October 2019

OCCASIO PARTNERS LLC

San Francisco, CA

Performance Summary: Despite all the assumptions that October would bring chaos and despair to the markets, the exact opposite actually occurred, as is often the case when the sentiment is lopsided. Stocks acted well in October as a whole, but beneath the surface there was more examples of extreme dislocation, a theme we continue to highlight.

As for our performance, we had one of our better trading periods, which was the primary catalyst for the profitable month. Also, we avoided a couple of landmines in Tesla and Twitter, both which reported earnings this month and both names that we flattened out our positions prior of the announcements, for reasons stated below. Hopefully, we have made it clear through the years that we either flatten out or hedge our positions when earnings announcements are coming. It's prudent, sometimes costly or wrong, or in the case this month extremely supportive.

Our Bitcoin position rallied nicely toward the end of the month after suffering through some serious bouts of selling earlier and ended up gaining **+12.3%.** We have more to say on that below. Also, we feel confident in re-establishing a long position in Snap after their earnings report this month. We also go over that analysis in the pages below.

As 2019 winds down, we are going to turn the majority of our focus to trading versus portfolio management. The reason being twofold: 1) The remaining two months should see some short periods elevated volatility with the current news cycle we are in and elevated levels for stock indices and 2) As a way to ensure that we hold on the bulk of our gains for this year. We don't need a situation like Twitter this month, which would have caused some damage to our bottom line, to rear its head and hurt our partner's returns.

It would be disingenuous to assert that we are pleased with our progress this year. We feel we have missed some opportunities, and that pains us to no end. But a double-digit return, with minimal drawdown, does help ease some of that discomfort.

Please don't interrupt that as a sign that we have given up on 2019, we haven't. It's more a candid reflection on where the calendar is (holidays fast approaching) and how the markets are behaving (seasonality, combined with an accommodative Fed).

Game Day: Earning season kicked off on a solid note when some of the big banks released their reports on October 15th: JP Morgan was the standout as it beat on all metrics and showed improved performance in its trading and investment banking arms, a theme that was shared throughout all the big money center banks reports, and a relief for many banking bulls who were fearful of more tepid results from those divisions that have suffered recently.

JPMorgan's total loan portfolio was up by 3% and deposits grew by 5% year over year, a significantly higher growth rate than we saw in the second quarter

JP Morgan's stock hit an all-time high on the news and continues to be the best in class for the major banks. However, CEO Jamie Dimon was not quite as sanguine on the conference call when he warned of a potential slowing economy due to trade tensions; but he was more upbeat on the American consumer and continued loan growth.

Not to be outdone, Wells Fargo, Citigroup, and Bank of America, also posted solid quarters and mimicked Morgan's results to a certain extent, especially when it came to faith in the American consumer and expanded loan growth. All three banks beat their estimates handily and kept their guidance in line to slightly elevated for the fourth quarter.

One stalwart that did not impress was Goldman Sachs; the banking (ex?) powerhouse missed on their estimates by $0.10 and only came in with in-line revenues. They are still dealing with the WeWork financing fall-out and some pending fines coming from dealings with the Malaysian government.

These results were the antithesis of other investment houses such as Morgan Stanley, Blackrock, and Blackstone – who all turned in excellent results and opined positively about the current and future environment. We are strong believers that the trading environment is very fertile right now and will only flourish in 2020 for a variety of reasons that we will be highlighting in an upcoming special report.

All in all, the positive results from the banking sector led to a relief rally in stocks. Mainly due to the fact that with rates staying so low this year, and most yield-curves still very flattish but not negative, investors were relieved to see that it did not have a detrimental effect on the bottom lines. Also, the continuous positive American consumer theme bolstered investors' confidence as well.

Many have felt the overall market can't advance in any significant fashion unless the financials finally show some leadership and break out technically. Well, we finally got both in October and the SP-500 responded in fashion. The next question is if it is sustainable and if we finally get some follow through? It's hard to answer considering the SP-500 has essentially gone nowhere for almost two years as the financials have remained range bound.

We have spilled some ink on these pages this year talking about Netflix and what an interesting/precarious position they find themselves in these days. This was never more evident than when they reported their Q3 earnings on October 16th.

On the surface, the top-line results seemed fine. The streaming giant beat EPS estimates by $0.04 and matched revenue estimates with a 31% year-over-year jump.

But when one looked beneath the surface, there were some troubling metrics to consider. For one, the new domestic subscriber numbers came in at only 6.77 million versus the 7.0 million expected. This was the 2nd straight quarter domestic subscriptions have failed to meet expectations, not inspiring news for a growth company. To be fair however, their international subscriber growth did increase 23% and came in at 6.3 million against expectations of only 5.3 million.

On the conference call, Netflix issued downside guidance for Q4 of only $0.51 per share. Estimates were for $0.81-$0.85. Revenue guidance also came in at almost $500 lighter than anticipated.

Currently, Netflix trailing 12-month free cash flow is a negative $2.87 billion; this translates to losing $0.15 of negative cash flow for every dollar of revenue generated. But they are still considered a growth company?

There has long been concern that Netflix will eventually face some stiff competition in the transformative streaming world. And it seems like that day has finally arrived. On November 1st, Apple will launch Apple TV+ - their streaming service for $5.99/month. Seven days later, Disney will launch their much anticipated streaming service Disney+ for $7.99 a month.

The price points of these two new services bring up an interesting dilemma that Netflix now faces. The basic price for Netflix is $12.99/month and can go as high as $15.99/month. At these prices, Netflix still is not cash flow positive, mainly due to the immense amount they spend on content.

Starting this month, they will have two huge competitors offering services for essentially 50% less than what they charge. Also, as more and more providers begin to offer their own streaming services (HBO, NBC, A&E, Bravo) there will be less content for Netflix to license and this will add to the immense stress and cost they are under to produce their own content (it is reported that their new Scorsese movie The Irishman cost $165 million to make).

So this all leads to a pretty obvious question: How can Netflix stop the free-cash-flow bleeding when they are seemingly unable to raise prices, but yet have to produce more and more expensive content? The also obvious answer is more subscriber growth. But we just went over the domestic growth disappointment above and keep in mind that is *before* the launch of Disney and Apple's services.

Here is what CEO Reed Hastings had to say on the conference call regarding subscriber growth:

"Since our US price increase earlier this year, retention has not yet fully returned on a sustained basis to pre-price-change levels, which has led to slower US membership growth.

While we had previously expected 2019 paid net adds to be up year over year, our current forecast reflects several factors including less precision in our ability to forecast the impact of our Q4 content slate."

In regards to the international growth versus domestic, it's hard to believe they are equal in added value. Is a subscriber in India the same as one in Indiana? For example, a monthly subscription in Malaysia and India is equivalent to $4 US dollars. So are the metrics equivalents? Is the retention the same? Is it equal in revenue generation? We highly doubt it.

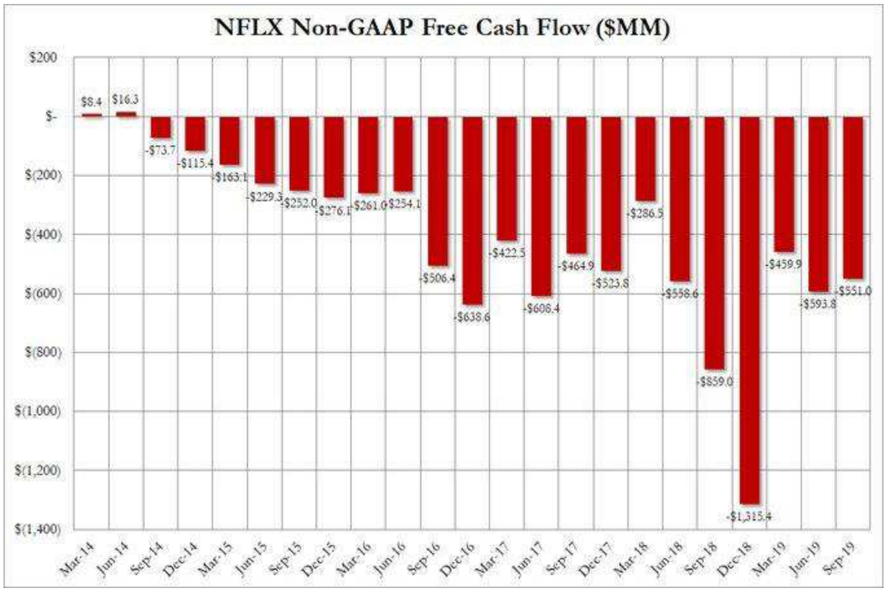
Before we throw dirt on Netflix and declare it a goner. Let's keep in mind that they still have surging international growth and understand that just because Disney, Apple and others are improving their streaming offers (at lower prices), it doesn't mean the world will dump Netflix for them. It is still to-be-determined how consumers will react and how much price elasticity they will display for the new plethora of monthly streaming bills.

However, there is little doubt Netflix now finds itself in a situation they haven't been in ever. The big guns are directly aimed at them, and are now starting to finally shoot, and they have some deep pockets and are showing that they are willing to lose money in the short-term to gain market share, as evidenced by Apple's paltry $5.99/month fees.

We have shown the chart below many times in various updates, but we think it is worth reminding folks of just how precarious the balance sheet at Netflix is. Which likely explains the reason they did a $2 billion debt offering in October, their second capital raise this year, to help fund more coming content.

We have been actively trading Netflix from the short-side in recent months as our thesis has begun to play out. However, we have had a hard time establishing a longer-term position due primarily to the fact that the overall markets have remained strong and shorting has been difficult task; Tesla being a perfect example.

We are in, and have been, in a period where growth is being sold and value is being bought. The cloud and software stocks have been taken to the woodshed and been beaten the past two months, but the indices have remained placid. This is something we touched on in last month's report. Thus, Netflix is now a stock that has significant more downside than upside. That is especially true considering Netflix is still considered a growth stock although they aren't growing anymore when you look at the new subscription rates.



Nothing new here, Netflix continues to burn cash to provide more content in an ever-expanding competitive arena.

This can go on for longer than many would assume in an easy-money environment.

But when things change this graph will equate to a huge dilemma for Netflix.

It seems like we spend a lot of time on tech in these pages, maybe it's due to the fact that we are headquartered in the heart of tech land. But that doesn't mean we are oblivious to other industries and companies that can help give us a clue to the state of general economy.

On October 22nd, we spent a good deal of time going through some non-tech reports and were cheered by what we saw and heard. American stalwarts such as Sherwin Williams, United Technologies, Kimberly Clark, Proctor and Gamble, Lockheed Martin, and Nucor Steel all turned in strong numbers with good to in some cases great guidance.

United Technologies was especially cheered due to its diverse portfolio of business and roots in manufacturing and heavy equipment. It's refreshing to get some real anecdotal economic data rather than relying on yield curves and Fed Fund rates.

Other American iconic names that produced good results in October include Harley-Davidson, Whirlpool, Pulte Homes, Honeywell, and Norfolk Southern; names which represent a wide swath in our economy.

One name that investors embraced is label and packaging material-maker Avery Dennison, whose revenues were flat year-over-year at $1.76 billion. But earnings came in at $1.66, or $0.05 ahead of estimates, the stock broke out to all-time highs on the news. Another sign that the domestic economy is hardly on life support.

Alaska Airlines, Delta, United Airlines, and Southwest all beat their estimates and provided upbeat guidance going forward - and yet the 10-year note still yields 1.80%?

On the tech side, more good news was in order. Intel, Microsoft, Lam Research, were decidedly positive while Amazon and Texas Instruments were not as cheery as many had hoped, but hardly reasons for concern. Google came in woefully light on estimates, but beat on revenues and maintained their 20%+ growth rate, which is awfully impressive considering their mature stage. Their core business remains solid, but their "other bets" division (Waymo, drones, etc.) continues to bleed money.

Despite all the criticism, Facebook was able to post another stellar quarter. They beat estimates by $0.24 and handily beat revenue numbers as well. Daily Active Users (DAU) increased 9% year-over-year and stands at 1.62 billion per day. Which goes to show that people love to criticize and complain about Facebook – but they aren't ready to stop using it.

Both Snap and Twitter reported their results in the 3rd week of October. Snap was first on the 22nd, followed by Twitter on the 24th. Because of the amplified volatility surrounding earnings releases and the overall current sour temperament regarding social media these days, primarily due to the ongoing public relations disaster that is Facebook; we significantly lightened up on our positions prior to the releases.

That proved fairly prescient seeing as Snap fell precipitously before the release, as did Twitter to a lesser extent. As for Snap's earnings, they were relatively impressive

The company reported third quarter results that exceeded its guidance on every metric. Revenue growth accelerated as the company increased daily active users for the third consecutive quarter.

Third quarter revenue grew 50% to $446 million as average revenue per user (ARPU) grew 33% to $2.12. The adjusted EBITDA margin fell to (9%) from (46%) in the third quarter of last year. Daily active users increased by 7 million sequentially to 210 million versus the company's guidance for 205-207 million users. The company guided for a 4-5 million DAU increase in the fourth quarter, which was above estimates.

The response however was not impressive. Shares shed 9% and fell to a 3-month low. While that makes our shedding of the position prior to the announcement look clairvoyant, the fact is we still think Snap will do well over the long run. But as mentioned above, the current environment for social media is toxic and to ignore that fact would be foolish and more importantly costly.

Twitter delivered a real bomb on October 24th when they shocked the Street with some frankly awful results. The social media giant missed estimates by $0.06, missed revenues by close to $50 million and guided Q4 below expectations.

They blamed the awful results and lowered guidance on seasonality (lame excuse) and software bugs that are still being worked out as they continue to deal with execution issues and try and clean up the cesspool that Twitter can be at times.

It is interesting that Twitter is being punished for trying prevent exactly what Facebook is being criticized for by users and in the October Congress hearings. That doesn't excuse the awful results, but it does show that the company is willing to take some short-term pain to hopefully garner some long-term success. Time will tell, but we still think Twitter may be the ultimate winner in social media when all the dust settles.

For the time being however, we will remain on the sidelines and are thankful (lucky?) that we were able to dodge this missile that Twitter just lobbed at all shareholders. Twitter just told us that the 4th quarter is not going to be good, they still have some tweaking to do and software bugs to manage. No need to rush into this name yet, even at these levels. Let's just sit back and watch for a while.

Speaking of avoiding bombs, Tesla reported their results on October 23rd and they were "interesting." Tesla beat their estimates by a whopping $2.19 despite revenues falling by 7.6% year over year and came in at $6.3 billion against the $6.48 billion expectation. All this just weeks after they reported a light delivery number. Interesting, to say the least.

It was that delivery number, and then the 7% rally right after it, that finally convinced us sell our puts and flatten out the position. That looks very lucky in hindsight, but in reality it just comes back to the old saying "*it's not the news that matters; it's the reaction to it that matters*." To see Tesla continue to march higher despite last quarter's abomination, combined with a light delivery number, was a sure tell sign to not be involved for this quarter's earnings release.

Much like Twitter, we will sit and watch Tesla for a while and let others with more conviction try and do battle with this extremely controversial stock.

Looking Forward and other Market Commentary: Earnings season is still in full bloom and will continue for another couple weeks into November. Some of the names we will be keying on include**:** Trade Desk, Uber, Telaria, Rubicon Project, GW Pharma, Plantronics, Baidu, Pan Am Silver, Booking Holdings, Planet Fitness, Stamps.com, Activision, among others.

Overall, FactSet reports that despite the projected **-4.7%** earnings growth expectations, the results so far are only a blend of **-3.7%.** Hardly a reason to throw a party, but it does lend itself to those who believe the economy is not headed for a recession.

In other news, a Phase One of the China trade deal agreement was allegedly to be signed on November 16th when the G-20 meeting in Chile takes place. That summit was cancelled due to security concerns and a new venue is yet to be found. This soap opera has been playing out for over a year now and shows little signs of abating despite the continuous proclamations by President Trump that a Phase One deal is agreed upon.

Nothing at all has actually been resolved. There is no contract. The Chinese are disputing that anything at all has been agreed to beyond a vague promise to buy more soybeans, a claim that is likely to be significantly smaller than promised. The major issues around Chinese subsidization and IP theft have not been remotely broached. And, with every passing day, the two countries are getting further apart in terms of the decoupling process.

We have long said there won't be any meaningful deal between now and the election. There may be some tariff delays and agriculture purchases, but the meat of the deal is far from complete. The fact that the 2020 election is now a year away and the impeachment threat is not going away it seems, only bolsters China's stubbornness and strengthens their resolve.

When listening to conference calls and combing through results it's apparent that the ongoing trade unease is a major concern (excuse?) for forecasting models in companies' finance divisions. We took this snippet from the Texas Instrument's conference call to highlight what we mean:

But the sense we get talking to those customers, getting input from them, from our salespeople and all the touch points that we have is that the weakness is broad-based, is due to macro events and specifically the trade tensions. And if you think about when there are tensions in trade and obstacles to trade, what do businesses do? They become more cautious and they pull back. And we are at the very end of our long supply chain and when the ones at the very front pullback, it becomes a traffic jam - Texas Instruments CFO Rafael Lizard

On October 30th, the Fed, to no one's surprise, cut rates another 25% and set the Fed Funds rate at 1.50-1.75%. This was communicated well considering the futures were pricing in a 94% chance of a cut. Now all eyes focus on the December 18th meeting and see if the Fed again kotows to the President and cuts rates for the 4th time in 2019.

After the cut, they released a lengthy statement, probably summed up best in this paragraph:

"In determining the timing and size of future adjustments to the target range for the federal funds rate, the Committee will assess realized and expected economic conditions relative to its maximum employment objective and its symmetric 2 percent inflation objective. This assessment will take into account a wide range of information, including measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial and international developments" FOMC statement 10/30

Translation…we are data dependent because we have to say that. But will cut rates again soon because we feel the pressure to and will use obscure data to justify it. Carry on.

"The U.S. Fed, out of nowhere, just came out and said "we are expanding our overnight repo operations to $120 billion and term operations to $45 billion." That is a 65% increase in Fed injecting daily liquidity into the system overnight. It smells way too fishy and is certainly not representing a system that the Fed claims to be a "temporary fix" or "not the start of quantitative easing." –Maleeha Bengali, CEO MB Commodities Capital

Many have feared that we may see a repeat of the final two months of 2018, when the SP-500 plunged 20% in nearly a straight line. While these are markets, and anything can happen, it would be quite surprising to see that repeat. The foremost reason being that the Fed, as we touched on above, is on a completely different path from last year's at this time.

This path may not bode well for 2020, but for the remainder of 2019 it *should* lead to somewhat calm waters.

October started out a bit rough for cryptocurrency space, and in particular Bitcoin. There isn't one direct catalyst to point to for the decline, but many are pointing to the deterioration of Facebook's Libra project as one glaring reason; this is ironic because as we discussed in previous updates, Libra is a payment facilitator, and not a store of value like Bitcoin and other alt-coins.

But that is not here or there right now; the bottom line is that Bitcoin is undergoing a painful correction, much like it did a year ago at this time. Ironically, this month we saw the Bakt exchange continue to show volume improvement in their Bitcoin futures contracts and also heard from the CEO of Greyscale, who reported that in Q2 of this year they saw $85 million come from investors — twice as much as in Q1 — with institutional investors contributing more than 80% in total.

"You know, it's really funny, I get asked this a lot - there's this rhetoric in the media about when are institutional investors going to get involved, when are they going to start investing, and it's so funny because it's ironic. ***We see institutional investors invest with us all the time and that's been the case for a long time now****."* Sharif-Askary, Greyscale

We did see a nice pop in the price of Bitcoin during the last days of October after President Xi of China made comments about how he thinks China needs to "seize the opportunity" afforded by block chain technology and make it a focus going forward.

Those comments were interrupted as bullish for Bitcoin and we saw a 26% rally in only three days; which obviously helped alleviate some of the damage done previously.

It surely is disappointing to see the crypto space "mature" with regard to increased facilitation and institutional flows continue to escalate; and yet the price of the coins continues to head sideways at best. Its worrying price action for sure, there is no point in trying to spin it otherwise. But we still have to remember that this is an infant industry (less than 11 years) and there is still a dearth of information and trust associated with it.

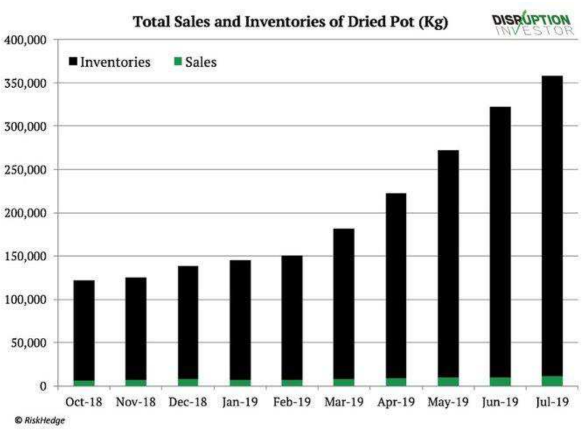
Also, let's remind ourselves that Bitcoin has appreciated more this year, over 150%, than any other asset on the planet.

This is a slowly changing space, as evidenced above, but the learning curve can be painful and overly exaggerated at times. As for our positioning, we are still holding the very small stake we initiated in the early summer. We are not adding, in spite of the drop in price we are painfully enduring. It's never a good idea to average down in our opinion. So we will stick with our discipline and wait for a turning point or a positive news catalyst that correlates with positive price action – something that has sorely been missing for a while.

It's been a frustrating few months for sure in this area, but we still believe in the long-term story and continue to be emboldened when we see the lunacy emanating from the central bankers and the continued push for block chain by nearly every industry.

Finally,

60 Minutes recently aired a piece on how poorly the first year of legal marijuana has gone in California. Looking at the chart below it's pretty obvious why. It's amazing how many got involved in this industry with the belief they were doing anything different from selling a commodity.



Not only is it a commodity, it is a planted commodity – much like wheat or soybeans. Which is fine, as long as you realize that the barriers to entry are very, very low. And to make matters worse, marijuana comes with strict regulations, higher taxes, and is unavailable for sale in 39 states. Currently, California produces 11 million more pounds of marijuana than it consumes.

But that apparently hasn't stopped producers from growing copious amounts of the crop despite sales remaining stagnant. And this graph doesn't even include the home-grown producers, of which they are still plenty as witnessed in the *60 Minutes* piece.

Maybe demand will eventually meet the supply, and maybe the increased calls to legalize nationally will be a huge issue in the 2020 election. But for now, supply is crushing demand.

Marijuana is called "weed" for a reason - *it is a weed* and grows like one. Anyone who spends their Saturdays doing yard work knows exactly how easy it is to grow weeds.

No wonder the marijuana stocks continue to linger around their lows.