

## The Disciplined Investor Podcast – Guest Interview Summary

Guest: Ed Easterling

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### **CPI Report Discussion**

Andrew and Ed discussed the upcoming CPI report, noting that the previous report caused a significant increase in inflation from 2.4% to 3.3%. They highlighted that the recent 13.3% inflation rate would remain in the index until next March. Andrew expressed concern about the high cost of goods, emphasizing that even with lower percentage increases, prices remain at historic highs. They agreed to discuss these topics further on an upcoming show, with Andrew planning to handle the introduction next week.

### **Market Trends and Growth Factors**

Ed and Andrew discussed market trends and factors driving current market highs. Ed explained that while short-term factors like stimulus, tax returns, and tariff reversals are contributing to market growth, these may not be sustainable long-term. They agreed that investor psychology and the market's resilience are key factors in its rapid recovery from downturns. Ed noted the tendency for forecasts to predict strong earnings growth despite rising inflation reports.

### **Market Cycle and Valuation Discussion**

Ed and Andrew discussed market cycles and valuations. Ed indicated that the market is likely in a late cycle phase based on economic factors, profit margins, and asset valuations. He advised against panic, suggesting that investors should focus on being resilient against potential pullbacks. Ed noted that multiple valuation measures are currently elevated, attributing this to both high earnings growth rates and inflation rates.

### **Economic Inflation and Business Cycles**

Ed discussed the elevated inflation rate and noted that while companies have posted growth rates exceeding economic growth, profit margins are near record levels, which typically indicates a late business cycle rather than an early one. Andrew highlighted significant capital expenditure spending across multiple hundreds of billions of dollars, particularly in technology sectors, which is creating price pressures and market dynamics. The discussion concluded with examples of contrasting market impacts, including Whirlpool's poor

performance due to customer recessionary mindset and Shake Shack's challenges with rising food costs and market competition.

### **Economic Expansion and Semiconductor Cycles**

Ed and Andrew discussed the current economic expansion, noting that it has lasted over 200 months without a traditional recession. Ed explained that while time alone doesn't drive recessions, the prolonged period without one, combined with existing dislocations in areas like AI spending and semiconductor cycles, suggests potential economic challenges ahead. Andrew highlighted the rapid increase in AMD's revenue projections from 17% to 35% over a few months, questioning the sustainability of such growth given the historical cyclical nature of semiconductors.

### **CAPE Ratio Market Valuation Discussion**

Ed and Andrew discussed the CAPE ratio and its use in evaluating market valuations. Ed explained that the CAPE ratio, created by Robert Shiller, uses a 10-year average of earnings to provide a normalized view of valuations, which is a better predictor of longer-term returns rather than short-term fluctuations. Ed noted that current high valuations, with a CAPE of 31 and reported PE over 25, indicate that the next decade is likely to see below-average returns. Andrew questioned whether this prediction could have been made in the past, and Ed confirmed that high valuations have historically led to below-average returns over the following decade.

### **Disciplined Investing and Portfolio Strategies**

Ed discussed the importance of disciplined investing and portfolio structuring to participate more in upside than downside while minimizing losses. He emphasized that controlling losses is crucial, as it takes significantly more to recover from large losses compared to smaller ones. Ed also highlighted the potential over-optimism in current market conditions and the importance of diversification, noting that history may prove these points right in the future. The conversation touched on the proposed changes to IPO requirements by S&P, which could affect the inclusion of unprofitable companies like AI firms in their indices.

### **S&P NASDAQ 100 Inclusion Changes**

Ed and Andrew discussed S&P's decision to accelerate the inclusion timeline for companies like SpaceX in the NASDAQ 100 from 12 to 6 months, waiving requirements around public float and market cap thresholds. They debated the implications of this move, with Ed expressing concerns about reduced transparency and increased concentration risk in the index, while Andrew noted that market cap-weighted indices like the S&P 500 could be considered ultimate trend-following tools due to their construction. The conversation concluded with concerns about potential negative impacts on S&P's reputation as a prudent

index provider, particularly regarding the inclusion of companies like SpaceX with complex share structure issues.

### **Earnings Reporting and Market Conditions**

Ed and Andrew discussed the evolution of earnings reporting methods, with Ed explaining how operating earnings have become more popular while expressing concerns about adding back non-recurring items. They analyzed current market conditions, including elevated valuations and debt levels, with Ed noting that while these don't appear imminent, history suggests risks can emerge suddenly. The conversation concluded with a brief discussion about weather and fishing in Oregon and Alaska.