ALTIUS Financial

Empowered Future Report

Short term thoughts about long term matters

May 20, 2020

Quote of the day:

"Who sows virtue reaps honor" -- Leonardo da Vinci

ALTIUS…..on the pandemic and opening up

Everyone is excited about getting back to work and "reopening" for business, which is generally a very good thing. But I wanted to make sure our clients, partners and employees are clear on my thinking here. This whole COVID health crisis and economic shutdown has caused a fair amount of anxiety and, it seems, exposed even more of our cultural divides.

First, I want to say thank you to my team here at ALTIUS. While we are very fortunate to be able to work from home and our group has in most cases made extraordinary efforts in the last few months to ensure we're not only functional but growing in our capacity to serve clients. Despite all the distractions that have come with this pandemic and the transition to a work from home environment – from supporting families, kids learning from home, pets wanting to join zoom calls and making the best of our workspaces – I've been proud of our transition. We have also attended to the office needs, checking the mail, getting necessary paperwork processed, maintaining the cleanliness and safety. We've also quickly embraced the fantastic technologies that allow for continuity and productivity. It's difficult because the longing for real connection is there but my belief is that we have been very accessible and responsive to client needs and that's a high priority. More and more I agree with the maxim that "when change is inevitable, flexibility is essential."

Second, as I've said throughout this crisis, the health of our team and our clients is a very important thing to me. We started working from home before the governor mandated it and we will continue to proceed with caution even though many companies are going back to work. Like a lot of business owners, I'm learning about my team, our adaptability and new potentials. I'm not sure we will ever fully return to the way things were before, but we won't be taking any unnecessary risks.

As you are aware, the mandated shutdowns are having an incredibly damaging effect on our state and nation's economy. My view is that these blanket shutdowns show a lack of leadership, tremendous violations of rights and a sign of panic on the part of many government officials. Yes, when you have the density, crammed public transportation, high infection rates in international travel hubs like Manhattan, it may have called for more drastic

(temporary) measures to protect people. But the crisis has been made much, much worse by government forbidding work, loss of jobs, businesses closing forever, mental health challenges, students losing a significant part of their education – not to mention increased suicides, abuse, depression and undiagnosed/untreated ailments of other kinds. Anyone who watched the flipflop on liquor stores and marijuana dispensaries as "essential services" here in Colorado must question the arbitrary nature in which these powers have been exercised.

There actually are many either/or choices in life but I absolutely think it's a false alternative between treating this virus as the serious health threat that is and having a productive economy. These sweeping lockdowns, it seems to me, have been a political decision and not driven by scientific or true health concerns. As a financial advisor and student of economic policy, I've spent my life studying *trade-offs* and it seems like that's what is lacking in how we're dealing with this pandemic: balancing real costs. I've already written and spoken extensively about the horribly distorting and crony empowering effects of the various stimulus packages Congress is foisting upon us, our children and our grandchildren.

But I must hasten to add that I think it's dangerously irresponsible for individual citizens to dismiss this pandemic as no big deal. From all we can tell, it is very transmissible and, especially in specific populations, it is life threatening. Yes, life will eventually end for all of us and, yes, life is full of risks…but life is precious and we can be grownups and respectful of those risks to others, even if we don't perceive it to be substantial for ourselves. We have several clients in healthcare, on the front lines, treating this disease and saving people's lives. They are not the ones preventing people from working – they're just doing their own jobs and I'm thankful for their minds, training, dedication and their objectivity.

I want to be clear that I am not in a hurry to have all of us return to the office on a daily basis. I believe the vast majority of you, our clients, have adapted as well and are mostly comfortable with meeting virtually. If you have an urgent need to meet me and/or Taylor in person, we want to know and will make all reasonable accommodations but, for your sake and ours, we'll take precautions. I had some extensive travel planned for this spring and summer, including speaking in Europe again, a conference in Austin and trips with my girls - all of which have been cancelled and I will keep you informed about future travel. My team and I are still limiting our social interactions and using PPE, as appropriate, to stay safe. Once we return, we request that you not schedule meetings if you have any symptoms at all, let us know if you've been traveling and follow appropriate guidelines. You're probably aware that Jenn has always made sure our office is extra clean and sanitized and that has/will continue even more so when we begin seeing clients in person.

On timing of when we will all be back in the office, I haven't quite decided but it will be based on my judgement regarding the safety of our team and our clients. My expectation is that potentially after July 1s would be appropriate for our unique circumstances, but we'll communicate more as we get closer to that date. While the local and state authorities are, in

my mind, starting to be somewhat more rational by allowing businesses to make their own responsible decisions, we can take our time. As long as we continue to deliver the excellent client service and responsiveness you expect of us, any downside risk of being too patient are manageable.

Our Workshops – Next on June 9th

We have held two virtual workshops over the last two months and I've been pleased with both the turnout and how we did…but it's really your evaluation that matters and, if you haven't already, I hope you'll take a few moments even if you did not attend to complete our survey here. This last one, we changed it up a little by having Taylor more involved, both with the main content (updating us on the CAREs act, the refinance market and the discussions she and I are having around Social Security strategy) as well as providing us a brief cooking lesson for homemade pizza. Many of you have asked for the recipe:

Recipe:
2cups flour
1cup water
1 packet of yeast
1.5 tsp sugar
Few shakes of salt, onion powder, garlic powder
2 tablespoons (or a hefty shake) of olive oil

-Stir all dry ingredients to combine
-add warmed water and oil stir until a dough begins to form
-knead dough on a countertop
-set in a bowl to rise and double in size
-once risen roll onto counter
-move to a pizza pan, tray, cast iron add toppings and bake at 450F for approx 9 mins (check at 7 or 8 as oven temps and cooking times vary)

We're going to continue trying different formats for our workshops, so we hope you'll participate and let us know what you think.

Please mark your calendar and look for an invitation regarding our next workshops on Tuesday, June 9th (10am and 6pm) – these will be a more intimate format where we'll allow a much smaller group (first come, first served) on the Zoom meeting so there can be more of a dialogue between us and all the participants. In the morning, we'll do a *Coffee & Conversation* and in the evening we'll do a *Drinks & Dialogue* format. Taylor and I will be on for both sessions, though one will take the lead and then we'll flip it for the other.

Overall Market Commentary

In this past workshop, as is my custom, I commented on the overall economic environment, the reactions by the capital markets and how we're adjusting our investment strategies. I'll briefly recap/elaborate on that now.

***I remind you that, if I mention specific securities, indexes or assets classes, nothing I say here should be construed as investment advice applicable to any particular individual or group. We have a number of people who, though not clients, do read this newsletter and we invite you to pass it on if you think someone might find it interesting, or better yet, we'd be happy to add them to our distribution list or talk to them about their situation/needs.

As I discussed above, the coercive shutdowns in reaction to the pandemic have caused a massive spike in unemployment which is collapsing consumer demand and GDP will potentially be negative for several quarters.

No one eats GDP but a drop in this economic abstraction is a sign that many might not be able to eat or eat as well as they've become accustomed to – I use "eat" here both literally and as a proxy for most other necessities and luxuries that human beings need and want to survive and thrive, including educating their kids, buy better living homes/living conditions/transportation, enjoy traveling/vacationing and exploring other cultures, etc. and receiving a good income/return on their activities and investments – which, of course, supports all the rest.

So, how to make sound financial decisions and allocate capital in such circumstances is particularly challenging. In the workshop, I laid out my framework for making any decision, posing the key philosophical questions that I think are really important but won't go into here – feel free to ping me if you want more details on the questions.

First, I was concerned about overvaluation of most asset classes well before the pandemic caused others to reevaluate their risk tolerance. This concern led us to be more conservative in our allocations and that has protected us some. We began to take a more constructive

approach in March but the major market indexes have recovered quite a bit, so I think most assets are still overvalued. Much of that overvaluation has been buoyed by easy money, low interest rates, a high debt public policy which bleeds/spirals into similar private decisions – and none of that is going away anytime soon.

It's interesting how investors look at things, even professionals. Fund managers who came of age during the last ten years have been characterized by some as "QE babies" (Quantitative Easing babies), or "born bulls" – having never really seen a bear market and believing that stock prices will be backed by the Federal Reserve no matter what. This, as I've stated over and over, is dangerous thinking. Yes, the Federal Reserve may print money, but it does not create wealth and stock prices ultimately must reflect actual wealth and production. I don't believe the US government is going bankrupt tomorrow but we're definitely on that path. The Congressional Budget Office recently totaled up all the legislative measures taken so far - as well as the effects of a shackled economy and prices not reflecting real costs (payments for generous unemployment benefits would be going up even without the recent law) - and they estimated this year's budget deficit at $3.7 trillion, which they forecast would represent about 18% of GDP. Even more trillions are working their way through the legislature and that's not counting the trillions the Fed has created/pumped into the economy already. We're talking an *annual deficit* trillions with a capital "T" and that stands for trouble since it's *just this year* and now being added to the trillions that already exist in the seemingly more permanent ongoing debt balances, we and our posterity already owe. Moreover, adding to the insult of what I characterized as crony empowerment, much of the new debt looks to be headed to state governments who were already in hoc for their long-time mismanagement and overpromising habits. I must say that Colorado is in somewhat better shape than many and much of that is due to the controversial but fiscally responsible TABOR law which has been under attack since it's passing in 1992.

As economist Brian Wesbury put it, "Yes, the debt is a burden on future taxpayers. In this way, the fiscal response magnifies the effects of other responses to the Coronavirus. So far, the age of the typical person who has died with the virus has been about 80 years old. Right or wrong, our government - and society in general - has taken enormous measures to contain the virus to save the lives of our elderly population, and these moves have imposed enormous costs disproportionately borne by the younger generations who are out of jobs, school, and business opportunities. The very same group who will be paying the costs well into the future."

For those who argue "don't fight the fed" and that you should just ride with the times, no matter the underlying fundamentals, there's an argument there, at least for the short term. I've said that I think it's possible we'll see higher highs on the Dow and S&P500 AND lower lows, all within the next year. For those who argue, no, the world is coming to an end as we know it and we should put all our money on the sidelines until everything settles down, it's definitely understandable, *but that's been horrible investment advice during every other downturn in American history* – longer term goals warrant longer term, more optimistic

outlooks no matter how bleak things look as we sit today. So, we are opting for a more nuanced position, while staying disciplined about historical valuations and tailoring our models to what I consider to be your real risks and tolerance for volatility.

Despite Wall Street's divergence from the Main Street economy, I don't think the full weight of what's happened will be evident to most investors until we get past 2nd quarter reporting, starting in July. We've heard from most major firms regarding their experience in the first quarter and most of them withdrew "guidance", admitting they really couldn't tell what was going to happen to their revenue and profitability. And, of course, these are just indications from large publicly traded (NOT publicly owned) firms. But small businesses employ close to half of all workers and create over 65% of new jobs. These small companies that have been disproportionately affected by the shutdowns, are viewed by many as a much better indicator of the health of our economy. Below is a chart from the WSJ-Vistage Small Business Confidence index.

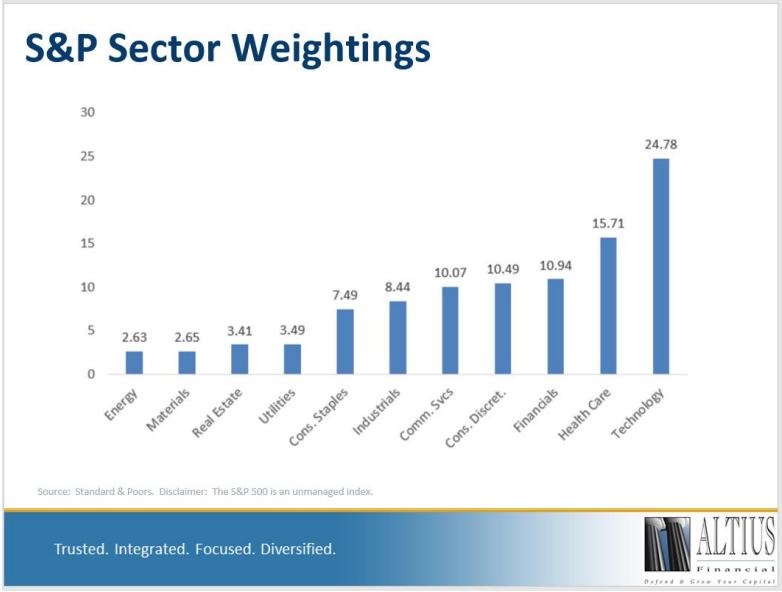
So how do I reconcile such bad news with a more balanced approach to risk and investing right now? What do I mean by "staying disciplined about historical valuations"? Where do we allocate capital (yours, mine and my mom's)? Well, I think it's important to bring up another quote from famous value investor, Shelby Davis (grandfather of Chris Davis, who runs the Clipper Fund we often use): "You make most of your money in a bear market; you just don't realize it at the time."

We are staying with some important core holdings: businesses/industries that we know and understand, and that we have tremendous confidence in the honesty, integrity, judgement and long-term focus of their leadership. In the case of active fund companies, that means

Clipper (mentioned above) Tweedy Browne, First Eagle, Hussman and Vanguard and potentially use of Janus in the area of technology. There are specific funds within those families we use for specific reasons – so definitely NOT all their fund offerings. In the case of specific stocks, that means strong financial/insurance conglomerates (Berkshire Hathaway, Fairfax Financial and possibly more Markel if/and as pricing gets more attractive), cable/media companies who's broadband and entertainment businesses look to be even more attractive in the long term because of the pandemic (Comcast, Liberty, Disney).

Now, some of the newer ideas mentioned in the workshop and that we are pursuing: biotech, other tech, energy, travel, and finance. While not quite new to our models, we've been using the Fidelity Biotech Fund and, while I warn about the volatility and originally added it based upon the trend of innovation, genome/disease/life extension research, this has been a good thing to have in our portfolios given the pandemic. It's an exciting and promising field with the challenge/risk that so much money has to be invested in such research with no guarantees of whether you will hit the right combination of a workable drug/device/methodology ALONG with FDA approval, perfect timing of marketing and distribution.

Also, in the fund/ETF category is energy – mostly the Vanguard Energy Admiral Fund with potential in the iShares Clean Energy ETF. Energy has been beaten down bad by a wicked storm of demand collapse potentially lasting longer than people realize, many many regulatory/environmental hurdles, a glut of oil and more, potentially devastating washout coming in the American fracking industry, irrational and short term price wars by Russia and the Saudis, etc. However, if we are ever to recover economically, cheap reliable energy will indeed be necessary, and the valuations are compelling. As I showed in the workshop:



The energy sector now is the smallest (by market cap) of the eleven different S&P sectors in the economy and the entire sector combined is worth about half of ONE tech company (Microsoft) today. I thought energy was cheap before COVID and now even more so. There is

no recovery without energy; I believe there will be more pressure (even though potentially driven by cronyism) for infrastructure spending, which requires lots of energy; the massive stimulus could be potentially inflationary which usually flows through commodities/energy early on; and inflationary pressure could build rapidly given that many people, though having been laid off, have more purchasing power than they otherwise would have; lastly, many major producers of energy (Russia, Saudi Arabia, some South American and Scandinavian countries) rely heavily on higher prices to support their welfare states. In many cases, they may not really care that much about their people, but they do care about staying in power and this leads me to believe that there is potentially more pressure on prices. Also, many of you know that I've been skeptical of "alternative energy" for awhile, believing that these industries were not economic and were way to subject to government subsides, which blows with the political winds. I think this is still true to some degree but that there are more and better technologies and business models proving themselves. I wish the culture took a more balanced look at energy generally, including nuclear options, but we are opening up to the case and that's why you might see more "clean energy" exposure.

We've also been nibbling at the travel/airline industry mostly in the form of an ETF called JETS but also some individual airlines. This is a tough one because airlines certainly have become smarter about managing much of their business but have been among the hardest hit by the pandemic. It's a difficult industry since it will be affected by fear on one hand; subsidies, bailouts, politicization on another hand; lower fuel costs for now and likely lower/more competitive wage market on another hand; potential pent up demand for travel on a…how many hands is that? Ok, we see opportunity but are going slow here….

These are a few examples we discussed, along with others, and of course are subject to change. While not new, I want to also stress my position on precious metals as this is mostly unique among our competitors. I won't go into detail since I've communicated frequently about it to current clients (ask if you need more information) but during such uncertain times, it's important for you to understand that your hard earned wealth is either going to be consumed now or in the future. If you're an investor, you're saying some of/much of it is for the future and that's what you want money to be – a store of value for the future. The problem is that money that is printed or created out of thin air has never been a good store of actual value…as they say, "the Fed can't print gold". The following chart shows some statistics comparing today verses the third quarter of 2011, when the price of gold hit it's all time high. These, to me, show that even though we've seen solid returns on our precious metals-based exposure, there is still solid or better underlying value in having such exposure, though it can be a bumpy ride.

Gold then and now

	Current	3Q11
Gold price (in $/oz)*	1,702	1,900
Year-over-year growth in M-3**	20.47%	2.43%
Federal Reserve assets/GDP†	24.40%	18.30%
U.S. debt outstanding (in $ bns)	25,153.11	14,790.34
Unemployment rate	14.7%	9.00%
Real interest rate on 10-year UST	0.66%	-1.98%
Sprott Gold Equity Fund AUM (in $ mns)*	1,093.00	3,000.00

* As of previous gold-price high on Sept. 5, 2011 and May 11, 2020.
** April 2020 estimate.
† As of 1Q20.

sources: ShadowStats.com, Board of Governors of the Federal Reserve, U.S. Department of the Treasury, Bureau of Economic Analysis, the Bloomberg

Now remember, gold itself is not exactly an "investment asset" – it creates no income and is not "productive" in the way that a business or real estate can be. But paper money cannot act as a true store of value as it should. Paraphrasing Ayn Rand: "money is [should] be a frozen form of productive energy"; it represents your energy, your work…a big part of your life. Savings (money stored) and it's real value should be protected as the result of virtue – long term planning and delayed gratification. Unfortunately, paper money is ultimately just another debt that can be repriced or defaulted upon – not a real value, in its own right. Today is potentially the perfect storm for gold. We've had incredible debasement of sovereign currencies by most of the world's central banks, with extended artificial interest rates, and restriction on new mining due to operational and environmental issues, now coupled with almost all mining costs (energy, etc.) dropping precipitously. If you haven't considered this important asset class, we are obviously thinking about it for our clients, but I want you to understand why.

***Again, none of the investment strategies mentioned here should be construed as individual investment advice and are provide only for illustrative purposes. Past performance is no indication of future performance. Please consult prospectuses and competent financial/tax/legal advice before making any investment decisions.

Website Update

Ok, I'm not exactly a marketing genius and would much rather be having conversations with you about your goals and concerns or researching the best possible places to defend and grow your capital over trying to find new ways of gaining clients and keeping our image up to date. But we do have more capacity and now the pain point (Taylor and some of you have been mostly benevolent in your nagging) on our aging website has reached the level of action forcing to me. We're about to unveil a fresher version and so I just want to mention that it will

hopefully be a better resource to you, using better tools and mobile access. The address won't change so there's nothing you need to do but we'll probably launch it by the first of June so look for it soon and let us know what you think.

Two Books and a TV Show

As I mentioned in the workshop, perhaps we'll start recommending more books, TV shows, movies to each other. Like some of you, I've been working more than ever since transitioning to home but have tried to find new entertainment. Ok, I'll admit my book recommendations this time are not exactly most people's idea of entertainment but I think they're both excellent, especially right now.

- Thinking in Bets, by Annie Duke – I may have mentioned this to you before but it's fantastic as a story of her life and as instruction in how to make decisions in an uncertain world. She explains that life is like poker, not chess…and has numerous entertaining examples from real life.
- Enlightenment Now, by Steven Pinker – One promotional blurb captures why I recommend it: "If you think the world is coming to an end, think again: people are living longer, healthier, freer, and happier lives, and while our problems are formidable, the solutions lie in the Enlightenment ideal of using reason and science." It won't necessarily support any/all of your political views – I disagreed with plenty - and Pinker called for more attention to the issue of virus contagion well before this pandemic. It is a really a good news story that everyone should read and heed.

Now for the TV show:

- Mr. Sunshine – no, not the one with Mathew Perry….it's a 2018 South Korean television series with subtitles, which might normally turn me off. I was surprised at how quickly my girls loved the series and are often explaining the plot twists to me. The first episode will confuse the heck out of you but lure you in and after that, you'll be intrigued by the romance, history and conflict. As one of my long time clients, who I consult often on matters of quality stage, movie and tv recommendations, said: "Fabulous cinematography... stunning sets and costumes... a fascinating piece of history that I know nothing about...roiling melodrama that reminds me of those epic mini-series from the 80s, like Winds of War and The Thorn Birds." This same client provided me a very helpful character map that you can probably google or I'll forward if interested.

Have a Fantastic Memorial Day Weekend!

If you made it here, I know this newsletter probably felt more like Mike's long term ramblings on everything – I appreciate your staying with me and please take care of yourself - know that we are here for you.