INVESTMENT NOTES - March 6th, 2019

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The markets continue to act well although not enthusiastically well except for China. Cash is still very high in portfolios and it remains to be seen whether this will be deployed before the end of the quarter in an effort to 'catch up' performance. Broad performance numbers for active managers in general until the end of February point indicate that 2018 losses were not recovered in January/February.

Although we have a dovish Fed, we don't have QE4 yet. Although we have postponement and progress in US/China trade talks, we don't have an actual agreement yet. There is speculation that an agreement could bring another 10% increase in the markets. If this is the case, or if we don't get a robust agreement or QE4, then we believe most of the largest gains in the market have been made for this year.

We do believe there are pockets of value however. Last week we added the British brick maker, Ibstock to our portfolio. We believe that the hard Brexit fears are overdone in the market and with a 40% market share plus the UK housing shortage, Ibstock presents long-term value.

We also purchased asset manager Anima Holding in Italy. The Italian tax authorities have encouraged people to have their assets in Italy. Anima has a 4.3% dividend yield and trades on a historical P/E of 11x and an estimated P/E of 8.4x with a P/CF of 2.23x.

Lastly, we purchased Applus Services in Spain. Applus is a worldwide leader (in 70 countries) in the testing, inspection and certification sector that enhances the quality and safety of their clients' assets and infrastructure while safeguarding their operations. The stock trades at 2x book value, P/CF of 10x and an estimated P/E of 14x.

We also shorted the US Russell 2000 index and the High Yield Bond index. We are currently analyzing car part manufacturers for possible short candidates for the following reasons. Investors are paying a great deal of attention to the weakness in the Chinese economy in the first quarter that is being explained by a buildup in inventories in the 4th Qtr. 2018 to protect from trade wars. This has led to a weak 1st Qtr. As inventories are worked off. Chinese imports from America have fallen substantially in 1st Quarter. The question is how much of this is inventory work off and how much is Chinese consumers boycotting American goods?
Of course the other end of this trade is in the USA. US car companies also loaded up on inventory pre-tariffs and now they are suffering for it. A slowdown in US demand for cars hasn't helped but it is the inventory overhang which must be worked off now which will slow auto parts sales over the next few quarters at least. This is in part why durable goods orders in the US are going off a cliff. Hence our search for shorts.

The slowdown in the auto sector, the government shutdown, dreadful weather across the US and the collapse in Chinese imports from the US, all point to a lower GDP number for the US. The question is whether this will stimulate the Fed into QE4. If the Fed hesitates with QE4- how will the US equity market react to weak economic numbers? We are predicting that the Fed will not start QE4 in time and equities could hit a pothole.

The President is trying to reflate the economy so that the elections are not lost next year. This is why he is talking down the price of oil (the quickest way to reflate the U.S. consumer). This will not help Texas energy producers or shale beneficiaries- hence our short on the high yield debt market as this is the majority of the borrowers. With no ability to reduce taxes, the White House has four options: 1. Deregulate. 2. Work the Fed to cut rates. 3. Start a fiscal spend. 4. Bring oil prices down.

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