LESA
SROUFE&CO INC.
VALUE ADVISORS

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First Quarter Update and Outlook

The economy continued to recover in the first quarter of the year, as the U.S. government continued to take on debt to replenish wallets following the Covid fallout. The $5 trillion in fiscal stimulus policies enacted over the past year have resulted in the largest transfer of wealth from the U.S. government to individuals in U.S. history. Federal debt is expected to reach 102% of GDP by year end, up from 79% just two years ago. The desired effect is working: consumer spending is up, investment spending is up, jobs have rebounded, as have interest rates and the stock market. Over the past year, the broad S&P 500 stock market index has rebounded by a breathtaking 56%. U.S. Treasury 10-year interest rates have risen from 70 basis points to 170 basis points.

So much free money combined with Covid related supply chain problems are resulting in higher prices for everything from food and gas to computer chips. For the first time in 40 years, it is possible that interest rates are headed materially higher. If so, the price to earnings ratio of the S&P 500 will seem expensive at its current 23 times estimated 2021 earnings. Over the past several months, expensive growth stocks have underperformed the cheaper value stocks, which more often represent the broader economy, including commodities and cyclical companies. The LSC portfolios have benefited as investors have turned their attention to those companies that will rebound from the reopening of the economy.

One consequence of cash payments to the general public has been the higher trading volume and volatility, especially among low priced stocks. Early in the quarter we sold our shares in Nokia, as traders had bid the stock up well beyond its near-term fair value. A subsequent sharp decline in the stock price allowed us to repurchase Nokia at significantly below our earlier sale price. Longer term, Nokia's participation in the 5G upgrade in telecom equipment worldwide should add to earnings. We also purchased International Seaways, a U.S. based petroleum transporter and Pfizer, the worldwide pharmaceutical company, most recently known for its successful Covid-19 vaccine.

Early in the quarter, we divested China Mobile, the best financed and largest telecom company in the world. Due to political pressure from the U.S. government, the New York Stock Exchange delisted the Chinese company. We also sold the remainder of our Hawaiian Holdings position as investors have sharply bid up travel and leisure stocks as beneficiaries of the reopening of the economy. We sold Avista, the electric and gas utility, because the stock's valuation exceeded our price target.

We believe investors' attention will soon turn to the prospect of higher U.S. taxes on all levels. Fiscal caution should follow the recent federal spending spree as the Covid pandemic ends. So, while the economy may roar, future income growth may be muted, especially for companies that had already benefitted from the work from home phenomena now slowly receding. Companies that have the ability to raise prices, benefit from inflationary pressures and a reopening of the economy stand to continue to lead the general stock market. Our portfolios are positioned for that likelihood.

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