December 2022 Newsletter: Head Up, Eyes Open

- Running Oak's Efficient Growth portfolio was up **5.65%** for the month of November, gross of fees, versus 5.59% for the S&P 500 Total Return Index (5.61% net)*
- Efficient Growth has **outperformed** the S&P 500 Total Return Index by **6.72%** over the last 12 months, gross of fees (6.24% net)*
- As of September, Efficient Growth had performed in the **top 2%** of Large Core managers over the last **10 years**, net of fees. (109 months audited, 11 months real-time but unaudited)*
- Efficient Growth performed in the **top 2%** of its peers over the last 10 years and **outperformed** the S&P 500 Total Return index by **0.81%** since Running Oak's inception in 9/13, annualized and gross of fees, *despite* arguably the worst environment in history for a strategy focused on discipline, valuations, and risk. How might it perform when in favor, like today and likely the next decade?

Head up, eyes open

My favorite line from the LEGO Batman movie:

Future Robin: My name's Richard Grayson, but the kids at the orphanage call me Dick.
Batman: Well, children can be cruel.

A similar misunderstanding:

Me: Based on history, there is a high likelihood that the S&P 500 doesn't revisit its most recent high for 5 to 10 years.
Response: Wow, you're really bearish.

I am not bearish stocks. In fact, I am actually bullish many stocks. For instance, our Efficient Growth portfolio has a forward PE of 17 and expected earnings growth of 10%; that's cheap, and there are plenty of other cheap stocks out there. I am simply bearish a particular portfolio of stocks, namely the S&P 500.

Let's review the last 14 years: the S&P 500 set a new all-time high of 4,818.62 in December 2021. That high was at least partially due to QE 1, and QE 2, and QE 3, annd QE 4, annnd a massive tax cut and deficit at the peak of an economic cycle during 5-decade low unemployment, annnnd historically low interest rates. Oh, and don't forget the **$1.5 TRILLION** in straight up **CASH** handed out! That historic stimulus helped produce the longest bull market in history, propelled the S&P 500 to a record high, and we will hopefully never see anything like it again.

History Lesson

7 Years: As the US economy battled inflation, the S&P 500 didn't recover its 1973 high until 1980.
7 Years: Following the Tech Bubble in 2000, the S&P 500 didn't make new all-time highs until 2007.
6 Years: Following the Global Financial Crisis, the S&P 500 didn't make new all-time highs until 2013.

Managing Expectations

Markets, like children, can be cruel. Are you and your clients prepared for the possibility of NO growth in passive and Large Cap Growth equity assets for potentially a decade? Will your clients be content paying fees for no growth and strategies they can find in their retail brokerage account? How will your business look with 0 growth in equity assets and displeased clients?

Of course, the above assumes the market is flat. Given the excesses of the last 6 years and the still very lofty valuations of Apple, Microsoft, Nvidia, Tesla, etc, that is likely optimistic.

Don’t Miss Out on Happy Clients and a Thriving Business

From 2000 to 2002, Value, High Quality, and our Efficient Growth portfolio were **UP** when the S&P 500 was down **-38%**.* The run-up of the Tech Bubble is arguably most comparable to the 5-year run from 2017 to 2021 that saw make-believe currencies appreciate to $3.1 Trillion, GameStop explode 100x despite no business model, and Nvidia and Microsoft trade at over 3x and 1.5x the most overvalued companies of the Tech Bubble. If the run-up was similar, the aftermath may be as well, and the magnitude of the Tech Bubble was smaller than that of 2017 to 2021.

Efficient Growth has outperformed the S&P 500 by almost 7%, gross of fees, over the last 12 months and is outperforming by another 1% so far in December.* Based on history and data, this is likely only the beginning. Following 1999, Efficient Growth outperformed in 2000, 2001, 2002, 2004, and 2005.* Following 2007, Efficient Growth outperformed in 2008, 2009, 2010, 2011, 2012, 2013, 2014, and 2015.* The structural inefficiencies set to serve as tailwinds for our portfolio and headwinds for the S&P 500 are far greater now than in 1999 and 2007. You haven't missed the boat; it's just pulling away.

Where will your firm and clients be six years from now, if the future parallels the past? If you take anything away from this email, let it be these 5 numbers:

102%: From 2000 to 2005, Efficient Growth provided **102% more return** than the Russell 1000 Growth, meaning 102% **more assets** at the end of 2005.*

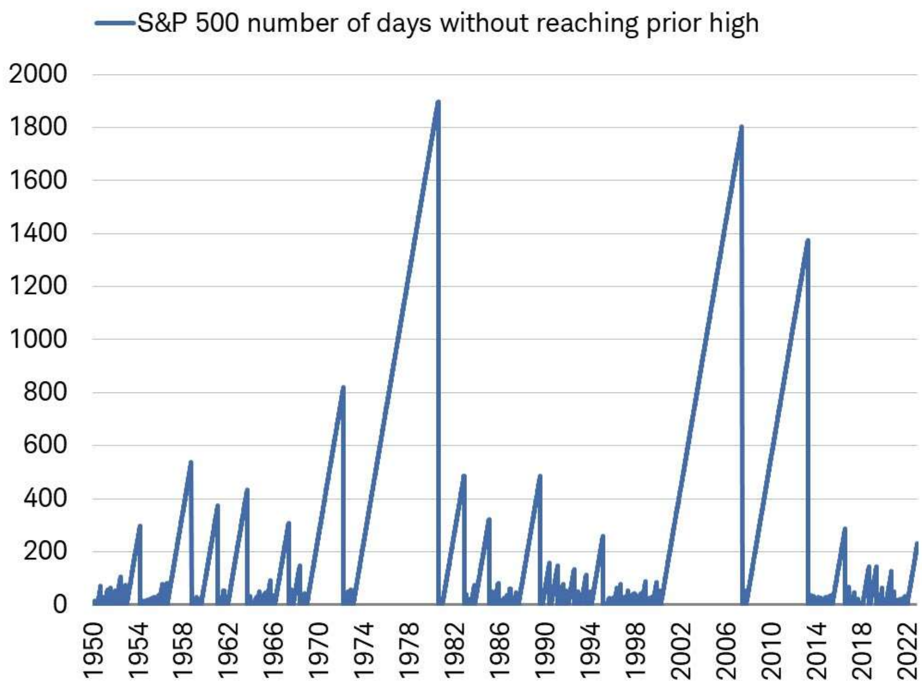
84%: From 2000 to 2005, Efficient Growth provided **84% more return** than the S&P 500 Total Return Index, meaning 84% more assets.*

29%: From 2008 to 2013, Efficient Growth provided **29% more return** than the S&P 500 Total Return Index.*

28%: From 2000 to 2013, Efficient Growth provided **28% more return** than the Russell 1000 Growth.*

7.4%: In just the last 12 months, Efficient Growth investors have **7.4% more in assets** than those invested in the S&P 500 Total Return Index.*

Investing in passive or Large Cap Growth portfolios for the foreseeable future is a heck of a poor gamble, if the past is any indication. While 14 years of an ever-rising market and CNBC pundits may lead you to believe there's nowhere to go from here but up, history says otherwise. (As an aside, I just read a Twitter post, stating that now is the best time to buy index funds since 2009. The S&P was down over 50% at that time and wasn't coming off a bubble top. The S&P is currently down only 17%, and several of its largest holdings *still* make the peak of the Tech Bubble look like a good buy. Numbers...) The only thing noteworthy about the current decline is just how short it has been. The S&P 500 and Large Cap Growth likely have a long, rough road ahead.



Source: Charles Schwab, Bloomberg, as of 12/2/2022. Past performance is no guarantee of future results.

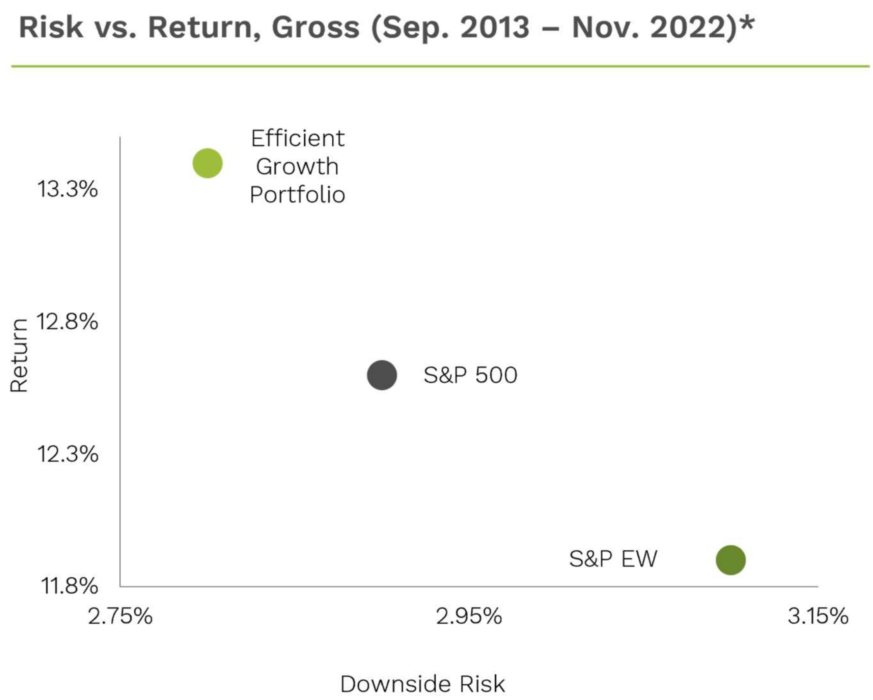
Common Sense

Trust in common sense, not a firm's self-serving narrative. The idea that it's best to invest simply based on the size of a company with zero regard for profitability, valuations, solvency, or risk makes little sense. Would you pay more for a house simply because it is bigger while overlooking the condemned sign? That is how index funds invest. One of the best aspects of our Efficient Growth strategy is simply that it makes sense - no leap of faith required.

1. Above Average Earnings Growth – Because owning a company that is making more and more money is obviously a good thing.
2. Attractive Valuations – Because paying a dumb price is, well, dumb.
3. Lower Downside Risk – Because losing money stinks. Lower drawdowns mean smaller bounces are required to get back to new highs.

With a new year quickly approaching, it's an excellent time to plan for the future. Whether booking losses before year-end or taking gains in January, now is the time to position client portfolios for the next 5 to 10 years. As many investors have recently experienced, it doesn't take much of a fall to wipe out years worth of gains, and it doesn't pay to hold on to good companies at terrible valuations.

Where will you and your clients be 6 years from now? If history repeats itself, will you be yearning for happy clients, more assets, higher revenue, and greater profitability? We won't turn you away 6 years from now, but wouldn't it be better to simply grow together?



If you appreciate critical thinking, math, common sense, and occasional sarcasm, we would love to speak with you. Please feel free to set up a time here: https://m.levitate.ai/25b96d-6d5n9i/30-minute-meeting

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**Past performance is no guarantee of future results. Performance expectations are no guarantee of future results; they reflect educated guesses that may or may not come to fruition.*

Performance of the Efficient Growth strategy has been tracked since 1989. Performance prior to September of 2013, while unaudited, was documented and generated on a real-time (not back-tested) basis. Such results are from accounts managed at other entities prior to the formation of Running Oak Capital. All indices are unmanaged and may not be invested into directly. Comparison described here are made relative to mutual funds included in the Morningstar Large Cap Blend universe, which were used for their availability and relative comprehensiveness of data. Other strategies managed in different vehicle structures may exist that are not represented here.

The S&P 500 Index is a capitalization weighted index of 500 stocks designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

The opinions voiced in this material are for general information only and are not intended to provide specific advice or recommendations for any individual. To determine which investments and strategies may be appropriate for you, consult with us at Running Oak Capital or another trusted investment adviser.

Stock prices and index returns provided by Standard & Poor's.