

CAZ Investments
Quarterly Letter

The Return of the Trade War

What a difference a weekend makes. As we write this, on May 6, 2019, the markets have been jolted by the President's actions over the weekend to increase the pressure on China in the trade negotiations. Just Friday, markets were celebrating historically low levels of unemployment and challenging all-time highs for stocks. This type of move illustrates how the markets are so heavily influenced by news flow and geo-politics. Therefore, investors need to avoid complacency and be sure that equity allocations are monitored to be sure they have not grown too large for the risk tolerance of the portfolio.

With this letter, we are reducing our rating on the **CAZ Scale from a 2 to a 1, our lowest level**. To be clear, we are not doing this based on trade related gyrations, or any other specific catalyst. We are reducing our rating on the Scale based on the fact that valuations have risen with the markets, we continue to see operating margin pressure at companies (as we discussed at length last quarter), and the risks from these levels are simply higher. As a reminder, the Scale is not a market timing tool, it is a risk/reward barometer. Investors should be comfortable with their stock market exposure and we would suggest maintaining exposures at the lower end of target allocations.

Strong Economy – OK Earnings

As of this writing, we are about halfway through the 1st Quarter earnings reporting season and the results have been "ok." They haven't been great, and they haven't been horrible. As always occurs, there have been some high-profile misses and beats, but by and large we have heard what we expected to hear from most companies. The uniform thing that most every company is talking about continues to be wage inflation. In many parts of the country, there simply are not enough workers for the jobs that are available. Companies are feeling pressure in two ways: in the cost of wages and in their ability to expand as rapidly as they might desire. The problem is not yet severe, but it is a challenge facing most every business in nearly every industry, with acute difficulties being experienced in certain sectors and geographies. This is creating operating margin pressure and that is going to make it harder to justify the valuations for many companies.

The economy continues to grow at a reasonable pace. The Federal Reserve appears to be on hold for the foreseeable future and so we are not likely to see any short-term rate increases. That is a positive and a negative. The positive is that we won't have valuation pressures from rising rates; the negative is that the Fed appears to believe that the economy is slowing and that we may not see the growth that they were expecting just a few quarters ago.

There are very few things in this world that one can say with total confidence. One of those things that is safe to state is that we are going to see gridlock in Washington D.C. for the next 18 months. Many will argue that is a good thing, as that is less that the government can do to mess things up, but the reality is that we have systemic issues that really need to be addressed and there is little to no chance that any of those items will be dealt with prior to January of 2021. The one potential area where consensus exists on both sides of the aisle would be infrastructure spending. We would expect a very significant effort from both sides to get a major infrastructure bill passed before year-end. Both sides will then claim victory from the campaign stump and ultimately there



1st Quarter 2019

will be a new round of very significant deficit spending, and economic stimulus, that is likely to result from that legislation.

Our team continues to expand, and we are very excited about many of the projects we are working on. It is very difficult to find compelling investment themes in an expensive world, and investments to maximize returns from those themes, but we are leaving no stone unturned looking for those opportunities. We will keep you posted on our progress and let you know when we identify actionable investments.

We are very pleased to now be able to offer one single place that you can go to get access to all quarterly update videos. When you click on the name of any fund on your statement, a hyperlink will direct you to a private page on our website that hosts all of our videos for that class of investment. We cannot emphasize enough how valuable those short videos will be for you. In 3 – 5 minutes we summarize everything that we believe you would want to know about how the investment is progressing. Please make it a priority to watch the video for each of the investments that you have made alongside us. You will be educated and feel informed as to what is happening in our portfolio. Please let us know if you have any trouble getting to the videos.

Yes, it may be early, but we would like everyone to go ahead and save January 14, 2020 on your calendar. That is the date for our Themes for 2020 event. We already have a very high-profile speaker confirmed for the evening, and you will want to be in attendance. In the meantime, we look forward to the second half of the year and hope to see you very soon.

All our very best,

The CAZ Investments Team

