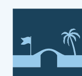
Quarterly Update

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

REVIEW

As the world turns: I'm sure we have all been preoccupied with the cascade of national news in the last few weeks. Our take is that while these events are not trivial, there is no cause for alarm, and we don't see much of an impact on the economy or the portfolio at this stage. Of course, that could always change. We continue to monitor China's economic slowdown and its effect on the global economy, as well as the ongoing geopolitical tensions in Eastern Europe, the South China Sea, and the Middle East. All the more reason to maintain a well-diversified and resilient portfolio.

Performance: This year has been a mixed bag for us. The portfolio is up 6.7%, which is not too shabby, given that we manage a more restrained portfolio. While we own several large tech stocks, including Nvidia, we did not have enough to keep pace with the S&P 500. However, we continued to outperform the classically diversified 60/40 stock and bond portfolio, which is arguably a more appropriate benchmark for our conservative strategy.

Most investors who didn't load up the truck with mega-cap technology stocks such as Nvidia, Microsoft, Google, Meta, and Amazon have struggled to keep pace with the S&P 500. The bulk of the market's performance this year has been concentrated in just a handful of these mega-cap tech stocks. To be fair, other pockets of the market have done well, but their overall impact on the S&P 500 has not been enough to move the needle.

Mea Culpa: The one thing we clearly got wrong was our big bet on commodities (23%) at the expense of technology stocks (11%), which has weighed on the portfolio this year. While we remain confident in our long-term view that many commodity prices are likely to trend higher over the next few years, we recognize that our exposure to such a small and volatile segment of the market was simply too big and are actively taking steps to rebalance the portfolio.

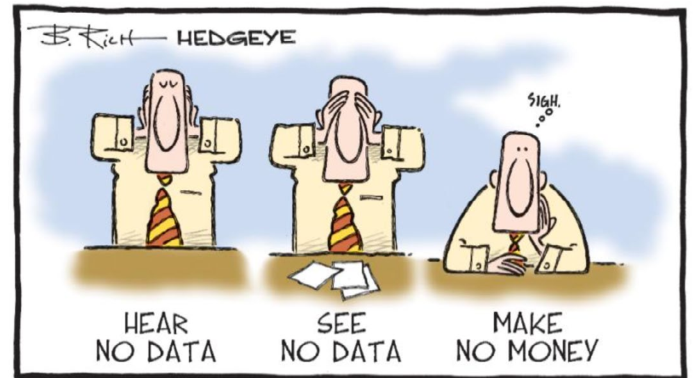
Lemmings: Just in case anyone was wondering, we aren't lemmings. Our equity portfolio does not seek to simply mirror the index. We manage an active strategy that aims to generate a compelling rate of return, albeit one that is more focused on defense and not hitting home runs. In a transitional world, we are careful not to make large one-way bets that could hurt our ability to protect assets or load the portfolio with too much risk. At the end of the day, appropriately sizing positions in line with investment objectives is arguably the most effective way to manage risk. Of course, markets can be fickle, so it's important to maintain a proper degree of balance. What doesn't perform well today might make us look like superstars tomorrow, and vice versa.

North Star: Our North Star is preserving capital while generating compelling risk-adjusted returns. To this end, we continue to deliver as intended. When the market was down 4% in April, the Fort Street Fund only fell 1%. Our strategy of outperforming on the way down not only protects capital but also allows us to acquire positions we favor at lower prices, thereby enhancing our long-term performance.

Fort Street
ASSET MANAGEMENT

OUTLOOK

We are still relatively sanguine on equities, even after such a big move in the first half of this year. Could we see a pullback? Absolutely. Markets, on average, experience a 10% correction every 12-18 months. Tick-tock. Regardless, we suspect this bull has more room to run. We would just highlight that our views and investment decisions are based on hard data – we don't try to divine the future to determine when the markets go up or down.



Fort Street's Secret Weapon: As highly sophisticated investors, we employ some of the most cutting-edge technologies to help us manage the portfolio and stay ahead of the markets and the competition. (see Exhibit A). The truth is that this highly sophisticated market-predicting tool sat on my late father's desk in his Wall Street brokerage firm more than 60 years ago.

EXHIBIT A

Economy and Earnings: The economy is finally showing signs of slowing, but it does not appear to be breaking down. Thanks to higher rates and somewhat tighter financial conditions, inflationary pressures have continued to dissipate, which should allow the Fed to start making modest rate cuts this year. Despite an overwhelming number of predictions from an army of market pundits, ranging from apocalyptic to utopic, many companies are still guiding for decent growth, forcing Wall Street analysts to revise up their earnings forecast. Rising estimates are usually supportive of higher stock prices. Many investors wonder why big tech stocks have gone up so much this year. While the so-called Magnificent Seven constitute 30% of the index, they have accounted for a whopping 89% of the S&P 500's earnings growth this year.

Statistics: While we certainly wouldn't go out and bet the farm on the following statistics, they can provide some insight into what may come next.

1.) Re-Election Years: Equity markets have done well in every Presidential re-election year since 1944. Why? Self-preservation. Presidential incumbents will do everything they can to be re-elected, which is why we have seen a slew of policy initiatives (Inflation Reduction Act, Chips Act, Advance Act, Student loan extensions) intended to spur economic growth. Allegedly, elections are won on the state of the economy. Yes, this year is different, but we'd say regardless of who is running, it still qualifies as a re-election.

2.) Newton's First Law—An Object in Motion, Stays in Motion: Based on historical data, a strong first half usually leads to a continuation of the bull market in the second half of the year with an average of +7.5%, approximately 79% of the time.

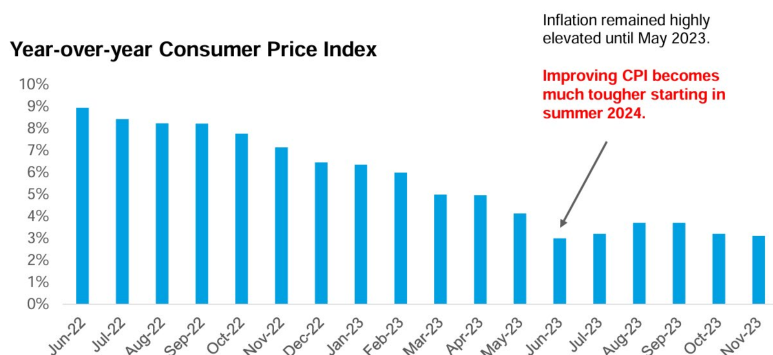
3.) Investor Positioning: Even though we are now well into a bull market, the data suggests that many investors are still sitting on the sidelines with oodles of cash. As long as the economy or the market does not fall off a cliff, there is a good chance that money flows will eventually make their way back into stocks. The slide below suggests that investor sentiment has yet to reach the euphoric levels that typically accompany a bubble. Anecdotally, I'm still hearing many investors say, "I still have plenty of money that I'd like to invest, but I'm waiting for a correction".

(As of June 2024)

Valuations: At 21x twelve-month forward earnings, the broader market is certainly not cheap when compared to historical 5 and 10-year averages of 19x and 17x, respectively. However, excluding high-priced mega-cap tech stocks, the market looks much more reasonably priced, especially as earnings are likely to be revised up.

RISKS

Inflation: Inflation could be stickier than expected, especially as year-on-year comparisons start to become more difficult. While price pressures seem likely to continue to ease for now, we remain concerned about the potential for renewed inflation volatility in the future.



Election and Geopolitics: There is no denying that the political situation in the US and around the world is a lot more precarious and unstable these days. Have the odds of more violence domestically or a larger war externally increased? Sadly, yes. And as such, it makes sense to take precautions against these possibilities. However, it's also important to make the distinction between events that cause greater alarm or fear and those that could actually have a material impact

on the US or global economy. We do not see the US election, thus far, triggering an event that would substantially alter the course of the economy. At least not in today's news cycle. At the end of the day, we suggest investors do not base their investment decisions on politics alone. It seems anytime we make a bet that is contingent on a political outcome, we lose money. Exhibit A: JetBlue's bid to buy Spirit Air.

We would also add that the sad fact is that Trump or whoever replaces Biden will continue policies that further stimulate the economy, further exacerbating our precarious fiscal situation. None of the potential candidates has the understanding, interest, or moral fortitude to try to defuse the ticking time bomb that is our national debt, which ultimately threatens our economic stability.

China and Taiwan Update: As we have pointed out over the last few years, China will struggle to find its economic footing as long as President Xi remains in power. His primary focus is not on fostering economic growth but on consolidating his and the CCP's hold on power, as well as taking a more aggressive foreign policy posture as that plays best to his domestic audience.

If Trump is elected, his talk of imposing tariffs of 60% or higher could set off a dangerous chain of events if such actions are perceived to severely threaten China's already slowing economic vitality. To further unsettle the apple cart, Trump recently suggested that Taiwan pay the US for protection. Any question of our commitment to Taiwan could further entice China to take some sort of military action against the island formerly known as Formosa. Without clear US support, could the Taiwan government or its people decide to take their chances with China? Unlikely, but the odds will rise the more the US shows signs of stepping away.

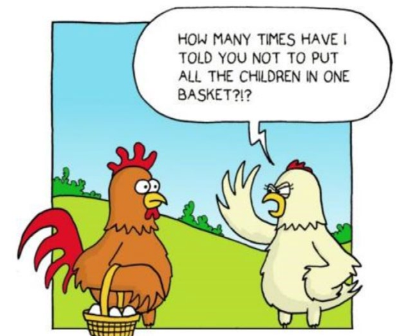
Despite the risks of war in the Taiwan straits, we remain skeptical that China will launch a full-scale invasion for several reasons. First, the odds of success are not high as China would probably struggle to overcome Taiwan's inherent defensive advantages. History suggests that such an undertaking is more likely to fail than succeed. Second, even assuming that China was able to invade and win, the task of governing would be extremely complex, especially if Taiwan's populace did not submit peacefully. Third, sitting at the epicenter of semiconductor manufacturing, it's hard to imagine any scenario where the US and the West would not sit idly by as China tried to take over Taiwan by force.

Oddly enough, Taiwan's economy is doing well despite the risks of a confrontation with China. The island has benefited from its critical position in the technology supply chain and Taiwanese bringing capital back from China as relations deteriorated over the last few years. The Taiwan stock market has been one of the best performing in the last year or two. Whether this has any bearing on the future of Taiwan is hard to say. For Fort Street, most of our exposure to Taiwan is via Taiwan Semiconductor. As circumstances change, we would not be opposed to adding to our Taiwan exposure.

Yield Curve: A few years ago, you couldn't open a financial news site without seeing a headline warning that the yield curve was inverted (short-term bonds are higher than long-term bonds) and, therefore, a recession was nigh. Fast-forward to today, and there isn't even a whisper about the yield curve, even though it remains inverted. We are not suggesting that an economic downturn is near; just that it pays to be aware when the curve un-inverts with short-term rates falling, for that does tend to signal a material slowdown in economic activity.

Volatility or the lack thereof: Despite a slew of forecasts that this would be a volatile year for equity markets, the truth has been the opposite. This year, the VIX (volatility or fear gauge) has averaged 13.7 (the five-year average is 21), while the maximum drawdown for the S&P 500 was 5.5%. Historically, the S&P 500 has experienced larger corrections (14.7% on average) the year following a year of low volatility. We are not predicting that the bull market will end in 2025; just pointing out the potential challenges ahead.

Portfolio Diversification - Eggs and Baskets: It's easy to look at today's equity market and conclude that it's all a big bubble and that a nasty fall is right around the corner. Indeed, that is certainly a possibility that we wouldn't deny. Again, we are neither sorcerers, witch doctors, nor economists, so we try to avoid making predictions on when the market will fall or rise or who will win the World Series (the Mets, obviously). Keeping an open mind, we prefer not to put all our eggs in one basket and take a more nuanced approach that allows us to position the portfolio for a range of possibilities, striking a balance between risk and reward. We just wish we had more of those tasty Nvidia eggs.



Nuclear Energy and The Advance Act: We remain optimistic about the potential for nuclear energy and what that means for uranium miners. The smoke signals coming from Washington and various climate groups looks encouraging.

President Biden has signed the ADVANCE Act to address long-standing flaws in nuclear energy regulation. The International Energy Agency notes that to reach net zero, global nuclear capacity must double by 2050. However, building new nuclear plants in the U.S. is costly, slow, and burdened by bureaucracy, leading to industry stagnation and a projected decline in nuclear-generated electricity from 18% to 12% by 2050.

The ADVANCE Act aims to reverse this trend by reforming the Nuclear Regulatory Commission. It would allow the commission to hire more staff, reduce licensing fees, expedite application processing, and simplify environmental reviews. The act also shifts the commission's mission to consider the public benefits of nuclear energy, not just potential threats.

Together with tax credits from the Inflation Reduction Act, this sets the stage for significant progress. While nuclear energy alone won't solve the climate crisis, it is essential. The act's bipartisan support, building on provisions from the Trump administration, signals a positive shift. The U.S. is finally addressing regulatory obstacles that have hindered new developments, marking a hopeful change. The portfolio still owns CCJ and NXE.

AI: As a general rule, we don't like to bet against technology. As we witnessed during the Covid pandemic, new technologies allowed vaccines to be developed in real-time. While the markets may be overstating AI's importance in the near term, it is probably underestimating its significance in the long term, which is not unusual for new technologies. Is AI overhyped and misunderstood today? Probably. While narrow generative AI for basic consumer tasks may be overblown, the application of AI in areas like energy, manufacturing, and medicine will have a profound impact over time. For a thought-provoking and optimistic view on AI, we've attached a link (click here) to Ray Kurzweil's recent article in The Economist. Subscription required.

Nvidia: Okay, so should we buy more Nvidia? Probably, but maybe size the position to account for current valuations and how much the company has to grow to justify current prices. The data suggests that Nvidia has a significant lead over its competitors and that capital expenditures for the AI buildout do not seem to be slowing down. Will there be significant drawdowns along the way? For sure. Our hope is that we have the cash and presence of mind to seize upon such opportunities.

Pink Elephants: Don't think about pink elephants. Whatever you do, don't think about a pink elephant. Don't picture it in your mind. Just don't do it. Now, what are you thinking about? The pink elephant paradox is a psychological phenomenon that describes how trying to suppress a thought can actually make it more likely to surface, which can negatively impact a person's emotions, focus, and decision-making abilities. (this summary brought to you by AI)

Because I like to torture my body, I've recently taken to running up and down the stairs at Koko Head Crater. It's 1,048 steps up, or just over 1,000 feet of elevation gain, and reaches an incline of 35 degrees or 70%. Halfway up, there is a bridge section that stretches over a ravine with nothing underneath. Falling between the cracks is bad. When traversing this section, I try to expunge my thoughts of pink elephants, saying to myself that all I see are wooden railway ties. It kind of works. Okay, but how does this relate to investing in the markets? To be honest, I'm not entirely sure. I was kind of smitten with the concept and just felt like sharing it. I was intrigued by how we often self-sabotage, limiting our ability for more healthy, rational thoughts. For investing, instead of seeing all the possibilities (good or bad), we become fixated on a pink elephant at the exclusion of other opportunities or risks.

What pink elephant?

CONCLUSIONS

- While the market's current infatuation with AI may prove fleeting, the longer-term implications could be revolutionary.
- Don't think of pink elephants. Allow your mind to stay open to all the possibilities, good or bad.
- Stay focused on the hard facts and figures, and don't try to predict the future.
- Be prepared for the unexpected. Be open to adjusting course as circumstances change.
- Don't let political events alone guide investment decisions.
- Ego is the enemy. Accept that we all make mistakes, and don't let our ego stop us from changing our views and course of action as and when necessary.
- Five out of six dentists recommend investing with Fort Street. That's a fact. Ok, not exactly a fact, but my dentist, Dr. Armand Chong, agrees.
- Sector and Stock exposure: Be careful not to let your convictions outweigh your risk profile.
- Don't panic! Recognize that the world can be volatile and sometimes violent. Everything usually works out, and in the event that it doesn't, then accept it and keep moving. Better times ahead.

https://www.airbnb.com/trips/v1/reservation-details/ro/RESERVATION2_CHECKIN/JEFKD3

Fort Street Asset Management **Q2 Update**

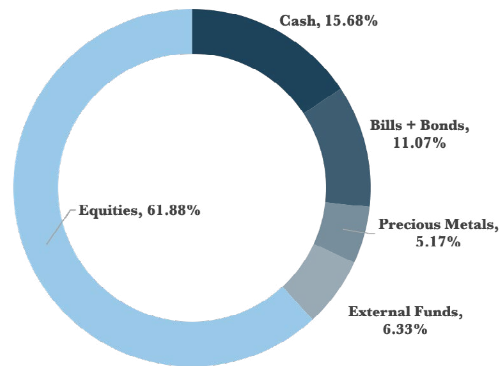
Fort Street
ASSET MANAGEMENT

	July 23	Aug 23	Sep 23	Oct 23	Nov 23	Dec 23	Jan 24	Feb 24	Mar 24	Apr 24	May 24	June 24	YTD
FSAM **net of fees*	**2.97%**	**-1.26%**	**-1.97%**	**-1.52%**	**4.95%**	**2.65%**	**0.71%**	**0.54%**	**3.50%**	**-1.17%**	**3.87%**	**-0.69%**	**6.86%**
S&P 500	3.11%	-1.77%	-4.87%	-2.19%	8.92%	4.42%	1.58%	5.17%	3.10%	-4.16%	4.80%	3.47%	14.48%
60/40 Blend	2.62%	-1.47%	-3.14%	-1.95%	5.66%	4.17%	0.00%	2.68%	2.37%	-2.46%	3.15%	0.05%	5.81%

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

Market ETFs	2.88%
Technology	9.79%
Financial Services	5.93%
Consumer Discr.	4.17%
Consumer Staples	3.38%
Industrials	8.17%
Healthcare	2.59%
Communication	2.96%
Materials	3.24%
Energy	19.77%
Total	61.88%

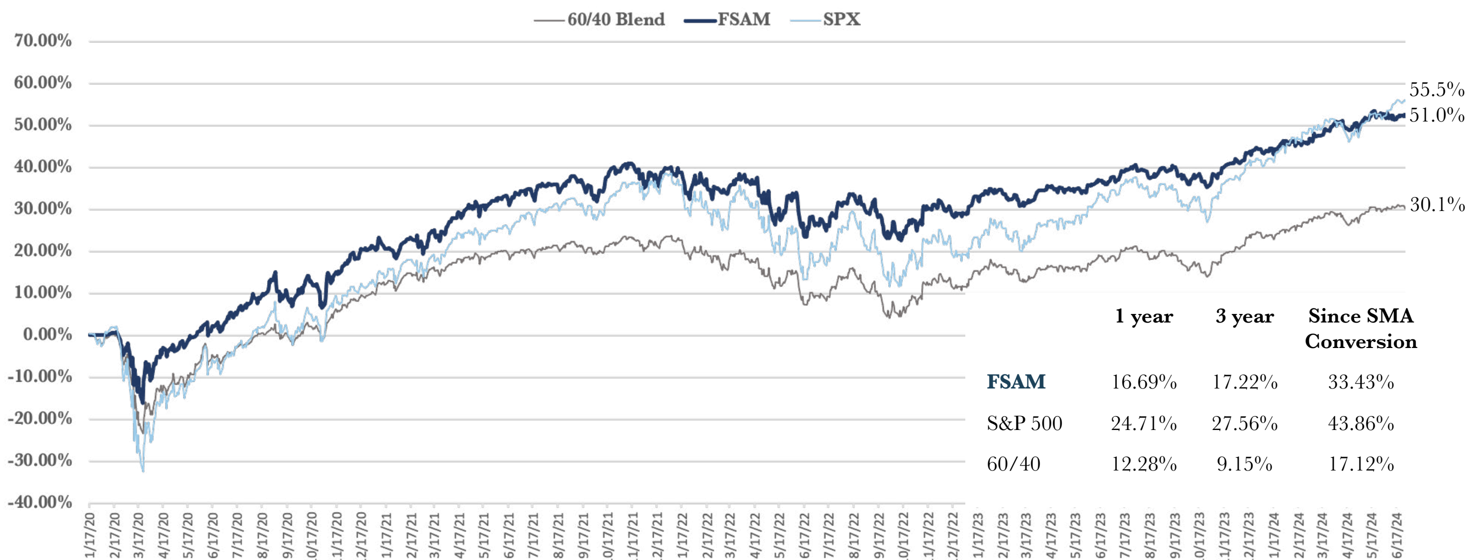
PERFORMANCE OF CORE PORTFOLIO

*Started core portfolio at Morgan Stanley in 2016

	2016	2017	2018	2019	2020	2021	2022	2023	Cumulative	Annualized **as of 6/30/24*
FSAM	**8.7%**	**29.0%**	**-7.4%**	**36.1%**	**22.5%**	**20.4%**	**-10.8%**	**13.4%**	**113.9%**	**13.6%**
S&P 500	9.5%	19.4%	-6.2%	28.8%	16.3%	27.0%	-19.4%	24.2%	103.2%	12.5%
60/40 Blend	5.7%	12.1%	-4.8%	19.5%	11.6%	14.8%	-12.1%	13.3%	61.6%	7.4%

PERFORMANCE SINCE FSAM INCEPTION

*Launched FSAM fund in 2020



	1 year	3 year	Since SMA Conversion
FSAM	16.69%	17.22%	33.43%
S&P 500	24.71%	27.56%	43.86%
60/40	12.28%	9.15%	17.12%

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