LVS ADVISORY

Investment Results	2019	Year-To-Date 2020	Since Inception[1]
LVS Defensive	9.1%	0.3%	9.6%
LVS Growth	-	2.2%	2.2%

Note: results presented gross of advisory fees and net of brokerage commissions. Investment results are as of January 31, 2020.
(1) LVS Defensive was incepted on January 1, 2019. LVS Growth was incepted on January 1, 2020.

February 4, 2020

Dear clients and friends,

The winter in New York City has been mild, but I've been productive nonetheless. LVS Advisory officially launched its second investment strategy, LVS Growth, on January 1st. The launch culminated over nine months of preparation which involved researching and updating research on dozens of companies I have followed over the years and then picking the 20 most promising names for the portfolio. I am proud to report that the Growth Portfolio is off to a strong start. LVS Growth appreciated over 2% in its first month while the S&P 500 declined slightly.

LVS Defensive continued to grind higher despite the volatility in the overall market. A large number of the deals we invested in during 2019 returned our money at the end of December, leaving our portfolio with a large cash position to start the year. At one point, our cash level reached 40%! While having a lot of cash sounds like a good thing, it is actually a drag on investment performance because cash doesn't provide a return. We have been able to re-deploy much of that cash into new opportunities and expect to return to a fully-invested position by the end of the first quarter.

In this letter, I'd liked to discuss the coronavirus epidemic and an investment we made for our Growth Portfolio.

REAL ECONOMIC CONSEQUENCES FROM THE CONORAVIRUS

At the time of writing, the 2019 coronavirus has claimed over 300 lives, primarily in mainland China, and has resulted in unprecedented travel restrictions placed on traffic to/from China. Its outbreak could not have come at a worse time for those living in China as it coincided with the country's Lunar New Year national holiday. What is normally a happy time filled with family gatherings and heavy spending on gifts and travel was substituted with locked-down cities and canceled plans.

There are real economic consequences to what has already manifested from the coronavirus but early estimates show a wide range of impact. Within China, some economists anticipate a mild impact of less than 1% of Q1 GDP while others project an impact as high as 4% of China's GDP (the more pessimistic projection is from *The Economist*).

Even if the coronavirus doesn't leave China, its economic reverberations will be felt in the United States because the two countries are major trading partners and China's economy now represents over 18% of global GDP. The US stock market has declined by about 3% from its mid-January peak in reaction to the crisis and Chinese stocks have declined closer to 10%. However, if the disruption from the virus continues for several more months and becomes a global pandemic, we can expect a greater impact.

WHAT WE KNOW FROM PAST HEALTH CRISES

The 2019 coronavirus isn't the first time a contagious disease has caused a global scare -- it's not even the first pandemic coronavirus. Most people will remember the 2002 SARS coronavirus which originated in Southern China. The SARS coronavirus infected a total of 8,096 people and resulted in 774 deaths. This compares to the 2019 coronavirus which has infected over 17,000 people and killed 360; in other words, the 2019 coronavirus may be more contagious but it appears to be less deadly.

The SARS coronavirus attracted the public spotlight in February 2003 when an American traveling to Singapore became infected and died from the symptoms. In the following month, global health organizations issued alerts and global efforts to contain the epidemic commenced. The virus was declared contained by the World Health Organization in July 2003 and there have been no new reported cases since 2004.

A greater fear remains that the 2019 coronavirus evolves into something more deadly such as the 2009 H1N1 pandemic which is estimated to have killed over 200,000 people or the 2014 Ebola outbreak which is estimated to have killed over 28,000 people. It is impossible to know for sure.

But unless the 2019 coronavirus achieves an unprecedented level of contagion, we should expect the long term impact on the economy and financial markets to be muted. At its worst, the SARS coronavirus resulted in the Hang Seng Index declining 18% from December 2002 to April 2003 and as the table below shows, major health crises have historically had little to no long term impact on the S&P 500.

Epidemic	Month end	6-month % change of S&P	12-month % change of S&P
HIV/AIDS	June 1981	-0.20	-10.73
Pneumonic plague	September 1994	8.22	26.31
SARS	April 2003	14.59	20.76
Avian flu	June 2006	11.66	18.36
Dengue Fever	September 2006	6.36	14.29
Swine flu	April 2009	18.72	35.96
Cholera	November 2010	13.95	5.63
MERS	May 2013	10.74	17.96
Ebola	March 2014	5.34	10.44
Measles/Rubeola	December 2014	0.20	-0.73
Zika	January 2016	12.03	17.45
Measles/Rubeola	June 2019	9.82%	N/A
			—Source: Dow Jones Market Data

To put things into perspective, the common flu on average infects 8% of Americans every year and takes 10,000 lives. While the rapid spread of a new virus is scary, it is unlikely to have a greater impact on society than a host of other recurring afflictions and issues.

AN INVESTMENT OPPORTUNITY: LVMH

As politician Rahm Emanuel once said, "Never let a serious crisis go to waste."

In this case, the 2019 coronavirus panic has led to a sell-off in the shares of LVMH stock which we find to be an attractive investment today.

LVMH owns a portfolio of iconic luxury brands including Louis Vuitton handbags, Dom Perignon champagne, Hublot watches, Belmond hotels, and several more. LVMH's stock price has declined over 10% since the coronavirus became a front-page news story because the company derives a significant portion of sales from Chinese consumers. The Lunar New Year holiday is a particularly important sales period for LVMH's Chinese customers.

The disruption caused by the coronavirus will certainly result in fewer items sold for LVMH in 2020 than previously anticipated; however, the coronavirus has not permanently impaired the company's long-term earnings power. Therefore, the current sell-off creates a good entry point for long-term investors.

A well-managed brand is a powerful business tool. Consumers develop long-term relationships with the brands they admire and trust. This engenders loyalty and repeat purchases. Unlike consumer products in discount or mid-tier categories, LVMH doesn't directly compete with other brands on the basis of price. Rather, the company has the ability to raise its prices and often does, contributing to steadily rising profit margins and returns on invested capital over time.

LVMH has a global reputation for high-end excellence and a growing presence in emerging countries around the world. The company has a long runway for growth across its portfolio as the global middle and upper-middle classes continue to grow in wealth. What's more, luxury businesses at the very high-end tend to hold up well during economic downturns. LVMH did not see much of a dip in its financial results during the last two recessions.

In recent months, LVMH announced the $16.2 billion acquisition of Tiffany financed all-cash with debt priced below 1%. The Tiffany brand fits nicely within the LVMH portfolio and there should be cost and revenue synergies to boot. Acquiring an iconic business like Tiffany with almost no financing costs will be difficult to screw up.

LVMH's long-term financial results have been fantastic and reflect the high-quality nature of its assets. Over the past 10 years, the company has grown its revenue on average by 12% and its earnings by 15%. We see no reason why earnings will not continue to grow at a double-digit rate over the next 10 years. The stock looks pricey at 25x forward earnings, but so long as the company continues to execute on its growth strategy, the current share price will prove to have been exceedingly cheap within a few years.

The stock market rarely serves up opportunities to buy great companies at attractive prices. We own shares of LVMH for our Growth Portfolio and will use any additional weakness resulting from the coronavirus scare to build on our position.

I'd like to wish everyone a safe and healthy winter.

Best regards,

Luis V. Sanchez CFA

ABOUT LVS ADVISORY

LVS Advisory is a full-service financial advisory firm providing active investment management, financial planning, and institutional investment research services for individuals, families, and institutions. Luis V. Sanchez CFA is the Founder and Managing Partner of LVS Advisory. Luis' professional experience includes working in investment banking, consulting, and investment management. Luis is a licensed Investment Adviser Representative and a CFA Charterholder. LVS Advisory LLC is a Registered Investment Adviser based in New York City.

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