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INFL progress report

"Well, actually, to be honest with you," Murray Stahl, co-founder, chairman, chief executive officer and chief investment officer of Horizon Kinetics, sponsor of the Inflation Beneficiaries Exchange Traded Fund (INFL on the Big Board's Arca subsidiary), was saying Monday morning, "I thought it would do better. I don't mean that in a money-raising sense"—the ETF has garnered $680 million in nine months, including a bit of your editor's money. "I mean it in a performance sense."

Price appreciation of not-quite 20% in a tad more than nine months wouldn't be everyone's idea of a letdown, but Stahl says he expects much bigger things from the 38 names in the INFL portfolio. As for oil and gas, to which the fund has a 20%-plus exposure, he reiterates his contention of last autumn (*Grant's*, Nov. 27, 2020), that persistent under-investment—not even enough to replace reserves, let alone to expand them—makes hydrocarbons a "once-in-a-lifetime investment opportunity."

Global demand for oil and gas "is at an all-time record," Stahl went on, "and that's while we still are in the coronavirus crisis. . . . So basically, maybe it's a terrible thing to say, but there's very little alternative now to oil and gas as a fuel for civilization. It's just the way it is."

Stahl is more adamant in characterizing today's price flare-up as deep-rooted and persistent than the Federal Reserve is in calling it shallow and transitory. How best to exploit it? Operating leverage and pricing power are the unifying analytical themes of a portfolio that encompasses securities and commodities exchanges (for instance, Deutsche Boerse A.G.), real estate (CBRE Group, Inc.), timber (Weyerhaeuser Co.), minerals (e.g., Dochester Minerals, L.P.) insurance (Marsh & McLennan Cos., Inc.) and pharmaceuticals (Charles River Laboratories International, Inc., the fund's top holding) as well as the old currency debasement standbys, gold and silver.

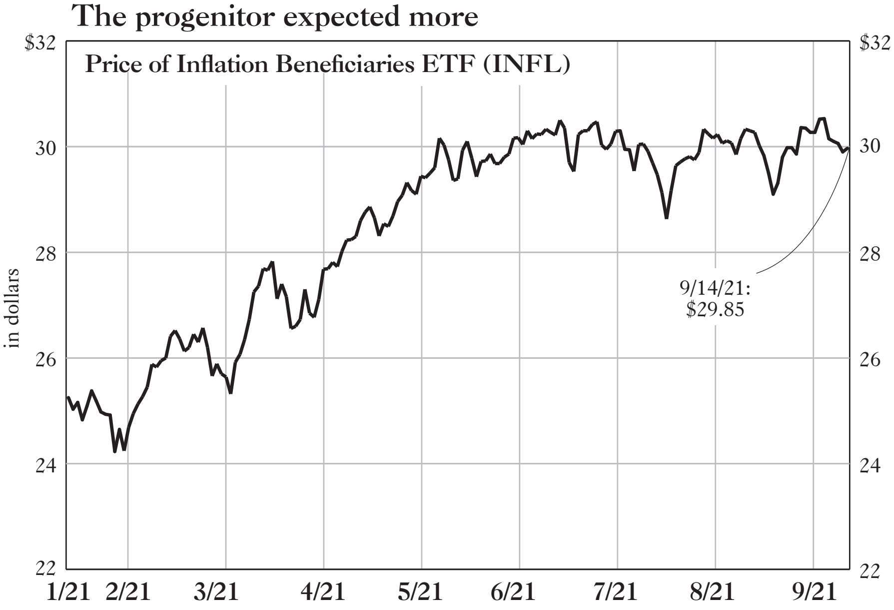
For perhaps the purest expression of the value of operating leverage in an inflationary environment, hear Paul Brink, president and CEO of Franco-Nevada Corp., the big gold royalty trust (and an INFL portfolio company), hold forth on the Aug. 12 Franco-Nevada earnings call:

> A theme for this reporting season has been cost inflation, labor materials and energy. This is the stage in the cycle where our business model really distinguishes itself. Our revenue-based royalties and streams aren't impacted by cost inflation, we operate with small headcounts and low G&A, commodity price increases flow directly to the bottom line. In fact, we have leverage to inflation as energy and steel prices increase. We benefit through our portfolio of energy and iron-ore royalties.

"Strategic commodities," was Stahl's reply to the question of which new inflation-themed ideas might be germinating in the Horizon-Kinetics seedbed.

"The 20th century was the century of commodities in plentiful supply," Stahl said.

The progenitor expected more



source: The Bloomberg

So it'd be oil or gas or lumber or coal. There's plenty of it in the world. We had to make the investment to obtain it. In the 21st century, technology rests upon commodities that are in short supply. So take, for example, cesium. There's not a lot of cesium in the world. As we go to 5G cellular, you have to have cesium. . . .

Another example of a commodity like that could be neodymium. So you need that in electric motors. So an electric motor is basically an electromagnet. The way it works is they reverse the polarity of the magnets to get a rotor to spin to basically create transverse motion to operate a motor. And there's not that much in the world. Now, if you're really going to have electric devices, and it's more than just electric vehicles, though electric vehicles need it. It's in your laptop. It's in your iPhone. It's basically in all the electronic devices. So if you want to have, let's say, autonomous driving, well, you're going to have to have all sorts of instruments that use neodymium magnets for their electromechanical [processes] in that sense. You're going to need neodymium. Where are you going to get it from? So people are going to compete.

I haven't figured out how to make that into an investment theme. I don't know if there are enough publicly traded companies to do it. You might actually have to go and just stockpile neodymium.

Wherever it is.

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