ASHVA
Capital Management LLC

July 2022

Dear Limited Partner,

The S&P500 ended the 1H 2022 at 3,785.38, reflecting a 20.6% year-to-date decline. As a result, it's possible that you've read various articles with financial journalists hyperventilating about the fact that this is the worst first half performance in 50 years. If we compare from the all-time high on the index of 4,796.56, the index is actually down 23.6%. Using either number we officially claim a bear market has started, based on the conventional definition of a decline greater than 20%. The primary concern weighing on investors has been the torrid pace of inflation combined with an overzealous Fed ready to hike interest rates until the economy dramatically slows. Although the recent sell-off still feels in many ways like a correction as opposed to a bear market, the biggest mistake you can make as an investor is to panic sell during significant market declines.

Bear Market Opportunity

Anyone invested in the stock market for virtually any length of time will inherently understand that volatility is normal. However, we must never forget that although stock prices continually fluctuate the underlying value of companies are relatively stable and tend to grow over time. Wharton Professor Jeremy Siegel has found that over the past 200 years stocks have produced a real return (after taking into account inflation) of 6.5-7.0%. Counterintuitively, equities will outperform even "hard assets" such as real estate and gold in an inflationary environment.

Since 1950, the S&P500 index has crashed by 20% or greater on 12 different occasions, including the most recent Covid crash in 2020. The average percentage price decline across all these bear markets was (33.4%). While the severity of the loss is important the duration of the downcycle also has a significant impact on investor psyches. Harvard researchers have found that people could endure high levels of pain if they knew it would only last a short time. However, the same subjects "gave up" more easily even with lower levels of pain if they were told it would last a long time. I feel the greater uncertainty for investors is not whether there is further downside, but how long this current downcycle will last. Based on the prior 12 occurrences the average length of a bear market was 342 days. Assuming that we're currently in an average bear market, we're probably half-way through at this point.

The key to not being scared out of stocks is to focus on the underlying value of the companies and not share price. Over time share prices will eventually reflect growth in the underlying fundamentals of the business. Share prices will track both earnings and free cash flow generation over time. In fact, the cheaper stock prices become in relation to the underlying the fundamentals the greater the potential for outsized returns.

Only charlatans claim they can time the market with any degree of accuracy. The best option for investors is to actually deploy capital as opportunities arise and then do nothing. The market may recover in the 2H 2022 or in early 2023. Nobody can accurately forecast the timing of the recovery. We can only have faith that the recovery will eventually occur and the market will move on to higher highs as it has done over the past 200 years.

Legendary investor Shelby Davis said the following: “a down market lets you buy more shares in great companies at favourable prices. If you know what you’re doing, you’ll make most of your money from these periods. You just won’t realise it until much later.” We’ve been adding to our existing positions and have also started a new position in Altria (MO). If the shares re-rate to their historical forward P/E level of 15x by 2024 the shares offer a total return of 115% or 36.3% annualized. Plus, the shares currently offer a market leading 8% dividend yield. Essentially, we’re getting paid to wait for sentiment to improve and the for the share price to find its footing.

Our Performance

The S&P500 has declined by 20.6% year-to-date. In comparison the Ashva Capital LP fund has declined only 19.0%. Although we’ve outperformed our benchmark index, it doesn’t provide much consolation to us. There is a strong likelihood that the US enters a recession in 2023. However, it’s important to note that the stock market doesn’t move in lockstep with economic growth. The market is a forward-looking discounting machine and will have bottomed well before the government officially declares the recession has ended. I personally believe that the bottom is already in and that we’re facing a relatively mild recession at worst. We continue to remain focused on buying high quality companies that provide some form of dividend yield and the prospects for future dividend growth. After a significantly long time, we’re finding great bargains across the market but particularly in the tech sector. I believe that our investors will be rewarded for remaining steadfast during the current selloff and will not have to wait long for the bull market to return.

Sincerely,

Ankur Shah

Ankur Shah
Managing Member
Ashva Capital Management LLC

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