"Two roads diverged in a wood, and I—
I took the one less traveled by,
And that has made all the difference."

–Robert Frost, "The Road Not Taken"

September 24, 2019

To: Queens Oak Clients and Friends

Re: **ROCKETS or RAILS**

Early in my investment career as a fund manager, circa the late 1990's, I recall the daily droves of Wall Street analysts pitching their most beloved buy-rated stocks; rarely if ever were there any sell-rated or even hold-rated stocks, but that's another matter entirely. Once, I recall two sell-side research analysts visiting our shop. The first, a telecom analyst coming in to pitch ideas like Nokia, Ericson, and a slew of other once high-flying tech and telecom companies. The second, a rail analyst, discussing the hub and spoke model and freight car loadings and recommending the likes of Kansas City Southern and Union Pacific. The former convened in our impressive plush conference room full of eager buy-side portfolio managers and analysts pulling in chairs from adjoining offices, enamored with the industry disruption impacting the traditional carriers and the future secular growth stories unfolding in China and India. Meanwhile, the latter held in a near broom closet-sized office attracted two— me and a semi-retired portfolio manager discussing locomotive topics like train speed and terminal car dwell. It was around this time, that I knew I ought to take the "road less traveled" looking for strong businesses with economic "moats" and selling at reasonable discounts, rather than following the "lemmings off the cliff" of momentum investing, particularly if I wanted to make money in the long run.

This story was brought home most recently when I overheard an investor at a gathering expressing their preference "to invest in rocket ships not old economy stocks." Truth be told, we do not currently own any rail, rocket, or space stocks. However, I think you understand the investment analogy. "Rails" are the quintessential value stock providing stability and steady dividend income with high barriers to entry, and "rockets" might be considered a momentum stock focused on growth and innovation. With the exception of the late 1990's when the phrase "Is value dead?" became fashionable, today "rockets" are as expensive relative to "rails" as they have been since the Nifty Fifty era in the 1960's and 70's. Although, avoiding "value traps" remains a priority, value stocks relative to growth stocks have never been more attractive.

However, as the market enthusiasm for some growth stocks will likely begin to fade, we still believe large cap domestic equities remain the most attractive asset class but with an emphasis on quality and valuation since we are nearly eleven years into the economic recovery. We have selective allocations to commodities

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including gold, emerging and frontier markets, and alternative investments that provide diversification benefits and offer opportunity if inflation ever returns or a flight to safety unfolds due to geopolitical risks. Likewise, with fixed income we are focused on higher quality and avoiding some of the riskier areas such as junk bonds and European debt. The odds of a U.S. recession remain low, but we recognize that a slowdown is inevitable. Nevertheless, we would avoid the pitfalls of market timing, realizing that the fourth quarter has historically brought volatility but positive returns to boot. In short, we remain vigilant on quality and focused on value driven opportunities in public markets while maintaining defensive positions in taxable and municipal intermediated bonds and low volatility liquid alternatives.

This summer afforded wonderful serendipity marking 50 years since the Apollo 11 landed on the moon and America winning the "space race" that would foreshadow the collapse of the Soviet Union and communism some decades later. Meanwhile, an equally dazzling engineering achievement occurred 150 years ago with the anniversary of the Golden Spike linking the Union and Central Pacific railroads in Promontory Summit, Utah creating the first transcontinental railroad across the United States. Both amazing feats involved hundreds of thousands of American workers as well as Chinese and other immigrants working together and serving as a reminder of our national spirit, ingenuity, and unity. Perhaps, I am a bit too sentimental about the rail industry; my dad worked 19 years at Southern Railway which would eventually merge into Norfolk Southern; but as Warren Buffett says, railroads are a "bet on the country" with exposure to so many industries beyond coal including automotive, agriculture, chemicals, forest products, etc.— a bet that seems worth making.

Therefore, when the newest version of Hasbro's famed Monopoly game rolled out, Ms. Monopoly, I was delighted to see an edition recognizing women entrepreneurs and inventors but dismayed to learn the longstanding railroad properties have been dropped in favor of ride share properties (e.g. Uber and Lyft) and water works and electric company replaced with Wi-Fi. So, despite profitless companies being in vogue and highly valued, let's not get too carried away with investing in cannabis, blockchain technology, robots and space travel despite the allure; as investments we favor the metaphorical "rails"— those more mundane companies in sectors from industrials to technology with solid business models and healthy profit margins selling at reasonable valuations.

As always, we appreciate your continued support of our firm. We have superb clients that are our close friends, staunch supporters, and trusted partners in the financial markets. In the meantime, do not hesitate to contact us if you have any questions or concerns during these periods of tough trade talks and inverted yield curves. Finally, we wish you all a healthy and prosperous end to 2019, and please remember we are here for you as we head into the election year that will undoubtedly have no shortage of noise and confusion to sift through.

Sincerely,

Eric M. Teal
Managing Partner
Chief Investment Officer