January 21, 2022

Dear Fellow Investor:

Happy New Year to you and your loved ones from all of us at Weybosset Research & Management LLC! We wish you a healthy and PROSPEROUS 2022.

From the point of view of prosperity, 2021 was not so bad, especially for investors in the U.S. stock market. The S&P 500 Index, our benchmark, was up 26.6% in 2021, 28.41% with reinvested dividends.

The accounts for which we are responsible trailed the S&P 500 by a few percentage points—we were up low-to-mid 20s for the year.

Before handing the mic over to Justin for his thoughts on the year, the quarter, the future, I would like to remark on a topic that should be of great importance to you, and that is the emergence of inflation as a headline topic on the global economic scene.

Many of our clients are retired and living on their investments; and many are saving for what is hoped will be a comfortable retirement. Inflation is probably the retired person's worst enemy because many, if not most, retired people live on a fixed income, a pension, for instance. Inflation simply means "the decline of purchasing power of a given currency over time" (*Investopedia).* That fixed income on which retired people live thus buys less and less of the things they want or need as time goes by. Because, over time, inflation *compounds*, the cumulative effect of those price increases can be devastating.

So, for instance, inflation has averaged 2.5-3.0% over my lifetime, a number, that, on the surface, does not look that bad. But because of the compounding effect, I now need about eight dollars for every one dollar I earned in 1965 when I got my first paycheck (for playing drums in a rock and roll band).

The official rate of inflation in 2021 was more than twice the average in my lifetime, the highest since 1982. And a return of the mid-teens-type inflation of the 1970s, which is not out of the question given the amount of currency printed in recent years as "stimulus", would indeed be ruinous.

If a fixed income is a bad place to be in inflationary times, assets delivering a fixed income are probably the worst assets to own in inflationary times. A bond, for instance, pays income regularly, every six months typically, and then at maturity returns principal. But in times of inflation, each fixed payment buys less and less, and the "real" value of principal at maturity, its purchasing power, is reduced by the cumulative amount of compounded inflation. A bad deal! Yet there are trillions and trillions of dollars of bonds out there.

And people keep buying bonds. What will happen to the bond market as investors come to realize that bonds are a bad deal?

Fortunately, you, Fellow Investor, own assets the products of which people will want (or need) regardless of price. Whatever the level of inflation a year from now, I (confidently) predict people will want to eat, even if they must pay up to do so. Our agricultural companies, which produce tractors, crop protection substances, finance farmers, and haul food to market, suddenly look like perspicacious investments. With only a little less confidence, I predict people will continue to brush their teeth, so our global toothpaste company looks like a good bet, too.

And while I'm predicting: people will continue to wreck their cars, and somebody has to dispose and recycle the wrecks. Glad Copart is here! The world remains a dangerous place, one that might feel a little safer if things like nuclear submarines, sophisticated tanks, and state-of-the-art cyber security

resources were on hand to ward off the bad guys. Call General Dynamics, call SAIC! We Weybosset Research investors appreciate the business!

This is the power of productive assets. People will always be willing to trade a portion of their labor for something to eat, a clean mouth, help after a car accident, or physical security. The nominal price at which such transactions take place is secondary to the need for the transactions themselves, hence the attraction of productive assets

So, I hope you will keep the importance of inflation in mind. I have no idea if inflation is “transitory”, newly structural, or if we’re headed for a train wreck. But I do believe that, whatever the outcome, you are properly invested.

Now, over to you, Justin!

2022: The year of the tangible, practical, and profitable.

Dear Fellow Investor,

The last three years witnessed spectacular returns for the major indexes--and Weybosset investors. We have kept pace with the broad averages, compounding your money at roughly 17% for the last six years, nearly doubling your money in the last three years.

Though the media and Wall Street talk mainly about the mega-cap tech companies, our businesses, which produce the things you need in your daily life--think food, specialty materials, disposal of wrecked cars, car safety systems, testing instruments, and clothing--have performed admirably.

Though Fla and I are of necessity market observers, we aim to be business analysts. Through the process of worrying about the business itself and not the market, we have done quite well over the last 30 years.

We choose to own stocks, shares of businesses that can outpace inflation. It’s not the time, it’s the fundamentals of the business. If we own a stock for several years and it does not produce an immediate return, we have time to accumulate additional shares of a fantastic business at advantageous prices. Eventually the market realizes the true worth of the wonderful gems we have selected, producing adequate returns over time.

“We have consistently invested in undervalued common stocks that, individually, are unlikely to present us with permanent loss and that, collectively, are close to risk-free.” - Warren Buffett

We are going to have good years and bad years and all kinds of years in between. We care very much about the price we pay for a security but not the price over the next twelve months. We care more about the next five, ten, and twenty years.

However, there are a few moments in history where it is important to focus on the macro environment and how that might affect our portfolio. We believe the time has come where the investing landscape is changing.

For the last thirteen years, the Federal Reserve has been in an accommodative stance, supporting the economy and markets through asset purchases and interest rate cuts. This has enabled the economy to revive from a tech bubble, a financial crisis, and a pandemic. Through each panic, the economy has healed, and markets--and our portfolios--have gone on to make new all-time highs.

The biggest beneficiary of the low interest rate environment was mega-cap tech and high-flying, high-multiple, no-earnings, pie-in-the-sky businesses.

These New World Ideas caught the attention of retail investors in 2020 and 2021 as they sat at home: stimulus checks in hand, abundant savings, and a government-induced coma from the pandemic.

Valuations were disregarded and true fundamentals of businesses were eschewed for the promise of profits in the future, a future where cars fly, apps rule the world, and software will manage every aspect of your life.

Many of these stocks were trading at 10, 20, even 50 times sales, with no earnings to speak of for the next five to ten years, if at all. We own no such businesses.

“If you can keep your head when all about you are losing theirs and blaming it on you, if you can trust yourself when all men doubt you but make allowance for their doubting too!”. – Rudyard Kipling

Low rates and even negative rates in parts of the world have forced investors to move up the risk curve to find yield and higher returns, disregarding fundamentals and risk. The permanent loss of capital grows as you move higher up the curve.

The new world fervor seems to have climaxed this fall in spectacular fashion unnoticed by most people, as the major averages sat at all-time highs.

As I write this letter, the tech-heavy Nasdaq has fallen roughly 12% year-to-date while the S& P 500 has fallen 7.75%. The accounts for which we are responsible are down roughly 5-6% year to date.

Growth stocks have outpaced Value stocks for the last thirteen years. As seen in the chart attached, the performance differential between Growth & Value is at its largest discrepancy ever, even wider than the tech bubble of the late 1990s.

For the last thirteen years there has been nothing to change this discrepancy--until now.

The Federal Reserve announced that it has begun tapering, dialing back the easy money policies in place since the early 2000s and will begin the process of raising interest rates.

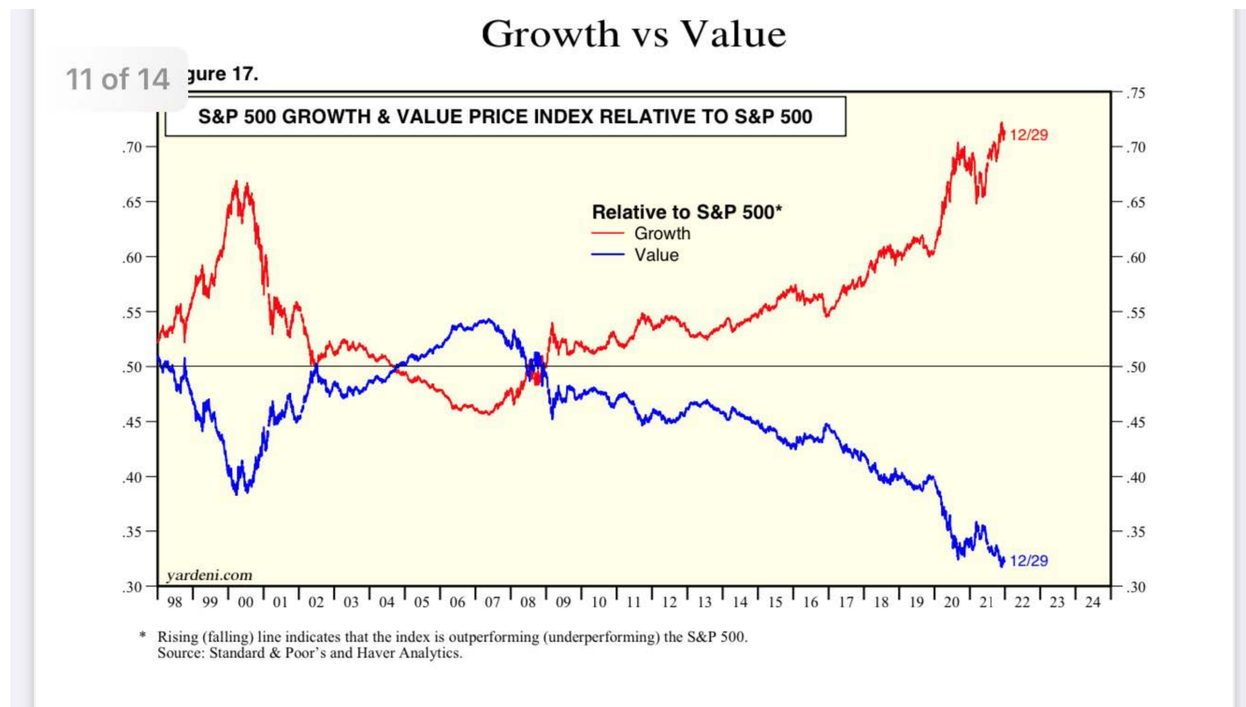
Most investors today have long forgotten or have never invested through an inflationary period or even a fed tightening cycle. We have.

Investors can barely remember that Value outperformed Growth for more than 15 years in the 1980s through the early 1990s.

The Federal Reserve is beginning to normalize monetary policy, restoring the time value of money.

This monetary policy shift has profound implications for assets and markets. We are already seeing the high-flying, high-multiple, and negative-earning businesses lose their luster.

In a short period of time many of these stocks are down 35-80% from their highs with much more room to the downside, while businesses with real earnings, superior cash flow, and dividends are beginning to be bid up. These are the characteristics of the Weybosset portfolio.



Though history does not repeat itself it does rhyme. In 2000, the S&P 500 declined roughly 8% and the Weybosset portfolio was up some 38%.

Based on valuations and earnings, many of our businesses today are undervalued relative to the SP500 by roughly 25-50%.

Fla and I have seen fads come and go. In the end, we have never forgotten rule number 1: never lose money. That rule starts with the foundation of investing in businesses that always make money.

We will continue to stay invested in our leading, earnings-positive, cash-flow-heavy businesses, while we search the world for new investments to make.

Predictions are futile; however, I can assure you, like Yogi Berra said, “the future ain’t what it used to be.” Perhaps the future, is already priced into the market, and it’s time to start valuing the tangible, practical, and profitable correctly.

As always thank you for your trust. We look forward to protecting and growing your capital for the next thirty years. Our commitment to client service remains steadfast. Please feel free to contact us with any questions, comments, or concerns.

Yours very truly,

Justin E. Deutsch

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