Weekend Thoughts 6/18/22

Weekly collection of unstructured hypotheses for current and future research projects

- Secular outweighing cyclical in a recession
    - Global-e Online (GLBE)
        - "So we definitely see--we have seen a change in the last few months over the entire e-commerce arena. However, there are differences between us and other players and also between different geographies across the world. I think that the most important point to start with is the fact that since we are enabling cross-border direct-to-consumer e-commerce and the brands are pushing that very hard as they tend to prefer this channel and strategize it over time. we have seen less of an effect than others, and we expect that to also continue in the future. . .So as we look forward, if the economy is a bit weak, I think that there will be influence on every company out there, but I think the gap between us and others will widen."
        - "For a decade, brands have been gradually going online. And within online have been gradually going to direct because that's the holy grail at the end for a brand to have a direct connection to its customers and to be able to disintermediate that as much as possible. So in that sense, that demand or the interest in our service is as strong as ever, are the investments that we've been making and we continue to make in increasing our capacity to take more and more merchants live … January to May, we've onboarded twice the number that we've onboarded at the same period of previous year. And bookings as well, as we've disclosed, is about double that in the same period of 2021. . .not only are we not seeing any slowdown, we're seeing bigger and bigger interest from bigger and bigger brands that previously, we're not kind of -- we're sitting on the fencing, we don't know if for us, maybe we'll -- maybe it's a 2022 or 2023 project, all of a sudden, what COVID did was to put that front and center in the strategy of many brands."
    - Oracle Corporation (ORCL)
        - "I'm not sure I'd call it countercyclical, but the cloud systems cost a lot less than the on-premise systems to run. So -- and they give you much better information. They allow you to control expenses better. They don't cost that much to implement because you pay for them over time. . . .We see our ERP business, both Fusion and NetSuite, accelerating, this in spite of the macroeconomic situation."
    - Cisco Systems (CSCO)
        - "Cisco is moving to a far more recurring revenue model. . .as we look at the total addressable markets out for the next 5 years, there's growth in that 5% to 7% range. . . growth of the subscription model within that overall growth is about 15% to 17%. . .$30 billion of RPO, which $16 billion is current, a little more than $16 billion is current and a $15 billion

backlog. I do feel like <u>we're fairly well positioned in terms of demand back to -- we've transacted more than $45 billion of sales that haven't yet showed up in our P&L</u>"

- Coupa Software Incorporated (COUP)
  - <u>"Well, what I'm seeing on CNBC is a lot -- quite a bit different than what I'm seeing in our business</u> at least so far. So <u>our North American business, which is about 60% of our business, has really not shown any signs of weakness of late</u>. We had a strong year last year. Q1 was strong as well."
- Adobe (ADBE)
  - <u>"we've been through multiple recessions before.</u> So we have some good insight into how these different cohorts respond to difficult financial times. <u>And overall, we fared very well. Enterprises. . .content is fueling the digital economy and needing to stay very focused on their digital investments.</u> From a pro market perspective, we have professionals that are making their living using our products. So we feel very good about that offering as well."
  - "From a communicators perspective, where they tend to be either working in departments or small businesses or they're part of this growing movement around the creator economy and they're aspiring to make money or build followers with that, so it's an essential part of their tool set that they're going to do to grow their side hustle and their activities. And as it relates to the consumer businesses, we've been very thoughtful with pricing there and have very attractive pricing that we think has fared very well for us in the past around through recession. So overall, we think the business is diverse, and <u>we see the business as very resilient. . .one of the areas that we're seeing just tremendous interest is what we are referring to as content supply chain. . .this notion of people creating campaigns, if you agree with us that the greatest value that we can provide is enabling every enterprise to do personalization at scale, the amount of content that's being created, the amount of content that's being delivered and to understand the efficacy of the campaigns is just absolutely top of mind</u>. . .when you talk about a recession, the question I ask people is <u>when you look at the 3 things that Adobe does, which is focus on content, focus on automation, focus on customer engagement, I just don't look at any of those and feel like the secular trend for that will change."</u>

- Supply chain normalization
  - Samsung halting orders (7th largest US importer)
    - <u>Samsung is temporarily halting new procurement orders and asking multiple suppliers to delay or reduce shipments of components and parts due to swelling inventories</u>. . .TVs, home appliances and smartphones. . .and the postponement of orders involves a wide range of components across chips, electronics parts and final product packages. <u>Notice to suppliers comes in stark contrast to its previous plan last month, when it</u>

    told suppliers that it had a relatively healthy view of the year ahead and that it still planned to ship at least 270 million smartphones in 2022, a similar level as last year. Chinese makers Xiaomi, Vivo and Oppo, by contrast, have scaled back orders by at least 20% due to the lockdowns in China and weakening demand in the European market.

  - Intuitive Surgical (ISRG)
    - "...the number of products now that are affected by severe issues is lower than it was previously. And where we've had opportunity, we have acquired inventory. So our inventory go up in the first quarter. So we've had the chance, we've kind of stocked up on these items."
  - Ford (F)
    - "And we're seeing increased transparency and cooperation through the supply chain all the way down to the fabs."
  - General Motors (GM)
    - "Supply chain is making great progress. Manufacturing is making great progress. . .we're still very much in line with our targets of up 25% to 30% year-over-year."
  - Fisker (FSR)
    - "we are seeing sort of the end of some of the supply chain crisis . . . I think once we move out of this crisis, we will again see the battery prices decline."
- Consumer health
  - Ford (F)
    - "We are not seeing any issues with demand at this point. . .we are seeing delinquencies start to increase. It's not yet a concern for us because it's -- as you know, coming out of last year and through the first part of this year, they were very low. Seems like we're reverting back more towards the mean."
  - General Motors (GM)
    - "We have not (seen signs of weakening consumer demand). And trust me, I'm looking for it and asking for every day. . .And if you look at May, yes, sort of industry sales were kind of down a little bit. But when you look at what we were able to do, average transaction prices were still strong and hasn't changed significantly. And we didn't grow any inventory, grounded dealer inventory. So that tells me that the vehicles are still moving, and that's probably the #1 thing that I'm looking at."
  - Capital One Financial (COF)
    - "the consumer cannot sustain the extraordinary credit performance that they have had up to this point. . . we have been seeing for a bunch of months now, some slow gradual normalization in charge-offs. . .striking thing about it is probably how moderate it is relative to in the rapidly changing world a case could be made that one would expect maybe faster normalization. But the normalization is clearly there. We also look at other

metrics like payment rates. I talked earlier about how outstandings have had trouble keeping up with purchase volume because payment rates are so high. . .Payment rates have -- are strikingly high and I don't see as much normalization yet happening in payment rates. I -- in the individual months, I say, yes, see, it's happening. . .lower income is normalizing faster. . .Also by FICO score band, we do see more normalization on the lower side. These are relatively -- these are modest differences."

    - Ferguson Plc (FERG)
        - "And so to date, we haven't seen demand destruction, but we keep a very keen eye towards that.. .We're certainly eyes wide open and mindful about what rates and price and consumer sentiment can mean in the overall macro. But as we sat here today, that market activity and that demand curve still looks reasonably strong."
    - Kroger (KR)
        - "Now the typical basket size for a customer coming in continues to decline. Part of that is just driven because of the economic environment some customers are having. . .And then customers are aggressively starting to buy Our Brands (2x rate of national brands). . .price spreads. . .those spreads continue to be where they've been or improving slightly has been the case over the last couple of years."
    - Adobe (ADBE)
        - "The consumer sentiment that we continue to hear from banks such as yourselves is that the consumer sentiment actually continues to remain strong, both in the U.S. and in Europe. So I didn't want to have anybody feel like that's not what we are seeing as well."
- High quality cash flowing companies taking advantage of multiple compression for M&A
    - IQVIA Holdings (IQV)
        - "Some of the acquisition pricing has been a little bit slow to adjust, and we probably passed on more things than we would have in the past. But there's still some attractive acquisition opportunities that are strategic in our pipeline."
    - Moelis & Company (MC)
        - "Whereas last year, very, very high visibility in the deal completion, this year, less visibility in the deal completions. And I think a lot of that stems from the fact that there's going to be a period of time where we find equilibrium on pricing of assets. . .all the macro forces that we've been talking about, structural forces for a long time that should help propel the M&A market for many years are still very much intact. Technological disruption that's ripping through every industry, all of which was accelerated by COVID, is still very much intact. That's a theme that's not going away and will impact corporates and financial sponsors. . .I think one of the countervailing factors which I think will help the M&A market

is what you're talking about. So as I mentioned earlier, corporates in every industry are very cognizant that they got to make sure they're well positioned for growth in light of all the technological disruption. And now we have a whole host of companies, growth companies, that we're raising -- easily raising rounds of venture capital, rounds of growth capital on the way to being public and now the IPO market's completely shut down. IPO market's shutdown, SPAC market's shut down and the private fundraising market is close to shutdown. And so lots of good companies that have good technologies or good market positioning are finding themselves in a position where a strategic exit to a cash flushed strategic who needs technological advancement is probably their only exit. And so I do think that will help the M&A market. And I do think you have corporates who are on the lookout for plays now that could have been outside of their comfort zone in terms of valuation. But as those private market values start to reflect what's happening in the public markets, I do think there'll be a lot of that kind of M&A."

- Jack Henry & Associates (JKHY)
  - "We've done a lot of acquisitions in our history. In fact, from 2004 to 2015, we acquired 32 companies. We are a very competent acquirer. We know how to value deals. We know how to integrate them in. We know how to put an emphasis on cultural fit. We know how to understand what would our customers buy. So if we acquire something, how do we get it out there in market and get the sales engine going quickly. We're very, very confident of that. In the past 3 years, however, between IPOs and specs and PE seemingly willing to pay anything for anything. As a disciplined acquirer, which we are, there weren't acquisitions to be completed. Every little company out there figured they were going to IPO and make a whole bunch of money, and they did. But now on the back end of all that, there's a lot of eye opening that's happened. A lot of these smaller companies with IPO-ed have been hit really hard in the recent past. And so I believe that may present opportunities. The better opportunity for us, I think, in the near term is some of these companies that were getting ready to IPO. And now they figure IPO is off the table. . . We're looking for technology solutions that, are appealing to our customers. So we don't go after deals where we can do some really clever financial machinations and take a bunch of cost out. What we tend to look for are things that we believe will be appealing to our customers that they will want to buy, we can hand off to our sales team and get the sales engine going quickly. We look for cutting-edge technology solutions that fit with our strategy. We look for things that fit with the focus that we have on serving community and regional financial institutions in the United States. . .We're in the service business. We're technology and service. That's what we're known for. We are not the low-price leader."

        - Adobe (ADBE)
            - "Clearly, valuations, to your point, have changed quite a bit. . .there are going to be a number of small single-product companies that are probably not going to survive what's happening. And the valuation sort of multiple changing is actually, I think, good for a larger company like Adobe. . .So it doesn't feel like we need anything, but we'll always be on the lookout for things that are additive, that are adjacent and that will provide great shareholder value. And our metrics associated with ensuring great technology, great cultural fit and adjacency remain. But we have so much going on within the company that we're excited about our current portfolio. Clearly, things will be more reasonable in terms of M&A as well."
        - Ferguson Plc (FERG)
            - "I'd tell you that from a multiple perspective, we remain towards the top end of that range that we've typically guided to in terms of M&A multiples. So in that 7% to 10% range, we're probably closer to the top end of that range collectively. But we're very disciplined as we look at the operating profit that those companies have generated. And we still see a pretty good pipeline as we move out of fiscal '22 and into fiscal '23. So we're very comfortable with the guidance that we've set out in the past that we can continue to consolidate our fragmented markets and add somewhere in the range of 1% to 3% revenue growth annually through acquisition."
        - Evercore Inc (EVR)
            - "Growth is still very much at a premium and a lot of companies want to be looking at growth."
    - Nearshoring and vertical integration
        - Moelis & Company (MC)
            - "So to the extent to which securing your supply chains and especially securing your supply chains in friendly jurisdictions or inside the United States, I think that could be an M&A theme for certain types of companies, industrial companies, some companies in technology spaces, . .I think historically, a lot of it's been around globalization, international exposure, going to the cheapest source of manufacturing. And I think that drove a lot of the global M&A market, cross-border M&A market. I think this will drive a different set of considerations."
    - Distressed cycle
        - Moelis & Company
            - ". . .the restructuring market as you look out over the next few years, I do think the ingredients for a restructuring wave are certainly there. So what are those ingredients: one, an economy that potentially may be headed into recession or slowdown; two, you have massive maturity walls of leveraged loans and high-yield debt really starting in '24, '25, about $1

trillion of maturities in those 2 years. And if you look out a few more years, another kind of $2 trillion of maturities. And so I think the LBO boom of the last few years, the leverage boom of the last few years as people want to capitalize on low rates, I think those maturities are going to have to be dealt with. And if you sort of roll through a weakening economy and maturity walls that's sort of a recipe for defaults and restructurings and balance sheet work."

    - Evercore (EVR)
        - "I would say that one of the things that we're spending time on right now is making sure that we're well positioned for restructuring. . . .The restructuring business seems to be gearing up. There's not a tremendous activity level at this point yet, but we see it starting to develop, and we're out with clients, spending a lot of time getting ready for this. And there is a significant amount of high-yield debt and leverage loans that are coming out and coming due. And I think there will be more and more activity on the restructuring side. So I think we're really gearing up for that. . . I never would have thought that we would be looking at a possibility of 75 basis points raised by the Fed, maybe over 2 successive months. That's unheard of. And I think that does destabilize a lot of things. And so I think it's a good idea to watch and wait and see. . .I think that as rates go up, that will push some companies. Some of the sponsors have activity levels where they are looking very, very carefully at their portfolios. I think that the restructuring business is really very much on the edge of starting to kick in."
    - TPG (TPG)
        - "because we're very theme and sector focused as a firm, we're developing relationships and dialogue with companies over a long period of time. . .No doubt, we're in a period where we're seeing that sort of bid-ask spread widening. . .we're definitely in a period where we think deployment pace is going to slow for a period of time. . .We look at things and look at different industry sectors. And they may be really interesting to us in terms of secular growth opportunity, where the world is going, but it may be expensive and it may be hard to find interesting opportunities. We're in a world now where competitive sources of capital have basically disappeared. The public markets, the IPO market kind of shut. . .So we're looking at a world where if you're a company in need -- that needs to transition ownership structure, looking for investment capital, looking for growth capital, so where are you going to get it? Private equity is where you're going to get it."
- Digitization of healthcare
    - Oracle (ORCL)
        - "Well, the national health records database solves 2 problems, and it allows patients, in the case of an emergency, to have their caregivers get

immediate access to all of their health records, which will deliver way better outcomes for people. The other is public health officials will get much better information about the state of health in their country. . .having this knowledge, it's -- we dramatically improve health care, but we also save an enormous amount of money by doing that. . .By providing this information, we save a lot of lives, and we save a lot of money. The scale of the opportunity is gigantic because it's not -- people think of it as a national opportunity. It's a global opportunity. Every country -- I mean if you look at Western Europe, the Western Europe's budgets are dominated by health care. If they can save lives and save money by putting in modern information systems, they'll do it, and they'll do it quickly. It's clearly going to be our largest business."

- Robot assisted surgery innovation, scale, and improving outcomes
  - Intuitive Surgical (ISRG)
    - "when I think about evolution of the industry and what robotics might -- what does it bring, I look get places where outcomes are not great. . .And that's where I get pretty excited that mechatronics, data imaging, those things can combine to actually improve outcomes. . .in surgery as a whole, there are just a myriad of opportunities where outcomes -- core outcomes can be improved. . .directionally in the world, it feels like to me more and more we're going to see cancer earlier, liquid biopsies, better imaging . .And if you are able to catch cancer earlier, you should be able to treat it earlier. And so more and more, we might see focal ablation, local resections of cancer as compared to taking out an organ. And so definitely better for the patient, better for the health care system and everything else. And so that's another area where I think opportunities and platforms like Ion to navigate through the lung as an example, and have the navigation required, the stability required to get to a lesion and do something. Today, biopsy it, hopefully, tomorrow, ablate it. That can really make a difference in the health care or the patient journey, those sorts of things in the future."
    - "if you look at some of the work that's going on in imaging, I think it really changed sort of the nature of outcomes if we look into the future. The work that we're investing in the digital platforms and how we might change the way surgeons learn, highly innovative and I think impactful"
    - "what are we focused on? . . it's around three primary areas. One is how do surgeons learn. And so one of the causes of the variance out there between surgical outcomes is the surgical team, right? And it's been shown over and over and over, that you can get a wide disparity of outcomes depending on who you go see. And so how do you close that gap? And I think one way is to say, how do surgeons perform in surgery and how might that differ from an expert surgeon with known good outcomes? And so we can look at video, use machine learning and AI and other things to help understand the differences between that learning surgeon or a surgeon who does not get great outcomes and an expert surgeon who would demonstrate great outcomes. . .So how do we

optimize outcomes for surgical patients using data? What's their journey look like through the care pathway? And then the final one is one that we've been doing for quite a while. Most of our systems are connected to the Internet. We can monitor all sorts of data streams from it. And so it's <u>through those data streams that we can look at the operational efficiencies of our program how often is being used, the time of the operations, number of instruments, things like that, that can help when we can consolidate that and return that back to a surgeon or to the hospital administration they can say, okay, here's how we want to utilize that capital in the future, optimize block time, optimize instrumentation, those sorts of things and really try to impact the cost equation.”</u>

- BNPL in a recession
    - Capital One Financial (COF)
        - “the most impressive part of buy-now-pay-later is that these fintechs have one access to some of the most precious real estate you can get, which is having a button on the merchant websites. . .<u>cautionary about some structural aspects of that marketplace</u> that I want to again highlight, and I've been pretty consistent in this story. <u>One is the big whopping merchant discounts that fund buy-now-pay-later, I've always felt are just likely headed down just due to increasing competition over time in a marketplace where merchants, of course, are counting every penny</u>. And in fact, <u>we have seen the merchant discounts go down significantly, and that puts a lot of pressure on buy-now-pay-later players. If at some point the discount gets low enough, it could flip that business to being one where the consumer is then charged for this short-term borrowing, and that would change the dynamics of that industry.</u> So one would have to really watch out for that. A second issue in the buy-now-pay-later marketplace is the fact, I think <u>a number of merchants are looking at some of the buy-now-pay-later players and saying, "Wait a minute, whose customer are these? Are these customers anyway?" And so there is, I think, growing merchant concern to make sure that they still own the customer. And you also see buy-now-pay-later migrating from a pay-in-4 products, where you pay over a short number of weeks to where more and more of the marketplace is expanding into longer installment loans, which is a natural place for it to go, but that turns it into much more of a really lending business instead of a very quick turnover transactional business. That's going to be a challenge for the fintechs. It's also going to raise funding issues and other challenges that come along the way</u>. . .I think it's an industry that is undergoing and will continue to undergo quite a few structural changes, many of which will be challenging for the buy-now-pay-later players.”
- Aggregation vs fragmentation in streaming
    - Comcast (CMSA)

            - "I, for one, am not a big believer that we've hit peak content. I think lots of viewers like lots of different things, and I think things will continue to fragment. And the reality is, as long as you're selling total audience, and can make a margin on your content, I think there's -- I don't think we're remotely close to peak content in the industry.
            - "I think the key is finding the right distribution kind of strategy for a piece of content that maximizes its chance to be a hit. Because for something to be a hit, whether it's a movie or a TV show, it not only has to be great, not only has to be marketed well, but it has to have the right distribution platform so that the people can find it and discover it and watch it."
- First inning of innovation in credit trading
    - MarketAxess Holdings (MKTX)
        - "I would say we're not even in the first inning. We're still warming up for the first inning, largely because it's traders in the credit market, even in the treasury market, even though it's more advanced and more evolved from an electronic standpoint, they continue to request price, which by definition is crossing a spread. We really want technology to help solve, finding the opportunities to avoid crossing spread and being in the market ready and waiting to respond to another RFQ. We're resting on an order book. So we have all the different protocols that help avoid crossing spread. It's really marrying technology solutions to the opportunity to avoid crossing spread. The big question for traders is how much time do I have to spend avoiding spread before I need to cross spread? And that's really a critical component in developing technology around the bond market to avoid crossing spread."
- Inflection Points
    - With supply chains and excess durable goods demand normalizing, the White House is now targeting energy prices
        - White House weighing federal gas tax holiday, not ruling out an excess profit tax.
        - U.S. Energy Secretary Jennifer Granholm is expected to meet with refining executives on June 23
    - Powell's 6/15/22 press conference seems to be his "whatever it takes" moment.
        - CPI miss was due to oil, and University of Michigan Sentiment survey inflation expectations jumped from 3 to 3.3%, which caused the Federal Reserve to change course and raise by 75 basis points. Energy prices are the priority.
    - Exxon calling out waivers of Jones Act, clear and consistent policy that supports U.S. resource development (regular and predictable lease sales, as well as streamlined regulatory approval and support for infrastructure such as pipelines).
    - Big Tech antitrust bill
        - A bill aimed at reining in the market power of Big Tech platforms like Amazon, Microsoft, Google, Apple, Meta had the votes to pass the both chambers of Congress in the next few weeks. It is very difficult for these platforms to make acquisitions and being disintermediated by platform

shifts in tech is very dangerous. Who will follow the Standard Oil and Baby Bell fact pattern of breaking up to acquire and grow?

- Instant, global connectivity and populism
  - KKR & Co (KKR)
    - “The populist environment is going to persist for many years to come, in my opinion, and it has a lot more to do than who the President is. It's the fact -- there are a lot of factors that explain it. The most important is what I call the Gutenberg 2 moment. So if you think about it, the printing press is invented, the greatest populist moment in history. There's revolutions that transformed science, everything else around the world, religion. Because fundamentally, human beings, when they discover what previously only popes or sovereigns knew, are furious. Today, every single person is a creator of information. Every single person is a witness. Every single person is a journalist. Every single person is an activist because it's not just that information is spread but the ability of every individual to spread it becomes transformational. Combine that with the fact that we have certain, again, very big structural challenges: one, around inequality; two, around the nature of what industrial revolutions do to people's jobs and people's communities; three, regarding also obviously, climate and what that does. All those things create huge challenges that reinforce the populism.