



CRESCAT CAPITAL[®]
THE VALUE OF GLOBAL MACRO INVESTING

Crescat Capital LLC
44 Cook St., Suite 100
Denver, CO 80206
(303) 271-9997
info@crescat.net
www.crescat.net

August 31, 2024

Asset Bubbles and Inflation

The Federal Reserve has signaled lower short-term rates ahead, but two important macro questions have yet to be answered:

1. Do the asset bubbles of the post Global Financial Crisis zero-interest-rate-policy era still need to be unwound?
2. Has the Fed truly conquered US long-term inflation expectations or might Jerome Powell's victory lap at Jackson Hole have been premature?

Lingering Asset Bubbles

We contend there is no permanent new plateau for large-cap growth equity valuations. In our view, the megacap tech segment of the Russell 1000 Growth Index, fueled by AI euphoria and the Magnificent 7, presents one of the biggest downside risks to financial markets and the economy today. We will build on this thesis throughout this letter.



Disclosure: Crescat may or may not hold positions at any given time in the securities referenced herein. This is not a recommendation or endorsement to buy or sell any security or other financial instrument. The information reflected in the chart above is represented as of 8/23/24.

Nvidia: Leading Vendor to the AI Hyperscalers

Nvidia has capitalized on its technological lead in graphics processing hardware. Its GPUs have become the dominant brute-force engine for AI training in the cloud. Nvidia's earnings growth and profit margins have reached historic high levels for the company over the past five quarters, with EPS year-over-year growth peaking to date at 1,089% in the quarter ended 10/29/23 and gross margins topping so far at 78.4% in the quarter ended 4/28/24 which is outstanding for the whole IT sector. But selling high-end computer chips to AI hyperscalers is a double-edged sword. It's great for Nvidia and its shareholders as long as the capital spending party is still raging, but what happens if Nvidia's customers are not getting a positive return on that investment? The party could be over and might even end in an economy-wide hangover. We'll explore this idea further below.

Some of Nvidia's customers may already be pulling in the reins as Nvidia's recent quarter featured growth deceleration, lower gross margins, lower positive earnings and sales surprises, and tempered guidance. Meanwhile, AI software is getting smarter and more efficient in burning less raw GPU power for the same computing tasks. Competition in GPUs from AMD and Intel is also heating up. In this environment, we don't see how Nvidia can continue to deliver the high growth and margins necessary to justify its historically high valuation with multiples of 52.4 times book value and 30.3 times enterprise value compared to trailing twelve months sales. Perhaps that is why billionaire investor and famed macro trader Stan Druckenmiller sold the vast majority of his formerly hefty Nvidia position over the last two quarters per his family office's 13F filings.



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Apple: Late to the AI Party

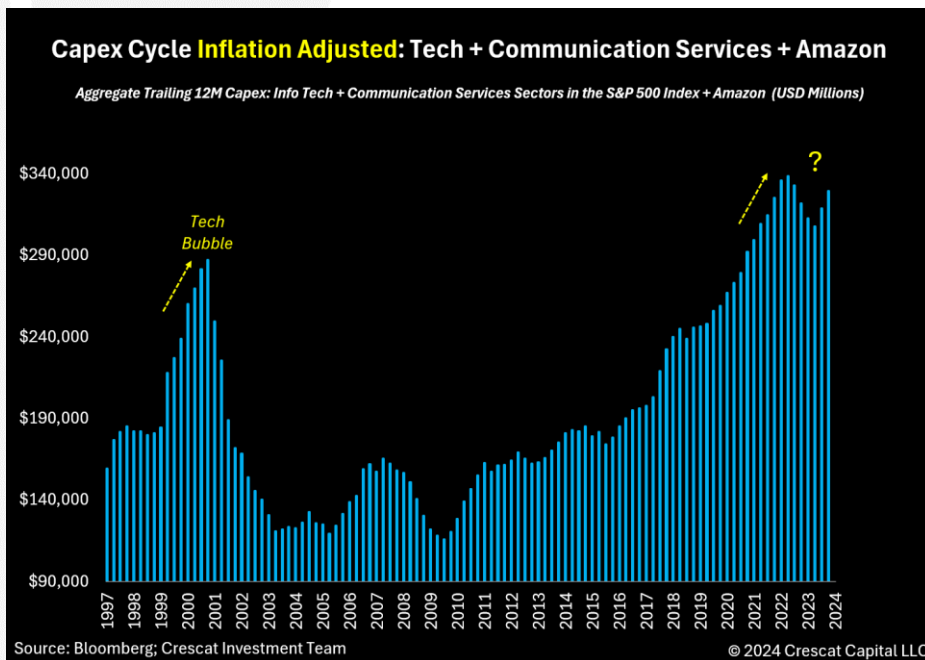
In our analysis, Apple represents another asset bubble in the IT sector at risk of unwinding. Other than the Apple Watch and AirPods, the company has not successfully introduced many new products to the market in recent years. Virtual reality headsets were essentially a flop. The self-driving car was a complete write-off. It seems that organic innovation at Apple has been lacking without the leadership of Steve Jobs. CEO Tim Cook has been adept at extending the company's dominant smartphone franchise, but growth has stalled. Apple's sales declined year-over-year in five of the last seven quarters while the company has missed out almost entirely to date on the AI party. Recently, its shares have been buoyed by the hope that adding outsourced AI features to its iPhone handsets will revive growth next quarter. We do not share the same optimism. Neither likely does value investing sage, Warren Buffett, the *Oracle of Omaha*, the company's largest shareholder who sold almost half of his firm Berkshire Hathaway's position per its latest 10-Q.



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Capex Cycles Drive Booms and Busts

We believe unsustainable capital expenditure trends in the broad technology and communications sectors are an economic warning signal. The chart below shows how the capex cycle drove the boom and bust of the 2000 tech and telecommunications bubble. We inflation-adjusted the data in this chart using the Consumer Price Index to display the entire time series in today's dollars. It reveals a comparably larger extreme capex binge in real terms in recent years compared to the 2000 Internet spending peak in those same two sectors. We have added Amazon to this group because the company is the largest tech hyperscaler today as we explain further below. It is otherwise overlooked because it is categorized in the consumer discretionary sector due to its online retail business. We are excited about the technological advancements in AI that all this spending has produced, but our research shows that capital spending trends are cyclical. It's a basic law of economics that companies cannot spend endlessly without a clear path to getting a positive net-present-value return on that investment.



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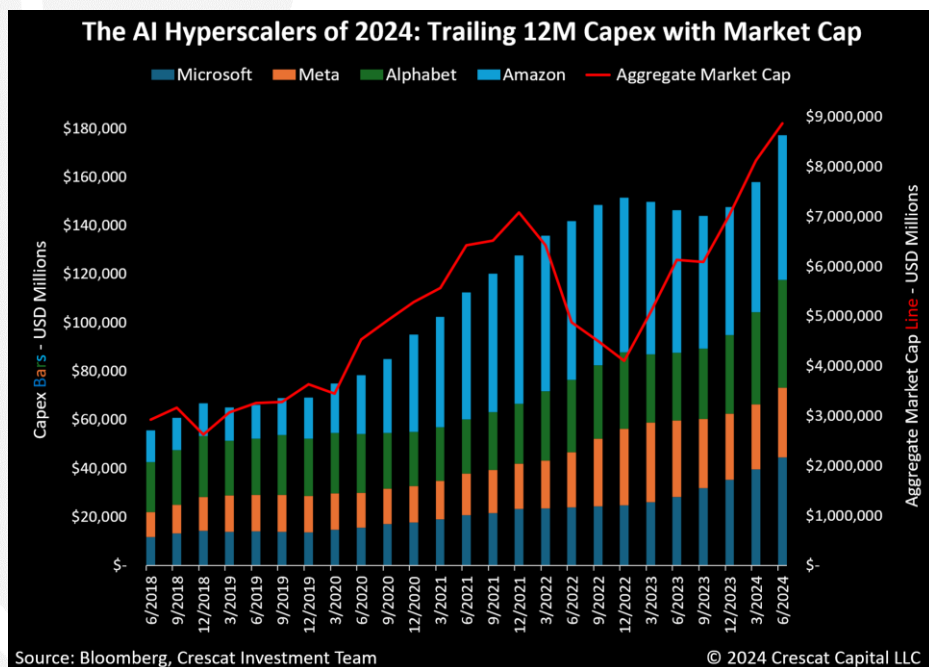
The AI Hyperscalers

The four leading capex spenders today, Amazon, Microsoft, Alphabet, and Meta have been dubbed the hyperscalers for their massive data centers and cloud computing businesses that can scale up and down based

on customer demand including demand for AI training and inference services. It is a high-capex, relatively low-profit margin competitive business. In the chart below, we show the capex spending trends and combined market caps of the four hyperscalers.

Amazon's AWS division is the leading cloud services hyperscaler. Alphabet and Microsoft have been trying to compete directly with AWS in this business, but it is not their high-profit-margin core business. Amazon is a company that thrives on efficiency, scale, and low margins based on the philosophy and competitive drive of its chairman and founder, Jeff Bezos. "Your margin is my opportunity" is his motto. Alphabet and Microsoft meanwhile are accustomed to earning high margins in monopoly-like search advertising and software businesses. We think Microsoft and Alphabet will continue to struggle to compete with Amazon in low-margin hyperscale AI cloud services yet both companies are significantly ramping up investment in that effort. We expect this to drive the return on capital and profit margins down for all three cloud providers.

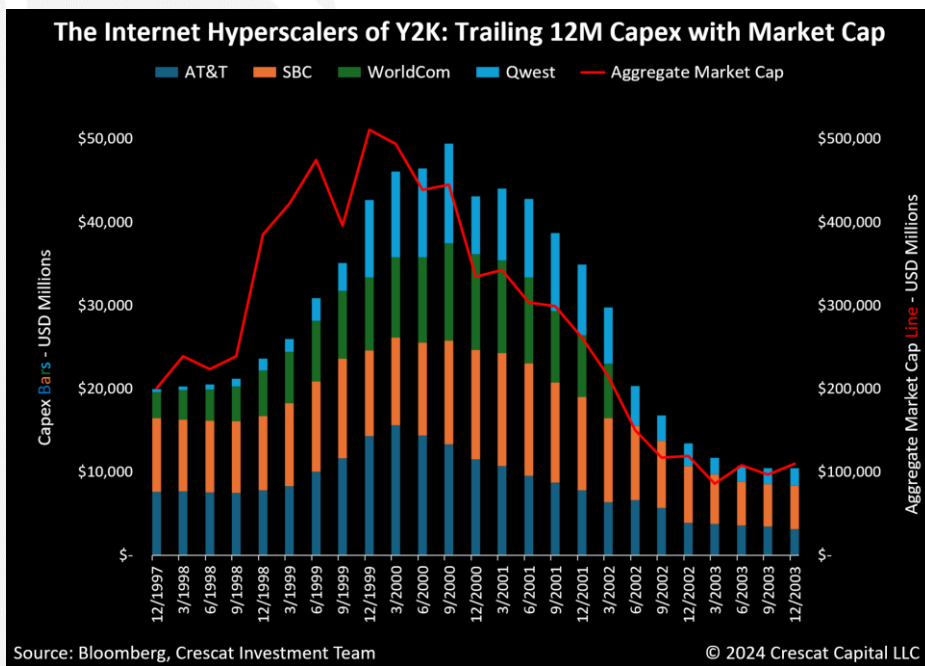
Meta does not compete in the cloud business but is still considered the fourth largest hyperscaler based on its massive data centers and high capex spend. Meta is building organic AI technology and applying it to its social media and advertising business. The high capital investment required to compete in the AI hyperscale business is extraordinary. The biggest portion of this spending today is going to richly priced, fast-depreciating Nvidia GPUs.



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Tech Hyperscaling is Not a New Phenomenon

For comparison to today's hyperscalers, we want to look at the four leading capex spending companies during the late 1990s Internet boom. Our Bloomberg research confirms those to have been AT&T, SBC Communications, WorldCom, and Qwest. We show these companies' capital spending and combined market cap trends, *at that time*, in the chart below. What it shows is that when big companies spend aggressively in a race to build tech infrastructure for an exciting new-era technology without a feasible business plan for getting a return on that investment, we believe it creates a boom and bust for the entire industry, sector, and economy. Could today's tech hyperscalers be taking us down the same path as these forerunners?

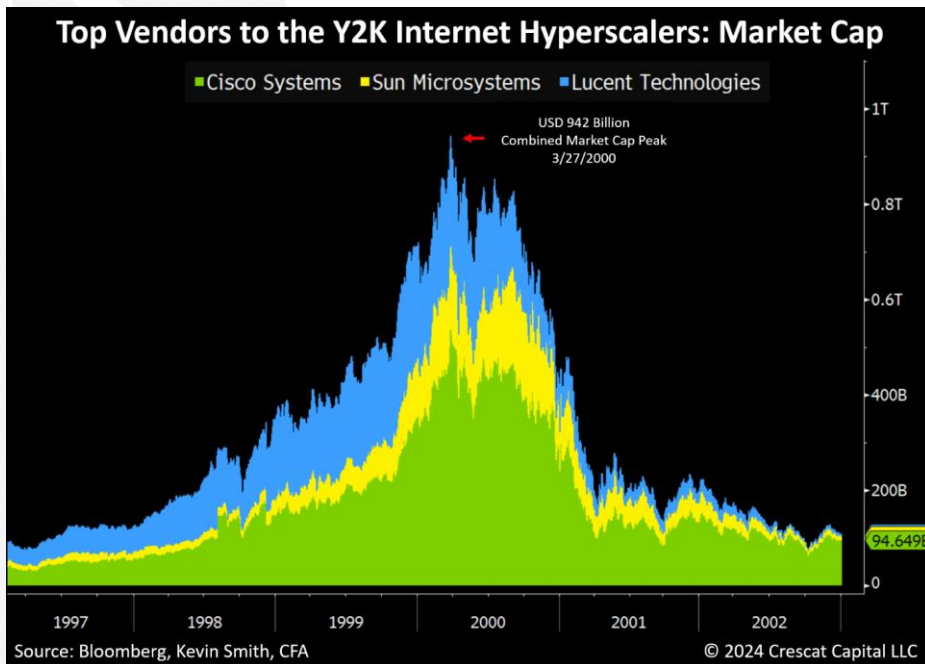


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What Happened to the Y2K High-End Equipment Dealers?

Nvidia is the leading vendor to today's hyperscalers, but who were their Y2K counterparts? Based on our Bloomberg research, Cisco Systems, Sun Microsystems, and Lucent Technologies were three of the top vendors at the time. The stacked chart below shows the combined market cap of these three companies during that period. First, they appreciated more than tenfold in the three years leading up to early 2000 while their

customers binged on capital spending. Then, their combined market cap declined by almost 90% as the capex spending trend reversed sharply in the tech bust and recession.



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The Capex Cycle for Mining Looks Bullish

While understanding the capex cycle can be helpful for warning when it could be late in the game for a particular sector or industry, it can also be useful for identifying when it might be early.

“Bull markets are born on pessimism, grow on skepticism, mature on optimism, and die on euphoria.” – John Templeton

This quote may capture the current opportunity in the mining industry, which, despite near-record gold prices, remains one of the most under-owned industries in the market today.

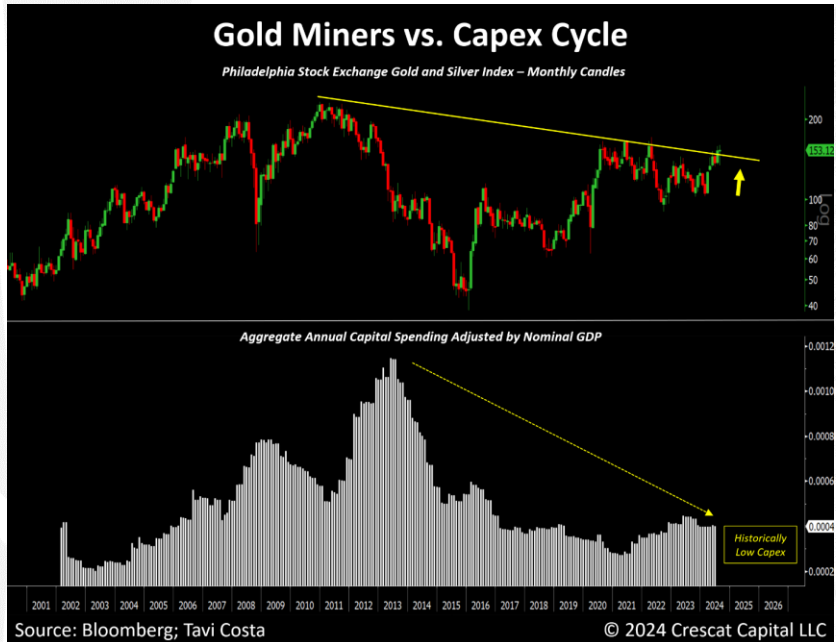
Gold, silver, copper, and zinc miners have suffered a prolonged period of investor disinterest combined with social and government permitting headwinds. Such forces have compelled these companies to exercise austere spending measures including drastically reduced capex. Poetic justice for mining companies may yet be served

because, in our analysis, the world no longer possesses the metal reserves necessary to supply its growing demand for electricity due to the climate-change-driven energy transition and artificial intelligence.

The world needs metals for electric vehicles, solar, wind, and AI data centers. Silver and copper are critical raw materials for solar panels and the electricity grid. We need zinc for windmills. Meanwhile, gold is a key ingredient in high-end electronics, such as Nvidia GPUs and next-generation quantum computers. The latter only solidifies our view that the yellow metal will remain in favor among global sovereign central banks and citizens alike, as it has for millennia, as the leading global hard-money reserve currency.

With metal prices rising because of these supply and demand imbalances, and due to ongoing global concern about inflation, we think investors will finally become attracted to the mining industry again. As a result, mining companies should start receiving the capital they need to invest in exploration and capex to build new mines. The problem is that it takes an average of 15 years to discover, permit, and build a new mine, so there is potentially a long cycle of rising commodity prices ahead as demand exceeds supply.

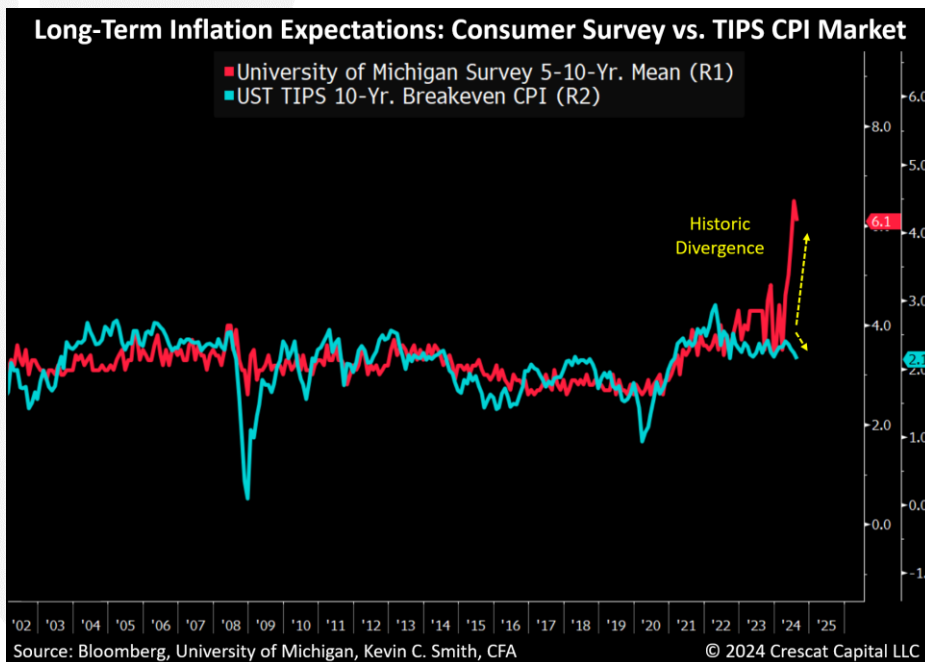
In the lower panel of the chart below, we show that it is still likely very early in the capex cycle for the mining industry. It last peaked in 2012 and then went through an 8-year contraction. In the upper panel, we can see that investors have been buying mining stocks as represented by the recent 13-year breakout in the Philadelphia Stock Exchange Gold and Silver Index. We believe that mining stocks have a long runway ahead as capital will likely continue to flow back into the industry under rising commodity prices. Note that the last secular increasing capex cycle lasted about 10 years while we are only about 3 years into the current one. Furthermore, the chart shows that we are far away from prior peak levels of capex spending as a ratio of GDP that would likely need to be reached again before warning of a top.



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Historic Divergence in Long-Term Inflation Expectations

According to the recent University of Michigan Consumer Survey data, the average US consumer believes that inflation will be 6.1% over the next five to ten years. The Treasury Inflation Protected Securities (TIPS) market on the other hand indicates that CPI will be only 2.1% during that time as we show in the chart below. This suggests consumers believe government CPI statistics will understate actual inflation in the future to a greater degree than ever before. Such a sentiment is understandable. We think the recent historic divergence between these two time series is a measure of current high government mistrust. So, if the Fed is claiming victory over long-term inflation expectations based on the TIPS market alone, we believe it has a lot more work to do. Furthermore, since the Fed has just signaled a green light for interest rate cuts, we expect consumers to remain skeptical that the Fed truly has inflation under control.



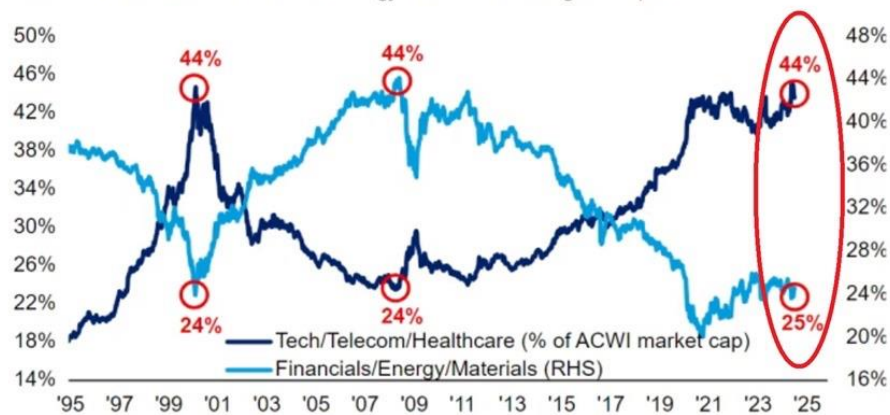
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Commodity Equity Bull Markets Can Begin with Tech Busts

The chart below from Bank of America shows how an equity bull market in energy, materials, and financials began simultaneously with the 2000 tech and telecom bust using the sectors in the MSCI All-Country World Index. We think a similar rotation in favor of commodity equities is poised to unfold again today based on similar imbalances, positioning, and relative valuations to 2000. The Great Rotation, one of Crescat’s overriding investment themes, which encompasses this transition out of overvalued large cap growth and into undervalued energy and natural resource equities, started to play out through all of 2022. However, here we are again with a complete retest of the extremes. We believe the Great Rotation is still to come.

Exhibit 14: Tech/telecom/healthcare peaked at 45% of global equities in July 2024

Tech/telecom/healthcare vs financials/energy/materials as % of global equities



POSTED BY @KOBESSILETTER

Source: BofA Global Investment Strategy, MSCI, Refinitiv

Disclosure: Crescat may or may not hold positions at any given time in the securities referenced herein. This is not a recommendation or endorsement to buy or sell any security or other financial instrument. AWCI refers to the MSCI All-Country Global Index. RHS refers to the right Y axis, i.e., “right-hand side”.

Performance

Net returns are shown below through July in a new format. Performance figures presented “Excluding SCM SP” represent the fund’s net returns calculated without the impact of the San Cristobal Mining, Inc. (“SCM”) side pocket that was designated on July 1st, 2024. The side pocket includes a private equity asset that is not available to new investors in the funds on or after July 1, 2024. Excluding these assets provides a clearer view of the performance to investors coming into the funds after that date. New investors cannot participate in the SCM Side Pocket and will not share in its potential gains or losses. Investors should consider both the overall performance and the performance excluding the side pocket when evaluating the fund’s returns.

Crescat Strategies Net Return Through July 31, 2024

| CRESCAT STRATEGIES VS. BENCHMARK (Inception Date) | JULY | YTD | ANNUALIZED TRAILING | | | | SINCE INCEPTION | CUMULATIVE SINCE INCEPTION | YEARS SINCE INCEPTION |
|---|-------|--------|---------------------|--------|--------|---------|--------------------|----------------------------------|--------------------------|
| | | | 1-YEAR | 3-YEAR | 5-YEAR | 10-YEAR | | | |
| Global Macro Hedge Fund¹ (Jan. 1, 2006) | 1.8% | -9.1% | -25.2% | -12.0% | 4.7% | 3.2% | 8.6% | 364.6% | 18.6 |
| Excluding SCM SP ² (Jan. 1, 2006) | 3.0% | -8.0% | -24.3% | -11.6% | 4.9% | 3.3% | 8.7% | 370.1% | 18.6 |
| Benchmark: HFRX Global Hedge Fund Index | 0.7% | 3.7% | 5.7% | 0.8% | 3.2% | 1.7% | 1.2% | 25.2% | |
| Long/Short Hedge Fund¹ (May 1, 2000) | 1.2% | -2.5% | -20.6% | -14.8% | 2.3% | 1.9% | 5.4% | 256.5% | 24.3 |
| Excluding SCM SP ² (May 1, 2000) | 2.0% | -1.6% | -20.0% | -14.6% | 2.4% | 1.9% | 5.4% | 259.7% | 24.3 |
| Benchmark: HFRX Equity Hedge Index | 0.7% | 5.9% | 9.1% | 4.3% | 5.8% | 3.5% | 2.9% | 98.8% | |
| Precious Metals Hedge Fund¹ (August 1, 2020) | -3.1% | -6.4% | -10.1% | -11.3% | - | - | 23.7% | 134.0% | 4.0 |
| Excluding SCM SP ² (August 1, 2020) | -5.2% | -8.5% | -12.0% | -11.9% | - | - | 23.0% | 129.0% | 4.0 |
| Benchmark: Philadelphia Gold and Silver Index | 10.9% | 22.3% | 22.0% | 3.8% | | | 1.3% | 5.4% | |
| Large Cap SMA¹ (Jan. 1, 1999) | 3.4% | -1.1% | -4.6% | -3.0% | 3.0% | 5.5% | 8.8% | 763.6% | 25.6 |
| Benchmark: S&P 500 Index | 1.2% | 16.7% | 22.1% | 9.6% | 15.0% | 13.1% | 8.0% | 621.7% | |
| Precious Metals SMA¹ (June 1, 2019) | -4.7% | -25.9% | -38.3% | -27.5% | 1.0% | - | 5.8% | 34.2% | 5.2 |
| Benchmark: Philadelphia Gold and Silver Index | 10.9% | 22.3% | 22.0% | 3.8% | 13.4% | | 17.9% | 134.8% | |

Performance data represents past performance, and past performance does not guarantee future results. Performance data is subject to revision following each monthly reconciliation and/or annual audit. Individual performance may be lower or higher than the performance data presented. The currency used to express performance is U.S. dollars. Before January 1, 2003, the results reflect accounts managed at a predecessor firm. See additional performance disclosures below.

We encourage you to reach out to any of us listed below if you would like to learn more about how our vehicles might fit with your individual needs and objectives.

Sincerely,

Kevin C. Smith, CFA
Founding Member & Chief Investment Officer

Tavi Costa
Member & Macro Strategist

Quinton T. Hennigh, PhD
Member & Geologic and Technical Director

For more information including how to invest, please contact:

Marek Iwahashi
Head of Investor Relations
miwahashi@crescat.net
(720) 323-2995

Linda Carleu Smith, CPA
Co-Founding Member & Chief Operating Officer
lsmith@crescat.net
(303) 228-7371

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These opinions are current opinions as of the date appearing in the relevant material and are subject to change without notice. The information contained in the letters is based on publicly available information with respect to the Issuers as of the date of such white papers and has not been updated since such date.

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1 - Net returns reflect the performance of an investor who invested from inception and is eligible to participate in new issues and side pocket investments. Net returns reflect the reinvestment of dividends and earnings and the deduction of all expenses and fees (including the highest management fee and incentive allocation charged, where applicable). An actual client's results may vary due to the timing of capital transactions, high watermarks, and performance.

2 - Performance figures presented Excluding SCM SP represent the fund's net returns calculated without the impact of the San Cristobal Mining, Inc. side pocket that was designated on July 1st, 2024. The side pocket includes a private equity asset that is not available to new investors in the funds on or after July 1, 2024. Excluding these assets provides a clearer view of the performance to investors coming into the funds after that date. New investors cannot participate in the SCM Side Pocket and will not share in its potential gains or losses. Investors should consider both the overall performance and the performance excluding the side pocket when evaluating the fund's returns.

3 - The SMA composites include all accounts that are managed according to CPM's precious metals or large cap SMA strategy over which it has full discretion. Investment results shown are for taxable and tax-exempt accounts. Any possible tax liabilities incurred by the taxable accounts are not reflected in net performance. Performance results are time weighted and reflect the deduction of advisory fees, brokerage commissions, and other expenses that a client would have paid, and includes the reinvestment of dividends and other earnings.

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Benchmarks

RUSSELL 1000 GROWTH INDEX. The Russell 1000® Growth Index measures the performance of the large cap growth segment of the US equity universe. It includes those Russell 1000 companies with relatively higher price-to-book ratios, higher I/B/E/S forecast medium term (2 year) growth and higher sales per share historical growth (5 years). The Russell 1000® Growth Index is constructed to provide a comprehensive and unbiased barometer for the large-cap growth segment. The index is completely reconstituted annually to ensure new and growing equities are included and that the represented companies continue to reflect growth characteristics.

HFRX GLOBAL HEDGE FUND INDEX. The HFRX Global Hedge Fund Index represents a broad universe of hedge funds with the capability to trade a range of asset classes and investment strategies across the global securities markets. The index is weighted based on the distribution of assets in the global hedge fund industry. It is a tradeable index of actual hedge funds. It is a suitable benchmark for the Crescat Global Macro private fund which has also traded in multiple asset classes and applied a multi-disciplinary investment process since inception.

HFRX EQUITY HEDGE INDEX. The HFRX Equity Hedge Index represents an investable index of hedge funds that trade both long and short in global equity securities. Managers of funds in the index employ a wide variety of investment processes. They may be broadly diversified or narrowly focused on specific sectors and can range broadly in terms of levels of net exposure, leverage employed, holding periods, concentrations of market capitalizations and valuation ranges of typical portfolios. It is a suitable benchmark for the Crescat Long/Short private fund, which has also been predominantly composed of long and short global equities since inception.

PHILADELPHIA STOCK EXCHANGE GOLD AND SILVER INDEX. The Philadelphia Stock Exchange Gold and Silver Index is the longest running index of global precious metals mining stocks. It is a diversified, capitalization-weighted index of the leading companies involved in gold and silver mining. It is a suitable benchmark for the Crescat Precious Metals private fund and the Crescat Precious Metals SMA strategy, which have also been predominately composed of precious metals mining companies involved in gold and silver mining since inception.

S&P 500 INDEX. The S&P 500 Index is perhaps the most followed stock market index. It is considered representative of the U.S. stock market at large. It is a market cap-weighted index of the 500 largest and most liquid companies listed on the NYSE and NASDAQ exchanges. While the companies are U.S. based, most of them have broad global operations. Therefore, the index is representative of the broad global economy. It is a suitable benchmark for the Crescat Global Macro and Crescat Long/Short private funds, and the Large Cap and Precious Metals SMA strategies, which have also traded extensively in large, highly liquid global equities through U.S.-listed securities, and in companies Crescat believes are on track to achieve that status. The S&P 500 Index is also used as a supplemental benchmark for the Crescat Precious Metals private fund and Precious Metals SMA strategy because one of the long-term goals of the precious metals strategy is low correlation to the S&P 500.

MSCI ALL COUNTRY WORLD INDEX (ACWI). The MSCI All Country World Index is a market capitalization-weighted index that offers investors a snapshot of global equity market performance. It is designed to represent the performance of both developed and emerging markets, providing a comprehensive overview of the global investment landscape. To determine the composition of the index, MSCI, the leading provider of equity indexes, considers three categories of stocks: 1) Large-cap stocks from developed markets, 2) Large-cap stocks from emerging markets, 3) Mid-cap and small-cap stocks from both developed and emerging markets. By including stocks from various market segments, the ACWI ensures a balanced representation across different regions and market caps. This helps provide a more accurate reflection of global equity market performance. The ACWI is rebalanced periodically to maintain its integrity and relevance as market conditions change. The index is reviewed on a quarterly basis, ensuring that any changes in market capitalizations or country classifications are appropriately reflected. The index consists of stocks from more than 50 countries worldwide, covering both developed and emerging markets.

References to indices, benchmarks or other measures of relative market performance over a specified period of time are provided for your information only. Reference to an index does not imply that the fund or separately managed account will achieve returns, volatility or other results similar to that index. The composition of an index may not reflect the manner in which a portfolio is constructed in relation to expected or achieved returns, portfolio guidelines, restrictions, sectors, correlations, concentrations, volatility or tracking.

Separately Managed Account (SMA) disclosures: The Crescat Large Cap Composite and Crescat Precious Metals Composite include all accounts that are managed according to those respective strategies over which the manager has full discretion. SMA composite performance results are time-weighted net of all investment management fees and trading costs including commissions and non-recoverable withholding taxes. Investment management fees are described in CPM's Form ADV 2A. The manager for the **Crescat Large Cap** strategy invests predominantly in

equities of the top 1,000 U.S. listed stocks weighted by market capitalization. The manager for the **Crescat Precious Metals** strategy invests predominantly in a global all-cap universe of precious metals mining stocks.

Hedge Fund disclosures: Only accredited investors and qualified clients will be admitted as limited partners to a CPM hedge fund. For natural persons, investors must meet SEC requirements including minimum annual income or net worth thresholds. CPM's hedge funds are being offered in reliance on an exemption from the registration requirements of the Securities Act of 1933 and are not required to comply with specific disclosure requirements that apply to registration under the Securities Act. The SEC has not passed upon the merits of or given its approval to CPM's hedge funds, the terms of the offering, or the accuracy or completeness of any offering materials. A registration statement has not been filed for any CPM hedge fund with the SEC. Limited partner interests in the CPM hedge funds are subject to legal restrictions on transfer and resale. Investors should not assume they will be able to resell their securities. Investing in securities involves risk. Investors should be able to bear the loss of their investment. Investments in CPM's hedge funds are not subject to the protections of the Investment Company Act of 1940.

Investors may obtain the most current performance data, private offering memoranda for CPM's hedge funds, and information on CPM's SMA strategies, including Form ADV Part 2 and 3, by contacting Linda Smith at (303) 271-9997 or by sending a request via email to lsmith@crescat.net. See the private offering memorandum for each CPM hedge fund for complete information and risk factors.