# Alpha Wealth Funds, LLC

"the opportunities never stop"

**January 24, 2018**

The Insiders Fund, LP 4th Quarter 2018 Partner Letter:

***Panic Rolls over the Market***

## Results and Benchmark Comparisons:

The Insiders Fund was down 16.94% for the month of December versus the S&P 500 down 9.18 %. The Fund was down 16.04% for the quarter versus the S&P 500 down 13.5%. For the year the Fund was down 24.76% versus the S&P 500, down 4.38%. This was the worst showing the Insiders Fund strategy has had since 2008. It's important to remind you that the following year, 2009, the strategy yielded gains of almost 70%. Often a bad year is followed by an outstanding one, but more on this later in **Our Outlook:**.

After the worst December for US Equities in 50 years, January is delivering tentative stability across risky markets, supported by a strong US payrolls report and dovish Powell remarks. We added modestly to many of our positions during the market sell-off, and as of this writing, have been rewarded handsomely. The Fund is up over 13% MTD at the time of this letter, erasing a significant portion of the carnage during the month of December.



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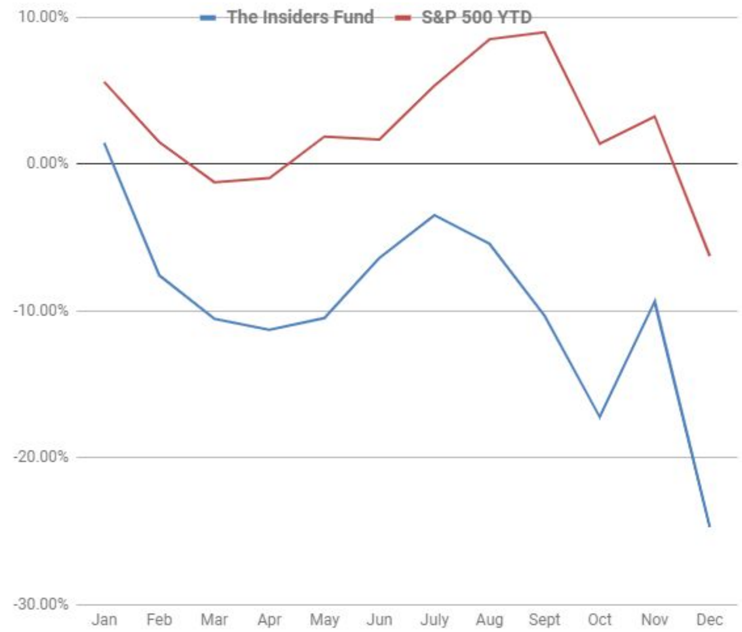
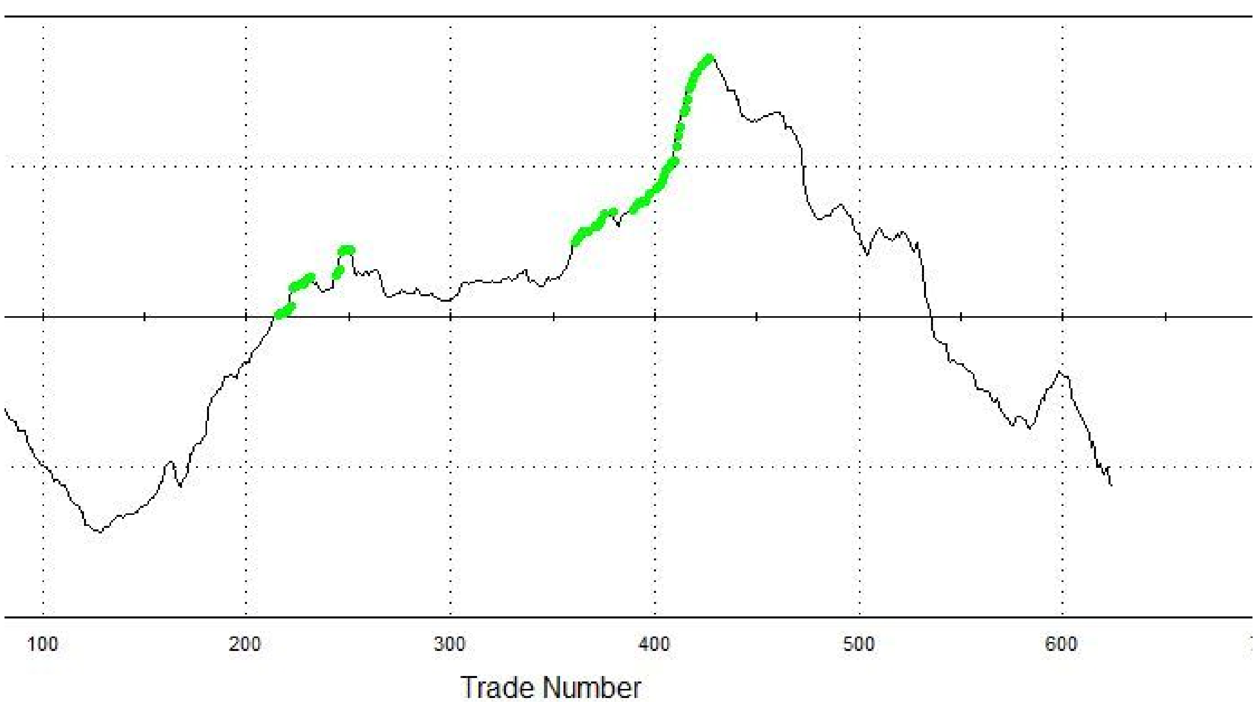



Equity Curve Line (10/1/2018 08:07:24 - 1/17/2019 07:49:02)



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**This equity line pretty much sums up the quarter. November was great and then the bottom fell out in December.**

We made 624 trades during the quarter, 419 on the long side and 205 on the short side. We were 47.76% profitable overall, with 45.35% win ratio on the long side and 52.68% profitable on the short side. This analysis shows that it wasn't the trading that hurt the account but the drop-in value of our core holdings. After a tremendous November recovery, the Fund entered the month of December 130% long and suffered outsized unrealized losses. We expect these positions to recover.

**Top 10 Gainers**

| Security | Symbol | Gain/(Loss) |
|---|---|---|
| EQT CORP | EQT | 77,531 |
| BAUSCH HEALTH C | BHC | 52,921 |
| TESARO INC | TSRO | 39,081 |
| NEWELL RUBBERMAID INC CMN | NWL | 13,729 |
| AMAZON.COM INC CMN | AMZN | 12,471 |
| HOME DEPOT INC | HD | 11,122 |
| INDEPENDENT BK | IBTX | 9,297 |
| SPDR S&P 500 ETF TRUST | SPY | 8,723 |
| LIBERTY LATIN A | LILAK | 8,589 |
| AUTOHOME INC | ATHM | 8,008 |



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## Top 10 Losers

| Security | Symbol | Gain/(Loss) |
|---|---|---|
| ENERGY TRANSFER | ET | -150,296 |
| GOOGLE INC. CMN CLASS A | GOOG | -81,553 |
| SOUTHWEST AIRLINES CO | LUV | -81,306 |
| ALLERGAN PLC CMN | AGN | -74,712 |
| PACWEST BANCORP | PACW | -50,924 |
| ANDEAVOR LOGIST | ANDX | -50,893 |
| BEAZER HOMES US | BZH | -50,151 |
| KELLOGG COMPANY | K | -48,383 |
| COTY INC | COTY | -47,560 |
| MICROCHIP TECHN | MCHP | -46,910 |

Most of these losses are unrealized with the notable exception of Google, Microchip, and PacWest.

No review of the Top Winners and Losers would be replete without asking ourselves, what if we did nothing and just rode our investments from the previous quarter? How would they have done? With that in mind, we examined the Top 10 holdings from the previous quarter. The results are outlined below.



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**Results: Buy and hold strategy**

| Description | Price 10-1-18 | Price 12-31-18 | % Change |
|---|---|---|---|
| Beazer | 10.634 | 9.13 | -14.14% |
| Intl Flavor Frag | 138.466 | 134.27 | -3.03% |
| Facebook | 162.44 | 131.09 | -19.30% |
| Dentsply Sirona | 37.68 | 37.21 | -1.25% |
| Cypress Semi | 14.35 | 12.729 | -11.30% |
| CommScope | 29.79 | 16.39 | -44.98% |
| Coty | 12.61 | 6.56 | -47.98% |
| Extreme Network | 5.53 | 6.1 | 10.31% |
| Tall Grass Energy | 24.4 | 24.34 | -0.25% |
| Cash | | | |
| **Average** | | | -14.66% |

## Current holdings:

**Because the fund is such an active trader, we may highlight an individual holding if it's a new position, major holding or represents some change to our normal holdings.**

**The point being is that the best way for you to follow our investments is through the client portal. There, you will find the daily performance and details on all of our holdings. If you haven't been able to log in, please let me know and I will have our fund administrator, NAV Consulting, send you new login credentials.**



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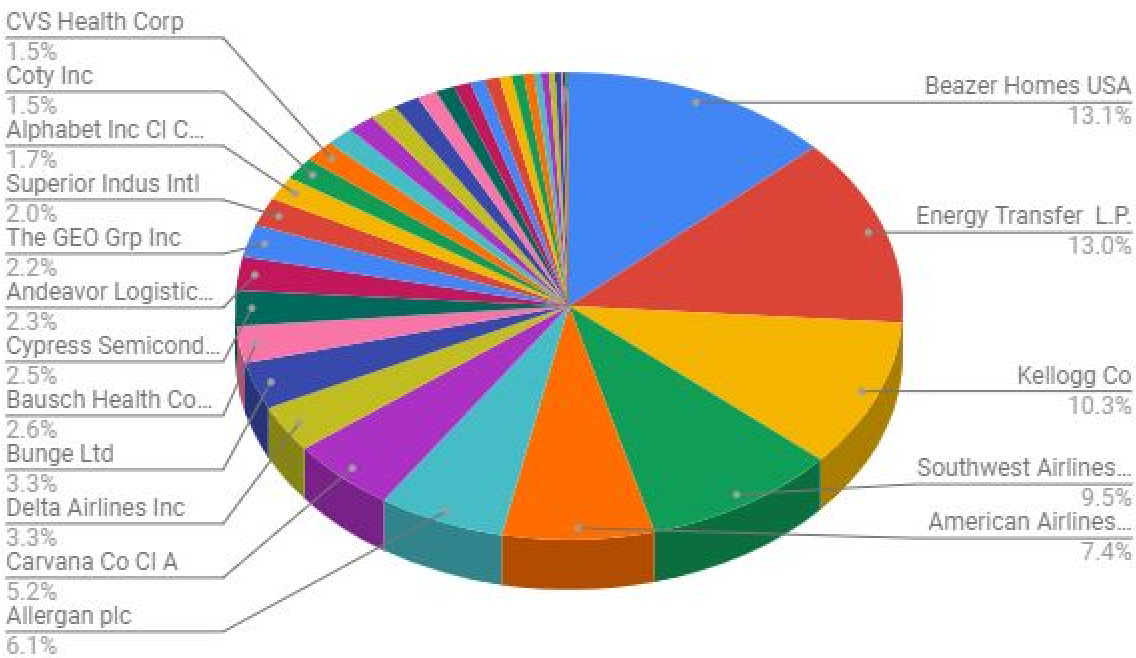
ALPHA WEALTH FUNDS

## Portfolio Holdings 1/25/19




**Energy Transfer Partners** is one of the largest energy infrastructures plays in the U.S. The merger between Energy Transfer Equity (ETE) and Energy Transfer Partners (ETP) is complete. The simplified entity is now operating as one Partnership known as Energy Transfer LP, and its common units are listed on the NYSE under the new symbol "ET."

The merger between ETE and ETP helped to streamline their organizational structure and improve transparency for their investors. This also helps provide the new Energy Transfer with an improved cost of capital. This gives them the ability to easily fund robust organic growth projects and to execute on strategic opportunities.

Energy Transfer will continue to lead the industry as one of the largest energy networks transporting natural gas, natural gas liquids, crude oil and refined products through more than 83,000 miles of pipelines spanning the country.

- Massive insider buying, a robust yield over 8% and expected dividend increases will eventually turn this into a profitable investment. There are long term risks with the electrification of the automobile fleet but even the most optimistic EV forecasts



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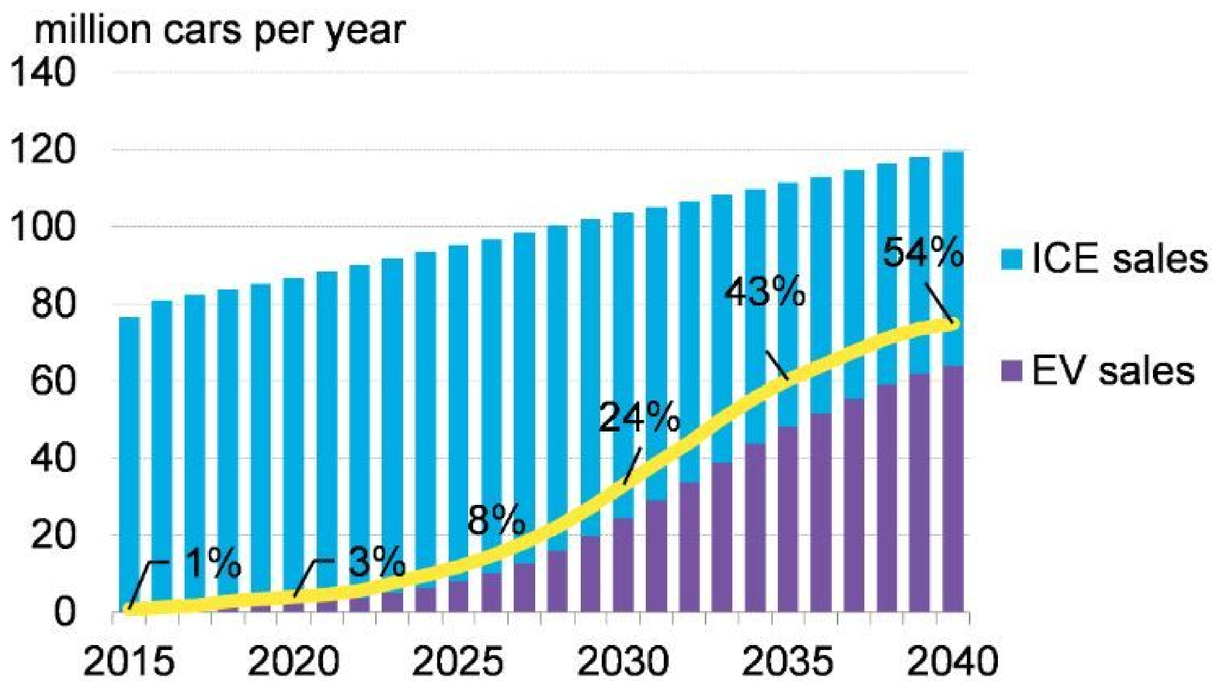
assume the  ICE is here for a long time.




After years of overestimating the market, it seems that EV adoption has finally started to take off, and the market is accelerating faster than ever.

**BZH Beazer Homes** now represents a 1.54% unrealized loss in the portfolio.  I would not get excited about the homebuilding sector with decreasing affordability and rising rates but then again, I don't know anywhere in the country where housing is so depressed that you can walking into a builder's office and buy the houses and lots for half of the builders' cost.

Besides, interest rates seem to be stabilizing at reasonably low rates.  Affordability is clearly a challenge, but Beazer is a national homebuilder selling homes with an average price around $364,000.

- Beazer 's tangible book value is $20.27.  The Company records the value of the lots on its book at the price it paid for them and work in construction at cost. A large part of that value, though, is in a deferred tax asset which would likely disappear if the company is purchased by another competitor.  Recently deep value shareholders, Donald Smith & Co., Inc. have accumulated a significant stake in the company. We



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think this margin of safety more than accounts for rising rates and decreasing affordability.

**K Kellogg Company,** founded in 1906 manufactures and markets ready-to-eat cereal and convenience foods. It's kind of boring without any solid hits in quite some time, yet somehow this company managed to steadily reverse a 7.24% decline in revenue in 2015 to a 5.62% increase in the 12 months ending Sept 30,2018.

Revenue for the twelve months ending September 30, 2018 was **$13.484B**, a **5.62% increase** year-over-year.

- Kellogg annual revenue for 2017 was **$12.923B**, a **0.7% decline** from 2016.
- Kellogg annual revenue for 2016 was **$13.014B**, a **3.78% decline** from 2015.
- Kellogg annual revenue for 2015 was **$13.525B**, a **7.24% decline** from 2014.

Kellogg (K) on November 13th delivered a downbeat investors day and suffered numerous downgrades. JPMorgan analyst, Ken Goldman, downgraded it to neutral from overweight and removed Kellogg from the firm's Focus List. He reduced his target price to $66, saying that while nothing at the company's investor day "necessarily disappointed" him, he also did not gain "much comfort that the bottom-line turnaround would be swift. BMO Capital analyst Kenneth Zaslow lowered his price target on Kellogg to $70 and kept his Market Perform. The analyst also lowered his FY19 EBITDA margin forecast to $2.36B from $2.44B to reflect the management's updated guidance of "flattish operating profit" as it will lag sales .

Deutsche Bank analyst Rob Dickerson lowered his price target for Kellogg to $66 saying "the company at its investor day emphasized the reinvestment needed to drive accelerated top-line growth. 2020 sounds like it could be the first year Kellogg returns to its long-term year-over-year growth targets of 1%-3% revenue growth, 4%-6% operating profit growth and 6%-8% earnings growth, "Dickerson tells investors in a research note. He believes consensus estimates for 2019 look too high currently and keeps a Hold rating on Kellogg.

As a result the stock declined sharply and On November 19th, 20th the CEO and CFO purchased $1.1 million and $509K at $61.63 and $62.14 respectively. Our average cost is close to $61.53. We are in the red as of Friday the 19th's close of $59.43. We initially thought we would get a bounce from the insider's purchase, but December came along and



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we are now weighing our alternatives. The 50-day MA is at $60.15 and the 200 day at $65.95.

- CEO Cahillane was recruited from Nature's Bounty October of 2017. Prior to that he was a senior executive at the Coca Cola Company.
- The rationale for this investment is the steady growth in dividends.
- Kellogg is a private equity buyout or takeover candidate. JP Morgan gives it a 15% probability to be taken out with a 25% premium.
- Post Holdings, a peer company, has rallied 20% since its December lows

**LUV Southwest Airlines -** Morningstar and CFRA have buy ratings on the stock. According to Morningstar, Southwest has been consistently profitable for more than 40 years thanks to exceptional execution of its low-cost-carrier strategy, which includes fleet commonality, point-to-point flying at secondary airports, short-haul routes, and a distinct company culture. Also, unlike most major carriers that rely on third-party distributors for ticket sales, Southwest has succeeded using its own distribution channel. This accounts for roughly 85% of bookings. Southwest currently commands the largest percentage of U.S. domestic market travel of any major carrier.

- LUV's historic trading range 5 yr high has been PE of 25.84 EXCl Extra and the low PE Excl Extra of 13.17. It's now trading at 13.09, lower than its historical range.
- Fuel, the largest cost input component appears to be a stable low price for the foreseeable future.
- Irrational pricing between the major competitors, UAL, DAL, AAL seems to be in check. JP Morgan's top ranked analyst has an underweight on LUV, with a price target of $45 due to Southwest's unusually high level of cost inflation. Merrill Lynch also a neutral on the shares as it expects core demand slowdown across the group.

The argument for **American Airlines, AAL,** is a little different. On both cases we think airline stocks are depressed for unwarranted fears of irrational pricing and economic slowdown. AAL was hit harder than most and last week's surprising beat in earning reaffirmed our thesis. We had a hint that business was not as bad as the market was forecasting as two directors bought over $1.3 million in stock on 10/29/18 and 11/19/18. Insiders rarely invest that much without confidence that they are going to make money. The stock shot sharply higher on their 4th quarter earnings release last week and we are in the black on both our airline stocks. We also initiated a new position in Delta as we expect



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a further bounce in airline stocks as winter travel warnings, the damage and perceived fears of a government shutdown abate.

**AGN Allergan -** The global drug behemoth is trading at a depressed valuation. At current levels, according to JP Morgan analyst Schott, "AGN shares are trading at only 8.6x/9.5x our 2019E EPS and EV/EBTIDA estimates, a significant discount to the group despite mid-single digit top line growth potential over time and a substantial and growing aesthetics franchise."

Numerous insiders have bought stock at higher prices. The CFO purchased 1000 shares at $157. Director Christopher Coughlin bought 10,000 shares at $190.64 on 9/6/18. Coughlin has been an Independent Director at Allergan plc since July 2014. Our average cost is $149.34, below the $153.96 that CEO and Chairman Brent Saunders paid in March of 2018.

**CVNA Carvana -** Carvana is a leading eCommerce platform for buying and selling used cars. On their platform, consumers can research and identify a vehicle, inspect it using 360-degree vehicle imaging technology, obtain financing and warranty coverage, purchase the vehicle and schedule delivery or pick-up, all from their desktop or mobile devices. Their transaction, technologies and online platform transform a traditionally time consuming process by allowing customers to secure financing, complete a purchase and schedule delivery online in as little as 10 minutes. Newly launched features allow sellers to participate as well.

Carvana has yet to turn a profit but this fast growing, disruptive company has some insiders that are buying into the story. Spruce House Partners upped their holdings by 15% with their purchase of $24.3 million shares at $33.28 during 12/17/18 - 1/3/19. Director Michael Marrone upped the ante 70% with a $933.1k purchase on 11/12/18 - 11/26/18 at an average price of $44.42. Maroone last purchased CVNA on the IPO on 5/3/17 at $15.00. Maroone knows a thing or two about selling cars as he served as President and Chief Operating Officer of AutoNation, Inc. from August 1999 until his retirement in February 2015.

On January 14,2019 Morgan Stanley initiated Coverage with an underweight, Wall St speak for a sell. On Dec. 7, 2018 Citigroup initiated coverage with a buy. Our average cost is $38.04 per share. CVNA was as high as $64.96 at the end of September 2018.



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Clearly this is a disruptive company, offering the ability to buy or sell your car in almost real time fashion. They aspire to be the largest and most profitable dealer of cars, in effect, the Amazon of the business.

## Housekeeping:

Michael Torrence joined our firm over the Summer and although he held a Series 7 & 63 license, he had to take the Uniform Combined State Law Examination (Series 66) to work as an Investment Advisor Representative. I am happy to say he passed it and is now bringing in lots of new prospects and clients. Michael recently was a pilot, and lieutenant in the Marine Corps, but aspired to make a career in the financial services industry. We feel very fortunate that he chose to work for us. He's a standup guy, great personality, and as a fiduciary, interested in our client's and prospect's welfare.



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## Our Outlook:

We wrote last quarter that, "The lack of stability in the White House is taking its toll on investor confidence… the radical trade agenda of Peter Navarro, Trump's trade guru on China, is threatening to undermine a world order that has allowed China to become the second biggest economy in the world." These are two obvious hazards investors should be aware of. The third thing to be aware of are interest rates. A rise in interest rates makes stocks less valuable. That's just math." Add to that our concern that the looming trade war will be inflationary. It's possible that the Fed raises rates on a faster path if employment holds up with rising cost pressures. I was right on both of those.

I also wrote that 4th quarter is seasonally the best time to be in the market. Last quarter was certainly the exception to this. I couldn't have been more wrong on that one. December was the worst December for equities in 50 years.

On January 5th, 2019 I blogged 5 Ways to Know the Stock Market Bottom is in.
https://www.theinsidersfund.com/2019/01/5-ways-to-know-the-stock-market-bottom-is-in/

1. You don't dread your statements any longer because you no longer open them and they just pile up in some dusty corner.
2. Your investment advisor stops calling you. The last thing you want to do is buy more stocks.
3. Stocks don't go down on bad news any longer. For example Apple's recent earnings warning doesn't send the stock down 8%. It might even go up.
4. The Federal Reserve reverses its rate normalization and folds and signals it's ready to "accommodate" the market.
5. Corporate insiders (officers and directors, not hedge funds and index/quant funds) stampede into the market buying great quantities of their company's stock.



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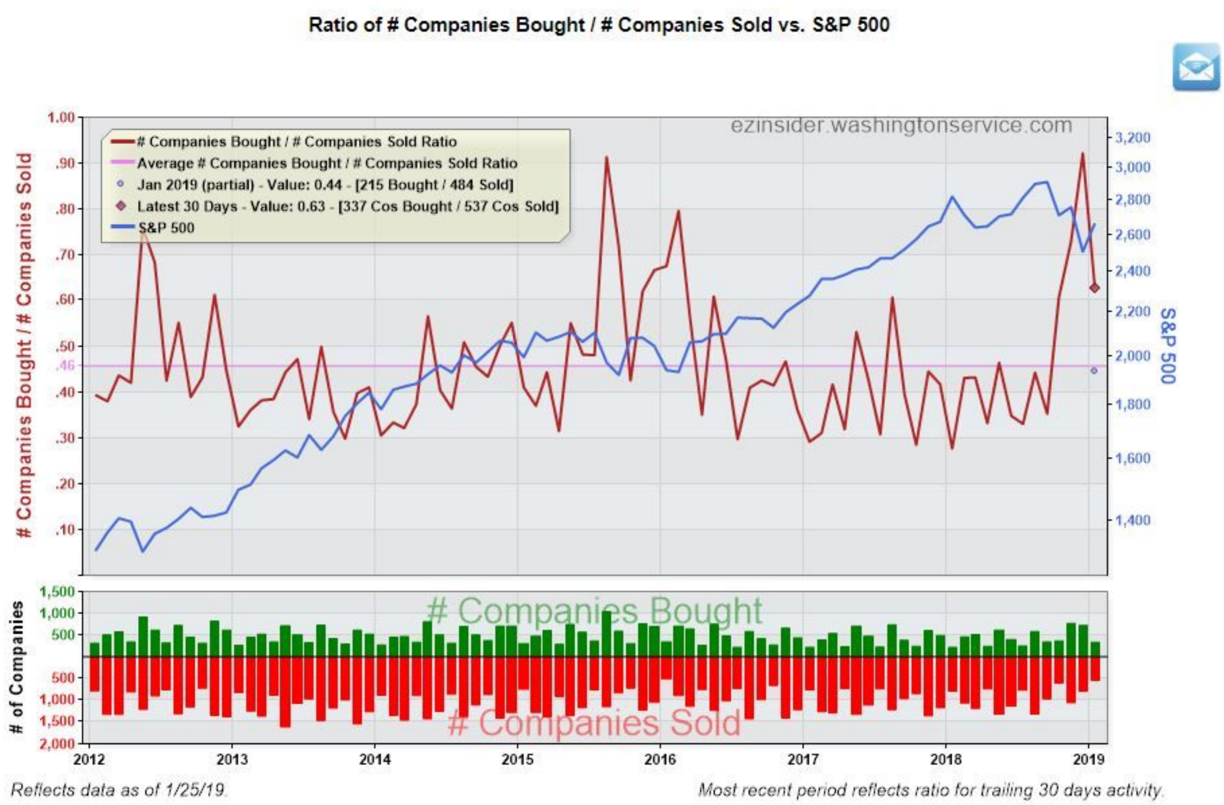
I can't realistically address the first two. You have to assess that emotional state for yourself but my anecdotal observations are that few investors have capitulated. We lost no clients and expect to gain a couple of sizable new ones.

- On 1-23-19 the semiconductor index had its biggest one day rally since 2008. Texas Instruments soared on reduced earnings guidance.
- On January 4th, the Fed blinked.On a monetary panel with past Federal Reserve Chairpersons, Powell said the Fed will be patient, in effect, the classic blink and the the market rallied immediately.

https://www.cnbc.com/2019/01/04/powell-says-fed-will-be-patient-with-monetary-policy-as-they-watch-how-economy-does.html




**Insiders have stepped up their buying but still more sellers than buyers**



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* Insider buying has picked up dramatically but still below the 1.0 line on the left of the graph. That signals that there are still more insiders selling than buying. Prices as a whole have still not fallen to the level that would initiate a crescendo of buying by corporate insiders.

As a result, I expect mediocre market returns in 2019 as corporate insiders still show what I would describe as a lack of animal spirits that would signal outsized returns. The Insiders Fund will continue to seek out value. Insiders are contrarians and buy their stock when they perceive it to be cheap. They are value investors. Value investing has underperformed growth for some time, but there are signs that this could be changing. It usually takes a market rout, to bring some sensibility to investors. Market participants gravitate between fear and greed. Last quarter's sell-off may wake people up that it does matter what you pay for growth. Eighty-three percent of the U.S. companies that went public in 2018 had lost money in the year leading up to their IPO, according to data compiled by University of Florida finance professor Jay Ritter. This is the highest proportion since 1980, according to Ritter's data.

As always, we greatly appreciate the honor and responsibility of managing your investments. Please feel free to reach out to us anytime. Our goal is to be your lifetime advisor and we know many of you, including myself, are very frustrated with the performance of The Insiders Fund. We have no qualms about you switching to any of the alternative offerings we have. I personally continue to believe in the strategy although clearly my implementation of it was disappointing. The Insiders Fund endeavors to significantly outperform while protecting the downside. Last quarter's results were not too far away from the market's returns but unacceptable to us. Hopefully January's results to date, far outperforming the market, will validate your continued faith in the strategy.

Sincerely,

**Harvey Warren Sax**

*Partner, Alpha Wealth Funds, LLC*

*Fund Manager of The Insiders Fund, LP*



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