SECOR ASSET MANAGEMENT

Equity Update

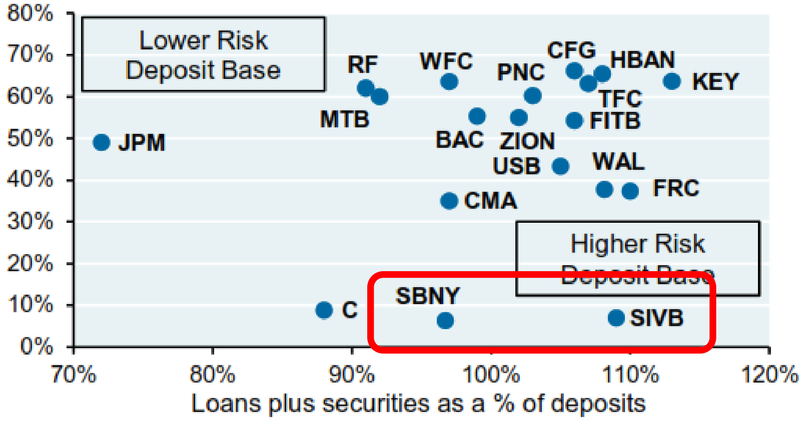
March 13, 2023

Bank Failures Are Back

- Silicon Valley Bank was taken over by the Federal Deposit Insurance Corp (FDIC) on Friday to pre-empt a run on the bank, becoming the second largest US bank to fail. The Treasury Dept. also announced over the weekend that the FDIC would take control of Signature Bank of New York.
- All depositors will be made whole and have access to their funds on Monday; equity holders and certain debt holders wiped out.
- Bank stocks tumbled on 10 March 2023, falling 8% on fears of more failures and banks being inadequately capitalized.
- SIVB and SBNY were especially vulnerable to rising rates and deposit withdrawals from their extreme levels of loans & securities as a percentage of deposits and extreme low levels of stickier retail deposits as a percentage of total deposits.
- Banks in the US remain well capitalized, although the aggregate Tier 1 ratio has decreased recently with the rise in interest rates.

US bank loan-to-deposit ratios

Estimated retail deposit share of total deposits



US bank tier 1 capital ratios

Tier 1 capital as a % of risk-weighted assets

Earnings Quality – The Quantity and Quality of Earnings Is Falling

- The purpose of accrual accounting is to match the recognition of revenue with related expenses when revenue is earned. Accruals are the non-cash component of earnings, i.e., the timing difference between reported earnings and cash flow.
  - When reported net income exceeds cash flow from operations, earnings are considered to be of low quality.

- Recently, high levels of accruals have led to the widest discrepancy between Net Income and Cash Flow in the last 30+ years.
  - YTD thru 30 Sep 2022, Net Income (adjusted for amortization and depreciation) topped Cash Flow from Operations by 14%.

Sources: UBS, Bloomberg.

Earnings Quality – The Quantity and Quality of Earnings Is Falling

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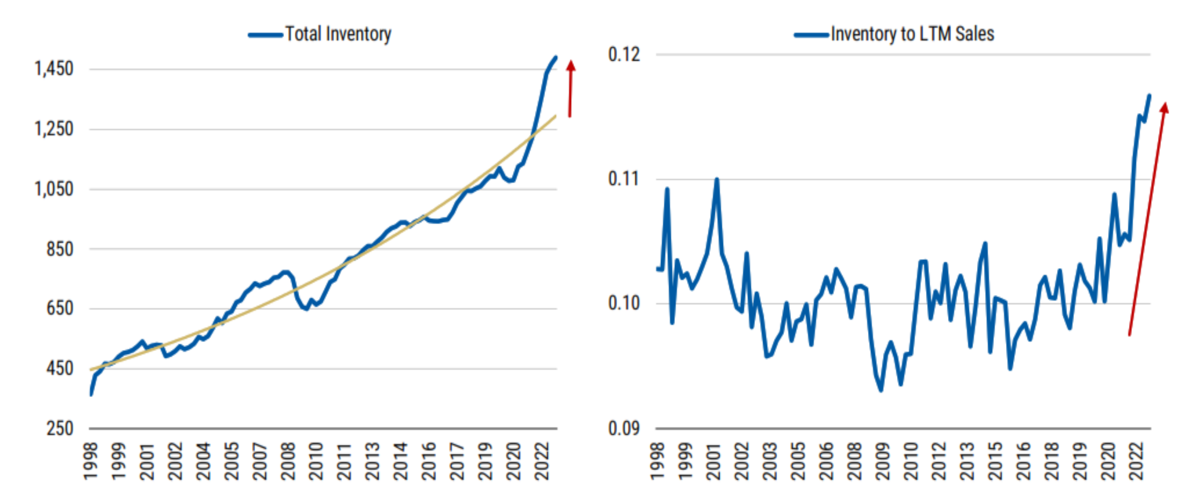
- **The bulk of the spread is attributable to an increase in accruals related to working capital, most notably from a surge in inventories.**
  - Continued supply chain issues, potentially misjudged demand, earnings "management" are possible reasons for an increase in the spread.
  - Inventory build-up has been broad based, cuts across virtually all sectors. Symptom of impending recession?
- **2023 consensus earnings expectations continue to be reduced.**
  - Consensus earnings growth in the US for 2023 has contracted from 4.6% at the beginning of the year to 1.0% at the end of February.



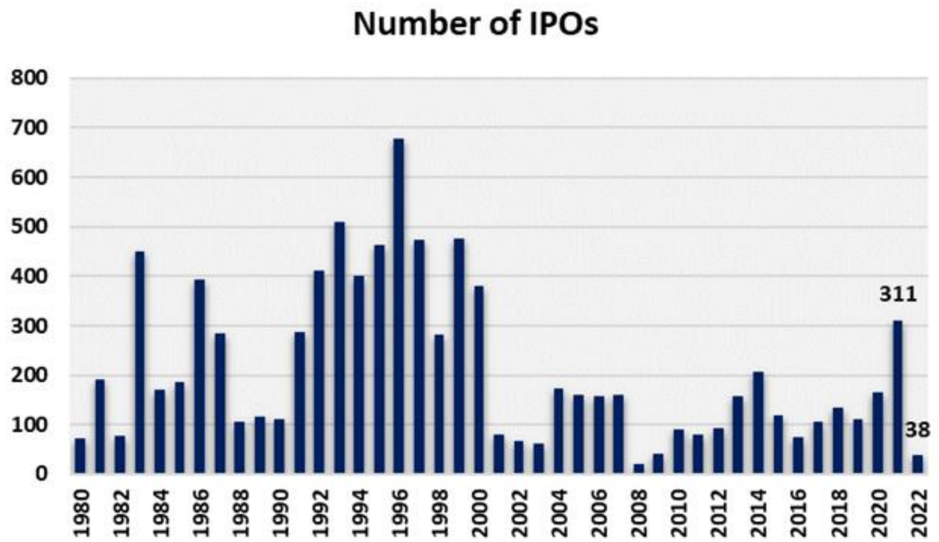
Note: Analysis using S&P 1500 ex Financials, Real Estate & Utilities.

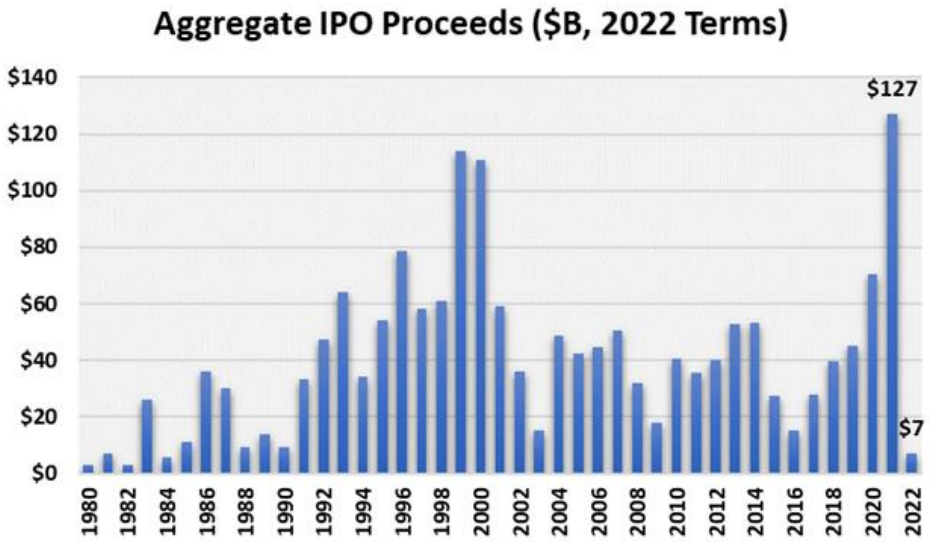
Industry Group	Inv/Sales Current Percentile ('95-22)
Semiconductors & Semiconductor Equipment	100%
Technology Hardware & Equipment	100%
Consumer Durables & Apparel	99%
Health Care Equipment & Services	99%
Household & Personal Products	99%
Automobiles & Components	97%
Capital Goods	97%
Food Beverage & Tobacco	94%
Retailing	84%
Materials	76%

Sources: FactSet, Morgan Stanley Research, Credit Suisse.

IPOs – A Terrible 2022

- 2022 was one of the worst years ever for traditional (non-Special Purpose Acquisition Company) IPOs.
  - Just 38 IPOs in 2023 after 311 in 2021.
  - Aggregate proceeds of $7 Billion was the lowest since 1984; approx. half of the aggregate proceeds in post-TMT bubble 2003 and GFC 2009.





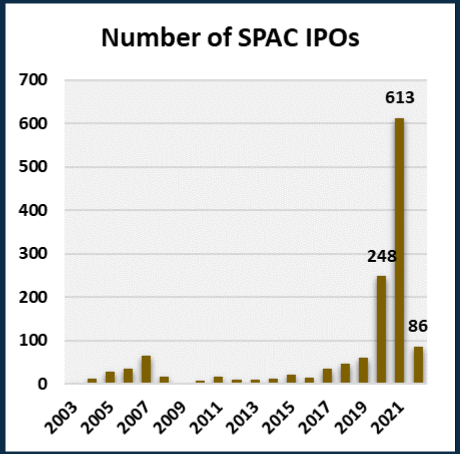
Note: IPOs with an offer price of at least $5.00. No ADRs, unit offers, closed-end funds, REITS, natural resource LPs, banks and S&Ls and stocks not listed on CRSP.

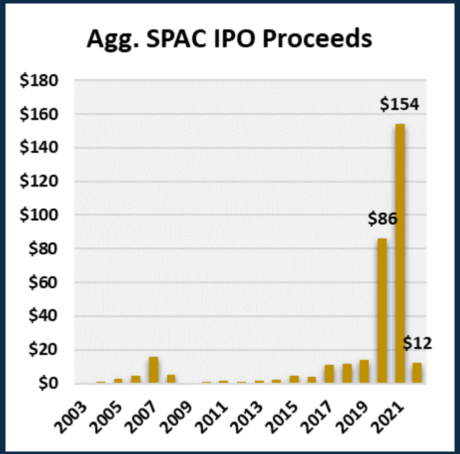
Sources: Professor Jay Ritter Data Library, SECOR.

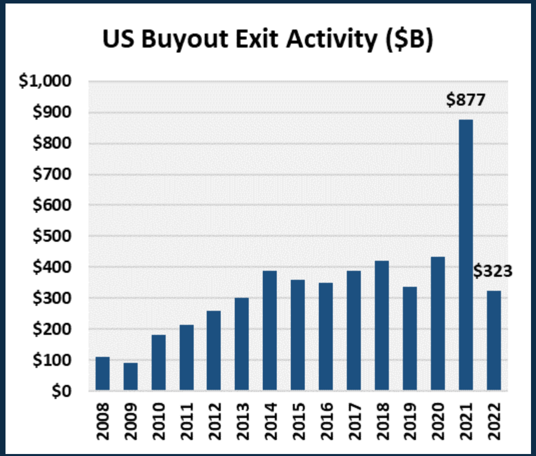
IPOs – A Terrible 2022

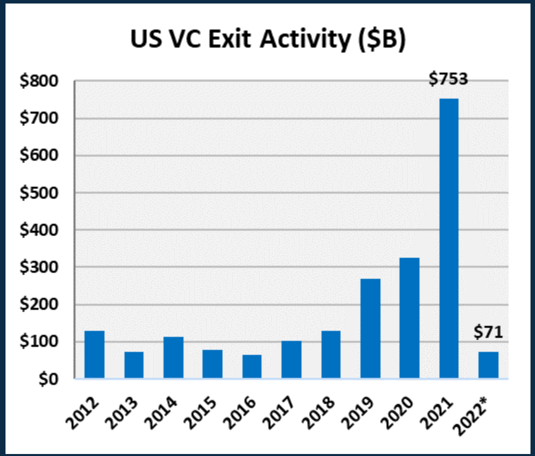
- **And after a brief moment in the sun, SPAC activity is about to go the way of the dinosaur (just 16 SPAC IPOs in H2 2022).**
  - There are approx. 600 SPACs set to expire throughout 2023 (400 in Q1) that have yet to close on a merger target.

- **The weak IPO market impacted Private Equity exits in 2022, most notably Venture Capital (VC).**
  - Total value of US Buyout exits in 2022 was $323B, well off of 2021's record smashing pace but near that of more recent years despite the weak IPO market.
  - Total value of VC exits were not as resilient in 2022, slipping to just $71B, well behind not only the 2021 amount, but also weak compared to recent years.
  - Exits via IPO for Buyout-backed companies: 2 companies in 2022 (versus average of 29 companies/yr. over the twenty years prior).
  - Exits via IPO for VC-backed companies: 14 companies in 2022 (versus average of 66 companies/yr. over the twenty years prior).







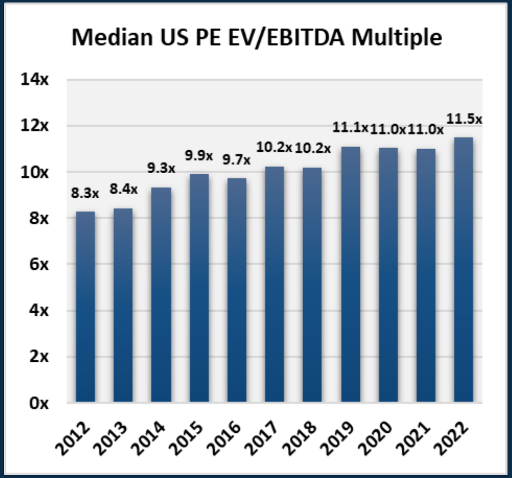


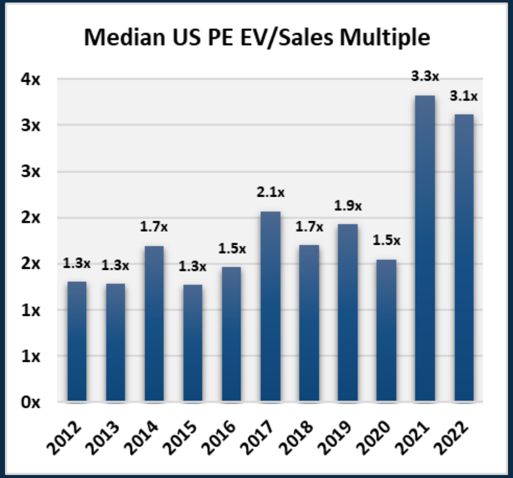
Sources: The SPAC Insider, Professor Jay Ritter Data Library, SECOR.

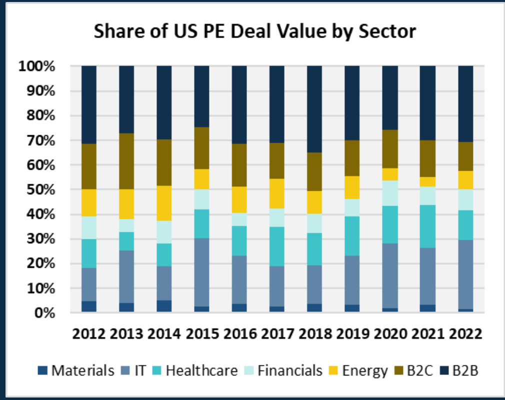
Private Equity Multiples – Warning Sign?

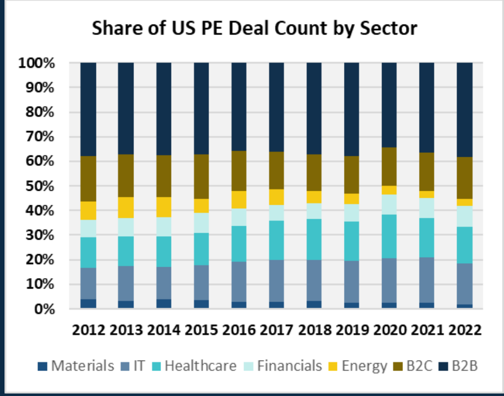
- **Although acquisition multiples measured on an EV/EBITDA basis have changed very little over the past few years, they have nearly doubled over the past couple of years on an EV/Sales basis.**
  - Would seem to indicate an increasing share of deals for lower EBITDA margin companies.

- **There have been modest shifts in the sector mix of PE acquisitions over the past two years.**
  - Increase in IT deal value (2012-2020 avg. = 17%; 2021-2022 avg. share = 26%).
  - Decrease in Energy (11%→6%), B2C deal value (19%→13%).
  - Overall, suggests lower quality businesses have been acquired recently, or at least businesses with much lower margins.









Sources: Pitchbook, SECOR.

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