FRIDAY, JUNE 28, 2024

Hello and welcome to the Dividend Cafe, I am recording, let's see, this my fourth city or fifth city I've been in and just over a week currently in Dallas, Texas, where I think it's about a hundred degrees outside. I am heading back to New York city tomorrow, but not before first recording Dividend Cafe. And I think that it's an important message that, that we're going to talk about here today. It's something that's been on my mind for a little while, and hopefully you'll come away with a little better understanding of I think the way that the money management world often unfortunately works. So from Connecticut to Atlanta, to Grand Rapids, to Dallas, and now back to New York, it has been a little bit of a whirlwind for me, a lot of meetings, a lot of speaking a lot of hotels and flights, but nevertheless, headed back to New York tomorrow, and we're going to use the Dividend Cafe next week to do a kind of mid year check in to look at the middle point today is the final market day of the first half of 2024.

So by the time we're all together next week, even though it is a kind of odd week, we have the 4th of July holiday happening in the middle of the week. So the market is actually open Wednesday, the 3rd and Friday, the 5th, but closed Thursday, the 4th. And nevertheless we're gonna bring you the Dividend Cafe per usual and use it to talk about the mid year state of affairs in the market, in the economy, and really try to dig into what we think is the lay of the land here as we look into the second half of the year.

Today the thing I want to talk about is when I talk about the way the money management world works. I just want you to pretend for a moment that your portfolio manager who is paid off of some form of relative outperformance to an index or is expected to manage to a certain benchmark. And yet, instead of being paid as if you're just overseeing the index passive funds have very low fee. You get paid more to actively manage an index and you get to a point. But we also now need to presuppose this is the part where I give away. Okay, where I'm going, but in this case, the premises involved are the conclusion.

And so bear with me, there's a reason I need to do it in this order. Assume you have no principles or assume you have no convictions or belief system or assume that when you do have convictions, you don't have the courage to act on them. Assume that, You are well paid and that your top priority, either subconsciously or consciously is protecting your career versus some form of a fiduciary duty that you feel bound to in terms of the people you are trying to serve with your money management.

And now The facts on the ground are that one sector has become over 30 percent of the market. One company has become 7%, about three companies have become 20%. That there is this top heaviness that essentially has created a mathematical reality where to not own it. And have it go higher almost ensures mathematically that you can't perform as well as that index is doing if that you care about such a thing.

And in this hypothetical case, people care about it because it's been defined as how they practice the art of self preservation. And then assume that those things that are 30, 40 percent of the index, you have to own them to keep up with the index if it's going higher. And if it's going lower, you are really well protected because even though you're going to go lower with it, that becomes the thing that you can very easily say is why you're lower of course, everyone's lower because all of this top heavy stuff, whatever it may be brought everything lower.

And so there's not really big career risk in owning the thing that everyone owns. So what you do is you become a closet indexer. You hug that index. You don't charge for the index. You charge for your best ideas and convictions, but then you operate as if your convictions are such that you either don't have any, They are you're convicted to preserve your career and paycheck and you then end up taking a view of heads.

I win. I've gone up with the index owning these big popular things and tails I don't lose because the cover is in the fact that when, if it goes down, this is just what happens when everything goes down that way. There's a lot I can unpack. further. There's a lot of different ways in which some of this stuff may be manifested, but no, I don't think I'm really speaking out of turn.

I don't think what I'm saying is very controversial. I don't think I'm being inflammatory. I think I'm describing the career decisions and career mentality at varying degrees of self consciousness for a significant amount of people that run money institutionally, professionally. 2024. I think it's been this way for quite some time.

I think that I've used the term countercultural at varying times to talk about managing money from a dividend growth orientation. And I do think that there is something countercultural about dividend growth as an investment philosophy, about a vigorous focus on fundamentals, a vigorous focus on business models, A centrality of cash flow that these things do often get quite removed from the cultural current when it comes to investing.

But I think that fundamentally, before we even get into how that counter culturalism is manifested in dividend growth, I think what I would say at the Bonson Group is the counter culturalism is about. The other item I just got done describing the caring versus not caring about the popularity of something in your pursuit of what you are doing, in your pursuit of what you believe to be right.

And what, how you view your fiduciary duty to those for whom you manage money. I think that sometimes the system the business model. the structure around the portfolio management world can reward low conviction, low courage low faith investing. And that there is a way to arbitrage the system to hedge for cowardice.

And this is what I'm referring to now, riding a fad up, but blaming the fad down. And I think that can be a systemic, mech. But I think that at the end of the day, our critique is not merely the system, that culture, that mentality. I think that there is ultimately an investment philosophy.

That one has to believe in and has to believe in it through periods of relative popularity and unpopularity and has to believe through it in where the deficiencies lie of other systems. The deficiency I find, and what many managers do by hugging an index with that which is most popular, is primarily a deficiency rooted in moral cowardice, in prioritizing a career risk over fiduciary duty.

And at the end of the day, those things play out. They come out in the wash. And that to me is a very basic, short, succinct explanation. of where a lot of the career components of money management lie. I want to go through a few other market tidbits for you. That was the main gist of the message I wanted to share today as to why a money manager, if I'm so right about overvaluation, and it's not just me, plenty of others saying it too, in certain aspects of the market is there really that many people out there that think they're going to time it all?

There is not. Are there really that many people that are just prepared to write it down? There most certainly are. And I'm trying to explain that they have a reasonably accurate view that they benefit and get credit for the up and they don't feel they'll get blamed for the way down. And so it becomes a safe way to play around this sort of benchmarking philosophy.

as opposed to goals based assessment, actually tying portfolio to goals, to cashflow, to fundamentals, to a point of view, et cetera. All right. Energy CapEx it really got very close to 250 billion trailing 12 months us energy capital expenditures. Back in 2015 oil had gotten down to about 50 a barrel.

That was extremely high. It stayed at a very high range from 2011 to 2016 over investment, over indebtedness, over leverage worked. Okay. With oil at a real high price did not work at all with oil at a low price. CapEx was down to about 50 billion during the COVID shutdown. And really even that was probably entirely maintenance CapEx.

I just can't imagine that there was a whole lot of productive new project capital expenditures in the midst of the shutdown. And I would argue that both things I just said describe over the last decade two different extremes that took place. Significant underinvestment at 50 billion and significant overinvestment at 250 billion.

As we sit here right now oil's at 80, capital expenditures are at 100 billion. So a hundred billion of CapEx with 80 oil versus 250 billion of CapEx with 50 oil, that's the sweet change versus where we were at the point of peak insanity. And I think that it describes a lot of the fundamental basis for optimism in the energy space.

Now that there's capital discipline. There's been de leveraging, there is better commodity price backdrop and overall economic sentiment. The fact of matter is you could almost call it Deglobalization. OPEC countries outside the U S are down 3 million barrels a day and their output were up over 2 million barrels per day.

So the net is still down almost a million barrels a day. It's about 900,000 and yet the reason it's not significantly worse is because of us output. Ironically, the incumbent president. Can't even run on this. I most certainly would be running on it if it were me, but he can't brag about it because it's not considered something to brag about for many of the people that would be voting for him.

So you have a really interesting dynamic. I think that the energy sector has a lot of fundamentals around this capital discipline adjustment that could be accurately called the sweet spot. I mentioned de globalization just to poke at this notion that really non U.S. production of oil is down and U.

S. production of oil is up. It isn't actually really that policy centric. There's other factors within the country that have created it. But nevertheless, When you look at global relationship to U. S. activity, assets, securities, economics foreign ownership of U. S. stocks is at an all time high, both in dollar terms, obviously, but also in percentage terms, in terms of the weighting and asset allocation So that I think is worth noting the way the rest of the

U S the rest of the world is viewing the U S and why the dollar has been so stubbornly strong. Hear me critique this top heaviness in the market. I focused a bit on this unbelievably successful, amazing story of the company that is Nvidia, but comment on the valuation of it. You hear people. The stock goes up 690 percent in 18 months and then it drops 8 percent and people think it went on sale or something.

And so we put a chart in Dividend Café to try to highlight what it looks like, if we're going to need a different analogy than the one we always use in our industry with charts like this, which is hockey stick growth. I don't, this is just, not so than you normally would see. And I don't think that it's fair to say that all of these shiny object things out there that become very popular, people buy them because they're cool, they're new, they're hip, they're have high momentum. They have other words that only a 50 year old would use to try to sound like it's what people describe things as being cool and shiny.

However, the cannabis sector has gotten killed. The solar energy, clean energy disruptive innovation sectors have gotten killed. Rare earth mining has gotten killed. There are certain elements of shiny objects that are sustaining. They happen to be largely contained in big cap growth right now that have held certain things together. There's three, 3 trillion companies. There's two 2 trillion companies. There's one 1 trillion company. And then, there's 400 and something companies, less than a hundred billion. So that bigness has become the shiniest, but it's been working and yet the, and you just have to look a year old, two years old, three years old to see some of the shiniest object things out there that have gotten their faces ripped off.

There's a divergence amongst the land of the shiny. Okay. I think that's enough fun facts for the day. Check out Dividend Cafe for the charts and whatnot that I alluded to today. Have a wonderful weekend. I'm looking forward to being back in New York next week And there will be the fourth of july holiday, but we will have our normal monday Dividend Cafe where we go around the horn and then we will on friday the fifth have a special mid year Check in Dividend Cafe, in the meantime reach out with questions anytime and thank you for watching Thank you for listening and thank you for reading the Dividend Café.