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THE SCHOONER

The Official Newsletter of the Dalhousie Investment Society (DALIS)

Alumni Spotlight:
Dan Parrack, CFA

Managing Director and Head, Canadian Debt Syndication
CIBC World Markets

What year and what program did you graduate from Dal?

I graduated in 2007 with a Bachelor of Commerce, Cooperative Program in Finance.

Can you briefly describe what syndication is and what your role entails?

I lead the Canadian Debt Syndication team within Debt Capital Markets, which is a function of the Investment Bank at CIBC. The role of debt syndication is to act as new issue bond sales and liaise between bond investors and bond issuers to deliver a recommendation on the most appropriate size, tenor and pricing of a bond transaction that meets both investor and issuer client objectives.

A good syndication manager has a general pulse on the market and macroeconomic trends, and has a solid understanding of the motivations and desires of buyers and sellers. We try to balance the expectations of bond issuers on one side of the transaction (i.e. companies or organizations that want/need to raise money like Bell, TELUS, Dollarama, or Loblaw) with bond investors on the other side (i.e those willing to lend/invest money like Asset Managers, Life Insurance Companies, Pension Plans, and Hedge Funds) – all while staying balanced on the advice given and on the feedback received. A great syndication manager has strong relationships on both sides of the deal in order to guide toward the best outcome for all clients.

As a leader on the team, I assist bond issuers with the marketing, structuring, distribution and pricing of bond transactions. My busier days consist of executing and negotiating bond deals as mentioned above, but when we are not live with a transaction, 80% of my day is spent discussing market themes and investing preferences with Fixed Income Portfolio Managers and Credit Analysts and the other 20% of my day is pitching issuers on opportunities to raise debt in the Canadian Debt Capital Markets.

What two pieces of advice would you give current DALIS members?

1 - Don't feel like you need to know it all – ask questions, be inquisitive, contribute and don't shy away from innovative ideas. As a manager, I think assimilation is the death of advisory, and my team is encouraged to debate and discuss their points of view and are prepared for each meeting with an informed opinion. When starting out, no one expects you to know it all, so take advantage of early opportunities by coming prepared to learn as much as possible.

A Glimpse of What's Inside:

What two pieces of advice would you give current DALIS members?

2- In the fast-paced world of finance and capital markets, it's important to avoid getting fixated on one transaction or one interaction but to always see the big picture, or the see the forest through the trees. The most successful Capital Markets professionals are able to step back and reflect on the end client and goal to ensure that all the pieces are connecting and the right advice is given. Reflecting on the big picture is something you can start doing on day one, and will become a muscle you strengthen over time. Keep moving forward, learn from your experiences and don't sell yourself short because it gets easier once you've "seen the movie before".

What do you see as the biggest challenge in the debt industry over the next 5 years?

I'd love to give a technical answer about where credit or rates are going to be in 5 years, but I believe the biggest challenge the debt industry will face is lack of technological integration and innovation. The bond market is a large over-the-counter market that is notorious for being a slow adopter of technology. The industry is ripe for disruption and we need to more proactively adapt. At the heart of it, it's a relationship-based industry, but we need to embrace secondary trading, risk management, and primary issuance technology that enhances liquidity, transparency, and unlocks efficiencies.

What is your favorite memory of your time at Dalhousie?

Summer semester during the co-op program. To be in Halifax during the beautiful summer months when the campus is relatively quiet is a pretty special experience. That time brought our program closer together and solidified some life-long friendships.

What is an opinion you have that most people disagree with (Finance or otherwise)?

You don't need social media to feel connected.

Trade of the Month

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Frequent readers of The Schooner will recall my industry analysis on the market for carbon from the February issue in 2021: Carbon – Fad or Future?. At the time, it was my position that the ratification of net-zero policies across developed economies had returns baked into the long-run investment horizon for greenhouse gas ("GHG") offsets. Informed by turn of the century goals for net-zero that bring forth demands such as capped timeframes for the proliferation of internal combustion engines – to name one of many – my stance was that carbon markets offered meaningful and guaranteed upside well into the future. This perspective was aligned with that of the market consensus which finds the GHG offset market to "offer significant potential for innovative solutions and strategy from new capital investment". And so, in typical Wall Street fashion, fee-hungry asset managers were quick to satiate the demand for hot new offset investments, developing a slew of offerings across securities markets. Subsequently, green ETFs and green bonds experienced large capital inflows, generating three years of demand-driven overperformance that was roughly 5x the fund flow of most major asset classes. In like manner, large fund issuers subsidised thousands of column inches dedicated towards covering their new "green" offerings; financial media allocated significant airtime towards ESG performance; and ESG-focused desks sprang up at most large institutions. Hindsight makes it clear that these developments were evidence that a bubble had formed in the market for carbon.

This bubble burst in 2022. As the world reopened from the pandemic, prolonged supply chain disruptions, elevated commodity prices, and a hot labour market put upward pressure on inflation and interest rates. In the case of carbon – indeed unfortunately for my original thesis – this new environment for risk premiums proved to be uniquely sticky. This is primarily explained by the fact that businesses who are best positioned to adopt strict ESG mandates tend to follow models for high growth which are reliant on debt capital markets. And so, rising rates forced growth and technology companies to use available cash flows (if any) to fund operations that were otherwise funded with debt. It was commonplace for R&D spending to be substituted by defensive saving, and layoffs and share dilution took place across the board of cyclical businesses.

It is fair to postulate that even if the rates-versus-inflation dichotomy were the only risk to ESG portfolios, they would have lagged the market. However, higher rates were not the only challenge to this space.

When Russia invaded Ukraine in February 2022, aggressive sanctions from the West heavily restricted the supply of key agricultural and energy commodities to global markets. The ensuing rightward shift to the supply curve for Russian hydrocarbons at the onset of Europe's winter put upward pressure on European energy prices. The Russia factor was compounded by years of neglect on the investment front for the exploration and build-out of hydrocarbon supply in favour of the build-out and utilisation of renewables. However, renewable energy supply proved incapable of meeting energy demand. And so, when Russian natural gas – sometimes accounting for 40% of energy supply to Germany and England – was cut off, European nations reliant on this supply were forced to walk back overly ambitious environmental mandates in order to keep elevated commodity prices from turning already high inflation into something catastrophic. By year-end 2022, carbon derivatives in Europe and California had experienced drawdowns of nearly 50% while ESG ETFs (irrespective of having a derivative, equity, or dual mandates) whose performance topped FY21 charts were replaced by ETFs with specific focuses to hydrocarbons. In other words, capital investment benefited from the strategy anathema to the green-finance approach.

At first glance, this might seem like a long-term catalyst for ESG. Indeed, net-zero by 2050 is at this point ubiquitous in Western policymaking, and a temporary pause means more aggressive quotas will be needed down the line if we hope to meet this goal. Wrong! In choosing to walk back and in some cases altogether ditch ESG policies, the fragility of the ESG thesis became explicitly clear: : Businesses whose operations yield environmental effects that are antithetical to the demands of ESG (i.e., hydrocarbon producers) were given incentives to ramp up production. Subsequently, governments with environmental quotas for reducing t/GHGe paused their annual goals in favour of bringing coal fired plants back online. This caused demand-driven price spikes in Newcastle 6000 kcal, South African, and Columbian equivalents, and proved that society is unprepared to prioritise the fundamentally destabilising demands of politically driven environmental policies over personal comfort. The carbon thesis was shown to balance, unstably, on political virtue signalling.

So, I fear that the bullish sentiment forwarded in my 2021 piece was more realistically an infatuation with the short-term, get-rich-quick performance ESG had offered during the stable growth period between 2018 and 2021 than it was an informed investment thesis concerned with the macroeconomic fundamentals of energy supply and demand. I had forgotten Buffett's famous credo: "Be greedy when others are fearful and fearful when others are greedy." For these reasons, my position on investment opportunities in the net-zero economy has shifted significantly, and I now view this market as not dissimilar to that of the Dutch tulip market in 17th century Holland, or dotcom names in 1990s America. Charles MacKay wrote about ordinary Dutch industry being neglected when tulips entered their ports in the late 16th century. In this case, history does seem to rhyme insofar as hydrocarbon producers had for years seen a lack of investment driven by the prioritisation of capital towards green alternatives. But while I was naive of the greedy/fearful dichotomy in 2021, my mistake judging carbon served as the impetus for the trade which is highlighted as this month's "Trade of the Month": DALIS Commodity's bull call spread on Peabody ($BTU) Q4 earnings.

Anticipating strong earnings from Peabody Energy ($BTU) who reported on February 14, 2023, Emmerson McNamara (Co-Portfolio Manager, DALIS Commodities), Max Barrow (Portfolio Manager, DALIS Financials, Consumer, Technology) and I (Co-Portfolio Manager, DALIS Commodities) elected to move one percent of the commodities book into a bull call spread on BTU. We purchased February 24 call options at a strike of $26.5 and wrote February 24 call options at a strike of $28. The Street called for an 8% climb after earnings on top of the additional 4.5% move BTU had made at Monday's close. Our position was that BTU would not move significantly outside the range between 8% and 12.5%. The time awarded by our two-week horizon offered a buffer should volatility prove significantly large. This was a wise decision, as within the first few days of our exposure, positive earnings drove BTU stock OTM on both ends of our trade. By midday on February 14, BTU was at $29.96. On February 15, we closed the $26.5 call options for a profit of 57%. On February 22, we sold the $28 downside hedge at a profit of 99.91%. In total, we returned nearly 157% in one week, a deal sweetened by the fact that the premium on our call options was cancelled out by the premium we received selling the hedge – we spent almost no money entering this position.

My editor will likely be angry if I make this much longer so I am going to conclude by briefly providing a lesson on time value. Namely, the success of our trade was predicated on our ability to allow volatility to relax over the two-week period following earnings. Both implied volatility and surface measures indicated that within the short term, BTU was going to move, and move significantly. By dating two weeks out, we were able to distribute volatility over a longer period, with our maximum upside being marginally higher than our maximum downside. However, at net credit on premiums, we were comfortable with exposing one percent of our portfolio to this risk. Looking back on this decision, I am glad we did.

DALIS Commodities now has AUM of nearly $32 million.

The Price of Geostrategic Advantage: How Pakistan's Economy is paying the cost.

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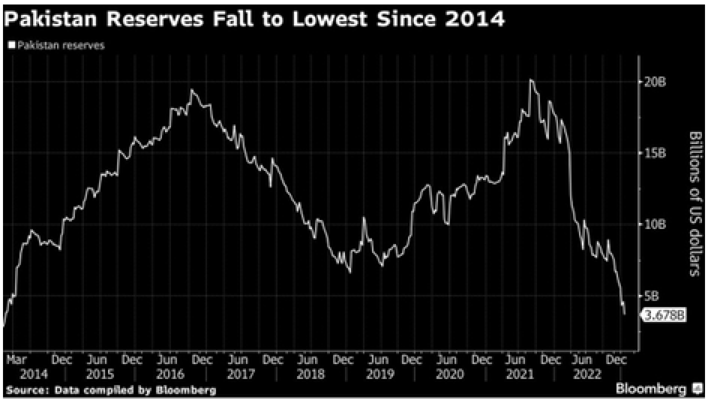
The Pakistani Rupee was trading at 230, and quickly depreciated to 277 PKR against the dollar beginning of February after Pakistan stopped controlling the currency and allowed the market forces to take over. The Rupee is currently stabilized at around 260 PKR against the US Dollar. So why is Pakistan facing an economic crisis, and what is currently happening? Let's find out.

Pakistan stated that it would add $700 million in Chinese debt to its existing $30 billion. But why is Pakistan experiencing its most significant financial crisis ever? What went wrong and hurt their current account? The answer is simple. Its most important revenue started to decline. The revenue being the rent from its geographic location. Seems absurd, huh? Since the cold war, the US has consistently used Pakistan as a base of operations, resulting in a steady inflow of US dollars for Pakistan. This continued until the US began to pull back its forces from Afghanistan. Due to being a neighbouring country to Afghanistan, the US had a significant presence in Pakistan. But, once its forces were withdrawn from Afghanistan, the US no longer saw the need to keep such a substantial presence in Pakistan. Due to this, Pakistan's dollar inflow from the US dramatically decreased. The graph below shows how this affected Pakistan's foreign exchange reserves after the US withdrew in August 2021. As the nation suffered devastating floods that cost them $30 billion, we also observe a further significant decline in the reserves in 2022. The country's food imports rose by 65% due to the floods, while the cost of fuel imports soared because of the war in Ukraine, which also affected the FX reserves causing it to be just over $3 Billion as of February 2023.



At 27.6%, the country's current inflation rate is at a 48-year high. Because there is not enough fuel to last a whole month, there are periodic national power outages. To make matters worse, Pakistan has failed to meet the IMF's standards for the loans against China, causing the IMF to halt the $1 billion tranche of the $6.5 billion bailout. Chinese debt makes up 30% of Pakistan's external debt. China is in a very comfortable situation and has no plans to restructure; instead, it is issuing new debt in order to take advantage of the debt trap strategy and acquire advantageous strategic locations, just like it did with the Sri Lankan Port.

Pakistan's reserves cannot cover more than 3 weeks of import and the country's defence minister quoted "You must have heard that Pakistan is going bankrupt or that a default or meltdown is taking place. It (default) has already taken place. We are living in a bankrupt country," The core inflation in Pakistan has reached 38.4%. To deal with the current scenario and save FX reserves Pakistan is shutting down many of its foreign missions, increasing the import sales tax from 17% to 25% and general sales tax to 18%. This plans to add $650 million per month in revenue. Since many sectors in Pakistan depend on imports, the government's actions caused numerous businesses to close or drastically scale back operations.

In an attempt to desperately save cash and convince the IMF, Pakistan is placing a ban on buying luxury items and new cars till June 2024, stop providing security, support staff, luxury cars and funds for miscellaneous expenditures to ministers, not only this but the ministers are not allowed to travel unless absolutely necessary and should promote teleconferencing. These measures are expected to save Pakistan a whopping $700 million. On the command of IMF it even stopped controlling its currency and let the market forces takeover. Pakistan needs to renew the IMF bailout in order to survive and get out of this crisis.

Low FX reserves, high short-term debt, high inflation, and a growth model reliant on imports indicate a bearish feeling on the PKR and the country's economic condition. Currently, Pakistan seems to have an extremely similar crisis to Sri Lanka. If Pakistan cannot secure the $1 Billion tranche from IMF it will face similar consequences to Sri Lanka.

Canada is a Global Oil & Gas Power, It's Time to Start Acting Like It

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Canada is the world's fourth-largest oil and gas producer, and an opportunity is opening to seize market share from the world's number two producer, Russia. However, even though the Canadian oil and gas industry has global trade potential, they face a barrier of a governmental effort to reduce carbon emissions.

The west's stand against Russia's invasion of Ukraine came in the form of oil and gas sanctions, targeting what makes up 18% of Russian GDP. Specifically, a ban on Russian oil product imports in the EU and a global price cap of $60 per barrel on seaborne exports. A large hole in the global of oil and gas supply resulted in prices reaching new peaks in 2022, but recently have fallen due to slowing economic growth in many countries. The winter's seasonal effect on oil prices was relatively mild in Europe, not drastically affecting demand. The EU must tread lightly, if sanctions become too brash, they could create long term disruption to their own economies through the global oil and gas trade. Russia reduced its oil production by 500,000 barrels per day, a retaliating attempt to hike oil prices. In the wake of Russian oil contraction, market share lies unclaimed, and Canada has an opportunity to step up.

The start of the Russia-Ukraine war developed a global eagerness to find a new major supplier of oil and gas. In January, Korea and Japan began looking to Canada to supply their Liquefied Natural Gas (LNG) needs, but Prime Minister Justin Trudeau reiterated Canada's 2030 carbon emission targets. An energy sufficiency ratio measures a country's energy output divided by their own energy consumption. Evidently, Canada's energy sufficiency ratio is 180%, meaning Canada has more than enough energy to go around. Trudeau claims that Canada is acting to reduce emissions more than any other stable democracy; in reality, Canada is one of the largest greenhouse gas (GHG) emitters among large economies.

The Canadian Pathways alliance was formed by the 6 largest Canadian oil sands companies with the goal to reach net zero emissions in their industry by 2050, and it is estimated that $45-65 billion will have to be spent to do so. The Pathways Alliance plans to reach this target by investing in carbon capture and storage (CCS), a process in which GHG is captured and stored underground safely and in some cases repurposed. Trudeau's desired milestone is to cut GHG emissions by 42% before 2030 in the energy sector. MEG Energy CEO, Derek Evans, responded to the goal using the words "ambitious" and "unrealistic," while Imperial Oil's CEO, Brad Corson, stated that it "stretches the truth of what is technically and economically feasible". All considered, one still wonders how environmentally progressive our global oil and gas competitors are feeling during this global supply crisis.

The government's reasoning for such aggressive targets is the energy sector's recent windfall profits from surging commodity prices in 2022. Energy fled 2022 as the only gaining sector within the S&P, attributed to the Russian oil sanctions. As a result The diversion of opinions is how these windfall profits should be spent. Why would any sane oil and gas executive invest their recent windfall profits into anything beside their core business, especially when the world is scrambling to fill supply?Obviously, that is an exaggeration, large energy companies do have the capacity to expand production whilst also investing in CCS, but it is still a valid question. Debt is expensive, commodity price outlooks are not promising, and demand is currently high for oil and gas products. Companies could repay debt, increase dividends and share repurchases, and invest in infrastructure to produce and export oil and gas. The government has tried to disable the energy industry's selfish form of capital distribution by implementing a tax on share buybacks beginning in 2024. Tax arguably has only encouraged oil and gas companies to return more capital to shareholders in 2023, with the likelihood that Canadian energy's free cash flow will not be as strong in 2024.

For Cenovus energy, they held oil and gas output relatively constant from 2021 to 2022, but still doubled revenues, doubled capital expenditures, and cut net debt in half (year over year as of Dec 31, 2022). Recently, UK oil giant BP PLC released their 2023 guidance in which they announced they are scaling back on their transition into renewable energy, which was met with a very positive reaction from investors. BP previously was one of the more environmentally aware companies that campaigned the most for transition into renewable energy so a reversion back to its core business was seen as a good sign for the industry.

Energy fled 2022 as the only gaining sector within the S&P, attributed to the Russian oil sanctions. The global commodity benchmarks gave them lemons in the form of free cash flow, and they are using it to make lemonade. Any good executive in the industry should be worried about sustaining profitability and sufficient capital as we enter a recession, not support the actions that oppose the foundation of their business. Canadian oil and gas companies have a lucrative opportunity ahead of them.

Bull is in the name

Tac Chatterson, Executive
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Toromont Industries Ltd. provides specialized capital equipment through its two operational segments: Equipment Group and CIMCO. The Equipment Group engages in the rental and sale services of Caterpillar and other equipment for various industry groups. CIMCO supplies commercial refrigeration units, particularly food and ice rink refrigerators.

Investment Summary
BUY Toromont ("TIH") with a one-year price target of $122.50, plus their forward dividend of $1.72 proves an upside of ~10%. To arrive at $122.50, I valued TIH based on a perpetual and exit multiple Discounted Cash Flow method, and a price-to-earnings relative valuation. Here are three reasons to support my recommendation: (1) TIH has significantly outperformed its supplier (CAT) and main pure play competitors since the 2015 mining downturn;

(2) TIH is financially positioned to grow; (3) TIH's target industries are necessary for the energy transition.

TIH.TO	BUY
Date	27-Feb-23
Current Price	$113.33
Target Price	$122.50
Dividend	$1.72
Upside	10%
Industry	Industrials
Sector	Industrial Dist.
Shares Outstanding	82.32M
Market Capitalization	$9,329M
Diluted EPS (2022)	$5.47

Valuation

WACC is estimated at 7.00% for TIH, given their low a-tax cost of debt of 3.34%, and low beta of 0.75. Three scenarios drive the intrinsic and relative valuations: Bear which was assigned a weighting of 10%; base at 50%; and bull at 40%. Given TIH's recent revenue growth of ~10%, I believe that their future is geared toward the upper end of the base case and lower end of bull. This growth is not shown in 2023, primarily due to North America's current monetary policy. However, when interest rates drop and companies look to grow their equipment through debt funding, TIH will be primed for growth. To reflect a low interest rate environment, I have forecasted a revenue growth rate of ~15-16% through 2025 – 2026.

2% serves as the perpetual growth rate after 2027, and a peer group median forward EV/EBITDA multiple of 11.45x based on Bloomberg's forecasted 2023 comparable analysis. The relative P/E analysis uses the same peer group with a median forward P/E ratio of 15.84x at EPS of ~$5.20.

Figure 1: Valuation Summary

Rationale

(1) As seen in figure 2, TIH has performed remarkably better than its pure play competitor Finning since the 2015 mining slump, as well as its main supplier Caterpillar. Their exposure to Eastern Canada provides optimal positioning equipment sales to Canadian mining companies in Ontario, Quebec, and Atlantic Canada. TIH has shown resilience through economic troughs, which makes them a great long-term investment.

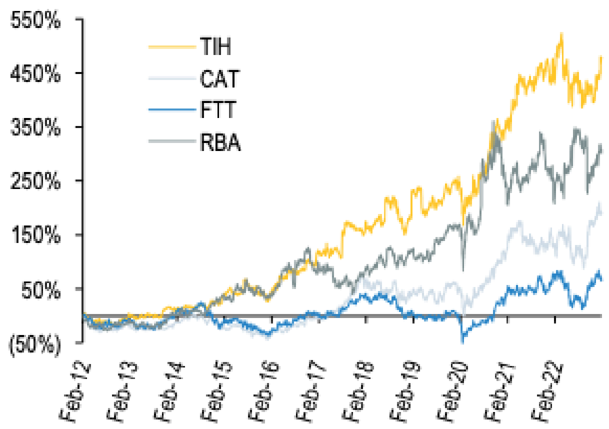

Figure 2: 10-Year Return

(2) TIH has had an increasing cash position and conservative leverage since 2018 which has resulted in negative net-debt since 2021, as seen in figure 3. With cash nearing C$1B and EBITDA greater than debt, TIH could be looking to deploy its cash in special dividends, share buybacks, or M&A (Ex: Hewitt acquisition in 2017 was ~C$1B).

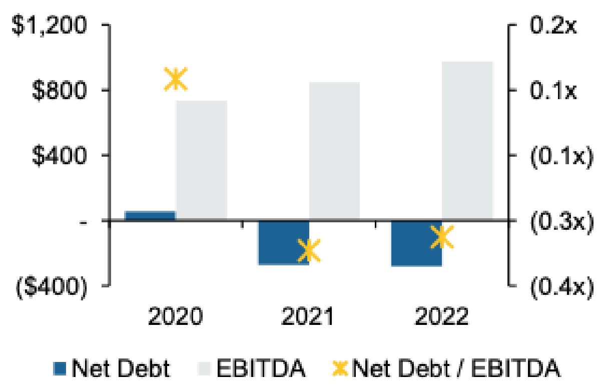

Figure 3: Net-Debt/EBITDA

(3) With the 2030 Sustainable Development Agenda in mind, and government funding such as Biden's Bipartisan Infrastructure Law, mining and construction companies should be ramping up their capex spending, especially once interest rates decline. For example, TIH had a quarterly increase in mining sales and rentals of 225%.

Risks

(1) Supply chain constraints: Caterpillar and other suppliers suffered backlogs in 2022 when the reopening of the economy outpaced the global supply potential.

(2) Strong dollar: Caterpillar sells its equipment in USD resulting in an increase in cost of goods sold for TIH, ultimately reducing the free cash flow.

(3) Decreasing commodity prices: When the prices of commodities dip, mining companies are more likely to decrease capital expenditures and service their equipment internally. 41% of TIH's revenue comes from product support and servicing and 39% from new sales.

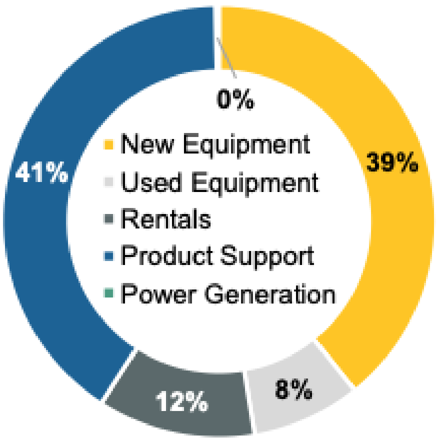

Figure 4: Revenue Segmentation

A Silver Tongued What?

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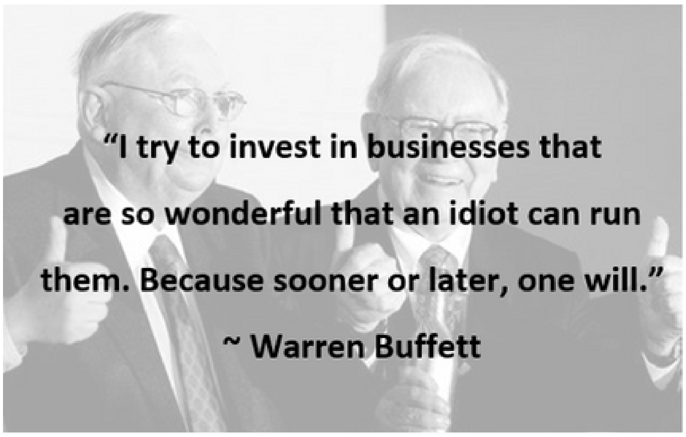
Berkshire Hathaway's recent shareholder letter has made headlines for its earnings miss and memorable quotes, including Buffett's criticism of anti-stock repurchasers as financial illiterates or silver-tongued demagogues". Warren Buffett needs no introduction, and many investors eagerly await Berkshire Hathaway's annual shareholder letter. But beyond the headlines, these letters offer valuable insights into Buffett's investment strategies and philosophy, which he has been refining for almost 80 years. Over 58 of those years are documented in his shareholder letters, which many investors consider sacred. Nevertheless, the objective of this article is not to simply recite performance numbers, but to highlight the major themes that young market enthusiasts can learn from the Buffet and Munger Archive. By studying these themes and applying them to their own investing strategies, they can benefit from the wisdom and experience of two of the greatest investors of all time.

How to Think About Investing

The philosophy behind Berkshire and long-term investing is often vague in the minds of young investors. A short-term mindset of moving in and out of stocks weekly, monthly, and annually is a path to ruin. Buffett repeatedly emphasizes that "Investment is the process of putting money out today to get more back at some point in the future. The only questions are: how far in the future, how much money, and what is the appropriate discount rate to derive present value?". This framework focuses on what businesses' future outlooks over decades and requires investors to know the company, and industry, inside and out. Charlie Munger echoes this sentiment, saying, "there is no buying stocks that wiggle around on paper with a chart attached", but only buying a business that you know and understand.



Efficient Market Hypothesis

Warren is a detractor of the efficient market hypothesis, a keystone yet highly disputable piece of modern financial theory. The hypothesis states that stocks will always trade at fair value and conducting fundamental or technical analysis to prove otherwise, is meaningless since there is no "beating the market". However, Buffet believes otherwise. In a letter from 1999 he states that "adapting to efficient market theory would be like learning the earth was flat, a terrible, terrible mistake". Additionally, Buffett accuses universities of teaching an incorrect approach to capital markets, resulting in generations of investors with flawed perspectives. Many students, including myself, struggle with this issue. My own family would put a spoon under their pillow to earn a mere 5% returns, while the basics of business valuation, and Berkshires Hathaway's approach to long-term investing are rarely taught. The fact is that Markets are often mispriced due to emotional factors like greed and fear, which have little to do with a company's actual assets, earning power, or brand value. To be a successful investor, it is essential to value a business correctly, a skill that according to Buffet is extremely hard to find in business schools. Although today, business schools are slowly changing. As someone who is currently pursuing a degree in finance, I have had to seek out extracurricular courses to learn these critical skills. I would give the same advice to any student besides me, a degree alone does not entitle you to anything, especially to young finance enthusiasts, you must be willing to go beyond your class schedule to gain a foothold in the world of investing.

Students Edge on Investing

One unique feature of Dalhousie's commerce program is the requirement for students to complete three mandatory Co-Ops, which is a major draw for prospective students due to the valuable experience gained. However, few students consider the strategic monetary benefit of these internships, apart from paying for necessities like rent and food. For students who are frugal and resist the temptation of excess beer and takeout food, the co-ops present an unprecedented opportunity to set up their future finances. But it's important to remember that investing at an early age is "the food of the wise, but the liquor of the fool". Those who can avoid the noise and stick to the long-term investment philosophy of Warren Buffet are likely to do exceptionally well. That is, before Buffett invests in a company, he will read as far back as statements go, understanding every aspect of its strategy, and the surrounding market. Once Buffett has purchased a company, he is loath to sell. The beauty of this strategy is that all of his analysis is well-documented, enabling others to read, adopt, and repeat it.

Warren Buffett and Charlie Munger have left an indelible mark on the world of finance. Their investment philosophy of focusing on value companies for the long-term is the only profitable option, especially for those with little market knowledge.Although it may be slow at the beginning understanding this concept is the single most valuable piece of advice one can receive. Unfortunately, the fundamental skills of knowing what you're investing in, how to truly value a business, and assessing the market atmosphere are rarely taught in business schools. This is why Buffet's opinion on efficient markets and the shortcoming of finance education is highly regarded advice for newcomers in the field.

His writing demonstrates a forceful perspective on academic finance, urging students to take responsibility for their own learning and go beyond what universities offer. It is a call to action for students solely trusting their institution to teach the finance materials to bring them success, based on Buffett's comments, they are actually failing. If you have yet to explore the Berkshire archives, make it a routine, and follow "the Buffett way" of investing. It is unheard of finding someone of Warren and Charlies tenure anywhere else, and studying them now, will undoubtedly pay massive dividends in the future.

Natural Gas Prices Take a Tumble: How did it Happen in the US and Europe

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At the end of October, I wrote an article focusing on Uniper, the German energy company that had to receive bailouts from the government just to keep the lights on. I went on to state that Europe's overdependence on Russian gas would lead to an energy crisis in Europe during the winter months. Fast forward four months and the only thing that has suffered is the price of natural gas. The turnaround has been remarkable and has left Europe in a position where the continent has successfully weaned off Russian gas. However, it is not just European gas prices falling to pandemic-era lows. US gas is also trading at two-year lows.

On the US front, natural gas prices have fallen around 80% from August to about US$ 2.55/MMBtu. The biggest reason for the price decline has been America's unexpected mild winter temperatures. Historically, the 48 contiguous US states reported this past January to be the sixth warmest on record. Breaking it down further, the six New England states said this January was the warmest ever. Finally, New York, Pennsylvania and Indiana had their second-warmest January since 1895. Another reason for the lower prices in the US is the ongoing recovery from the Freeport liquid natural gas (LNG) plant explosions in June. . Before the explosion, the plant accounted for almost 20% of all US natural gas exported to Europe. However, this explosion caused European countries to scramble to find alternative gas sources when they believed a harsh winter was imminent.

The gas that could not be shipped was put back into the US market, which increased supply with no increase in demand. Overall, the unexpected warm winter and excess domestic supply are driving forces behind the significant decrease in the price of US natural gas.

On the European front, the situation is similar to the US, with future prices falling more than 80% from August's peak. Mild weather has also been a factor in Europe, with January being one of the warmest in decades. German gas storage facilities are currently around 80% full, drastically higher than the 35% reported a year ago. In addition to the mild winter, methods to encourage a reduction in fuel consumption, such as price caps, have allowed storage facilities to remain filled. Finally, the Russian gas that Europe used to rely on has now been almost entirely replaced by gas coming from the US, Qatar, and Norway. Relying on three countries rather than one allows European countries greater flexibility when importing gas. Uniper has stated that the company will overcome the problems caused by Russian gas cuts by 2024. Europe seems to have dodged economic collapse due to some lucky weather and alternative gas sources and now seems destined to have enough supply to last this winter and next.

I did not envision the significant drop in gas prices after following Europe's desperation over the past year. I am glad that Europe could dodge such an economic disaster and not let Russia win. However, selfishly a cold winter would have significantly benefitted numerous positions within the Energy, Industrials and Real Estate portfolio.

Navigating Energy Earnings Season

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This month marks a tragic milestone in the modern history of Europe, for it was exactly one year ago when Russia invaded Ukraine. It is old news that the strict sanctions are among the Western response to Russia's invasion, and that Russia's counter was to effectively ban the sale and export of key agricultural and energy commodities to countries they deemed unfriendly. This resulted in developed economies struggling to source cost-effective energy. North American companies were quick to fill a gap of larger than usual demand. In turn, natural gas prices hit multi year highs, and oil stabilized near all-time highs throughout 2022.

The Energy, Industrials and Real Estate desk at DALIS is tasked with the responsibility of diversifying the Maritime Fund with, among other things, energy exposure. As such, by fall 2022, this mandate was far from our most challenging. Energy demand was soaring, oil and gas companies were spitting out record revenues, and their share prices were following suit. Our outlook on oil and gas companies was straightforward and simple. We took on multiple long positions in plenty of oil companies that we believed to be undervalued in the midstream, upstream, and downstream sectors. And for about three months or so, it almost became a case of 'if it's not broken, don't fix it' with every pitch for an energy position being a long. We are pleased that nearly every one of our investments in the space ultimately yielded profits for the portfolio. However, during late 2022 and early 2023, our portfolio exited majority of our oil and gas long positions.

The energy sector was experiencing increased volatility and new uncertain bears and bulls meant the fourth quarter of 2022 was an important earnings season. The uncertainty of 2023 energy outlook forced our hand at diversifying our strategy away from vanilla long positions towards a more event-oriented, short-term approach. During earnings season, we focused our opinions on specific energy company's projected Q4 strength and 2023 guidance. The first industries to capture the attention of our new outlook was the coal and mining industries. Most of the companies in the sector reported earnings in February, before the oil and gas sectors which report in early March. We narrowed our approach to certain businesses we felt we understood, specifically focusing on those companies we believed would outperform estimates by a good margin.

Our most profitable trade was on Peabody Energy ($BTU). Peabody is a coal company headquartered in the Midwestern United States. They reported earnings on February 14th. Our outlook had the company reporting very impressive cash flows and revenues, and because of our short-term approach in the position, EIR felt almost no pressure from the long-term negative sentiment towards the proliferation of coal mining. Following their release, Peabody shares shot up approximately 12%. The group had purchased out of the money calls and held the underlying stock for weeks leading up to the earnings call. We exited both positions shortly after the earnings release, after hitting our targets and bringing in some respectable gains. Our portfolio profited roughly 75% all together from the trade and since exiting our positions, BTU has drop about 12% from the Feb 14 high. It is no surprise that our partners at DALIS Commodities were successful in trading the same name – their BTU trade is, after all, the February trade of the month.

Speaking into investor sentiment on coal long term, Vancouver based mining firm Teck Resources made headlines days before their fourth quarter earnings call by announcing plans to spin off their coal business. The firm has been exploring their options in separating its metallurgical coal and copper businesses into two units for almost a year but had never made a clear announcement on moving forward with doing so. The coal operation will be renamed Elk Valley Resources (EVR), and the remaining copper and zinc business will be named Teck Metals. As a result of investment from steel companies, Teck shareholders will own 100% of Teck metals and 87.5% of EVR. Investors will earn 0.1 EVR share per Teck share plus cash. Potential reasons behind Teck's decision are firstly to relieve ESG pressures from weighing down the business, and secondly to boost copper production to take advantage of the growing demand. The largest and most profitable part of Teck's business, metallurgical coal, is valued around $8 to $10 billion. The breakup has also created headlines that Teck could now be in the crosshairs for mining giants such as BHP, Glencore, and Rio Tinto who are looking to grow their copper exposure. Looking forward at the coming weeks, earnings reports aren't slowing down. This week, investors hear from Tourmaline, a natural gas company based in Western Canada. Shares have been put to the test as of late, and it will be interesting to see how the company addresses investors who have voiced expectations of the bleed easing (down roughly 24%, in the past 6 months). EIR is set to remain active in the energy sector looking to take advantage of uncertainty and an extremely sensitive earnings season.

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