Our *Promise* to Clients

*W*e are anything but just another Wall Street firm, and therefore not everyone who knocks on our door is an appropriate client for us.

*O*ur clients are our partners, and just like partners in a marriage, we need to share the same values. Our values are spelled out in Six Commandments of Value Investing (read, listen).

*W*e promise to be honest and transparent with our partners. We will invest their money with the same thoughtfulness, care, diligence, and slight hint of paranoia that we employ in investing our own (easy for us to do, as nearly all the liquid net worth of our portfolio managers and their families is invested in the same stocks our clients own).

*W*e are a firm with a soul, and we'll never do anything that would put our interests before those of our clients.

*W*e're not trying to be the biggest investing firm, just the best one. In addition to striving to provide great true-risk-adjusted returns, we'll deliver excellent customer service and a one-of-a-kind client experience.

INDIVIDUAL PORTFOLIO MANAGEMENT SINCE 1979

March 31, 2025

Dear Client,

In this letter, I address questions from our clients about European defense spending, the outlook for the US dollar, and how our portfolio is positioned for potential economic changes. I examine trade war implications, whether "value" needs redefining in today's environment, and how AI tools are affecting our research process. I share perspectives on Tesla, cryptocurrencies, portfolio hedging strategies, and noteworthy lessons from the past year.

The Paranoid Russian Jew Approach to Investing

When asked about his money manager, our long-term client Ed, who became a dear friend, proudly stated, "My money is managed by a paranoid Russian Jew."

This perfectly sums up our approach to investing.

Let me double-click on this a bit.

Historically, Jews were always on the receiving end of the very tip of the spear of adversity. As a result, they had to be more paranoid than the rest of society. My maternal grandfather taught me that when you open a Soviet newspaper, you needed to read between the lines and pay attention not only to what is said but, more importantly, what is not said.

This paranoia is passed from generation to generation. That is what Ed saw in our approach. We pay a lot of attention not just to what is in front of our eyes but to risks (and opportunities) that are lurking around the corners.

Of course, there is healthy and unhealthy paranoia. Unhealthy paranoia is being haunted by shadows everywhere you go. Healthy paranoia is being alert, noticing subtle changes, and paying attention to the health of both the foundational structure of the environment and the inner workings of the system.

Jews have faced adversity for centuries, and their healthy paranoia has helped them to survive. This is precisely how we approach your portfolio. Healthy paranoia is deeply woven into our portfolio construction and visible in our holdings (as I've explained in my letters and articles).

Our investing in defense stocks is the latest example of this. The global security environment was changing, and our process allowed us to see that early. We started accumulating these positions *before* the war in Ukraine (at the time we saw them as extremely cheap, noncyclical, high-quality monopolies providing protection if the relationship with China escalated). We added to them when the war started, during the conflict, and as recently as February (as we kept updating our research).

IMA's goal is to grow your wealth and for you not to worry about the markets. We want to make you wealthier while minimizing the volatility of your blood pressure. We try to achieve this by ignoring the crowd and focusing on buying high-quality businesses run by excellent management at good prices. As a result, healthy paranoia is an integral part of our process – we pay attention to risks and opportunities that are not in today's headlines.

We're guided by our research and are willing to make unpopular decisions. When animal spirits hijack the market, our portfolio will lag. When panic takes over as the market declines, we will hopefully do better than the market (of course, we cannot make any promises). The last five years were a great example of that.

This year is playing out that way so far, too.

At the end of last year, I wrote to you about how while our portfolio delivered objectively good returns on an absolute basis, it didn't keep pace with the frenzied market. The market was fixated on AI and disregarded valuations. Consequently, despite our businesses performing fundamentally well, their stock prices were left in the dust by the "Magnificent Seven" – terrific but overvalued stocks that became even more overvalued.

Investing is a peculiar endeavor where your decisions in any given year may have little connection to your returns. We haven't gotten any smarter in 2025, but essentially the same portfolio that did not impress the market in 2024 is now up double digits this year.

There's a crucial distinction between our portfolio's gains today and the market's gains in 2024. In most cases, the market's average stock valuation went from overvalued to insanely overvalued. These gains were not sustainable, because they happened from expanded valuations and thus borrowed from future returns that have to be paid back. In 2025 our stocks have gone from severely undervalued to simply undervalued, with a few becoming fairly valued (we reduced those or sold them).

Our team typically spends hundreds of hours studying each company before we buy a full position. We have talked to the management team of almost every company we own, and we try to meet with them when we can. A year ago, I attended Babcock's (our largest holding) investor day in Plymouth, England, met their management, and also had a chance to visit their shipyard. On my recent trip to Switzerland, I had the pleasure of spending time with International Petroleum's CEO and CFO. And in early April, I'm going on a research trip to visit a few companies we are researching in the Washington, DC area, and I plan to visit Huntington Ingalls shipyards in Norfolk and meet with their management.

But we don't just talk to companies. For every single stock we own and many we analyzed but don't own, we build a financial model in which we try to *kill* the business And of course our research doesn't stop when we buy a company – in fact it intensifies.

People have been conditioned to think about stocks as "the market," but your portfolio with IMA today looks nothing like the market. A few months ago, I had a conversation with a good friend who has invested for four decades. We did our usual thing and talked stocks. I went through our top holdings, and he did not know two-thirds of them.

I've emphasized this point forever but it still bears repeating: The overall market is overvalued. It was overvalued last year, and it is still overvalued today. The average stock is at one of the highest valuations in modern history. But we don't own the market. Our portfolio is two dozen carefully placed investments in high-quality businesses run by good management teams. We made these research-driven decisions at the time of our choosing when our analysis led us to conclude these businesses were undervalued – when we were buying $1 for 50 cents or less.

I am comfortable admitting that we'll be wrong on some of these investments – we are dealing with imperfect information and occasionally life will simply happen to some of these companies. But as long as we stay disciplined, process-driven, and employ healthy paranoia, our strategy should work over the long run. I put my money where my mouth is, and my family and I own the same stocks you do.

I asked clients to send me questions they wanted me to answer. I'll attempt to do so in this letter, and in the next one I'll discuss individual stock positions. But before I start answering these questions, I need to address an orange elephant in the room.

Politics and investing

I am in an unenviable position. The policy coming out of the White House has a significant impact on economics, more than ever before in my career. If I say anything positive about that policy, I'll be put in the MAGA camp. If I criticize it, I'll be accused of suffering from Trump derangement syndrome.

I am hired by you to make the best investment decisions possible. Rather than see me as engaged in political commentary, I'd ask that you view my remarks as purely analytical.

Let me give you this analogy. I live in Denver. Let's imagine I am a huge Broncos fan, and the Broncos are playing the Chicago Bears. If I am betting a significant amount of money on this game, I should put my affinity for the Broncos and hatred of the Chicago Bears aside and analyze data and facts. The Broncos are either going to win or lose; my wanting them to win has zero impact on the outcome. The same applies to my analysis here.

My motto in life is Seneca's saying, "Time discovers truth." I just try to discover it before time does.

When it comes to politics, I also have a significant advantage. I was not born in this country. From a young age, I was brainwashed about communism, not about team Republican versus team Democrat. The failure of the Soviet Union de-brainwashed me fast concerning the virtues of communism and converted me into a believer in free markets.

As a result, I never bought into either party's ideology, and thus in the last four presidential elections I voted for a Republican, an independent, a Democrat, and wrote in my youngest daughter, Mia Sarah (not necessarily in that order). In my articles I have criticized the policies of both Biden (student loan forgiveness, unions) and Trump (Bitcoin reserve).

I remind myself that in times like these you have to be a nuanced thinker. Some of Trump's policies are terrific, others… not so much (I am being diplomatic here).

F. Scott Fitzgerald once said "The test of a first-rate intelligence is the ability to hold two opposed ideas in mind at the same time, and still retain the ability to function." In 2025 we are taking this "first-rate intelligence" test daily.

What will happen to the US dollar?

The US dollar will likely continue to get weaker, which is inflationary for the US.

Let me start with some easily identifiable reasons:

We have too much debt. We ran 6-7% budget deficits while our economy was growing and unemployment was at record lows. Now we have $36 trillion in debt. Our interest expenses exceed our defense spending, and these costs will continue to climb. If/when we go into recession, we may see something we have not seen in a long time – higher interest rates. Our budget deficits will balloon to between 9–12%, and the debt market, realizing that inflation (i.e., money printing) is inevitable, will say, "Pay up!"

New competition from Bitcoin. President Trump's approval of Bitcoin as a potential reserve currency is one of the most self-serving and anti-American things I've seen any president do. The US dollar is the world's reserve currency. We still have little competition for that title. China could be a contender, but it is not a democracy and has capital controls. This policy has no upside for America, only downside.

A stronger Europe. Ironically, we may inadvertently create a stronger Europe by threatening to abandon NATO. I don't want to insult European clients (or my European friends), but the following analogy describes the US-Europe relationship on some level: Europe gradually evolved into a trust fund kid (when it came to security) and the US turned into its sugar daddy. The trust fund kid was incredibly dependent on the sugar daddy. It criticized its parent for being a barbarian and money-driven, but it relied heavily on that parent to protect it from bullies.

President Trump cut off Europe's allowance by threatening that the US might not protect Europe from Russia. This has forced Europe to spend more money on defense. Outside of Germany (which has little debt), few European economies can afford that. This may force Europe (or at

least some European countries) to become more pragmatic – to cut social programs and bureaucracy. If this leads to a stronger Europe both economically and militarily, the euro will be competing with the US dollar. This is a big if.

Our new foreign policy. When people describe President Trump's foreign policy as "transactional," they're highlighting a fundamental shift in how America engages with the world – one with profound implications for our global standing, national interests, and the US dollar. The shift affects both types of capital – financial and reputational.

Reputational capital isn't at risk in 'one-shot' transactions like house selling. Imagine you're selling your primary residence and moving elsewhere. Do you disclose every flaw, or let the buyer figure things out? Your incentive is to maximize short-term profits. You'll likely never meet this buyer again, and therefore there are incentives not to care what they'll think of you afterward. You'll be transactional, seeking the highest price possible for your biggest asset. This exemplifies a 'one-shot' system where future interactions aren't expected.

Contrast this with a relationship- and trust-based system. Now imagine you are a homebuilder in a small town. Your suppliers only extend credit if you have a reputation for paying on time. Your employees do quality work only if you treat them fairly. Your buyers tell friends about their experience with you. The incentives naturally create a relational approach. In this trust-based system, incentives skew toward maximizing long-term profits, where reputational capital becomes the glue creating continuity.

Reputational capital radiates predictability – you know how someone will behave based on their history – but operating with low or negative reputational capital is difficult and expensive. People won't enter long-term contracts with you or will demand external guarantees. Many potential partners will simply refuse to deal with you.

Building reputational capital works like adding pennies to a jar – each good deed incrementally adds to your standing. Yet reputational capital can collapse instantly by removing the jar's bottom. A single breach of trust doesn't just remove one penny; it can wipe out your entire balance and plunge you into reputational bankruptcy. The math is brutally asymmetric: good deeds might add a point or two, while bad deeds subtract by factors of 50 or 100.

This doesn't mean transactions shouldn't be profitable. If you're accumulating reputational capital while consistently losing money, you're probably in the wrong business. Each deal should be evaluated considering both long-term financial and reputational capital.

Individual transactions can sacrifice some profit but cannot afford to lose reputational capital. A "one-shot" transactional approach used in a trust-system environment may provide greater short-term profitability, but if this success comes at the expense of reputational capital, the long-term consequences for America's global position could be devastating.

This brings us to our current foreign policy.

Relationships between nations are a trust-based system. I’d argue it’s a super-relational system because it’s multigenerational, lasting beyond the life of any one human. Reputational capital is paramount here.

Part of the US’s strength has been the soft power – the reputational capital – it exerted. We had a lot of friends, which helped us to be more effective in dealing with our foes. We keep telling ourselves that America is an “exceptional” nation. This exceptionalism didn’t just come from our financial and military might – it accumulated based on our reputational capital.

Though we don’t always succeed, we are a people who try to do the right thing. Our exceptionalism has been earned through our actions. We are the country that helped rebuild Europe and gave it six decades to repay lend-lease. We toppled communism.

I don’t know the nuances of the Ukraine mineral deal, but initially it had the optics of extortion. Though I think the renegotiated and signed version appears to be fair to both sides, forcing repayment while Ukraine is dodging Russian missiles made the US look transactional.

Actions by President Trump over the last month have undermined our reputation. We are quickly becoming a “one-shot” transactional player in a trust-based environment. Imposing tariffs on Canada on a whim to try to get it to become the 51st state erodes American reputational capital. So does not ruling out America invading Greenland. This puts us on the same moral plane as Russia invading Ukraine.

The conversation about tariffs has many nuances. For instance, I don’t know anyone who opposes reciprocal tariffs – they seem fair and don’t consume any reputational capital. But tariffs that are used as weapons in a trade war in order to annex another country erode reputational capital. Threatening to leave NATO and not protect countries that don’t spend enough on their defense diminishes reputational capital. Maybe the only way to get European countries to spend on defense was to threaten not to defend them – you can agree or disagree with the rationale behind each of Trump’s decisions, but what can’t be argued is that they undermined our reputational capital.

As we lose soft power, our influence will diminish, and thus so will perceptions of our power. The world will start looking at us not from the perspective of the continuity of generations but of presidential cycles. The word of the American president will have an expiration date of the next presidential or mid-term election.

There are two negotiation styles – Warren Buffett’s and Donald Trump’s. Both have their advantages and disadvantages. Buffett will give you one offer and one offer only. Once the deal is agreed to, even just verbally, that is the deal. Critics would say that there is downside to that predictability, as foes know how you are going to respond. Donald Trump’s style is to be unpredictable, which has its own advantages when you deal with foes – it keeps opponents guessing. But it destroys trust with your allies.

In a world of fiat currencies, all currency is a financial and reputational promise. President Trump, with the help of DOGE (and maybe even tariffs) may increase our financial strength. I

hope he does, but it will likely come at a very high cost to our reputational capital, and therefore US global influence and the US dollar will continue its decline.

How are we positioned for this?

About half of our portfolio is foreign companies whose sales are not in dollars. They will benefit from a weaker dollar. We also have exposure to oil, which is priced in the US dollar and usually appreciates when the dollar weakens.

A weaker dollar means our imports will become more expensive, which is inflationary. We own many companies with pricing power and also companies that have claims on someone else's revenues. Take Uber for example: they get about 20% of each ride. If the cost of the ride goes up, so does their dollar take.

Why does President Trump keep pushing crypto?

In July 2019, Trump said the following: "I am not a fan of Bitcoin and other cryptocurrencies, which are not money, and whose value is highly volatile and based on thin air." Five years later he promised to establish the US Crypto Reserve, and in 2025 he did.

What changed? There is no logical reason for an American president to endorse crypto. None. Here is the honest answer: Crypto bros made mega-contributions to his campaign.

To top it off, three days before he took office he issued $TRUMP – a shitcoin. Believe it or not, "shitcoin" is a technical term in the crypto community (any coin other than Bitcoin is called a shitcoin by Bitcoin "maximalists", folks who believe Bitcoin is the one and only digital currency). The future sitting president literally issued – I don't want to call it a currency, so I guess shitcoin is the right name – that will at some point decline to zero in value. In other words, he'll fleece his loyal followers who purchase $TRUMP of billions of dollars.

I previously referenced both reputational capital and soft power. These types of acts by a sitting president subtract from both.

What are your thoughts on European defense companies?

NATO was founded in 1949 by the US and Europe, four years after the end of WWII. The idea behind the alliance was simple – you attack one member country, you attack them all. Over the last fifty years, American presidents (starting with Nixon) have complained that Europe is not spending enough money on defense.

Americans have always outspent Europe on defense, but to be fair, we have a currency advantage. Our military might, combined with a strong political system and a very large and robust economy, elevated our currency to reserve status. Being the world's reserve currency meant we had constant inflows into the US dollar, allowing us to live beyond our means and not pay the price in skyrocketing rates – and which made it easier to run budget deficits and finance

a bigger military. In other words, we received a return on our defense investment in the form of lower interest rates.

Europe was a different story.

The reasons European countries underspend on defense vary, but share underlying commonalities. After starting two world wars in the past century, Germany (the largest economy in Europe) looked at military armaments the way an alcoholic in AA looks at beer, trying desperately to steer clear of them. France – Europe's third-largest economy – was spending almost one-third of its GDP on social programs, at least 13% more than the US as a percentage of GDP, and conversely only dedicating 1.9% of GDP on defense.

In general, European countries have infused so much socialism and regulation into their economies that their economic growth has lagged behind the US. As a result, their GDP per capita (i.e., average salary) is a third lower than in the US.

In a world where the US became a cradle of innovation and China turned manufacturing into a science, Europe has perfected the art of drafting regulations – and not much else. It is very hard to think of a single startup or newly created company in Europe. I can only think of one – Spotify in Sweden (the exception that proves the rule). Overregulation, high social spending, high energy costs, burdensome taxation, prohibitive labor laws, and a slew of other structural obstacles killed economic growth in Europe, and thus the ability to spend on defense.

Europe has plenty of highly educated and brilliant people. When they come up with startup ideas, they move to the US.

It is politically hard to allocate money to defense spending when economies are stagnating. Since the euro does not enjoy reserve currency status and the EU cannot issue "euro bonds" (though this may change), higher defense expenditures cause interest rates to go up. This is exactly what happened in March when European countries announced that they'd be spending more on defense – their long-term rates jumped.

This defense-spending money could have come from cutting other expenses (i.e., social programs), running larger deficits, or raising taxes. Of course, Europe had another choice – doing what seems to be the impossible: cutting regulations (maybe even taxes), loosening restrictive labor laws, and growing the economy by making their environment business-friendly.

Over the last quarter of a century, Europe has underinvested in defense by several trillion dollars. According to the NATO charter, Europe was supposed to spend 2% of GDP on defense, but it has spent about 1.4% – a gap of about $120 billion a year (in today's dollars).

Most importantly, there seemed to be little need or urgency. The Cold War was over. The Soviet Union had fallen. Russia was in shambles, and Eastern and Western Europe were forging economic and political ties. There were no immediate threats. Consequently, Europe cut defense spending and went about collecting its peace dividend. And of course it was protected by its

most powerful friend and NATO partner, the United States of America, which spent more on defense than the rest of the world combined.

Then, in 2022, the unthinkable happened: a territorial war in Europe. Russia invaded Ukraine, and Europe found itself in an uncomfortable situation: it wanted to help Ukraine but could not.

This excerpt from an interview with Ukraine's ex-foreign minister Dmytro Kuleba captures this harsh reality perfectly:

> When the war started and I realized that the best way I can help my country as foreign minister is not to negotiate with the enemy, because it didn't make sense to negotiate with them, but to negotiate weapons for Ukraine….
>
> It got really scary when I realized that there is very little to negotiate because Europe has proudly positioned itself as the state of the art, of cutting-edge military technologies. The problem is that these technologies existed in the quantities necessary for arms exhibitions taking place simultaneously in different parts of the world. That was it. That was the scariest moment – when you realized how quickly warehouses will run out of reserves because they were not replenished for decades.

Europe had armies but only showroom weapons. Germany quite literally did not have a rifle and ammunition for each of its soldiers. In other words, it was going to defend itself with bow and arrows against Russia – whose army was the largest in Europe.

(Side note: Think about this next time you hear Putin claim that the invasion of Ukraine was to stop a NATO invasion. Europe simply did not have the weapons to pose a threat to Russia).

Russia invading Ukraine was a wake-up call for Europe (sort of). European governments increased their defense spending in large part to help Ukraine. However, the increase came from a very small base. While the US was spending 3% of GDP on defense, Germany went from 1.2% to 1.9%, and the UK went from 2.2% to a whopping 2.3%. Most of Europe clearly was not concerned about defending itself against the still-low probability of a Russian invasion. After all, it was protected by the US.

On the other side of the pond, the US found itself in its own pickle. It had run up $36 trillion of debt, with interest payments that became larger than its defense spending. Russia is far and away a bigger threat to Europe than to the US – we are protected by two huge oceans.

Also, the US had a new and, in many ways, a stronger rival – China. Over the last three decades, the US industrial base has been shipped to China. The Chinese shipbuilding industry has a 200 times greater production capacity than the US's. China's navy surpasses ours in ship count, though not yet in overall capability – but while theirs grows in strength and number, ours continues to shrink.

The essence of the NATO alliance was that all partners would protect each other. In reality, Europe had demilitarized itself over the last three decades. From the US perspective, the issue is

not just about money. If Europe has no military force, then it will be young American men and women who will be dying protecting Parisians from speaking Russian if Putin's tanks roll in. Meanwhile, the war in Ukraine has shown that our European allies don't have the means to come to our rescue if we are attacked.

During his first term President Trump raised the issue of the Europeans not holding up their part of the NATO bargain. In his second term, unencumbered by reelection concerns and emboldened by America's economic dominance over other major powers, his self-described transactional approach led him to question both NATO's value to the US and America's commitment to defend Europe if attacked.

The US and Europe are "the West" – we share similar values and have strong economic ties. However, over the last few months there was a significant shift in this multigenerational relationship. Europeans felt that the US suddenly switched sides and aligned with the enemy when the United States joined Moscow to vote against a UN General Assembly resolution condemning Russia's war against Ukraine. Trump then bypassed European allies and Ukraine by negotiating peace with Russia directly, excluding Europe from the conversation altogether.

Armin Papperger, CEO of Rheinmetall – the largest defense company in Germany and one in which IMA is a shareholder – aptly described the American perspective: "If parents have dinner, the kids sit at another table. Right now, the US is negotiating with Russia, and no Europeans are at the table. It has become clear that Europeans are being treated like kids. If you don't invest, if you aren't strong, you end up being treated accordingly."

This stunned Europeans.

The trust that was built over almost 80 years, while not quite shattered yet, has been significantly cracked in a span of just a few weeks. Whether your friend will come to your defense is not something you want to discover at the last minute. Europe therefore suddenly found itself in an existential need to rearm.

This is a difficult but not insurmountable task. Europe has a population of 400 million people, while Russia's is only 140 million. The European economy is $20 trillion – ten times larger than Russia's $2 trillion. To be sure, Russia has certain advantages – it has been at war for three years, which has weakened its economy but made its military stronger and battle-tested. Russia is also ruled by a dictator who can make decisions fast. Europe, by contrast, is a collection of several dozen democratic countries, each with their own internal politics. Consequently, reaching consensus is a painstakingly slow and difficult process.

But nothing unites these countries and expedites decision-making like the threat of learning Russian – it is a very difficult language.

I know this sounds over the top. I'm sure you're thinking that Russia is not about to invade France. I would have said (and did say) the same thing about Russia invading Ukraine. But Finland, Lithuania, Latvia, Estonia, Poland, Czechoslovakia, and Ukraine have been invaded by Russia (or the Soviet Union) over the last 100 years.

Abraham Maslow, American psychologist, described food, shelter, and safety as fundamental human needs; we cannot focus on anything else unless these needs are satisfied.

Europe no longer feels safe.

Today Europe has the will and the urgency to act. It now needs to find the money. Two-thirds of Germans support increased defense spending – an astonishing figure. Badly scared by hyperinflation a century ago, Germany today is no longer concerned about increasing its debt for defense spending. This point is very important, as Germany previously was the spending hawk in the EU. Germany's new chancellor is working on passing $800 billion in spending on infrastructure and defense, increasing the country's defense budget to 3.5% of GDP (tellingly, German and EU governments want to exclude defense spending in fiscal deficit calculations).

Other European countries are trying to figure out how to raise money. There will be a lot of social programs that will get cut.

We are at the beginning of a significant European defense spending supercycle. It is payback time after decades of underspending. European defense spending is going up – and will go up a lot.

What is even more important is that revenues of European defense companies – for several reasons – will likely outpace headline increases in GDP.

Not all defense spending in the past went for weapons. In fact, the bulk of European defense spending went for paying soldiers, pensions, etc. – pretty much anything other than weapons.

Here is one way to understand the difference in priorities between European and American defense spending. In 2010, Germany spent $43 billion on defense; only $6 billion of that was on weapons. The same year, the US spent $786 billion on defense, out of which $235 billion went for weapons. Even when adjusted for population (the US is four times larger than Germany), Germany would still have spent only one-tenth as much as the US on weapons.

European defense spending went up sharply in 2022, but these countries had to make up for at least a quarter-century of underinvestment. A much greater proportion of new defense spending will go to weapons, outpacing the growth of total defense spending. Additionally, a much greater portion of that spending will go to European companies, at the expense of American defense firms. Let me explain why.

My friend Ben says, "Sometimes little things tell us a lot about big things."

The US co-developed the Trident nuclear weapon with the UK. Lockheed Martin developed the missile, while the UK developed the nuclear warhead. The Trident missiles are not owned outright by the UK but are leased from the US. The US maintains the missiles and stores them in King Bay in Georgia. But now the UK is considering alternative plans, uncertain whether the US is going to honor its lease agreement. It is talking to France about potentially providing a nuclear shield for the UK. This tells you the level of trust America's closest ally has in us.

We think of countries as monoliths, but they are run by people, and when countries have a relationship, these people may experience emotions similar to those of a married couple. When your partner breaks your trust, you start questioning all aspects of the relationship that were based on that trust.

Let me give you another example. In March 2025, at President Trump's direction, the US stopped intelligence sharing with Ukraine. The US also halted software support for the electronic warfare systems of the F-16s operated by Ukrainians. This removed radar jamming capabilities, making F-16s nakedly vulnerable to Russian anti-aircraft missiles.

A good chunk of Lockheed Martin's revenue comes from sales of F-35 planes to European countries. The F-35 is the best plane made today. However, if the US stops software and parts support, it becomes an expensive brick. It is costly to cancel orders that have already been placed, but we have already seen other nations decide not to order F-35s – Portugal was very vocal about it.

We estimate that EU spending on weapons over the next five years (from 2026 to 2030) will exceed $1.4 trillion, which is 130% more than over the previous five years. This estimate is based on defense spending that is 3.0–3.5% of GDP. I can see this figure going to 5%. Historically, about 20% of weapons spending has gone to US contractors, but this percentage will decline significantly in the future.

What is next?

Defense stocks represent a significant part of our portfolio – firmwide about 35% (this percentage is somewhat inflated because of recent price appreciation). We have been adding to our defense stocks opportunistically over the last few years and increased our position as recently as early February.

Now comes the hardest part – sitting on our hands. There is going to be a lot of news flow impacting the price of these companies, driving them up and down. Most defense companies in our portfolio today – with maybe the exception of Huntington Ingalls (HII) and Babcock (BAB in London) – don't look in-your-face cheap. However, this apparent lack of cheapness is a bit deceiving.

Their current and near-term earnings reflect a different geopolitical environment than the one that is emerging. It will take time – a few years – for this process to unfold. Legislation must be passed, social programs cut, funds raised, plans formulated, and orders placed before these changes translate into sales. When this happens, profits will rise, and rise substantially.

The end of the war in Ukraine is mixed news for European defense companies. On one hand, they'll need to send fewer weapons and ammunition to Ukraine. On the other hand, a not-at-war Russia will rearm and become a more dangerous Russia, thus increasing the urgency for Europe to rearm.

We want to prepare you that fluctuations on this side of the portfolio are likely to increase – but please, don't confuse them for increased risk. Our patience is likely to be rewarded in the long term.

Current thoughts on TSLA?

Tesla has a market capitalization as of this writing of $780 billion. It made around $14 billion of profit in 2023 and $7 billion in 2024. A good chunk of profit comes not from selling cars but from regulatory credits. It sold fewer cars in 2024 than in 2023. Unless we see a significant shift change in battery capacity, speed of charging, and improved quality and availability of charging infrastructure, we have reached peak EV penetration (I wrote about this earlier).

However, today Tesla is not trading based on car sales but on future dreams of self-driving robo-taxis, robots, semis, and whatever else Elon dreams up. The car company may be worth $100–180 billion; the rest is what investors are willing to pay for Elon's dreams.

Quick thoughts on each dream:

Self-driving: I would not trust my life or my kids' lives to a car company that only uses cameras. They are passive sensors that have limited range and are easily impacted by bad weather. I've used Tesla self-driving software – it is great most of the time, except when it's not – and then it might kill you or others.

Robo-taxis: They may work in geo-fenced areas, but they pose a huge reputational risk to Tesla. One death and this business is done. That's what happened to Uber's self-driving business, and why Google's Waymo has taken a much more conservative route. It uses radar/lidar and launched the service in geo-fenced areas first.

Semis: They were announced in 2017 and were going to hit the road the next year. They are still not out there. I suspect Elon is waiting for a breakthrough in battery technology.

Robots: Exciting, huge market, but this will be a crowded field.

New competition: There are lots of Chinese EVs invading Europe and the rest of the world. BYD looks like a real competitor.

China looked like a great opportunity for Tesla, but may turn into a liability if the trade war intensifies.

Finally, though at times he seems superhuman, Musk is constrained by the number of hours in the day. As of today he is running Tesla, SpaceX, Twitter (x.com), xAI (the maker of Grok – a ChatGPT competitor), The Boring Company, Neuralink, and oh, yes, DOGE. The EV market is getting more, not less, competitive. Tesla needs an undistracted Musk.

One last thought: folks have been telling me that Tesla declined by 40% off its high. I want to offer this gentle reminder: it is the same price as in November 2024 when President Trump got

elected. Trump was supposed to be a huge tailwind for Tesla, and may still be for the approval of robo-taxis, but so far he has ended up being a huge headwind for Musk's brand.

We live in a very politically charged environment and a divided country. Half of America and the bulk of Europe hates Musk and thus Tesla (though I'm sure they love him in Russia). Anyway you look at it, this is not helping Tesla's brand.

How can we protect the gains we have made, if the market enters a deep bear phase? How do we hedge the portfolio?

I have several answers to this question.

First, we don't own the market. I keep repeating this, but it's important to remember, especially in a recession. The market – the average stock listed in the US – is very expensive, but your portfolio looks nothing like "the market." In fact a good chunk of your portfolio is outside of the US, in markets that are not nearly as expensive as the US.

Second, as our stocks approach fair value, we'll be trimming or selling them. We have done some of that already.

Third, it is impossible to completely hedge out your market exposure economically. We can take large swaths of capital and buy put options, but to reduce short-term volatility we would have to give up a huge amount of return. We are not going to do that.

Fourth, we are going to be opportunistic about limited hedging. Our track record with hedging is mixed: our out-of-the-money puts on indices expired worthless, but our costless UBER collar twice was profitable.

Fifth – and this is the most important point – volatility is not risk. Risk to us is permanent loss of capital. As we analyze and value individual stocks, we look at them as businesses, and we require a margin of safety.

This is not what index fund investors are doing. Over the last fifteen years, index investing has turned into a religion that promises never-ending returns from stocks, no matter how expensive the stock market might be. "Buy the dip" and "never sell" have become this religion's commandments. This faith has received endless reinforcement from stock market appreciation… so far.

Of course, as stock market growth outpaces earnings growth, these dollars invested in stocks buy less and less. But inflows never end. In their defense, investors typically keep doing what worked for them. Most are given a menu of index funds they can buy in their 401k. They check off the box, and then billions of dollars buy the index every month, with no research and no attention paid to how much these dollars buy per unit of earnings and cash flows. The longer this cycle lasts, the higher stocks will climb the cliff from which they will eventually fall.

This is where things get nuanced, and this is where risk becomes volatility, because in the case of downside volatility (nobody looks at price appreciation as risk) there may be a semi-permanent loss of capital – losses or near-zero returns for a decade or two.

“The market” is a somewhat nebulous entity to wrap your hands around. Instead, consider Microsoft, Qualcomm, or Wal-Mart. It took them a decade or longer to return to their 1999 levels. A decade is forever in the stock market, especially when you’re losing money. Only a few investors who bought them in 1999 held on through 10–15 years of negative or no returns before things turned around. This is why I am so glad we don’t own the market.

Do we need to redefine “value” in this era of the US stock market, or should we continue to sit on the sidelines if traditional metrics show equities to be overvalued?

I love this question.

Value only needs to be redefined for those who misdefined it.

What is value investing? It is buying undervalued companies, requiring a margin of safety, taking a long-term time horizon, being an investor (not a speculator), having faith that mispriced assets will eventually be fairly valued, and treating the stock market as your servant.

This last point is very important – not letting the market be your master.

Today the market is at one of the most expensive levels over the last century.

If we just give up and “redefine value” such that we start buying overpriced companies, it might actually work for a while. But when it stops working, the price you pay will be steep. Historically, when investors have bought “the market” (an index fund) at similar or even slightly lower valuations, they received zero to negative returns for a decade or two. I wrote two books on this subject.

We are going to continue to aim to be the master of the stock market and not its servant. When you say “sitting on the sidelines,” it implies that we are trying to time the market and the economy. We don’t do that, because it is impossible to incorporate that into a repeatable process. Analyzing and valuing companies, however, can be structured into a repeatable process. Even a crazily overvalued market has some undervalued gems, though they are harder to find and fewer in number. Additionally, we are looking for stocks globally, increasing our opportunity set and thus hopefully reducing the time it takes to become fully invested.

What was the biggest surprise in 2024?

I knew that Europe had underinvested in defense; I just didn’t realize just how much. This gave us confidence to increase our position in European defense companies.

What was the biggest change/improvement to IMA's investment process in 2024?

Selling. I've been thinking a lot about my past mistakes. Most of them had commitment bias – a certain amount of pride and ego trapped in my investments. This will continue to be an area of focus in the future.

What are the biggest perceived threats to companies in the portfolio in 2025?

Me! I am the biggest risk to the portfolio. In 2024, our results looked like I had an IQ of 80, but in 2025 so far I look as if my IQ is 180. In truth my IQ has not changed. The threat comes if I start thinking and behaving like I can walk on water – then I'll get overconfident and make mistakes.

The last fifteen years of being a value investor was a master class in how to handle pain. I keep telling myself to stick to the process. To keep myself grounded, I go back through the mistakes I have made over the years, trying to figure out what I can learn from them. They are a good reminder that I am not infallible.

It has actually been quite informative self-analyzing my past self. In both extremes of success and failure, I double down on research. We spent a lot of time researching defense companies before they ran up. We have doubled and tripled our research efforts since then.

About risk on a portfolio level: We have been cutting dead weight from the portfolio over the last few years. Our selling has become a bit more proactive. I am sure there is a risk we are missing on the individual stock level, but overall we are very satisfied with the portfolio.

How will a trade war impact our portfolio?

In all honesty, it's very difficult to gauge the full impact because of second- and third-order effects. Also, we have no idea what this trade war will ultimately look like as Trump keeps changing his mind. However, it won't be existential to any of the companies we own.

Tariffs will be immediately mildly inflationary and possibly stagflationary – prices of goods and services will rise, but the quantity of goods sold will decline. Tariffs create uncertainty, which will lead to reduced hiring and capital investment by companies globally, not just in the US. The White House may engineer its own recession out of thin air.

If we have a recession, we'll have a recession. It's not the end of the world.

Why? First, by design, most companies we own aren't cyclical, so demand for their goods won't change much.

Second, a recession may actually benefit some of our companies as they take market share from weaker competitors. Uber is a great example – it emerged as a much stronger company after the pandemic, taking market share from Lyft and other rivals.

Third, recessions are a part of life. They are less fun than economic expansions, especially for those folks who are out of a job and looking for one, but they are the price we pay for economic growth. They are the break the economy needs to take after periods of expansion. Companies need them to evaluate if they employ too many people, if these people are in the right seats, and if they have too much inventory or too many assets. Though this recession would be self-inflicted by the president, the impact would be similar to previous recessions – in the end, it will wind up making strong companies stronger.

How are any AI tools being incorporated into IMA's investment process?

I have been humbled by AI; its rate of improvement is accelerating. It is a truly incredible tool.

Here is one example: I have almost stopped using Google. Google used to be a place where I searched for a specific company's website and looked for answers. AI has now replaced the looking for answers part. When most people Google, they don't usually go past the links on the first page. And then they go only a few pages deep on the sites they stumble onto. AI search goes miles wide and deep and provides comprehensive answers with links.

Going from Google to AI search is like switching from coffee to crack cocaine. Speaking of Google, it has one of the best AI's on the market, but it faces competition from extremely well-funded companies and it is no longer my default option for search.

I am not going to go elaborate on what we are doing with AI (for competitive reasons), but we have definitely been using AI to go deeper and wider into our research. It is almost like we have hired a few more junior analysts.

Are you going to retire or become a full-time writer?

One of the questions I receive is whether I have any plans to retire or become a full-time writer. It is hard to retire from retirement. I've been retired for the last twenty years. I wake up early in the morning. Write for two hours. Drive my 11-year-old, Mia Sarah, to school (the highlight of my day). Then I go to the office and do research. I read, talk to my analyst Max and my friends, and build spreadsheets.

I go for a daily walk in the park for an hour. At the end of the workday I go home for a dinner my wonderful wife has prepared. On Fridays in winter my daughter Hannah (who is a freshman at Denver University) and I go skiing. We leave the house at 6:30 am, ski for two hours, and I'm

at the office by 1 pm. My family, including my kids and their significant others, gathers for Friday night dinner.

At a practical level becoming a full-time writer is out of my reach. I cannot write more than two hours a day. Also, I can only write so much about life, while all the writing I do about investing is based on "lived" experience.

I am one of the luckiest people in the world. I do what I love and have complete control over my life. I work with wonderful people, spend plenty of time with my loved ones, and travel as much as I want to. I have nothing to retire from. In my next life I want to come back as me (just maybe with more hair?).

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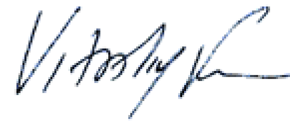
Thank you so much for your confidence in IMA. We'll keep working hard to continue to earn it. If you have any questions for us, or if your personal circumstances change, please reach out to us. We are delighted to help.

Enjoy Life and Prosper,



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