Auxier REPORT

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## Fall 2023 Market Commentary

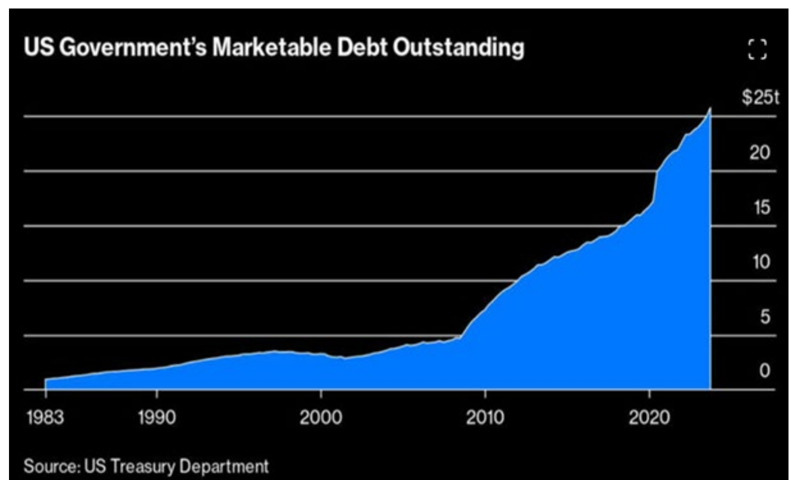
The "bond vigilantes" came out of hibernation in the quarter as longer-term bond rates moved up to compensate for growing government deficits, bond supplies and the new surge in defense spending needed in the fight against global evil. Just as Silicon Valley Bank and First Republic failed due to balance sheet mismanagement, the bond market is coming alive in the face of a deteriorating federal balance sheet.

**Table 1: The greatest Treasury bear market of all time.. 2020-today**
History of US Treasury bond bear markets

| Date of Market Peak | Date of Market Trough | Peak to Trough Performance | Recovery One Year from Trough | Duration of Bear Market (mos) |
|---|---|---|---|---|
| 7/31/2020 | 10/31/2022 | -24.7% | 0.0% | 28 |
| 06/30/1860 | 05/31/1861 | -18.7% | 32.4% | 12 |
| 05/31/1835 | 12/31/1839 | -16.1% | 19.0% | 56 |
| 06/30/1979 | 02/29/1980 | -15.8% | 8.2% | 9 |
| 05/31/1931 | 01/31/1932 | -15.4% | 18.5% | 9 |
| 06/30/1980 | 09/30/1981 | -14.6% | 43.1% | 16 |
| 09/30/1833 | 03/31/1834 | -13.7% | 16.5% | 7 |
| 05/31/1811 | 03/31/1813 | -11.3% | 6.8% | 23 |
| 02/28/1987 | 09/30/1987 | -10.5% | 14.7% | 8 |
| 10/31/1993 | 11/30/1994 | -10.2% | 25.1% | 14 |
| 7/31/2012 | 12/31/2013 | -10.1% | 10.8% | 18 |

Source: BofA Global Investment Strategy, Global Financial Data; "bond bear market" = total return decline of 10% or more

For the past three years we have been reporting on bond market risk with record low yields leading to record high risk. This quarter, longer-duration Treasuries have suffered drops that rival some of the biggest US stock market crashes in history. According to data from Bloomberg, at the end of the quarter bonds with maturities over 10 years were down 46% since their highs in March of 2020. This drop was almost as large as the 49% decline that the stock market saw during the dot-com bubble. Near the end of September, the 20-year Treasury bond had fallen by 48% from its 2020 highs. 30-year bonds have struggled even more, down over 50% which is nearly as high as the 57% drop equities saw during the 2008 financial crisis. US Treasury yields recently reached their highest level since 2007 with 30-year and 10-year Treasuries rising to over 5% and 4.7%, respectively. Using historical bond market data, strategists from Bank of America found that the current bond bear market is the worst in US history as shown in this chart detailing some of the largest peak-to-trough drops.




Years of low interest rates made it easy for the government to invest trillions into new programs and free money masked the issue of skyrocketing debt. The Congressional Budget Office estimates that if the government does not change course, they will add more than $20 trillion to the national debt in the next 10 years. However, higher rates may spur the government to return to a more reasonable spending budget. While the federal deficit has improved since the pandemic it is still

higher than any time prior to the 2008 financial crisis. The last time the federal government was in a surplus was in 2001. With elevated rates becoming the new normal and the era of free and easy money seemingly at an end, more prudent debt management from businesses will be vital.

Historically a free functioning bond market has been just as, if not more, volatile than the stock market. I can remember 1994 when rates climbed 2.5% and 1987 when rates rose 3%. Both led to sharp declines and great investment opportunities in quality businesses.

The S&P 500 Utilities Index was the worst performing sector, down 9.25% and 14.4% year-to-date. Utilities suffer from negative cash flow, a reliance on debt financing and high mandatory capital spending —a toxic combination in a rising interest rate environment. We see growing legal liabilities in west coast utilities due to fires, in particular for both PacifiCorp and Hawaiian Electric. This period of heavy capital investment reminds me of the late 1970s and early 1980s when the utility industry embarked on a massive investment in nuclear power plants. Rising inflation and interest rates led to cost overruns that state rate commissions were unwilling to absorb, hammering shareholders. Today, windmills are suffering from similar headwinds and do not pencil without major subsidies. Many are being replaced after only 10 years. That is why we gravitate to businesses with low mandatory capital spending, steady demand dictated by free markets (not government mandates) and high inventory turns with growing free cash flow.

**Dangers of Buying into the Hype**

Over the last several years, more companies have gone public with sky-high valuations, little-to-no profit and big promises of transforming their markets. When money was cheap it was easy for a new business to attract significant investment. Not so today as the spigot is shut off. One company that fell victim to overhype is Beyond Meat which went public in May of 2019. The alternative meat company's stock surged 163% on its first day of trading which at the time made it one of the best day-one performances for an IPO in nearly 20 years. JPMorgan originally estimated that Beyond Meat would be able to grow their sales to $5 billion in 15 years. The hope was that millions would abandon traditional meat for plant-based meat which was deemed to be more environmentally friendly and sustainable. After the IPO, the market consensus was for Beyond Meat to turn free cash flow positive by 2022 and have compound annual sales growth of around 40%. Instead sales fell 10% that year and they have yet to attain positive free cash flow even today. The company continues to struggle due to factors like its premium price and low availability. Since the stock's all-time high in July of 2019, it has fallen over 95%. Another more extreme example of a torpedo is WeWork. Its valuation ballooned to $47 billion in 2019 before crashing to less than $100 million today and it is closing in on bankruptcy. Euphoria surrounding the growth of electric vehicles led Rivian's valuation to surpass $120 billion before the company reported even a single dollar in revenue. The company's valuation has since fallen to under $16 billion. The Robinhood trading app tried to capitalize on the massive IPO craze by going public in 2021 with a peak market cap of over $45 billion. Since then the stock has declined over 80% to a market cap of around $9 billion. Talk is cheap and the markets tend to eventually punish bad behavior.

**Disruption in Weight Loss Drugs**

New weight loss drugs have recently become increasingly popular; some are proclaiming them as the next big breakthrough in the health industry. These products, called GLP-1 agonists, work by making patients feel less hungry and can also affect how the body absorbs fat. Novo Nordisk and Eli Lilly are the two leaders in this new market which analysts at Goldman Sachs and JPMorgan estimate could reach $100 billion by 2030. Some investors are concerned that these drugs will be so effective at curbing appetites that they could fundamentally change consumption patterns and impact demand for businesses like food and beverage

companies. Investors worry that fast food restaurants already contending with rising inflation will also have to deal with a potential loss in customers if the use of weight loss drugs becomes more common. It is estimated that just over 42% of US adults are obese and could potentially be prescribed weight loss drugs. Wall Street has been quick to herald these drugs as the ultimate healthcare product, but it is important to take a more cautious stance, especially in the early stages of research. There are still many unknowns surrounding these treatments, specifically around potential side effects like thyroid tumors, pancreatitis, diarrhea and nausea. It is expensive too, with an average monthly cost for shots of around $1000.

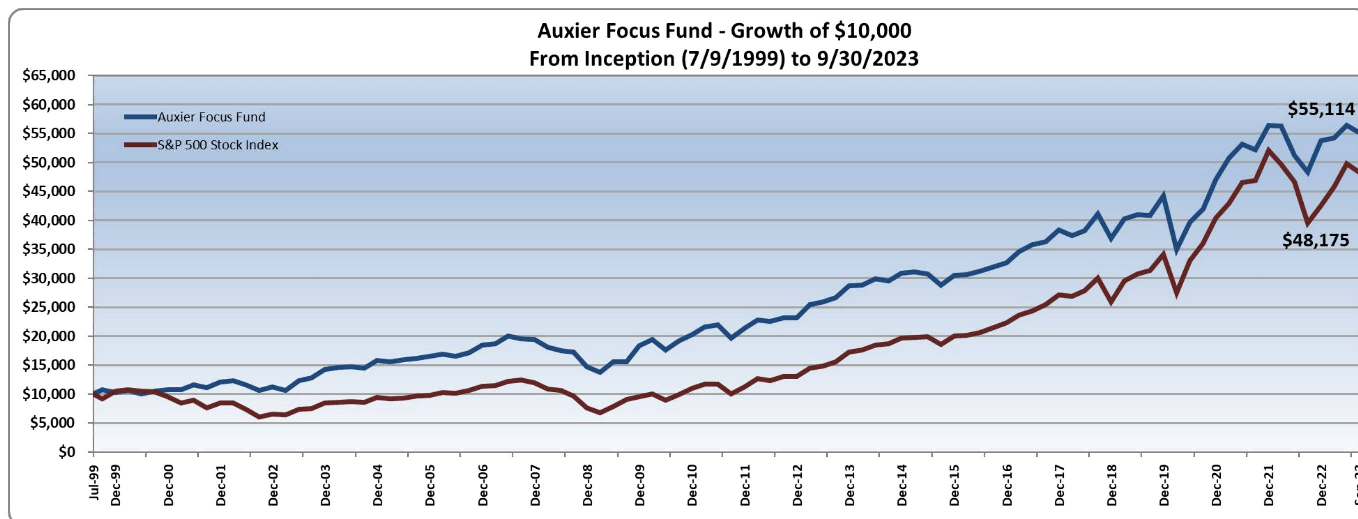
In the third quarter excitement over these drugs led to indiscriminate selling in food, beverage, medtech and medical devices to name a few examples. It is similar to the selloff in traditional food stocks when Beyond Meat went public as referenced earlier in the letter. McDonald's believes there are currently about five million people using obesity drugs with the potential to increase to 15 million in the next few years, which they figure could hurt volumes by one half a percent. Pepsi and Starbucks have seen no change in demand year to date.

Energy was the best performing S&P 500 sector during the quarter, up 12.2%. Continued supply cuts by OPEC+ have kept oil prices elevated as the West Texas Intermediate (WTI) Crude rose by 29% in the third quarter. The US Energy Information Administration (EIA) expects that OPEC+ will keep production limited for the remainder of 2023 and into 2024. They forecast an average Brent Crude spot price of $91 per barrel in the fourth quarter and an average of $95 per barrel for 2024. Lower supply has been a boost to oil companies in the Fund like Valero Energy, BP, ConocoPhillips, Chevron and Phillips 66. The recent conflict in Israel has fueled fears over the stability of global oil markets as there are uncertainties around what countries like Iran will do in response to escalations. Iran is one of the largest producers of oil in the world and in August their output reached 3.1 million barrels per day, the highest since 2018 (*Reuters*). Potential Iranian involvement should lead the US to enforce stricter sanctions on the country's oil exports. Iran also controls the Strait of Hormuz which is the most important oil checkpoint in the world, with around 20% of global oil supply passing through daily.

**Insurance Hard Market**

Property casualty stocks are enjoying a hard-pricing market. Global commercial insurance pricing increased for most lines of coverage in the third quarter, according to Marsh McLennan, marking the longest run of consecutive quarterly rate hikes since 2012. US property rates are up 14% for the quarter. Auto insurance rates are up 15.5%, with rates in Florida up 88% and electric vehicles up over 70%. Disciplined operators benefit from rising prices and rising premium volume. In addition, higher interest rates improve portfolio cash flows. The insurance component of the S&P 500 trades at 12 times next year's earnings, a steep discount to the overall market. We have a wide exposure to the property casualty industry with names like Berkshire Hathaway, Travelers, AIG, Marsh McLennan, AON and Ryan. In addition, health-related insurers like Aflac, UnitedHealth and Elevance are seeing positive fundamentals in pricing and volume trends.

## Third Quarter 2023 Performance Update




Auxier Focus Fund's Investor Class declined 2.28% in the third quarter 2023. The S&P 500 cap-weighted index declined 3.27% for the third quarter, while the equal weight declined 4.90%. The Russell 1000 Value Index fell 3.16%. Fixed income investments suffered with the S&P Aggregate Bond Index and the IDC US Treasury 20+ Year Index (4PM) declining 2.67% and 13.00% respectively. The S&P 500 Utilities lost 9.25%. Smaller stocks as measured by the Russell 2000 declined 5.13%. Stocks in the Fund comprised 90.5% of the portfolio. The equity breakdown was 81.4% domestic and 9.1% foreign, with 9.5% in cash and short-term debt instruments. A hypothetical $10,000 investment in the Fund since inception on July 9, 1999 to September 30, 2023 is now worth $55,114 vs $48,175 for the S&P 500 and $44,226 for the Russell 1000 Value Index. The equities in the Fund (entire portfolio, not share class specific) have had a gross cumulative return of 877.55%. The Fund had an average exposure to the market of 81.9% over the entire period. Our results are unleveraged.

Auxier Focus Fund – Investor Class
Average Annual Total Returns (9/30/2023)
Since Inception (07/09/1999) 7.30%
10-year 7.51%
5-year 6.04%
1-year 13.86%
3-month -2.28%

*Performance data quoted represents past performance and is no guarantee of future results. Current performance may be lower or higher than the performance data quoted. Investment return and principal value will fluctuate so that an investor's shares, when redeemed, may be worth more or less than original cost. As stated in the current prospectus, the Fund's Investor Class Share's annual operating expense (gross) is 1.10%. The Fund's adviser has contractually agreed to waive a portion of its fee and/or reimburse Fund expenses to limit total annual operating expenses at 0.92%, which is in effect until October 31, 2024. Other share classes may vary. The Fund charges a 2.0% redemption fee on shares redeemed within 180 days of purchase. For the most recent month-end performance, please call (877) 328-9437 or visit the Adviser's website at www.auxierasset.com.*

## In Closing

On a recent multistate trip we visited the new $40 billion Taiwan Semiconductor (TSMC) facility under construction in North Phoenix. The amount of cement required is straining supplies for the entire metro area. Over 60% of the workforce for that plant will have a masters or higher degree. This is just one of several plants going in as a result of the government CHIPS act. That roughly $52.7 billion stimulus has attracted another $200 billion in private funds which is just starting to filter through the

economy. In addition, $433 billion of government spending is earmarked over the next 10 years under the Inflation Reduction Act. It is hard to see a recession in those industries related to such massive fiscal stimulus.

Most stocks and bonds have been in a grueling bear market for two years. More than half the Russell 3000 stocks are down over the past twelve months. Usually the last third of a bear market is a capitulation and the most painful. We are finally seeing attractive values in many businesses that have been experiencing multiple compression with tighter money, especially in smaller companies. Our biggest winners coming out of the 2000-2002 bear market were in smaller companies like Scottsdale credit card processor eFunds. It traded at a single digit p/e under $10, was debt free and ultimately acquired by private equity for over $37. During these challenging market conditions we strive to add value by mitigating risk through our cumulative knowledge and experience along with a ramped-up research effort. Our research centers on the earnings power and growing intrinsic value of the individual businesses we own. Longer term there is a direct correlation to the earnings and ultimate stock price return.

We appreciate your trust.

**Jeff Auxier**

***Before investing you should carefully consider the Fund's investment objectives, risks, charges and expenses. This and other information is in the prospectus, a copy of which may be obtained by calling (877) 328-9437 or visiting the Fund's website. Please read the prospectus carefully before you invest.***

**Fund returns (i) assume the reinvestment of all dividends and capital gain distributions and (ii) would have been lower during the period if certain fees and expenses had not been waived. Performance shown is for the Fund's Investor Class shares; returns for other share classes will vary. Performance for Investor Class shares for periods prior to December 10, 2004 reflects performance of the applicable share class of Auxier Focus Fund, a series of Unified Series Trust (the "Predecessor Fund"). Prior to January 3, 2003, the Predecessor Fund was a series of Ameriprime Funds. The performance of the Fund's Investor Class shares for the period prior to December 10, 2004 reflects the expenses of the Predecessor Fund.**

The Fund may invest in value and/or growth stocks. Investments in value stocks are subject to risk that their intrinsic value may never be realized and investments in growth stocks may be susceptible to rapid price swings, especially during periods of economic uncertainty. In addition, the Fund may invest in mid-sized companies which generally carry greater risk than is customarily associated with larger companies. Moreover, if the Fund's portfolio is overweighted in a sector, any negative development affecting that sector will have a greater impact on the Fund than a fund that is not overweighted in that sector. An increase in interest rates typically causes a fall in the value of a debt security (Fixed-Income Securities Risk) with corresponding changes to the Fund's value.

Fund holdings and sector allocations are subject to change and should not be considered a recommendation to buy or sell any security.

Foreside Fund Services, LLC, distributor.

*The S&P 500 Index is a broad-based, unmanaged measurement of changes in stock market conditions based on 500 market-capitalization-weighted widely held common stocks. The Russell 1000 Value Index refers to*

*a composite of large and mid-cap companies located in the United States that also exhibit a value probability. The Russell 1000 Value is published and maintained by FTSE Russell. The S&P 500® Equal Weight Index (EWI) is the equal-weight version of the widely-used S&P 500. The index includes the same constituents as the capitalization weighted S&P 500, but each company in the S&P 500 EWI is allocated a fixed weight - or 0.2% of the index total at each quarterly rebalance. The S&P 500® Utilities comprises those companies included in the S&P 500 that are classified as members of the GICS® utilities sector. The S&P 500® Energy comprises those companies included in the S&P 500 that are classified as members of the GICS® energy sector. IDC US Treasury 20+ Year Index (4PM), is a 4pm pricing variant of the ICE US Treasury 20+ Year Index, which is market value weighted and is designed to measure the performance of U.S. dollar-denominated, fixed rate securities with minimum term to maturity greater than twenty years. The Russell 2000 index is an index measuring the performance of approximately 2,000 smallest-cap American companies in the Russell 3000 Index, which is made up of 3,000 of the largest U.S. stocks. It is a market-cap weighted index. S&P US Aggregate Bond Index is designed to measure the performance of publicly issued U.S. dollar denominated investment-grade debt. Brent Crude is the benchmark used for the light oil market in Europe, Africa, and the Middle East, originating from oil fields in the North Sea between the Shetland Islands and Norway. West Texas Intermediate is the benchmark for the U.S. light oil market and is sourced from U.S. oil fields. One cannot invest directly in an index or average.*

*OPEC+ represents around 40% of world oil production and its main objective is to regulate the supply of oil to the world market. The leaders are Saudi Arabia and Russia, which produce around 10 million barrels per day of oil each.*

*Cash flow is the net amount of cash and cash-equivalents being transferred into and out of a business.*

*Free cash flow (FCF) represents the cash a company generates after accounting for cash outflows to support operations and maintain its capital assets.*

*Multiple compression is an effect that occurs when a company's earnings increase, but its stock price does not move in response.*

*The price-to-earnings ratio (P/E ratio) is the ratio for valuing a company that measures its current share price relative to its per-share earnings.*

*The spot price is the current price in the marketplace at which a given asset—such as a security, commodity, or currency—can be bought or sold for immediate delivery.*

*As of 9/30/2023, the Fund's top equity holdings were: UnitedHealth Group Inc. (6.7%); Microsoft Corp. (5.9%); Mastercard Inc. (4.8%); Kroger Co. (3.3%); Elevance Health Inc. (3.0%); Philip Morris International (3.0%); Merck & Co. Inc. New (2.7%); Visa, Inc. (2.7%); Pepsico Inc. (2.5%); Medtronic PLC (2.4%).*

*The views in this shareholder letter were those of the Fund Manager as of the letter's publication date and may not reflect his views on the date this letter is first distributed or anytime thereafter. These views are intended to assist readers in understanding the Fund's investment methodology and do not constitute investment advice.*