



The Good, the Bad, and the Ugly

The Good, the Bad, and the Ugly is a 1966 Italian spaghetti Western film starring Clint Eastwood. The movie’s plot centers around Eastwood’s character forming an uneasy relationship with the “Bad” and the “Ugly”, in the search for \$200,000 of gold. **October’s performance (+3.5%) was split into three similar categories.** The good, was our financial stocks led by JPMorgan, Berkshire Hathaway, and Goldman Sachs, and Apple. The bad was our technology holdings, including Google, Microsoft, and Amazon, while the ugly was Meta. With Markets’ moving higher in October, we were pleased to have generated positive returns, yet our disproportional degree of bad and ugly has us searching for answers.

From the table below, significant inferences can be made. Over the past 3 years, the growth of revenues and earnings of each of these companies has been astounding. Specifically, sales have increased by \$638 Billion to nearly \$1.5T, representing 75% growth, while earnings have increased by \$148 billion, or 84%, outpacing revenue growth. Despite the astounding improvement of these metrics, the market capitalizations have not budged. **In fact, at the time of writing, the combined market capitalizations are essentially flat at \$6 Trillion.**

Dollar change (2022 LTM) versus 2019

| Company | Market Cap \$ | Revenue \$ | Earnings \$ | Decline from ATH |
|--------------|---------------|----------------|----------------|------------------|
| Microsoft | -200B | +71B | +36B | 35% |
| Amazon | +7B | +282B | +9B | 53% |
| Apple | +400B | +150B | +54B | 25% |
| Meta | -320B | +61B | +9B | 75% |
| Google | +200B | +74B | +40B | 42% |
| Total | +\$87B | +\$648B | +\$148B | |

Without question, there are only two possible answers that can explain this riddle –historic overvaluation or opportunity. With respect to overvaluation, I will eliminate this assertion immediately. Prior to covid, Microsoft was trading at 25X, Apple 16x, Meta 15x, Google 20x and Amazon at 70x (note that Amazon always has traded at a premium multiple as it builds out its infrastructure and expenses the costs). None of these are lofted multiples, nor do I recall anyone claiming the FAANG’s were overvalued.

We believe the recent price declines represent opportunity and note from the chart above, how far they have fallen. This conclusion is based on **our knowledge that earnings, free cash flows and balance sheets are the factors that determine value.** After their past three years of dramatic growth, it is not surprising that their near-term prospects have declined; Yet their \$600B in cash and \$350B in annualized cash flows should allow for significant future growth. Each now trade at P/E multiples that are among their lowest in history (except for Apple) and all are trading at discounts of

50%+ to their respective intrinsic value as calculated using discounted cash flows (DCF's).

Recently, we have taken advantage of these declines and added to our positions.

In the movie, The Good, the Bad and the Ugly, Clint Eastwood stars as “the Man with No Name”. One of his most famous lines is “every gun makes its own tune” in direct reference to the fact that no two guns are identical, despite their model. Like Eastwood’s guns, all companies are not alike. Like the movie, we are confident that our holdings will come together and strike gold. We maintain optimism, look forward to next month’s communication and thank you for your continued support.

Sincerely,

Steven Tucher
Founder and CIO

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