



# Auxier REPORT

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## Summer 2021 Market Commentary

The market and economy continued a strong rebound during the second quarter as COVID restrictions eased further. The 7-day moving average for new COVID cases in the US recently reached its lowest level since the start of the pandemic. However, the spike in the Delta variant is adding headline uncertainty. Economic growth has been strong thanks to vaccine distribution efforts, businesses reopening and emergency fiscal and monetary stimulus. JPMorgan estimates full-year US GDP growth of around 6%, the highest since 1984. The ten-year treasury bond yields less than 1.5%. Back in 1984 we were buying Washington State general obligation bonds yielding 10% when the GDP had similar readings. Retail sales are 20% higher than pre-COVID levels, indicating strong consumer spending and sentiment. Back-to-school spending should be boosted with the liberalized Child Tax Credit (CTC). Nearly 70% of US economic growth is tied to consumer spending. The housing market fundamentals are benefiting from record low mortgage rates, surging demand from millennials, buy-to-rent institutions, foreign buyers and Airbnb conversions. In addition, the pandemic and technology advances enabled millions to work at least part time from home, adding unanticipated demand from the migration out of the major cities. Home equity values now exceed \$22 trillion.

We continue to meet with numerous management teams and see powerful earnings on the back of companies that have scale and have been aggressively digitizing, with a focus on improving the customer experience. The pricing power has been the strongest I have seen in my career across most industries. Surprisingly, margins have held up as well.

## Inflation

The pandemic put a strain on global supply chains which has resulted in dramatic price increases in the shipping container space. According to research from Sea-Intelligence, the average price to ship a 40-foot container has increased by more than fourfold to \$8,399 as of July 1. Some short-term rates have exceeded \$25,000. Global vendors like Amazon cannot afford to delay their shipping in hopes of better rates and so they have been forced to pay these elevated prices, which has boosted global shipping companies. The leading container company Textainer has had tremendous operating results. Philip Damas, head of supply chain advisory at Drewry, expects that the strains on the container shipping industry will remain in place until early 2022. Ironically, just as consumers get used to online shopping, the cost of transportation is soaring. The American Trucking Association projects a shortage of 100,000 drivers by 2023. Numerous CEOs are echoing the price pressures that seem to be accelerating. Unemployment benefits have been so attractive that it has been difficult to motivate workers to return, prolonging bottlenecks.

The ongoing microchip shortage has caused the used car market in the US to heat up as new car inventory in the US was 54% lower in June 2021 versus June 2019, which has boosted demand for used vehicles. Prices are up 40% more than in February of 2020 before the peak of the pandemic. The average 9-year-old vehicle sold for \$13,250 in June, which is approximately up 30% over June 2020. Microchips are a critical component of nearly every electronic device in the world so the shortage of new cars could continue for some time.

So far, we are seeing most businesses raise prices and consumers willing to pay up. This has contributed to a tremendous broad-based earnings improvement for our portfolio companies.

The dollar has depreciated over 85% the past 50 years. Purchasing power risk is hidden as people mistakenly perceive safety in fixed income. Today we are seeing negative real yields all the way out 30 years as inflation is running over 5.3%. Owning businesses is a better bet. However, you can't just pay any price for stocks as higher inflation tends to compress P/E ratios. In 1972, conventional wisdom was to simply buy the 50 most popular stocks known as the "Nifty Fifty." The idea was to buy, hold and forget. In the frenzy the stocks traded over 80 times earnings on average. Then, despite strong earnings, a surge in oil and inflation crushed valuations leading to a 70%-90% decline for the group. A good general rule for a market multiple has been 20 less the inflation rate. In 1979, with 11% inflation the P/E of the market sunk below 10.

It appears the current inflation is understated, especially if you add back energy, food and housing which are all excluded. The consumer price index (CPI) only includes the rent component of housing; however, rents are now catching up too. Invitation Homes, the largest single-family landlord in the nation, recently boosted rents by 8% across the country. Back in the 1970s, Fed chairman Arthur Burns claimed that rising inflation was nothing to worry about—it was "transitory" and best ignored. When oil quadrupled, they solved the problem by taking oil out of the index. Food prices, a 25% weighting, soared and were also removed. So was housing, a 16% weight. The Dow hit 1,000 in 1972 and was flat until 1983. As cost price pressure hits, consumer wage expectations and compensation demands go up, which are hard to reverse—especially in areas difficult to digitize like skilled labor. Historically, government intervention in the form of wars, extreme socialism and confiscations have contributed to supply disruptions and higher inflation. After the American Civil War, inflation drove interest rates to 20%. When Zimbabwe confiscated private farms their inflation soared 3000%. As Venezuela nationalized most of their businesses inflation exceeded 500%. Inflation in Argentina recently gained 70% as the government interrupted free markets and politics moved to the extreme left. Domestically, recent bans on natural gas turbines and pipelines have led to a reduction in fossil fuel capital investment which should contribute to higher sustained power prices. Over the years, societies with free market competition and innovation have generally kept inflation in check. However, heavy-handed socialism is a recipe for more permanent price increases. The potential for the Delta variant could further extend the interruption in supply chains.

## **Companies That Can Thrive During Inflationary Periods**

When I started in the business, inflation was one of the biggest headline worries. I initially went back over the prior 80 years and studied the types of businesses that could survive, thrive and outperform during high inflation. Generally, undervalued companies that had powerful brands with freedom to price, consistent and growing demand, rapid inventory turns and high returns on invested capital with low mandatory capital expenditures tended to outperform. Drug stores and supermarkets with low ticket necessities were notable winners. Investment selection becomes much more important as higher inflation can put a lid on valuations. Often markets can become rangebound and can go flat for years. In 1983 when the Dow rallied to 1,000, I remember experienced investors wanting to sell out as the market had been stuck in a narrow trading range for the prior 18 years with 1,000 the top. A higher inflationary environment is not a friendly environment for the "growth at any price" momentum approach. Making an exceptional buy becomes much more important as inflation acts as a headwind to breakout valuations.

## **Kroger Shows Confidence Amid Fears of Rising Inflation**

Kroger is an example of an inexpensive (13 P/E), low expectation stock that has survived well during periods of higher inflation. The company turns over inventories 14 times a year, which helps to maintain a high return on invested capital and pricing power. They recently recorded another strong quarter and beat consensus estimates for both revenue and non-GAAP (generally accepted accounting principles) EPS.

Kroger has been able to maintain their momentum despite the lifting of pandemic restrictions and restaurant re-openings. Digital sales continued to grow, up 16% on the quarter and 108% over the last two years. Due to their success this quarter, the board announced a new \$1 billion share repurchase program. Management also raised their guidance for full-year 2021 adjusted EPS to \$2.95-\$3.10, up from their previous guidance of \$2.75-\$2.95. Since Amazon's acquisition of Whole Foods in 2017, some investors have feared that Kroger would begin to lose market share to the e-commerce giant. The pandemic has bolstered their position as a leader in the US grocery market with an 11.7% share. Despite all the fear surrounding Amazon's Whole Foods purchase, they have only been able to amass a market share of 2.6% since entering the grocery space. Management has also addressed fears that future inflation could dampen growth, stating that they operate at their best when the inflation rate is around 3%-4% and more shoppers move away from large brands, opting for Kroger's lower-cost private label options. Kroger also continues to build their Ocado automated warehouses that will greatly enhance the company's delivery capabilities and allow them to better compete with e-commerce giants like Walmart and Amazon. In addition, they are well positioned to benefit from the robust back-to-school market this fall.

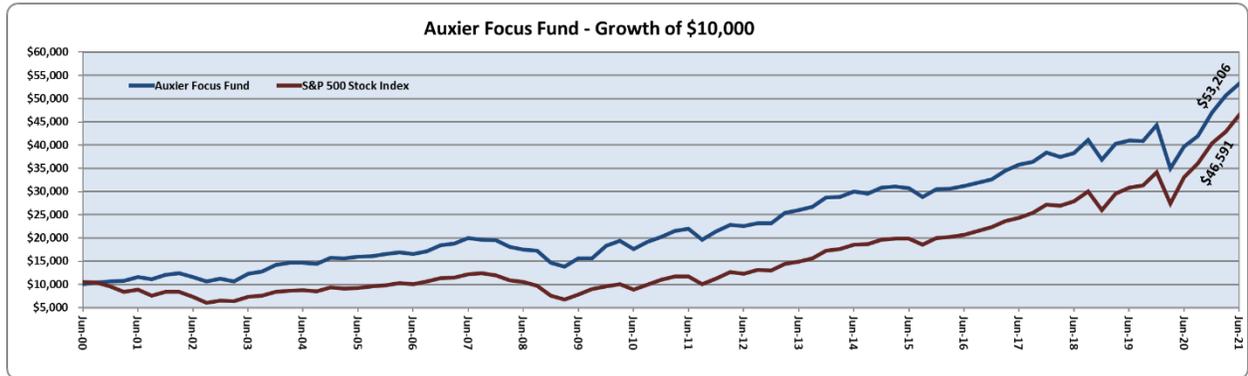
### **Reality of Automation in the Auto Industry**

The advancement of AI technology has increased interest in developing self-driving cars and has led to over \$120 billion in investments from 2017 to 2019, according to research from McKinsey. Companies like Tesla, Uber and Lyft have bet big on driverless technology, but it may take longer than expected before fully autonomous vehicles are available to consumers. Elon Musk, CEO of Tesla, recently stated that creating AI programs that can adapt to complex roadways and unpredictable human drivers has proven to be a greater challenge than they originally thought. Tesla is still committed to the technology as they continue to test an advanced beta version of their self-driving software that Musk believes could one day solve the challenge of autonomous vehicles without the use of expensive lidar and radar sensors. Companies like Alphabet's Waymo have been able to achieve fully autonomous vehicles using lidar sensors and highly detailed maps of specific areas around Phoenix, Arizona. However, this approach will likely be difficult to scale and could be cost-prohibitive for the average consumer. It remains to be seen if these challenges will be solved any time soon, and companies may be better off investing in safe and effective driver assist systems until AI technology advances further. McKinsey also estimates that any company that intends to remain competitive in the driverless car market could potentially have to invest \$70 billion through 2030. As always, talk is cheap, and it is important to look past the hype and focus on execution.

### **Value Potential**

In 2000, Yahoo and AOL were two of the most exciting technology stocks that were going to transform the world. In the dot com mania they reached a combined valuation in excess of \$250 billion. This year Verizon sold both companies to Apollo Global Management for \$5 billion—a 98% decline. AT&T acquired DIRECTV for \$49 billion in 2015 and recently sold 30% of the business for \$1.8 billion. Overpaying and overborrowing are the recurring sins that consistently destroy shareholder capital. Just like in 2000, the spread between the cheapest and most expensive stocks is now one of the widest in history. Historically, the Russell 1000 Growth Index trades at a 5.6 times point premium over the Value Index but is currently trading at a 10.3 premium. We expect a reversion to the mean, especially if the economy broadens and inflation continues to rise.

## Second Quarter 2021 Performance Update



Auxier Focus Fund's Investor Class returned 4.91% in the second quarter vs. 8.55% for the cap-weighted S&P 500 Index and 5.08% for the DJIA. The equal-weight S&P 500 returned 6.90%. Small stocks as measured by the Russell 2000 were up 4.29%. The MSCI Emerging Markets Index gained 5.05%. A 60/40 S&P 500 and Bloomberg Barclays US Aggregate blended index returned 5.84% and bonds, as measured by the Bloomberg Barclays US Aggregate Bond Index, returned 1.83% for the quarter.

Stocks in the Fund comprised 96.3% of the portfolio. The equity breakdown was 85.1% domestic and 11.2% foreign, with 3.7% in cash and short-term debt instruments. A hypothetical \$10,000 investment in the Fund since inception on July 9, 1999 to June 30, 2021 is now worth \$53,206 vs. \$46,591 for the S&P 500. The equities in the Fund (entire portfolio, not share class specific) have had a cumulative return of 775.05% since inception and the Fund as a whole has had a cumulative return of 432.05% vs. 365.91% for the S&P. This was achieved with an average exposure to the market of 80.6% over the entire period.

Auxier Focus Fund – Investor Class  
 Average Annual Total Returns (6/30/2021)  
 Since Inception (07/09/1999) 7.90%  
 10-year 9.27%  
 5-year 11.23%  
 1-year 34.03%  
 3-month 4.91%

*Performance data quoted represents past performance and is no guarantee of future results. Current performance may be lower or higher than the performance data quoted. Investment return and principal value will fluctuate so that an investor's shares, when redeemed, may be worth more or less than original cost. As stated in the current prospectus, the Fund's Investor Class Share's annual operating expense (gross) is 1.10%. The Fund's adviser has contractually agreed to waive a portion of its fee and/or reimburse Fund expenses to limit total annual operating expenses at 0.92%, which is in effect until October 31, 2021. Other share classes may vary. The Fund charges a 2.0% redemption fee on shares redeemed within 180 days of purchase. For the most recent month-end performance, please call (877) 328-9437 or visit the Adviser's website at [www.auxierasset.com](http://www.auxierasset.com).*

**Contributors to the quarter: Our outlook on a cross section of positions with a positive impact on the portfolio for the quarter ended 6/30/2021.**

### Microsoft Corporation (MSFT)

As a tech-focused company, Microsoft has benefited from digitization and the shift to working from home that was accelerated by the pandemic. Since 2017, revenue has grown by at least 10% every quarter and that has continued this year. Microsoft Teams, the company's virtual collaboration tool, now has over 145

million daily active users around the world. This is up from just 32 million daily active users back in March of 2020. Microsoft management believes that the pandemic will forever change how people work and learn, and that their software and cloud services will enjoy improving fundamentals from this change in the long term. Azure cloud revenue has grown over 40% every quarter for well over three years now. As the second largest cloud player in the world, Microsoft's scale in the Cloud industry will be hard for smaller competitors to replicate any time soon.

<b>Top 10 Equity Holdings</b>	<b>% Assets</b>
UnitedHealth Group Inc.	6.1
Mastercard Inc.	5.8
Microsoft Corp.	5.6
Medtronic PLC	3.9
Philip Morris International	3.2
Bank of America Corp	3.2
Bank of New York Mellon Corp	2.9
Johnson & Johnson	2.9
Kroger Co.	2.9
Visa, Inc.	2.7

#### Philip Morris International, Inc. (PM)

Philip Morris is executing on their transition towards more smoke-free products. The success of their heated tobacco product IQOS has led their smoke-free portfolio to account for nearly 30% of total revenues. Management expects that heat-not-burn products will account for about 40% of total revenue by 2023. Volumes for their IQOS device are growing in the double-digit percentages every quarter. Philip Morris is targeting a compound annual growth rate for EPS of 9% from 2021 through 2023. The company maintains a strong dividend with a yield that has remained above 4% since 2018 and they have increased the payout for 12 consecutive years. It ranks as one of the top performing stocks in the market since 1926.

#### Biogen, Inc. (BIIB)

Biogen stock had an incredible quarter and was up 24.24% due to the approval of their Alzheimer's drug Aduhelm. This is the first new treatment approved for Alzheimer's in nearly two decades. Alzheimer's is the sixth leading cause of death in the US and affects more than 30 million people worldwide. Due to few treatment options for the disease, Biogen anticipates that Aduhelm will grow into a multibillion-dollar product over the next several years. Bernstein analysts estimate that Aduhelm could reach peak sales of \$10 billion, which would lead to record levels of revenue for Biogen. Along with their work on Aduhelm, Biogen will continue to invest in other areas of need such as neurodegenerative diseases and retinal disorders. The company expects to invest \$2.3 billion to \$2.4 billion into research and development in 2021. Biogen is committed to returning capital to shareholders through share repurchases as they have \$4 billion of authorized share repurchases remaining.

#### Alphabet, Inc. (GOOGL)

Alphabet continues to benefit from the strength of Google Search, which controls over 90% of the global online search market. There are over four billion internet users worldwide and Google is the dominating presence in the global online space. Alphabet owns Google.com and YouTube.com, the #1 and #2 most visited websites in the world. Google gathers large amounts of data from their users, enabling them to advertise more effectively than their competitors. Alphabet benefits from a network effect and as their userbase grows, more advertisers will be drawn to their services. They maintain a solid balance sheet with over \$120 billion in cash, allowing them to continue to invest in new products and technologies such as their cloud service which is now a top five player globally. Alphabet is also actively investing in the areas of drone delivery, autonomous vehicles and quantum computing. The company is buying back \$50 billion of their stock.

#### UnitedHealth Group, Inc. (UNH)

As the largest private health insurance provider in the US, UnitedHealth has proven to be resilient to uncertain market environments. The company also has a top three pharmacy benefits manager with OptumRx. UnitedHealth's integrated strategy has led to consistent performance with revenue growing every quarter for over 20 years now, including during the 2008 financial crisis and the COVID-19 pandemic. The company's scale and integration also create cost advantages that make it hard for smaller competitors to

take substantial market share. Analysts call for earnings per share of \$18.57 for 2021 and \$21.37 for 2022. Management is targeting 13%-16% earnings growth for the long term. UnitedHealth recently announced their plan to acquire Change Healthcare for \$13 billion, which would strengthen their digital health capabilities.

**Detractors to the quarter: Our outlook on a cross section of positions with a negative impact on the portfolio for the quarter ended 6/30/2021.**

Discovery Communications, Inc. (DISCA)

Discovery has had dramatic moves in stock price this quarter, mainly due to a major blow up of the hedge fund Archegos and the announcement of a merger with AT&T's WarnerMedia. The combined company, which should be finalized in a year, puts a current EBITDA multiple under 10x. Amazon just paid close to 40x for MGM. With lots of streaming competition, the market has been uncertain about how well Discovery and WarnerMedia will perform. However, John Malone is a major investor with an excellent track record. We have held his companies for over 20 years. We expect further consolidation in streaming with the new Warner Bros. Discovery, an attractive candidate due to their global franchise.

Johnson & Johnson (JNJ)

Though Johnson & Johnson underperformed during the quarter, the company is seeing a boost to sales and earnings as virus-related restrictions are lifted. The second quarter saw record levels of both sales and earnings thanks in large part to previously deferred medical procedures being completed. Johnson & Johnson expects to produce up to 600 million doses of its COVID vaccine in 2021 though, unlike Pfizer and Moderna, they do not expect to make a profit on the sale of the vaccine. Management has increased their full-year guidance and now expects EPS of \$9.60-\$9.70 and base business sales growth of 10.5%-11.5%. Johnson & Johnson continues to invest heavily in their future growth with one of the top 10 largest pharmaceutical pipelines in the world. The company also has a solid history of returning capital to shareholders with 59 consecutive years of dividend growth.

Mastercard, Inc. (MA)

Concern over the Delta variant of COVID-19 spreading and hampering travel has been reflected in Mastercard's performance this quarter. Cross-border transactions have suffered. However, unless lockdowns are reinstated, we don't see Mastercard's growth slowing down. They continue to be a duopoly with Visa, controlling the toll road of payments. They are relentlessly focused on the future. Mastercard's CEO was quoted saying, "If you wandered around the office and asked people, from the junior most employee, to the employee who has been here 35 years, 'what do you think Mastercard's mission is?' they will say 'killing cash.' It's embedded in everything that we're doing. And it's not mixed in with other things. Our mission is to kill cash."

Abbott Laboratories (ABT)

After having benefited from COVID testing this past year, Abbott Labs fell when it guided for lower earnings due to decreased demand in equipment. Abbott has a fortress balance sheet and has grown earnings at 17% annually over the last five years. Innovative products like the FreeStyle Libre blood glucose monitor franchise continue to drive growth. Healthcare stocks in general have lagged this year and we see many names that sell at the cheapest valuation versus the market in over 20 years, despite favorable demand demographics.

Corning Incorporated (GLW)

Corning pared back gains after having a nice 25% runup from the start of the year. Corning makes everything from the glass that is on iPhones, to pharmaceutical vials, to their largest business segment, which is focused on 5G specialized fiber, an area of strong future growth. Their advanced fiber technology is only matched by one other competitor, YOFC, who charges more for a similar product.

## In Closing

We strongly believe that investing is “the craft of the specific.” There has been such a proliferation of passive pools and ETFs that nobody truly knows what they own. The real advantage of following an active, rigorous research approach covering hundreds of individual companies and managements comes when we hit long periods of flat to declining markets. In the 20<sup>th</sup> century, the Dow went up 180-fold. However, while the market rose for 43.75 years it was down for 56.25 years. During the period 1900-1921 the Dow rose from 66 to 71, less than 10% over 21 years. Between September 1929 and December 1948, the Dow declined from 381 to 180, over 50% in 19 years. For the years 1964-1981 the Dow gained one point from 874 to 875. More recently Tokyo’s Nikkei 225 plunged from a high of 38,915 at year-end 1989 to 7,862 by March of 2003. Being passive works great in raging bull markets, but in the flat-to-down periods returns are much more dependent on well-researched individual buys. Knowing intimately what you own, what to buy and when to buy is where the years of cumulative knowledge become valuable.

We appreciate your trust.

## Jeff Auxier

*Before investing you should carefully consider the Fund’s investment objectives, risks, charges and expenses. This and other information is in the prospectus, a copy of which may be obtained by calling (877) 328-9437 or visiting the Fund’s website. Please read the prospectus carefully before you invest.*

**Fund returns (i) assume the reinvestment of all dividends and capital gain distributions and (ii) would have been lower during the period if certain fees and expenses had not been waived. Performance shown is for the Fund’s Investor Class shares; returns for other share classes will vary. Performance for Investor Class shares for periods prior to December 10, 2004 reflects performance of the applicable share class of Auxier Focus Fund, a series of Unified Series Trust (the “Predecessor Fund”). Prior to January 3, 2003, the Predecessor Fund was a series of Ameriprime Funds. The performance of the Fund’s Investor Class shares for the period prior to December 10, 2004 reflects the expenses of the Predecessor Fund.**

The Fund may invest in value and/or growth stocks. Investments in value stocks are subject to risk that their intrinsic value may never be realized and investments in growth stocks may be susceptible to rapid price swings, especially during periods of economic uncertainty. In addition, the Fund may invest in mid-sized companies which generally carry greater risk than is customarily associated with larger companies. Moreover, if the Fund's portfolio is overweighted in a sector, any negative development affecting that sector will have a greater impact on the Fund than a fund that is not overweighted in that sector. An increase in interest rates typically causes a fall in the value of a debt security (Fixed-Income Securities Risk) with corresponding changes to the Fund’s value.

Fund holdings and sector allocations are subject to change and should not be considered a recommendation to buy or sell any security.

Foreside Fund Services, LLC, distributor.

*The S&P 500 Index is a broad-based, unmanaged measurement of changes in stock market conditions based on 500 market-capitalization-weighted widely held common stocks. The Dow Jones Industrial Average is a price weighted index designed to represent the stock performance of large, well-known U.S. companies within the utilities industry. The S&P 500 Equal Weight Index (EWI) is the equal-weight version of the*

widely used S&P 500. The index includes the same constituents as the capitalization weighted S&P 500, but each company in the S&P 500 EWI is allocated a fixed weight (0.2%) of the index total at each quarterly rebalance. The MSCI Emerging Market Index captures mid and large caps across more than two dozen emerging market countries. The index is a float-adjusted market capitalization index and represents 13% of global market capitalization. The 60/40 Hybrid of S&P 500 and Bloomberg Barclays U.S. Aggregate Bond Index is a blend of 60% S&P 500 Composite Index and 40% Barclays U.S. Aggregate Bond Index, as calculated by the adviser, and is not available for direct investment. The Bloomberg Barclays US Aggregate Bond Index, or the Agg, is a broad base, market capitalization-weighted bond market index representing intermediate term investment grade bonds traded in the United States. The Russell 1000 Value Index refers to a composite of large and mid-cap companies located in the United States that also exhibit a value probability. The Russell 1000 Growth Index measures the performance of the large cap growth segment of the US equity universe. It includes those Russell 1000 companies with higher price-to-book ratios and higher forecasted growth values. One cannot invest directly in an index or average.

EBITDA, or earnings before interest, taxes, depreciation, and amortization, is a measure of a company's overall financial performance and is used as an alternative to net income in some circumstances.

Earnings per share (EPS) is calculated as a company's profit divided by the outstanding shares of its common stock.

The price-to-earnings ratio (P/E ratio) is the ratio for valuing a company that measures its current share price relative to its per-share earnings (EPS).

The Consumer Price Index (CPI) is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food, and medical care.

Return on invested capital (ROIC) is a calculation used to assess a company's efficiency at allocating the capital under its control to profitable investments.

*The views in this shareholder letter were those of the Fund Manager as of the letter's publication date and may not reflect his views on the date this letter is first distributed or anytime thereafter. These views are intended to assist readers in understanding the Fund's investment methodology and do not constitute investment advice.*