ROD CAPITAL
MANAGEMENT

LONG / SHORT & SPECIAL SITUATION FUND

Offices in Los Angeles, CA and Las Vegas, NV
admin@rodcapitalmanagement.com
310.801.8748

Q3
2023

Dear Investor,

In this letter we will review our performance in Q3 2023 including our biggest impact performers as well as our investment focus for the remainder of the year.

<u>Rod Capital Q3 2023 Results</u>

In the third quarter of 2023, Rod Capital was down -7.72%. The S&P 500 was down -3.28% and the Russell 2000 was down -5.14%. Year to date, Rod capital is up 10.18% while the S&P 500 is up 13.04% and the Russell 2000 is up 2.52%.

Our top long performer in the quarter was Sphere Entertainment Co. (SPHR), a position we opened in June 2023. The stock rose 36% during the quarter as people learned about the new spectacular Las Vegas attraction. We were able to acquire shares before it became well known at what we estimate to be a purchase price of less than a quarter of the company's adjusted book value.

Our top short performer was Opendoor Technologies Inc. (OPEN), a stock which fell 34% during the quarter. Insiders continue to sell their shares as the company – whose business model is highly questionable - burns through their remaining cash.

Our worst performer in Q3 was Magnachip Semiconductor Corp. (MX). The stock fell 26% in the quarter as the company has apparently not yet executed its new stock buyback program – which we did not expect. We are hopeful they will execute on their program next month.

<u>Q3 2023 Review</u>

The underlying engine of a growing modern economy are its people – how free they are to pursue opportunities, how hard they work, and how much calculated risk taking they do. The world is still returning from an odd time in 2020 which led to a massive amount of government stimulus – which, in turn, led to less working and more risk-taking. We're now in an era where hard work is rising again and risk-taking is declining. This could be a very long drawn-out cycle until the next big thing happens to our world.

In recent months, markets are beginning to reluctantly accept that interest rates are likely not going back down for some time. Recall, that a year ago, many experts were commenting that today we should be seeing rate cuts. But massive amounts of government spending and stimulus have led to both respectable economic performance and inflation pressure. Rate increases have not been enough to offset corporate gains.

Instead, government bonds have been selling off, which might be a sign that a future squeeze in government spending is imminent. But there is also an optimistic take – that taxes from steady growing inflating corporate profits will continue to secure government spending. And forward we march towards a moderate economy with harder work and less risk-taking.

This is kind of like my story. I've never worked harder and yet my risk tolerance has declined – to the detriment of our performance. That's because the market has had a different idea of managing risk tolerance than I have. The market's idea of risk moderation is buying Apple stock and S&P at whatever price and calling it a day. My idea has been buy a beat up small cap company well under its value and hide there. Or buy a special situation stock with an upcoming catalyst and take the money and run.

Well, this has proven to be a difficult strategy at this particular time.

But things change. And sometimes that change is quick and abrupt. Part of my job is to predict that change, not just assume the same unusual trend will happen forever.

Apple's market cap, incidentally, is the same as the lower three quarters of all American stocks – or all small caps combined. The top eight stocks together are over four times all of the small caps (and equivalent of all stocks under a $36B market cap combined – which leaves you with only around 200 stocks left). Market performance has been weak if you just remove the outperforming eight stocks.

For the next decade, a good economy will not necessarily mean that the S&P 500 will perform well. Small caps could fly and the super 8 stocks (AAPL, GOOG, MSFT, AMZN, NVDA, META, TSLA, BRK) could languish given their relatively high collective valuation in this new market dynamic. This reversed dynamic is essentially how I see things playing out and why I believe being an active stock picking manager is set up to pay off.

Now the hard part. What are we doing and what stocks are we buying and what are we shorting?

<u>Q4 2023 and 2024 Investment Focus</u>

As mentioned, we have opened a top 5 position in Sphere Entertainment Co. (SPHR). The company was created in a separation from Madison Square Garden Entertainment (MSGE) and was the result of $2.3B in construction costs to build a, "wonder of the world," as some have called it – a one-of-a-kind concert arena surrounded by high resolution LED screens on the outside and inside. The company trades at near a third of its adjusted book value. In other words, it trades as if it is a failed business venture. And yet, the whole world knows about it and the venue is beginning to offer breathtaking experiences.

Sphere has several upcoming catalysts in the next year: 1) they may sell or divest MSG Networks, which has no synergies with the Sphere. Sphere is not responsible for MSG Network's debt, but there is misunderstanding about that, and divestiture will simplify the balance sheet; 2) they may announce a major partnership/naming rights for The Sphere. This annual revenue would have no cost; 3) they may announce new acts and shows in the pipeline; 4) they may present first ever projections for future revenues and profit.

On the short side, we have a negative position in EXP World Holdings Inc. (EXPI). The company is a multi-level marketing real estate agent network that boasts 88,000 agents. Insiders hold a significant portion of the company's shares and are consistent sellers into a brilliant scheme. The company funds its operations by throwing a ton of shares at its employees to keep them interested, in the hope that they won't sell those shares. Meanwhile, they use all of their cash to purchase shares in the open market so that insiders can sell their shares. Each year, we calculate that over 10% of the company's shares are exchanging hands from institutions to the company's own agents. This, along with insider sales, is creating an unsustainable situation where unsophisticated agents are left holding the bag.

Our market exposure looks like this at the moment: we are about 180% long and 80% short after adjusting out a small number of unusual cases of companies with large cash positions (Nextdoor (KIND), for example, consists of roughly 80% cash and 20% enterprise value so we adjust out the cash since it is unusually large). Out of that net 100% after cash number, roughly two thirds of this exposure involve special situations such as mergers & acquisitions and special positioning for near-term events. This reflects our balanced view of a good-but-not-great economy and our conservativism regarding long-term growth. We are also closely monitoring our collective portfolio's use of leverage above net assets and keeping that within similar ranges.

The market is becoming more and more dangerous for unsophisticated investors going forward. I don't believe simply buying the S&P 500 and familiar stocks will keep working. A swift tide can change everything and blindside the passive market – as it has been savagely blindsiding the bond market of late. I continue to believe that the market has a need for more active managers who can help bring greater efficiency and prevent more painful financial events. Being proactive will soon have its day.

Please let us know if you have any questions. We hope you and your families are well and I look forward to writing you once again in a few months.

Best Regards,
Perry Rod
Chief Investment Officer
Rod Capital Management LLC

Contact: admin@rodcapitalmanagement.com
Website: www.rodcapitalmanagement.com