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Phil Kiernan's

Highlander Report

Creating Wealth by Avoiding the Herd

Inflation and Speculation

by Philip J. Kiernan, Jr.

In our last issue, I highlighted the difference between working with an asset management firm like ours versus an asset gathering approach. Asset gatherers often use outsourced ETF programs or sell packaged products such as mutual funds and annuities, and, as a result many investors today don't know who is actually managing their money.

On August 20-22, 2021, I had the pleasure of meeting many of my Florida clients at an event I hosted at the Hilton Cocoa Beach Oceanfront. We discussed some of the speculative excesses that have occurred during my almost 27-year career. Among them were the Long-Term Capital Management crisis in 1998, the dot.com bubble (1999-2000) and the financial crisis/housing bubble in 2007-2008. Today we have what is in my opinion an "everything" bubble. Tech stocks, crypto currencies, NFTs, classic cars and real estate in many areas are all examples of this "everything" bubble. In this vein, I am looking forward to hosting the sequel to *The Housing Bubble* movie (see back page), *The Bigger Bubble* documentary, sometime in late spring or early summer 2022, live in New Jersey.

The effect of zero percent interest rates for too many years as well as the accompanying FOMO ("Fear of Missing Out") has led to irrational decision making in many of these asset classes. One sees this with new investors and their trading applications being encouraged to gamble/speculate with little or no due diligence.

While in Florida, I reviewed everyone's portfolios and the stocks that they're invested in. Topics discussed included free cash flow, stock buy backs, and reading investor presentations on the companies' websites. I reiterated that investing in stocks represents fractional ownership of a business and not just a flashing red and green light on a computer screen. We also discussed my willingness and ability to hold cash positions in the absence of attractive purchase prices. This is not meant to be an exercise in market timing, as in my opinion, jumping in and out of the market is a fool's errand. I'm happy to say that I received positive feedback from those who attended.

Our Motto is "Creating Wealth by Avoiding the Herd"

Our primary process is to identify and invest in good businesses at attractive valuations and we consider ourselves to be disciplined buyers.

If you buy into a well-run business at a reasonable valuation, that's run by capable and honest management who are not only good at running the business, but skilled at making prudent capital allocation decisions, then you are very likely to have a good outcome.

Constructing a portfolio with a collection of 15-20 companies that fit those characteristics should over time, produce satisfactory returns.

I purchased these "WIN" pins to highlight past failed programs by President Gerald Ford's administration.

The (WIN) Whip Inflation Now policy designed to combat inflation was a disaster. Inflation is currently reported at around 7%. Investors in a 10 year treasury bond are receiving around +/- 2%. Does anyone see a problem with that?

Meet Your Highlander Team

Philip J. Kiernan, Jr.
Senior Managing Director, Senior Portfolio Manager

Phil entered the securities industry in 1994 while obtaining his BS degree in Business Administration from Montclair State University . After graduation he was asked to join the University's Alumni Association Board of Directors where he served from 1997-2008. He also served as their representative to the Montclair State Foundation Board of Trustees from 1998-2008.

Phil is a lifelong Giants fan (as well as season tickets holder). His investment commentary has appeared in *The Wall Street Journal, U.S. News & World Report, The New York Post* and CNBC.com. Phil maintains FINRA Series 7, 24, 63 and 66 licenses.

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Eckart A. Weeck
Senior Managing Director, Senior Portfolio Manager

Eckart has over 30 years of direct investment and portfolio management experience. Prospective clients are invited to read his annual client letters under the commentary tab on www.highlanderreport.com. He maintains FINRA series 7, 24 and 63 licenses.

Eckart has a B.A. in Economics from Fairleigh Dickinson University.

He is an avid runner and longtime member of the Hoboken Harriers Running Club.

Highlander Capital Management, LLC, founded in 1996, incorporates a disciplined approach to provide you with the peace of mind and confidence that accompanies superior professional management services.

We are a dynamic team of seasoned and accessible financial professionals with complementary skills, experienced in many financial markets. Fee-based advisors, we utilize easy-to-understand investments to focus on reaching your long-term goals. Our Separately Managed Accounts are investment portfolios custom-designed for each individual client including:

- Equity Portfolios for capital appreciation
- Balanced Portfolios for capital appreciation plus income
- Fixed-Income Portfolios for income generation.

Douglas MacWright
Founder, President, Chief Executive Officer

Ryan MacWright
CFP®Certified Financial Planner™ (CFP®),
Research Analyst, Associate Portfolio Manager

Cheri L. Harris
Senior Portfolio Manager, Fixed Income Specialist

Ellen D. Sandler
Senior Managing Director, Senior Portfolio Manager

Richard K. Martino
Director

Steve Caruso, MBA
Managing Director

Cindy E. Bluestein
Senior Manager of Client Support Services,
Operations Manager

Eckart's Excerpts

2021

In Eckart's 2021 Shareholder Letter he indicated that we have assembled what we believe to be a reasonably diversified portfolio of companies, at favorable prices, that should generate good returns over time.

"As a practical matter we should expect several increases in the Fed funds rate and an end to the Fed's bond buying; the era of free money seems to have ended. From an investment standpoint, we have no special insights into the magnitude or duration of the upcoming rate hikes, only that they will likely cause headwinds for stock valuations. Particularly vulnerable are those that are richly valued with far off earnings streams. To understand why it is that high-multiple stocks are disproportionally impacted by higher interest rates, one can use a discounted cash flow formula. The present value of any business is the current value of future cash-flows. In order to obtain present value, future cash flows need to be "discounted". When interest rates are near zero, future cash flows- no matter how far off- are as valuable as current ones, and thus stock price values- based on those far off cash flows- can become grossly inflated. This may account for the extreme valuation disparity between expensive stocks (those defined as having a price to sales multiple of 10X) and the cheapest quintile of stocks (also as measured by price to sales). By late last year the expensive cohort were worth $14 trillion versus $4 trillion for the cheapest. This valuation disparity is similar in scope to that of the dot.com boom of the early 2000s. We wrote about the subsequent 78% peak to trough decline in the NASDAQ in last year's letter and believe mean reversion is likely with respect to the high price to sales cohort."

2020

In Eckart's 2020 Shareholder Letter he highlighted the performance of the S&P 500 during the "lost decade". Measured from January 1, 2000 thru December 31, 2009 the index returned a cumulative 4.56% or .41% per year including dividends.

"Much like the early 2000s, a large component of the S&P 500 is characterized by high multiple technology companies. The top 5 companies (AAPL, MSFT, AMZN, FB, TSLA) make up more than 20% of the index. At the end of the first decade of the new millennium, the S&P 500 index produced an overall 10-year return of 4.56%, or .41% per annum including dividends. This mediocre return was due in large part to the big tech companies' inability to live up to the extremely high expectations priced into the stocks at the beginning of that decade. Given the current high multiples, we think multiple compression, rather than expansion, is probable for the current crop of market leaders. This suggests that passive returns will lag and, as a corollary, active managers owning attractively priced securities other than the current leaders will perform better."

Eckart manages the Highlander composite portfolio. His annual shareholder letters back to 1999 can be found on the market commentary tab at ***www.highlanderreport.com***.

Client Appreciation Events

Photo Credit -Michael Priest

Client appreciation event with NFL player Damon "Snacks" Harrison at our Short Hills, NJ office coordinated with Steiner Sports Marketing.

We hosted the (virtual due to the pandemic) New Jersey premiere of *The Housing Bubble Movie* directed by Jimmy Morrison. This documentary on the financial crisis featured many notable economic and financial experts.

"Be fearful when others are greedy and greedy when others are fearful."

–Warren Buffet

Past Client Conferences

These events allowed us to meet individually with clients in those areas and review their portfolios and discuss all of their positions.

Turning Stone Business Center
Verona, NY

Hilton Cocoa Beach Oceanfront
Cocoa Beach, Florida