Quarterly Update
Fort Street

Contact Us

Fort Street Asset Management LLC
900 Fort Street Mall Suite #1727
Honolulu, Hawaii 96813

info@fortstreetam.com
www.fortstreetam.com

Fort Street
ASSET MANAGEMENT

Preamble – Random Musings Of An Aging Fund Manager

As I was staring vacantly into space (as I am wont to do), pondering the nature of today's bull market, I found myself wondering why we use the terms "bull or bear" to describe the direction of the financial markets. Why not Chicken or Sea Cucumber? Anyway, according to the Internet, the terms bull and bear markets relate to how each animal attacks. A bull thrusts its horns upwards, while a bear swipes its paws downward. Riveting stuff. I'll admit it wasn't much of a revelation, but I suppose a possible takeaway is that we tend to accept certain "truths" without question. The earth was flat until it wasn't. (Electric vehicles will make conventional cars obsolete by 2035)

You're probably asking what this has to do with the price of tea in China ($1.59 per kilo), and to be fair, I'm not entirely sure. The weather and waves in Hawaii have been uncooperative of late, so I've arguably had too much time on my hands. In any event, I think this underscores the importance of staying curious and questioning the prevailing wisdom. We humans can be a lazy bunch and are often happy to settle for the status quo, even when the facts have changed or are no longer valid.

Question everything. Learn something. Answer nothing. Euripides

Catch the Chicken. Cook the Chicken. Eat the Chicken. Cousin Peter
*for the record, he never actually said this, but I'm pretty sure he was thinking about it.

After years of evolution, most humans are hardwired to be cautious, often favoring the avoidance of loss over the pursuit of gain. We fear change. At Fort Street, we try to incorporate this psychological or physiological dynamic to enhance our investment approach as we strive to protect and grow assets. Understanding human behavior is a crucial component of how we formulate our investment and trading strategies, empowering us to make informed decisions.

Who dares wins. British Special Air Service (SAS)

George Soros once said that it takes courage to be a pig. This is especially true in a herd sport like investing. The truly gifted money managers are not afraid to roam independently from the pack. So are the ones not playing with a full deck. There is a fine line between genius and becoming lion food. Based in Hawaii and far from the madding crowd, Fort Street attempts to pursue its investment strategy with less distraction and temptation to conform. We just need to be mindful of not becoming shark bait in the process.

PERFORMANCE AND MARKET REVIEW

Speaking of shark bait, the waters were unexpectedly pleasant for equity investors in the first quarter of this year. Bonds, on the other hand, were caught in a tempest, as higher-than-expected inflation put the kibosh on hopes that the Fed will cut rates anytime soon. Why the markets obsess over what the Fed will or won't do is beyond us; such a waste of time and energy. Rest assured that we do not base our strategy on the daily whims or utterances of the high priests at the Fed.

Risks? What risks?

Our crystal ball has done a commendable job so far this year. While we did not predict that we would be on the precipice of a regional war in the Middle East, we did note that geopolitical risk was rising. Equity markets continued to grind higher, clocking in a return of 10.16%. Over the same period, the Fort Street Fund was up 4.67%, but with significantly less risk. Our total equity exposure has averaged 55% this year, of which approximately 23% is in commodity-related stocks. The rest of our capital is spread out between bonds, cash, gold, protective strategies, and several externally managed specialized funds.

Despite being relatively bullish on the economy and equities, a variety of short-term and long-term risks has tempered our enthusiasm. The prospect of more inflation, higher interest rates, rising geopolitical tensions, stretched valuations, liquidity concerns, a polarized political climate, alien invasion (little green men), and a looming national debt crisis has led us to keep risk low across the portfolio.

In light of this backdrop, we are happy to invest in risk-free short-term bonds yielding 5% and spread our bets across a variety of assets and strategies. Coming to terms with our own fallibility, we are reformed egomaniacs. Our goal is not to beat the S&P 500 in all periods – we accept that we will often underperform during raging bull markets. As for the S&P 500 index, it is just one of our benchmarks – our main focus is on protecting capital in down markets and our ability to generate excess returns by taking advantage of falling prices. The portfolio is designed not to move in lockstep with the S&P 500, so our performance will often diverge on the way up and down.

THE MIDDLE EAST – AN INVESTOR'S VIEW

After more than thirty years as a market practitioner, I have learned that political events in and of themselves are generally not the arbiters of market prices. While they certainly affect sentiment and investor behavior, economic fundamentals are the ultimate determinant of price levels.

Having said that, a direct war between Israel and Iran or an all-out war in the Middle East would likely send the global economy into a recession, ushering in a bear market for financial assets. While certainly adding another layer of risk to an already volatile situation, our guess is that the current conflict will stay limited for now. Could we be wrong? Absolutely. Is the Fort Street Fund prepared for that possibility? To a certain extent, yes. Barring a major escalation in the Middle East, we are inclined to buy into a market that falls more on sentiment and less on actual economic data.

Looks kinda safe

As a rule, we do not invest where the outcome is predicated on political factors. Decisions that are not based on economic considerations can lead to results that defy logic. It's like gambling when you know the odds are stacked against you. This is one of the main reasons why we have minimal exposure to China. The Chinese government is making decisions that are more based on political objectives and not economic factors.

Our crystal ball is far from perfect. It's not even made of crystal. How things play out is next to impossible to predict. As paranoid optimists, we can see the bull and bear case. Our sense is that an escalation is in no one's interests and that cooler heads should prevail. We suspect many conversations are taking place that could create conditions for a more stable region. At the same time, a fair and durable political solution for everyone looks elusive. At the end of the day, we need to maintain hope, perspective, and, if possible, a sense of humor, although when people are dying, that is not so easy. I usually pray for surf (and ice cream). Today, I pray for peace.

FORWARD OUTLOOK

"Good thing I'm wearing my invisibility cloak."

Cautiously Bullish: Despite recent inflation jitters and the Fed's reluctance to cut interest rates, we remain relatively sanguine on the outlook for equities over the next 12 months. Contrary to the media headlines, the economy continues to chug along, and corporate profits are growing. Valuations for the broader market are not cheap, and certain sectors, such as tech, are priced for perfection and vulnerable to a correction. The situation in the Middle East remains fluid, and the recent surge in the VIX, the market's volatility gauge, suggests that the road ahead could be bumpy. We would also point out that a lower base effect will probably keep inflation data somewhat buoyant, especially as we head into the second half of the year.

In bull markets, higher prices initially extend investor skepticism until the pain of not being invested (FOMO) and the data outweigh concerns that a bear market is just around the corner. A bear market is always around the next corner – or tree. It just depends on which tree we are talking about.

Market cycles: Sir John Templeton said, "Bull markets are born on pessimism, grow on skepticism, mature on optimism, and die on euphoria." Our guess is that we are now in the maturing phase. Market cycles are inherently dynamic, so it's hard to know with any certainty. The market's path will gyrate as circumstances change. Stretched sentiment in and of itself is not reason enough for equity gains to reverse, but as the bull camp gets more crowded, weak hands can be quickly vanquished. We will, as always, tread carefully.

At the end of the day, trying to predict what the market will do in any given period is like nailing jelly to a wall. I've tried doing this at home with an assortment of jellies. The results speak for themselves.

Market prediction experiment – spoiler alert: they don't work

Election Volatility: This year's presidential election is likely to inject an extra dose of volatility into the markets. It doesn't necessarily change our investment outlook, but it does suggest that we prepare for some potential turbulence. Clint and I have installed seatbelts on our chairs, and we often wear helmets in the office for extra safety. Mine is made of aluminum foil (aluminium for our British cousins) to prevent the aliens from further messing around with my brain and causing us to underperform. Please note that helmets with the pointy end at the top are more effective.

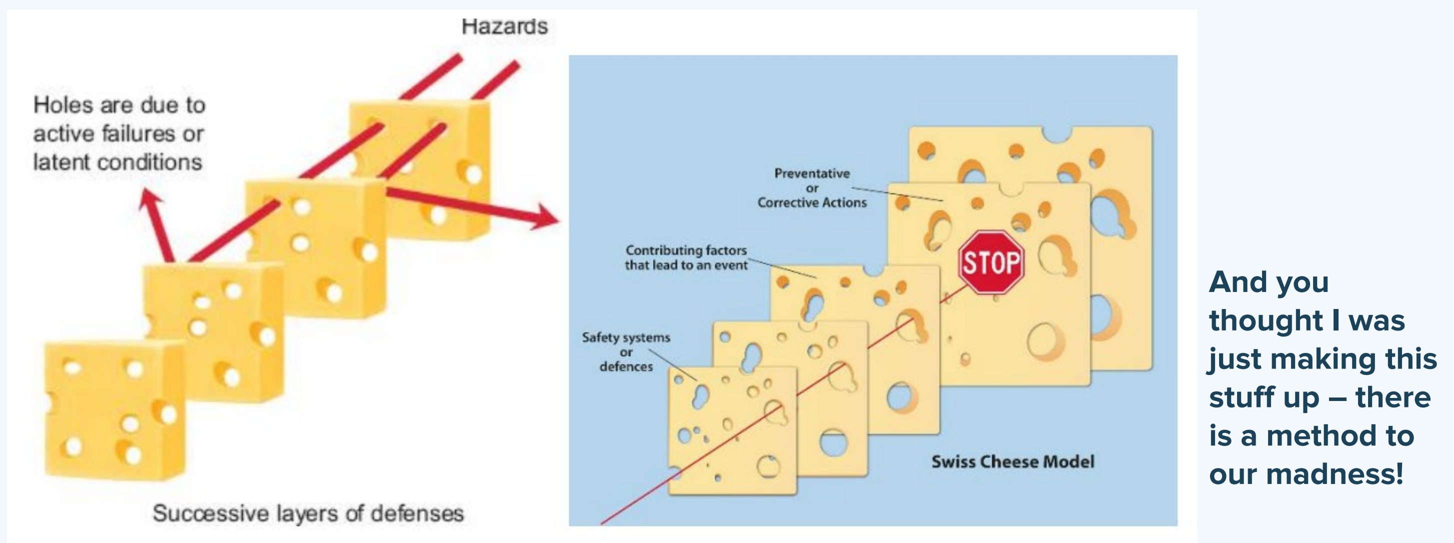
"No one's going to mess with my brain! Sid, is that you?"

Beyond the horizon: Part of our general thesis has been that we are transitioning to a more inflationary world. We are not saying that this is a foregone conclusion; we are just pointing out that it is a more than plausible scenario and that we want to ensure the portfolio is ready for whatever the future has in store.

Decades of excessively loose monetary policy and irresponsible fiscal spending, turbocharged by COVID-19, have created the preconditions for a period of higher prices. In addition, deglobalization, geopolitical tensions, dysfunctional political systems, populism, deteriorating demographics, wage pressures, and a looming national debt crisis could all conspire to fan the inflationary flames / stoke the inflationary embers. Conversely, we fully recognize that technological advances will help boost productivity and could offset many of these burgeoning inflationary pressures. While we are hopeful, we aren't completely convinced that these productivity gains will be enough. Time will tell.

We recommend watching this interview with Jonathan Ruffer, the founder of the eponymous asset management firm (**link here**). Ruffer LLP is a unique investment house that provides an unconventional and uncorrelated strategy in a world dominated by conformity. In the interview, Jonathan paints a rather dreary picture of the long road ahead. Granted, their investment strategy is constructed to weather and ultimately profit handsomely during times of extreme duress. While we don't agree with all their assumptions and expectations, we respect their approach and plan to increase our investment with them as time goes on.

Swiss Cheese School of Investing: In the event that Ruffer is 100% correct, the Fort Street portfolio should be able to survive and thrive. We liken our investment approach to adding layers of Swiss cheese, one on top of another, to help minimize risk.



Fun Fact: Why Does Swiss Cheese Have Holes?

In 1917, William Clark published a detailed explanation of how Swiss cheese holes were caused by carbon dioxide released by bacteria present in the milk. Clark's idea was accepted as fact for almost 100 years — until a 2015 study by Agroscope, a Swiss agricultural institute, blew a hole right through his theory (pun definitely intended).

The eyes are actually caused by tiny bits of hay present in the milk, according to Agroscope researchers. This theory explains why the holes have mysteriously become smaller — and sometimes nonexistent — in recent years. When cheese is made in barns using open buckets, it's likely that hay particles will find their way into the collected milk. It's those little bits of hay that cause a weakness in the structure of the curd, allowing gas to form and create the holes.

"It's the disappearance of the traditional bucket" used during milking that caused the difference, said Agroscope spokesman Regis Nyffeler, adding that bits of hay fell into it and then eventually caused the holes. Milk for cheese-making is now usually extracted using modern methods, which explains why we don't see nearly as many holes in our Swiss any more.

COMMODITIES

While we are bullish on commodities in general as a hedge against inflation and for their underappreciated role during the transition to renewable energy, we also fully recognize that they are cyclical assets whose prices are prone to the invariable vagaries of supply and demand. Supply tends to have a way of increasing when demand spikes. It's often just a question of time. However, we suspect that the run-up in commodities will be more than a fling, lasting longer than investors expect or are accustomed to. We subscribe to the notion that macroeconomic and structural changes could see a sustained period of outperformance, akin to the 1970s. Exxon's market cap just overtook Tesla. A harbinger?

Fossil-fuel Consumption: While the fossil-fuel percentage share has declined, the absolute amount of fossil energy consumption rose by approximately one-fifth over the last 12 years. For all of the emphasis on renewable energy and electric vehicles—there is no escaping the utility and ubiquitousness of petroleum, petrochemicals, and other non-renewable energy forms, such as natural gas and coal. Meanwhile, governments continue to throw gobs of money into EV subsidies. As Ronald Reagan said, the nine most terrifying words in the English language are: "I'm with the government, and I'm here to help."

Outlook for Oil: Our sense is that today's prices more than fully reflect the current conflict in the Middle East. If political tensions and the threat of a supply disruption dissipate, oil prices are likely to ease. Additionally, the US presidential election and Saudi Arabia's spare capacity may put further pressure on oil prices.

Biden needs the economy to stay strong if he hopes to be reelected. High oil prices could dampen growth while hitting voters right in their wallets. Elections are often won or lost on the state of the economy. We expect to see the Biden administration continue to release more barrels from the Strategic Petroleum Reserves (SPR).

Furthermore, the current administration is frantically trying to secure the normalization of relations between Saudi Arabia and Israel. Such a deal would usher in a new security pact, the prospect for Palestinian statehood, and a slew of economic agreements; it would also conveniently translate to a higher chance that Saudi spare capacity would be brought back sooner than later. Everyone wins except for those speculating on a further spike in oil prices. As intimated above, Fort Street's investment in oil is not tied to politics but to longer-term supply/demand considerations.

Nuclear Energy Update: The US could be on the cusp of a nuclear renaissance. The federal government will provide a $1.5 billion loan to restart a nuclear power plant in Covert, Michigan, following support from the state of Michigan and the Biden administration. It would be the first nuclear power plant to be reopened in the U.S. However, it still needs to obtain the blessing of the US Nuclear Regulatory Commission (NRC), which is anything but guaranteed. It's instructive to note that President Biden, California Governor Newsom, and Michigan Governor Whitmer are throwing their political weight behind nuclear as part of their energy transition strategies. Perhaps this is a testament to the utter unworkability and unpopularity of a renewables-only approach.

Palisades Nuclear Power Plant in Michigan – restart your engines?

GOLD – SHINING BRIGHTER

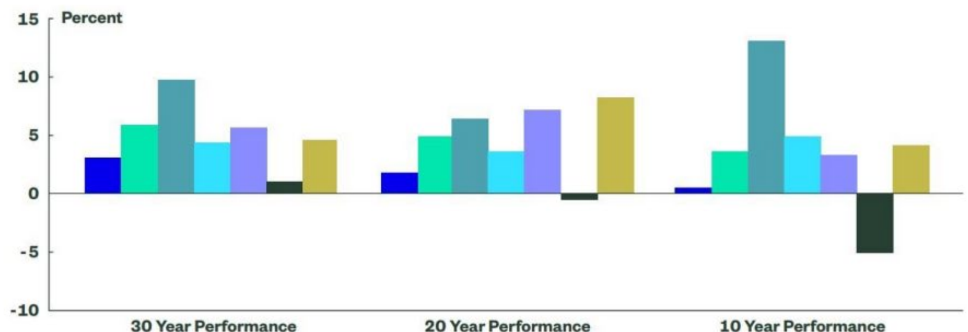
The argument for owning gold has become more compelling. At Fort Street, we are neither gold bugs nor doomsayers, but we have held an average 5% position since our inception and will probably add more going forward.

Misconceptions about Performance: Gold has actually performed significantly better than popular belief. From 1971 to today, the dollar gold price has returned 7.98% annually (see Figure 1). Yes, gold massively underperformed over the last 100 years, but that is simply because it was pegged at $35 before Nixon took the US off the gold standard in 1971.

Gold tends to get a bad rap, which we think is mostly unjustified. Admittedly, it is an unproductive asset that generates no income and, by default, is hard to value using conventional metrics. However, gold has played an essential part in our economies for thousands of years, a track record unrivaled by just about every other asset.

Figure 1
Long-Term Asset Performance

- US Cash
- US Bonds Agg.
- US Stocks
- EAFE Stocks
- EM Stocks
- Commodities
- Gold

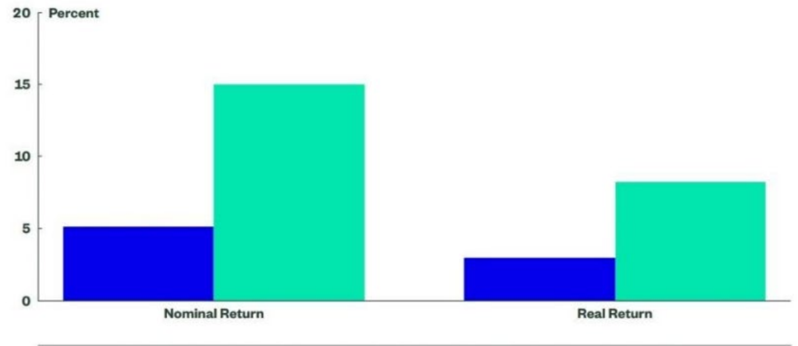


Source: Bloomberg Financial L.P. and State Street Global Advisors, date as of September 30, 2019.[5]

Inflation Hedge: Gold has shown its greatest effectiveness in preserving purchasing power when price inflation runs above 3% a year. During such times, the price of gold has increased by an average annual rate of 15.05%.

Figure 7
ious
Inflation Scenarios

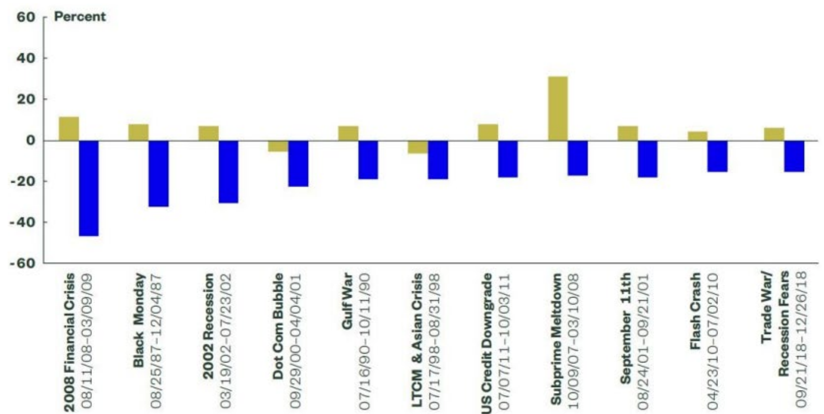
Low inflation (<3%)
High inflation (>3%)



Capital Preservation: Uncorrelated to stocks and bonds, gold is an effective way to preserve capital and limit portfolio drawdowns to capital during market dislocations. As a safe haven in times of crisis, Gold has a track record of holding its value or even rising when many other assets are falling. Based on Figure 2, gold was up 7.2% when the S&P 500 fell 23.5%. It would be even higher if this chart included the last few years.

Figure 2
Gold Performance in US Equity Drawdowns ≥ 15%

Gold Price Return
S&P 500 Total Return



Fiat Currency Risk: While fiat currencies have helped facilitate the biggest economic expansion in history, they are neither bulletproof nor irreplaceable. Just about anything can qualify as a means of exchange and a store of value. Personally, I'd argue for mint chip ice cream. All kidding aside, this is partly why we shouldn't reflexively dismiss the concept of cryptocurrencies. And why we have recently invested in Room40 Capital.

Many of us were either too young or not yet born when Nixon took the US off the gold standard in the summer of 1971. I'm sure a few of you out there remember the exact day (August 15). I was seven and blissfully unaware. My point is that the vast majority of us have become accustomed to our paper money being backed by the credit of the US government. What happens if that credit falters? I'm not saying that will happen; I'm just asking the question.

Rising Demand: Demand for gold is likely to increase in an increasingly bifurcated and unstable political world. China and Russian central banks have dominated fund flows over the last year or so, sending the price of gold to an all-time high of $2,315. As a percentage of individual savings in the US, gold accounts for approximately 0.5%. The forty-year average is 2%. A reversion to the mean would quadruple demand.

IN CONCLUSION

On a lighter note, here are the top 5 regrets of the dying from a book I recently read with the same title. Ok, I think I need to get out more. Nothing like a dose of reality to keep things in perspective and remind us to take the good wherever and whenever we can find it.

1. I wish I'd had the courage to live a life true to myself, not the life others expected of me
2. I wish I hadn't worked so hard
3. I wish I'd had the courage to express my feelings
4. I wish I had stayed in touch with my friends
5. I wish I had let myself be happier

I think I would add a few of the following to my list:

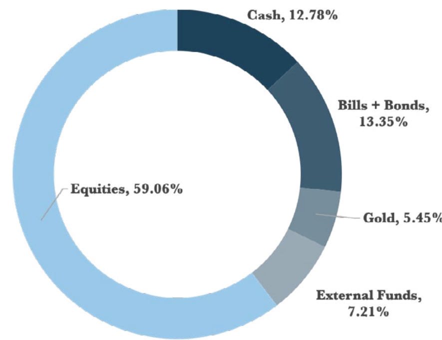
- I wish I stayed more active and healthy, exercising my body and mind.
- I wish I surfed more often – this one is debatable.
- I wish I listened to more live music and went dancing more often.
- I wish I had traveled more, learned more languages, and met more fun and interesting people.
- I wish I gave more money to those nice people at Fort Street Asset Management.
- I wish I was more present and spent less time worrying about small and inconsequential stuff.

	April 23	May 23	June 23	July 23	Aug 23	Sep 23	Oct 23	Nov 23	Dec 23	Jan 24	Feb 24	Mar 24	YTD
FSAM **net of fees*	**1.27%**	**-1.23%**	**3.26%**	**2.97%**	**-1.26%**	**-1.97%**	**-1.52%**	**4.95%**	**2.65%**	**0.71%**	**0.54%**	**3.50%**	**4.67%**
S&P 500	1.46%	0.25%	6.47%	3.11%	-1.77%	-4.87%	-2.19%	8.92%	4.42%	1.58%	5.17%	3.10%	10.16%
60/40 Blend	0.77%	-1.29%	3.44%	2.62%	-1.47%	-3.14%	-1.95%	5.66%	4.17%	0.00%	2.68%	2.37%	5.11%

TOP 10 HOLDINGS

Securities	% NAV	Sub-sector
Cameco	3.92%	Uranium Mining
Google	3.23%	Internet Media
Vanguard Energy ETF	2.87%	Oil & Gas
Constellation Software	2.61%	Software
Microsoft	2.60%	Software
Freeport-McMoRan	2.29%	Base Metals
Lockheed Martin	2.10%	Defense
Berkshire Hathaway	1.93%	Semiconductors
Schlumberger	1.91%	Oil and Gas
Total	25.48%	

ASSET ALLOCATION



SECTOR BREAKDOWN

Equities	% NAV
Market ETFs	2.51%
Technology	9.60%
Financial Services	4.61%
Consumer Discr.	4.32%
Consumer Staples	3.96%
Industrials	4.81%
Healthcare	2.95%
Communication	2.85%
Materials	3.37%
Energy	20.08%
Total	59.06%

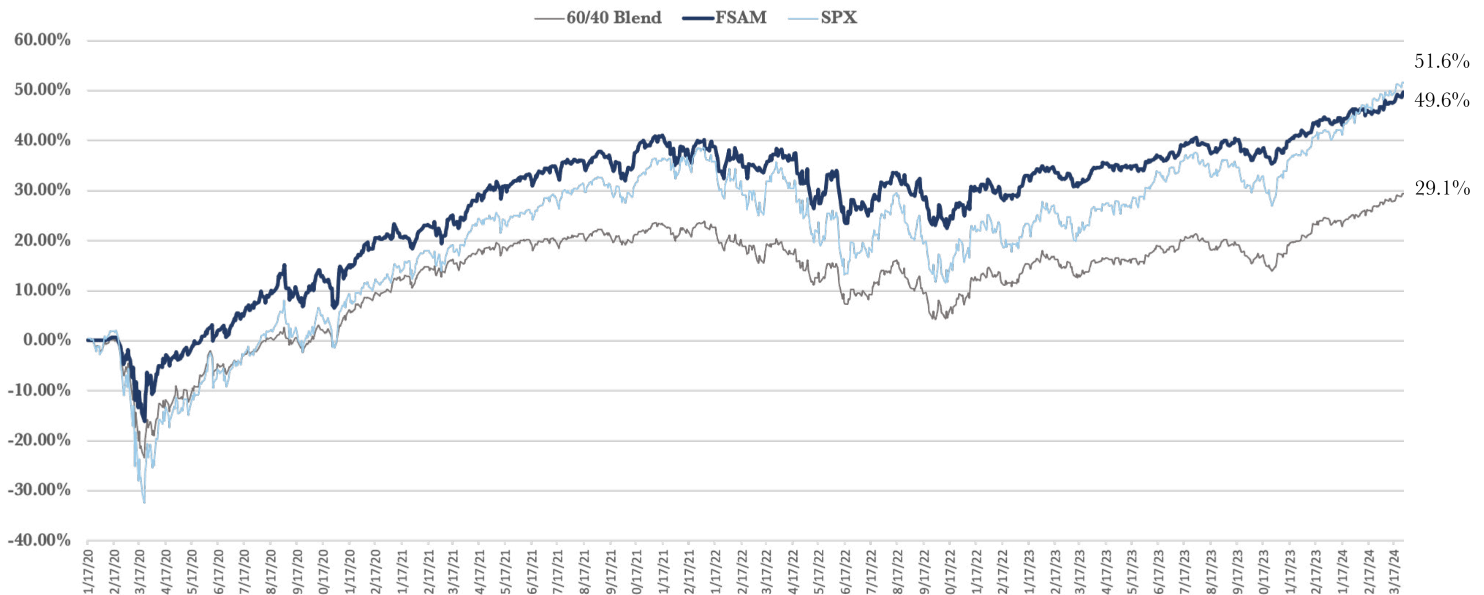
PERFORMANCE OF CORE PORTFOLIO

*Started core portfolio at Morgan Stanley in 2016

	2016	2017	2018	2019	2020	2021	2022	2023	Cumulative	Annualized **as of 3/29/24*
FSAM	**8.7%**	**29.0%**	**-7.4%**	**36.1%**	**22.5%**	**20.4%**	**-10.8%**	**13.4%**	**113.0%**	**14.1%**
S&P 500	9.5%	19.4%	-6.2%	28.8%	16.3%	27.0%	-19.4%	24.2%	102.1%	12.7%
60/40 Blend	5.7%	12.1%	-4.8%	19.5%	11.6%	14.8%	-12.1%	13.3%	61.4%	7.6%

PERFORMANCE SINCE FSAM FUND INCEPTION

*Launched FSAM fund in 2020



DISCLOSURES

Fort Street Asset Management, LLC ("FSAM") is a Registered Investment Advisor ("RIA") registered with the State of Hawaii. Registration as an investment adviser does not imply a certain level of skill or training, and the content of this communication has not been approved or verified by the United States Securities and Exchange Commission or by any state securities authority. FSAM renders individualized responses to persons in a particular state only after complying with the state's regulatory requirements, or pursuant to an applicable state exemption or exclusion. The information contained in this brochure is intended to provide general information about FSAM and its services. It is not intended to offer investment advice. Investment advice will only be given after a client engages our services by executing the appropriate investment services agreement and shall be subject to the terms and conditions therein.

Information regarding investment products and services are provided solely to read about our investment philosophy, our strategies and to be able to contact us for further information. You should not rely on any information provided on our web site in making investment decisions. Market data, articles and other content in this brochure are based on generally available information and are believed to be reliable. FSAM does not guarantee the accuracy of the information contained in this brochure. The information is of a general nature and should not be construed as investment advice and relied upon in making investment decisions. FSAM will provide all prospective clients with a copy of our current Form ADV, Part 2A (Disclosure Brochure) prior to commencing an advisory relationship. However, at any time, you can view our current Form ADV, Part 2A on our web site. In addition, you can contact us to request a hard copy.

Fort Street
ASSET MANAGEMENT