Old West Investment Management, LLC

January 16, 2024

Dear Investor,

The stock market finished 2023 on a high note with the S&P up 11% in the fourth quarter and 24% for the year. The Russell 2000 Small Cap Index was up 17%. At year end, there was tremendous bullish sentiment among individual investors who are apparently ignoring many risks at home and across the globe. As impressive as the 24% gain was last year, it only got the market back to even after 2022's 19% loss.

As you can see on your enclosed statement, although the Old West portfolios under-performed their benchmarks in 2023, this was the first time we under-performed in the past four years. Our three-year and five-year numbers continue to be some of the best in the business.

Much has been made of the dramatic effect the magnificent 7 stocks had on the S&P 500 last year. Apple was up 48%, Microsoft up 57%, Alphabet up 58%, Amazon up 81%, Nvidia up 239%, Meta up 194%, and Tesla up 102%. As an American, I am proud of the dominance and success of these companies on the world stage. As a value investor, I look on in dismay. The MSCI index, which is comprised of companies worldwide, is 62% invested in U.S companies. Contrast this to the U.S. representing only 4.2% of global population and 15.4% of global GDP. Looked at a different way, the Magnificent 7 stocks are nearly the same value as the combined equity weightings of Canada, Japan, the U.K., China and France. The Magnificent 7 stocks made up 70% of the S&P 500 gain last year, and 72% of the 500 stocks in the S&P under-performed the index. This type of concentration of performance is rarely seen. The only Magnificent 7 stock in the Dow index is Apple. If you look at the ratio of the Dow/S&P 500, it's the lowest since the 2000 tech bubble. Remember what Mark Twain said about history repeating itself.

With the market near all-time highs, it begs the question, "Are valuations justified?" The measurement that makes the most sense to me is the Buffett Indicator (Warren's favorite); the ratio of total equity value, as measured by the Wilshire 5000, to the U.S. GDP. The indicator is currently 180%, which is 50% higher than the historical trend line, and higher than the 159% reached at the peak of the dot.com bubble. Apple is the world's most valuable company and is trading at 31 times earnings, double its historical average. Apples's revenue has fallen for four consecutive quarters and profit growth is negative. Microsoft is the world's second most valuable company and is trading at 36 times earnings. Revenue grew 3.7% last year and net income grew by 3.5%. 42% of all public companies are currently losing money, something you only see during recessions. All of these facts and figures reinforce my belief that value investing is the best way to protect and grow capital. Trillions of dollars have been invested in the mega-cap tech companies not because investors are up until midnight reading the 10-K's, but rather because trillions are invested in passive index funds that are market weighted. The higher they go – the higher they go.

There is a lot to worry about in today's world, but there is no greater threat to our country and our markets than our out-of-control budget deficits, which I have written about in past letters. In just the past few days, the total government debt surpassed $34 Trillion. The U.S Treasury market is now 14% bigger than our banking system. As a reference point, in 2006, the Treasury market was only 44% of the total banking system. The U.S. Treasury Department has a massive task before it. We need to fund this year's $2 Trillion deficit, fund $1 Trillion in interest on our debt, and we have $7.6 Trillion in maturing debt next year (31% of the total debt). In the past we were able to depend on China, Japan, and other foreign governments to participate in our debt offerings, but that is no longer the case, as both China and Japan have massive debt problems of their own. The business media pays a ridiculous amount of attention to the Fed and speculation as to when the Fed will begin cutting rates. At Old West, we believe the Fed might lose control of the interest rate narrative as massive government debt issuance causes rates to stay higher for longer. A very likely outcome is that the Fed becomes the buyer of last resort, akin to Japan, to fill the gap of a lack of buyers for our debt. This will be extremely bullish for gold and commodities. Our portfolios have significant exposure to metals producing companies that will greatly benefit from a weakening dollar and the pending commodity super cycle.

We are in uncharted waters with this debt situation. There has never been this much federal debt relative to GDP, and the debt interest expense has never been this high relative to the budget. The current average interest rate on the federal debt is 2.6%. As I said earlier, we have $7.6 Trillion maturing this year which will be refinanced at rates exceeding 4%. Add to this state and local government borrowing needs, and you can see a debt crisis brewing. One more tidbit…there is $500 billion of commercial real estate debt coming due in 2024, followed by another $500 Billion in 2025. It's amazing to me that this issue is not getting more attention. The media is obsessed with how AI is revolutionizing our lives while turning a blind eye to this brewing crisis.

<u>U-Haul Holding Company</u> (UHAL)

A real sweet spot for our investment style is discovering companies run by owner/managers, CEOs with huge ownership stakes in their company. It's hard to find a better example of this then Joe Shoen, CEO and Chairman of U-HAUL Holdings (UHAL). Shoen owns 55%

of the company, with his stake valued at nearly $6 Billion, and his total annual compensation is $1 million. He clearly has more to gain from a higher stock price than his paycheck.

UHAL is based in Reno, Nevada, and is North America's largest "do-it-yourself" moving and storage operator. UHAL is synonymous with self-moving and is four times larger than its biggest competitor, Penske Truck Leasing. UHAL was founded in 1945 by Shoen's father as a trailer rental company and began renting trucks in 1959. In 1973 they began their network of U-HAUL managed retail stores where they rent trucks and trailers, self-storage units and moving supplies like boxes and tape. UHAL has 23,000 locations in North America of which 2,200 are company-owned and over 21,000 are independent franchised dealers. UHAL's rental fleet consists of 192,000 trucks, 138,000 trailers and 44,000 towing devices.

A major growth area for the company has been the self-storage business. Most locations have large property footprints, and with a captive audience walking in the door it made the storage business a natural. They now operate 1,900 self-storage locations with 950,000 storage units.

The pricing of UHAL moving trucks has recently been coined the UHAL growth index. It can cost $1,200 to rent a truck from California to Texas, and as little as $400 from Texas to California. It has become a useful tool to track migration patterns between states. Last year the leading migration growth rates were Texas, Florida, and North Carolina. The states suffering the most losses were California, Massachusetts, and Illinois.

For fiscal year 2023 UHAL had $5.75 Billion in revenue and $923 million in GAAP net income. Revenue has grown 70% over the past five years. GAAP earnings per share were $4.71, and with today's share price at $67, the shares are trading at 14 times earnings. UHAL's share price has doubled over the past five years. One negative of UHAL's financial performance has been the lack of free cash flow. This is due to huge capital expenditures of more than $2 billion per year due to the build-out of their self-storage business. This is expected to subside in the future as the build-out develops. UHAL has a strong balance sheet with net debt at 2.1 times EBITDA and interest coverage of 8.5X. The current market Cap is $12.8 Billion.

Joe Shoen does not have a great reputation with Wall Street analysts. He rarely speaks to the press, and he chafes at certain questions on conference calls. He doesn't like analyst's focus on short term results, and he chooses to focus on the big picture and long-term results. While many money managers are happy to invest in money losing tech companies trading at a high multiple of revenue, we prefer to invest in solid companies like UHAL run by owner/operators like Joe Shoen.

Thank you for your continued loyalty and support and we wish you a happy, healthy and prosperous 2024.

Sincerely,

Joseph Boskovich, Sr.
Chairman and Chief Investment Officer

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