2022 Mead Capital Management Annual Letter

	MCM Performance Vs. Benchmarks			
	MCM	MSCI	SPY	Russell 2000
2018..	(3.0%)	(9.2%)	(4.6%)	(11.1%)
2019..	18.1%	26.6%	31.2%	25.4%
2020..	8.1%	16.3%	18.4%	20.0%
2021..	26.2%	18.7%	28.7%	14.5%
2022..	(13.9%)	(18.4%)	(18.2%)	(20.5%)
Compounded Annual Gain 2018-2022......	6.1%	5.3%	9.3%	4.0%
Overall Gain 2018-2022...........................	34.5%	29.6%	56.2%	21.9%

Note: MCM result is after fees.

Dear Partners,

On a composite basis and after fees[1] MCM client portfolios *declined* 13.9% for the year. I consider 2022 a very good year.

Those two introductory statements appear contradictory, but they are not. First, the performance, while negative in an absolute sense, beat all three of the major indexes against which I benchmark (S&P 500, MSCI World Index, and Russell 2000) by over 4 percentage points. This relative performance advantage is key to outperforming over time. Second, the down market allowed me to make active investment decisions that I believe improves our chances of future outperformance.

Let's start with that good 13.9% decline. Down years are part of the investing "game". Human nature guarantees that greed and fear will periodically grip markets and consequently that they will overshoot in either direction.

Consider the following hypothetical investment results of two investors over two years. We'll call them Bill and Bob, both of whom beat the index by 5 points one year and match it the other year. Bill gains his advantage on the upside while Bob outperforms on the downside.

[1] See important disclaimers at the back.

	Bill	Bob	Index
Year 1	+20%	+15%	+15%
Year 2	-10%	-5%	-10%
CAGR	+8.0%	+9.25%	+3.5%

We come away with two conclusions. One is that outperformance can occur in either direction. It seems obvious that doing better in an up year and matching performance in the other year would lead to outperformance. It might even seem obvious that doing better in a down year (i.e., less bad) will lead to outperformance.

Looking deeper we observe that outperforming in a down year creates a disproportionate two-year gain. Both Bill and Bob outperformed by 5 percentage points. Yet Bob walks away with a two-year compounded gain some 1.25% greater than Bill and far ahead of the index. Or, said another way, Bob could have underperformed by 1.3% during his up year and still matched Bill's record. The lesson here is that downside protection works, and it comes with a bonus. Doing less bad means less ground to make up later. To use a simple example to drive home the point: A 10% decline requires an 11% increase to return to zero.

MCM's 5-year track record now includes two years of downside outperformance. In 2018 the 3.0% loss was 1.6% better than the S&P and in 2022 the 13.9% loss was 4.3% better. I chose the S&P 500 here so I wouldn't be accused of being selective. The five-year result still trails by 3.2% on a compounded basis because of the three other years in the series. Those monstrous returns in 2019, 2020, and 2021 were in my mind a result of low interest rates, fiscal stimulus, and some exuberance; at best they represent a pull-forward of future returns. Still, the record is the record.

But I need not make excuses. MCM's record is better than the other two indexes over the full five-year period. Yet even if the record included outperformance over the S&P 500 there's still the luck factor. It's only been five years. I won't really know if I'm a better investment manager until probably the 10-year mark or perhaps after 20 years. What I do know is that I'm much more comfortable owning the wonderful businesses in our portfolio than any index.

A note on the three indexes benchmarked above: I chose them because they are large, widely available at low expense ratios, and tough competition. I can't compare exactly to them, or any other "style" index. It's up to you to decide if my past performance, present philosophy, and future outlook justify continuing (or joining) this partnership of separate account management.

So much for this year's lesson on the mathematics of compounding returns. Let's turn to the other part of my enthusiasm for the down market: active investment decision making.

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The main reason I'm happy with last year is that it afforded us the opportunity to invest in new companies at attractive valuations. In any given year I'm happy with one or two new ideas. In 2022 we welcomed four. On top of that we added to two positions already in the portfolio. In addition, new partners benefitted from getting into all constituent companies at what I consider good prices.

When I say active investment management the word active is in a relative sense. Look at the following table of year-end holdings. MCM client portfolios have owned a grand total of 13 stocks in the past five years. I believe that outperforming "the market" (pick your index) requires conviction and concentration. A focused portfolio allows more time to really get to know portfolio companies, their competitors, and industry dynamics. A "well diversified" portfolio of 30 or more stocks is, in my view, a recipe for burnout, surface-level thinking, herd behavior, and probably a good chance of being below average.

Mead Capital Management, LLC
Table of Historical Holdings

	Year ended December 31:				
Company	**2022**	**2021**	**2020**	**2019**	**2018**
Berkshire Hathaway	42.4%	51.0%	50.0%	68.3%	73.8%
Hingham Institution for Savings	20.2%	14.9%	10.5%	3.1%	
Copart, Inc.	7.0%	7.7%	10.4%	8.9%	5.5%
Boston Beer Company	6.5%	5.2%			
Creighton's PLC	6.1%				
Heineken Holding NV	4.7%				
Triumph Financial	4.1%				
Activision Blizzard	4.1%				
Synchrony Financial	2.7%	4.3%	6.8%	3.3%	2.6%
Cimpress PLC	1.3%	2.8%	4.8%	9.3%	6.3%
Nestle			1.2%	0.5%	0.4%
ALJJ Regional Holdings			0.1%	1.1%	1.4%
Trupanion				4.7%	3.8%
Total common equity	99.2%	85.9%	83.8%	99.2%	93.9%
Cash	0.8%	14.1%	16.2%	0.8%	6.1%
Total	100.0%	100.0%	100.0%	100.0%	100.0%
Equity securities #	*10*	*6*	*7*	*8*	*7*

Notes:
1. Heineken Holding NV includes ADRs

The portfolio turnover statistics below don't seem to jive with the 13-company list above. While a 29% average turnover ratio implies a holding period of about 3 years and 5 months – miles beyond the mere months most active fund managers' report – it still feels high.

Mead Capital Management, LLC
Turnover Summary

2018	67.8%
2019	0.4%
2020	61.5%
2021	6.1%
2022	28.7%

3 Year Average	32.1%
3 Year Median	28.7%
5 Year Average	32.9%
5 Year Median	28.7%

Portfolio Updates:

Let's look at the portfolio, starting with the newcomers:

Creighton's PLC

Creighton's is a UK-based beauty products company. It operates in three main segments: private label (about half of revenues), in which it manufactures beauty products for sale under the name of a retailer; contract manufacturing (a quarter to a third of revenues) in which it manufactures other company's products using their own formulas; and owned products (around 20%) of revenues) representing its own in-house branded product lines. Creighton's is tiny with just £61 million of revenues in 2021.

A couple of things attracted me to the business. For starters, it is a simple business with a long history and long tenured/experienced management. The Chairman and Managing Director (CEO or President equivalent in the US) have been with the company since 2000. Their communications struck me as rational and shareholder friendly.

On the operations front the business was very clearly in the process of gaining economies of scale. Revenue growth was leading to operating efficiencies which was leading to higher margins. Consequently, returns on invested capital, perhaps *the* most important metric I care about, was increasing at an exponential rate. In 2012 the business earned a pre-tax ROIC of 5%; between 2014 and 2016 it increased to 9%; between 2017 and 2020 returns were in the low-to-mid 20s range; and in 2021 pre-tax ROIC was 31%.

Lastly, the business was available at an attractive price with clearly defined reasons for being undervalued. For starters, Creighton's market cap at the time I started buying was around £45 million, down from a high of over £100 million nine months before. A company of that size simply isn't worth the time for a fund of even modest size to consider. A $1 billion fund wanting to invest just 1% of assets would require a $10 million position. Shares would be difficult to acquire due to the low float and it would entail filing with the UK financial authorities (the threshold for disclosing ownership in the UK is 3%). Even a $250 million fund probably would be turned off by the illiquidity of the stock.

On top of that, the company just came from a year in which it earned one-time revenues/profits from the sale of hygiene products which it manufactured during the pandemic. An analyst looking at a small company with low float probably would be quickly turned off by a temporary boost to the bottom line. But their dismissal was our opportunity. Taking the time to understand what was happening beneath the surface revealed a company growing its underlying business at impressive rates.

Our shares are down 25% since purchasing them in May at an average cost of 48 pence. Interestingly, exchange rates have only contributed 1% to the decline. At one point in September, however, the exchange rate alone put our investment down 12%. Some of you might be wondering if we should hedge our exposure to the Pound. For me, that gets into the realm of macroeconomics and predicting relative currency movements, etc., and would add an ongoing layer of costs. I expect to own Creighton's for a long time, and if I'm right about the business and the degree of undervaluation, any currency movement up or down will be a minor part of the total return.

Heineken

With 12% of worldwide market share, Heineken is the world's second largest brewer of beer behind industry giant Anheuser-Busch InBev. Though half the size of ABI, Heineken has important characteristics that make it a better investment, in my view. Like ABI, Heineken maintains dominant positions in key markets throughout the globe that give it the scale and breadth needed to generate very good, protected returns on capital. In other words, it has a clear scale-based and brand-driven moat.

Heineken is run by a great-granddaughter of the company's namesake founder. She and her family effectively control the company via a unique holding structure. Controlling the company means Heineken can ignore the more short-term oriented holders of its stock and focus on building value over the long-term. It can wait patiently to make transformative acquisitions. For example, it saved $2 billion by ignoring Wall Street and acquiring a major Brazilian brewer half a decade after Wall Street was hot on the deal. And it can plant seeds that take years to grow, such as its investment in Vietnam in reusable bottles and moped-based distribution system.

Heineken is well positioned to benefit from world population growth and premiumization (reaching for more expensive beers) as billions climb out of and beyond poverty.

Triumph Financial

Triumph joined the ranks of our portfolio in December 2022. This $5.5 billion (assets) Texas-based bank is squarely focused on becoming the leader in the relatively boring-sounding transportation payments business. The company arrived at that aspiration after trying its hand in a few other financial industries such as healthcare finance and asset management, looking to move beyond its simple deposit-and-lend community banking operation. Triumph entered the factored receivables business in 2012 attracted to their high yield (companies that make a sale on credit can sell their receivables to a third party for a discount or fee in exchange for immediate cash). Not content to simply remain a participant, Triumph co-founder and CEO, Aaron Graft, began looking for ways to remove inefficiencies from the business.

Factored receivables earn very high yields, sometimes into the 20% range. This may seem high, and it is. But it's not for the reason you might think at first glance. Factored receivables have high yields not because of credit risk (the risk of getting stiffed) but primarily because of the high cost of servicing accounts. With an average invoice of $2,000, it takes very few dollars to add up to a meaningful percentage of the invoice.

Enter TriumphPay. TPay is Triumph's solution to the antiquated method of moving an invoice from presentment to audit to collection largely based on paper and phone. Its structured data allows participants in the transaction to see and confirm data electronically, drastically reducing costs. I love that this ambition is a win-win for Triumph and the industry. If it succeeds, and it looks like it will – after just one year these network transactions already surpassed the $1 billion mark – Triumph could be a big part of the some $400 billion annual transportation factoring market.

You might expect a company like this to sell at a premium. In fact, it did not long ago. Shares were as high as $135 at the end of 2021 and fell to around $55 when I began buying. Our cost basis implies a valuation of around $1.2 billion. The core community bank should continue to earn $50 million to $60 million pre-tax, and the factoring business should earn $100 million. That means we're effectively getting the upside of the payments business for "free". I like those odds.

Activision Blizzard

Activision Blizzard is a merger arbitrage investment I made on the heels of the 2022 Berkshire Hathaway Annual Meeting. Is it a Warren Buffett coattail investment? Yes. But it's mine too and I'll own it – both literally and figuratively – no matter how it plays out.

The rationale is straightforward: Microsoft offered, and Activision accepted, $69 billion or $95 per share in cash to buy the company. Yet shares continue to trade at around $75 per share, a whopping $20 or 21% discount. Why? In a word, regulators. The market is worried that the sale will be blocked on anti-trust concerns either or both in the United States or Europe.

Now, it's a friendly transaction from the standpoint of the primary participants. We're not speculating on a hostile takeover or some other corporate action to unlock value. The holdup is an argument that Microsoft will gain a monopoly position in a certain segment of the video game market.

Wall Street doesn't know what to make of the situation. For starters the deal isn't slated to close until May 2023, almost a year after we purchased shares. Then there's the ongoing uncertainty over whether it'll be blocked or not.

Our average price is just over $77 per share. If I'm right and the deal closes, we'll earn a return of almost 24% over the course of a year. As a bonus, if it closes in May or later, we'll benefit from the gain being treated as long-term. If I'm wrong and the deal falls through shares will probably decline. By how much? I don't know. It would likely be below our purchase price. But Activision is a good company. It earned $1.7 billion on $7 billion of revenues in the last twelve months. Those are real profits that would serve as a backstop, albeit one that could be far below our cost. Given the 24% upside potential I'm comfortable making that bet.

Berkshire Hathaway

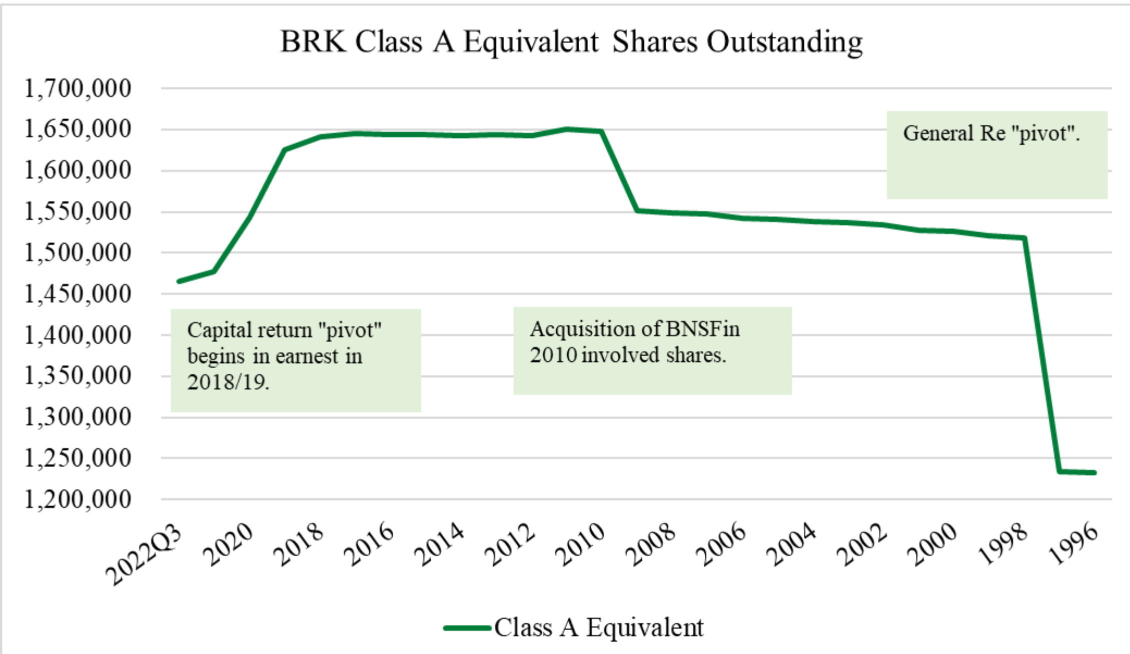
Berkshire is now 42% of client accounts, down from 51% at the end of last year. In 2018 it was almost three-quarters of the portfolio. This decline in allocation has nothing to do with price. In fact, Berkshire's share price has increased over 50% since 2018. The reason for the decline is the change in my relative appraisal of Berkshire's attractiveness compared to other opportunities.

Berkshire has always been my rock-solid opportunity cost benchmark. It's a company I know extremely well, and it has a satisfactory and steady (if limited) earning power. And even at this "low" of 42% of the portfolio it's still probably considered a recklessly high allocation by many. That's fine by me. Berkshire is a gem.

Berkshire Hathaway After-Tax Earnings ($ millions)	**Oct. 1, 2021- Sept. 30, 2022**		**Oct. 1, 2020- Sept. 30, 2021**		**Oct. 1, 2019- Sept. 30, 2020**		**Oct. 1, 2018- Sept. 30, 2019**	
Insurance - underwriting	$38	*0%*	$57	*0%*	$99	*0%*	$957	*4%*
Insurance - investment income	5,703	*18%*	4,858	*19%*	5,212	*24%*	5,248	*22%*
Railroad	6,162	*20%*	5,798	*23%*	5,092	*24%*	5,429	*23%*
Utilities and energy	3,657	*12%*	3,441	*14%*	3,039	*14%*	2,754	*12%*
Manufacturing, service and retailing	12,312	*39%*	10,796	*43%*	8,063	*38%*	10,446	*45%*
Other	3,497	*11%*	280	*1%*	(223)	*-1%*	(1,392)	*-6%*
Operating earnings, after tax	**$31,369**	***100%***	**$25,230**	***100%***	**$21,282**	***100%***	**$23,442**	***100%***
Investment and derivative gains/losses	($32,706)	*-104%*	$60,805	*241%*	($25,504)	*n/a*	$4,617	*20%*
Net earnings (loss)	($1,337)	*-4%*	$86,035	*341%*	($4,222)	*-20%*	$28,059	*120%*

Note: Other adds back goodwill/intangible impairments of $10,863 for the TTM 2020 period and $129 for the TTM 2021 period. The TTM 2022 period includes $2.7 billion of foreign currency gains.

Berkshire retired about $5 billion or 1% of its shares over the first nine months of 2022. I'd expect the full year number to come in modestly higher. Berkshire likely picked up some additional marketable securities in the 4th quarter at the expense of more aggressively purchasing its own shares. The share count today is just 19% above where it was in 1996 prior to the Gen Re and BNSF acquisitions, both of which used shares as currency. Notwithstanding any major acquisition that involves shares (unlikely at current valuation levels), and possibly one year of aggressive buybacks, we might see a 1996-like share count return in 2028 – almost assuredly prior to Buffett's 100th birthday in 2030. But I digress…



Berkshire sat on a cash pile (ex. rail / energy) of $105 billion at the end of Q3, so it has the firepower for repurchases or acquisitions and probably both. The company is a cash-generating machine. Let's look at operating earnings for the trailing twelve months ended 3Q2022:

BNSF: The rail brought in $6.2 billion of after-tax earnings. We will probably hear that carloadings are down, especially in consumer sectors, when BRK reports earnings in a week or so. That shouldn't affect the rail's earning power that much given its importance to a growing western United States.

BRK Energy: The stable utility business is a consistent earner. It earned $3.7 billion after-tax and will probably report higher earnings for the full year 2022. These earnings increase largely because of additional capital investment. Berkshire hasn't taken a dime of dividends from its energy business since purchasing MidAmerican Energy over two decades ago. But the cash-generating ability is real. Last year we saw Greg Abel sell his $870 million stake to BRK. We'll see if the Scott family sells its interest this year.

MSR: The manufacturing, service and retailing businesses span the gamut. They earned $12 billion TTM and should report good but mixed results for the full year. Included in this segment are the homebuilders and the auto business, which have been strong lately. Some of the consumer businesses will probably retain weakness going into 2023.

Underwriting: I include an allowance for insurance underwriting profits in my valuation framework given its history. At current premium levels of $72 billion BRK should earn $2.9 billion in normalized pre-tax from underwriting activities. Results for full year 2022 will show some weakness due to storms, catastrophes, and continuing weakness at GEICO.

Equity method: Berkshire also has partial interest in Kraft Heinz, Occidental Petroleum, Pilot Flying J, and Electric Transmission Texas that earn about $1 billion per year.

Insurance income: My valuation framework doesn't capitalize insurance dividends and interest because I count the asset value separately (that would be double counting). But in looking at BRK's cash-generating ability it has a nice $5 billion per year stream of cash coming in from dividends and an increasing stream of interest income thanks to higher rates.

Add all these and you come to a cash-generating ability of around $30 billion per year. That's hard, take-it-to-the-bank cash that Berkshire can invest organically, make bolt-on or other acquisitions, or repurchase stock. Berkshire also has a lot going for it going into 2023. It just purchased Allegany Corp for $12 billion, which will increase its earning power and float. It will also increase its stake in Pilot Flying J to 80% this year, laying out capital and increasing earnings at essentially no additional risk since it already knows the company well.

The market appears to be pricing Berkshire at a 9% going-forward return.[2] For such a high-quality collection of businesses that is a good return. But it gets even better. It assumes no insurance underwriting gains, which Berkshire has historically generated. It doesn't include any optionality from the significant cash resources on the books, nor any benefit from organic growth in float, which is a possibility. In sum, Berkshire is a wonderful collection of many very good businesses that remains attractively valued.

[2] After tax earnings of $22.1 billion divided by the implied residual value of the operating businesses of $250.7 billion.

Breaking down Berkshire Hathaway's market value
What do we get for our money?

($ millions)		*% market cap*
Market capitalization on February 3, 2023	$675,000	*100%*
Balance sheet totals as of September 30, 2022:		
Insurance cash & Treasuries	$105,201	*16%*
Equity securities (net of deferred tax)	271,757	*40%*
Equity method investments	28,714	*4%*
Fixed maturity investments	18,602	*3%*
Subtotal cash & investments	$424,274	*63%*
Implied residual value of operating businesses	$250,726	*37%*
After-tax earnings (12 mo. 9/30/22):		
BNSF Railroad	$6,162	
Utilities & energy	3,657	
Manufacturing, service, and retailing	12,312	
Subtotal - after-tax earnings	$22,131	
Value assuming 10x	$221,310	*33%*
Value assuming 15x	$331,965	*49%*

Assumes:
1. Equity & debt securities are fairly-valued.
2. Breakeven insurance underwriting ($38m profit not included above).
3. MSR business results represent normalized earnings power.

Hingham Institution for Savings

Hingham is the perfect combination of simple business, trustworthy management, long runway, and price. My growing appreciation for the company is reflected in our increased ownership and 20% portfolio allocation. Only few companies deserve such weightings, and only Berkshire has been as large.

Hingham management continues to execute on its strategy of lending on low-risk real estate projects in the major gateway cities of Boston, Washington DC, and now San Francisco, while keeping overhead extremely low. The strategy is paying off. Hingham grew its balance sheet from $2.5 billion in total loans and $2.9 billion in total assets at FYE 2020 to $3.7 billion in loans and $4.2

billion in assets at FYE 2022. Core return on assets and equity were 1.89% and 17.3% in 2021, and 1.43% and 14.6% in 2022.

Only at Hingham does a poor quarter and weak finish to the year look like a decent result. Hingham's liability-sensitive balance sheet has taken a hit with the pace of interest rate increases, which means its cost of funding is rising much faster than what its assets are earning. Loan growth of 22% in 2022 mitigated the effect somewhat, as new loans carry up-to-date interest rates.

Results for Q4 2022 are illustrative. Net interest margin came in at a paltry 2.09% leading to a core ROA of just 0.96% and core ROE of 10%. Look at what transpired between Q4 2021 and Q4 2022:

Yield on / cost of	Q4 2021	Q4 2022	Change
Interest earning assets	3.68%	3.91%	+0.23%
Interest bearing liabilities	0.29%	2.24%	+1.95%
Spread	3.39%	1.67%	-1.72%

Again, not a bad result all things considered. It's Hingham's efficiency (efficiency ratio of 24% and operating expenses at just 70 bps of assets) that saved the day, on top of no net credit losses.

HIFS is a coiling spring. Shares have gone nowhere in two years despite quite meaningful business progress, and now trade at 1.6x book value. That's okay with me. It's been an ideal time to increase my ownership position. I only wish the bank could repurchase its own shares during periods of seriously depressed prices. I retain the utmost confidence in Hingham's management. This is a tough period but not one the bank hasn't navigated before. Here's Chairman Robert Gaughen (taken from the Q4 press release):

> "…During all such periods - whether fair or foul weather - we remain focused on careful capital allocation, defensive underwriting, and disciplined cost control - the building blocks for compounding shareholder capital through all stages of the economic cycle. These remain constant, regardless of the macroeconomic environment in which we operate."

You should be proud to be partners in such a wonderful enterprise. I sure am.

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Other portfolio companies

My thoughts on Copart (7% of the portfolio), Boston Beer Company (6.5%), and Synchrony Financial (3%) haven't changed since I wrote about them in prior years. I covered Copart and Boston Beer as Deep Dives for my investing newsletter, Watchlist Investing (a separate and distinct company). If you would like to read those analyses please let me know.

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The pari-mutuel system … in reverse

Charlie Munger has related investing to the pari-mutuel system of horse betting. Participants betting on horse races often know which is the best horse. But the payoff is typically miniscule because everyone knows which horse will win. The trick is finding misplaced bets such that you receive an outsized payoff compared to the odds of the horse you're backing. The analog in investing is that the obvious winners have their shares bid up to the point that even if the underlying company is successful the payoff isn't very large.

I found myself thinking about this as I contemplated selling our smallest portfolio holding, Cimpress, PLC. Cimpress, at 1.3% of the composite portfolio at year end, has been in the portfolio since day one. In fact, I've owned shares personally since 2014.

Cimpress, PLC

Operating statistics

$ in millions	2018	2022
Revenues	$2,600	$2,900
Gross profit margin	51%	48%
Operating margin	4.8%	2.1%
Operating income	$125	$61
Unlevered free cash flow	$189	$198

Major capital allocation 2018-2022

	Sources	Uses
Net income	$90	
Depreciation/amortization charges	$860	
Increase in net debt	$455	
Dispositions	$94	
Share repurchases		$764
Capital expenditures		$260
Acquisitions		$424
	$1,500	$1,448

Valuation

	2018	2022
Year end share price	$103.42	$27.61
Shares outstanding (millions)	30.9	26.1
Market value of equity	$3,201	$720
Net debt	$926	$1,466
Enterprise value	$4,127	$2,186
Operating income / EV	3.0%	2.8%
Unlevered free cash flow / EV	4.6%	9.1%

You might know Cimpress from its largest operating unit, Vistaprint, or perhaps have ordered or used pens from its National Pen business. Cimpress has multiple operating units, but all come down to what it calls mass customization – using technology to gain the economies of scale inherent in mass production but with customizable orders available on a smaller scale.

Our cost basis for Cimpress is $56 per share. Some accounts purchased shares at over $100 per share. As of this writing, shares trade at $40, which corresponds to a market capitalization of $1.5 billion. Cimpress faced many challenges over the past five years including the pandemic and now inflation. It's also shifted away from a discounting strategy to one of integrating with small businesses and providing design solutions to them. It has done this via numerous acquisitions that span the globe.

Over the past five years Cimpress management, led by Founder and CEO, Robert Keane, has allocated about $1.5 billion in capital. About half of that went to share repurchases and half went to acquisitions or capital expenditures. A large part or $860 million of that was funded via depreciation and amortization charges that flowed through the income statement. Another big chunk was funded via an increase in net debt.

The problem I face is the pari-mutuel system in reverse. By owning shares I've made the bet. But do I keep my ticket or sell it to another bettor at a lower price? Shares have declined so much (by about two-thirds from the end of 2018 to the end of 2022) that a potentially large future payoff makes holding shares the rational course of action. In other words, the horse has gotten worse, but the odds have increased significantly.

I'm conscious of the psychological biases that causes investors to hold when they should sell so that they don't have to recognize the loss, both in the financial and the psychological sense of the term. I don't think this is the case here. You might fault me for not selling earlier, and that's fair. But given where we are now, I find myself thinking the rational course of action is to hold. The business has made some (albeit slow) progress over the past year, and the outlook appears satisfactory, if not brighter. Most important, I trust Keane and appreciate his candid reporting to shareholders.

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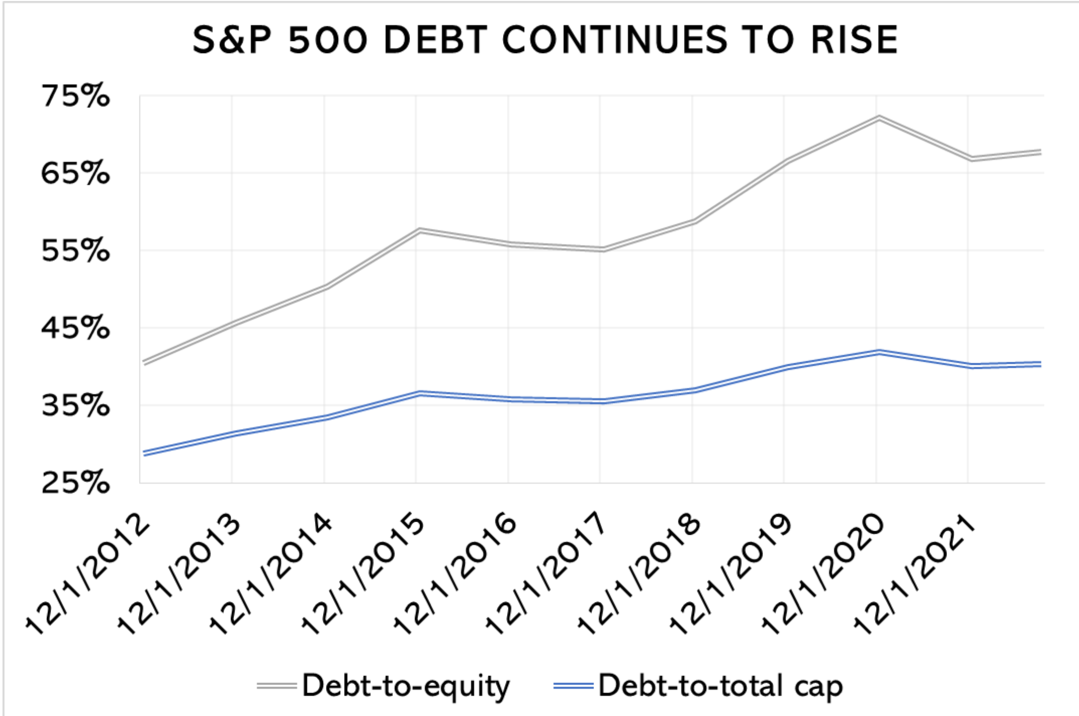
A closer look at the S&P 500

The Standard and Poor's website provides some interesting raw data on the index, open for anyone to see. These include operating earnings, net earnings, dividends, buybacks, and data on book value, among many other data points.

A few observations with updated data through September 30, 2022:

- The price/earnings ratio has come down from its multi-year highs but remains elevated at 17.6x trailing operating earnings. The inverse of the P/E ratio is the earnings yield. At 5.7% it doesn't jive with current interest rates. Why would you accept that yield when 100% safe US Treasuries were yielding 4% and on the rise? (Today you can get nearly 5% on a one-year Treasury.)

- The balance sheet of the S&P 500 continues to deteriorate. Debt-to-equity and debt-to-total capitalization remain elevated, a result of continued corporate borrowing.



- An investor purchasing the S&P 500 at 12/31/12 and holding through 9/30/22 would have earned a total return of about 12%. It would have come from 10% annual price appreciation and 2% dividends. But did that investor *deserve* such a return? Looking deeper the answer is no. Operating earnings over that period increased at just shy of 8%. The 4% difference represents the annualized increase in the price/earnings multiple. Investors over time shouldn't expect to earn more than what the underlying businesses earn.

- Worse, net debt per share from 2012 to 3Q22 increased at a 14% annualized clip. Companies increased earnings in part by leveraging their balance sheets. That's not a recipe for sustainable returns.

- Something must give, and indeed something has. The 18% negative total return on the S&P 500 in 2022 was a good start. But I'd say it has further to go. We've worked off and out some of the speculation we saw in the prior few years. Earnings very well might increase due to inflationary forces but with it interest rates will rise too. Once investors fully wake up to higher rates and realize alternative (and safer) places to put their money we could well see continued multiple compression. But I really have no idea. Anything could happen. Still, I'd continue to bet on mid-single-digit returns from the S&P over the next decade, maybe more if inflation sticks around.

Conclusion

Last year I wrote:

> *Many indicators point to market turmoil ahead. After more than a decade of low interest rates, generally rising markets, and government backstops, investors appear to have been lulled into a false sense of security about the future.*

All I can say this year is ditto. Each generation, unfortunately, must learn firsthand the lessons of history. If history is any judge it will take some time for today's investors to fully wake up to inflation, higher interest rates, and – gasp – the requirement for businesses to actually earn real cash profits.

Such an uncertain world portends opportunity for value investors. Those of us continuing to search for good businesses with simple business models, consistent business results, and favorable long-term prospects should thrive. These are the markets Mead Capital was built for. Good businesses don't change overnight, and bottoms-up fundamental analysis cuts through the fog of seemingly impenetrable uncertainty.

My confidence is bolstered by having wonderful client-partners. Each of you has added, in at least some small way, to my understanding of business and investing. I'm thankful for you trusting me with your hard-earned capital. As proof of just how awesome you are, I'm happy to report I received no panicked calls last year. Your understanding of what we're trying to accomplish together – building wealth by owning parts of good businesses – goes a long way in helping me achieve our goals. It gives me more time to read, think, focus, and analyze businesses, time of which you are the beneficiary.

While I prefer to offer my in-depth thoughts in long-form once a year, I very much enjoy speaking with clients. Don't be shy. I relish these days of small beginnings because the present size of Mead Capital allows me to interact with client-partners and not get overwhelmed by calls or feel that it detracts from research. It also allows me to search for and buy shares in companies others simply cannot because of their size. At some point in the future, I intend to close MCM to new clients to remain in this nimble state. If/when anything changes on that front, you'll be the first to know. In the meantime, I'd appreciate referrals to like-minded individuals.

I look forward to reporting to you in another year.

Rationally yours,

February 14, 2023

Important Disclosures:

Mead Capital Management, LLC is a registered investment adviser based in Derry, New Hampshire. Adam J. Mead is its principal, CEO, Chief Investment Officer, and managing member.

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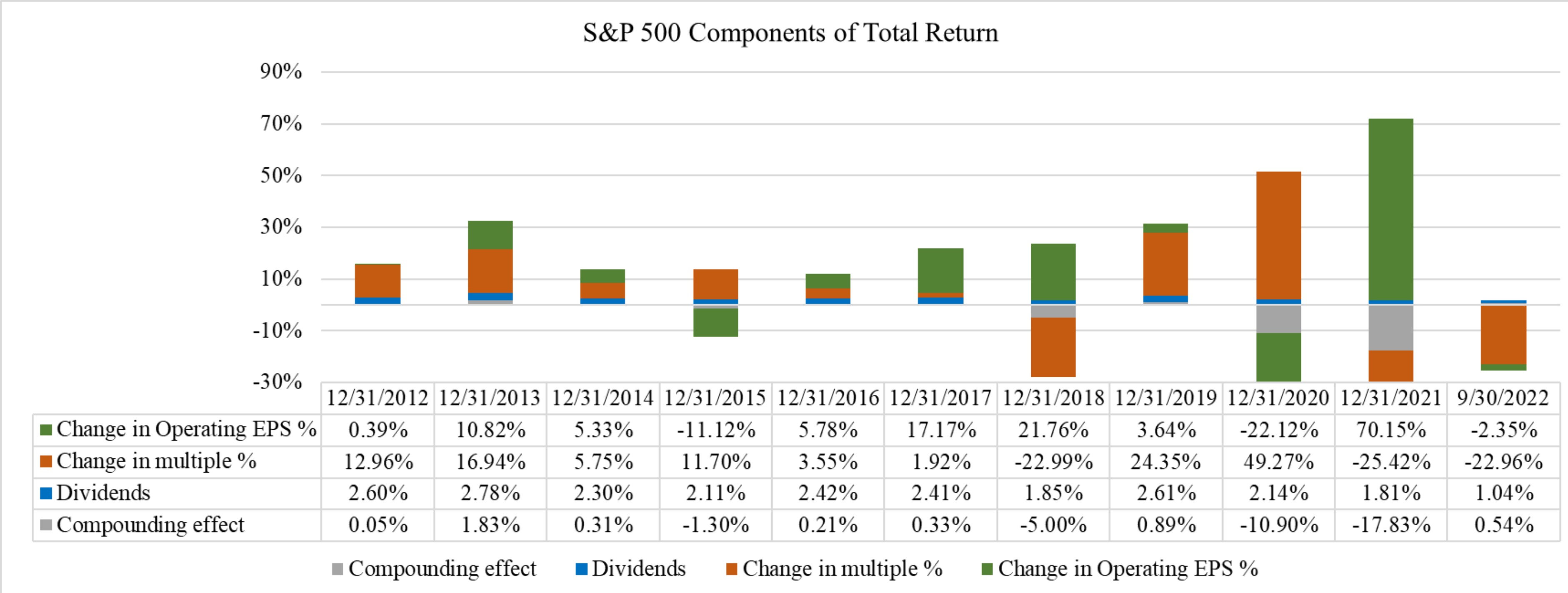
Past performance is not indicative of future performance.

S&P 500 Per Share Analysis

	12/31/2012	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018	12/31/2019	12/31/2020	12/31/2021	9/30/2022	Annualized Change ('12-'21)
S&P 500 Index	$1,426	$1,848	$2,059	$2,044	$2,239	$2,674	$2,507	$3,231	$3,756	$4,766	$3,586	14.35%
EPS (last 12 months)	$86.51	$100.20	$102.31	$86.53	$94.55	$109.88	$132.39	$139.47	$94.13	$197.87	$187.07	9.63%
Multiple	*16.5x*	*18.4x*	*20.1x*	*23.6x*	*23.7x*	*24.3x*	*18.9x*	*23.2x*	*39.9x*	*24.1x*	*19.2x*	4.30%
Price return	*13.41%*	*29.60%*	*11.39%*	*-0.73%*	*9.54%*	*19.42%*	*-6.24%*	*28.88%*	*16.26%*	*26.89%*	*-24.77%*	*14.35%*
Dividend %	*2.60%*	*2.78%*	*2.30%*	*2.11%*	*2.42%*	*2.41%*	*1.85%*	*2.61%*	*2.14%*	*1.81%*	*1.04%*	*2.27%*
Total return	*16.00%*	*32.38%*	*13.69%*	*1.38%*	*11.96%*	*21.83%*	*-4.39%*	*31.49%*	*18.40%*	*28.70%*	*-23.73%*	*16.61%*
Operating EPS 12mo	$97	$107	$113	$100	$106	$125	$152	$157	$122	$208	$203	8.9%
Multiple	*14.7x*	*17.2x*	*18.2x*	*20.3x*	*21.1x*	*21.5x*	*16.5x*	*20.6x*	*30.7x*	*22.9x*	*17.6x*	*5.0%*
Book value per share	$667	$716	$727	$740	$769	$827	$852	$914	$928	$1,008	$996	4.7%
Debt per share[1]	$270	$327	$366	$426	$430	$456	$500	$609	$669	$673	$674	10.7%
Cash per share[1]	144	174	184	192	203	228	196	222	272	258	238	6.7%
Net debt per share	126	153	182	234	227	229	305	387	397	416	437	14.1%
Debt-to-equity	40%	46%	50%	58%	56%	55%	59%	67%	72%	67%	68%	
Debt-to-total cap	29%	31%	33%	37%	36%	36%	37%	40%	42%	40%	40%	

Sources: S&P Indices data on S&P 500, and author's calculations.

Note: The S&P 500 total return for calendar year 2022 was -18.2%.



	12/31/2012	12/31/2013	12/31/2014	12/31/2015	12/31/2016	12/31/2017	12/31/2018	12/31/2019	12/31/2020	12/31/2021	9/30/2022
Change in Operating EPS %	0.39%	10.82%	5.33%	-11.12%	5.78%	17.17%	21.76%	3.64%	-22.12%	70.15%	-2.35%
Change in multiple %	12.96%	16.94%	5.75%	11.70%	3.55%	1.92%	-22.99%	24.35%	49.27%	-25.42%	-22.96%
Dividends	2.60%	2.78%	2.30%	2.11%	2.42%	2.41%	1.85%	2.61%	2.14%	1.81%	1.04%
Compounding effect	0.05%	1.83%	0.31%	-1.30%	0.21%	0.33%	-5.00%	0.89%	-10.90%	-17.83%	0.54%

Note: The compounding effect is the result of multiplying the change in earnings by the change in multiple. Each has an effect on the other when determining the overall change. For example, in 2020, the 22.12% drop in operating earnings was offset by a 49.27% increase in the price/earnings multiple. Simple addition would leave 27.15% plus the dividend of 2.14% for a total of 29.29%. The math works like this: (1 - 0.2212) x 1.4927 = 16.25% plus the dividend of 2.14% to get 18.40%.

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	Q4 2022	YTD 2022	Annualized Performance 1 Year	3 Years	5 Years	Inception
MCM	**11.7%**	**-13.9%**	**-13.9%**	**5.5%**	**6.1%**	**6.1%**
Avg. cash % NAV	*1.1%*	*4.9%*	*4.9%*	*11.4%*	*10.6%*	*10.6%*
MSCI	9.9%	-18.4%	-18.4%	4.1%	5.3%	5.3%
SPY	7.6%	-18.2%	-18.2%	7.6%	9.3%	9.3%
Russell 2000	6.2%	-20.5%	-20.5%	3.0%	4.0%	4.0%

Calendar Year Performance

	MCM	MSCI	SPY	Russell 2000
2018	-3.0%	-9.2%	-4.6%	-11.1%
2019	18.1%	26.6%	31.2%	25.4%
2020	8.1%	16.3%	18.4%	20.0%
2021	26.2%	18.7%	28.7%	14.5%
2022	-13.9%	-18.4%	-18.2%	-20.5%

Important notes and disclaimers about the performance table presented above:

MCM includes all accounts managed by Mead Capital Management on the Interactive Brokers ("IB") platform beginning on January 1, 2018, with the exception of one account open for less than two quarters. MCM's principal, Adam J. Mead, maintained accounts outside of IB during and prior to this time. These outside accounts were excluded because i) one proportionally-large account employed a strategy inconsistent with MCM's current strategy, and ii) to maintain consistency of reporting from IB.

MCM performance is after a 1.00% annualized fee or 0.25% per quarter (MCM's maximum fee) deducted from the performance data taken from IB. MCM believes this is conservative because some accounts managed by MCM paid fees through the IB account (the majority of accounts paid fees outside of IB or had no fee).

Calculations presented above are unaudited. They are believed to be accurate, however, MCM does not and cannot guarantee accuracy.

All performance results are unaudited and are not an estimate of any specific investor's actual performance, which may be materially different from such performance depending on numerous factors. Performance results may vary from account to account due to timing and other factors. No representations or warranties whatsoever are made by MCM or any other person or entity as to the future profitability of an investment account or the results of making an investment. All information provided is for informational purposes only and should not be deemed as advice in relation to legal, taxation, or investment matters. Past performance is not indicative of future results.

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The S&P Index return was determined by Interactive Brokers using the performance of SPDR S&P 500 ETF Trust (SPY). The MSCI Index return was determined using the performance of iShares MSCI ACWI ETF (AWCI). The Russell 2000 Index return was determined using the performance of iShares Russell 2000 ETF (IWM).

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