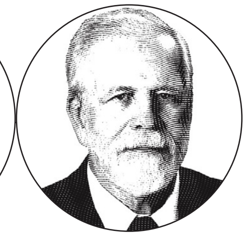
MUHLENKAMP Memorandum

Issue 140 | Published Fourth Quarter | October 2021

QUARTERLY LETTER



By Jeff Muhlenkamp, Portfolio Manager and Ron Muhlenkamp, Founder

Fellow Investors,

In July we described at length the uncertainty that COVID-19 had introduced into the global economy. We called it "noise." A summer wave of COVID hit a number of countries across the globe from Israel to Vietnam, including the United States, with the peak case count generally appearing in early September. The resurgent COVID slowed economic recovery and exacerbated the problems in global supply chains which had not fully recovered from the winter round of the illness and associated containment measures. While some shortages have been alleviated (lumber comes to mind) other shortages remain problematic (semiconductors for the auto industry, for example). Global transportation systems are still overwhelmed resulting in longer shipping times internationally and higher costs. Interestingly, late in the third quarter we began to see reports of energy shortages in a variety of countries: natural gas prices in Germany have more than tripled, there was a shortage of gasoline in England, power was curtailed to businesses in Northern China, etc. There is no single cause for the energy problems but it is interesting that they all cropped up simultaneously.

So the economic noise hasn't abated. We didn't really expect it would.

Shifting to inflation and interest rates the August 31st U.S. CPI number was 5.25% higher than a year ago, indicating inflation of about 5%; well above the Federal Reserve's target of 2%. The interest on the 10-year Treasury bond began the quarter at 1.48%, hit a low on August 3rd of 1.17%, and ended the quarter at 1.51%. While interest rates are little changed from the beginning of the quarter to the end the upward movement in the 2nd half of the quarter coupled with higher than targeted inflation has market participants wondering if higher interest rates are coming. We don't know, but it is worth mentioning that the Federal Reserve has shifted its stance on monetary policy and is now saying it will start reducing its bond purchases and may begin to consider raising short-term rates.

We have two thoughts on interest rates. First, we are not predicting higher rates, but we observe that the current interest rates are well below the rate of inflation, a situation we last saw in the 1970s. In that decade you could become wealthier via a bigger mortgage on a bigger house because mortgage rates were below the rate of inflation – you were being paid to borrow. Ron revisits that topic in a separate article in this quarter's newsletter. Second, IF long term interest rates continue to rise you should expect to see a decline in the value of existing bonds and downward pressure on the stock prices of high growth and high price to earnings (P/E) companies.

We also observe that corporate interest rates are very low, both on an absolute basis and relative to Treasuries, even for less creditworthy borrowers. There is currently no shortage of willing lenders.

Looking forward we expect the noise to remain with us for at least another quarter. COVID-19 is not done with us yet, though we think its economic impact will fade with time as vaccines and treatment options become more widespread. There are still a lot of exceptional measures in place both domestically and globally and while unwinding them may cause some disruption we continue to expect modest economic growth.

During the 3rd quarter, the portfolios we manage declined by generally two to three percent. We sold our holdings in Biogen as it became increasingly apparent to us that their new Alzheimer's drug was unlikely to be a blockbuster. Our holdings in Biogen achieved a roughly 30% gain over the five years we held the stock, which was somewhat disappointing. Also during the quarter we initiated a small position in a Real Estate Investment Trust (REIT) that is selling for the cash on the balance sheet. The REIT management team has a very good track record of finding value and we expect to see a good return on our investment. Otherwise our holdings remain largely unchanged.

With our best wishes for your continued success and good health.

The comments made in this article are opinions and are not intended to be investment advice or a forecast of future events.

MUHLENKAMP

WAKE UP, AMERICA – AN UPDATE

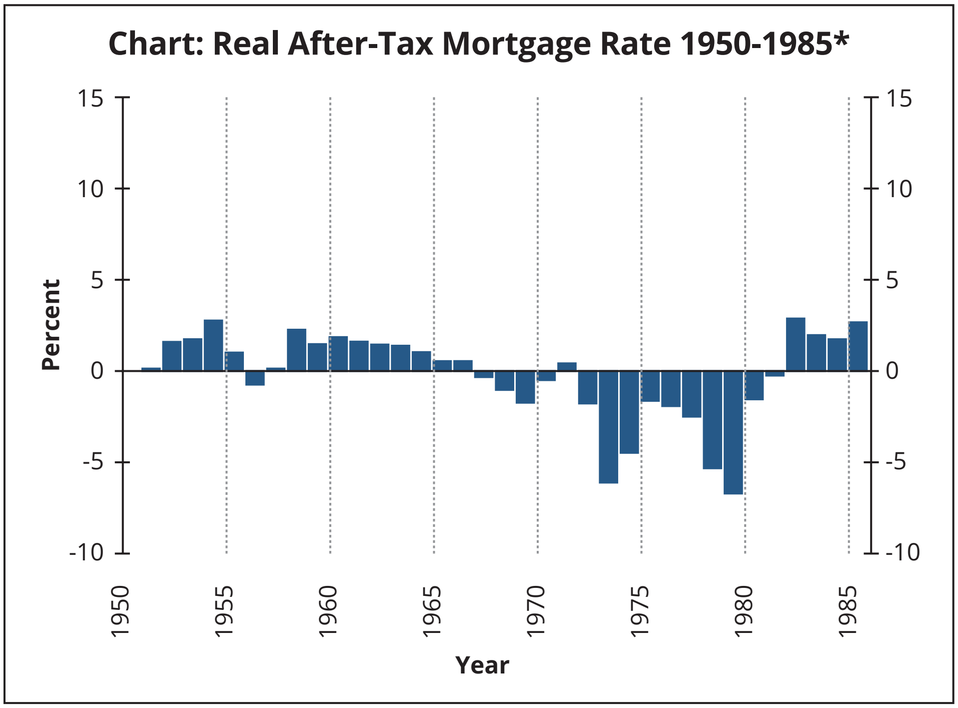
By Ron Muhlenkamp, Founder

In 1987, I wrote an essay titled "Wake Up America, Houses Don't Make You Money." Based upon questions we are getting from clients and friends, it's time to revisit that topic.

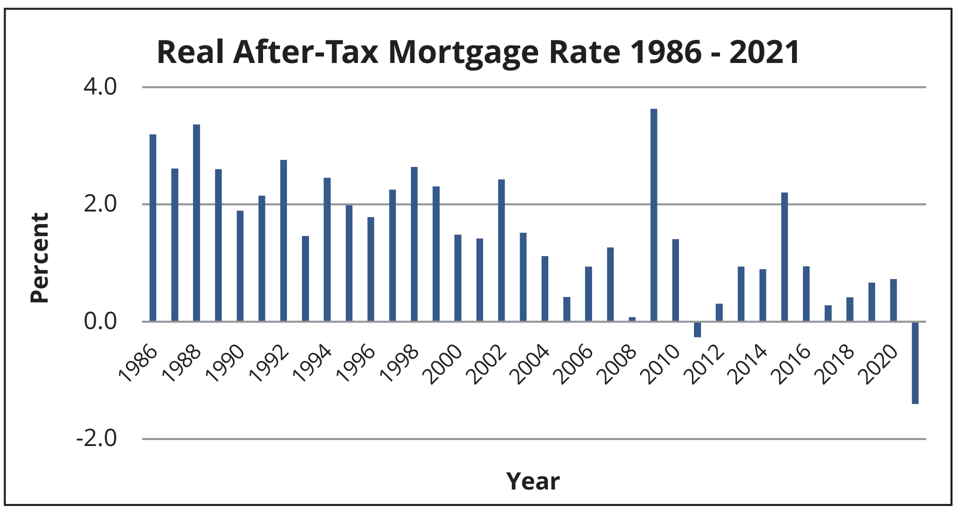
In the 1970s (when inflation rates were higher than mortgage rates), one of the best investment strategies was to borrow money. The easy way for people to borrow money was on real estate. It worked in housing, in farmland, and in commercial real estate (which was also an effective tax shelter).

The first chart represents annual mortgage rates for the period from 1950 to 1985 (adjusted for taxes at a 50% rate), and for inflation (at the annual change in the Consumer Price Index). For much of the period 1968 to 1980, after-tax interest rates on mortgages were less than the inflation rate. In fact, mortgage rates were 8% or less as long as savers were willing to accept 5% on their passbook savings. This allowed borrowing at 8% to buy houses appreciating at 10%. When borrowing money at 8% (4% after taxes) to finance a house appreciating with inflation at 10%, purchasing power increases by a net 6% of the amount borrowed. You get paid to borrow money! As the chart shows, from 1968 to 1980, this net gain averaged 4% per year, or $4,000 on a $100,000 mortgage. So, the key to getting ahead between 1968 and 1980 was to buy a big house with a big mortgage.

Today, we once again see mortgage rates below the current inflation rate.



**Source for data to calculate both charts include: Inflation Rate [U.S. Bureau of Labor Statistics]; Top Marginal Tax Rate [U.S. Tax Code]; and Mortgage Rates [Fannie Mae]*



So, the question is: Can you increase the real value of your assets in the near future by borrowing money against them? The short answer is, I don't know. It will depend on several variables, primarily the relevant interest rate, inflation rate (of the asset), the relevant tax rate, and time.

1. Relevant Interest Rate: Ideally, you would like a long-term fixed-rate mortgage or one that you have the option to refinance at a lower rate. You do not want a short-term or variable-rate mortgage (or one the lender has the option to refinance to a higher rate).

2. Inflation Rate of the Asset: Will the value of the property appreciate in nominal terms, or even depreciate at a rate less than the (negative) after-tax cost of the mortgage? A truism of real estate investing is the focus on location, location, location. An acre in a city has different investment drivers than one in the suburbs or the country. Commercial acreage differs from residential. You get the picture. The bottom line is that the real value of the assets must cover the after-tax cost of the mortgage.

3. Relevant Tax Rate: The third variable is the tax deductibility of the mortgage. At the current rate of government spending, I expect all tax rates and tax deductions to be up for negotiation in the foreseeable future. Ironically, higher tax rates make the mortgage deduction more valuable (assuming the mortgage remains deductible).

4. Time: The fourth variable is time. I believe the experience of 1972 – 1980 lasted as long as it did because the savers of the time (my parents and grandparents) feared depression more than they feared inflation. It took a decade of high inflation (and negative real interest rates) to overcome that fear. Today, I'm not certain that the savers (your parents and grandparents) fear depression. And I'm not sure the fears of individuals are dominant in determining interest rates. Many of today's savers are represented by pension funds. U.S. pension funds now total over $12 trillion, plus another $1.5 trillion unfunded. In recent years, pension funds have funded non-traditional assets such as timberland and single-family rental properties. Pension funds tend to invest assets as they come in, but this is not a given. Of course, the other major influences on current interest rates are the policies of the U.S. Fed. Currently those policy goals include U.S. inflation rates exceeding 2% and interest rates below 2%. I don't know how long these policy goals will be in place. Nor does the Fed.

Finally, in the 1970s, many farmers and homeowners believed that farmland and houses appreciated relentlessly. The mid '80s disproved that for farmland. 2008 – 2009 disproved it for housing.

So, the answer to our question is: If your assets appreciate sufficiently over your after-tax cost of borrowing for long periods of time then yes, you can increase the value of your assets by borrowing against them.

The comments made in this article are opinions and are not intended to be investment advice or a forecast of future returns.

ANNOUNCEMENTS

Mailing List Update
If you are receiving a paper copy of our Memorandum and would rather receive it via email or if you would like to be removed from our mailing list, please let us know. We will update our mailing list to accommodate your preference. If there's someone who you think would enjoy reading our material, please pass along our contact information. Visit www.muhlenkamp.com or call us at (877) 935-5520.

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GLOSSARY:

Price-to-Earnings (P/E) Ratio is the current price of a stock divided by the company's (trailing) 12-month earnings per share.

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MUHLENKAMPMemorandum

Inside this issue:

- Quarterly Letter
- Wake Up, America – An Update
- Announcements

Ron Muhlenkamp was a guest speaker on the Value Investing Live Series of GuruFocus on August 18, 2021, he covered the following topics:

- *The Problem with Inflation*
- *Inflation, Business Cycles, & the Population*
- *Failure of Macroeconomics*
- *Fundamental Value*
- *Life Cycle of Industries*
- *Market Corrections*
- *Audience Q&A*

Visit www.muhlenkamp.com to watch a recording of Ron's presentation.

MUHLENKAMPSMA ALL-CAP VALUE

For the period ended 09/30/2021

Muhlenkamp & Company's All-Cap Value SMA (Separately Managed Account) is designed for investors' accounts over $100,000. We employ full discretion, applying fundamental analysis.

INVESTMENT OBJECTIVE

We seek to maximize total after-tax return through capital appreciation, and income from dividends and interest, consistent with reasonable risk.

INVESTMENT STRATEGY

We invest in undervalued assets wherever they may be found. Typically, this results in holding a portfolio of companies we believe are materially undervalued by the market. Bonds may be included in the portfolio if they are a good investment.

INVESTMENT PROCESS

We start with a bottom-up scan of domestic companies, typically looking at most U.S. companies at least four times per year. We add to that an understanding of the sector dynamics in which companies are operating, an assessment of the business cycle, and a review of macroeconomic conditions.

Our primary screening metric is return on shareholder equity (ROE). We are looking for companies with stable returns that can be purchased cheaply, or for companies with improving returns that have not yet been recognized by the market.

We don't believe that a holding period of "forever" is appropriate in all cases, but are comfortable holding companies as long as they continue to meet expectations.

INVESTMENT RISK

We define investment risk as the probability of losing purchasing power over long periods of time, which is quite different from Wall Street's definition of price volatility in very short periods of time. Taxes, inflation, and spending will ALL impact the purchasing power of your assets.

MUHLENKAMP

ALL-CAP VALUE COMPOSITE PERFORMANCE (NET OF FEES)

	Year to Date	One Year	Annualized Past 3 Years	Past 5 Years	Past 10 Years	Past 15 Years
Return	15.87%	32.45%	10.12%	8.50%	8.99%	3.61%
S&P 500 Total Return*	15.92%	30.00%	15.99%	16.90%	16.63%	10.37%
Consumer Price Index**	5.03%	5.25%	2.76%	2.58%	1.90%	1.98%

*** The S&P 500 is a widely recognized, unmanaged index of common stock prices. The figures for the S&P 500 reflect all dividends reinvested but do not reflect any deductions for fees, expenses, or taxes. One cannot invest directly in an index.**

** Consumer Price Index (CPI) – As of August 2021 – U.S. CPI Urban Consumers NSA (Non-Seasonally Adjusted), Index. The Consumer Price Index tracks the prices paid by urban consumers for goods and services and is generally accepted as a measure of price inflation. Price inflation affects consumers' purchasing power.

Consolidated performance with dividends and other earnings reinvested. Performance figures reflect the deduction of broker commission expenses and the deduction of investment advisory fees. Such fees are described in Part II of the adviser's Form ADV. The advisory fees and any other expenses incurred in the management of the investment advisory account will reduce the client's return. It should not be assumed that recommendations made in the future will be profitable or will equal the performance of the above accounts. A list of all security recommendations made within the past twelve months is available upon request.

TOP TWENTY HOLDINGS

Company	Industry	% of Net Asset
WESCO International Inc.	Trading Companies & Distributors	4.96%
Microchip Technology Inc.	Semiconductors & Semiconductor Equipment	4.24%
Alliance Data Systems Corp.	IT Services	4.04%
Microsoft Corporation	Software	4.03%
Cameco Corporation	Oil, Gas, & Consumable Fuels	3.96%
Dow Inc.	Chemicals	3.95%
Apple Inc.	Technology Hardware, Storage & Peripherals	3.78%
Mastec Inc.	Construction & Engineering	3.73%
Broadcom Inc.	Semiconductors & Semiconductor Equipment	3.61%
McKesson Corporation	Health Care Providers & Services	3.28%
Schlumberger NV	Energy Equipment & Services	3.10%
Meritage Homes Corporation	Household Durables	3.08%
UnitedHealth Group Inc.	Health Care Providers & Services	3.07%
CVS Health Corp.	Health Care Providers & Services	3.05%
Berkshire Hathaway Inc. Class B	Diversified Financial Services	3.02%
ALPS Alerian MLP ETF	Exchange Traded Funds	2.92%
Tenneco Inc.	Automobile and Components	2.82%
Kirby Corp.	Marine	2.61%
SPDR Gold Shares	Exchange Traded Funds	2.60%
NMI Holdings	Thrifts & Mortgage Finance	2.48%

Composite holdings are subject to change and are not recommendations to buy or sell any security.

Composite Top Twenty Holdings are presented as supplemental information to the fully compliant presentation on the next page.

Return on Equity (ROE) is a company's net income (earnings), divided by the owner's equity in the business (book value).

PORTFOLIO MANAGER

Jeffrey P. Muhlenkamp, Portfolio Manager, CFA, has been active in professional investment management since 2008. He is a graduate of both the United States Military Academy and Chapman University.

INVESTMENT ADVISER

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SMA FACTS

Average Number of Equity Holdings	30
Cash & Cash Equivalents	16.44%

SMA Facts are presented as supplemental information.

SMA INFORMATION

The inception date for the All-Cap Value Composite is December 31, 1993. The All-Cap Value Composite was created in December 2003. The Composite includes fee-paying accounts over $100,000, full discretion, under management for at least one full quarter which are invested in the All-Cap Value strategy. The composite excludes the Muhlenkamp Fund and any wrap fee account.

Minimum Initial Investment	$100,000.00
Management Fee*	1% (first $1 million); 0.5% on the remainder

** May vary by account.*

Muhlenkamp & Company serves individual and institutional investors through our no-load mutual fund and separately managed accounts.

MUHLENKAMP & COMPANY, INC. ALL-CAP VALUE COMPOSITE ANNUAL DISCLOSURE PRESENTATION

Year End	Total Firm Assets (USD) (millions)	Composite Assets (USD) (millions)	Number of Accounts	ANNUAL PERFORMANCE: Composite Gross	ANNUAL PERFORMANCE: Composite Net	S&P 500 Total Return Index	THREE-YEAR ANNUALIZED STANDARD DEVIATION*: Composite	THREE-YEAR ANNUALIZED STANDARD DEVIATION*: S&P 500 Total Return Index	Composite Dispersion**
2020	265	38	45	14.06	13.14	18.40	18.63	18.79	1.38
2019	253	34	48	14.70	13.78	31.49	10.33	12.10	1.37
2018	254	32	51	(11.71)	(12.45)	(4.38)	9.24	10.80	1.21
2017	342	40	52	15.24	14.30	21.83	8.70	9.92	2.12
2016	339	39	52	(1.86)	(2.68)	11.96	9.73	10.59	1.17
2015	422	48	67	(4.66)	(5.45)	1.38	10.41	10.47	0.68
2014	541	51	67	10.27	9.37	13.69	9.55	8.97	2.06
2013	585	50	60	35.50	34.39	32.39	11.29	11.94	3.13
2012	491	41	66	11.29	10.34	16.00	12.02	15.09	1.14
2011	555	45	74	(2.84)	(3.67)	2.11	16.60	18.70	0.85
2010	724	59	82	2.96	2.15	15.06			1.45
2009	839	90	107	32.68	31.72	26.46			2.80
2008	759	112	155	(40.53)	(40.94)	(37.00)			1.97
2007	1886	327	289	(7.61)	(8.19)	5.49			3.77
2006	3393	371	337	6.09	5.34	15.79			3.70

The objective of this All-Cap Value Composite is to maximize total after-tax return, consistent with reasonable risk—using a strategy of investing in highly profitable companies, as measured by Return on Equity (ROE), that sell at value prices, as measured by Price-to-Earnings Ratios (P/E).

Muhlenkamp & Company, Inc. ("Muhlenkamp") claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Muhlenkamp has been independently verified for the periods December 31, 1993 through June 30, 2016 by Ashland Partners & Company LLP and for the periods July 1, 2016 through December 31, 2020 by ACA Performance Services. A firm that claims compliance with the GIPS standards must establish policies and procedures for complying with all the applicable requirements of the GIPS standards. Verification provides assurance on whether the firm's policies and procedures related to composite and pooled fund maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in complince with the GIPS standards and have been implemented on a firm-wide basis. The All-Cap Value Composite has had a performance examination for the periods December 31, 2006 through December 31, 2020. The verification and performance examination reports are available upon request.

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Muhlenkamp is an independent registered investment advisory firm registered with the Securities and Exchange Commission. A list of composite descriptions and a list of broad distribution pooled funds are available upon request.

Returns are based on fully discretionary accounts under management, including those accounts no longer with the firm. Composite may invest in American Depositary Receipts (ADRs).*** Accounts may be shown gross or net of withholding tax on foreign dividends based on the custodian. Past performance is not indicative of future results.

The U.S. dollar is the currency used to express performance. Returns are expressed as percentages and are presented gross and net of management fees and include the reinvestment of all income. Net of fee performance was calculated using actual management fees. The annual Composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the Composite the entire year. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request.

* **Three-Year Annualized Standard Deviation** *is a measure of volatility, calculated by taking the standard deviation of 36 monthly returns, net of fees, then multiplying the result by the square root of 12 to annualize it. Since standard deviation measures the dispersion of a set of numbers from its mean, higher results indicate more variation in monthly returns over the trailing three years.*

** **Composite Dispersion** *is a measure of the similarity of returns among accounts in the Composite. It is the standard deviation of the annual returns, net of fees, for all accounts which were in the Composite for the entire year.*

*** **American Depositary Receipts (ADRs)** *are shares that trade in U.S. markets, but represent shares of a foreign company. A bank (the depository) purchases a number of the foreign shares and holds them in a trust or similar account; in turn, the bank issues shares tradable in the U.S. that represent an interest in the foreign company. The ratio of ADRs to foreign shares is set by the bank. ADRs do not mitigate currency risk, but can reduce transaction costs and simplify trading compared to buying the local shares in the foreign markets.*