INSIDER Weekly

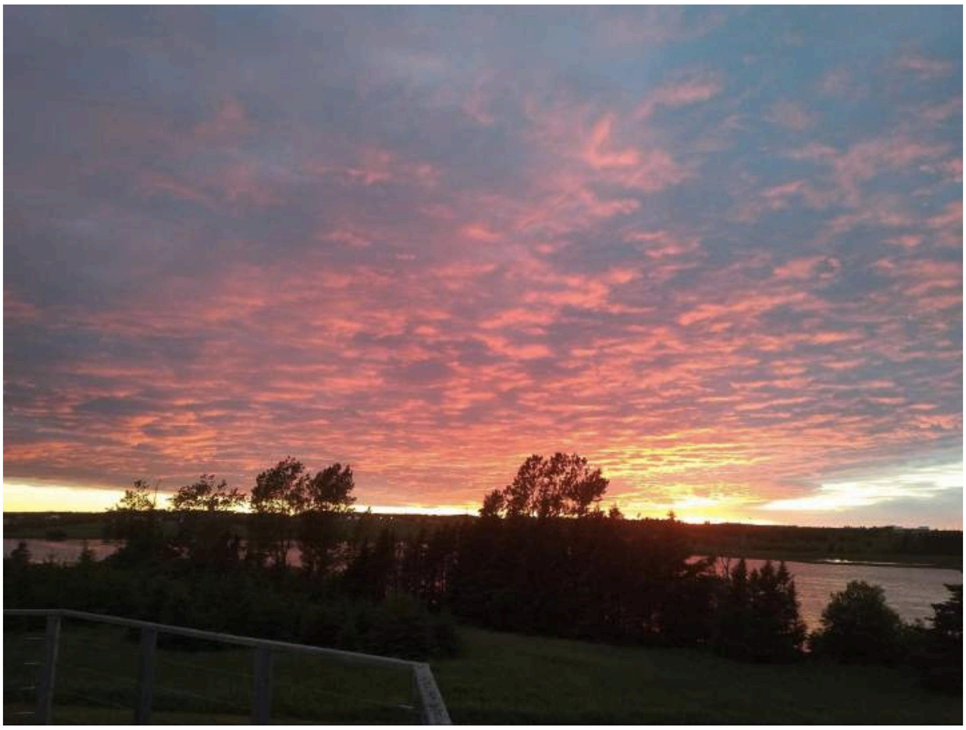
ISSUE 120 (30 JUN 2019)

DID I JUST HEAR "THIS TIME IS DIFFERENT"?

Hello, and welcome back!

Kohuratahi, eastern Taranaki in New Zealand from subscriber Hass.

Sunset North Rustico, PEI, Canada. Courtesy of David.



THIS WEEK

- Ireland: ICE ban
- Did I just hear “this time it is different”?
- OMG: Vanguard looking at private equity
- Former EQT boss blasts shale
- Oil’s toxic investor sentiment
- What’s really driving gold?
- A little math around hydrogen
- Offshore drillers: Selling for scrap value
- South Africa’s mean reversion process
- 100-year bond at 1%? Why, of course!
- Bitcoin: Edumacation
- The Big Five:
    1. Vallourec
    2. Petropavlovsk
    3. Africa Oil
    4. Hylea Metals
    5. Diana Shipping

IRELAND: ICE BAN

Not wanting to be left behind, Ireland now bans internal combustion engines and wants to have close to 1 million EVs by 2030.

> **Ireland’s climate plan calls for ICE ban, 950,000 EVs by 2030, net zero emissions by 2050**
>
> Phil Dzikiy - Jun. 18th 2019 11:48 am ET @phildzikiy

Once again we believe this is herd mentality or political pandering. Perhaps both? It is all very well being ambitious, but if it is so far removed from reality, it is delusional.

Let’s see: Ireland has about 2.7 million cars on the road today, and so to get about 1 million EVs on the road by 2030, then sales of ICE cars must stop today. Literally.

Then there is the “slight” problem in that EVs cost significantly more than ICEs.

You are well advised to read this article, which makes one wonder how many Guinnesses the Irish government downed before putting this forward.

Climate plan: 1m electric cars by 2030 does not look realistic

Analysis: A decade ago Government set a 10% goal for electric cars and missed target spectacularly

Tue, Jun 18, 2019, 10:50 | Updated: Tue, Jun 18, 2019, 12:19

Michael McAleer

5

We thought the article above was brilliant, although it fell short of mentioning the additional electricity requirements for those EVs. But that's our gig here and one you're well aware of.

You may say, who really cares about the crazy Irish? Well, all the Irish are doing is copying most of the policies of other European states.

ICE sales ban or 100% ZEV sales target

Costa Rica 2050
Denmark 2030
France 2040
Iceland 2030
Ireland 2030
Israel 2030
Netherlands 2030
Norway 2025
Portugal 2030
Spain 2040
Slovenia 2030
Sweden 2030
United Kingdom 2040

The additional costs of all this will be absolutely huge, and guess who's going to have to pay for it. Taxpayers.

What's so fascinating to us is that all of this talk of banning ICE vehicles across the world simply assumes there are materials available to build out all these EVs.

I had a flatmate when in my 20's, who had a saying that always stuck with me, *"Assumptions are the mother of all fuckups."* It's crude but it's so true.

Not only are EVs more expensive than ICE vehicles. Anyone with half a brain, some fingers, a calculator, and a desire to look at some facts will realise that when demand ramps up for all these EV inputs and this demand is met with scarce supply, the cost/price goes up.

Investment implications: Invest at bottlenecks, rare earths, nickel, copper, etc. Although we are quite sure that these targets will never be achieved, resulting in oil being in short supply.

And the clowns who are enacting these policies now will turn around and say, *"Oh, but we thought we'd not need oil. Oops, sorry about that."*

DID I JUST HEAR "THIS TIME IS DIFFERENT?"

If you want an insight to the popular narrative, then here we go:

When Everything That Counts Can't Be Counted

Posted June 13, 2019 by Joshua M Brown

This article gives me flashbacks to the "good old days" of late 1999 and early 2000.

> *"In the battle for capital right now, the brands and intangibles and user bases and networks are winning by a landslide against the things that used to be important. And the companies that are rich in those old fashioned things, like Walmart, Disney and McDonalds, are spending all of their time and attention to transform themselves into the spitting image of their upstart competitors.*
>
> *Disney wants to look like Netflix, Walmart wants to retail like Amazon, McDonalds wants to be as habit-forming and celebrated for its freshness as its former protege Chipotle is. Goldman Sachs wants to grow up to be BlackRock. And in emulating these younger models, they hope, their multiples will soon be following suit.*
>
> *And as for those stodgy old stalwarts of the 20th century that aren't pursuing this transformation…it remains to be seen whether the rusty old assets they do possess will ever matter to investors ever again."*

Yet another echo of what we heard some 20 years ago.

The headline below is so familiar.

INVESTING

Is value investing dead? It might be and here's what killed it

PUBLISHED SUN, JUN 23 2019 · 8:30 AM EDT | UPDATED SUN, JUN 23 2019 · 11:35 AM EDT

Yun Li
@YUNLI626

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Seems it all comes down to too much cheap money and low inflation. It is all one big trade, one big theme.

VANGUARD EYEING PRIVATE EQUITY?

Would John Bogle turn in his grave?

MARKETS

Indexing Giant Vanguard Examines a Push Into Private Equity

Firm has held early-stage talks with prospective partners as it considers expanding alternative investments

I wonder is this not another contrary sign of the 10-year growth vs value trend coming to an end?

I am quite sure that if there wasn't all this fanfare over the Uber, Zoom, Beyond Meat, Slack, and other "unicorn" listings, entering into private equity wouldn't even have crossed Vanguard's mind.

FORMER EQT BOSS BLASTS SHALE

A no holds barred go at shale from the former CEO of EQT.

Former Shale Gas CEO Says Fracking Revolution Has Been 'A Disaster' For Drillers, Investors

By Sharon Kelly • Sunday, June 23, 2019 - 04:02 *Read time: 10 mins*

We don't know much about Steve Schlotterbeck, and we are certainly not into retrospective commentary.

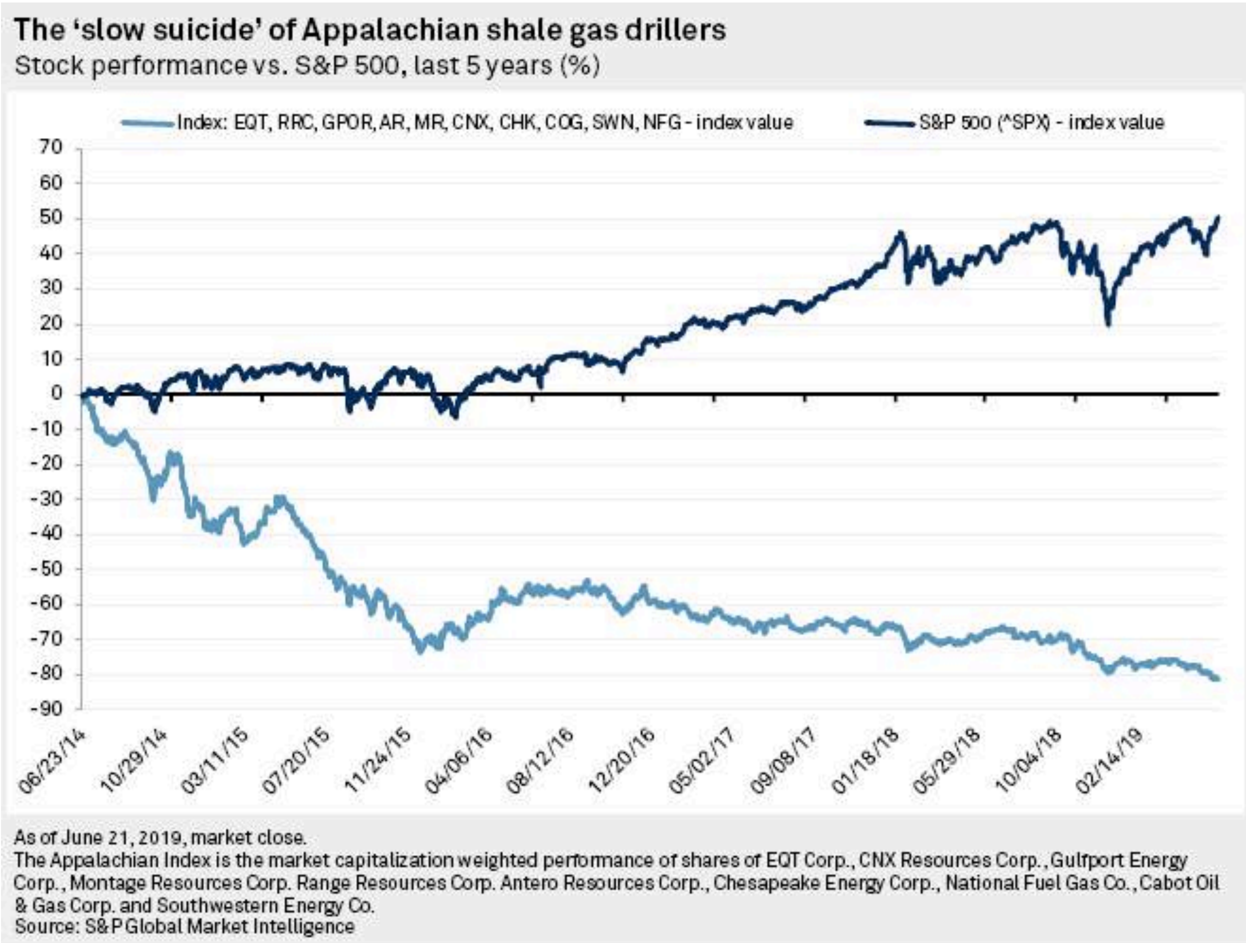
So apart from stating the obvious, what is our take from the article? What we have seen from shale in the past (production, growth rates, etc.) should not be extrapolated into the future.

And with capital expenditures being slashed, we will probably see shale production surprise to the downside over the coming months.

Boom? What boom? A boom in production but a complete bust for investors.

This cannot continue!

Something's gotta give, and though the industry may find more ~~investors~~ fools to continue fronting up with more money to fund the “fracking revolution,” it’s not the way to bet.



While shale E&Ps have succeeded in boosting oil and gas production to levels that were unthinkable only a few years ago, prices have crashed precisely because of the surge of supply.

And, because wells decline at a precipitous rate, capital-intensive drilling ultimately leaves companies on a spending treadmill. We think that treadmill is grinding to a halt, and **soon we will see oil and gas production from shale surprise to the downside.**

Yet another echo of a cut back in expenditure:


A Leader of America's Fracking Boom Has Second Thoughts

Pioneer Natural Resources once promised production to rival Libya. Now it's pulling back.

Folks, this is the head of Pioneer telling us that investment (drilling) is going to be curtailed dramatically.

Now, we've been singing this tune for over a year now, and only now we are seeing industry executives coming out and saying what we've been saying for a good length of time. The numbers don't work.

My guess is that this is simply human nature at work. If you're getting paid (and paid well) in an industry that doesn't actually turn a profit, you'll probably take the money.

But when you see the risks to being on that side of things are shifting, it pays you to stand up and either get out or "be the guy that called it". It's self preservation. We expect the tide to soon turn with "experts" appearing on CNBC telling us how this industry is a bust and why not to invest in it, blah, blah, blah. It'll be amusing.

OIL'S TOXIC INVESTOR SENTIMENT

Armageddon in oil services!


ENERGY

Oil traders have almost fully priced in a 'Lehman Brothers moment,' Standard Chartered says

PUBLISHED TUE, JUN 11 2019 • 6:54 AM EDT

Sam Meredith
@SMEREDITH19

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There was a really interesting quote from the video in the article. It went words to the effect:

> *"Algos are causing huge volatility. A $10 move should be a $2-$3 move without the algos. Algos aren't creating the reason for the move rather they are extending the move."*

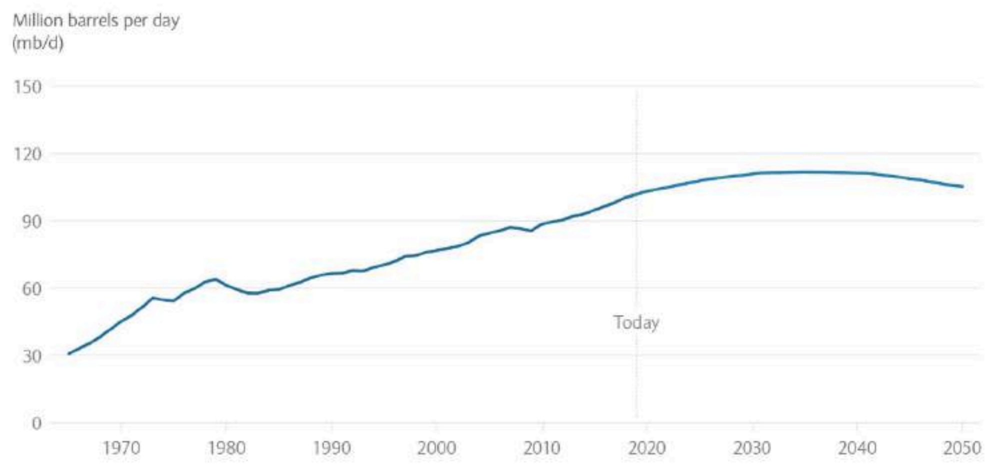
This makes a lot of sense to us. We just cannot understand why there is this huge volatility. Well, blame it on the algos.

One thing is for sure. The short term movements have little/nothing to do with the long-term fundamentals.

And as for traders "fully pricing in a Lehman Brothers moment..." we think the market is pricing something more than that in. Something more like the world won't need oil by 2030.

But can the world really get off oil? We have been very vocal about this saying it will take a helluva lot longer than what most "energy transformationalists" are suggesting. Here is a forecast from Barclays that appears reasonably objective.

Oil demand is expected to remain flat to slightly down by 2050



Source: BP Statistical Review for historic data. Barclays Research for forward looking estimates.

Going forward, oil is likely to remain an important player in the energy mix: alternatives that provide the capacity to support growing populations and economies do not yet exist. But by 2050, the world will undoubtedly look different as advances in renewable energy, technological innovation and strict low-carbon policies help to ease the reliance on fossil fuels.

The key thing to understand is the world will be using materially more oil by 2040 than it uses today. But for every one barrel of oil being discovered today, 4 barrels are being consumed.

Here is an interesting breakdown of the differing uses for oil:

So the world currently consumes about 100 million barrels of oil a day.

However, if no new oil is found to add to reserves, then the world will only be able to pump 20 million barrels per day by 2050 (page 13 of this report).

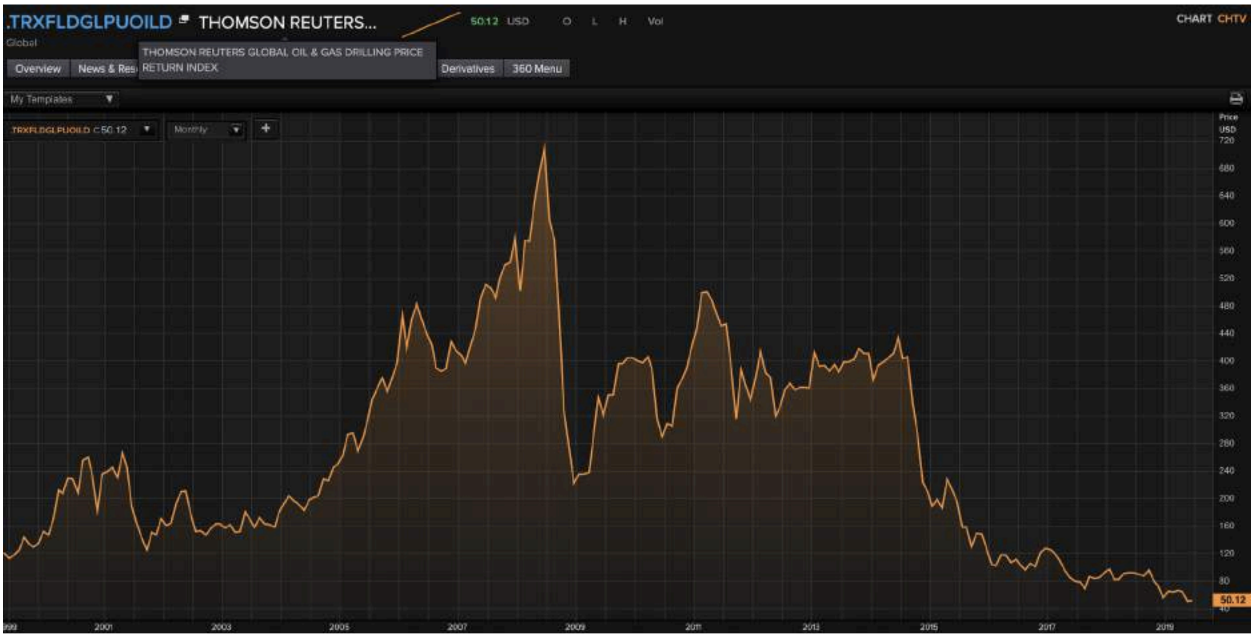
What will demand be by 2050?

Let's say the world still will be consuming 100 million barrels per day by 2050 (we think it will be more but let's keep it simple):

- Saudi currently produces about 12 million barrels per day
- The Permian produces about 4.2 million barrels per day
- Russia produces some 11 million barrels per day

From "back of envelope" calculations we figure the world is going to have to find about 80 million barrels per day just to maintain current reserve levels by 2050. That is field(s) big enough to produce 6x Saudi's daily output, 9x Russia's, or 20x the Permian.

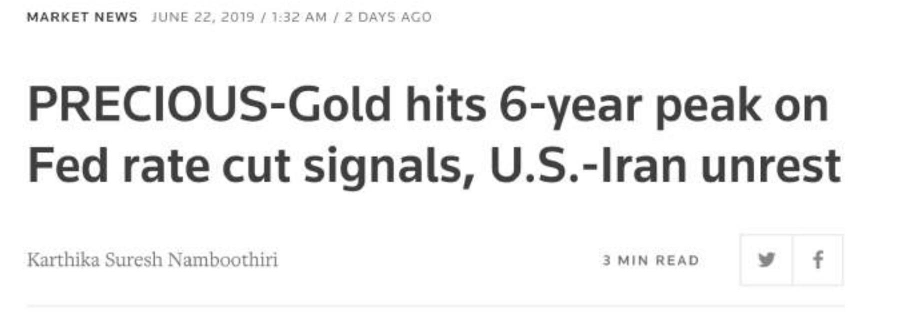
We think it is a fairly safe bet that 5 years from now oil and gas exploration and development expenditures will be at record highs, and the absolute worst performing investments over the last 7 years or so will be the best performing over the next 7.



Thomson Reuters Global Oil & Gas Drilling Price Index

WHAT IS REALLY DRIVING GOLD?

The press of popular opinion would have us believe that it is the problems with **Iran or maybe the Fed cutting Interest rates** that is driving gold higher.



MARKET NEWS JUNE 22, 2019 / 1:32 AM / 2 DAYS AGO

PRECIOUS-Gold hits 6-year peak on Fed rate cut signals, U.S.-Iran unrest

Karthika Suresh Namboothiri 3 MIN READ

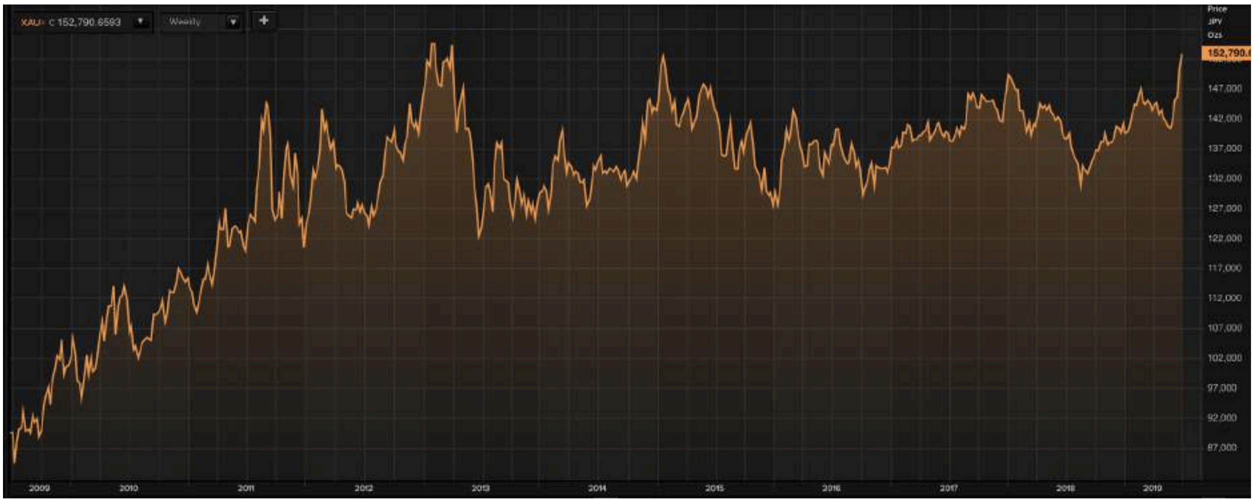
But is there something else happening beneath the surface?

I mean, we've had interest rate cuts in the past and gold couldn't get out of bed. And Iran isn't exactly a surprise here. It seems to us that **the something that is now pushing gold higher has been building for a while.** Gold is breaking higher in multi-currency terms:

Gold in AUD

Gold in USD

Gold in SGD



Gold in JPY

What we find remarkable is that there is no talk of what gold is doing in multi-currency terms, especially when gold is registering record highs against a number of currencies.

What is the driver? **We suspect it is the beginning of a loss of confidence in paper currencies (that includes government debt).** And if that is the case, then there is a hell of a lot of upside on offer.

In any event, the charts themselves are suggesting (in our minds) that considerable upside is coming.

A LITTLE MATH AROUND HYDROGEN

A brilliant report around hydrogen:

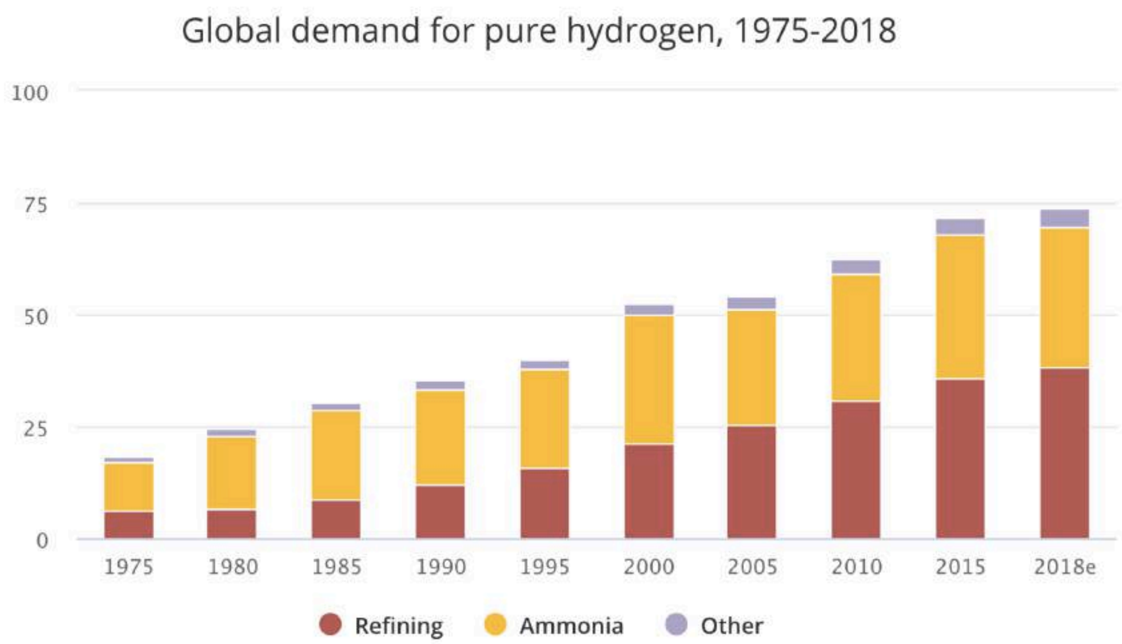
Here are a few takeaways from the report:

> *"Demand for hydrogen, which has grown more than threefold since 1975, continues to rise – almost entirely supplied from fossil fuels, with 6% of global natural gas and 2% of global coal going to hydrogen production.*
>
> *As a consequence, production of hydrogen is responsible for CO2 emissions of around 830 million tonnes of carbon dioxide per year, equivalent to the CO2 emissions of the United Kingdom and Indonesia combined."*

And hydrogen from water electrolysis?

> *"Producing all of today's dedicated hydrogen output from electricity would result in an electricity demand of 3 600 TWh, more than the total annual electricity generation of the European Union."*

And what is "95%" of hydrogen used for?



So can we have significant numbers of FCell cars and trucks on the road by 2030 to rival battery electric cars? Yes, that can happen.

However, if that happens, they will be **running on hydrogen stripped out from natural gas,** which doesn't do much for the world's greenhouse gas emissions "problem". But it requires oil and gas companies to keep exploring for gas.

Unless technology changes, we won't have millions of FCell cars and trucks running on hydrogen produced from water electrolysis.

This isn't to say that there will not be a proliferation of hydrogen produced from water (we still think investing in stocks like Nel and Hydrogenics is a good idea). Rather, hydrogen from electrolysis cannot fulfill any significant part of the world's energy needs.

We're thinking that, unless there is a giant leap forward in technology, it is going to be really hard for the world to wean itself off petroleum. So in 20 years from now, gasoline powered cars will still dominate the world's roads.

Sooner or later big oil is going to have to start spending on exploration and development to makeup for rapidly diminishing reserves.

Hence the reason we believe that offshore oil services is a “when, not if” situation.

OFFSHORE DRILLERS: SELLING FOR SCRAP VALUE

The sell-off in the offshore oil drilling sector has gone beyond the stage of stupid.

A number of drillers are now trading at the money they would get if all their rigs were “parked up” on an Indian beach.

The market is essentially pricing drillers as if the world will not need oil and gas from offshore sources beyond say 2025 (something like that). It’s as if most drillers will go belly up within a few years.

So buying a basket of offshore oil drillers now is **merely a call on oil being produced from offshore sources 5+ years from now.** If we are still getting substantial amounts of oil and gas from offshore sources come 2030, then offshore drillers will have 10x returns from current levels.

If not, then the rig companies go bust and we lose 20-30% of global oil and gas production. It is that simple!

Looking at this we think the market has finally lost any form of rationality that it may have had.

If you want the "least risky" option, then have a closer look at Maersk Drilling (the spinoff from Maersk Shipping). This bad boy turns a profit, has lots of cash on hand, and is trading well below book value.

SOUTH AFRICA MEAN REVERTING

A wee while ago (early 2000's), while on holiday in Tanzania with his girlfriend (now wife), Brad was roaming the streets of Dar Es Salaam.

He looked up at the buildings and saw that what once would have been clean, modern, and trendy, was now an absolute mess.

They were the same buildings but in complete shambles.

The thought crossed his mind, what is preventing South Africa becoming like this? Then it hit him. South Africa would "mean revert" to the rest of Africa, so Johannesburg would eventually become just like any other African city. All the underpinnings to make this happen were there.

Brad's wife goes back every year to see family, and she is shocked at how quickly the place is going backward (mean reverting). For those of you who haven't been there, take a look at this article. It is absolutely shocking!

Charts That Show the Financial Woes of South African Cities

By Prinesha Naidoo
27 June 2019, 00:33 GMT+10

Of course, the powers that be will continue to blame it on apartheid (which incidentally ended a generation ago).

It is a trend you can bank on.

AUSTRIA'S 100-YEAR BOND AT 1%

If there was anything that gave you a good understanding of how there is absolutely no fear of inflation and every fear of being invested in asset classes that benefit from inflation, then this would have to take the cake.

Markets

100-Year Bond Yielding Just Over 1% Shows Investors' Desperation

By John Ainger
25 June 2019, 20:01 GMT+10 *Updated on 25 June 2019, 21:26 GMT+10*

- Austria's 2117 yield has dropped 100 basis points since launch
- Bonds have rallied, with German yields hitting record lows

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Honestly, why invest in this bond when it isn't hard to get a 5% return on large cap stocks in Europe? It's beyond nuts.

BITCOIN: EDUMACATION

It was bad enough when I was a young snot. School never taught me a goddamn thing about money. And they still don't, which I suppose makes sense since most teachers haven't a clue about it either.

And so two weeks ago, while at dinner, I proposed to my kids that I'd give them $500, but they had to earn it the following way:

They needed to go on their own and independently research what Bitcoin is, how to buy it, trade it, and store it. I'd mark them on the project and they needed to get all elements right.

It took a week. I had to send them back a couple of times because of some rookie mistakes such as storing their crypto on an exchange... or in an online wallet. There was a mention of buying Bitcoin via a brokerage account. This received a fail.

In the end, my kids now know how to buy Bitcoin, why it makes some sense, they know how to move it between wallets, trade it for other coins, and they know how to put it in cold storage.

They also understand the statement "if it's not your keys, it's not your coins". In short, they understand sovereignty.

I think it may have been one of their most important lessons this year.

So how well do I think my kids $500 investment into Bitcoin will do?

Nobody knows the future, and as I've said before, *"I have two balls and neither are crystal."* That said, here's what I think.

They're going to learn all about volatility. Serious volatility. Numerous 20 to 30% drawdowns ultimately followed by new highs. Each time that happens we'll see articles saying "bloodbath in Bitcoin" and "crypto crash" and so on.

They need to be understood for what they are: written typically by people with no skin in the game or simple clickbait. Likely we'll see a bunch from gold pumpers who've a product to sell. And I say this as a gold bull.

Don't get me wrong, gold is great.

However, gold is easily seized, censored, and even weaponized by central banks, who are the largest holders of gold on the planet. Bitcoin, on the other hand, is money, separate from both the state and central banks. Will it succeed against a fiat regime? I don't know and nobody else does either. However, it is easily the best asset I can think of with a snowballs hope in hell of doing just that. For that reason alone one should own some.

For an objective comparison the below chart is useful.

Transaction Cost	Precious Metals	Fiat Currencies	Bitcoin
Storage	0.15% to 1% per year	Subsidized by FRB*	*Free and 100% reserve*
Transportation	Expensive	Inconvenient	*Free & Easy*
Security	Physical	Institutional	*Cryptographic*
Fiduciary media	Inevitable	Inherent	*Impossible*
Recordkeeping	Manual	Manual	*Automatic*
Counterfeiting	Impossible	Inevitable	*Impossible*
Issuance	Mining	Politics	*Algorithm*
Payment clearing	Expensive	Centralized	*Cheap & Distributed*
Scarcity	High	Arbitrary	*Fixed - 21 million btc*
Authentication	Expensive assay	Trust counterparty	*Built-in*

** fractional reserve banking*

As things progress and institutional ownership begins to take hold Bitcoin will appreciate in value quite simply due to its fixed supply. This will be exacerbated by the halving in May of next year, which will cut supply by 50%.

On the demand side we have many factors supporting further price appreciation. Large scale institutional adoption, ETF products, regulatory approvals. And all this taking place while geopolitical tensions increase, global economic instability intensifies, and central banks pull out ever more fanciful tools to act as levers to a broken machine.

Oh, and on that note... We're in the trade wars period which we promised. Just wait until currencies become weaponized. Those who think that currency wars are not coming are just not paying any attention. This instability in currencies will act as a further propellant to Bitcoin.

Many "experts" will call tops as it moves higher. Some may even temporarily get these tops and bottoms right, but there is an extremely low probability of them doing so consistently.

In my original Bitcoin report, which is available in the Archive, I said that the dumbest thing you can probably do is not store them properly, losing them, and trying to trade this market.

In fact, if they're on an exchange, you'll be tempted to check your wallet balance every day. I won't be doing that. They're stored like my gold. Safe and under my control, not stored with some bank or exchange.

And I'm a lazy guy, so I wont be wanting to expend the energy to get them out, move them to an exchange, and trade them. Which is exactly what I've done ever since buying way back when they were in the hundreds per coin.

"Wow, Chris you're smart."

No, I'm not. It's not about being smart. This is just about having a view and executing on that view and simply not being dumb.

You'll notice it's the same strategy used for most of our investments here.

And if I'm wrong, I will lose a small percentage of capital. And if I'm right in a couple years from now, we'll be between 6 and 10x from today's $10,000 price point.

My kids, on the other hand, may pay for their own college tuition. And if not, they will have had one of the most remarkable real time market learning experiences I could ever have hoped for.

THE BIG FIVE

FROM OUR TRADING DESK

Five stocks that few would know about — let alone be invested in — putting their hand up begging for someone to take a closer look. These aren't official trade alerts or even ideas but rather invitations to take a closer look.

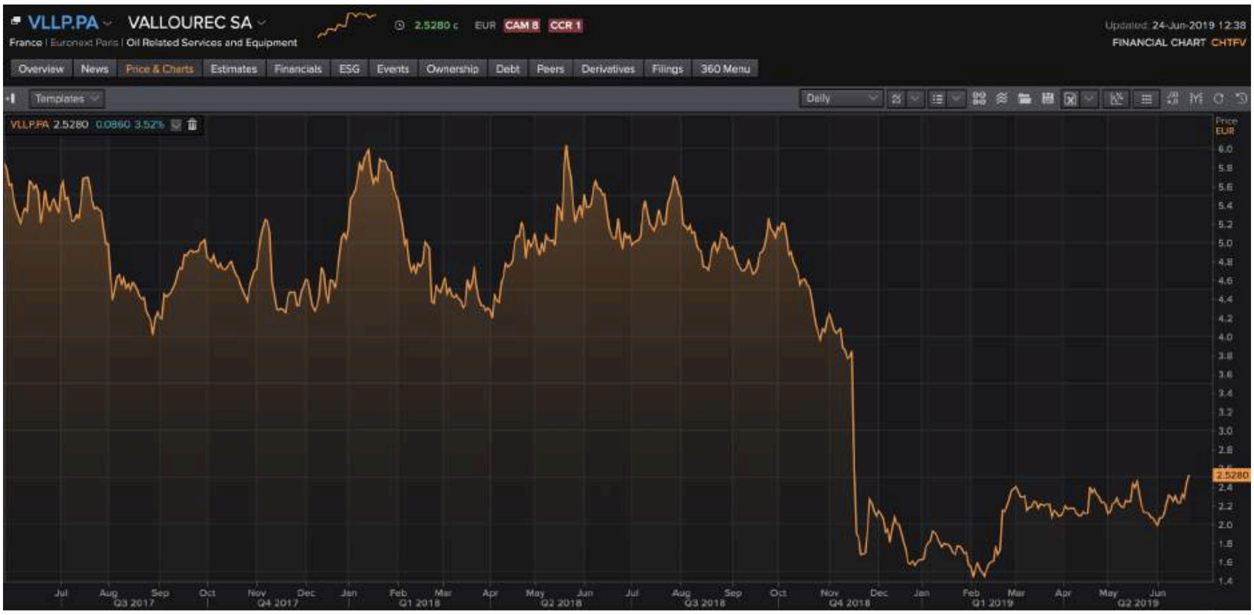
1. Vallourec
2. Petropavlovsk
3. Africa Oil
4. Hylea Metals
5. Diana Shipping

VALLOUREC

A manufacturer of steel tubing primarily for the oil and gas industry.

We have talked about Vallourec before. They have debt issues, but it's probably worth a punt that they make it through without a debt reorganisation (equity holder wipeout).

Of course, Vallourec wouldn't have made it into the Big Five if it was making new lows.



PETROPAVLOVSK

Yet again, Petropavlovsk makes it into the Big Five.

Such an interesting long-term setup. And we like to bring something a little different to the table. Doubt you hear of anyone talking about Russian gold miners.

Popping to the upside out of a remarkably tight long-term trading range.

AFRICA OIL

An exploration and development company with a number of really interesting assets in Africa. No debt, trading at 0.5x book value, and 75% of its market cap accounted for by cash.

HYLEA METALS

Hylea is acquiring Paladin's Malawi uranium mine for $10 million.

That is a mine that Paladin put into C&M in 2014. It has produced some 11mlb and still has about 32mlb in the ground. And it was a mine that cost some $200 million to build. A bargain, you could say.

Beats me why Paladin sold it. Anyway, probably a very cheap call option on the price of uranium.

HELIX ENERGY SOLUTIONS

Lost of cash, limited debt, making a slight profit, yet trading for way below book value: ROV operator Helix.

And at current levels it is more or less at the price it listed at some 20 years ago and not too far from GFC lows.

DIANA SHIPPING

An owner of some 50 dry bulk ships. Making a profit, lots of cash, and trading at half book value. Seems like a reasonable sort of bottoming action.

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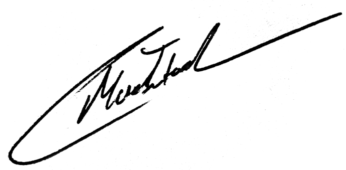
INSIDER COMMUNITY

As per usual, a gentle reminder to join us on the Slack community. Just go here.

As always, thanks for reading and being part of Insider.

Sincerely,



Chris MacIntosh

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Founder & Managing Partner, Glenorchy Capital

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