

CHARON SPECIAL SITUATIONS GROUP

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#### Notable Trends

- 1) Equities and bonds both dropped in unison – though uncommon, the correlation makes sense given that fear of inflation is causing the sell-off in stocks.
- 2) Increased vertical consolidation has been seen recently in aerospace & defense sector to address pricing and product mix – multiple deals in the pipeline.
- 3) There has been increasing hedge fund activism, specifically in “sum of the part investment opportunities whose value can be realized via break-up or spin-out.”

## Weekly Recap

10/08/2018 – 10/14/2018

*“The Fed’s going to raise interest rates in December unless something really bad happens to the stock market. It seems quite likely that the 30-year will be headed towards 4% in the not too distant future and that would mean a steeper yield curve. The movement now in the long end has been occurring faster than the changes in the perception of the Fed, which hasn’t changed much. The long end is going up by 50 basis points in a month, which is a pretty quick annual rate and will probably continue as long as we have this situation with moving higher rates.”*

- Jeffrey Gundlach, CEO of DoubleLine Capital ([Forbes](#))

### MARKET SUMMARY

- Equities had the worst weekly performance in seven months following a selloff from the rise in long-dated interest rates (10Y Treasury rose to seven-year high above 3.26%). ([MarketWatch](#))
  - Bob Prince, Co-CIO of Bridgewater believes investors have realized that growth and earnings have reached an inflection point as optimism has already been priced into equity valuations, causing more pressure. ([FT](#))
  - Wells Fargo, J.P. Morgan, and Citi posted double-digit percentage gains in profit as a result of higher rates and lower taxes, indicating a strong economy / good consumer activity and topping estimates. ([LA Times](#))
- Investment grade bond funds had outflows of \$7.5B followed by \$6.1B from junk bond funds; despite this, yields haven’t risen compared with recent years and there were bigger outflows during the February correction which indicates that this isn’t a systemic trend. ([WSJ](#))
  - BBBs make up more than half of IG index and BB (the best junk rating) has a high share of the junk index since risky companies have been looking to leveraged loans.

### DEALS & CORPORATE ACTIONS

#### October 8, 2018

- Airbus has assigned Guillaume Faury, head of its plane-making unit as the next CEO pending shareholder approval. Stock lowered after the announcement – issues to be addressed include backlog, delivery targets, and bribery investigations. ([WSJ](#))
- SEC has decided to enforce a five-year-old cybersecurity rule in a cease-and-desist against Voya Financial. The Identity Theft Red Flags Rule requires up-to-date programs that alert warnings to potential data breaches. ([NYT](#))
- Terrence Hahn has been removed as Axalta CEO after a month following a probe into undisclosed conduct unrelated to financial matters. Berkshire Hathaway holds a 10% stake in the automotive paint supplier. ([Bloomberg](#))
- Triun Fund Management is considering a takeover of Papa John’s. The pizza company has been undergoing internal fights with the ousted founder John Schnatter, who remains on the board and owns 30% of shares. ([WSJ](#))
- With more and more ESG scrutiny, unions and interest groups have been successfully lobbying pension funds to confront PE firms on human impact issues such as denying severance for laid-off workers, lack of diversity, and foreclosures. ([NYT](#))

#### October 9, 2018

- Bill Ackman unveiled his \$900MM bet on Starbucks. Ackman believes that same store sales and valuations will revert to historical averages and that China will provide a significant growth opportunity. ([CNBC](#))
- Boeing completed its acquisition of KLX, an aerospace parts distributor, in an effort to enhance its services business. The acquisition is a reflection of growing consolidation in the space. ([PR Newswire](#))
- Blackstone and Hellman & Friedman are exploring a bid with CPPIB and GIC into Nielsen which is facing activist pressure from Elliott. Carlyle is also interested, and Nielsen has also explored potentially merging with Kantar, a WPP division. ([FT](#))
- Triun Fund Management disclosed a 2.9% stake in PPG, a Pittsburgh based paint company. The underperforming paint maker failed in acquiring Akzo Nobel last year. ([WSJ](#))

#### October 10, 2018

- Justice Department approved CVS Aetna merger on the condition that Aetna sells its private Medicare drug plans ([NYT](#))
- TransDigm is set to acquire Esterline Technologies in a \$4BN all cash acquisition. This prices Esterline at a 38% premium to its current market value. This follows a long list of M&A activities in the aerospace industry. ([Esterline](#))

#### October 11, 2018

#### October 12, 2018

- Sears is seeking buyers as it heads toward an imminent bankruptcy filing. The company hopes to maintain operations until Christmas and expects to do so through a \$300-500MM raise. Eddie Lampert has already been liquidating parts of the business and trying to buy units such as Kenmore ([CNBC](#)).

#### October 13, 2018

#### October 14, 2018

- Harris Corp and L3 Technologies announce largest-ever defense merger of equals which would end up ranking sixth among US contractors by revenue as Pentagon increases spending after five years of budget cuts. ([WSJ](#))

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