INVESTMENT NOTES - April 2nd, 2019

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Please pardon the lack of notes last week- we were travelling and really didn't have much to say! Our 'climbing the wall of worry' theme still seems to hold. Chinese stock leverage hit its highest levels in March since 2015. Last week, after registering the largest net shorts in over two years, S&P 500 futures turned positive which is the first time since mid-January. US money market assets are however close to the highest levels they've been in eight years.

March was a difficult month although both bonds and stocks did well- stocks less so. Investors were divided as to whether the rally in the long term bond market was correctly reflecting the state of the economy or whether the resilient stock market was. It seemed both could not be correct.

Although the jury is still out, we believe the stock market has it correct and the long-term bond market was over-reacting to dovish announcements from the Central Banks. We spoke about this in our last notes- so we will not beat a dead horse.

Instead we would like to talk about one of our newer positions, a short in Facebook. The March 29th Financial Times featured an article by Rana Foroohar which interviewed Lina Khan. Lina is a 30 year old Yale Law School graduate who wrote a paper entitled, "Amazon's Antitrust Paradox" in which she made the case that the current interpretations of US antitrust law, which is meant to regulate competition and curb monopolistic practices, are utterly unsuited to the architecture of the modern economy. For four decades, antitrust scholars have pegged their definitions of monopoly power to short-term price effects. Therefore, if the company is making prices lower, it is not a monopoly. But Khan's argument is that it doesn't matter if things are becoming cheaper if predatory pricing strategies used choke off competition and choice. She found Wall Street was valuing Amazon on monopoly pricing power which the classic economic models were missing. Her argument is now at the core of Big Tech antitrust actions on both sides of the Atlantic. For example, Amazon's portion of ecommerce in the world is roughly 25% but on the US it is approximately 52%.

Khan has served on the FTC, consulted with EU officials and has recently joined the House Subcommittee on Antitrust, Commercial an Administrative law in what the FT believes is a sign that the Democrats are gearing up to more aggressive oversight of platforms such as Amazon, Facebook and Google. Khan states the goal of the committee should be how to structure the 21st century digital economy not just to benefit consumers but citizens.

Her next paper to be published in May explores the case for separating the ownership of technology platforms from the commercial activity they host, so big tech firms cannot both run a dominant marketplace and compete on it. Historical precedence has been set that a form of infrastructure cannot compete with all the businesses dependent on that infrastructure. Khan believes current laws are not reflecting current values but outdated values and need to be updated for the internet revolution.

Of the big three, Amazon, Facebook and Google- we decided to short Facebook because its revenue model is the most exposed to this type of legal change. We also read a Vanity Fair article describing the working conditions of outsourced Facebook monitors which included barely above minimum wage salaries along with incredible mental stress. We have a long history in values based investing or socially responsible investment as the first hedge fund in the late 90s to short companies with bad values and tell them we were shorting them for their bad values. We also like to invest in companies that have improving, pro-active values that reflect all the stakeholders in the company.

Next week, we should have completed our study on what 5G is doing to the robotic industry.

Jane Siebels