Muhlenkamp & Company, Inc.

# Quarterly Letter, April 2020

Fellow Investors,

Before Ron and I start with our normal topics, please allow us to extend our heartfelt wishes for good health and good luck during this exceptional period. Also, our deepest thanks to all of you that are reaching out to help others. We are continually amazed at the many, many ways we see people helping each other and are inspired and heartened by such actions. Thank you.

Additionally, we'd like to reassure you that Muhlenkamp and Company is fully operational and open for business. Our employees are doing a fantastic job working from home continuing to provide the service you've come to expect. I'd like to publicly thank Rich Dean, our Operations and IT Manager, for his hard work putting in the systems that allow us to do that. Thanks Rich.

Now, here's what we're seeing:

The week of March 9th is when America changed its mind about the novel Coronavirus now called COVID-19. To be sure, the subject had been in the news prior to that, but received little notice. That week, however, the seriousness of the illness caught America's attention and decision makers at all levels reacted. Like a school of fish that suddenly changes direction with no obvious leader or signal, America shut down its colleges, athletic events, concerts and gatherings, local schools, bars and restaurants, then finally, in many places, anything deemed "non-essential". I find it really interesting that this change in direction was much more "bottom up" than "top down".

The stock market reaction was similarly rapid with the S&P 500 Index falling approximately 34% from the peak on February 19th to the trough (to date) on March 23rd. Bond markets tanked as well. Investment-grade bonds as represented by the Markit iBoxx USD liquid investment-grade index fell 18.9% from March 6th to March 20th. High-yield bonds, as represented by the Markit iBoxx USD liquid high-yield index fell 21.8% from February 20th to March 23rd.

Unlike most recessions where the change in economic activity is relatively slow, and even at the trough most businesses have some revenue, this time we shut down many businesses (airlines, cruise ships, theme parks, restaurants, many retail stores, etc.) very suddenly and many of them will have zero revenue for an indeterminate period of time. Businesses and investors suddenly started thinking about cash the way consumers suddenly started thinking about toilet paper: they couldn't get enough of it fast enough. Companies drew down lines of credit, businesses and investors sold assets to include stocks, bonds, and shares in money market funds. This was not just a U.S. phenomenon. Overseas companies have borrowed heavily in dollars and they too ran for cash denominated in dollars. This sudden dash for cash created enormous stress in the banks and asset markets.

In order to support the continued functioning of credit markets, the Federal Reserve has embarked on a massive buying program of pretty much everything but junk bonds and equities. They've also created swap lines with other central banks to get dollars overseas. Their intervention has been huge, fast, and necessary. In order to help small businesses, households, and specific industries remain solvent during this shutdown, Congress passed a $2 trillion support package. It is not yet clear if the Federal Reserve interventions or the Federal Government support will be enough, it's too early to tell. The speed with which the government acted is noteworthy.

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America is intentionally holding the economy down to slow the spread of the virus. The key to letting the economy back up off the mat is: reduce the risk of rapid contagion to a level we can live with. I don't think we'll eradicate the virus any more than we've eradicated the flu or the common cold. In the long term this will be another chronic condition that we will collectively manage. We think the leading indicator now for economic activity is going to be the change in the acceleration of new corona virus cases. In other words, when will the spread of the virus slow? Our guess, based on the Chinese experience, is that the acceleration will begin to slow 2-4 weeks after social distancing measures really took effect. We are tracking publicly available information to see if our base case is working out, or not. That will give us some idea of the duration of the intervention. The other big unknown is how much damage was done to the economy. We probably won't really start to understand that until April as companies start to report their quarterly earnings and government data starts to come in. There remain a lot of unknowns.

The United States is not, of course, the only country affected by the virus. China has already been through the worst of it and is recovering. Europe is maybe a week or two ahead of the U.S. in dealing with the virus. Even as China's lock down affected our supply chains, China's exports are going to be affected by the shutdowns in Europe and the U.S., two of their biggest customers. These linkages will slow everyone's recovery somewhat.

It is also possible that the economic stress of dealing with the virus kicks off a self-reinforcing cycle of problems. Cascading defaults on loans are possible which is why governments are pumping money into households and businesses so quickly in an attempt to deal with the problem before it grows out of control. The increase in oil production by Russia and Saudi Arabia, which has collapsed the price of oil to $20 per barrel, is putting enormous stress on energy producers globally, increasing the likelihood of defaults there. Banks are always vulnerable in a recession: reduced credit availability or even bank failures are possible. (The Federal Reserve, in particular, is acting quickly to nip this potential problem in the bud). Finally, this is an election year in the U.S. and the agenda just changed. It's too early to know what new policy proposals will be put on the table or to hypothesize what their impact will be economically, but a major shift in how the government interacts with all or some of the economy is possible. Europe is also vulnerable to upheaval, and we'll be watching that.

The selloff in the markets is presenting us with better pricing on companies than we've seen in quite a while and we are working hard looking for the best opportunities. Jeff developed a rule of thumb in '08-'09 that goes like this "When the market is down 30% and the headlines are all screaming 'Recession!' the next six months will be a pretty good time to put money to work." Substitute "Virus" for "Recession" and that is exactly where we are today. We're not calling a bottom, we really don't know if we've hit the market bottom or not, but we are pretty sure the next six months will be a good time to go shopping, and that's what we're focusing on.

With our best wishes for your success and good health!

Ronald H Muhlenkamp

Jeff Muhlenkamp

Ron Muhlenkamp, Founder
Muhlenkamp & Company, Inc.

Jeff Muhlenkamp, Portfolio Manager
Muhlenkamp & Company, Inc.

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

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**S&P 500 Index** is a widely recognized, unmanaged index of common stock prices. The S&P 500 Index is weighted by market value and its performance is thought to be representative of the stock market as a whole. *You cannot invest directly in an index.*

**Markit iBoxx USD Liquid High Yield Index** consists of liquid USD high yield bonds, selected to provide a balanced representation of the broad USD high yield corporate bond universe. The index is used as a basis for tradable products, including ETFs. *You cannot invest directly in an index.*

**Markit iBoxx USD Liquid Investment Grade Index** is designed to reflect the performance of US Dollar (USD) denominated investment grade corporate debt. The index rules aim to offer a broad coverage of the USD investmen grade liquid bond universe. *You cannot invest directly in an index.*

Corporate Office • 5000 Stonewood Drive, Suite 300 • Wexford, PA 15090-8395 • (877)935-5520
www.muhlenkamp.com • info@muhlenkamp.com

# MuhlenkampSMA All-Cap Value

For the period ended 03/31/2020

*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.

## All-Cap Value Composite Performance (Net of Fees)

| | | | Annualized | | | |
|---|---|---|---|---|---|---|
| | Year to Date | One Year | Past 3 Years | Past 5 Years | Past 10 Years | Past 15 Years |
| **Return** | -24.22% | -19.05% | -6.09% | -4.79 | 1.98% | 0.51% |
| **S&P 500 Total Return*** | -19.60% | -6.98% | 5.10% | 6.73% | 10.53% | 7.58% |
| **Consumer Price Index**** | 0.66% | 2.33% | 2.02% | 1.96% | 1.78% | 2.01% |

* **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 February 2020 – 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 |
|---|---|---|
| Microsoft Corporation | Software | 8.02% |
| Apple Computer Inc. | Technology Hardware, Storage & Peripherals | 6.40% |
| Gilead Sciences, Inc. | Biotechnology | 4.33% |
| SPDR Gold Shares | Exchange Traded Funds | 4.31% |
| McKesson Corporation | Health Care Providers & Services | 3.77% |
| Dow Inc. | Chemicals | 3.63% |
| Bristol-Myers Squibb Company | Pharmaceuticals | 3.59% |
| Microchip Technology Inc. | Semiconductors & Semiconductor Equipment | 3.54% |
| CVS Health Corp. | Health Care Providers & Services | 3.52% |
| Invesco Buyback Achievers | Exchange Traded Funds | 3.51% |
| Berkshire Hathaway Class B | Diversified Financial Services | 3.40% |
| UnitedHealth Group Inc. | Health Care Providers & Services | 3.33% |
| Lockheed Martin Corp. | Aerospace & Defense | 3.27% |
| Biogen Inc. | Biotechnology | 3.09% |
| Broadcom Inc. | Semiconductors & Semiconductor Equipment | 3.07% |
| Jazz Pharmaceuticals Inc. | Pharmaceuticals | 2.58% |
| Cameco Corporation | Oil, Gas, & Consumable Fuels | 2.54% |
| Alerian MLP ETF | Exchange Traded Funds | 2.49% |
| Lennar Corp Class A | Household Durables | 2.40% |
| Mastec Inc. | Construction & Engineering | 2.36% |

*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).*

**Muhlenkamp & Company, Inc.**
*Intelligent Investment Management*

## 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.

## SMA Facts

| | |
|---|---|
| Average Number of Equity Holdings | 32 |
| Cash & Cash Equivalents | 9.85% |
| Portfolio Turnover | 31.39%‡ |

‡ *Trailing 12 months*

*SMA Facts are presented as supplemental information.*

## SMA Information

The All-Cap Value Composite was created in December 2003 and 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.*

## Investment Adviser


Muhlenkamp & Company, Inc.
5000 Stonewood Drive, Suite 300
Wexford, PA 15090-8395
(877)935-5520
services@muhlenkamp.com

**www.muhlenkamp.com**


**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

| | | | | ANNUAL PERFORMANCE | | | THREE-YEAR ANNUALIZED STANDARD DEVIATION* | | |
|---|---|---|---|---|---|---|---|---|---|
| Year End | Total Firm Assets (USD) (millions) | Composite Assets (USD) (millions) | Number of Accounts | Composite Gross | Composite Net | S&P 500 Total Return Index | Composite | S&P 500 Total Return Index | Composite Dispersion** |
| 2019 | 253 | 34 | 48 | 14.70 | 13.79 | 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 |
| 2005 | 3471 | 287 | 289 | 10.04 | 9.22 | 4.91 | | | 3.38 |

*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 June 30, 2019 by ACA Performance Services.

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The All-Cap Value Composite has been examined for the periods December 31, 1993 through June 30, 2019. The verification and performance examination reports are available upon request.

Muhlenkamp is an independent registered investment advisory firm registered with the Securities and Exchange Commission. The firm's list of composite descriptions is 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 portfolios, calculating performance, and preparing compliant presentations are available upon request.

* **Three-Year Annualized Standard Deviation** *is a measure of volatility, calculated by taking the standard deviation of 36 monthly returns, 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 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.*