

QUARTERLY LETTER

By Jeff Muhlenkamp, Portfolio Manager and Ron Muhlenkamp, Founder

Economic activity in the U.S. and around the world continues to be driven by the spread of the COVID-19 virus and reactions to it. We said that in July and it remains true, if perhaps a little too obvious to be worth stating. What is not obvious to us is what factors account for the differences in the severity of the virus in different places, which mitigation measures are effective in coping with the pandemic, and what actions have mattered little to the progression of the disease. No matter how much time we spend researching the subject we remain uncertain that we really understand why the virus is behaving the way it is. Our current assessment is that the virus has largely burned itself out in the U.S. and Europe, is well controlled in Asia, and that extreme lockdown measures did more economic harm than virus-control good. We hold these conclusions lightly and are ready to change them if new evidence or analysis suggest we should.

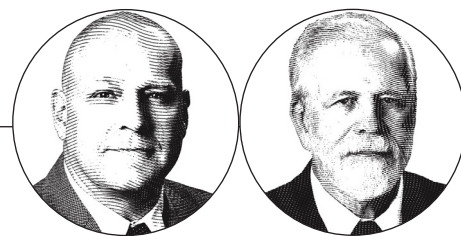
Early in the year the range of responses by governments to the virus was extremely wide: everything from do nothing to restrict everyone to their homes. It is our observation that the range of responses has narrowed a little bit since then, with the most restrictive measures falling out of favor and more moderate or targeted measures being employed in the late summer, early fall.

“Many businesses are surviving on government loans or grants. While we know the extent of the existing assistance, we don’t know if more will become available in the future. So we really don’t have any idea how many businesses will ultimately fail.”

Thus, we believe things are getting better from: the virus is receding and the reactions to the virus are less economically damaging. From an investment point of view there remain two important and interrelated questions that we don’t have answers for yet:

1. How much economic damage was done that we don’t know about yet?
2. Which changes in how we work, play, vacation, educate, eat, etc. will be temporary, and which will prove longer lasting?

With regard to the first question, we still don’t really know how many businesses will never reopen. Government restrictions are quite impactful to many businesses and we don’t know when they’ll end. How long consumer aversion will last is probably unknowable. So whether we look at restaurants, airlines, hairdressers, or other businesses we don’t know how long their revenues will remain depressed. Many businesses



are surviving on government loans or grants. While we know the extent of the existing assistance, we don’t know if more will become available in the future. So we really don’t have any idea how many businesses will ultimately fail. Business failures have a direct impact on unemployment, commercial loans, and commercial real estate values to name just a few things that are top of mind. Loans and real estate are assets, so we don’t know the magnitude of the losses that are coming, or who, exactly, will bear them. It’s our observation that the share prices of bank stocks have gone up very little from their March lows—we’re not surprised. Listening to the big banks during their earnings calls and speaking to smaller bank CEOs on several occasions, it is clear the banks have little idea which of the loans on their books are still good, and which will end up defaulting.

Regarding the second question, there have been some huge changes in the workplace, education, recreation, etc. How many of these changes are permanent? How much business travel never comes back, impacting airlines, hotels, taxis, etc. on a permanent basis? How many workers continue working from home, reducing the demand for office space and putting downward pressure on real estate values? There appears to be a significant movement of people out of cities and into the

continued on page 3

VIEW FROM THE FRONT OFFICE: THE ELECTION



By Tony Muhlenkamp, President

The election is the recurring theme of my conversations with clients these days; usually consisting of two questions: “What is going to happen?” and “What should we do?” The short answers are “I don’t know” and “Don’t panic”.

I think it is useful to flesh that out a little bit.

The two candidates for President of these United States clearly differ in a number of significant ways on several issues: climate change and energy policies, immigration, abortion, COVID, systemic racism, foreign policy, taxes and regulation; etc.

2 There are fewer, but no less important, commonalities between them. They are both receiving the same fiscal and monetary policy advice from the same economists: print more, borrow more, and spend more. This will predictably increase the federal deficits and federal debt. They are both older than any Presidential candidate we have had in the past, making the Vice-Presidential candidates an important consideration in this election. They both seem to be appealing to the more “radical” elements on either end of the political spectrum, and they both seem to generate extreme emotional reactions from both their supporters and their detractors.

For me, it’s important to realize that everyone ALREADY knows this. There are no surprises here. Additionally, we all expect: a close election, continued protests and demonstrations, and that half the country will be unhappy when all the dust settles. Everybody already knows who they are voting for and thinks “the other guy” spells the doom of the Republic and The End of the World as We

Know It (TEOTWAWKI). During the run up to Y2K we saw a similar phenomenon in that everyone knew what was going to happen, when it was going to happen, and took steps to prepare for it. So, it turned out to be a non-event. In this case, we may not know exactly what will happen, but we have a pretty good idea of what to expect from each candidate should he win. In fact, the only surprising outcome would be a landslide victory and a simple, straightforward, uncontested, transition of power. THAT would take everyone by surprise.

“Nothing will change overnight, there will be no immediate catastrophes or instant salvations per se, but instead a long slow grind.”

No matter who is elected, certain geopolitical realities will constrain their actions. (Read George Friedman’s work at Geopolitical Futures and his books for explanations.) Nothing will change overnight, there will be no immediate catastrophes or instant salvations per se, but instead a long slow grind. Whether it’s up or down will depend on your point of view.

So, what will happen? It will be a close and contested election that winds up going to the courts. Protests and counter protests will continue with both ends of the political spectrum instigating and responding. Once the Inauguration is over government spending and borrowing will increase, the Federal Reserve will continue to “print money”, and COVID will infect more people. GDP growth will remain low and

unemployment will remain high until well after we “re-open” the economy because they always do. The stock market will be volatile, driven by emotions in the short term (any given day, week, month, or year) and rational in the long term (3 years or longer). Whether the market trends up or down over time will depend on the mix of policies that result from the election.

So, what should we do? Recognize that much of the rhetoric about the election is hyperbolic and overwrought; DON’T PANIC. Now is a good time to take stock. What are your physical, mental, emotional, and spiritual resources? Since we are financial advisors we like to ask, what are your financial resources? Are your financial dreams and goals still the same? What has changed in terms of your income, spending and savings? How have your investments performed (put a number to it, don’t just say “good”)? How does your plan have to adapt to current conditions, and what assumptions are you making about the future that you DON’T know you’re making? We are asking ourselves these questions, and persisting until we have rational, reasonable answers. If you have a financial plan, dust it off and take a look at it. If you don’t have one, make one. We are here to help review and provide a second opinion on your existing plan or to help you create a new one. Just let us know if you would like our help. We look forward to hearing from you. 📞

The comments made in this article are opinions and are not intended to be investment advice or a forecast of future events.

LETTER

Continued from page 1

suburbs, how long does that continue and what does the total impact look like? How many workers decide to stay home to help the kids with school and how does that affect the work force? We don't know the answers to any of these questions yet and it will take time to start to understand what the long-term effects are. This results in more uncertainty regarding the future of many businesses and industries than we had at the beginning of the year.

So, a lot of uncertainty still around the short-term and long-term impact of the virus, some of which we think is priced into the market, some of which is not.

Also of interest this quarter was the announcement by the Federal Reserve that they would begin targeting average inflation, not "spot" inflation. What does this mean? It means that if inflation has been below their target of 2% for a period of time, which it has, the Federal Reserve will now allow inflation to run above 2% for a period of time before they take action to reduce it. It remains to be seen whether this change in attitude by the Federal Reserve actually matters or not since the Fed has been unable to generate the inflation they sought the last ten years or so. Inflation as measured by the U.S. Consumer Price Index (urban) in August was 1.31%. Interestingly, that rate is almost twice the current yield on the 10-Year U.S. Treasury, which was .66% on 9/29/2020. So the holder of a 10-Year Treasury is losing purchasing power due to inflation at twice the rate he is growing his wealth via receipt of interest. The longer that situation persists, the more the bondholder loses ground, which is why we remain uninterested

in being long-term bondholders and are skeptical of owning companies that have large holdings of long-duration bonds (examples are banks and insurance companies).

The portfolio is tilted towards economic recovery consistent with our view that the economy is improving. Some of our long-term holdings are trading at a premium to our assessment of their value and so we have reduced our position size in those companies. We've put some cash to work and are happy to hold on to the rest until we find attractive opportunities to employ it; we're not in a hurry. We also continue to hold a position in gold, which we view as a hedge.

With our best wishes for your continued success and good health.

P.S. - Jeff here— I just finished reading "Thinking in Bets: Making Smarter Decisions When You Don't Have All the Facts" by Annie Duke. Making decisions without all the facts is essentially my job description and I am always looking for ways to improve. Mrs. Duke does a great job laying out the problem, what she learned as she tried to improve her decision-making process as a professional poker player, and how the rest of us can improve our thinking as well. I highly recommend the book if you have an interest in decision making and will add this one to my recommended reading list. 

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ANNOUNCEMENTS

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We have a collection of webcasts and seminars on our Vimeo Channel located at <https://vimeo.com/muhlenkamp>

One of our latest webcasts is REBUILDING "BUSINESS" FINANCIAL STABILITY AFTER COVID

Don't Miss our Blogs (<https://muhlenkamp.com/blog/>) with topics like:

THE IMPACTS OF COVID-19 ON THE DAILY ROUTINE, AT HOME AND WORK

WHICH RETIREMENT PLAN IS BETTER FOR MY TEAM, A SEP OR SIMPLE IRA?

WHY AN EMERGENCY FUND IS A GOOD IDEA


THE DIFFERENCE BETWEEN A SAVINGS ACCOUNT AND INVESTING

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MUHLENKAMP Memorandum

Inside this issue:

- Quarterly Letter
- View from the Front Office: The Election
- Announcements



COVID has changed the way we live; dealing with the pandemic is the new normal right now. We would love to talk with you about your financial aspirations and needs during this time. At Muhlenkamp making your money grow is our top priority.

MUHLENKAMPSMA ALL-CAP VALUE

For the period ended 09/30/2020

Muhlenkamp & Company's All-Cap Value SMA (Separately Managed Account) is designed for investors' accounts over \$100,000. We employ full discretion, applying fundamental analysis.

INVESTMENT OBJECTIVE

We seek to maximize total after-tax return through capital appreciation, and income from dividends and interest, consistent with reasonable risk.

INVESTMENT STRATEGY

We invest in undervalued assets wherever they may be found. Typically, this results in holding a portfolio of companies we believe are materially undervalued by the market. Bonds may be included in the portfolio if they are a good investment.

INVESTMENT PROCESS

We start with a bottom-up scan of domestic companies, typically looking at most U.S. companies at least four times per year. We add to that an understanding of the sector dynamics in which companies are operating, an assessment of the business cycle, and a review of macroeconomic conditions.

Our primary screening metric is return on shareholder equity (ROE). We are looking for companies with stable returns that can be purchased cheaply, or for companies with improving returns that have not yet been recognized by the market.

We don't believe that a holding period of "forever" is appropriate in all cases, but are comfortable holding companies as long as they continue to meet expectations.

INVESTMENT RISK

We define investment risk as the probability of losing purchasing power over long periods of time, which is quite different from Wall Street's definition of price volatility in very short periods of time. Taxes, inflation, and spending will ALL impact the purchasing power of your assets.

ALL-CAP VALUE COMPOSITE PERFORMANCE (NET OF FEES)

| | Year to Date | One Year | Annualized | | | |
|------------------------|--------------|----------|--------------|--------------|---------------|---------------|
| | | | Past 3 Years | Past 5 Years | Past 10 Years | Past 15 Years |
| Return | -1.02% | 5.11% | 0.65% | 2.42 | 5.66% | 1.65% |
| S&P 500 Total Return* | 5.57% | 15.15% | 12.28% | 14.14% | 13.74% | 9.19% |
| Consumer Price Index** | 1.15% | 1.31% | 1.92% | 1.75% | 1.76% | 1.89% |

* The S&P 500 is a widely recognized, unmanaged index of common stock prices. The figures for the S&P 500 reflect all dividends reinvested but do not reflect any deductions for fees, expenses, or taxes. One cannot invest directly in an index.

** Consumer Price Index (CPI) – As of August 2020 – U.S. CPI Urban Consumers NSA (Non-Seasonally Adjusted), Index. The Consumer Price Index tracks the prices paid by urban consumers for goods and services and is generally accepted as a measure of price inflation. Price inflation affects consumers' purchasing power.

Consolidated performance with dividends and other earnings reinvested. Performance figures reflect the deduction of broker commission expenses and the deduction of investment advisory fees. Such fees are described in Part II of the adviser's Form ADV. The advisory fees and any other expenses incurred in the management of the investment advisory account will reduce the client's return. It should not be assumed that recommendations made in the future will be profitable or will equal the performance of the above accounts. A list of all security recommendations made within the past twelve months is available upon request.

TOP TWENTY HOLDINGS

| Company | Industry | % of Net Asset |
|------------------------------|--|----------------|
| Meritage Homes Corporation | Household Durables | 4.70% |
| Dow Inc. | Chemicals | 4.38% |
| Apple Computer Inc. | Technology Hardware, Storage & Peripherals | 3.97% |
| Microchip Technology Inc. | Semiconductors & Semiconductor Equipment | 3.96% |
| Microsoft Corporation | Software | 3.88% |
| Lennar Corp Class A | Household Durables | 3.87% |
| SPDR Gold Shares | Exchange Traded Funds | 3.84% |
| Broadcom Inc. | Semiconductors & Semiconductor Equipment | 3.56% |
| McKesson Corporation | Health Care Providers & Services | 3.17% |
| UnitedHealth Group Inc. | Health Care Providers & Services | 3.13% |
| Mastec Inc. | Construction & Engineering | 3.00% |
| Berkshire Hathaway Class B | Diversified Financial Services | 2.99% |
| Bristol-Myers Squibb Company | Pharmaceuticals | 2.94% |
| Jazz Pharmaceuticals PLC | Pharmaceuticals | 2.79% |
| Lockheed Martin Corp. | Aerospace & Defense | 2.79% |
| Gilead Sciences, Inc. | Biotechnology | 2.75% |
| CVS Health Corp. | Health Care Providers & Services | 2.62% |
| Cameco Corporation | Oil, Gas, & Consumable Fuels | 2.56% |
| NMI Holdings | Thriffs & Mortgage Finance | 2.45% |
| Alliance Data Systems Corp. | IT Services | 2.18% |

Composite holdings are subject to change and are not recommendations to buy or sell any security.

Composite Top Twenty Holdings are presented as supplemental information to the fully compliant presentation on the next page.

Return on Equity (ROE) is a company's net income (earnings), divided by the owner's equity in the business (book value).



PORTFOLIO MANAGER



Jeffrey P. Muhlenkamp,

Portfolio Manager, CFA, has been active in professional investment management since 2008. He is a graduate of both the United States Military Academy and Chapman University.

INVESTMENT ADVISER

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SMA FACTS

Average Number of Equity Holdings 27
Cash & Cash Equivalents 21.11%

SMA Facts are presented as supplemental information.

SMA INFORMATION

The All-Cap Value Composite was created in December 2003 and includes fee-paying accounts over \$100,000, full discretion, under management for at least one full quarter which are invested in the All-Cap Value strategy. The composite excludes the Muhlenkamp Fund and any wrap fee account.

Minimum Initial Investment \$100,000.00
Management Fee* 1% (first \$1 million);
0.5% on the remainder

* May vary by account.

Muhlenkamp & Company serves individual and institutional investors through our no-load mutual fund and separately managed accounts.

MUHLENKAMP & COMPANY, INC. ALL-CAP VALUE COMPOSITE ANNUAL DISCLOSURE PRESENTATION

| Year End | Total Firm Assets (USD) (millions) | Composite Assets (USD) (millions) | Number of Accounts | ANNUAL PERFORMANCE | | | THREE-YEAR ANNUALIZED STANDARD DEVIATION* S&P 500 | | |
|----------|------------------------------------|-----------------------------------|--------------------|--------------------|---------------|----------------------------|---|------------------------|------|
| | | | | Composite Gross | Composite Net | S&P 500 Total Return Index | Composite Total Return Index | Composite Dispersion** | |
| 2019 | 253 | 34 | 48 | 14.70 | 13.79 | 31.49 | 10.33 | 12.10 | 1.37 |
| 2018 | 254 | 32 | 51 | (11.71) | (12.45) | (4.38) | 9.24 | 10.80 | 1.21 |
| 2017 | 342 | 40 | 52 | 15.24 | 14.30 | 21.83 | 8.70 | 9.92 | 2.12 |
| 2016 | 339 | 39 | 52 | (1.86) | (2.68) | 11.96 | 9.73 | 10.59 | 1.17 |
| 2015 | 422 | 48 | 67 | (4.66) | (5.45) | 1.38 | 10.41 | 10.47 | 0.68 |
| 2014 | 541 | 51 | 67 | 10.27 | 9.37 | 13.69 | 9.55 | 8.97 | 2.06 |
| 2013 | 585 | 50 | 60 | 35.50 | 34.39 | 32.39 | 11.29 | 11.94 | 3.13 |
| 2012 | 491 | 41 | 66 | 11.29 | 10.34 | 16.00 | 12.02 | 15.09 | 1.14 |
| 2011 | 555 | 45 | 74 | (2.84) | (3.67) | 2.11 | 16.60 | 18.70 | 0.85 |
| 2010 | 724 | 59 | 82 | 2.96 | 2.15 | 15.06 | | | 1.45 |
| 2009 | 839 | 90 | 107 | 32.68 | 31.72 | 26.46 | | | 2.80 |
| 2008 | 759 | 112 | 155 | (40.53) | (40.94) | (37.00) | | | 1.97 |
| 2007 | 1886 | 327 | 289 | (7.61) | (8.19) | 5.49 | | | 3.77 |
| 2006 | 3393 | 371 | 337 | 6.09 | 5.34 | 15.79 | | | 3.70 |
| 2005 | 3471 | 287 | 289 | 10.04 | 9.22 | 4.91 | | | 3.38 |

The objective of this All-Cap Value Composite is to maximize total after-tax return, consistent with reasonable risk—using a strategy of investing in highly profitable companies, as measured by Return on Equity (ROE), that sell at value prices, as measured by Price-to-Earnings Ratios (P/E).

Muhlenkamp & Company, Inc. ("Muhlenkamp") claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Muhlenkamp has been independently verified for the periods December 31, 1993 through June 30, 2016 by Ashland Partners & Company LLP and for the periods July 1, 2016 through December 31, 2019 by ACA Performance Services.

Verification assesses whether (1) the firm has complied with all the composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policies and procedures are designed to calculate and present performance in compliance with the GIPS standards. The All-Cap Value Composite has been examined for the periods December 31, 1993 through December 31, 2019. The verification and performance examination reports are available upon request.

Muhlenkamp is an independent registered investment advisory firm registered with the Securities and Exchange Commission. The firm's list of composite descriptions is available upon request.

Returns are based on fully discretionary accounts under management, including those accounts no longer with the firm. Composite may invest in American Depositary Receipts (ADRs).*** Accounts may be shown gross or net of withholding tax on foreign dividends based on the custodian. Past performance is not indicative of future results.

The U.S. dollar is the currency used to express performance. Returns are expressed as percentages and are presented gross and net of management fees and include the reinvestment of all income. Net of fee performance was calculated using actual management fees. The annual Composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the Composite the entire year. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

* **Three-Year Annualized Standard Deviation** is a measure of volatility, calculated by taking the standard deviation of 36 monthly returns, then multiplying the result by the square root of 12 to annualize it. Since standard deviation measures the dispersion of a set of numbers from its mean, higher results indicate more variation in monthly returns over the trailing three years.

** **Composite Dispersion** is a measure of the similarity of returns among accounts in the Composite. It is the standard deviation of the annual returns for all accounts which were in the Composite for the entire year.

*** **American Depositary Receipts (ADRs)** are shares that trade in U.S. markets, but represent shares of a foreign company. A bank (the depository) purchases a number of the foreign shares and holds them in a trust or similar account; in turn, the bank issues shares tradable in the U.S. that represent an interest in the foreign company. The ratio of ADRs to foreign shares is set by the bank. ADRs do not mitigate currency risk, but can reduce transaction costs and simplify trading compared to buying the local shares in the foreign markets.