WALL STREET UNPLUGGED

AUDIO TRANSCRIPT

Frank Curzio: How's it going out there? It's Wednesday, September 20th. I'm Frank Curzio, host of the Wall Street Unplugged Podcast, where I break down the headlines and tell you what's really moving these markets. Just watching CNBC on Tuesday. What a line up of guests, especially in the early hours for covering Trump's speech at the UN. I'm not going to comment about it. I don't want to get into politics.

But first, on Squawk Box, Ray Dalio, the founder of hedge fund giant Bridgewater Capital. It's the best performing hedge fund ever. They have over $160 billion in assets in their management, 160 billion. Insane. The system's mostly based on quantitative analysis, computer metric models, although Dalio doesn't describe it that way and says his firm is more about following certain principles with management and stuff like that, but these guys have literally never had a bad year. Twenty-six years in operations, just three down years, and those years that they were down were not even that bad. Think about that for a minute. Twenty-six years in operation. Must be doing something right. It's incredible.

Then they had on Nelson Peltz, it's around the 9:00 hour. He's the founder of Trian, another multi-billion dollar hedge fund, where he's trying to get a seat on the board of P&G. Usually, he gets seats on boards of smaller companies. Everybody knows how large P&G is. Big fight going on there, back and forth. Peltz, I have to say, brought up a lot of good points, how P&G restructured itself several times over the years which means what? That these restructurings obviously didn't work. If you restructure it once and say, "Okay, cutting costs and new outlook," whatever it is, whatever you're going to do, restructuring, selling off non-core assets, whatever ... They haven't worked, and they've done it a couple times over the last few years. Yet, every time he restructures companies, they do it once, sits on a board, and they do pretty well. Look at Dr. Pepper, Snapple, Wendy's, Heinz. He does have failures just like everybody else, but look at Trian. Peltz's net worth which is over pretty close to two billion dollars while Dalio's only worth 17 billion. That's it. He's only worth $17 billion. He's not in the class of Zuckerberg or Buffet yet. Seventeen billion.

But you look at Peltz, successful investor. Look, if you measure P&G's performance over the past 10 years it's been not good. The stock's up 95%. You say, "Wow. That's great." But again, you want to compare it to what? Because when you compare it to the consumer staples, ETFs on average, they're up 170%, almost double. The direct peers for Proctor and Gamble, these guys are up over 200% in the same time frame. Peltz has a great point. His average stay on the board for him, believe it or not, is seven years. After that period, those companies he's on the board, outperform the S&P 500 by 8%. Now these guys were great. Awesome interviews on CNBC, but here's where the media really screws you, or should I say misleads individual investors which is such a shame.

Let's start with the headlines on the CNBC website. You have Ray Dalio who just wrote an amazing book that's why he was on, that's why institutional investor and everything else which was on a couple weeks ago he talked about. They really went into details on this where he's talking about his successes and failures, how his firm has a unique operation structure, not accounting wise. They actually have meetings with their top employees all the time, and they sit in a chair and other executives highlight this person's biggest weaknesses. Even himself, he has other executives do this and even other employees. Pretty crazy when you think about it, right? I'm trying to think about it and I can't even say it. I'm thinking about sitting in a chair and having my employees telling me all the things I'm terrible at. Because when you look at executives they have egos the size of, you fill in the blank. It's gotta be really difficult to do.

But he mostly talked about principles that are important to Bridgewater that you're not gonna find any place else. You're saying, "Why aren't they found any place else?" Well, think for yourself, which you really can, especially a lot of sell side firms. They cover something, here's the outlook, here's what we think the economy is, the whole company thinks that way. Things like most of what you see and hear, or what you see, or others do is basically out-modeled all wrong. If you're reading about it, it's already factored in, it's probably wrong, you gotta adjust it. Don't follow the old accepted path to learning. Don't simply do what others do. Don't be afraid to speak the unvarnished truth. Don't be afraid to tell others they're wrong even if they're your bosses or chief executives of the company. You can see why few, if any, companies use these principles. I don't really want my employees telling me that, even though it would be really good. "Hey Frank, that stock pick sucked." You're like, "What are you talking about?" It's not easy to do, but when you're looking at performance, it's pretty amazing.

Instead, on CNBC, talking about how this person ran the greatest hedge fund ever and those principles which they talked about a little bit. Dalio also highlighted many mistakes in his book. CNBC has this headline on their website: The World's Largest Hedge Fund says 'Bitcoin is in a bubble.'

I love it. It says Bitcoin is very popular these days. They get a lot of clicks, right? CNBC doing their job. But who doesn't think Bitcoin is in a bubble? What is it? 500 to 4,000 over the past 12 months or so? I mean who doesn't think it's in a bubble? We know bubbles can go much higher, maybe it goes seven, eight, nine. I don't know. I knew the internet was in a bubble in 1999 and it has doubled. It's still in a bubble. He said based on the metrics that he uses, and computer models, whatever, it's in a bubble. Thank you, but that's what they actually put there. He talked about Bitcoin. Even Trump mentioned Bitcoin in his speech at UN about North Korea. Now it needs to be regulated, easily funnel money through terrorist organizations using these ledgers called Blockchain, which we'll get very much in detail in a minute. Gonna be a great podcast. You do a lot of this stuff and easily funnel money in and out, especially to terrorist organizations without anyone knowing. There has to be some kind of regulation, not over regulated, but there has to be some kind of accountability.

Then, with Peltz. CNBC, they did everything they can, even Cramer who I love, did everything that had basically poke the bear, so you have P&G CEO said you're track record is terrible, and they did. They highlighted P&G how ... They didn't even talk about the timeframe. The last couple of days P&G has been destroying Peltz's track record. I don't know Peltz. I take all the information and come up with my own opinion. I think he's brilliant, I don't know if he'd ever be a friend, maybe a little too arrogant for me, great guy, but something I can learn off. I'm gonna get to that in a minute as well.

They question Peltz about it and on the commercial break he had someone print out his performance when they went on break, from his company, and they showed his performance. He said, "This is from my white papers." His performance shows from the time that he's on the board until he leaves, which is seven years, not the like, I don't know what it was ... might've been like a 15-month or 20-month performance, it just took a range of 15 months from 2015 until I think to 2017 P&G, and highlighted how he was on these boards and these companies. They didn't take the whole entire portfolio. They said the consultants who did that at P&G should get fired. He's like, "Here's everything you need to know. This isn't like cherry picking. Here're the details."

Showed from his white papers that his performance when he sits on a board is great. CNBC's headline. "Now it's personal: P&G takes aim at activist investor who is trying to disrupt business." Think about that guys, and what does that do for you as an individual investor? Pretty much nothing, at least those headlines. They're entertaining. CNBC's ratings surged after they had, what was it? Icahn and Ackman fight on their network? Those two guys squared off about Herbalife. "I'm richer than you. I have more money than you. What's $100 million?" I just thought it was funny. Guy from Queens, New York, seeing guys like that fight, it's almost like a slap fight was gonna break out, it was kind of funny. I'm not knocking CNBC about this. They're incentivized to get people to click their stories. That's how they make money.

They're incentivized to get more viewers, right? But I don't care about CNBC. What I do, is I care about you, and you could've learned a ton yesterday listening to Dalio and Peltz, and some of the stuff they said, I was so impressed. I was like, "This is amazing. I gotta go out and buy Dalio's book." I love to read things that I think that are absolutely crazy, and some of the things that he said in terms of his principles I'm like, "Wow, this is insane." But yet you see the results and you're like ... and this is how these guys are, both of them. Data driven. The other guy comes up and says, "I think we should ..." No. Everything is based on data. Here's what the data is telling us to do, here's how we do it. All AI. Every day. Every day, right? Not a day goes by where you don't hear of a major company purchasing an AI firm. Intel just got into that business, you look at Google and the number of transactions, you look at Facebook, all buying AI companies. Data driven companies.

But again, you could've learned a ton yesterday. Two of the smartest guys in the world on TV within an hour of themselves, and again they're incentivized to make money for their investors. And I want to make this very, very clear to you. Dalio, Peltz, I'm sure they're not the nicest people in the world. It's rare to meet a really cool billionaire. I think I've met 12 or 13 billionaires. I've interviewed a few. I've been kind of fortunate. It's about half those guys are really cool, but they're usually cut throat guys. They're not like Buffett who's nice. I'm sure Buffett was like that 20 years ago before he was doing so many interviews. It's hard to meet a billionaire that's not arrogant or somebody would call it an SOB, or whatever, but that's perfectly okay. You could hate the guy, but what's important you could learn a ton from these people.

You got Peltz who made some great points about P&G, who had several restructurings over the past year that never really worked, that's why the performance has significantly lagged its peers. I mean you have Dalio talking about running a company where you go out the door. Question management. If you're in the consensus, then you're probably wrong. This kind of system resulted in one-third of his employees leaving the company, that's what he said, while the ones that stayed were a part of an amazing culture, and they probably couldn't work any place else, and that's what Dalio highlighted because their cultures are just they're so used to Bridgewater and speaking their own mind now. They couldn't really do that in other places, so they're probably gonna stay there forever. Pretty cool stuff.

My point here, be aware of everyone's agenda. If he invested in hedge funds, some are motivated by excess of fees. At Vanguard they charge .00 whatever percent. Hedge funds are like, "Well you only have to pay us 2%," but that 2% is no matter what, but 20% of fees. That's why when I think of these companies they say, "Well, we have 35, 40%. Apollo's returned." Apollo as a private equity fund, they'll say for the last 20 years they've been up an average of 39% our average annual returns and they put before fees, after fees you can just basically compare that to ... They still outperform S&P 500, but they take a lot of money. Be aware of that if you're investing.

If someone's selling you annuity, ask how much they're getting paid. If you invest in a company, are the executives paying themselves a ton of money regardless of what happens? Artificially inflating earnings, buying back stock, well maybe not even big owners of the stock which is something you want to see, right? Make sure their interests are aligned with yours. This way if the whole stock goes up and their incentives are based if the stock goes higher their interests are aligned with yours because you're gonna make money if stock goes higher too.

Okay, research firms. The [Sell Site 00:12:39], Goldman, JP Morgan, Morgan Stanley, their research divisions exist because they generate massive fees for the companies. Maybe these firms are, especially this more sell side firms, they're not gonna provide research on a company unless they get a promise from that company they're covering, not in writing of course, the secret handshake, unless they get that promise that, "Hey, when that company raises money you guys come to us so we can generate those fees."

Financial news letters. Is the editor allowed to invest in their picks before they recommend them to you? Imagine that? Especially if you have a big following. Hey, I cover small stocks, imagine me being able to buy a company with low volume, send it out to my clients, you guys buy it based off whatever target price, it goes up, and I can sell it whenever I want? Be careful of that. They have to disclose that. That's a huge red flag. Something we would never do. Does a newsletter get paid by companies to recommend them? That's an even bigger red flag because they're getting paid by the company which is the only reason they're telling you about it. It's crazy.

When it comes to Curzio Research, here's how I make money: By giving you good stock picks. Period. That's it. If not, what's gonna happen? You're not gonna subscribe to my newsletters. I can tell you, I know Curzio Venture Opportunities subscribers are really happy that a 180% gain three weeks on one of the names, and yesterday another one of our picks announced it was getting acquired. We have about four 50% plus winner in less than a year since we started this newsletter, and a lot of you Curzio Research Advisory stuff getting your shares winners as well. I'm working hard on that which includes a recent pick I sent out, and this was last week, great controversial stock that I think has enormous upside potential and is going to pay you huge, huge dividend considering it's a small company that's projected to generate $30 billion in cash flow from their fixed investments over the next 20 years. Based on the policy, 30% of that they return to the investors, which they have, even more than that the past couple of quarters. They return all of that back to investors in the form of buy backs and dividends.

Got a lot of good recommendations coming, Curzio Research Advisory, I know Curzio Venture Opportunities, we now have a lot of home runs which is where the humbleness comes in. I'm always like, "Be careful," because I'm never want to pat myself on the back because usually that can change, the momentum could change. It happens to the best of us, but for me I'm just really happy to see that subscribers are making money. That you put your trust in me which is really, really cool.

But as individual investors guys, just be careful what you read, who you listen to because CNBC, great job of having these guys on. Two guys who rarely do media, Peltz and Dalio, best of the best, but just make sure you don't get caught up in the hype of a story when you can learn so much from those two interviews, and this was on Tuesday. Again, you can go on and see them, go on to the CNBC website. Definitely worth it. But that's what makes you become a better investor. That's what makes you money.

That's going to allow you to retire comfortably. Simply by realizing the entertainment side, and I admit, I loved watching Icahn fight Ackman on TV, two billionaires fights, like children on TV, pretty exciting, but I use that to recommend Herbalife to you because I thought all the negatives that Ackman highlighted were already reflected in the name. If you couldn't prove Herbalife was a ponzi scheme after three years of data, which he compiled, and witch hunts with regulatory authorities that he pushed on Herbalife, then it wasn't a ponzi scheme. Investors did a great job, made a lot of money on that name. That's how I play it.

Now, I have a great interview for you today with another insider. Brilliant fund manager, also a good friend, Frank Holmes. Frank's the CEO and chief investment officer of US Global Investors which he has been with the company more than 25 years, and under his leadership they've launched several ETFs including JETS, the first airline ETF, and more recently, US Global GO GOLD ETF, which has significantly outperformed almost every major index within the gold industry. They also have several funds targeting gold, all the commodity, stuff like that.

But today? Gonna get into that in a little bit, but more important, talk about crypto-currencies as Frank just took on another big role where he'll become a non-executive chairmen of a company that is a big player in a Blockchain Data center market, not sure if he's gonna give you that name or not, but Frank's been right about crypto-currencies a lot over the past few years. His recent story is getting a lot of buzz, it's titled The Blockchain, because it's called 'The Blockchain,' not just 'Blockchain,' could potentially be as disruptive as Amazon was in the 1990s. In this piece, he basically explains how Jamie Dimon, CEO of JP Morgan, where he says that Bitcoin was dangerous, stupid, fraud. Talking out of both sides of his mouth and it's gonna be a fantastic, fantastic interview, and you know what? Let's get to that interview right now. Frank Holmes, thanks so much for joining us again on the podcast.

Frank Holmes: It's great to be with you all.

Frank Curzio: Well, I tell you what, let's start, we have so much to talk about. Really good stuff. You've been writing your blogs, amazing stories I love to read on Frank Talk, but I want to start with gold. In June on the New York Stock Exchange, you launched your new ETF, which I know a lot about, happened to be there that day, called GO GOLD, symbols G-O-A-U, and when you back tested it, and you shared a lot of this research with me. It outperformed GDX and GDXJ for I want to say decades I believe it was when you back tested it. Since your launch, by no surprise, it's out performed these indexes again. Can you talk about this specific fund and why you're able to outperform the GDX and the GDXJ in both bull and bear markets?

Frank Holmes: Well, what we learned from doing JETS, which is a smart beta, was you have to have a quant approach both in stock picking, and then you have to have the portfolio structure. You have to really understand what are the drivers. We learned a lot from the airlines, JETS Global ETF, and it's done exactly what it's going do, that's follow the model and the back testing the index is just perfect. There's a friction for the fees, but otherwise it's done. Every quarter gets rebalanced, and so GOAU, we even have more experience with GOAU because we've been active gold fund managers for decades and we have that passive knowledge, and then we went on to apply this explicit knowledge.

In the world of stock picking, there're two audiences. They talk about value and growth, but there's also momentum and mean reversion. You want to look at stocks that are the cheapest on a certain metric every quarter because they bounce back to the mean. Some headline news like Santeria can knock it down because of the government wants to take away the mine, but they can't because they can't run it, the stock gets clobbered, and then boom. It always comes back. Then, you'll have something out of South Africa. The headline news can knock the stocks down for this quarter and usually they end up being a great buy.

The other real key factor when creating that balanced portfolio is to look at where there's momentum. The quant world looks at not an NEV or discounted cash flow model, they predominantly look at book value. Is book value rising? Is book value volatile? They compare that to the revenue and the cash flow. What we saw with this is in this sort of quant approach, one of the biggest places for attracting capital has been low volatility, not just in the stock price, because you say, "Well, how do you get low volatility in a gold stock? Because gold's very volatile." What you look for is low volatility in cash flow and revenue per share.

When you go and look at 88 gold stocks around the world and you come back, there's a basket that had this lower volatility. Guess what they are? Royalty companies. When you look at Franco-Nevada when gold when from 1,900 down to 1,100 and bounces back to 1,300, during that decline Newmont and Barrick fell more than two times on a revenue per share than Franco-Nevada did. Franco has the royalties on their assets in Nevada, but Franco-Nevada's revenue per share is not as hurt. There's some detailed analysis that shows that that revenue stream at the top is more significant, so our particular ETF is 30% or the three amigos. That's

Franco-Nevada, Royal Gold, and Silver Wheaton. They rebalance each quarter and they just have this lower volatility.

The other thing that's interesting about them is that they have much higher revenue per employee. When you look at Franco-Nevada, as I mentioned, has the royalties on Barrick's and Newmont's assets in Nevada, the revenue for Newmont is $300,000 of revenue per employee, and for Barrick is about 400,000, but for Franco-Nevada it's 17 million, Frank. Seventeen million.

Frank Curzio: Explain that really quick, Frank because people used to ... mining companies have thousands of employees, but when you look at the royalty companies they could have 10, 15, 20 employees, right?

Frank Holmes: Correct. Twenty-five at Franco-Nevada. They have engineers, metallurgists, financials, lawyers working on these contracts, so with that it's to me it's a superior model. They have less debt than most mining companies, and they've been raising their dividend for the past five years at a faster rate than the S&P 500. Royalty companies are a unique, and they also have what Warren Buffett likes to talk about a moat. Once you get one of these assets and you have the right to those assets it's forever. You find that these are usually valued at 10 years acquisition, but these are absolutely good for 30 years. That's where after the 10th year they make huge cash flow. If you have future discovery, you're the mining company and I have a royalty on your assets, Frankie, if you have a big discovery, I get it free. If you increase your production, I get it free. You have to develop the capital, you have to deploy the capital. They're in a very special sweet spot and that's why I've always loved the royalty companies. They are 30% of GO GOLD, GOAU.

Then the other factors are, as I mentioned, are quant factors and half the portfolio's looking for momentum, momentum in the income statement. They're looking for who the cheapest each quarter, get a bounce and these bounce the most. We went out and showed that if you look at just revenue per share and you just pick the 10 best stocks on revenue per share each quarter, in 2016 those 10 stocks were up 120 some odd percent and the GDX was up 52. It's a real important point. If you look at operating cash flow to enterprise value, if you buy just the cheapest names there they've been sold down relative to the price of their gold, those stocks also have a massive surge. We like to look at what are the cheapest, and then we want to look at who has the best momentum, that is the revenues for the last quarters above four quarters, the operating cash flow for the last quarter is above four quarters.

I thought that that was the genesis that went in to it, and we rigorously back tested it. We'll go down to $200 million in market cap. The majority of the names are North American names. I'm so thrilled that it's doing exactly what it said it would do. The overall arcing reason for it, like what is the number one reason why it's outperforming the GDX and GDXJ, is that they're just indexes. There's no separation from bad management or good management, bad projects or good projects. We separate them, and one of the biggest ways of what I'd call bad management is the value destruction. When we looked at the GDXJ, which had the smaller cap stocks, they've issued shares at a rate of over 25% a year for the past four years. That means it's over 100% shared dilution, so either the price of gold had to go up 25% a year, or the production had to go up 25% a year to offset this massive dilution and guess what? It didn't happen, so when you turn around and focus on those companies that have the best value per share they outperform.

Frank Curzio: Now Frank, how much is it based on quant, which I love about you and I love how you look at the numbers and data. You did mention there's nothing broken down to individual companies where they're looking at the ETFs or maybe the entire fund. How much is fundamental analysis? Like you say, you brought up a great point when it comes to management, but I'll bring up another great point where, and you probably back tested this and know this, but if you look at the royalty companies today, I would say they're in pretty much the best shape that they've ever been considering the majors … they were in so much trouble and spent so much money. They sold off a lot of their great projects, not just percentages of them, to these royalty companies even Sandstorm Gold in there as well, where these guys are in great shape to make a lot of money on some of the best products. These aren't even speculative projects that could develop three, four, 10 years from now. If you look at the portfolios and what these guys did, especially over the past two years, they're in much better standing today. How much is it that you look through those individual companies, even past management like you say, how much is focused that, how much maybe a percentage would be focused on quant?

Frank Holmes: Well, coming back, it's a good question. There's no doubt, when you do quantimental analysis, the quant world goes on even looking at more anomalies and statistical patterns than what we're talking about. I basically said, "Well, what are the fundamental factors that you would normally look at for stock screens?" What does the generalist ... because when the generalist loves gold, these gold stocks far outperformed. When it's just gold funds, they just go with the price of gold. And so what do they look for? The narrative that comes from most of the banks, from gold analysts, is "Well, this is a very cheap discounted valuation, and my NAV says the stock should be trading at $10 and it's trading at seven."

To the world of quants, that's irrelevant. You have to say, "What do they look for?" What we found is that they look for this change in book value. Is the book value rising? Does the book value have big hits? Usually, when book values are very, very cheap on a PE ratio, like a PE model, you look at low price in the book. That usually means there's going to be a really big write down. They prefer looking at momentum in book value rather than trying to be the value approach buyer. That's what we noticed and that's how we added to our models, and coming out with the revenue per share, revenue per employee also. They're unique factors, and it was a lot of work pulling the data from other countries that may not publish that data. How do you get down to dig it in to do that relative analysis?

Frank Curzio: Now how many companies actually do this, Frank? I know you launched the ETFs, you launched JETS and GOAU. That focus on, you're taking an industry and you're separating it to here's the data, here's within these industries what you need to know, here's the fund that creates, and if you back test it it outperforms during good and bad markets. I mean, I'm thinking you could probably do this for almost every single industry whether it's consumer staples, energy, biotech, whatever, and really strip out the fundamental component, so it's not just quant. I mean, it seems that you're on to much more bigger things where this could be applied to a lot of different industries even though I know your focus is on gold and stuff like that.

Frank Holmes: Well, you see, there's been some real flops out there with the smart beta, and that is they just say, "Okay, just buy me the cheapest stocks in this factor," and that's flawed. Because what we found is that you have to dig down and say, "Okay, what does a gold fundamental analyst look at, and then what are the best ratios on income statement or when you look at momentum, a second derivative." That's very important to us is that we want to see not only who's the most revenue per share growth, that's year over year, each quarter over 12 months. That's a momentum factor. A lot of us looked at momentum, say in price action, and so we said, "No, we've got to do this sort of combination."

It requires us much more work, and you need analysts also to be looking at your model. Every quarter we have an independent person run these models, and then we run them ourselves and every quarter, we always have a discussion, this name, why is this name and we don't think that's appropriate," and so it's not just a black box you walk away from it.

I'll give you where I really learned this, was luxury goods. In that space, is that most of the world does not publish same store sales. That's an important factor in that retail business, and they don't show you sales of new stores. They just give you an aggregate number. Now Starbucks will do it, as a prestige product, and other companies in America. When you go global, you can't get the data points, so we had to sit back and say, "Analyze same store sales momentum of Starbucks," for example, and then look at factors that said, "Well, what factor would correlate the highest with same store sales that I could pull out of LVMH or Ferrari that would be competitive that I would have an idea of other same store sales and I could see what their return on capital is?"

The momentum and returns on invested capital allowed me to see how good they were at opening new stores. Will they profit or not, because we had high correlations in looking that as a ratio. We learned this also from JETS doing PRASM, of how PRASM works so well in American but doesn't … that's what they call it's a tool for the revenue per seat mile. For the US airlines that's data was populated and you can turn around and just take that financial number and back test it to look for to give me the cheapest PRASM, give me the momentum in PRASM, give me all these different ratios. We found that it doesn't work so well when you leave North America. It works really well here. You're going to have to have two parts running. It works for picking for the American stocks, but it doesn't pick … so you can't use this one ratio around the world. That's what we learned from the gold space.

The other thing that's really interesting is that this discounted cash flow model. There're some of the banks out there that have a zero discount rate. Others have a 5%, 10% and 15%. In our analysis, what we noticed with the big write downs it's because a lot of times the discount rate for valuing these stocks was too low. If you have a 15% discount rate it means that it's assuming all kinds of risks to the country, to the property, etc., and that valuation is priced better. That's based on this quantitative analysis we're able to go and aggregate.

The other part with this quant world is really, really important is looking at headlines. We, in one of our sites, we noticed this study done years ago in Toronto by an analyst that looked at whatever these headlines, he had five headlines, and whenever they appear in a press release the stock falls from 12% to 50% and stays trending lower for 18 months.

Frank Curzio: What were some of those headlines? Do you remember some of headlines?

Frank Holmes: Property dispute.

Frank Curzio: Slow traffic.

Frank Holmes: Environmental delays.

Frank Curzio: Perfect, yup.

Frank Holmes: Stock exchange corporate governance concerns. Before the lawsuits, just those headlines can trip up the stock and it starts to decline. What you realize today is that the quant world reads that headline in one minute, one minute, and they're out of the position that they're in. you have to be able to identify that narrative.

The other thing that the quant world does, and Frankie, I was really going to share with you is you go on Google and you can download for your Android app a lie detector. It's not perfectly accurate, but it says that it has this 30% accuracy. If you have a bad balance sheet and you're doing a press release and you're doing … they read the words, and then if you do a conference call and they ask questions and your voice they're analyzing your voice. That's what the world quant's doing today. They're trying to see if that's 30% accurate, but your balance sheet's impaired, then sell the stock or go short. That is how our world's changed. I'm really trying to help investors. I'm going to be giving the keynote at the Denver Institutional Mining event coming up next week on the world of quants and how it's impacting stocks and valuations and fund flows.

Frank Curzio: Yeah, it's incredible. I wish you had mentioned that lie detector thing, especially for when … my wife, forget it, be in a lot of trouble with that thing. I didn't even know that's that what they did because my wife is always on this thing anyway. That is interesting how many different things that they do to find out this information. We can go on this. You know what? I will say this because I want to actually give you one more quick …

Frank Holmes: I would give an idea just to help you with that is our analyst, Ralph, a top gun analyst, he took the data and went out to one of these organizations that he was valuing. I forget the exact name, but they ran the voice question, Q&A, and the responses and they came back with highly suspect, highly suspect, highly suspect.

Frank Curzio: Wow.

Frank Holmes: Almost the answer to every question which is so sad because the CEO of GoldCorp is a nice guy, but his voice by these tools is saying he's highly suspect. Well, Gold Corp is one of the worst performers.

Frank Curzio: Wow, that is interesting. That's amazing. Technology coming down the pipeline. I want to try to keep this one short because I want to get to the really great topic which is crypto-currency which you've been writing about a lot which is awesome. Do you have any fears on these quant models where you're looking at Ray Dalio, Bridgewater? He probably doesn't call himself a quant, but it is a quant fund, 160 billion dollars. The amount of money that's going into these funds and the performance we know when something works the whole world wants to get in. The fact that the whole world is getting in and you talk about volatility you don't know if this is because of the reason flash crash has occurred, but does any of this worry you when you look at it on a massive scale where these asset managers are performing so well using these systems compared to everybody else that is everybody jumps into this could we have something that disrupts the markets or that could pornography crash the markets? Is that a fear from someone who's in the industry and does this you're not too worried about it?

Frank Holmes: It's a very good question. Based on 400 years of research on financial crisis the number one factor is leverage. You have once you talk to everyone in the crash of '08 did you know that the brokers were leveraged 33:1? Merrill Lynch, Lehman Brothers, and others.

Frank Curzio: Incredible.

Frank Holmes: You have a bank that's leveraged 8:1, and their investment, their brokerage firm, is leveraged to 33:1 all you need is a 3% move in the underlying portfolios of them and they're wiped out. We go back to the futures market and the crash of '87 that's because they were leveraged 20:1, and all you need is a 5%. When long-term capital went under they were leveraged 100:1.

The real estate debauchery that took place because of the '08 crash is because a lot of people bought homes with 1% down, and they were able to get his massive leverage. When we now apply that concept what would be in the hedge fund world and especially the quant world is that that they're borrowing a lot. What I'm told is that if their borrow rate is tenfold, then they settle that day. If they're fourfold, they'll hold a position for four days. You can have a billion dollar fund and you want to go fight everyday you're turning over 10 billion a day.

Frank Curzio: Wow, that's incredible numbers.

Frank Holmes: That's where we get into this whole issue that they're not long-term investors because there's certainty of their decision is only good for 24 hours or for 48 hours. That's all the math says that some external factor comes in and wipes out that performance. Then they try to leverage that to get those great numbers. That is a big factor that I think at the risk end.

I think the other big real systemic risk is brewing is what happened to GDX and GDXJ where money didn't go into the active gold fund managers. It all went into the GDXJ and the GDXJ all of a sudden woke up and found they're going to own 20 companies more than 20%. Well, that's in violation of getting securities laws that they can take over the whole company. They're not going to do that, and then all of a sudden the five billion that went into GDXJ over 12 months gets blown out in a month. Three billion dollars.

That's just really damaged a lot of those high quality stocks and the junior stocks that were in that portfolio. What happens now is the S&P 500 with Vanguard, Vanguard all they do is sell cheap, cheap is better. They're now showing up in the S&P owning more than 5% of these companies. What happens when they're 20% of these companies? They've turned the voting over to CalPERS because CalPERS controls and creates the ISS, and they do the voting. They're all pro union. What will that do to the allocation of capital? They're two big risks that I see. I think that the ETF risk where it's not smart beta is just an index of names and cheaper is better concept than you're going to run into a concentration of problems if money is not going to active managers.

Frank Curzio: Yeah, it's incredible. Once again, we're talking to Frank Holmes, CEO and chief investment officer of US Global Investors. I could stay on that topic for a very long time. I'm sure the listeners would love it too, but they're going to love even this one as well because everyone's talking about crypto-currency, a sector that has more interest than almost any sector I probably covered since the Internet and the AOL launch making it easy for people to go online.

We've watched Bitcoin, other crypto-currencies, soar in value. People calling it a bubble. I'll just say Bitcoin will go to 50,000.

There's a lot more to just Bitcoin when it comes to this market, right? It's Blockchain technology where you say Blockchain could potentially be as disruptive as Amazon was in the 1990s. you actually wrote that was one of your last blog posts that US Global Investors that Franks talks. Amazing, guys. Read it. Lot of great stuff. Explain what Blockchain is since I know so many of my listeners they heard of Blockchain, but if I had a bet they can't really explain what it is or the potential impact it could have on just about every single industry.

Frank Holmes: It's a challenging concept to really verbally discuss with with him. And I highly recommend they go to YouTube. There're a couple of how Blockchains, there's two minutes. Someone will go on and on and on. Just forget those. Netflix has a great movie on the history of Bitcoin. It's a fantastic movie, and I highly recommend people watch to understand the genesis and how its evolved. There're a couple of video clips that are out there. I Think even he Guardian in the UK have done a great animation short video clip that explains the technology, the concept of the technology and proof, how proof is taking place.

The biggest thing for Bitcoin is that it's limited the numbers of the coins that are going to be out there. Unlike paper money it's unlimited. Two is that there's no central clearing system like MasterCard or Visa or a central bank. It's basically who validates that credit card transaction is through one house, where here the validation of contracts and trade are done by a million people around the world. They all get paid like an ATM machine for processing that trade. For them to process that trade they have to have computer graphic cards because it's a very challenging calculation. It's like the old TV program Get Smart with all the doors you had to unravel. Well, the same thing here. You have to this cryptology. Why it's called that it's a code that's at every transaction a block has embedded on it. You have to be able to unravel it and match it with the other transactions and say, "This is a real trade," and then that block of a trade gets added.

Everyone can see if someone tampered with the trade because a block has been damaged. They can't see what's inside the trade. They could just see that the trade has met all of these protocols. It's done by young people all over the world. That's where Genesis Mining which is the biggest company in the world and I highly recommend your visitors go to YouTube and follow just to Google in there Genesis Mining and YouTubing you'll see they have lots of good video clips showing what they've done in Iceland.

For the people that do this what you have to have is this technology I told you about, this computer graphic card, because you have to process lots of data very quickly, but you need cheap electricity.

Frank Curzio: Talk about that Frank. You led right into the segment. So many people look at Bitcoin, how do I invest in coin base and stuff like that. You're going right into the segment which is perfect. Talk about like people aren't really addressing that I think. Electricity costs, lightning speed Internet connections that you need. It also helps to have cold climates. This is amazing stuff.

Frank Holmes: It is. The fact that when you look around the world where you're going to get this great electrical bill that you can do this? They were able to go to Iceland, and they found that they could get inexpensive electricity. In fact, Genesis Mining consumes more electricity than the aluminum company. I thought that was most interesting. Ross Beatty I believe has been on your program and one of Marin's biggest investments is that whole power, geothermal power, but they're big in Iceland. Ross was saying that he knows Genesis Mining because how much electricity they consume processing Ethereum and Bitcoins.

Frank Curzio: That's incredible.

Frank Holmes: The other part for your listeners is the sort of concept is that there's that no one person can take it down. It's decentralized processing and everyone gets a little reward who does it first. That's what creates this sort of global economic engine. It's peer to peer, and I think that from the other big part is this sort of protocol. What's happening is that they're saying, "Wow, this Blockchain, and then you have Ethereum which is proof of contract we could put insurance on there. We could put your insurance bill, your insurance contract, all the parts of your insurance. We can do back office. We can do stock trading." Can you imagine if you can settle stocks every hour, 24/7?

That's why the New York Stock Exchange is worried that they're going to be uberized. They're going to become irrelevant. They put money along with USA up the street from us San Antonio into a venture capital fund, a VC fund in Silicone Valley, to invest in Coinbase. It's now become a unicorn, this particular exchange. You can go there and open an account and convert your dollars into Bitcoins or Ethereum, and then if you have an account at USAA or Fidelity you can have that like you're having a gold fund, a gold stock. It shows up in your overall total assets everyday what the valuations are.

I think that that's how this business has evolved. What Bitcoin has done it's like the email was to the Internet. The Internet came out in the 90s and really it was people said it was a bad place because there was porn on there and there're other bad things to trade on there, and then what really made it become clean and go straightforward was emails. That's before Google. Remember, Jeeves was there, then Yahoo. Yahoo's almost gone, Jeeves is gone. Whoever thought Google and Facebook would come out to sort of dominate those platforms and LinkedIn.

We were early on this. Bitcoin is early. It's like you're going what five years now? Sorry, more than that, came out in 2008, but it's really started to take off in the past few years that it's now so much publicity that 54% of the world, Frankie, 54% of the world are aware of Bitcoin. They don't know what it does, but they're aware of it. I think that that's an important sort of branding they have globally. There's a scramble.

Jimmy Diamond comes out and says it's a fraud and etc. Well, he's got 50 scientists right now worried and writing code to do in the Blockchain crypto-currency world before they get uberized because they make a lot of money. I'll give you a statistic that blew me away. Economists said that in 2014 that the money-centered banks around the world charged fees of 1.7 trillion dollars, 2% of the global GDP.

Frank Curzio: Wow.

Frank Holmes: They're out to protect that from being uberized.

Frank Curzio: It is amazing. I guess that leads to the next question. I didn't know. That is an insane stat. I didn't know it was one point whatever trillion that's just on the fees. You have the government here where they're going to resist a lot of stuff that disrupts it and you write about this, the status quo, which is what do we see? China restrict new initial coin offerings. You say probably a few more countries are going to attempt to do the same thing.

How do you see this market playing out considering you look at Bitcoin, Ethereum, crypto-currencies had a monster year where more than two billion has already been raised in ICO so far in 2017. Again, this is stats that I'm pulling from your research as well. It's 150 billion in crypto-currencies that's in circulation around the world. Bitcoin itself at its high which is not far off a tie worth around 80 billion which is close to the 90 billion dollars invested in all the gold ETFs combined. Where do you see where we do need regulation? You don't want terrorist organizations, you're not being able to track that money. When people say regulation they cringe up because they think the whole industry, but like you said when you look at the Internet it worked out. How does this work out? Is this something that you thought about as someone who's investing in this industry?

Frank Holmes: I'm always a believer that sporting events need referees because people will cheat to win, so referees are there to make sure it's a fair game. What's happening in this ICO market it's just bizarre what people create and it's just so easy to cheat and defraud. I think there's no doubt they need regulation there.

The hard part for the regulators they're so consumed with AML, anti-money laundering laws, that they're making it black and white. I think that that's the problem that they have to stop that and try to say, "Okay, let's create some crowd funding concepts that there has to be some type of data collection, but we want to do like it's crowd funding."

That shocked me. I was looking at the local San Antonio angel group and I went out and invited ... and I was so surprised how easy it was to make one-page documents, put a presentation up on the board, lawyers, accountants and lots of entrepreneurs were there and three companies were bidding and they raised 10 million dollars.

Frank Curzio: Geez.

Frank Holmes: There're more legal agreements after you agreed to participate in the round. To me, it was so easy. You just can't do that with FINRA and the FCC today for any fund. That bifurcation I could see where people are hungry to invest and they want the opportunity, but it's just the cost and the process of getting in to take a look at something is really just too high.

What shocked me about the ICO market in this research I've been doing is I said, "Where did all this information come from? Where did the people learn," and then I find out from TED Talks. TED Talks have two million downloads a day from 180 countries download two million interviews, 18-minute interviews a day are watched. Mind boggling.

Frank Curzio: Yeah, it's wild.

Frank Holmes: Guess what? It's all over, all over the world, Blockchain, Bitcoin, Ethereum, what it means. You've had this sort of crowd funding that's taking place and the crowd funding was slow to get traction here, but it's showing up in the angel investing world and it's showing up in this ICO world because money's being printed, people want to be involved, people want to invest, and the worst part is to make it so prohibitive because it creates these pools where there's going to problems. I think that ICOs should have to register.

They should be not to the quality of the Sarbanes Oxley or things like that, but it is something that has to be put in there to make sure the disclosure because the keywords like full, true, plain and timely disclosure or something, you don't get with ICOs. You do not get full. You do not get true. You do not get plain. You do not get timely disclosure. That is paramount to build trust in the industry.

Frank Curzio: I wonder how long this is going to take. If you think about, because I asked you a question earlier and it was amazing that when I said, "Blockchain explain it." You said, "It's so difficult to explain." I'm the same way where I've been doing this for over 20 years and I'm able to pick up industries and different styles if investing. For some reason I just have a knack for that. Don't ask me to fix your car. I can never do it. When I just comes to that I don't know why I get it, but I get it.

This is the one industry I have to say almost in my entire career where every time I'm researching it I learn something new about it and it's another industry it's going to impact. It just opens up so many doors that for me I'm like I just can't grasp it. My question to you is when it comes to regulations just like the Internet I feel like it took a while for them to understand it. Maybe it's just like Facebook and Google, right? They track everything everyone does even though 90% of the people have no idea. They'll figure that out one day maybe to regulate that a little bit more, but does that mean we may not see regulation down the line or maybe they could over regulate because of guys us who follow the markets are having trouble, and I'm not saying we're having trouble understanding it, but even describing it and stuff like, imagine people who are not in this industry, especially regulators who are usually last to know this may take a long time to regulate. Don't You think?

Frank Holmes: Yeah. Well, they're so consumed with AML, anti-money laundering law, that they're missing this whole space. The crowd funding is so big and it's not just done here. What the Chinese did was they said, "No more new ICOs because it's out of control." They didn't say stop Bitcoin or stop Ethereum. That was all the rumors, no. They said these new ICOs are out of control.

One of the things that made Bitcoin and Ethereum take off this year was a consortium of banks in South Korea and Japan embraced using the coins. Now when you get all these problems in North Korea there's another methodology is not only is it good for gold, that sort of fear trade, it's also very good for crypto-currency for moving money. I think that that's been a more significant factor in Asia. I found out there're only two countries that have real white papers as how they define crypto-currency and one is Switzerland, and so the Zug which is outside of Zurich has become the Silicone Valley of the world for these foundations and Singapore. Both of them have written papers on how they view what they think of these sort of crypto-currencies.

Frank Curzio: That definitely makes sense. I guess we'll end with this, Frank, where would you look to invest in the industry? You brought up different areas already, but is it ICOs as investors? Because any of those investors who want to get into this industry is ICOs where ... of course, you have to read the prospectus fine print where some of themselves insiders are allowed to sell pretty much one week right after the ICO which is terrible. Is it the data mining companies like you talked about, or it is Ethereum or Bitcoin? What are some of the areas that you would look?

Frank Holmes: If you're going to play the Bitcoin you want to try to play the Bitcoin world, but you don't want to play it by buying a closed in fund that's over-the-counter. You want to look at these Nvidia has been on a tear. Their stock is just like Bitcoin. Why? Because they're selling their graphics cards to both gamers and the processors of coins. You can play this by buying the technology that's the infrastructure. Otherwise, I think that a hive is a great way to play the infrastructure.

Now it's gone to a big market valuation, but it has revenue. It has cash flow. It has less than 10 employees. The Genesis Mining Group own 30% of the company. It has a special contract. We get to buy other assets in Iceland and Sweden. There are very attractive multiples, extremely attractive. I think it bodes well for the opportunity in a hive. Otherwise, you buy the Nvidia.

Frank Curzio: Definitely makes sense. This is the last one because I actually got a couple questions on this most important question here since you are based in San Antonio. They wanted me to ask you since with your quant models and stuff like that the probability of Ezekiel Elliott, is he going to get suspended from those six games? What are your computer systems telling you for fantasy football?

Frank Holmes: I have no opinion on that.

Frank Curzio: Because I know that you are a huge, huge sports fan in San Antonio for the Spurs and stuff like that. I'm sure that when football comes and stuff like that you must have fun with all the algorithms and things like that. Frank, I want to say thanks so much for coming on. I could really had this conversation last for two hours just picking your mind and stuff. I know my listeners really love when you come on because you just really get detailed and you learn something every single time. I really, really appreciate it, bud.

Frank Holmes: Thank you. You're very kind and you're a great interviewer.

Frank Curzio: That sounds great. Frank, thanks again for just coming on, and we'll definitely talk again soon.

Frank Holmes: Thank you. Happy investing you all.

Frank Curzio: All right, guys, great stuff from Frank Holmes. I really love having him on. I always learn something new when I have him on. He's just brilliant. Whenever I'm with him and I meet his team they're a bunch of young investors. He always keeps younger people around him and I guess it makes him feel young. I mean his drive is almost like he's started a new company. He's been at US Global Investors I want to say for 25 years which is incredible.

I love his system of fundamental and quant. He explained a lot of things. It might've been a little difficult when you look at smart beta, if you're looking at some of the metrics he uses, operating cash flow, enterprise value. If you don't understand these concepts you can go on Google, learn about them. Sometimes it gets technical. I love the fact that he dialed it down. I always try to tell my guys, "Remember, we have an audience who are professionals in so many different things any maybe not so much investing," this way we can all get on the same level. Otherwise, if someone's talking about a great idea but they just lose everybody through metrics and stuff like that, then it doesn't really work out. It doesn't make sense. I felt like he did that a lot.

If there're a concepts and things, man, I was writing down and taking notes, just to let you know, when he was talking about the ETFs and Vanguard, how they're getting bigger. You have maybe CalPERS owning 20%. CalPERS is a teacher retirement fund which is monster, right? Huge biggest funds in the world, especially the US, that invests and gives money to different money managers. Under CalPERS if you own a certain amount of an ETF, say Vanguard or whatever, you're going to have those voting rights. If it is CalPERS, you say union based, yeah, they can vote for whatever they want for through, again, the company itself like that. There's a lot of of implications when you think about it as these ETFs and stuff get bigger and bigger and bigger.

It's interesting that some of the things that worry him, same things that worry me, but there was just a lot of great things including royalty companies, much footing than they are today. That's what he's focused on and that's why his fund, GOAU, is outperforming. Those are amazing companies right now that are set up perfectly for gold, especially at this price where they're taking a big piece of the profits of some of the majors who sold off. Why did the majors sell off some of their best properties in the gold industry? Because they were getting killed. A lot of them also almost went bankrupt because they were leveraged, something he talked about, with their firms being leveraged was it 30 something to one during the credit crisis.

You're looking at all this, especially when it comes to gold in these companies, they're going to be generating … they're going to have pieces you could sand storm like a Franco-Nevada. You look at World Gold's is another one I don't know if he mentioned, some of the largest ones in the world right there on the royalty side. Take a look at those companies. Maybe they come in with bad news here or there and you'll see a nice pull back. Might be a good time to invest in these individual names or through his fund, again which is outperforming almost every single index attached to gold.

Really, really great stuff. Let me know what you thought, because again, this pod cast is about you not about me. I could love whoever's on here and you guys, "I'm not too crazy about it." Again, it's about you, right? That's why this pod cast has grown so big. Word of mouth, still not really advertising, but we are going to start and get bigger and bigger and bigger which is really cool. Again, email me what are thought, frank@curzioresearch.com.

On a final note, be sure to check out our new Facebook page at facebook/curzioresearch. You can see my latest pod cast research content, getting video, the whole thing is set up really soon. Talking about weeks away, so I guess we'll be doing a lot of live things. Also, Facebook live videos in the field at conferences talking to colleagues, analysts, so a lot of live videos, lot of great content which is going to be used to introduce so many different people to our services. Again, try to get them as subscribers and clients and that's basically the goal here. If you guys want to check it out, let me know. I'm always welcome to feedback, good or bad. You can do that at frank@curzioresearch.com and send me that feedback, but go check out our Facebook page. You just go to Facebook and search for Curzio Research and you'll definitely get there.

Guys, thank you so much for listening. I'll see you in seven days. Take care.