CORDA

TOGETHER WE'RE INVESTED

Back to the New Normal

December 31, 2020

As we head into the New Year, in addition to reflecting on the past, it also seems obligatory to drag out our crystal ball to help set a course for the upcoming year. Our customary optimism about owning high quality, cash flowing, and shareholder friendly businesses at the right price is a permanent feature to our investment plan, virtually set-in stone. However, you can be assured we maintain a cautious mindset about how to deploy capital in an ever-changing environment. This past year, more than one client has reminded us how in our letter 12 months ago we predicted a decline at some point, but it was going to be from something that nobody was talking about – and lo and behold, we wish we had not been so on point with that comment!

Our sense for 2021 is that we will have our hands full as we grapple with a change in administration, the ongoing impact from the pandemic and the ramifications of ever larger budget deficits at the federal and state levels. Additional speed bumps include the fear of interest rates moving too high/too quickly because of massive stimulus programs via Congress and the Federal Reserve, while others argue that a deflationary bust is still ahead. Other worries are frothiness in sections of the capital market, with IPO's and SPACs (special purpose acquisition companies) shooting higher in spectacular fashion, crypto currencies garnering renewed attention, and continued strained relations with China and Russia. One could decide the world is fragile and fraught with risk and maybe just too complex, but we view the template with excitement and opportunity.

What is or is not priced into the market is always the question. Frankly, our biggest worry now is that in some corners of the market there is excess optimism, and the resulting respective shares are priced for perfection. The caveat is to be careful as we move into 2021 and prepare for volatility as the market swings from one extreme to the other. But isn't that always the case?

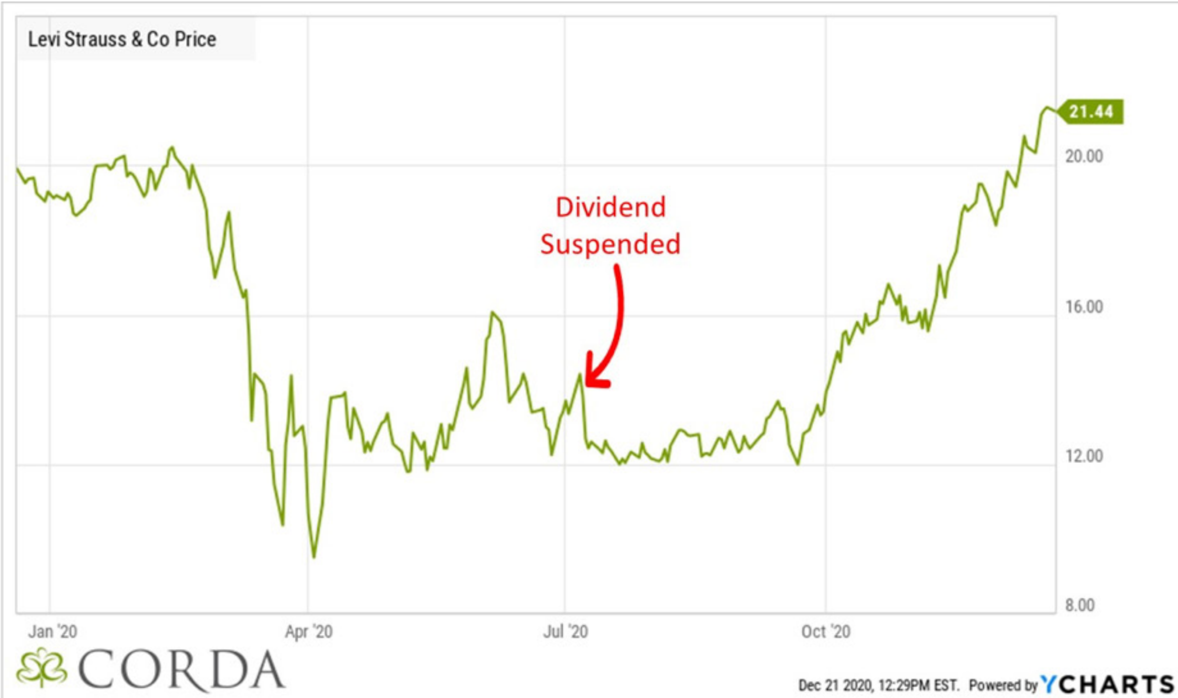
Preparing yourself for unpredictability should be standard operating procedure by now, but we have seen how investors let their emotions get the best of them and sometimes make regrettable decisions when the stakes are highest. For example, if you had been able to visit our office this past March…we were active buyers – putting more dollars into the market in one month than we had for the entire full year of 2019. We often speak in terms of temporary losses, and we know for certain when folks were scrambling for toilet paper, they were tested like never before with the urge to sell their stakes in some of America's best businesses. Sometimes the hardest thing to do is nothing. Even Warren Buffett unloaded some holdings during the 1st & 2nd quarters of the year, and he might like to take those trades back. We did some "sell to buy" trades (sell one position and immediately put the proceeds into another business), but the jury verdict on those trades won't be known for years.

The biggest takeaway for the year is how our companies were able to continue to pay dividends on schedule. In the depth of the crisis during March, we again thoroughly reviewed our holdings and focused exclusively on each company's ability to continue to pay dividends. We concluded at that time we might see eight of our businesses either reducing or suspending their dividends. Even in the face of that potential adverse event, we determined the share prices had already discounted much of the worst-case scenario and if we were to hold, we would see higher share prices down the road. Therefore, we held firmly to those businesses we projected to be at the highest risk of a dividend cut. Fast forward nine months later, only four of the original projected eight have cut or reduced those dividends. Incidentally, had we sold those four companies on or near when they made those dividend changes, we would have sold at or near the lows.

The good news, 18 of our companies have raised their dividends in calendar year 2020 and we project a continued streak of further hikes in the years ahead. If there is one thing our crystal ball is pretty good at predicting, it is those dividends!

We think it is worthwhile to review the share price action of the companies that reduced their dividends. Here are the four over the last 12 months:

One Year Time Frame:


Levi Strauss & Co Price
21.44
20.00
16.00
12.00
8.00
Dividend
Suspended
Jan '20
Apr '20
Jul '20
Oct '20
CORDA
Dec 21 2020, 12:29PM EST. Powered by YCHARTS


Simon Property Group Inc Price
150.00
120.00
90.00
83.48
60.00
Dividend Cut
Jan '20
Apr '20
Jul '20
Oct '20
CORDA
Dec 21 2020, 12:31PM EST. Powered by YCHARTS

There is certainly plenty of room for appreciation in many of these businesses, and we monitor them each day to see if they remain on track. Fortunately, the benefit to a diversified portfolio with exposure to so many different sectors including consumer staples, pharmaceuticals, telecom, technology, materials, and the industrials allows us to forge ahead even when groups like real estate and banking are temporarily lagging. We have a variety of businesses operating across many industry groups and by design, not all of them will be rising or falling in unison. As you know, many times the laggards propel the portfolio forward in future time periods. We are of firm conviction that is what is ahead in '21 and '22.

One significant change that has occurred since March when the Fed announced, "unlimited resources if necessary", and its messaging around inflation and unemployment – signaling that low interest rates could be with us for some time. In real time, it means interest rates at the short end of the curve are virtually zero and even if you try to extend out five or more years, you might find something over 1%, but it's probably not investment grade rated, i.e., safe! If there is ever the specter of inflation, or rates rise because the dollar is depreciating, or investors demand higher yields because of large current deficits or there is even more stimulus spending from Congress or the White House - those holding fixed income for safety and yield may be in for a rude awakening. Be wary of high rates on any fixed income securities that you own today. Frankly, there may be more intermediate term risk in bonds than stocks! Here is one to ponder: You can buy bonds issued by PepsiCo with a maturity in 2040. You will get about 2% per year holding for those twenty years. At the same time, you can buy Pepsi common stock at the current price and its dividend yield is 2.8%. Which one do you think will provide the better investment return over the next twenty years? Maybe take that same thought and apply it to the risk free 10-year U.S. Treasury bond paying about 0.90% per year for the next ten years. Do you think that bond will out or under-perform the broad CORDA portfolio which yields 3% or more?!

For any allocation towards preserving capital (not subject to inflation) in the near term, we advocate staying in high quality short duration bonds. If interest rates move higher, it can be viewed positively in the following three ways: 1. It means the stress across the economy and in the capital markets of a disinflationary environment has diminished 2. Generally higher rates will be accompanied by stronger or faster GDP growth rates which translates into increased corporate sales and profits, and 3. Those with fixed income needs will achieve higher rates of the return on their capital in the future. Wouldn't it be great to achieve a "modest" return on our more secure assets?! So, should you hear about higher interest rates or the Federal Reserve Bank raising rates in 2022 or 2023, that should not directly correlate to a negative stock market outcome. And for those who do need safe yield in the short run, maybe one day we will be able to achieve it in fixed income again! Win Win!

Dividends, capital appreciation, and staying the course:

Whether your goal is to provide for retirement, legacy, education, or peace of mind, CORDA's long-term philosophy is to successfully grow your capital by owning the highest quality, financially strong, iconic, durable, and shareowner friendly businesses with the financial discipline to increase their dividends over time. We believe our philosophy is a powerful prescription that should lead to good results. We view it as the surest path towards success and our own capital is deployed right alongside yours in a commitment to participate wholly in your outcome.

The vagaries of the market will create periods of exuberance when one should stand aside and watch and wait, while at other times, when fear is more palpable, one should be a buyer. We experienced both of those scenarios in the past 12 months! There is a middle ground between the two extremes where we like to choose our skirmishes. The "buy low and sell high" strategy sounds simple to replicate, but few do it successfully over time. The annual Dalbar study, which we have highlighted in previous updates, proves empirically that many investors do the exact opposite. This behavior was on full display in 2020 and will without a doubt be re-enacted in future time periods. The market is not a rational being. Successful investors will use the manic-depressive state of the markets to their advantage!

What does this mean? A newer investor or someone with large cash holdings wanting to invest should act prudently and judiciously as we enter 2021. Some sectors and individual share prices seem over-heated, while some sectors and individual stocks are still trading at reasonable valuations. Holding some cash in reserve as the market hits new highs is our recommendation. There will be the inevitable correction, and when that occurs, it will be a better time to move more aggressively with cash into stocks.

Here, again, is a rundown of CORDA's investing principles:

1. Price is an essential factor when assessing value.
2. Try to determine what a company is worth.
3. Book value is an important feature. Attempting to forecast earnings is more difficult.
4. Remember you do not own slips of paper but shares of a business.
5. Have patience, the odds of picking the low point in any period are a million to one.
6. Have the courage of your conviction; the crowd, public and media will try to shake your faith.
7. Fully accept there is no certainty, and you can be wrong but look for blind spots.

8. Try to buy closer to lows than highs.
9. Do not be in a hurry to sell; just because share price has risen 50% or more does not mean a stock should be sold.
10. Keep in mind overall market PE, interest rates, optimism/pessimism, overall market levels.
11. Assets change slowly. Earnings can change rapidly at any time...so buy assets at a discount.
12. Watch and learn from other successful investors.
13. Fear and greed are the worst emotions.... try to stay grounded. It is never as good as it appears and never as bad either.
14. Be careful of leverage, in your own portfolio or that of the businesses you own.
15. Have a philosophy and stick to it.

In closing, the key as we move into 2021 is to expect the unpredictable and to keep your laser-like focus on the rewards possible for you when you own high quality companies at the right price. The dividend and interest income will sustain you in the near term and the growth of your principal over time will likely help you achieve financial security. Be wary of and careful with parts of the market or even the "hot tip" from your neighbor as investor behavior is again exhibiting signs of too much enthusiasm. It is the exact opposite of where investors were this past March and April.

We thank you for your commitment to the value, contrarian, and growth and income strategy that we have put in place for you. Please let us know if anything has changed regarding your financial plan. Also, for your safety, both CORDA and our custodians require your verbal instructions to move money from one location to the next. In an age where cyber security is paramount, we hope you understand that we cannot act upon any email or voice messages and our requirement is to verbally confirm instructions from you. This is all for your safety and our serious intent to protect your savings.

With that, our sincere wishes for a wonderful 2021 and we are looking forward to a pleasing year and hopefully a nice long string of years ahead that are quiet, safe, and gentle. We hope you can reconnect with family & friends and get in some long overdue trips! Enjoy!!

All the best from the entire CORDA Team.

Bonner C. Barnes John Schloegel Brian Raupp Dustin Slater