of the dynamic you saw in 2022 and would leave you with prices close to $8."

Continue reading here (subscription may be required).

Bill Gates-backed company seeks to deploy small modular nuclear reactors in the U.S. (*from The Financial Times*)...

TerraPower, a company founded by Bill Gates, says it plans to start building the first of a new generation of nuclear power plants in the US in June, joining a race with Russian and Chinese rivals to develop and export lower-cost reactors.

Chris Levesque, TerraPower's chief executive, told the Financial Times the company would apply for a construction permit from US regulators this month for its reactor, which is cooled with liquid sodium rather than water.

He said the company's Natrium-branded reactors could be built for about half the cost of standard water-cooled reactors, which have been the cornerstone of the nuclear energy industry since the mid-20th century.

TerraPower, which has raised almost $1bn in private funding, signed an agreement with Emirates Nuclear Energy Corporation in December to explore using Natrium reactors to generate electricity and produce hydrogen in the United Arab Emirates. The company has secured pledges from the US government to provide up to $2bn to complete work at TerraPower's first plant in Kemmerer, Wyoming.

Levesque, a former officer on a nuclear submarine, said construction work near the site of a coal power plant, would begin in June regardless of whether the company received a permit from the Nuclear Regulatory Commission by that date. Much of the initial building work related to non-nuclear activity due to the innovative design of the Natrium reactor, he said, adding that TerraPower planned to bring the plant online in 2030.

Continue reading here (subscription may be required).

OTHER COMMODITIES

The world needs more critical minerals. Governments are not helping (from *The Economist*)...

Mining companies have always mattered. Without the iron ore and copper they unearth, there would be no steel to build with and no wiring to carry electric power. Today miners have an extra responsibility. If the world is to decarbonise, it will need 6.5bn tonnes of metals between now and 2050, according to the Energy Transitions Committee, a think-tank—and not just lithium, cobalt and nickel, the much-talked-about battery metals, but steel, copper, and aluminum, too. Because that output is several times greater than today's capacity, producing it will require miners to invest more and dig faster.

Unfortunately, miners are investing a lot less than they once did, as their latest set of earnings, released this week, confirm. The world's biggest miner, BHP, last year spent less than half of what it did a decade ago. In part that is for sensible reasons: miners are rightly conscious that theirs is a boom-and-bust industry. The last time they splashed out, during the China-led bonanza of 20 years ago, a spectacular crash followed. Markets are volatile. Whereas copper prices remain relatively high, those for cobalt, nickel and lithium have fallen dramatically, as more supply has come on stream. But lately investment decisions have also been tied up in red tape. Governments insist they want to encourage the green transition. Their actions too often say otherwise.

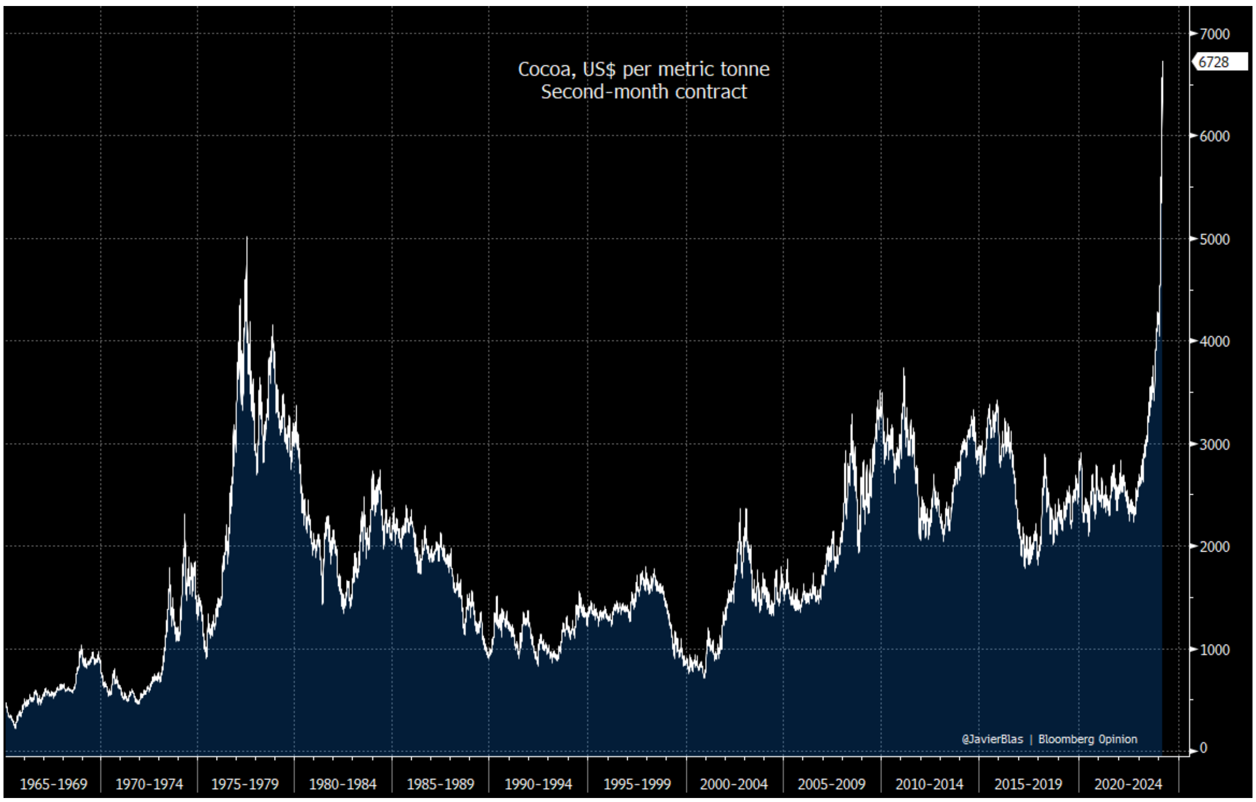
Continue reading here (subscription may be required).

Cocoa prices continued to surge to record highs this month (from Javier Blas via X)...

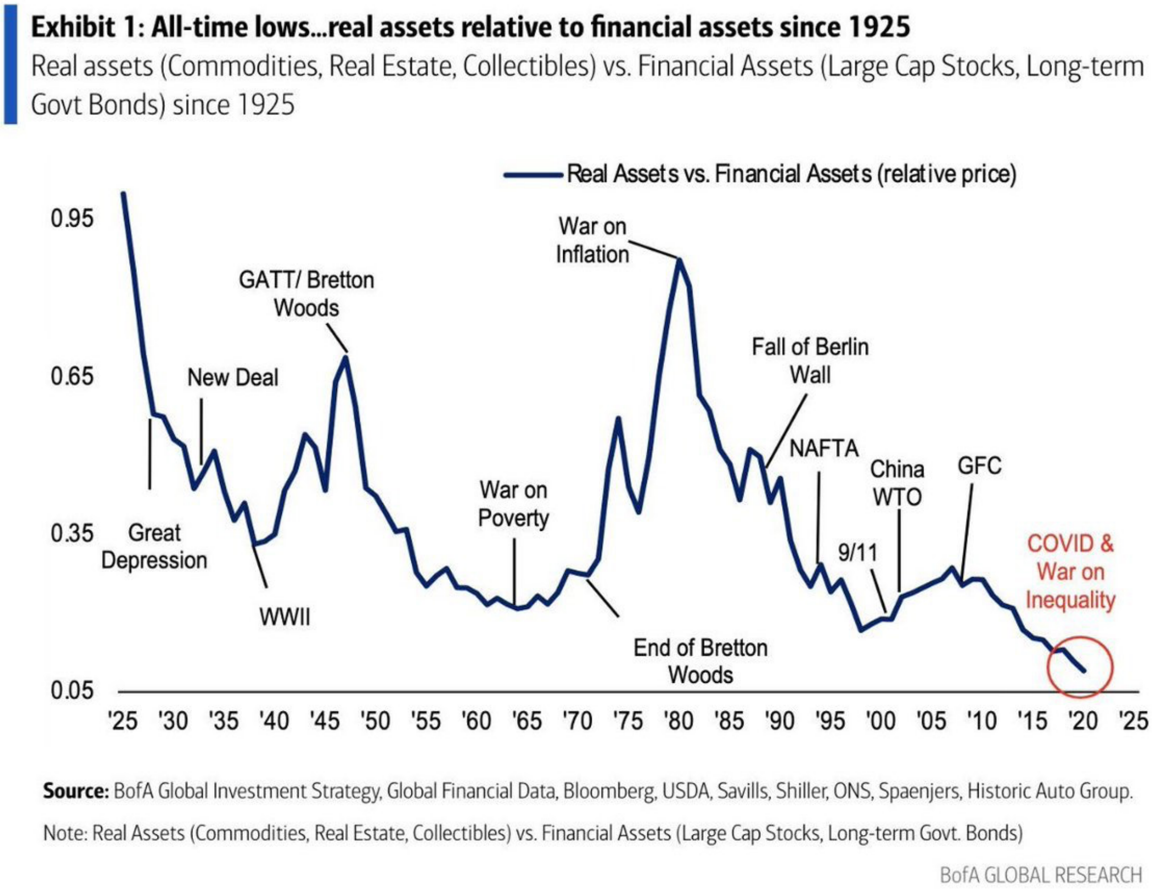
CHART OF THE DAY: The cocoa rally.

Cocoa prices hit a fresh record high, fast approaching the once unthinkable $7,000 per tonne level.

At current levels, we will see soon widespread retail price increases for all kinds of chocolate.

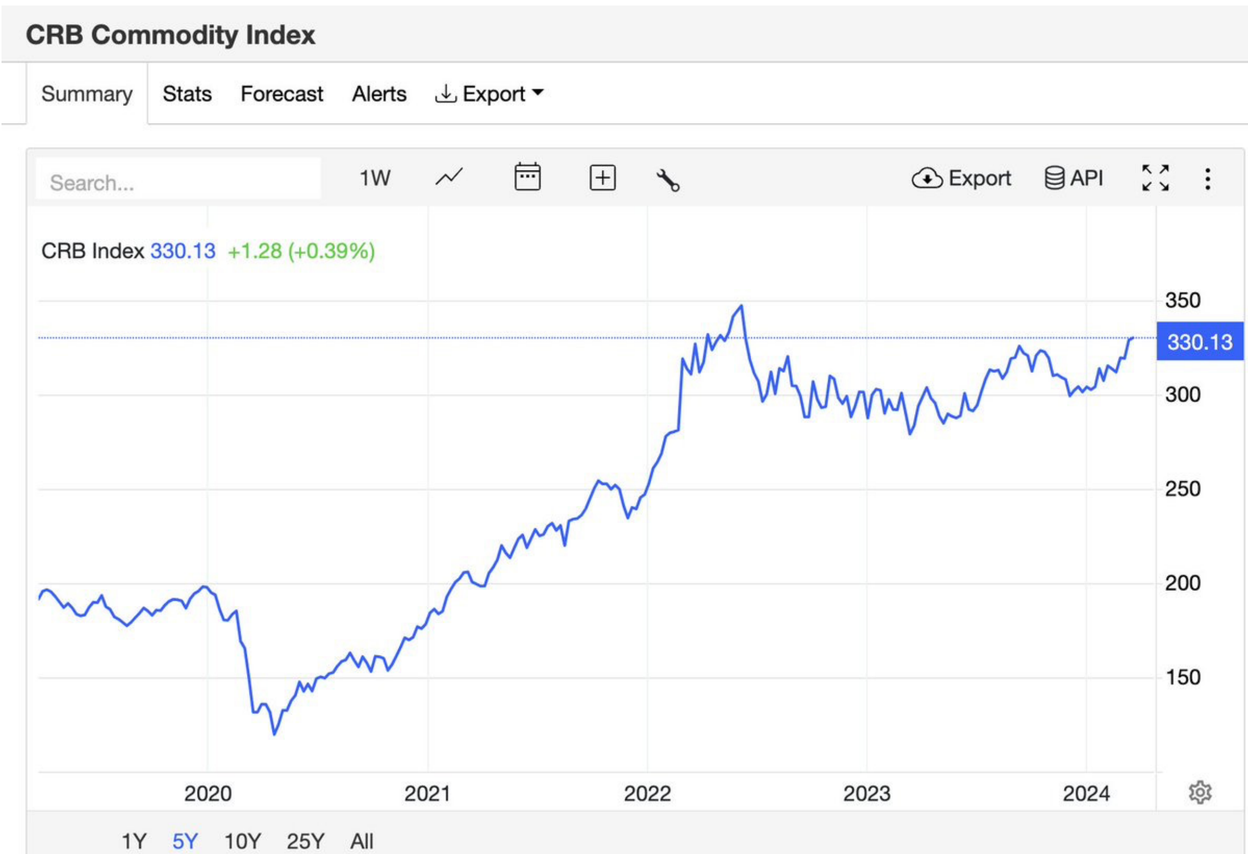


Hard assets are trading at their lowest valuations relative to financial assets since 1925 (from Sean Gibson via X)...



Like gold, the broad commodities index appears to be on the verge of a massive breakout (from Peter Schiff via X)...

Look at this chart of the CRB. Commodity prices are about to rip. This will likely be the biggest commodity bull market since the 1970s. By 2025 #inflation will likely be in double digits, and the first digit may not be a one!



"Dr. Copper" is warning of higher inflation ahead (from Francois Trahan, M²SD via X)...

In recent decades, higher copper prices were not really a big deal because the starting point to a conversation about inflation was usually one where CPI was low and well contained. This development might mean more this time around ... for a short while anyway.

How to solve America's critical minerals problem (from Energy Talking Points by Alex Epstein)...

America’s economy and its national security depend on the secure availability of numerous “critical minerals”—such as lithium, copper, cobalt, and various “rare earth” elements—that, due to their unique chemical properties, are essential for many of today’s leading technologies.

Take cobalt, an important ingredient in the high-tech alloys used in many batteries, jet engines, and permanent magnets. Without a secure supply of cobalt, production of significant portions of high-tech industry and high-performance military equipment are jeopardized.1

To have ample, secure critical minerals, we must:

1) liberate domestic industry to mine and process them cost-effectively

2) encourage friendly trading partners to do the same

3) not artificially drive up demand before supply chains are ready

We are doing the exact opposite.

Continue reading here.

BITCOIN AND CRYPTO

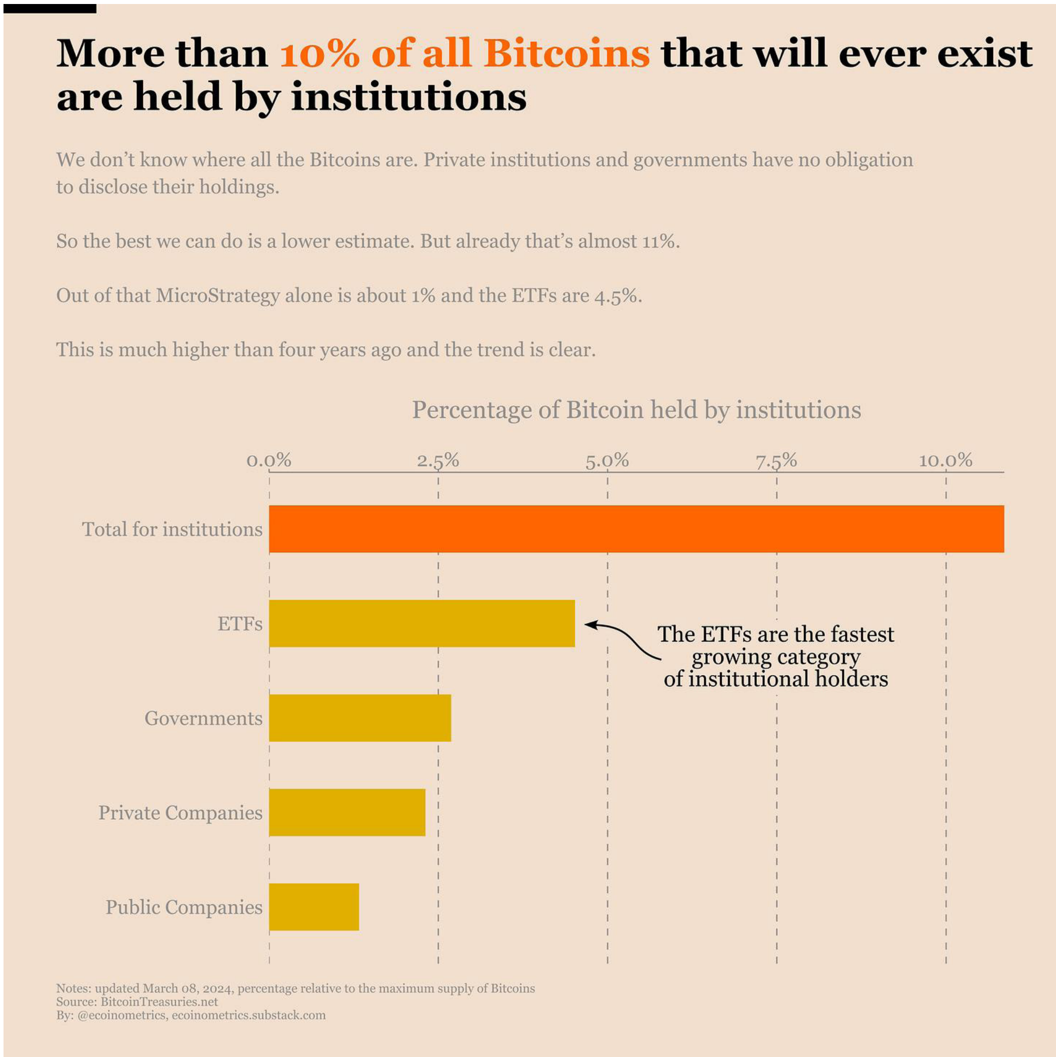
The institutionalization of Bitcoin is now underway (from Ecoinometrics)...

For Bitcoin to become a multi-trillion dollar assets you need the institutional money. There is no way around it.

This is not the cypherpunk dream. But it does the job.

The low estimate, based on public information, is that 11% of the maximum supply of Bitcoins is already held by institutions.

The ETFs alone represent 4.5% and are the fastest growing category of the lot.



Continue reading here.

The mainstream financial media is beginning to take an honest look at Bitcoin (from Alex Gladstein via X)...

This was bound to happen, eventually

@TheEconomist is starting to understand how Bitcoin mining is going to revolutionize electricity access in Africa.

Middle East and Africa | Cryptocurrencies in Africa

Why Africa is crypto's next frontier

Cheap power is fuelling a new sort of mining boom

Powering Virunga's virtual mine IMAGE: AFP

Mar 7th 2024

"BITCOIN MINING is like pouring water on an even floor. It will always go to the lowest point," says Erik Hersman, a tech entrepreneur in Nairobi, Kenya's capital, explaining how the energy-intensive activity of creating, or "mining", the digital currency gravitates to places with the cheapest power costs. Until 2021 the Dead Sea for bitcoin was China, before the government banned it, citing the environmental harm it causes. The proverbial water swiftly flowed to America, with its plentiful supply of cheap energy and deep capital markets. Profits soared. Within months America accounted for a third of global bitcoin production.

Bitcoin miners are making more money than ever before (from Danny Marques | Investing Informant via X)...

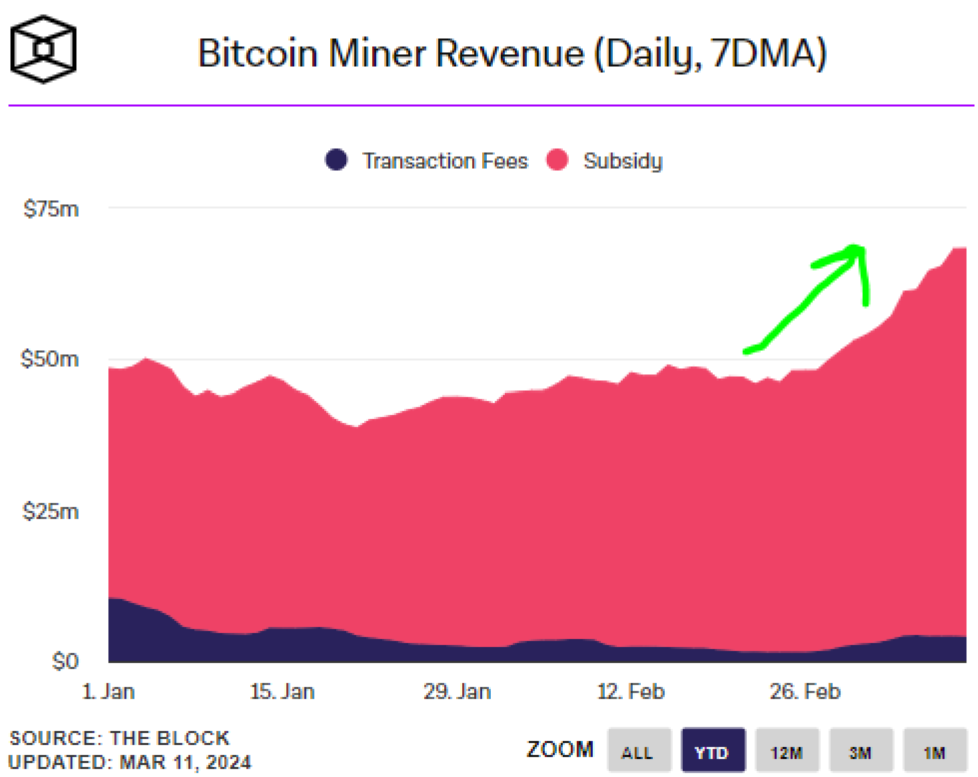
MUST read for all those freaking out on #Bitcoin miners

Miners are making more money than EVER BEFORE from mining. They have the best operating leverage of any BTC proxy (for me) as they are on the front lines of the network. Subsidies, aka their "block rewards" have gone up as Bitcoin price has gone up which means their profit margins are also improving dramatically as price goes up.

Has this reflected in the stock price? No. But are you investing in the business or the stock price?

For now, publicly traded miners performance lag BTC price performance (currently at $72k). Key word: For now.....This offers a good opportunity to evaluate which are still laggards, but will be the most profitable and lean, with highest growth expectations, and place some chips on the table. Historically, this lag ALWAYS occurs in halving cycles, and the discount window can close in the blink of an eye, so don't be shaken out.

They are quite literally more profitable than ever before.



Global asset manager Bernstein: Miners remain best equity proxy as Bitcoin targets $150,000 (from The Block)...

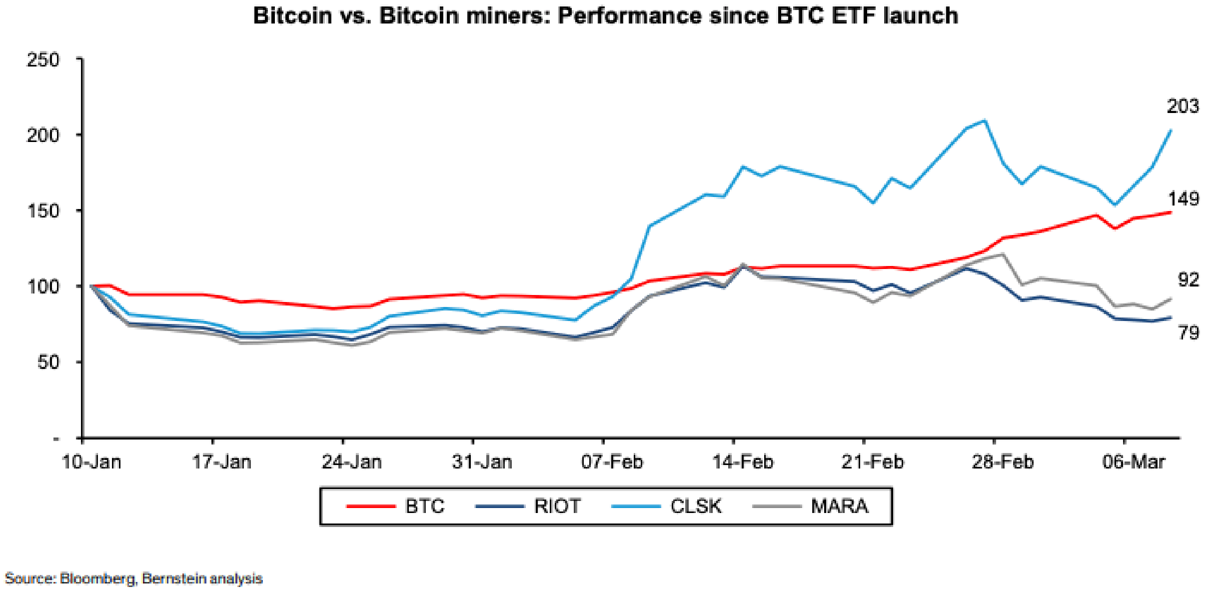
Investing in bitcoin miners is the best equity proxy to bitcoin as the largest cryptocurrency by market cap heads toward $150,000, according to analysts at research and brokerage firm Bernstein.

"Investors merely look at daily correlation of Bitcoin miners, only during days when they see bitcoin rallying," Bernstein analysts Gautam Chhugani and Mahika Sapra wrote in a note to clients on Monday. "This selective periodic view is incomplete."

The analysts noted that miners almost always outperform bitcoin during bull markets and underperform during bear markets. "Investors have to take a through-cycle view and for us, we are still mid-way into the 2024-25 cycle and see every window of miner weakness as a buying opportunity," they said.

Chhugani and Sapra argued that bitcoin miner stocks are retail-dominated, with institutions largely avoiding bitcoin proxies. "Traditional equity investors remain skeptical and still approach crypto with a rear-view bias," they said. "Bitcoin miners' under-performance during strong bitcoin days are opportunity windows, as bitcoin sucks away retail liquidity from miners."

With bitcoin climbing to all-time highs above $72,000 today, Bernstein's analysts expect institutional interest in bitcoin-related equities to awaken, with miners set to be the largest beneficiaries.



Bitcoin vs Bitcoin miners since U.S. spot ETFs launch. Image: Bernstein.

Riot Platforms and CleanSpark to benefit most

The Bernstein analysts said they were particularly focused on Riot Platforms and CleanSpark stocks, suggesting that at current bitcoin price levels and above — even if their production costs were to double after the halving — Riot and CleanSpark would generate around 70% and 60% gross profit margins, respectively. "Any reduction of miner capacity post halving (we estimate 10-15% would shut down), would lead both RIOT and CLSK to gain relative market share," they added.

Bitcoin halvings are programmed to occur automatically every 210,000 blocks — roughly every four years. The next halving event, expected in April, will see the reward subsidy for miners on the network drop from 6.25 BTC to 3.125 BTC per block. However, they continue to earn additional transaction fees for each block mined.

Furthermore, as activity in the Bitcoin ecosystem builds up through the development of additional Layer 2/sidechain solutions, DeFi and NFTs, the analysts expected the current 5% of miner revenue generated from Bitcoin fees to rise to a sustainable 15%.

'More convinced' about $150,000 bitcoin price target

Though bitcoin is already trading past its prior $69,000 all-time high, moving into price discovery, Chhugani and Sapra expect a further breakout post-halving, with the analysts now "more convinced" about their $150,000 bitcoin price target.

The analysts said they had built institutional flows into their estimates to arrive at the price target — initially expecting $10 billion of inflows this year following the launch of spot bitcoin ETFs in the U.S. on Jan. 11 and another $6 billion in 2025.

However, net inflows have already crossed $9.5 billion, with an average run rate of approximately $370 million daily. If this continues, the spot bitcoin ETFs will surpass Bernstein's 2025 estimates within 166 trading days.

Continue reading here.

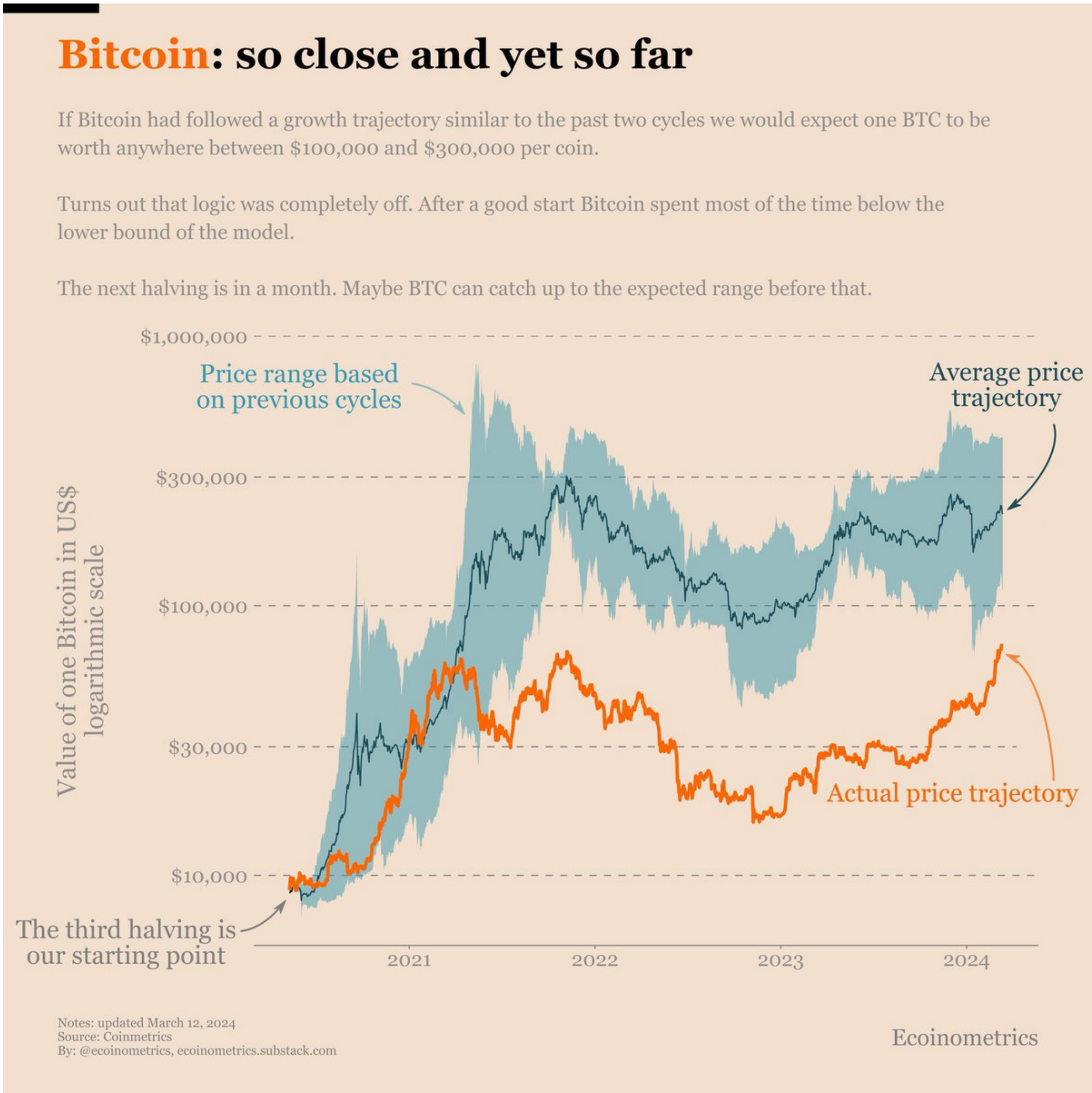
This classic indicator suggests the Bitcoin bull market has further to run (from On-Chain College via X)...

The Bitcoin Mayer Multiple is currently at 1.77

Historically, the MM has exceeded the 2.4 level during bull cycles

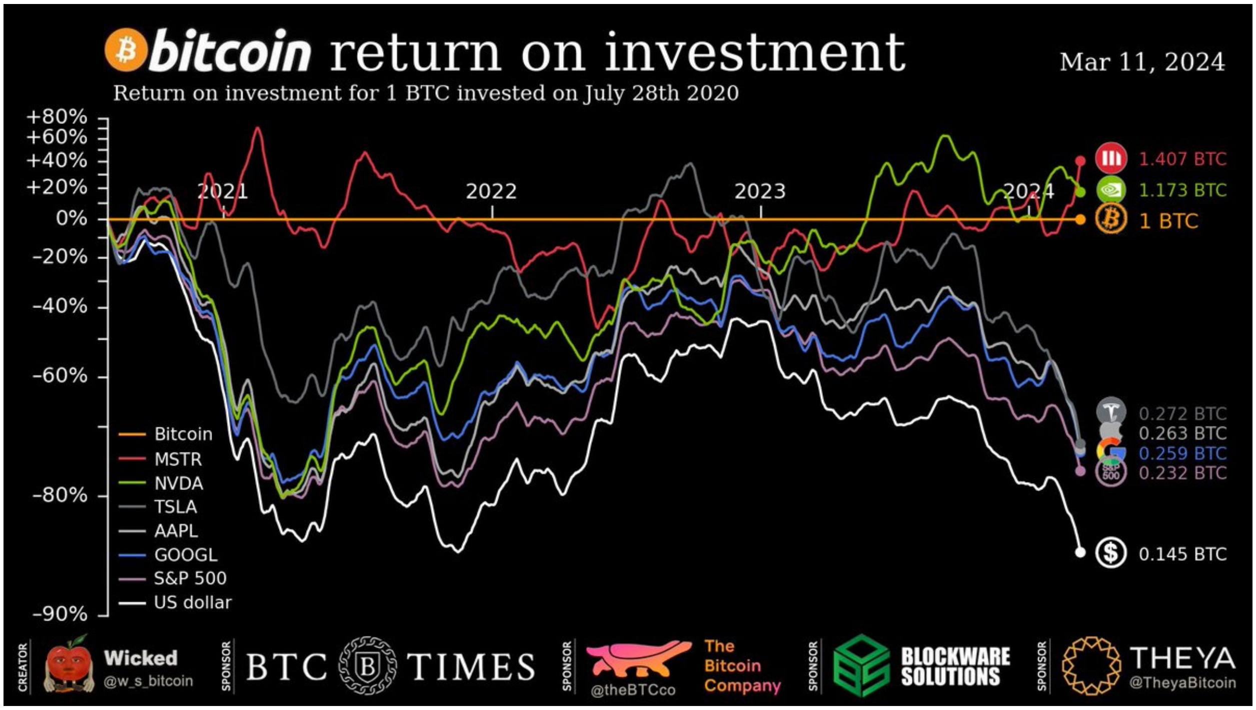
COVID-19 lockdowns appear to have stifled the last Bitcoin bull market (from Jordan Lindsay via X)…

The global lockdowns in March 2020 played a significant role in diminishing last cycles's performance.



MicroStrategy (MSTR) has outperformed Bitcoin and the Magnificent 7 since it began purchasing Bitcoin in 2020 (from Wicked via X)...

On July 28th, 2020, @MicroStrategy announced its plans to purchase #bitcoin. Since then, $MSTR has performed exceptionally well in terms of #bitcoin.



Coinbase Global (COIN) may be following in MicroStrategy's footsteps (from Bitcoin Magazine via X)...

JUST IN: Coinbase proposes private offering of $1.0 billion of convertible senior notes due 2030.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 8-K

CURRENT REPORT
Pursuant to Section 13 or 15(d)
of the Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): March 12, 2024

Coinbase Global, Inc.
(Exact name of registrant as specified in its charter)

A $1.7 trillion asset manager filed with the SEC to buy Bitcoin this month (from MartyParty via X)...

Breaking: $1.7t Patient Capital Management just filed with the @SECGov to buy #Bitcoin ETFs with up to 15% of its Opportunity Trust Fund.

15% is the new institutional fund allocation number. That's huge.

ADVISOR MANAGED PORTFOLIOS
(the "Trust")

Patient Capital Management

Patient Opportunity Trust
(the "Fund")

March 11, 2024

Supplement to the Fund's Prospectus
and Statement of Additional Information
dated December 15, 2023

Effective immediately, the Fund may seek exposure to bitcoin by investing up to 15% of its net assets in exchange traded products that are registered under the Securities Act of 1933 and invest primarily in bitcoin ("Bitcoin ETPs"). Therefore, all references to Grayscale Bitcoin Trust throughout the Prospectus and Statement of Additional Information are replaced with references to Bitcoin ETPs. Previously, the Fund's exposure to bitcoin was limited to investment in Grayscale Bitcoin Trust, which was a privately offered investment vehicle whose shares were also available over-the-counter, and which recently converted to a Bitcoin ETP.

In addition to replacing references to Grayscale Bitcoin Trust with references to Bitcoin ETPs, the following risk factor replaces "Bitcoin risk" and "Cryptocurrency regulatory risk" in the principal risk sections of the Prospectus:

Bitcoin ETP risk. The value of the Fund's indirect investment in bitcoin through Bitcoin ETPs is subject to fluctuations in the value of bitcoin. Bitcoin is not pegged to a currency nor the value of any underlying asset; its value is determined by the supply of and demand for bitcoin in the global market for the trading of bitcoin. The global supply of bitcoin consists of transactions on electronic bitcoin exchanges. The electronic bitcoin exchanges are not subject to any government regulation or oversight. Pricing on bitcoin exchanges and other venues can be volatile and can adversely affect the value of the exposure to bitcoin. Currently, there is relatively small use of bitcoin in the retail and commercial marketplace in comparison to the relatively large use of bitcoin by speculators, thus contributing to price volatility that could adversely affect the Fund's investment in Bitcoin ETPs. Bitcoin transactions are irrevocable, and stolen or incorrectly transferred bitcoin may be irretrievable. As a result, any incorrectly executed bitcoin transactions could adversely affect the value of the Fund's investment in Bitcoin ETPs.

Cryptocurrency generally operates without central authority (such as a bank) and is not backed by any government; therefore, as a cryptocurrency, bitcoin is not subject to the same degree of regulation as are registered U.S. securities. The reporting, accounting and

auditing standards for bitcoin may differ from the standards for registered U.S. securities. Due to the unregulated nature and lack of transparency surrounding the operations of digital asset platforms, which may experience fraud, manipulation, security failures or operational problems, as well as the wider bitcoin market, the value of bitcoin and, consequently, the value of the Fund's investment in Bitcoin ETPs may be adversely affected.

Countries, including the U.S., in the future may restrict or outlaw the acquisition, use, or sale of bitcoin, and regulation in the U.S. is still developing. Ongoing and future regulatory actions may alter, perhaps to a materially adverse extent, the nature of an investment in cryptocurrency generally. Depending on its characteristics, a digital asset may be considered a "security" under the federal securities laws. The test for determining whether a particular digital asset is a "security" is complex and difficult to apply, and the outcome is difficult to predict. A determination that cryptocurrency or any other digital asset is a "security" may adversely affect the value of the digital asset.

The Fund will indirectly bear its proportionate share of management fees and other expenses that are charged by Bitcoin ETPs in addition to its own direct expenses and will pay brokerage commissions in connection with the purchase and sale of shares of Bitcoin ETPs. Like other exchange-traded products, the shares of Bitcoin ETPs may be bought and sold in the secondary market and may trade at a premium or discount to their net asset value ("NAV"). This risk is heightened in times of market volatility, periods of steep market declines, and periods when there is limited trading activity in the secondary market, in which case such premiums or discounts may be significant and the bid-ask spread could widen. Although the shares are listed for trading on an exchange, it cannot be assumed that an active trading market for the shares will be maintained. The lack of an active trading market for the shares may result in limited market liquidity and losses when selling the shares.

In addition, Bitcoin ETPs have a limited number of financial institutions that may act as authorized participants ("APs") and there may be a limited number of market makers and/or liquidity providers in the marketplace. To the extent that (i) APs exit the business or otherwise become unable to process creation and/or redemption orders and no other APs step forward to perform these services, or (ii) market makers and/or liquidity providers exit the business or significantly reduce their business activities and no other entities step forward to perform such functions, shares may trade at a material discount to NAV, the bid-ask spread could widen, and shares could face trading halts and/or delisting.

Furthermore, the inability of Bitcoin ETPs to facilitate in-kind creations and redemptions of shares could have adverse consequences for the performance of Bitcoin ETPs. The use of cash creations and redemptions, as opposed to in-kind creations and redemptions, may adversely affect the arbitrage transactions by APs intended to keep the price of Bitcoin ETPs' shares

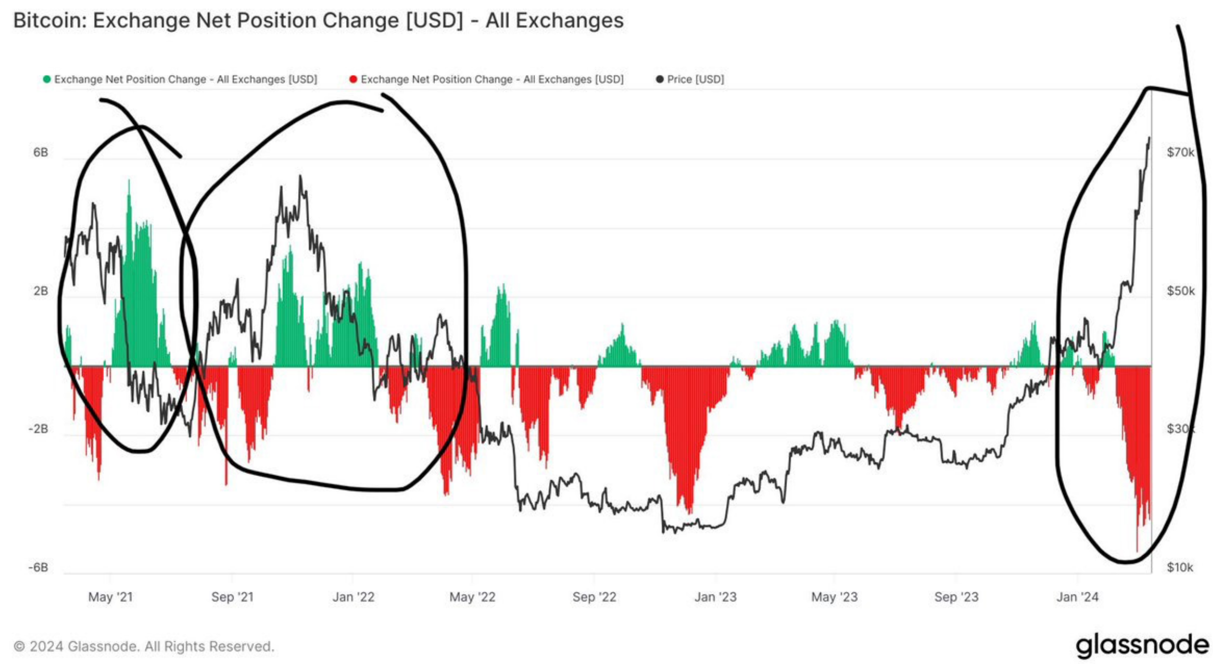
This Bitcoin rally has been different than prior cycles so far (from Bitcoin Munger via X)...

Continue to see signs that "this time is different"

Behaviorally this market has changed.

Coins were sent to exchanges in past runs, now on this run, coins are leaving exchanges.

Do with this info as you wish.



Why an Ethereum ETF may be more likely than consensus believes (from DCinvestor via X)...

i'm not going to tell you it's a done deal, but here are the ETH ETF facts as i see them:

- CFTC has declared ETH to be a commodity and previous SEC chairs have also

- ETH has the CME futures with sufficient liquidity and years of runtime

- ETH has futures-based ETFs

- no other crypto-assets have these attributes except for BTC and ETH

- BTC ETF already paved the legal precedent for a spot ETF in court

- Gary keeps losing crypto cases and in increasingly dramatic fashion each time, with the SEC being sanctioned for misconduct in the Debt Box case in US District Court just yesterday

- Gary can't politically afford another capricious enforcement action he knows he can't win

- Fidelity yesterday adds staking income to their ETF (likely not payable to customers at first, but still) as maybe something they are willing to give up in negotiations with the SEC as a face-saving maneuver allowing for approval

so while it's not certain, most people here have priced the ETF at ZERO probability over the past week

this seems like an overreaction, and also like an opportunity

tbd, but ETF in May or soon thereafter seems very much on the table

The world's largest pension fund is reportedly exploring Bitcoin as an investment (from CNBC)...

Japan's government pension fund on Tuesday said it is requesting information on "illiquidity assets" such as bitcoin, as part of research into potential new investments.

The Government Pension Investment Fund (GPIF) of Japan, the world's largest pension fund by assets under management on several different rankings, said it is looking for "basic information" on illiquid assets other than those in which it already invests.

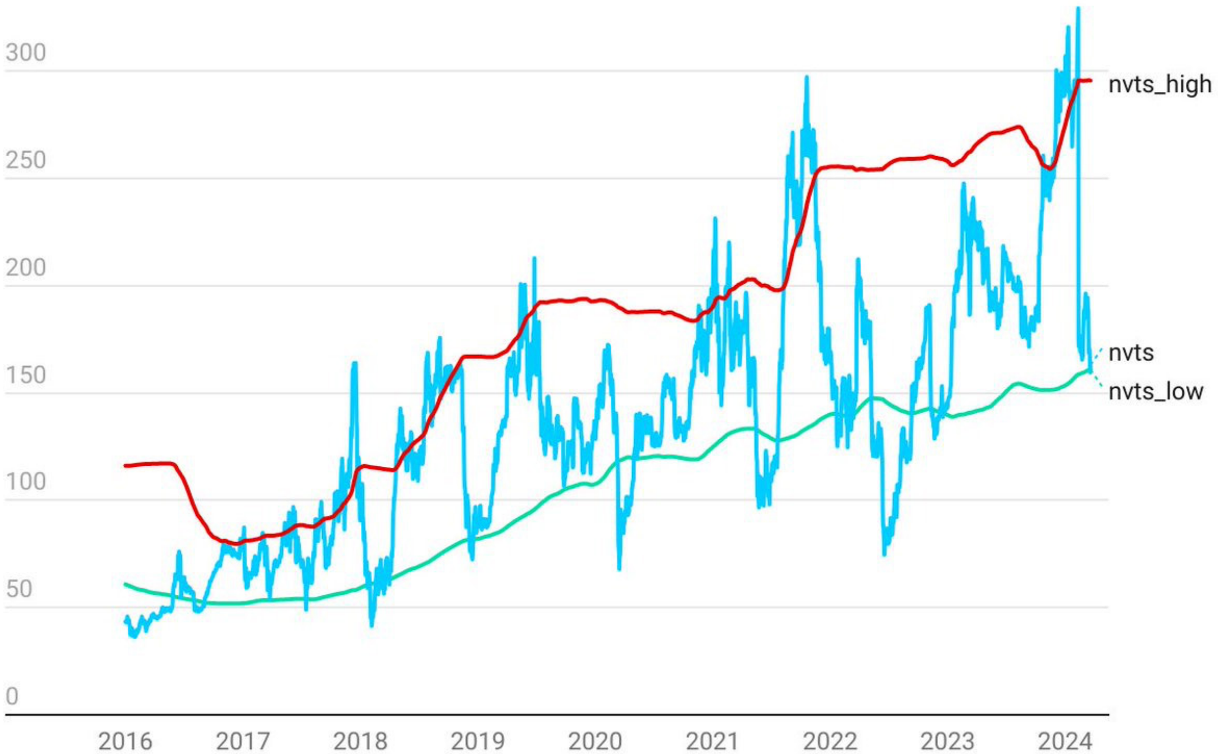
GPIF said it currently puts funds in domestic and foreign bonds and stocks, real estate, infrastructure and private equity. It is now looking for information about other assets such as forests, farmland, gold and bitcoin and how these might be incorporated into the portfolio of pension funds.

Continue reading here.

The Bitcoin network is as undervalued today as it was at $16,000 based on transaction value throughput ([from Charles Edwards via X](#))...

Dynamic Range NVT

NVT is often called "Bitcoin's PE Ratio", it is the ratio of on-chain transactions to market cap. The use of dynamic range bands here helps to identify regions of under- and over-valuation (green/red). Read more: capriole.com/bitcoin-valuation-using-dynamic-range-nvt-signal

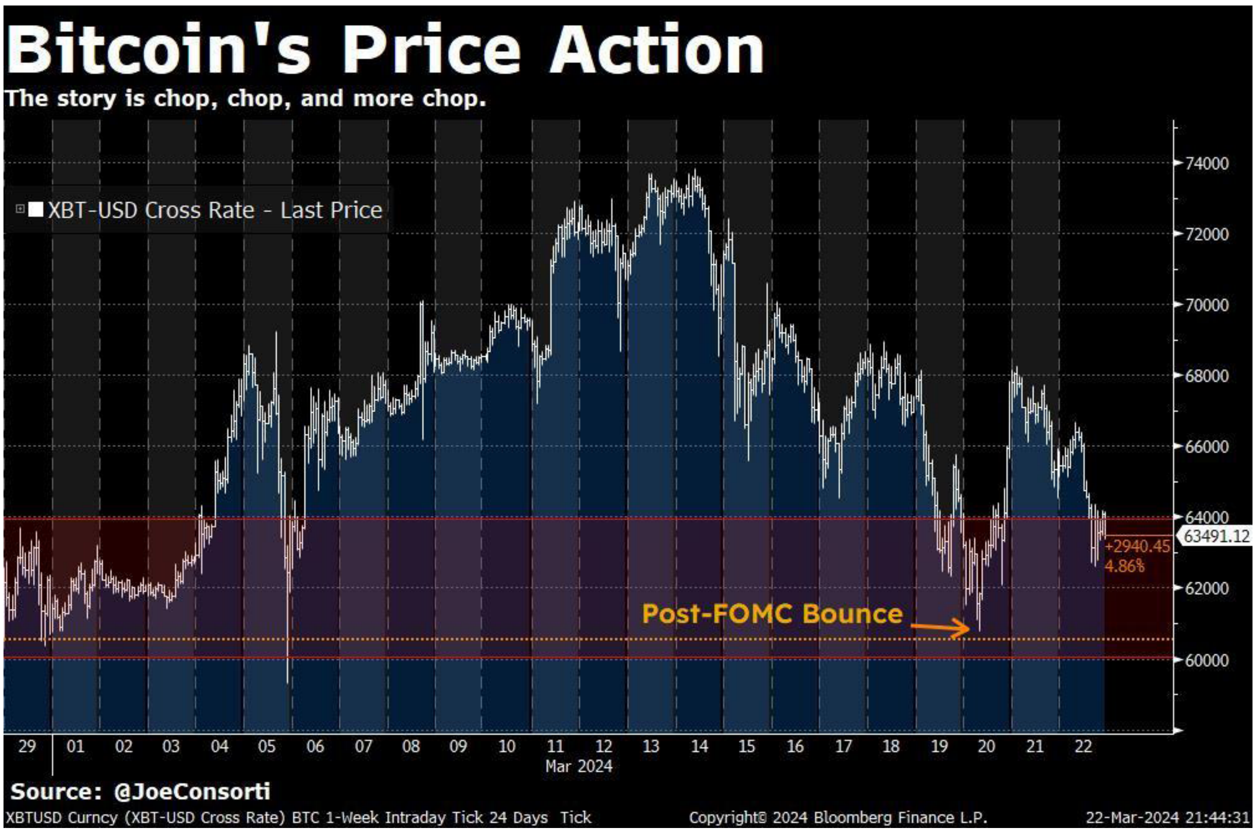


Source: Capriole Investments • Created with Datawrapper

Bitcoin ETFs just saw their first big week of outflows since approval earlier this year (from The Bitcoin Layer)...

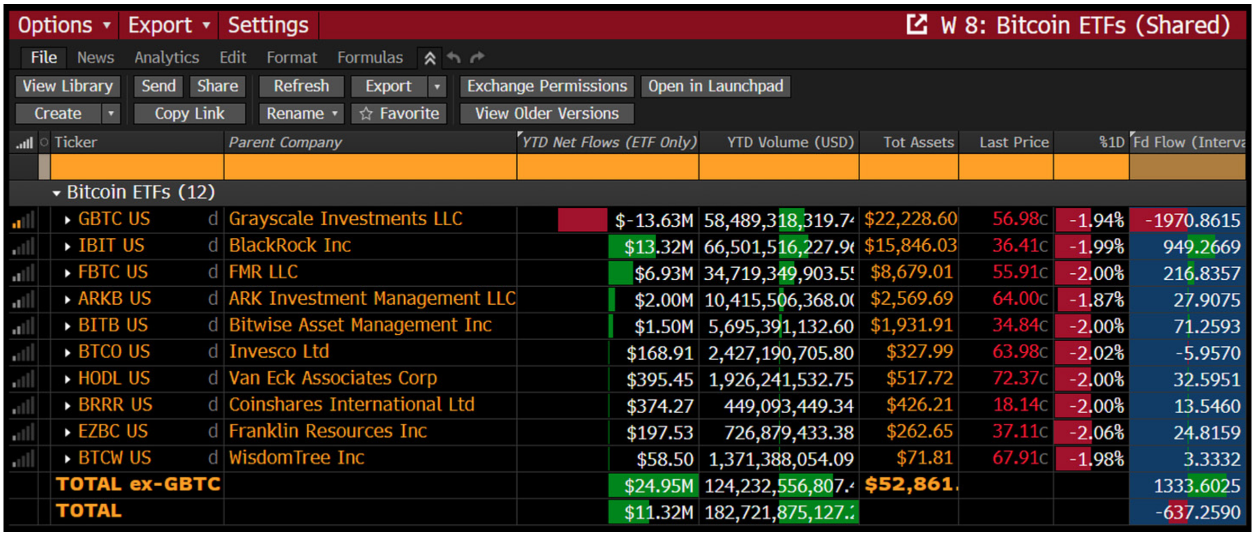
Consolidating in a bull market

Bitcoin has had a very choppy week, ending $5,000 lower than it started and closing our Friday's trading at the $63,000 mark. The story of the bull so far has been chop, chop, chop, enough to make Gordan Ramsay blush. Consolidation is par for the course in a bull market, as profit-takers trade places with dip-buyers. Bitcoin has a strong support range in the low-$60k range to gather steam before the bull market can chug onward:



GBTC liquidation from Gemini bankruptcy and Gemini Earn

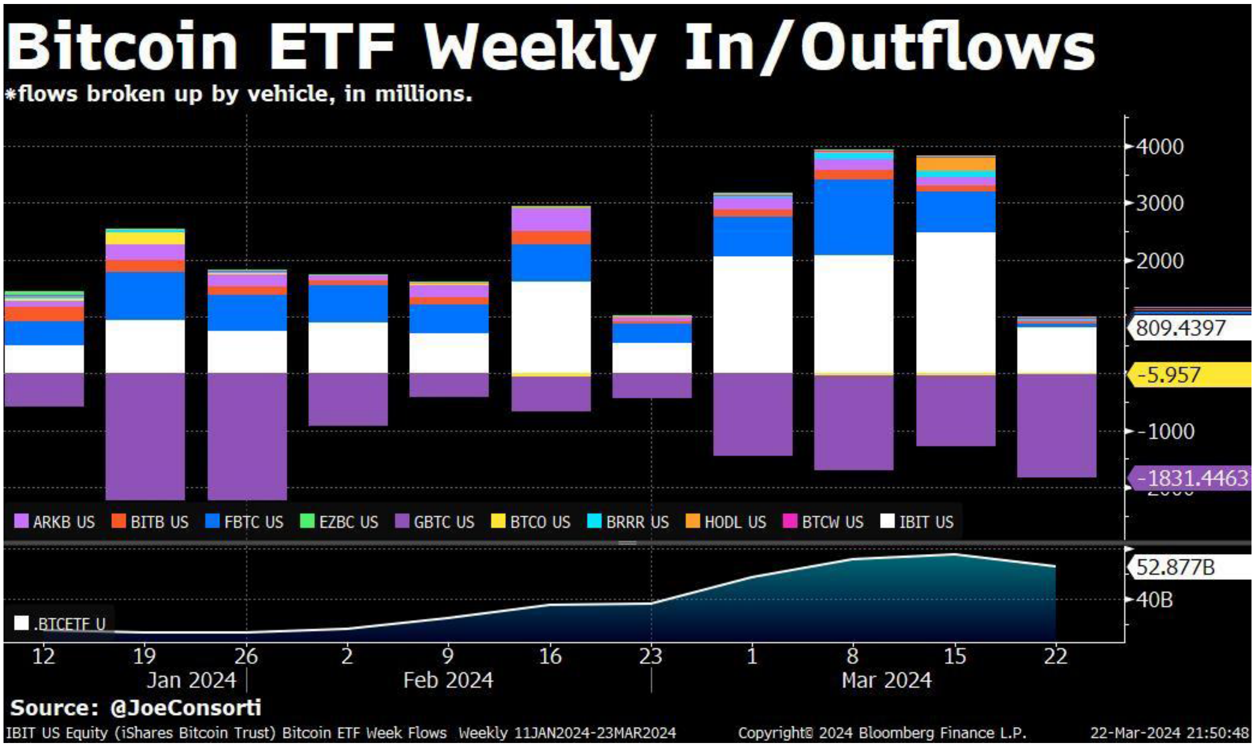
The S&P 500 was up over 200 points this week, so what gives for bitcoin? The first part of the answer has to do with forced selling of GBTC in bankruptcy proceedings, which has caused all of the spot bitcoin ETFs to have their first week of net outflows since January at -$637.5 million, highlighted in blue in the far right column:



Options ▾ Export ▾ Settings — W 8: Bitcoin ETFs (Shared)

Ticker		Parent Company	YTD Net Flows (ETF Only)	YTD Volume (USD)	Tot Assets	Last Price	%1D	Fd Flow (Interva
Bitcoin ETFs (12)								
GBTC US	d	Grayscale Investments LLC	$-13.63M	58,489,318,319.7	$22,228.60	56.98c	-1.94%	-1970.8615
IBIT US	d	BlackRock Inc	$13.32M	66,501,516,227.9	$15,846.03	36.41c	-1.99%	949.2669
FBTC US	d	FMR LLC	$6.93M	34,719,349,903.5	$8,679.01	55.91c	-2.00%	216.8357
ARKB US	d	ARK Investment Management LLC	$2.00M	10,415,506,368.0	$2,569.69	64.00c	-1.87%	27.9075
BITB US	d	Bitwise Asset Management Inc	$1.50M	5,695,391,132.60	$1,931.91	34.84c	-2.00%	71.2593
BTCO US	d	Invesco Ltd	$168.91	2,427,190,705.80	$327.99	63.98c	-2.02%	-5.9570
HODL US	d	Van Eck Associates Corp	$395.45	1,926,241,532.75	$517.72	72.37c	-2.00%	32.5951
BRRR US	d	Coinshares International Ltd	$374.27	449,093,449.34	$426.21	18.14c	-2.00%	13.5460
EZBC US	d	Franklin Resources Inc	$197.53	726,879,433.38	$262.65	37.11c	-2.06%	24.8159
BTCW US	d	WisdomTree Inc	$58.50	1,371,388,054.09	$71.81	67.91c	-1.98%	3.3332
TOTAL ex-GBTC			$24.95M	124,232,556,807.	$52,861.			1333.6025
TOTAL			$11.32M	182,721,875,127.				-637.2590

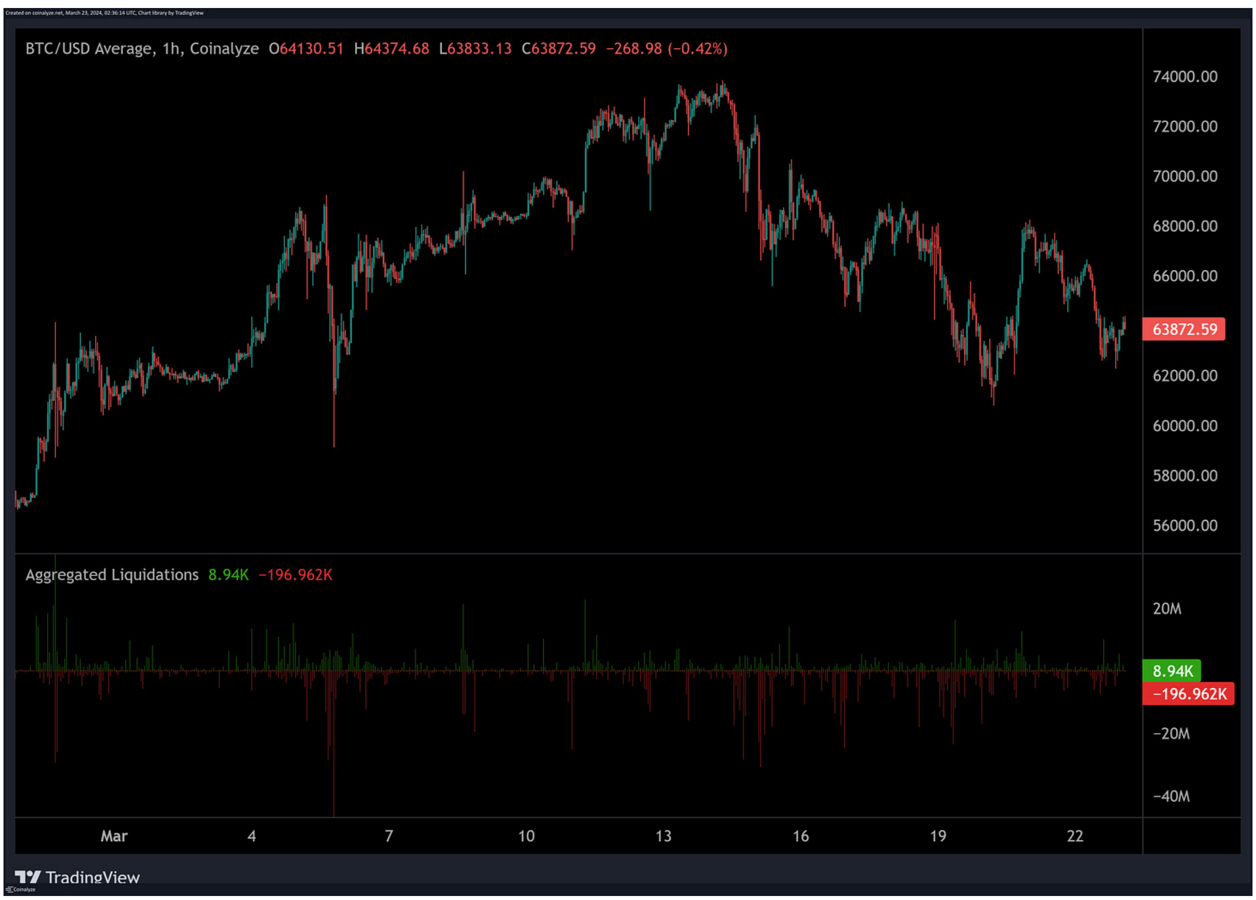
Not a bad start for Q1. This shift in the ETFs started at the end of February when a judge approved the sale of both Gemini and Genesis' GBTC holdings totaling 65.9 million shares of GBTC, or 17% of its total supply. Genesis, the now bankrupt lender is liquidating all of its GBTC, while Gemini is merely selling its GBTC and rotating into BTC as it unwinds the collateral for its defunct Earn product—so realistically, only half of these GBTC sales are impacting bitcoin's spot price. The outflows are also in dollar terms in the charts I've created, so considering the price fell 8% this week and what outflows have occurred have been largely a result of bankruptcy proceedings, spot bitcoin ETF owners are holding the line very well, albeit with a minor reduction in inflows to the other vehicles, which you can see here:



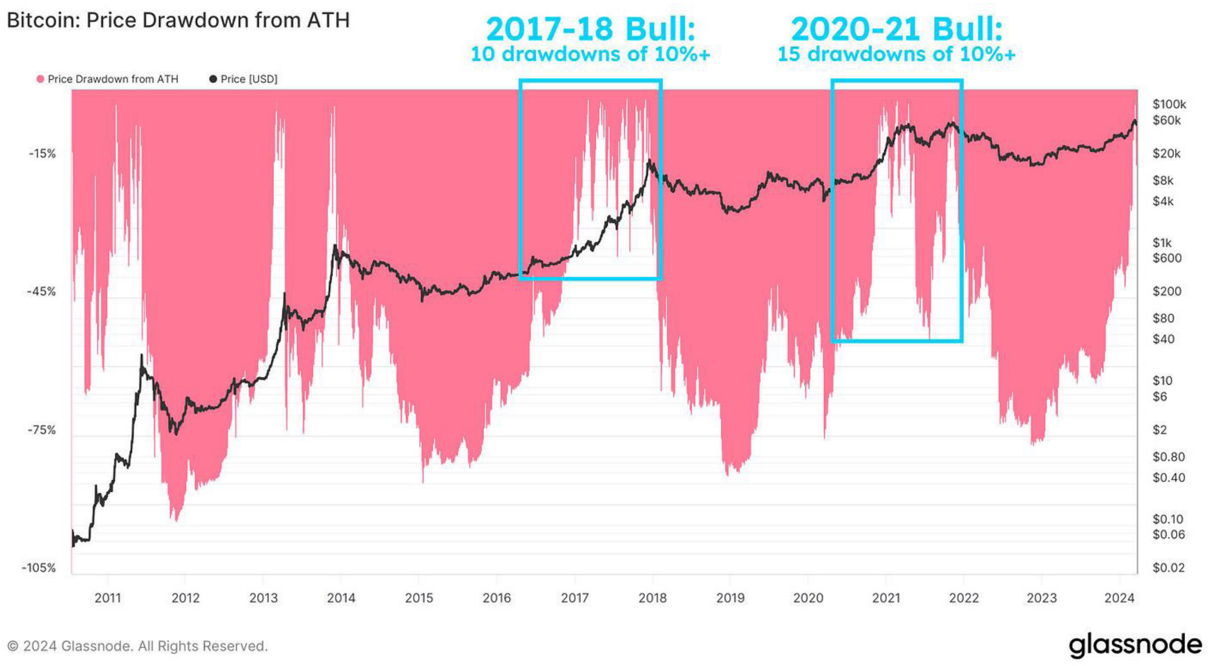
According to Bloomberg's Senior ETF Analyst Eric Balchunas, boomers are an investor class which heavily contribute to ETF flow and tend to "get it right." Boomers, although not all ETF buyers are boomers, dumped $167 billion into ETFs in 2008 when SPY was down 35% and $600 billion in 2021 when SPY was down 17%. Generally, 401k contributions increase when the market is down, they don't fall, and this point of observation backs that up.

Bitcoin drawdowns may be larger given its high market beta, but this is a mature investing class that knows what they're getting into, and capitalizes on dips rather than capitulating. It is actually the bitcoin owners who tend to be more flighty, at least the short-term holders who make up large amounts of bull market liquidity.

Selling pressure is not coming from a blowout in derivatives either. Derivatives still have a long bias with positive funding rates across the board, but short and long liquidations in both the options and futures markets are more or less balanced, and there have been less than $100 million in daily liquidations in futures, which is low:



Selling isn't coming from derivatives land, and it is not coming from these ETFs in a meaningful enough volume to send the price tumbling 15%, so who is selling? Occam's razor: we can deduce the selling is coming from profit-takers. Like in every bull market, we'll endure several consolidation phases before moving higher… I've made this clear chart to illustrate it: bitcoin's last two bull runs have had between 10 and 15 drawdowns of 10% or more. We are on 10%+ drawdown number two or three of this bull run, so there's plenty of air left in the tires

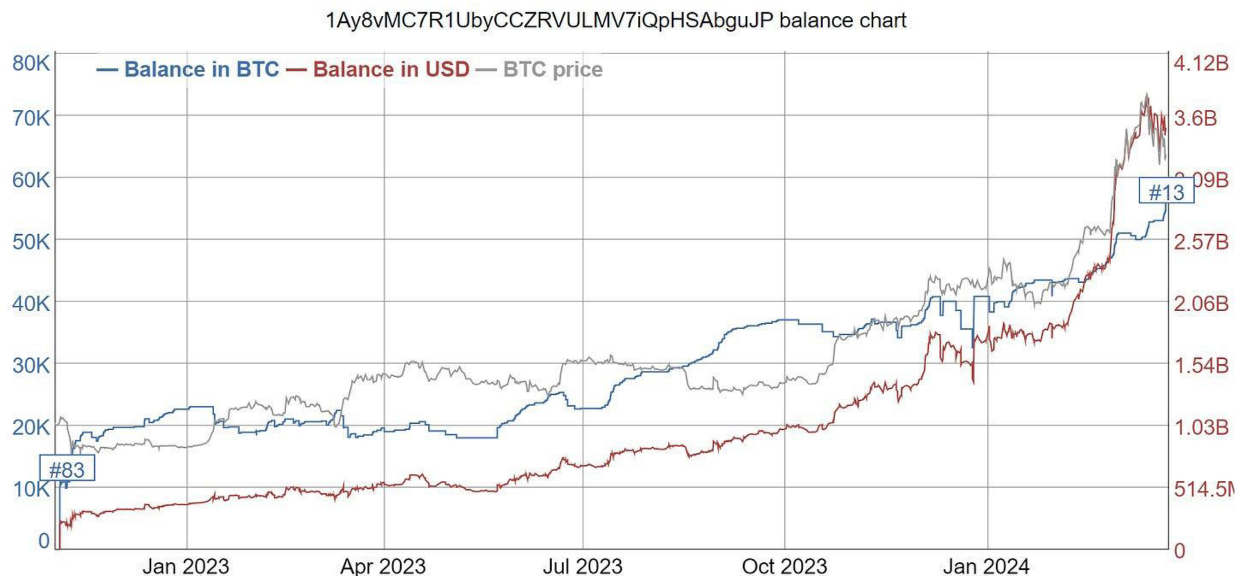


Whales keep accumulating under the surface

Under the surface and like ETF investors, whales are stacking the dip in earnest.

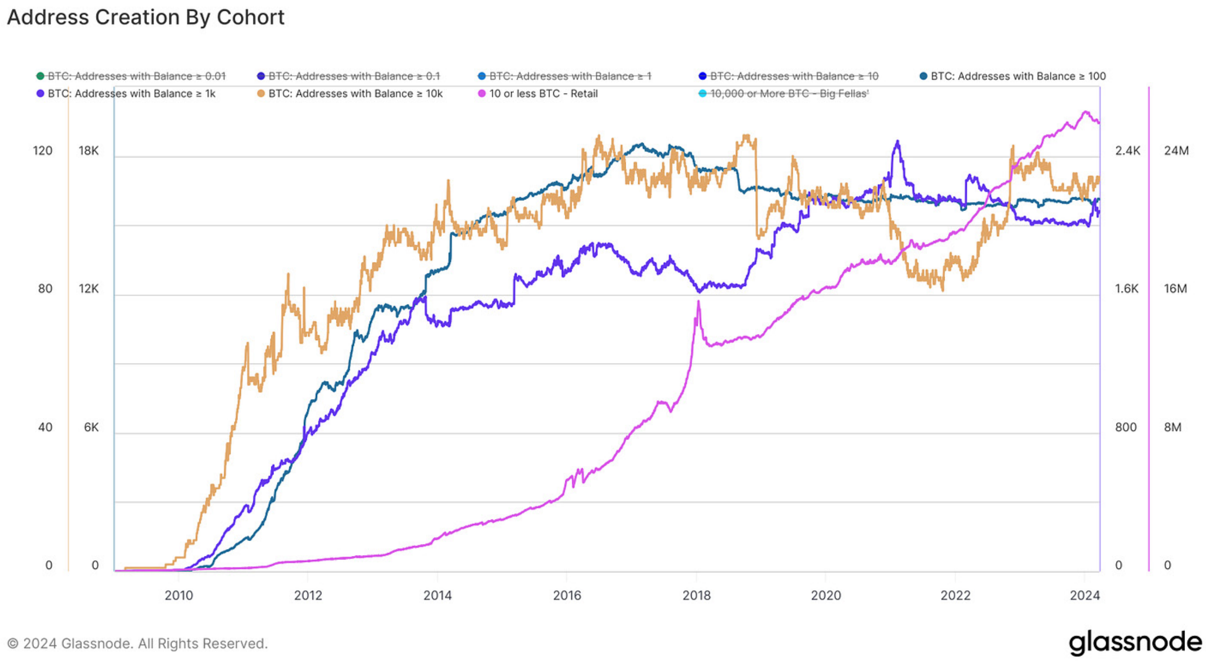
The market is currently observing some interesting behavior. There is a single address with over $3 billion worth of BTC leaving a highly fascinating footprint. A South Korean exchange called Upbit is linked to purchases in 100 BTC increments. According to on-chain analysts, this is not an entity buying bitcoin on behalf of an ETF, this is instead by our understanding a segregated balance acquiring BTC via Upbit. Who is it, and what other details do we have? We will investigate this further—the pattern has caused the community to give "him" the name Mr. 100. He has slowly built his holdings to 54,925 BTC, making him in control of the 13th largest bitcoin address. Instead of perpetuating rumors, we'll patiently await more evidence. The whole episode is a healthy exercise in observing the semi-anonymous nature of bitcoin.

This behavior is a perfect representation of this more mature and capital-rich investing cohort coming into the bitcoin ecosystem, instead opting to buy spot bitcoin rather than the ETF products:



BitInfoCharts

Retail investors continue to make up the majority of addresses on bitcoin, with individuals holding 10 or fewer BTC, denoted below in pink, rising persistently since 2018 without fail, bull or bear. It is encouraging from a protocol security standpoint that bitcoin continues to be dominated by smaller participants and further distributing balances and the ownership of the network around the world:



With bitcoin's 4th halving approaching in just 26 days, potentially around April 19, 2024, supply is about to get a whole lot tighter. Whales and ETFs combined are scooping up 10x the daily BTC issuance on a normal day, and bitcoin's supply constraint is slated to enter completely unchartered territory as these buyers only grow more interested and the supply shock hits the market like a ton of bricks.

As Nik said in his latest stellar interview with Peter McCormack on What Bitcoin Did, you need to prepare for $100,000 bitcoin, because it's coming sooner than you think.

NOTABLE INSTITUTIONAL BUYING

From SEC Form 13F Filings by Top Investment Managers and Concentrated Hedge Funds This Month

Institution or Fund	Reporting Manager	Report Quarter	Stock Purchased/Sold	Ticker	Shares Owned	Value of Holdings (Average Price)	% of Portfolio	Change in Shares	Purchase Value
Absoluto Partners Gestao de Recursos Ltda	Edward Wygand	2023Q4	VTEX	VTEX	1,148,174	$7,899,437($6.88)	4.00%	1,148,174(New Position)	$7,899,437
Altimeter Capital Management LP	Mara Davis	2023Q4	PDD HOLDINGS INC	PDD	1,882,770	$275,468,074($146.31)	5.00%	191.32%(1,236,490)	$180,910,849
AMANSA CAPITAL PTE. LTD	Richard Astorga	2023Q4	ICICI BANK LTD	IBN	2,684,650	$64,002,056($23.84)	34.00%	2,684,650(New Position)	$64,002,056
AMANSA CAPITAL PTE. LTD	Richard Astorga	2023Q4	COGNIZANT TECH SOLUTIONS	CTSH	400,000	$30,212,000($75.53)	16.00%	400,000(New Position)	$30,212,000
Anabranch Capital Management LP	Philip Yang	2023Q4	TEMPUR-SEALY INTERNATIONAL	TPX	489,308	$24,940,029($50.97)	15.86%	6.66%(30,551)	$1,557,185
Anabranch Capital Management LP	Philip Yang	2023Q4	HILTON WORLDWIDE HLDGS	HLT	63,996	$11,653,031($182.09)	7.41%	47.10%(20,492)	$3,731,388
APPALOOSA MANAGEMENT LP	Michael L Palmer	2023Q4	ALPHABET INC	GOOG	10,723,000	$406,874,000($37.94)	9.00%	10,723,000(New Position)	$406,874,000
APPALOOSA MANAGEMENT LP	Michael L Palmer	2023Q4	WHIRLPOOL CORPORATION	WHR	1,614,904	$237,181,000($146.87)	5.00%	42.45%(481,211)	$70,675,515
APPALOOSA MANAGEMENT LP	Michael L Palmer	2023Q4	ENERGY TRANSFER PARTNERS LP	ET	5,143,082	$173,476,000($33.73)	4.00%	5,143,082(New Position)	$173,476,000
APPALOOSA MANAGEMENT LP	Michael L Palmer	2023Q4	KINDER MORGAN INC	KMI	9,445,321	$140,924,000($14.92)	3.00%	9,445,321(New Position)	$140,924,000
Arthedge Capital Management LLC	Samir Gupta	2023Q4	GLOBAL-E ONLINE LTD	GLBE	288,763	$11,443,678($39.63)	8.00%	9.69%(25,500)	$1,010,565
Bain Capital Investors LLC	Michael D. Ward	2023Q4	CEREVEL THERAPEUTICS HOLD	CERE	65,679,781	$2,784,822,815($42.40)	60.00%	9.10%(5,480,052)	$232,354,213
BERKSHIRE HATHAWAY INC	Marc D. Hamburg	2023Q4	CHEVRON CORPORATION	CVX	126,093,323	$18,808,080,506($149.16)	5.00%	14.37%(15,845,031)	$2,363,444,839
BERKSHIRE HATHAWAY INC	Marc D. Hamburg	2023Q4	OCCIDENTAL PETROLEUM CORP	OXY	243,715,808	$14,552,270,657($59.71)	4.00%	8.74%(19,586,616)	$1,169,516,808
Bridgewater Associates LP	Helene Glotzer	2023Q4	ELI LILLY AND CO	LLY	317,586	$185,127,226($582.92)	1.00%	412.51%(255,619)	$149,005,423
BRX Global LP	Brian Jackelow	2023Q4	MOODY'S CORPORATION	MCO	43,107	$16,835,870($390.56)	16.00%	37.73%(11,809)	$4,612,123
CAS Investment Partners	CLIFFORD SOSIN	2023Q4	CAPITAL ONE FINANCIAL CORP	COF	533,460	$69,947,273($131.12)	8.00%	52.61%(183,900)	$24,112,967
CROSSLINK CAPITAL INC	Mihaly Szigeti	2023Q4	SALESFORCE,INC	CRM	208,345	$54,823,906($263.14)	8.00%	93.15%(100,480)	$26,440,309
CYPRESS FUNDS LLC	Robert Miller	2023Q4	CADENCE DESIGN SYS INC	CDN	166,000	$45,213,420($272.37)	5.00%	166,000(New Position)	$45,213,420
Dalal Street LLC	Mohnish Pabrai	2023Q4	ARCH RESOURCES, INC	ARCH	234,994	$38,994,904($165.94)	16.00%	200.36%(156,756)	$26,012,090
Dalal Street LLC	Mohnish Pabrai	2023Q4	WARRIOR MET COAL INC	HCC	629,712	$38,393,541($60.97)	15.00%	629,712(New Position)	$38,393,541
Dorsey Asset Management LLC	Michael Harriett	2023Q4	HERC HLDGS INC	HRI	516,894	$76,960,347($148.89)	10.00%	19.34%(83,755)	$12,470,283
Dorsey Asset Management LLC	Michael Harriett	2023Q4	DANAHER CORP	DHR	314,516	$72,760,131($231.34)	9.00%	314,516(New Position)	$72,760,131
Duquesne Family Office LLC	Sue Meng	2023Q4	TECK RESOURCES LIMITED CLASS B	TCK	5,525,148	$233,548,000($42.27)	8.00%	34.57%(1,419,471)	$60,001,031
Duquesne Family Office LLC	Sue Meng	2023Q4	SEAGATE TECH HLDS PLC	STX	2,116,108	$180,652,146($85.37)	6.00%	131.26%(1,201,065)	$102,534,922
Duquesne Family Office LLC	Sue Meng	2023Q4	ARISTA NETWORKS INC	ANET	234,185	$55,153,000($235.51)	2.00%	234,185(New Position)	$55,153,000
Duquesne Family Office LLC	Sue Meng	2023Q4	WOODWARD INC	WWD	404,635	$55,083,000($136.13)	2.00%	404,635(New Position)	$55,083,000
Elm Ridge Management LLC	Sheetal Acharekar	2023Q4	ARCBEST CORPORATION	ARCB	34,106	$4,099,882($120.21)	5.00%	79.16%(15,069)	$1,811,444
Greencape Capital	Hannah Crabbe	2023Q4	ABBOTT LABS	ABT	631,287	$69,485,760($110.07)	35.41%	2.38%(14,687)	$1,616,597
Greencape Capital	Hannah Crabbe	2023Q4	ZILLOW GROUP INC	Z	846,190	$48,960,554($57.86)	24.95%	69.97%(348,354)	$20,155,763
GREENLEA LANE CAPITAL MANAGEMENT LLC	JOSH TARASOFF	2023Q4	BROOKFIELD CORP	BN	1,615,220	$64,802,625($40.12)	20.00%	3.54%(55,211)	$2,215,067
GREENLEA LANE CAPITAL MANAGEMENT LLC	JOSH TARASOFF	2023Q4	BERKSHIRE HATHWY INC	BRK-A	71	$38,526,377($542,625.03)	12.00%	71(New Position)	$38,526,377
GREENLIGHT CAPITAL INC	Daniel Roitman	2023Q4	TENET HEALTHCARE CORPORATION	THC	1,315,970	$99,447,852($75.57)	5.00%	44.33%(404,190)	$30,544,638
GREENLIGHT CAPITAL INC	Daniel Roitman	2023Q4	ALIGHT INC	ALIT	9,241,670	$78,831,446($8.53)	4.00%	9,241,670(New Position)	$78,831,446
GREENOAKS CAPITAL PARTNERS LLC	Patrick Lai	2023Q4	TOAST INC	TOST	8,841,611	$161,447,817($18.26)	19.00%	10.17%(816,075)	$14,901,528
Greenstone Partners & Co. LLC	Gregory M. Tusher	2023Q4	APPLOVIN CORP COM	APP	796,837	$31,753,954($39.85)	18.00%	3.86%(29,585)	$1,178,963
Greenstone Partners & Co. LLC	Gregory M. Tusher	2023Q4	ACUITY BRANDS INC	AYI	110,075	$22,546,662($204.83)	13.00%	16.88%(15,900)	$3,256,797
Greenstone Partners & Co. LLC	Gregory M. Tusher	2023Q4	PROCORE TECHNOLOGIES INC	PCOR	282,958	$19,586,353($69.22)	11.00%	26.86%(59,915)	$4,147,316

Institution or Fund	Reporting Manager	Report Quarter	Stock Purchased/Sold	Ticker	Shares Owned	Value of Holdings (Average Price)	% of Portfolio	Change in Shares	Purchase Value
Greenstone Partners & Co. LLC	Gregory M. Tusher	2023Q4	GUIDEWIRE SOFTWARE INC	GWRE	163,639	$17,843,197($109.04)	10.00%	12.40%(18,050)	$1,968,172
Greenstone Partners & Co. LLC	Gregory M. Tusher	2023Q4	SCHWAB CHARLES CORP	SCH	218,842	$15,056,330($68.80)	8.00%	7.73%(15,700)	$1,080,160
KEYWISE CAPITAL MANAGEMENT (HK) Ltd	Fang Zheng	2023Q4	TAIWAN SEMICON MFG LTD	TSM	1,186,400	$123,385,600($104.00)	20.00%	31.85%(286,600)	$29,806,402
KEYWISE CAPITAL MANAGEMENT (HK) Ltd	Fang Zheng	2023Q4	MINISO GROUP HLDG LTD	MNSO	3,789,500	$77,305,800($20.40)	13.00%	17.53%(565,300)	$11,532,121
KEYWISE CAPITAL MANAGEMENT (HK) Ltd	Fang Zheng	2023Q4	PDD HOLDINGS INC	PDD	474,600	$69,438,725($146.31)	11.00%	39.71%(134,900)	$19,737,219
Lodge Hill Capital LLC	Jon Hanlon	2023Q4	APOLLO GLOBAL MGMT INC	APO	162,968	$15,186,988($93.19)	7.00%	85.26%(75,000)	$6,989,250
Lodge Hill Capital LLC	Jon Hanlon	2023Q4	OLIN CORP	OLN	285,000	$15,375,750($53.95)	7.00%	39.02%(80,000)	$4,316,000
Lodge Hill Capital LLC	Jon Hanlon	2023Q4	ARCH RESOURCES, INC	ARCH	85,000	$14,104,900($165.94)	6.00%	85,000(New Position)	$14,104,900
LONG WALK MANAGEMENT LP	James Zimmerman	2023Q4	FLOOR & DECOR HLDGS INC	FND	275,000	$30,678,999($111.56)	20.00%	50.68%(92,500)	$10,319,300
LONG WALK MANAGEMENT LP	James Zimmerman	2023Q4	SHOPIFY INC	SHOP	352,000	$27,420,801($77.90)	18.00%	22.43%(64,500)	$5,024,550
LONG WALK MANAGEMENT LP	James Zimmerman	2023Q4	RH COM	RH	80,000	$23,318,400($291.48)	15.00%	80,000(New Position)	$23,318,400
LONG WALK MANAGEMENT LP	James Zimmerman	2023Q4	APPFOLIO INC	APPF	122,000	$21,135,280($173.24)	14.00%	62.67%(47,000)	$8,142,280
Lynx1 Capital Management LP	Weston Nichols	2023Q4	ALPINE IMMUNE SCIENCES INC	ALPN	3,813,926	$72,693,428($19.06)	29.00%	58.61%(1,409,312)	$26,861,486
Lynx1 Capital Management LP	Weston Nichols	2023Q4	C4 THERAPEUTICS INC	CCCC	3,134,396	$17,709,338($5.65)	7.00%	207.53%(2,115,166)	$11,950,688
Lynx1 Capital Management LP	Weston Nichols	2023Q4	STOKE THERAPEUTICS INC	STOK	2,956,918	$15,553,389($5.26)	6.00%	72.90%(1,246,764)	$6,557,979
Marcho Partners LLP	Craig Simkin	2023Q4	DLOCAL LTD	DLO	1,677,009	$29,666,289($17.69)	10.00%	40.85%(486,415)	$8,604,681
Marcho Partners LLP	Craig Simkin	2023Q4	GRAB HLDGS LTD	GRAB	9,037,719	$30,457,113($3.37)	10.00%	39.05%(2,538,110)	$8,553,431
MFN Partners Management LP	Jon Reisman	2023Q4	RXO INC	RXO	13,008,225	$302,571,316($23.26)	10.00%	2.63%(332,856)	$7,742,231
MFN Partners Management LP	Jon Reisman	2023Q4	HCA HEALTHCARE INC	HCA	973,898	$263,614,704($270.68)	9.00%	26.61%(204,700)	$55,408,195
MFN Partners Management LP	Jon Reisman	2023Q4	LIBERTY GLOBAL LTD	LBTYK	6,706,460	$125,008,414($18.64)	4.00%	6,706,460(New Position)	$125,008,414
OLP CAPITAL MANAGEMENT Ltd	Di Fan Shen	2023Q4	QIFU TECHNOLOGY, INC	QFIN	12,919,407	$204,385,015($15.82)	31.00%	0.62%(79,952)	$1,264,841
PAULSON & CO. INC.	Stuart Merzer	2023Q4	MADRIGAL PHARMACEUTICALS INC	MDGL	1,105,741	$255,846,358($231.38)	23.00%	121.15%(605,741)	$140,156,350
PECONIC PARTNERS LLC	Wook Lee	2023Q4	DYCOM INDS INC	DY	3,265,682	$375,847,329($115.09)	18.00%	0.67%(21,635)	$2,489,972
PECONIC PARTNERS LLC	Wook Lee	2023Q4	CLEVELAND-CLIFFS INC	CLF	2,074,927	$42,370,009($20.42)	2.00%	2,074,927(New Position)	$42,370,009
Pershing Square Capital Management L.P.	William A Ackman	2023Q4	HOWARD HUGHES HLDG INC	HHH	18,852,064	$1,612,794,133($85.55)	16.00%	12.17%(2,045,156)	$174,963,102
Redpoint Management LLC	Jeffrey Cheng	2023Q4	SENTINELONE INC	S	13,101,096	$359,494,081($27.44)	40.00%	400.00%(10,480,877)	$287,595,270
RR Advisors LLC	Robert J. Raymond	2023Q4	MPLX LP	MPLX	1,099,000	$40,355,281($36.72)	7.00%	30.06%(254,000)	$9,326,880
Scion Asset Management LLC	Michael J. Burry	2023Q4	HCA HEALTHCARE INC	HCA	20,000	$5,413,600($270.68)	6.00%	20,000(New Position)	$5,413,600
Scion Asset Management LLC	Michael J. Burry	2023Q4	ORACLE CORPORATION	ORCL	50,000	$5,271,500($105.43)	6.00%	50,000(New Position)	$5,271,500
Scion Asset Management LLC	Michael J. Burry	2023Q4	CITIGROUP	C	100,000	$5,144,000($51.44)	5.00%	100,000(New Position)	$5,144,000
Scion Asset Management LLC	Michael J. Burry	2023Q4	CVS HEALTH CORPORATION	CVS	65,000	$5,132,400($78.96)	5.00%	65,000(New Position)	$5,132,400
Scion Asset Management LLC	Michael J. Burry	2023Q4	ALPHABET INC	GOOGL	35,000	$4,889,150($139.69)	5.00%	35,000(New Position)	$4,889,150
Sharp Capital Gestora de Recursos Ltda.	Ivan Guetta	2023Q4	NU HLDGS LTD	NU	10,880,270	$90,632,649($8.33)	47.00%	10,880,270(New Position)	$90,632,649
Sharp Capital Gestora de Recursos Ltda.	Ivan Guetta	2023Q4	MERCADOLIBRE INC	MELI	25,995	$40,852,183($1,571.54)	21.00%	23.09%(4,877)	$7,664,401
Sharp Capital Gestora de Recursos Ltda.	Ivan Guetta	2023Q4	STONECO LTD	STNE	675,908	$12,186,621($18.03)	6.00%	675,908(New Position)	$12,186,621
SIR Capital Management L.P.	Ben Fooshee	2023Q4	PHILLIPS 66	PSX	349,114	$46,481,038($133.14)	5.00%	349,114(New Position)	$46,481,038
SIR Capital Management L.P.	Ben Fooshee	2023Q4	CHENIERE ENERGY INC	LNG	276,515	$47,203,878($170.71)	5.00%	2,783.07%(266,924)	$45,566,598
SIR Capital Management L.P.	Ben Fooshee	2023Q4	EOG RESOURCES,INC	EOG	347,011	$41,970,980($120.95)	4.00%	347,011(New Position)	$41,970,980
SOMA EQUITY PARTNERS LP	Jessica Lane	2023Q4	ILLUMINA INC	ILMN	851,599	$118,580,000($139.24)	7.00%	851,599(New Position)	$118,580,000
SOROS FUND MANAGEMENT LLC	John DeSisto	2023Q4	SPLUNK INC	SPLK	1,580,001	$240,713,162($152.35)	9.00%	174.80%(1,005,039)	$153,117,698
Squadra Investments - Gestao de Recursos Ltda	Luis Felipe Saramago Stern	2023Q4	MERCADOLIBRE INC	MELI	151,078	$237,425,126($1,571.54)	49.00%	31.96%(36,588)	$57,499,508
Squadra Investments - Gestao de Recursos Ltda	Luis Felipe Saramago Stern	2023Q4	XP INC	XP	9,018,875	$235,122,068($26.07)	49.00%	30.11%(2,087,205)	$54,413,434
SVB FINANCIAL GROUP	Nicholas Grossi	2023Q4	COINBASE GLOBAL INC	COIN	531,319	$92,407,000($173.92)	82.00%	30.55%(124,346)	$21,626,256
Systrade AG	Helmut A. Friedrich	2023Q4	ALPHA METALLURGICAL RES INC	AMR	270,000	$91,508,404($338.92)	82.00%	8.00%(20,000)	$6,778,400
Systrade AG	Helmut A. Friedrich	2023Q4	T-MOBILE US INC	TMUS	100,500	$16,113,165($160.33)	15.00%	100,500(New Position)	$16,113,165
TIGER MANAGEMENT L.L.C.	Elouise Manhertz	2023Q4	COUPANG INC	CPNG	91,645	$1,483,733($16.19)	27.00%	91,645(New Position)	$1,483,733
Tudor Investment Corp	Thayer Swallen	2023Q4	SPLUNK INC	SPLK	1,669,609	$254,364,941($152.35)	4.00%	45.27%(520,301)	$79,267,861
Tudor Investment Corp	Thayer Swallen	2023Q4	PIONEER NAT RES	PXD	850,681	$191,301,143($224.88)	3.00%	1,251.90%(787,756)	$177,150,569
YACKTMAN ASSET MANAGEMENT LP	Krista Infante	2023Q4	KENVUE INC	KVUE	5,409,457	$116,465,613($21.53)	1.00%	43.33%(1,635,395)	$35,210,055

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
Harpoon Therapeutics Inc.	HARP	$492,135,712	$0	1	0
Liberty Media Corp	LSXMK	$469,232,104	$3,501	6	1
COMSTOCK RESOURCES INC	CRK	$100,450,000	$0	1	0
Veradigm Inc.	MDRX	$66,001,500	$0	1	0
Perspective Therapeutics Inc.	CATX	$57,409,488	$0	1	0
Archer Aviation Inc.	ACHR	$39,082,073	$0	4	0
RARE ELEMENT RESOURCES LTD	REEMF	$29,326,030	$0	1	0
BlackRock ESG Capital Allocation Term Trust	ECAT	$25,937,922	$0	10	0
Corbus Pharmaceuticals Holdings Inc.	CRBP	$23,327,560	$0	1	0
BlackRock Capital Allocation Term Trust	BCAT	$20,925,391	$0	3	0
89bio Inc.	ETNB	$20,722,500	$48,173	1	1
Rezolute Inc.	RZLT	$17,508,435	$0	5	0
BlackRock Innovation & Growth Term Trust	BIGZ	$17,248,204	$0	8	0
TALOS ENERGY INC.	TALO	$15,031,526	$0	2	0
LENZ Therapeutics Inc.	LENZ	$15,000,075	$0	1	0
Transocean Ltd.	RIG	$14,670,000	$0	3	0
Cardlytics Inc.	CDLX	$13,919,894	$272,323	2	1
MERCURY SYSTEMS INC	MRCY	$11,057,678	$0	1	0
BlackRock Health Sciences Term Trust	BMEZ	$10,244,649	$0	5	0
Sphere Entertainment Co.	SPHR	$10,706,222	$618,694	3	1
Citi Trends Inc	CTRN	$10,027,037	$0	4	0
AmBase Corp	ABCP	$8,840,092	$0	1	0
Liberty Latin America Ltd.	LILA	$8,764,509	$0	3	0
Maplebear Inc.	CART	$16,460,721	$8,227,288	4	4
OCULAR THERAPEUTIX INC	OCUL	$7,000,000	$0	1	0
TILE SHOP HOLDINGS INC.	TTSH	$6,666,654	$0	6	0
SLR Investment Corp.	SLRC	$6,251,807	$0	4	0
TruBridge Inc.	CPSI	$5,080,044	$0	4	0
SONIDA SENIOR LIVING INC.	SNDA	$5,000,002	$0	1	0
Skye Bioscience Inc.	SKYE	$4,500,000	$0	1	0
Globalstar Inc.	GSAT	$4,595,580	$104,250	3	1
2seventy bio Inc.	TSVT	$3,899,050	$0	1	0
Mallinckrodt plc	MNKTQ	$3,620,875	$0	1	0
GEN Restaurant Group Inc.	GENK	$3,309,731	$0	15	0
MasterCraft Boat Holdings Inc.	MCFT	$3,250,907	$0	1	0
Biglari Holdings Inc.	BH	$3,120,092	$0	4	0
TILLY'S INC.	TLYS	$3,105,740	$0	5	0
Gogo Inc.	GOGO	$2,768,657	$0	3	0
NEXTNAV INC.	NN	$2,869,663	$123,550	2	1
EchoStar CORP	SATS	$2,671,400	$0	2	0
OPKO HEALTH INC.	OPK	$2,400,680	$0	5	0
Bakkt Holdings Inc.	BKKT	$2,394,662	$44,047	1	1
Nuveen Core Plus Impact Fund	NPCT	$2,341,001	$0	4	0
Paysign Inc.	PAYS	$2,362,758	$79,429	6	1
BankUnited Inc.	BKU	$4,621,590	$2,420,652	3	4
Ondas Holdings Inc.	ONDS	$2,000,000	$0	1	0
NUVEEN PENNSYLVANIA QUALITY MUNICIPAL INCOME FUND	NQP	$1,960,129	$0	6	0
AMN HEALTHCARE SERVICES INC	AMN	$1,944,587	$0	8	0

Stock Purchased/Sold	Ticker	Total Buy Value	Total Sell Value	Total Buy Filings	Total Sell Filings
Institutional Investment Strategy Fund	XIVYX	$1,860,000	$0	3	0
Texas Pacific Land Corp	TPL	$1,841,783	$0	25	0
ENVESTNET INC.	ENV	$1,714,794	$0	2	0
Marpai Inc.	MRAI	$1,501,500	$0	1	0
Invesco Pennsylvania Value Municipal Income Trust	VPV	$1,484,784	$0	5	0
LEE ENTERPRISES Inc	LEE	$1,474,990	$0	4	0
AMERICAS CARMART INC	CRMT	$1,436,049	$0	2	0
Jazz Pharmaceuticals plc	JAZZ	$1,435,800	$0	1	0
Allegion plc	ALLE	$1,324,146	$0	1	0
Astera Labs Inc.	ALAB	$1,322,892	$0	3	0
NU RIDE INC.	NRDE	$1,245,308	$0	1	0
Core Scientific Inc.	CORZ	$1,233,709	$0	5	0
OmniAb Inc.	OABI	$1,167,750	$0	1	0
Option Care Health Inc.	OPCH	$1,104,352	$0	1	0
DOMINION ENERGY INC	D	$1,097,889	$0	2	0
BLACKROCK CALIFORNIA MUNICIPAL INCOME TRUST	BFZ	$1,076,293	$0	3	0
ONE Group Hospitality Inc.	STKS	$1,059,498	$0	1	0
CECO ENVIRONMENTAL CORP	CECO	$1,038,859	$0	2	0
PhenixFIN Corp	PFX	$1,013,306	$0	3	0
Absci Corp	ABSI	$999,999	$0	1	0
ILLUMINA INC.	ILMN	$991,673	$0	1	0
Nerdy Inc.	NRDY	$1,051,564	$89,337	5	1
Traeger Inc.	COOK	$933,006	$0	1	0
BLACKROCK MUNIYIELD PENNSYLVANIA QUALITY FUND	MPA	$916,669	$0	7	0
NUVEEN NEW JERSEY QUALITY MUNICIPAL INCOME FUND	NXJ	$903,640	$0	6	0
AGREE REALTY CORP	ADC	$888,000	$0	1	0
LIONS GATE ENTERTAINMENT CORP	LGF-B	$884,000	$0	1	0
Cyteir Therapeutics Inc.	CYT	$845,706	$0	2	0
Reservoir Media Inc.	RSVR	$845,667	$0	2	0
Western Midstream Partners LP	WES	$840,205	$0	6	0
APPLIED OPTOELECTRONICS INC.	AAOI	$802,352	$0	4	0
BrightSpring Health Services Inc.	BTSG	$776,742	$0	5	0
Gates Industrial Corp plc	GTES	$727,500	$0	1	0
FIRST TRUST HIGH YIELD OPPORTUNITIES 2027 TERM FUND	FTHY	$724,910	$0	1	0
NB Bancorp Inc.	NBBK	$710,866	$0	6	0
Agrify Corp	AGFY	$700,000	$0	1	0
Cartesian Therapeutics Inc.	RNAC	$677,620	$0	2	0
DEVON ENERGY CORP	DVN	$666,300	$0	1	0
abrdn Global Infrastructure Income Fund	ASGI	$656,306	$0	1	0
AerSale Corp	ASLE	$655,345	$0	6	0
STANDARD BIOTOOLS INC.	LAB	$646,169	$0	1	0
Caesars Entertainment Inc.	CZR	$621,750	$0	1	0
Pono Capital Two Inc.	PTWO	$621,645	$0	7	0
Elanco Animal Health Inc	ELAN	$617,802	$0	3	0
GEO GROUP INC	GEO	$624,025	$25,000	1	1
HARROW INC.	HROW	$592,600	$0	2	0
DARLING INGREDIENTS INC.	DAR	$589,520	$0	2	0
NATIONAL HEALTH INVESTORS INC	NHI	$586,882	$0	1	0
RBB Bancorp	RBB	$586,083	$0	6	0
IonQ Inc.	IONQ	$1,067,200	$500,849	1	2
Regional Management Corp.	RM	$695,078	$142,696	2	1
Princeton Bancorp Inc.	BPRN	$541,220	$0	2	0
TEAM INC	TISI	$538,167	$0	7	0
MAIA Biotechnology Inc.	MAIA	$529,695	$0	5	0
Greenwich LifeSciences Inc.	GLSI	$510,838	$0	4	0
SunOpta Inc.	STKL	$495,883	$0	2	0
StoneBridge Acquisition Corp.	APAC	$495,750	$0	2	0
Fulcrum Therapeutics Inc.	FULC	$492,028	$0	1	0
Mativ Holdings Inc.	MATV	$484,545	$0	5	0
Enphase Energy Inc.	ENPH	$482,154	$0	1	0

Stock Purchased/Sold	Ticker	Total Buy Value	Total Sell Value	Total Buy Filings	Total Sell Filings
SOLAREDGE TECHNOLOGIES INC.	SEDG	$474,250	$0	1	0
ISSUER DIRECT CORP	ISDR	$467,600	$0	5	0
HAWTHORN BANCSHARES INC.	HWBK	$467,141	$0	6	0
ADVANCE AUTO PARTS INC	AAP	$458,552	$0	3	0
CALIFORNIA FIRST LEASING CORP	CFNB	$446,089	$0	1	0
Alteryx Inc.	AYX	$440,953	$0	1	0
Invesco Trust for Investment Grade New York Municipals	VTN	$435,412	$0	3	0
Broadstone Net Lease Inc.	BNL	$427,278	$0	4	0
Holley Inc.	HLLY	$420,101	$0	1	0
QNB CORP	QNBC	$417,616	$0	1	0
RE/MAX Holdings Inc.	RMAX	$412,560	$0	1	0
Pioneer Municipal High Income Opportunities Fund Inc.	MIO	$412,291	$0	3	0
Federated Hermes Premier Municipal Income Fund	FMN	$359,810	$0	4	0
USCB FINANCIAL HOLDINGS INC.	USCB	$355,584	$0	4	0
Pinstripes Holdings Inc.	PNST	$343,000	$0	1	0
BNY MELLON MUNICIPAL INCOME INC.	DMF	$340,200	$0	3	0
Ribbon Communications Inc.	RBBN	$333,475	$0	5	0
Sunnova Energy International Inc.	NOVA	$1,054,954	$721,538	1	12
AG Mortgage Investment Trust Inc.	MITT	$330,275	$0	2	0
Great Elm Group Inc.	GEG	$326,853	$0	4	0
BANC OF CALIFORNIA INC.	BANC	$325,232	$0	2	0
PIONEER MUNICIPAL HIGH INCOME FUND INC.	MHI	$322,303	$0	2	0
Medalist Diversified REIT Inc.	MDRR	$317,144	$0	4	0
V F CORP	VFC	$310,620	$62	1	0
HEALTHPEAK PROPERTIES INC.	DOC	$300,780	$0	1	0
Timberline Resources Corp	TLRS	$300,000	$0	2	0
VICI PROPERTIES INC.	VICI	$288,080	$0	1	0
FRESH DEL MONTE PRODUCE INC	FDP	$312,974	$26,371	1	1
MainStay CBRE Global Infrastructure Megatrends Term Fund	MEGI	$282,357	$0	2	0
Clearfield Inc.	CLFD	$275,670	$0	3	0
OPENLANE Inc.	KAR	$508,220	$234,632	1	1
HUNT J B TRANSPORT SERVICES INC	JBHT	$1,014,950	$745,502	1	1
FOMO WORLDWIDE INC.	FOMC	$255,750	$0	6	0
Paragon 28 Inc.	FNA	$255,226	$0	1	0
CommScope Holding Company Inc.	COMM	$253,876	$0	2	0
PERRIGO Co plc	PRGO	$252,168	$0	1	0
AMREP CORP.	AXR	$251,364	$0	3	0
BALL Corp	BALL	$249,767	$0	1	0
Axos Financial Inc.	AX	$248,750	$0	1	0
BRIGHTCOVE INC	BCOV	$247,055	$0	4	0
Palmer Square Capital BDC Inc.	PSBD	$246,600	$0	1	0
Atlantic Union Bankshares Corp	AUB	$245,910	$0	1	0