

# AIM Newsletter

## Spring 2018

LEGENDARY ADVANTAGE

IN THIS ISSUE

## Welcome

The spring 2018 semester is nearly complete, and the Applied Investment Management (“AIM”) class just finished voting on the new portfolio allocation. One of the priorities of the multi-day decision process was to reduce investment concentrations in technology and industrials. The new AIM portfolio can be found on page 5.

On Monday, April 30, AIM students will meet with the AIM Advisory Board to present their discoveries and insights from the semester. The following Wednesday, the portfolio will be formally transitioned to the fall 2018 AIM cohort.

In the previous issue of the AIM newsletter, we shared that AIM XLVI deviated from the traditional class structure by including both graduate and undergraduate junior students in the spring roster. This mixture of students and experiences contributed to many great discussions and will likely be implemented in future AIM cohorts.

Adhering to the investment guidelines continues to be top-of-mind, with the following notable segments all in compliance. However, there is some deviation in the match composition of the S&P 500 when looking at the AIM Portfolio against the benchmark.

### Investment Objectives

- Outperform the S&P 500 +1.95%
- Outperform Russel 2000 +2.15%
- Outperform HBI +1.86%
- Maintain Principal +\$3.63m

### Investment Policies

- Liquidity (Common Equities)
- 3-5 Year Time Horizon
- Following all Laws and Regulations

### Policies and Guidelines

- Target Allocation: 11.9% /88.1%
- Some deviation to the Match Composition of S&P 500
- No Single Equity Cap > 10%
- Cash Holding Close to Zero: < 0.1%

### AIM Analyst Chicago Trip

Page 2

### State of the Economy

Page 3

### Portfolio Performance

Page 4

### Sector Updates

Page 4

### Portfolio Composition

Page 5

### Alumni Update

Page 6

### Class Profile

Page 7



# AIM Analyst Chicago Trip

Thursday, April 5 – Friday, April 6

Students visited AIM alumni at four area firms. These alumni shared their AIM experiences, highlighting the valuable lessons learned and how AIM helped shape how they identify and evaluate investments in an increasingly sophisticated and fast-paced market.



Notre Dame hosted the students' first meeting at the University's Railway Exchange Building. The class met Greg Salter, a VP at the Farbman Group. The Farbman Group is a full-service real estate company based in Southfield, MI and manages over 25 million square feet of real estate. Greg walked the AIM class through a case study on a local real estate transaction. He spoke about the specifics of the transaction, the value of good partners, and the trade-offs between holding and selling an investment property. AIM XLVI has several students who interned with and/or will be working full-time for real estate firms.

Morningstar. R.J. presented the company's methodologies and processes for evaluating investment opportunities within Morningstar's coverage universe. After the methodology presentation, R.J. walked the class through a case study on Amazon. He explained how he segmented and forecasted Amazon's various business units. Furthermore, he walked through his three-phase forecast horizon. After the case study, there was much discussion about the future of retail, e-commerce growth, and potential areas for future monetization. AIM students also took interest in learning about the most rewarding and challenging aspects of equity research.



Prairie Capital hosted AIM students at its Wacker Drive office for a working lunch. The lunch was hosted by D.J. Lipke, a VP at the firm. Prairie Capital seeks to partner and invest in privately-held middle market companies. Rather than investing in specific industry verticals, Prairie Capital focuses firms with good growth potential and quality management teams. D.J. shared the extensive due diligence processes which are necessary to ensure sound investment decisions. The firm's

management-focused strategy and commitment to the middle market stood in contrast to many of the AIM students' experiences and views of private equity.



The final presentation of the day had students returning to the Railway Exchange Building to meet with Michael Melby, Gate City Management's founding partner. Mike and Gate City invest solely in publicly-traded micro-cap companies. The visit opened with a stock picking exercise. Mike picked a stock by way of a newspaper stock listing and a dart board. He then asked each student to select a stock that he or she believes will outperform over the next 12-months. Mike's presentation walked students through his process for identifying overlooked micro-cap stocks which are severely undervalued and his "boots on the ground" research techniques that are performed before investing in a company. He presented a case study on one of the firm's current investments, outlining his due diligence process and interactions with the management team. The firm is committed to a relatively concentrated investment portfolio, helping maintain focus on each investment.

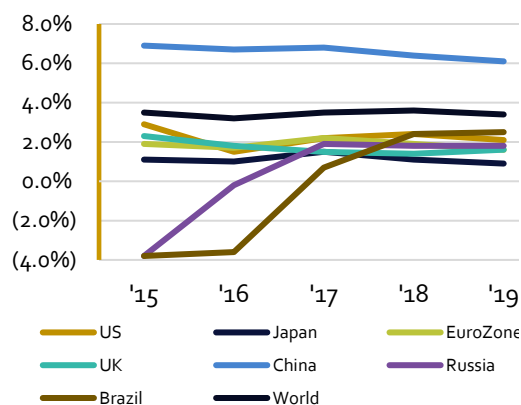


TM

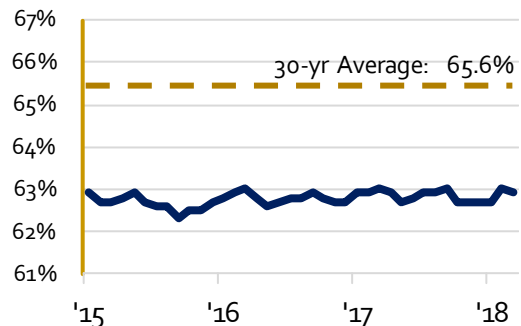
Next on the Chicago trip was Morningstar. The class met R.J. Hottovy, a Consumer Equity Strategist at

# State of the Economy

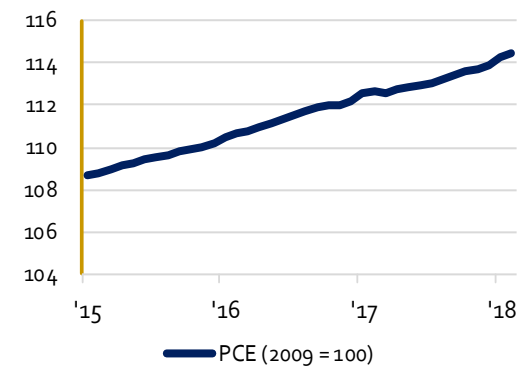
## Real GDP Growth



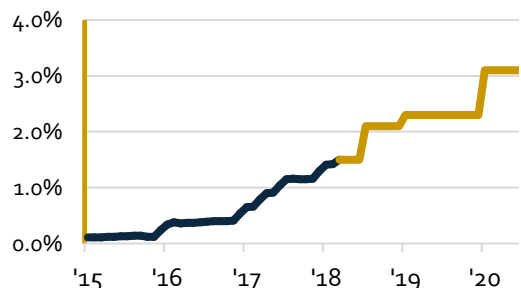
## Labor Force Participation



## Inflation Trends



## Federal Funds Rate



## Tariffs

Trade tensions are high between the United States and China. Both countries have threatened tariffs on \$50 billion worth of imports between the countries. A trade war between the two economic juggernauts would negatively impact global growth.

In March 2018, President Trump exercised his authority under Section 232, a safeguard to national security, to impose a 25% tariff on steel imports and a 10% tariff on aluminum imports. Temporary exemptions were provided for several countries, including Canada, Mexico, South Korea, and European Union members. This tariff exemption will expire on May 1, 2018.

Higher metal input prices could be a drag on profitability in certain industries that are unable to pass the cost through to consumers. Since the start of 2018, hot-rolled coil, the base price for rolled steel, has increased 30%. In addition, primary aluminum prices have been volatile.

## Oil Prices

Global oil supplies are beginning to come into balance with demand and supply. In January 2017, OPEC and its partners reduced their oil production. This measure would reduce oil inventories, causing oil prices to slowly recover. Since the production cuts were enacted, oil prices have risen by approximately 30%.

Over the past year, domestic oil production has surged, exceeding 10 million barrels per day. The majority of oil production growth has occurred in the prolific Permian Basin, which stretches from western Texas to eastern New Mexico. The Permian accounts for 30% of domestic oil production. However, growth in this basin may be constrained because of insufficient takeaway capacity.

Oil prices have reached their highest level since December 2014, with WTI

crude oil trading at \$68 per barrel and Brent crude oil at \$74. As a result, sustained higher oil prices could erode some of the benefits from lower taxes.

## Interest Rates

Under the new leadership of Jerome Powell, the Fed raised its short-term rate target to between 1.50% and 1.75%. The Fed signaled that it would raise its benchmark rate 25bps two more times in 2018 and three times in 2019.

The Treasury yield curve continues to flatten. Spreads between 2-year and 10-year Treasury yields continue to tighten. Recently, the spread fell 50 basis points, a level not seen since 2007. A negative spread precedes an economic downturn.

## Unemployment

The unemployment rate continues to remain at a 17-year low. Over the past six months, the unemployment level has held steady at 4.1%. Low unemployment levels are supported by lower corporate taxes and elevated government spending. Despite low unemployment, wage inflation has not increased significantly. Further strengthening in the labor market should put upward pressure on wages. As a result, companies in labor intensive industries could experience profit margin erosion. According to the Federal Reserve Board members' forecasts, the median unemployment rate is expected to decline to 3.8% and 3.6% in 2018 and 2019, respectively.

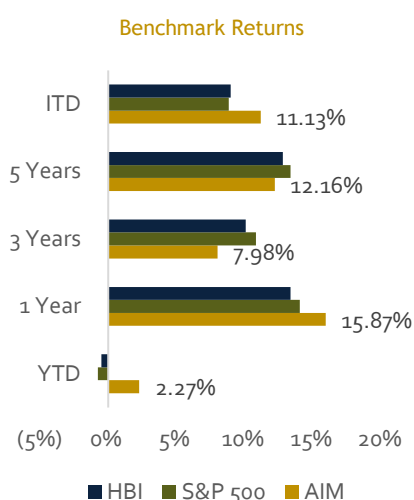
## Inflation

Bond yields have been increasing as the market anticipates higher levels of inflation. Since the beginning of 2018, the yield on 10-year Treasuries has increased 55 basis points to yield 296. Core PCE inflation increased 1.6% year-over-year in February. Analysts are expecting core PCE in March to reach 2.0%. This would mark the first time PCE has reached the Fed's 2% target since December 2011.

# Portfolio Performance

## Benchmark Comparisons

Since its inception to date ("ITD", since January 1, 1996), the AIM portfolio has outperformed its relative benchmarks – the Russell 2000, S&P500 and Hank Blended Index (a composition of 35% Russell 2000 and 65% S&P 500). This is also the case in the AIM portfolio's year-to-date (as of April 15, 2018) and last one year. However, in the last three years and last five years, the portfolio has underperformed its benchmarks.



## Portfolio Attribution

The current AIM portfolio (as of 4/15/2018) has become overweight in sectors such as Financial Services and Producer Durables. However, Consumer Discretionary and Consumer Staples remain underweight. Correcting these over and under-weightings were a priority during AIM XLVI's security selection process.

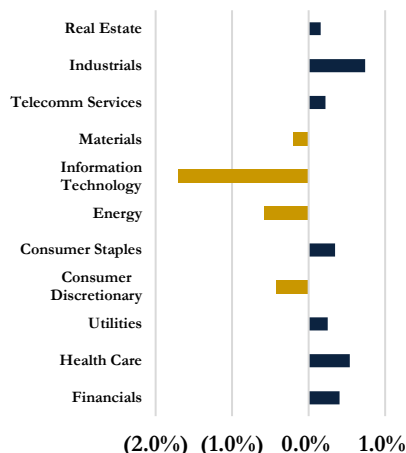
	Policy	AIM	Differential
Consumer Discretionary	12.6%	8.0%	(4.6%)
Consumer Staples	7.6%	4.0%	(3.6%)
Energy	6.0%	4.0%	(2.0%)
Financial Services	14.6%	23.5%	8.9%
Health Care	13.7%	16.4%	2.7%
Materials & Processing	2.9%	4.0%	1.1%
Producer Durables	10.1%	16.2%	6.1%
Technology	25.0%	20.1%	(5.0%)
Utilities	2.8%	3.8%	1.0%
Real Estate	2.7%	0.0%	(2.7%)
Telecommunication Services	1.9%	0.0%	(1.9%)

## Sector Updates

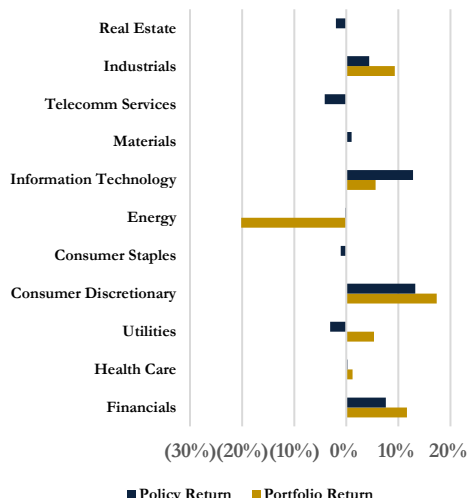
The net management effect is 0.49% for all portfolio holdings, which indicates a moderate ability to manage the

overweight and underweight holdings relative to the primary benchmarks.

Net Management Effect



Portfolio Returns vs. Target Returns



## Technical Indicators

Alpha relative to all major benchmarks has been decreasing, indicating decreasing abnormal returns over what is predicted by CAPM. Over the past two quarters, Alpha relative to HBI and S&P is essentially zero while Beta (1.03), is currently above/in-line with the S&P 500. Additionally, the standard deviation is close to historically low levels, and the tracking error is below 2% for the S&P 500 benchmark. The Treynor ratio remains at 2-year lows, indicating that returns are not keeping up with the amount of risk being taken on. Similarly, the Sharpe Ratio of 0.3 sits near 5-year

lows. By comparison, the S&P 500's Shape Ratio is roughly 1.3 over the same time period.

## Stock Performance

In the last year (since April 13, 2017), the AIM portfolio has seen substantial success in the performance of several holdings including Trupanion and Paypal Holdings, returning 85.4% and 79.3%, respectively. Numerous tech holdings have seen massive gains as well, with Palo Alto Networks gaining 71% and Microsoft gaining 45%. The poorest performing stock in the past 12 months has been Impinj, Inc., with a -57% return. Kinder Morgan and Under Armour are the only others to have lost value in the past year, declining by 26% and 20% respectively.

Since the last cohort (November 29, 2017) the five best-performing stocks have been Palo Alto Networks (33%), Bookings (23%), Ritchie Brothers Auctioneers (23%), Total System Services (21%), and TransDigm (17%). The five worst-performing stocks for this same period have been Impinj (-46%), Trupanion (-8%), Exelon (-7%), Southwest Airlines (-7.0%), and Facebook (-5%).

## Past 12 Months Performance

### FIVE BEST PERFORMING STOCKS

Trupanion	85%
Paypal Holdings	79%
Palo Alto Networks	71%
Total System Services	63%
Microsoft	45%

### FIVE WORST PERFORMING STOCKS

Impinj	(57%)
Kinder Morgan	(26%)
Under Armour	(20%)
Southwest Airlines	1%
Exelon	11%

# Portfolio Composition

The intent is to have an equal portfolio weight across 25 selected stocks. Note, the two Alphabet stocks (GOOG and GOOGL) are considered singular and have been held in the portfolio since before the class-share split.

Company Name	Ticker	Number of Shares	Price per Share (April 23, 2018)	Position Value	Portfolio Weight
Activision Blizzard, Inc.	ATVI	8,800	\$64.82	\$570,416	4.2%
Alphabet Inc	GOOGL	340	\$1,022.99	\$347,817	2.6%
Alphabet Inc	GOOG	170	\$1,021.18	\$173,601	1.3%
Apollo Global Management, LLC	APO	18,820	\$28.10	\$528,842	3.9%
Arconic Inc.	ARNC	23,880	\$22.15	\$528,942	3.9%
Biogen Inc.	BIIB	1,960	\$269.45	\$528,122	3.9%
Cleveland-Cliffs Inc.	CLF	70,700	\$7.48	\$528,836	3.9%
Comerica Incorporated	CMA	5,500	\$96.07	\$528,385	3.9%
Dollar Tree, Inc.	DLTR	5,460	\$96.91	\$529,129	3.9%
Exelon Corporation	EXC	13,500	\$39.16	\$528,660	3.9%
Facebook Inc	FB	3,040	\$159.69	\$485,458	3.6%
Intercontinental Exchange Inc	ICE	7,670	\$73.21	\$561,521	4.2%
Kinder Morgan Inc	KMI	30,920	\$16.26	\$502,759	3.7%
Lockheed Martin Corporation	LMT	1,605	\$329.50	\$528,848	3.9%
Microsoft Corporation	MSFT	6,450	\$92.31	\$595,400	4.4%
Palo Alto Networks Inc	PANW	3,170	\$190.55	\$604,044	4.5%
Paypal Holdings Inc	PYPL	6,530	\$74.00	\$483,220	3.6%
Ritchie Bros. Auctioneers Inc	RBA	18,580	\$32.54	\$604,593	4.5%
Stryker Corporation	SYK	3,280	\$165.38	\$542,446	4.0%
The Kraft Heinz Company	KHC	9,300	\$56.85	\$528,705	3.9%
The Walt Disney Company	DIS	5,230	\$101.15	\$529,015	3.9%
Thermo Fisher Scientific Inc.	TMO	2,780	\$214.47	\$596,227	4.4%
Total System Services, Inc.	TSS	6,940	\$84.49	\$586,361	4.3%
Trupanion Inc	TRUP	18,300	\$26.18	\$479,094	3.5%
UnitedHealth Group Inc	UNH	2,395	\$234.90	\$562,586	4.2%
Waste Management, Inc.	WM	6,510	\$81.25	\$528,938	3.9%
Cash				\$10,232	< 0.1%
<b>Total AIM Portfolio</b>				<b>\$13,522,192</b>	<b>100.00%</b>

# Alumni Update



**Aldo Arcieri**

Senior VP, Head of West Coast Fixed Income Sales at HSBC  
AIM XXVII, MBA Class of 2008

## ***What has been your career path since AIM?***

Our MBA class graduated during the throes of the financial crisis. A few of us had been blessed to secure Sales & Trading positions the summer prior. I was putting in my time on the UBS High Yield sales desk in late 2009 before transitioning over to Investment Grade sales. An opportunity emerged in San Francisco when the market began to open to new corporate issues, and I moved from New York City to San Francisco in 2010 to focus solely on West Coast clients. In 2014 I was recruited to HSBC where I now run a small team of Fixed Income salespersons focusing on Investment Grade, Emerging Markets and Rates products.

## ***What was the most valuable skill that AIM provided you?***

There were countless lessons and skills translated and it's a bit tricky to distill it down to just one. That said, Professors McDonald and Langley challenged us to be more than just your role and not be satisfied. In essence, are you ready to outwork your competition? Spend the additional time either within or outside your discipline to build a sound knowledge base and find ways to continue adding to your skill set.

## ***What has been the most valuable professional lesson you have learned since graduation?***

Embrace new opportunities that at first seem out of reach or outside of your comfort zone. Very few of my career moves revolved around turning down opportunities. The times when I was nervous or uncertain about whether I could perform, it was having the faith that I could ultimately deliver down the road that got me through any early rocky starts. Rely on your body of work and understand that the individuals who put you in those new roles have the faith in you to deliver.

## ***What were the stocks you covered and your opinion on them?***

I was assigned Zimmer Holdings and spent a fair deal of time delving into the exotic world of joint replacements and medical devices. We maintained our holding before it was sold three AIM classes later for a slight loss. My second stock was Intercontinental Exchange (ICE). While I recall liking their aggressive CEO Jeffrey Sprecher and equally aggressive acquisition strategy, the valuation at the time was a bit stretched.



**Thomas Laughner**

VP of Mergers and Acquisitions at Worley  
AIM XXXVII, MBA Class of 2014

## ***What has been your career path since AIM?***

After graduation, I spent three years as a Director at E&A Companies; a Multi-Family Office that focuses on direct private equity investments in the lower middle market. In that role I actively sought out new platform companies as well as provided valuation, due diligence, and support throughout the deal process. In February 2017, I started in my current role as VP of M&A at Worley Claims Services. Worley is a PEG backed company that specializes in insurance claims management. In this role, I lead our M&A efforts covering everything from deal origination all the way to post-close integration.

## ***What was the most valuable skill that AIM provided you?***

Identifying value and anticipating questions. The majority of my time is spent evaluating businesses in a lot of different industry categories. AIM not only provided me with the hard technical skills to model out and identify a company's intrinsic value, but it also pushed me to poke holes in my own assumptions, anticipate questions, and prepare answers. That skill has been invaluable to me in being able to present investment theses to executive teams and investment committees.

## ***What has been the most valuable professional lesson you learned since graduation?***

Networking. I know this may not be the most unique answer, but in my experience building meaningful relationships and networking is one of the fastest ways to succeed and one of the strongest indicators for someone having long term success.

## ***What were the stocks you covered and your opinion on them?***

I inherited Jos. A. Bank a couple weeks prior to Men's Warehouse's public announcement of a hostile bid to buy Jos. A. Bank. It was a great discussion each week about whether or not the deal would be consummated. The stock received a healthy bump after the announcement, and the class sold the stock. My second stock was Kinder Morgan Inc., a US based energy infrastructure company. I recommended a buy in 2014. The class added the stock and it remains in our portfolio as one of the historically worst performers. Ouch.

# Class XLVI Profile

Analyst	Email (@nd.edu)	Hometown	Internship	Post-Graduation Plans	Second Stock	Ticker
Jan E Alam	jalam	Lahore, Pakistan	Ecolab	Exelon	NextEra Energy	NEE
Gabriel Albuquerque	galbuque	Belo Horizonte, Brazil	AFS Investment Boutique	Undecided	Alphabet	GOOG
Sonakshi Bahety	sbahety	Indore, India	Ecolab	Ecolab	TransDigm Group	TDG
William Bowser	wbowser	Grand Rapids, MI	N/A (1-Year MBA)	Ottawa Avenue Private Capital	Apollo Global	APO
Matthew Bushland	mbushlan	Austin, TX	BMO Capital Markets	Undecided (College Jr.)	Dollar Tree	DLTR
Kyle Carlson	kcarlso2	Bay City, MI	Goldman Sachs	Vanguard	Waste Management	WM
Robert Cowen	rcowen	Ashland, OH	Parker Hannifin	Ernst & Young	Cleveland-Cliffs	CLF
Nicolas DeLong	ndelong	Stevensville, MI	N/A (1-Year MBA)	Undecided	Costco Wholesale	COST
Yash Dhariwal	ydhariwa	Ahmedabad, India	ACI Worldwide	ACI Worldwide	Thor Industries	THO
Michael Driscoll	mdrisco8	Madison, NJ	Sintokogio	Undecided	Antero Resources	AR
William Garland	wgarland	Virginia Beach, VA	Intel	Intel	Starbucks	SBUX
Conor Hogan	chogan5	Harleysville, PA	Lazard	Undecided (College Jr.)	Alexion Pharmaceuticals	ALXN
Jintao (Charles) Jiang	jjjiang1	Zhengzhou, China	JD Finance	Undecided	Biogen	BIIB
Matthew Kauffmann	mkauffm1	Raleigh, NC	Belveron Partners	Undecided	Amerco	UHAL
Raja Krishnan	rkrishn2	Princeton, NJ	N/A (1-Year MBA)	Undecided	Azul	AZUL
Garrett Leahy	gleahy	St. Louis, MO	Ford	IBM	TerraForm Power	TERP
Nicholas Lotz	nlotz	Ramsey, NJ	PPG Industries	PPG Industries	Arconic	ARNC
Patrick McHail	pmchail	Harrison, ID	McHail Consulting	Undecided	Hexcel	HXL
George Renaldi	grenaldi	Hinsdale, IL	BP Capital Management	BP Capital Management	Disney	DIS
Brock Reneer	breneer	Princeton, IN	KeyBanc Capital Markets	KeyBanc Capital Markets	Escalade	ESCA
Eric Salter	esalter	El Cajon, CA	Ernst & Young	Ernst & Young	Comerica	CMA
Jack Shannon	jshanno4	Chicago, IL	Dimensional Fund Advisors	Undecided	WestRock	WRK
Jocelyn Susilo	jsusilo	Jakarta, Indonesia	Nomura	Undecided (College Jr.)	Kraft Heinz	KHC

AIM  
Newsletter

University of Notre Dame  
Mendoza College of  
Business