

Mott Capital Management

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We survived and flourished in 2020. That is the good news.

For the year, the Mott Capital Management Thematic Growth Composite climbed by 25.4% net of fees and transaction costs, easily beating the S&P 500 Total Return Index gain of 18.4%, including dividends. For the second year in a row, we outperformed the Total Return Index, and at the same time strengthened our relative performance over the past three years, rising by 16.2% vs. the S&P 500 Total Return gain of 14.2% on an annualized basis.

Thematic Growth Composite Performance

Thematic Growth Composite	S&P 500 Total Return Index	S&P 500 Index
+25.4%	+18.4%	+16.3%

The not so good news is that for the last few quarters, these letters have grown harder to write, not because I don't have good news to report (which, as you see I do), but rather because trying to put together a rational explanation of how markets act has become increasingly difficult.

Valuations in the market are very stretched, advancing to levels not seen since the early 2000's. Monetary and fiscal actions tied to COVID 19 including historically low interest rates and stimulus checks drive equity prices higher, while traditional financial ratio analysis and fundamental business drivers are more and more put to the side. This is not a good thing.

My long term, up-close observation of the markets, starting when I was a teenager in the late 1990's, makes it very difficult to be excited about the seeming euphoria of the current market period. In the end, we know that when the music stops and the chair is pulled, the drop can be painful. It leaves me in an awkward position because my basic investment strategy is picking ideas for the long-term, based on trends that are likely to change the way we live over a generational evolution. I have been pretty successful using this model. But when stocks are attracting valuations based on aggressive forward projections, buying for the future is increasingly tricky since today's market is trading as if that aggressive (and unlikely) future were already here.

Portfolio Review

The significant gains in 2020 were attributable to Tesla, which surged by more than eightfold. It seems hard to believe, but the stock made up 6 years of underperformance and then some all-in-one year. I will be honest, I'm not sure we will have an experience like it again. The stock reached a very high concentration level in the portfolio given the outsized gains, which I was not always comfortable with given the stock's volatility. The run-up in price led to the stock being trimmed back on a few occasions when it reached 20% of the overall portfolio value.

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Tesla has surged roughly another 20% in 2021, which has led it to hit 20% of the portfolio value. As a result, I trimmed the position again. It now accounts for about 15% of individual portfolios as of this letter. If it should reach 20% again, I will assess the situation and manage the risk accordingly.

Company	4Q % CHG	2020 % Chg
Tesla Inc	64.49%	743.44%
Apple Inc	14.58%	80.75%
Microsoft Corp	5.75%	41.04%
Alphabet Inc	19.59%	30.85%
ACADIA Pharmaceuticals Inc	29.60%	24.96%
Mastercard Inc	5.55%	19.54%
Visa Inc	9.38%	16.41%
Unilever PLC	-2.14%	5.58%
Verizon Communications Inc	-1.24%	-4.32%

Apple, Microsoft, and Alphabet also surged this year, as investors flocked to stocks that offered predictable cash flow and earnings growth streams. Additionally, the work from home movement led to technology stocks overall having outsized gains. I anticipate these three companies will remain critical components in the portfolio for the foreseeable future.

Verizon finished the year lower by around 4.3% and has been a hard holding over the past 6 years. It has gone nowhere and has been the one stock I struggle with. However, 5G has finally arrived. If 5G can deliver on the promise I think it can, then Verizon should eventually come around. I remain hopeful.

The Situation Today

Currently, the portfolio has a strong defensive position, with cash at 30-35% of the overall balance. Several stocks remain attractive, but it is hard to justify buying them at current levels with a longer-term view. Although the economic environment is likely to improve considerably in the second half of 2021, any change in the ultra-low-interest rate environment certainly cannot be ruled out. While I do not see rates scaling up to pre-pandemic levels anytime soon, a simple move higher in the 10-year rate of 40-50 bps could easily lead to a contraction of between 15% and 20% in the S&P 500, and perhaps more in many overvalued technology stocks.

Since our core focus is looking for themes that significantly disrupt or change how we live, most of the stocks I have researched fall into the overvalued camp currently. As long as we can continue to outperform or remain in line with the broader indexes, we are better off taking our time and picking our spots to put money to work rather than feeling the need, or the pressure, to chase the market higher. I don't want to be caught in a replay of the irrational exuberance of the late 1990's.

Looking Forward

I expect plenty of disruption in 2021. The most significant risk is rising rates on the 10-year Treasury and its potential for climbing to around 1.5%, and the concomitant inevitable fears of inflation. On this point, I don't see inflation actually returning in the foreseeable future. The current pace of money printing and GDP growth is so misaligned that inflation cannot emerge. For inflation to spark, GDP growth needs to be more than that of the money supply; that simply will not happen this year, or likely any time soon.

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There will, though, be some false signals. Remember, the first half of 2020 saw commodity prices and demand collapse, and that means when periodic 2021 readings start to compare against prices from 2020, it will appear as if inflation is hot. I believe that illusion will spark the rise in the 10-year rate, potentially disrupting the current bull run in the equity market.

Because of these market influences, I expect the first half of 2021 to be turbulent as the market tries to grapple with inflation fears and higher rates. I suspect the second half of 2021 will be a recovery phase for the equity market, as inflation readings subside.

But then, I just re-read our 2019 fourth quarter letter. Predicting the future is never a science. You can't know what news the world may deliver that upsets all your reasonable thoughts.

As always, I will work my hardest to understand the current investment landscape while identifying new long-term thematic strategies shaping generational and demographic shifts.

Until next time,

-Mike



Year End	Total Assets		Number of Accounts	Composite Performance	S&P 500 Total Return	Annualized 3-Year Standard Deviation**		Internal Composite Dispersion
	Firm	Composite		Net		Composite	Benchmark	
2020	2,720	2,688	19	25.43%	18.40%	19.93%	18.53%	2.57%
2019	2,470	2,120	18	35.85%	31.49%	12.24%	11.93%	1.65%
2018	1,969	1,605	20	-7.98%	-4.38%	12.46%	10.80%	0.99%
2017	2,118	1,716	20	18.77%	21.83%	12.70%	9.92%	0.90%
2016	1,717	1,377	17	-2.10%	11.96%	-	-	0.90%
2015	1,681	1,325	17	1.52%	1.38%	-	-	0.60%
2014†	1,026	628	8	3.82%	7.60%	-	-	N.A.

N.A. - Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year.

† Performance reflects the non-annualized performance from 8/1/2014 to 12/31/2014.

** For periods with less than 36 months of composite performance, no 3-year ex-post standard deviation measurement is available.

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strategy of different market capitalizations, which is approximately divided equally among three sectors. The Core Growth sector includes large multi-national companies, the Growth Sector includes mid- to large-cap companies, and the Aggressive Growth sector includes small- to mid-cap companies. The strategy is concentrated, and typically includes approximately 20 positions, and 5% cash. The strategy only invests in stocks, ADRs, and ETFs denominated in USD. The All-Cap Growth Composite was created June 2015. The inception date of the strategy is August 1, 2014. The S&P 500 is a free-float capitalization-weighted index of 500 large-cap common stocks actively traded in the United States. The index is shown as a general market indicator, and may not reflect the same exposures as the composite. The investment management fee schedule for the composite is 2% on the first \$250,000, 1.5% on the next \$750,000, and 1.0% on the remainder. Actual investment advisory fees incurred by clients may vary. Further information regarding investment advisory fees is described in Part II of the firm's Form ADV. Past performance is not indicative of future results. The U.S. Dollar is the currency used to express performance. Performance shown represents total returns that include income, realized and unrealized gains and losses. Net of fee performance was calculated using actual fees. Composite performance is presented net of foreign withholding taxes on dividends, interest income, and capital gains. Withholding taxes may vary according to the investor's domicile. Policies for valuing portfolios, calculating performance, and preparing GIPS reports are available upon request. The annual composite dispersion presented is an asset-weighted standard deviation calculated using accounts in the composite the entire year. The 3-Year Standard Deviation represents the annualized standard deviation of actual composite and benchmark returns, using the rolling 36-months ended each year-end. The 3-Year ex-post Standard Deviation of composite and benchmark returns is not presented because the composite strategy has less than three years of history.