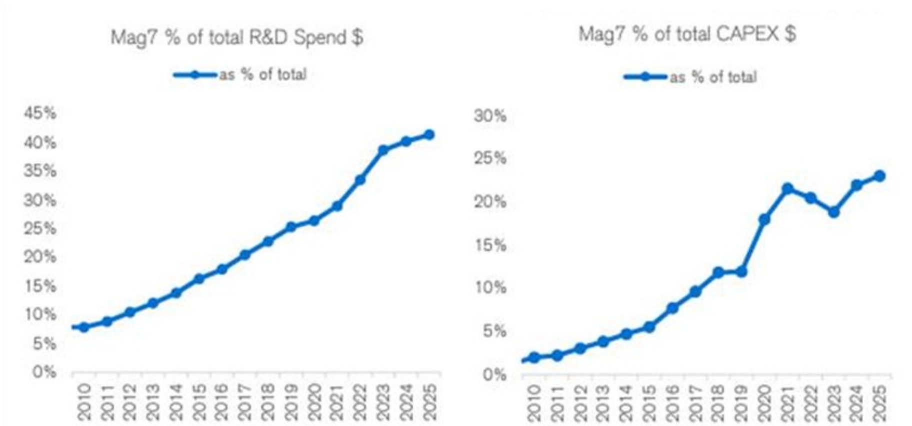
Covered Call Commentary

February | 2024

Navigating the AI Space

Artificial Intelligence is dominating the investing world. It's well documented that the top tech names have the largest stock market capitalizations in the US. They are also among the most profitable businesses *and* account for a huge percentage of the capital investment in the country.

For example, the "Magnificent 7" account for nearly 45% of the total R&D spend of the 1000 largest companies in the US. This is an incredible statistic. And despite being less capital intensive than many other industries, these seven companies also account for nearly 25% of the total CAPEX of the group. See below.



Source: Credit Suisse HOLT™

This is a space you simply cannot ignore as an investor. But growth is such an important factor in understanding relative valuation, you need to have a disciplined process for ranking and selecting which stocks to own.

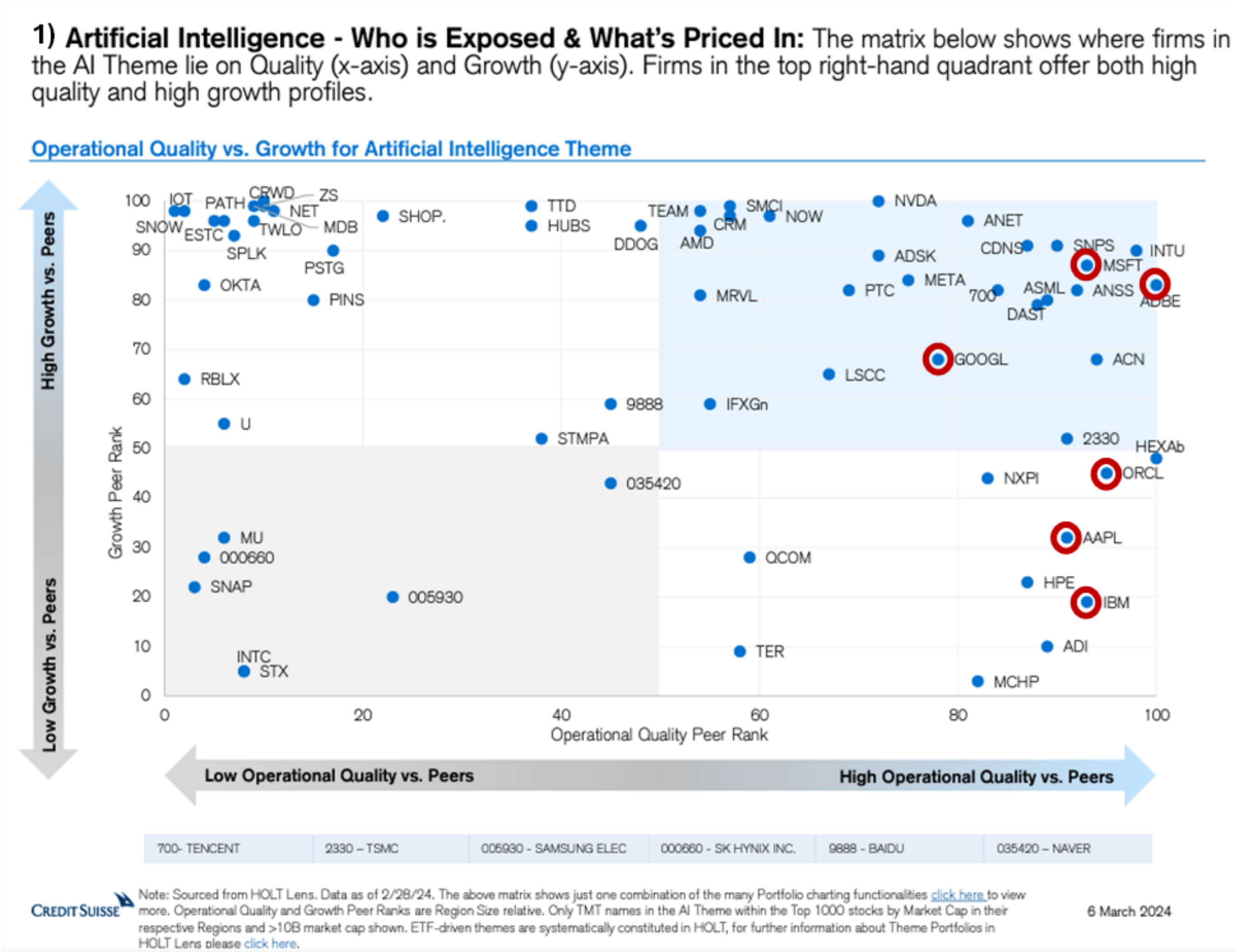
Our Approach

As income-oriented covered call managers, we consider risk management a core foundation of our approach. We do not chase trends or speculate. Our investment process requires that our holdings have at least 2x the upside potential versus downside risk.

Having said that, our portfolio is well-diversified across all sectors and has exposure to the most relevant technologies, including AI. Our approach is to select the highest quality companies with the strongest management teams and strongest competitive advantages (widest moats). Growth is an important factor, but it must be profitable growth. And of course, valuation matters to us.

One of the investment tools we use in our process is the Credit Suisse HOLT™ valuation system, which is very helpful in identifying quality and also quantifying the future profitability and growth priced into current valuations.

The following chart shows where HOLT plots each AI company on a quality/growth matrix. The highest quality companies plot on the right side of this chart, and the highest growth companies plot on the top half of this matrix. Our holdings are circled in red. Note: This is a global matrix (not just US).



As you can see, our holdings are among the very highest quality in the space (ranging from the 80th to 100th percentile, left to right). The HOLT Quality factor assesses the relative attractiveness of a company based on level and variability of Cash Flow ROIs. The factor incorporates the most recently achieved CFROI level, 5-year median CFROI, and the 5-year range in CFROI.

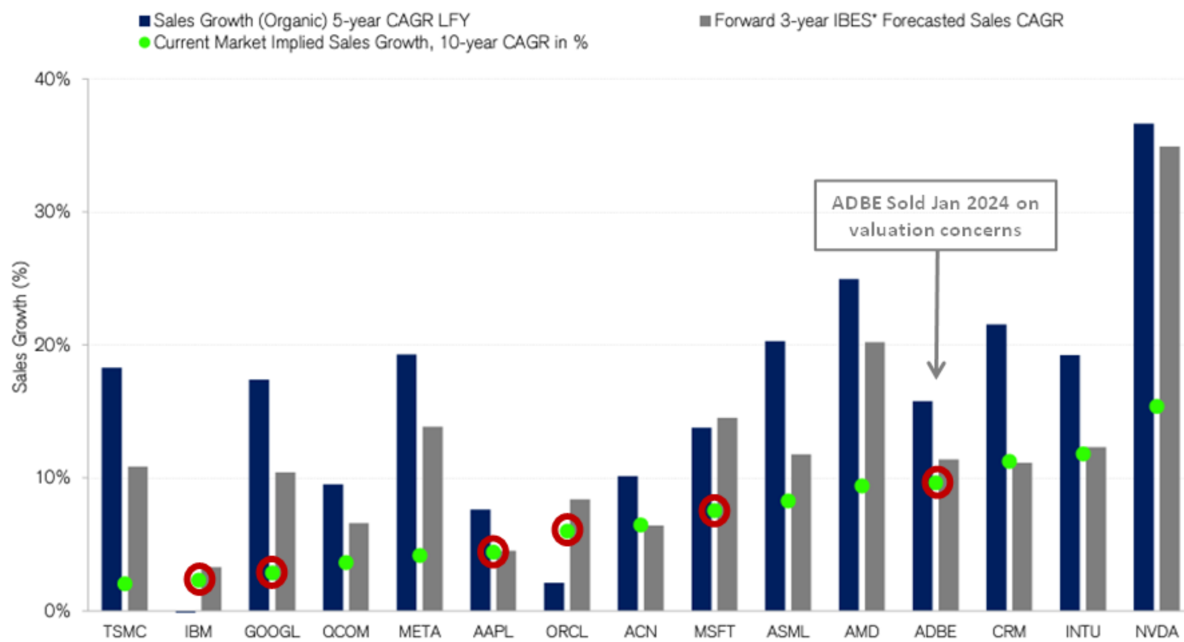
From a growth standpoint, our holdings are spread fairly evenly across the spectrum. IBM and Apple have historically shown below average growth relative to this global group, whereas Microsoft and Adobe are both in the top quintile for growth. It is the combination of profitability and growth that creates or destroys shareholder value. Companies in the top right quadrant (high quality, high growth) have created the most shareholder value, whereas companies in the top left quadrant (low quality, high growth) have destroyed the most value over the past 3 years. Jim Cramer "faves" Splunk and Okta are among this group.

Looking Forward: Market-Implied Growth

Once you've assessed quality and historical growth, its important to understand what level of growth is "priced in" to each stock. And compare this to what you believe is a reasonable growth forecast. The green dots in the following chart show the forward 10 year CAGR that is currently priced into each of the largest AI stocks in the US.

2) Artificial Intelligence - Who is Exposed & What's Priced In: The below contextualizes Market Implied Sales Growth for the largest AI Exposed TMT Firms. The market has low long-term growth expectations for TSMC, GOOGL, QCOM and META (compared to peers, history and IBES consensus estimates). Conversely, NVDA is priced with the highest long-term sales growth expectations at 15%.

HOLT Market Implied Sales Growth for Top 15 TMT firms by Market Cap in Artificial Intelligence Theme



CREDIT SUISSE Note: Sourced from HOLT Lens. Data as of 2/28/2024. 3y IBES sales, margins and tax rates estimates are used when available in HOLT Lens, asset turns are set to LFY level, and the implied annual sales growth over 2027-2033 (10y forecast window) are solved for (2026-2032 for TSMC, IBM, ORCL, CRM). Top 15 companies from the HOLT Artificial Intelligence theme in TMT shown with CFROI > Discount Rate and a low Market Value of Investments (relative to Equity Value). LFY margins used for Salesforce in lieu of compatible IBES margins.

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The AI names in our portfolio (red circles) are priced to deliver approx. 5% CAGR over the next 10 years. We believe this is very reasonable. By comparison, according to HOLT's analysis, NVDA is priced for 15% growth *per year* for the next decade. Although 15% is much lower than they have posted in recent quarters, it's worth noting that a 15% CAGR implies that NVDA's annual sales (currently ~$60 billion) will reach $250 billion. And a 3% miss (12% CAGR) results in a 30% haircut to its current warranted value.

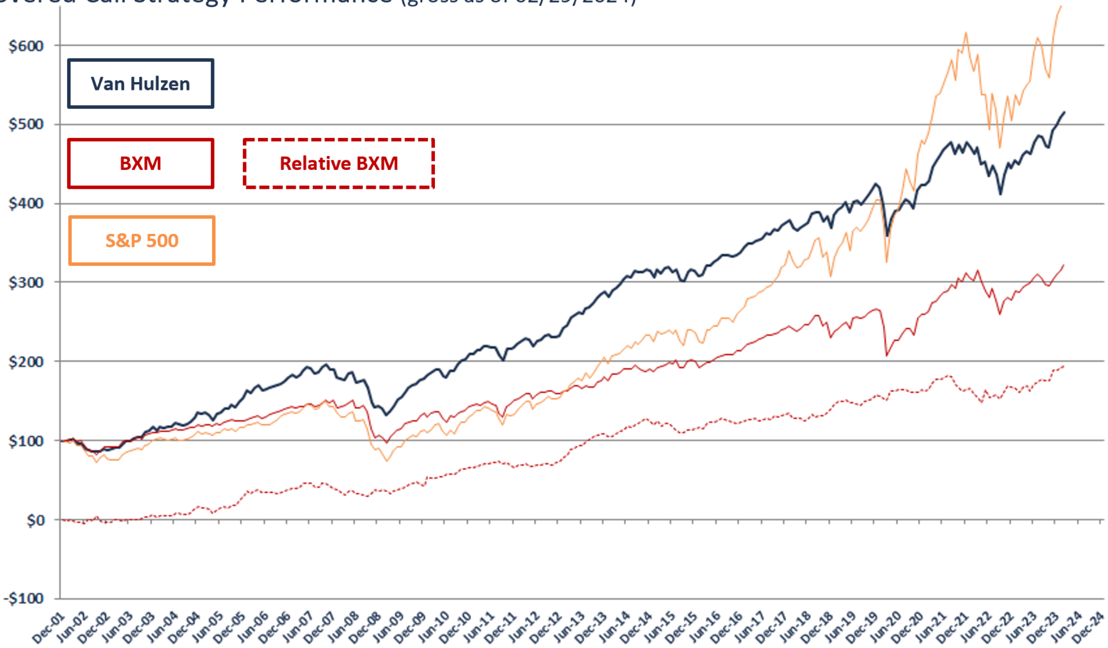
Key Takeaways

- The AI names we hold in the portfolio are among the very highest quality in the space (far right of chart 1) and have delivered average growth compared to their global peers in the space.
- However, they are "priced" for lower than average growth going forward (chart 2). We believe these expectations are reasonable and our holdings are attractively priced relative to the group.
- And of course, the extra income we collect from writing call options gives us very nice downside cushion in case future performance falls short. This is true across the entire portfolio.

Van Hulzen Covered Call Strategy

The Van Hulzen Covered Call strategy invests in US companies that we consider to have high shareholder yield (dividends and share repurchases) and uses call options with the goal of reducing portfolio volatility and creating incremental income. The goal is a portfolio that has equity exposure while seeking higher than average annual income (target of 6-8% annual), although there is no guarantee that the strategy will achieve its objective, generate profits or avoid losses. Below you will find the graph of the Van Hulzen Covered Call Strategy and the Covered Call Index BXM.

Covered Call Strategy Performance (gross as of 02/29/2024)



Returns (annualized)*	Feb 2024	3M	6M	YTD	1 Year	3 Years	5 Years	7 Years	10 Years	Inception
Van Hulzen (Gross)	1.4%	4.6%	6.5%	3.2%	14.7%	6.4%	5.6%	5.7%	5.9%	7.7%
Van Hulzen (Net)	1.4%	4.5%	6.2%	3.1%	14.1%	5.8%	5.0%	5.1%	5.3%	6.8%
BXM	1.9%	5.8%	5.2%	3.7%	11.5%	7.0%	5.8%	5.4%	5.7%	5.4%
Difference (Gross-BXM)	-0.6%	-1.1%	1.3%	-0.5%	3.1%	-0.6%	-0.2%	0.3%	0.2%	2.3%
S&P 500	5.3%	12.0%	13.9%	7.1%	30.5%	11.9%	14.8%	13.6%	12.7%	9.1%

*Inception date : 12/31/2001. Figures greater than one year are annualized. Van Hulzen returns represent actual returns from composite of accounts

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