Eleon Capital Management Ltd.

- MARKET OUTLOOK -

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*H*oward Marks is the co-founder of Oaktree Capital Management. During the great financial recession (GFR) of 2008, he cemented his reputation when Oaktree raised $10.9 billion, the largest distressed debt fund in history, to buy distressed assets, which subsequently yielded above-average returns for their investors. In his latest memo, "*Taking the temperature*", he described five instances where the investing climate was characterised by the extreme investor over-optimism or pessimism, in which he made market calls which paid off handsomely – he said: "once in a while – once or twice in a decade – markets go so high or so low that the argument for action is compelling and the probability of being right is high."

These periods included:

1)The tech bubble in Jan 2000;

2) late 2004 to mid-2007;

3) late 2008 post the GFR;

4) March 2012, and

5) March 2020 the start of the COVID pandemic.

*H*e went on to explain that above-average performance, in his opinion, cannot simply be achieved through the analysis of company financials or macroeconomic projections. It is necessary to understand the investor psychology driving market prices at a point in time, which results in significant distortions between asset prices and their value and in turn can be invested in with much lower risk.

Two observations stood out in particular:

*T*he first was that these market calls proved to be correct and cemented his reputation largely because the market dislocations due to investor sentiment were so enormous that they created significant gaps between price and value and hence lowered the risk of investing.

The second is that such significant market dislocations do not happen very often – these were five calls out of a fifty-year investment career (although he did qualify that statement in noting that it took him a very long time to understand the 'markets temperature' and having the conviction to act).

Upon further reflection, one can observe many similarities regarding extreme market dislocations upon inspection of Berkshire Hathaway's investments. Charlie Munger said: "If you took our top fifteen decisions out, we'd have a pretty average record. It wasn't hyperactivity, but a hell of a lot of patience. You stuck to your principles and when opportunities came along, you pounced on them with vigour." Berkshire purchased GEICO following its share price collapse as a result of rapid growth at an underwriting loss; Coca-Cola following the disastrous launch of New Coke; American Express following the salad oil scandal; Washington Post due to the ramifications of exposing the Watergate Scandal; Apple when most analysts were concerned on the sustainability of its margins and growth prospects of the iPhone. In each instance, stock-specific market dislocations created extreme gaps between price and value.

Another legendary investor Peter Lynch of the Fidelity Magellan Fund said:

"You only need a few good stocks in your lifetime. I mean how many times do you need a stock to go up tenfold to make a lot of money? Not a lot."

Once again, Peter Lynch looked for stocks with good growth prospects and suitable ROIC trading at a significant discount to their intrinsic value and then held them for a long-time horizon to allow the power of compound interest to materialise. It is, therefore, evident from the above observation that:

a. Good investment opportunities (significant gaps between price *and value and hence the low risk) are rare and occur infrequently.*

b. They usually present themselves when extreme market dislocations occur at the macro or at the stock-specific level.

c. When they do present themselves, investors need the knowledge, conviction and temperament to invest even though their hypothesis is contra to that of the market; and

d. They usually present themselves when extreme market dislocations occur at the macro or at the stock-specific level.

Market dislocations are periods when the prices of assets deviate significantly from their intrinsic values due to external shocks, liquidity constraints, or information asymmetry. Market dislocations can create opportunities for investors who can identify undervalued or overvalued assets and exploit price discrepancies. However, investing in market dislocations also involves higher risks and uncertainties, as well as the need for patience and conviction. Therefore, investors should conduct thorough research and analysis before entering or exiting a position and diversify their portfolio to reduce their exposure to specific risks.

In conclusion, understanding market psychology and identifying investment opportunities during market dislocations are important skills for investors who want to achieve long-term success in the financial markets. By applying these concepts, investors can enhance their decision-making process, improve their performance, and avoid costly mistakes.

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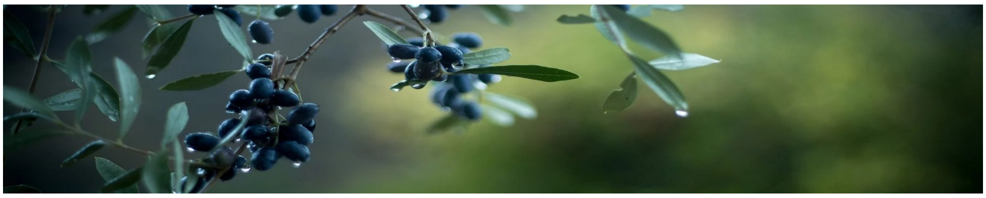

Strong Roots, Sustainable Growth

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