April 18, 2023

Dear Fellow Investor,

The performance of the broad averages in the first quarter of 2023 was positive, up 7% for the S&P 500, but it felt like a continuation of the 2022 bear market. The accounts for which we are responsible trailed the averages by a handful of percentage points—we were up low single digits, but nonetheless **UP**.

The suspicion that the performance of the indices might not reflect conditions in the overall market was confirmed to me when Justin shared a research piece from 22V, a New York-based boutique, which showed that, without the inclusion of seven mega-cap technology companies, the S&P 500 *dropped* 4.34% in the first quarter of 2023.

That finding is more in keeping with an environment in which inflation is very much an open question, in which interest rates are surely trending up (but how much?), in which the broad economy is slowing down (but how much?), and in which a hot war in Europe rages unabated, with all its spillover effects on global economic activity. 1Q 2023 feels more like a rally in a bear market.

The turmoil in the real economy has sparked its share of financial crises, including the collapse of significant participants in the cryptocurrency market, the end of the SPAC (Special Activity Corporation—essentially a blank check to acquire, well, almost anything) craze, but, perhaps most ominously, the collapse of several banks in the U.S. and overseas.

But as my partner Justin points out, bank failures are a normal part of the capitalist system. (Failure in principle must be an inherent component of any system that also offers success.) That's because banking is itself a risky business for the following reason: if everyone who has money in a bank wants his or her money today, he or she can't have it because it's not there—it's been lent out. The system works because not everybody wants his or her money today; but he or she has CONFIDENCE that when he or she needs money, it will be there. Take the CONFIDENCE away, and you have a run on the bank as panicked depositors scramble to get what money they can before the doors close.

The failures of Silicon Valley Bank in California, Signature Bank in New York, and Credit Suisse in Switzerland have left jittery observers wondering which shoe is next to drop. Alas, speculation—and it is only speculation-- has fallen on Charles Schwab & Co., the custodian of our accounts, Fellow Investor.

Fortunately, the system is set up such that we are all well protected against the failure of Charles Schwab & Co. We enjoy at least three lines of protection. The first and most important is that a custodian such as Schwab is strictly required to keep customer assets separate from all other, including custodian, assets. Your securities may appear on the books of the issuers as "Street Name" at Schwab, but Schwab is required by US law to keep your shares of, say, Berkshire Hathaway separate from anybody else's shares of Berkshire Hathaway, including Schwab. In the (highly unlikely) event the lights went out at Schwab, your securities, which have always been separated from everyone else's, would be transferred to a new custodian and you could do whatever you like from there.

I remember when Drexel Burnham Lambert imploded in the late 1980s. Clients went to bed on a Friday night with their accounts at Drexel and woke up on Monday morning with their accounts at another custodian, JP Morgan as I recall. Over the weekend, Drexel had ceased to exist. Crazy stuff and an unpleasant surprise, but no clients were harmed. Similarly, in 2008 Merrill Lynch was our custodian, but Merrill got in big trouble during the mayhem of the housing bubble's collapse. Eventually Bank of America had to come in and acquire Merrill Lynch. Our clients never missed a beat.

The second line of defense is SIPC, or the Security Investor's Protection Corporation, a U.S. Government agency which is much to the brokerage industry as FDIC is to the banking business. SIPC insures each customer up to $500,000, including $250,000 in cash, against the failure of Schwab (not against declines in market value).

And finally, Schwab holds private insurance, in this case from Lloyds of London, of up to $20 million per customer.

So, I remain CONFIDENT in Charles Schwab & Co., even though we live in an era in which financial institutions are biting the dust. The chances of Schwab getting into financial trouble are extremely low. Schwab is large—over $7 trillion in customer assets—conservatively managed and has multiple lines of liquidity. But even if the worst were to happen, we have multiple lines of defense as I have outlined above.

Thank you for your CONFIDENCE in Weybosset Research & Management LLC. We pledge our very best to deserve that confidence. Now I think Justin has a word or two for you,

Fla

When everything seems to be going against you, remember that the airplane takes off against the wind, not with it. – **Henry Ford**

The hits keep coming!

No, I am not referring to Casey Kasem, the great radio broadcaster, of the 1990s, but rather the first quarter of 2023 in financial markets.

In the first three months of the year, we saw another fed hike (in keeping with the fastest and largest rate increases ever) and several bank runs.

And yet to most people's dismay, the S & P 500 finished the first quarter **UP** 7%. **Yes up**. However, underneath the surface of the major averages a different story is shaping up. The S & P 500 **ex the biggest 7 tech stocks was down 4.34%** according 22V Research. The accounts for which we are responsible at Weybosset, finished up low single digits, slightly lagging the major averages.

Despite the major averages being up for 2023, **fear is widespread**, as measured by the Bank of America Sell Side Indicator reaching its **lowest point since 2009** (the financial crisis), gripping even seasoned investors. (The Sell Side indicator measures the average recommended allocation to stocks by Wall Street strategists and is a remarkably dependable CONTRARY indicator)

Economists and investors alike are pre-occupied with the threat that the Federal Reserve will put us into a deep dark recession, that the failure of a few poorly managed banks (Silicon Valley & Signature), will tank the economy and stocks along with them. But remember, in a capitalist system investors occasionally lose money, the strong survive. That's what's supposed to happen.

Banking failures in this country are as American as Apple pie. There have been thousands of bank failures since 1900. Banking is inherently a risky business.

With the Federal Reserve keeping interest rates at or near zero for a decade, some banking executives did dumb things that have become exposed recently. Higher interest rates and a slowing economy undress problems in the economy. However, they have not stopped the great American economic engine.

Since 1900, including bank failures, depressions, recessions, World Wars, pandemics, bubbles, and crashes, the Dow Jones has returned 9.79% per annum--plus handsome dividends.

The stock market is a forward-looking mechanism, which means it usually experiences turbulence ahead of the real economy. Last year we wrote to you that when the market prices in a recession it goes down on average 30% with individual stocks going down 50-90%. Well, that's exactly what happened last year. So, is it really a surprise that all these bad things keep happening in the real economy? What if the Fed restoring interest rates to more normal levels boosts the economy?

Fears regarding the long-term prosperity of the nation's many sound companies make no sense. Perhaps the biggest fear should be the government's fiscal policies? Inflation has doubled in the last year from where it has been for the better part of two decades, eroding your and everyone else's purchasing power.

Milton Friedman told us in the 1970s "*inflation is made in Washington because only Washington can create money. And any other attribution to other groups of inflation is wrong. Consumers don't produce it, producers don't produce it, the trade unions don't produce it, foreign sheikhs don't produce it, oil imports don't produce it. What produces it is too much gov't creation of money and nothing else."*

Our businesses will indeed suffer earnings misses and bumps in the road as they always have. But most will be setting new profit records in the next 5, 10, 20 years.

Though markets are still 20% from their all-time highs, and Weybosset portfolios are off single digits from their all-time highs, "*I haven't the faintest idea as to whether stocks will be higher or lower a month or a year from now. What is likely, however, is that the market will move higher, perhaps substantially so, well before either sentiment or the economy turns up. So, if you wait for the robins, spring will be over*." - **Warren Buffett**

We own a curated collection of some of the finest businesses in America, businesses that provide goods and services we need in our daily lives. We own these stocks based upon our expectations about their long-term business performance and not because we view them as vehicles for timely market moves. In the long term our productive assets' returns will outpace inflation.

Economic forecasts are of no use to us. They say economists have correctly predicted 9 out of the last 7 recessions. We manage your money by allocating it to the best businesses with seasoned management who have steered their businesses through every economic cycle.

We implore you to keep adequate liquidity, so that you will always be prepared for the unexpected (job loss, health issues to name a few) and do not have to worry about "the market".

Fla and I are not stock pickers, we are business pickers.

Last year, during the market sell-off we made a few new investments, taking advantage of the panic to do something smart with your money. From time to time the markets may make us look foolish or badly out of step, but in time the earnings power of the wonderful gems we have selected prevail and those returns become our shareholder returns.

It is our job to think about risks. We have our entire net worth invested in this collection of businesses, alongside you and our relatives. We take pride in investing and growing your hard-earned capital so you can safely retire, pay for a house, college, a vacation, or any other use of your capital that you desire.

No one knows if there will be more bank failures or if the Federal Reserve will knowingly put us in a recession. I do know, whatever the outcome, we are properly positioned in our conservative and patient approach for when the storm clouds pass and the American engine fires up again.

Thank you for your continued trust and support. Spring is here and we look forward to seeing and hearing from you.

Sincerely,

Justin