

MuhlenkampMemorandum

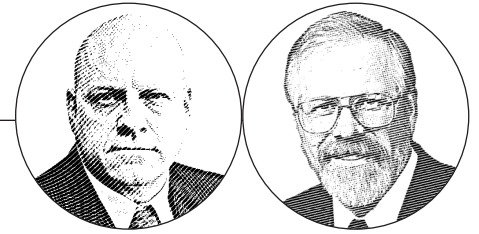
Issue 130

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Quarterly Letter

By Jeff Muhlenkamp, Portfolio Manager and Ron Muhlenkamp, Founder



A couple of noteworthy changes have occurred in the first quarter of 2019:

First, the Federal Reserve has reconsidered their program of interest rate increases and balance sheet reductions. They now intend to hold short-term rates steady in 2019 and end their balance sheet reduction program in October 2019. Last year, we wrote extensively about the risk to asset prices we saw in the Federal Reserve's asset reduction program and, we believe, the market started reacting to that program in October 2018. We are not at all surprised that the stock market rebounded when the Federal Reserve announced the change in their thinking.

Second, the U.S. Treasury yield curve inverted in late March 2019. A "yield curve inversion" occurs when short-term interest rates are higher than long-term interest rates. In this case the 3-month Treasury yield was higher than the 10-year Treasury yield. As we've mentioned before, conventional wisdom considers this a sign of an impending recession, with the recession following the inversion by anywhere from 6 months to 2 years. As a result of the inversion, stock prices didn't move too much, but bond prices did: the yield on the 10-year Treasury went from 2.6% to 2.4% in two weeks—a sharp move in the bond market. Even with the recent drop in interest rates, short-term rates have remained above the rate of inflation—a benefit to savers and pension funds and increasingly a rare set of

circumstances when looked at from a global perspective.

Looking at the domestic economy, economists expect 2.4% real GDP growth in the U.S. this year and 1.9% real GDP growth next year. That's significantly slower than the 2.9% GDP growth we saw in 2018. On balance, the economic data we are seeing is consistent with slower growth than last year. We are not seeing signs of an imminent recession. One bright spot is the housing market where we are seeing better than expected sales numbers as the spring selling season begins. Inflation remains subdued between 1.5% and 2%. We don't currently see a reason for inflation to increase meaningfully.

Globally, economic growth is weak in China and virtually non-existent in Europe. The Chinese government is actively trying to manage its growth slowdown and, so far, appears to be successful—keeping growth in a range that they consider acceptable. Europe isn't faring as well. As a result of weak economic numbers the European Central Bank (ECB), which ended its asset buying program in December, is talking about restarting the program to support growth. The "Brexit" debacle in Great Britain isn't helping matters. After two years of negotiations, the British Government still has no clear idea what they want the split from the European Union (EU) to look like. The British parliament has voted

on eight separate concepts, and rejected them all. The deadline for "Brexit" has been extended from March 29, 2019 to April 12, 2019. We expect it will be extended several more times as the debacle drags on. Also, on the international front, the U.S. and China continue to negotiate over trade and we expect something to get worked out this year. Neither "Brexit" nor the trade negotiations with China appear to move the stock market any more—we believe our views to be widely held.

In summary, the U.S. economy appears to be slowing this year, but perhaps not as much as we thought four months ago. The threat to asset markets posed by the Federal Reserve's shrinking balance sheet is receding, and disruption due to tariffs or Brexit is also less likely. Slowing global growth remains a concern and we'll be watching what happens in China pretty closely. The inversion of the yield curve is also a cautionary sign. During the last quarter we've invested some of our cash in good companies at prices we found attractive. We will continue to do so. 

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

Gross Domestic Product (GDP) is the total market value of all goods and services produced within a country in a given period of time (usually a calendar year).



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Letter to My Daughters: On Financial Health and Wellness



By Tony Muhlenkamp, President

You girls remember how a few years ago I was 80 pounds overweight and taking all kinds of medicines for various ailments (high blood pressure, high cholesterol, sleep apnea, metabolic syndrome). And you were so supportive while I worked to get healthy, which I knew how to do (eat better, manage stress, move the body) but hadn't done for a long time. And you helped me do that EVERY DAY for 18 months because I needed help doing something simple, but not easy. And you have supported me in continuing to do the work ever since. Thank you for that, I couldn't do it without you.

But, I don't think I ever told you WHY I did it; why I continue to do it. It's because I didn't want to die in my 50s; I want to live to be a healthy, active, and involved grandpa playing volleyball and frisbee with your children, teaching them how to ride a bike, motorcycle, and to shoot pool. The only way I know to hopefully do that was to get fit and healthy, to try to avoid the path to heart disease, stroke, and diabetes, etc.

Financial Health and Wellness has a LOT in common with Physical Health and Wellness, especially in the sense that

everyone knows it's important, and they even know how to do it (make more, spend less, and invest the difference), but very few people actually do what it takes to achieve it. So, I'm starting to think people haven't determined WHY they should work to get and stay financially healthy. Just as I needed a sufficient WHY to eat better, manage stress, and exercise; people need a good WHY to earn, save, and invest.

My WHY for being financially healthy is remarkably similar to my WHY for being

**Diligence
Discipline
Determination**

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physically healthy: to be able to watch and enjoy all the things you girls and your children are going to do and achieve and accomplish. I want to be *financially* healthy enough to enjoy my *physical* health, and I want to be *physically* healthy enough to enjoy my *financial* health.


Now, I had very good reasons for eating poorly and not working out: I was busy with work and you girls; I was stressed; I was tired; etc. But my good reasons for my bad habits were all short term gratifying and long term destructive. I had to shift my focus to the good reasons I have for being healthy.

The same thing is true for your finances. You could have 100 reasons why you can't save, and they are all good and rational reasons, but they are short-term reasons that are counterproductive to your long-term goals and ambitions. Do the right things, do them consistently, and do them for sustained periods of time measured in years.

John Templeton once explained to a reporter one of his secrets for becoming wealthy; for the first 20 years out of college he saved half of everything he earned. Period. Now John Templeton is a LEGENDARY investor and earned good returns for his clients by investing. But one of his methods for becoming wealthy was not some stock-picking tip; it was to save HALF of everything he made. Simple really, dirt simple—but not EASY. Just like being physically healthy is simple, but not easy, so is being financially healthy. I'm not saying you have to save 50% of everything you earn, but you could probably save 5% (maybe even 10%). Most of us can find a

way to save a nickel or a dime out of every dollar we earn (and if you can't find a way, come talk to me; I'll help you.)

We should go over the wonderful effect of compound interest on your finances, but the key to compounding is TIME. The earlier you start, the more consistent you are, the better it works. Just like being physically healthy, the benefits compound over time. The longer you do it, the more consistent you are, the better your results.

Let me know if you want to talk about any of this, or if you need help getting started. At your age, you don't need much in the way of financial planning, just save and invest, save and invest. As you get older, it will be useful for us to go through a formal and comprehensive financial planning process; but for right now just save and invest, save and invest. 

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

Investing in stocks, mutual funds, and other assets involves risk. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Principal loss is possible. Past performance does not guarantee future results.

Announcements

Register for our Upcoming Webcast

Please join us for our webcast with Tony, Ron, and Jeff Muhlenkamp.

Thursday, May 30, 2019
4:00 p.m. – 5:00 p.m. ET

Register at www.muhlenkamp.com or call us at (877)935-5520.

Webcast Archive Available on Website

At our February 28, 2019 webcast, Ron and Jeff updated their views on the economy and the global investing environment. Visit www.muhlenkamp.com for the webcast archive and to access other videos and essays available in our Library collection.

Request for Email Address

Muhlenkamp & Company regularly publishes information that gets distributed by email only. To be added to our email list, visit www.muhlenkamp.com or call us at (877) 935-5520. Your contact information will not be released to any third party. 



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MuhlenkampSMA

All-Cap Value

For the period ended 3/31/2019

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.



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All-Cap Value Composite Performance (Net of Fees)

| | Year to Date | One Year | Past 3 Years | Annualized Past 5 Years | Past 10 Years | Past 15 Years |
|------------------------|--------------|----------|--------------|-------------------------|---------------|---------------|
| Return | 6.53% | -1.40% | 3.05% | 1.05 | 8.64% | 2.67% |
| S&P 500 Total Return* | 13.65% | 9.50% | 13.51% | 10.91% | 15.92% | 8.57% |
| Consumer Price Index** | 0.61% | 1.52% | 2.16% | 1.49% | 1.77% | 2.06% |

* 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 2019 – 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 | 4.79% |
| Apple Computer Inc. | Technology Hardware, Storage & Peripherals | 4.40% |
| Alliance Data Systems Corporation | IT Services | 4.05% |
| UnitedHealth Group Inc. | Healthcare Providers & Services | 3.99% |
| AutoZone, Inc. | Specialty Retail | 3.89% |
| Microchip Technology | Semiconductors & Semiconductor Equipment | 3.39% |
| Cameco Corporation | Oil, Gas, & Consumable Fuels | 3.26% |
| Alerian MLP ETF | Exchange Traded Funds | 3.26% |
| Celanese Corporation - Series A | Chemicals | 3.19% |
| Broadcom Inc. | Semiconductors & Semiconductor Equipment | 3.07% |
| Annaly Capital Management Inc. | Real Estate Investment Trusts | 3.02% |
| Gilead Sciences, Inc. | Biotechnology | 2.97% |
| Invesco Buyback Achievers | Exchange Traded Funds | 2.96% |
| SPDR Gold Shares | Exchange Traded Funds | 2.82% |
| DowDuPont, Inc. | Chemicals | 2.63% |
| Celgene Corp. | Biotechnology | 2.58% |
| Cognizant Technology Solutions Corp. | IT Services | 2.48% |
| McKesson Corporation | Health Care Providers & Services | 2.43% |
| Federated Investors, Inc. - Class B | Capital Markets | 2.28% |
| Biogen Idec Inc. | Biotechnology | 1.87% |

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.



SMA Facts

Average Number of Equity Holdings 26
Cash & Cash Equivalents 23.72%
Portfolio Turnover 9.16%‡

‡ 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

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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 | | | THREE-YEAR ANNUALIZED STANDARD DEVIATION* | | |
|----------|------------------------------------|-----------------------------------|--------------------|--------------------|---------------|----------------------------|---|----------------------------|------------------------|
| | | | | Composite Gross | Composite Net | S&P 500 Total Return Index | Composite | S&P 500 Total Return Index | Composite Dispersion** |
| 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 |
| 2004 | 2261 | 197 | 206 | 24.54 | 23.56 | 10.88 | | | 3.33 |

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, 2017 by ACA Performance Services, LLC.

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 December 31, 2017. 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.