

**Michael Anderson**  
Chief Investment Officer

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## STRATEGY SPOTLIGHT: AMERICAN EXPRESS

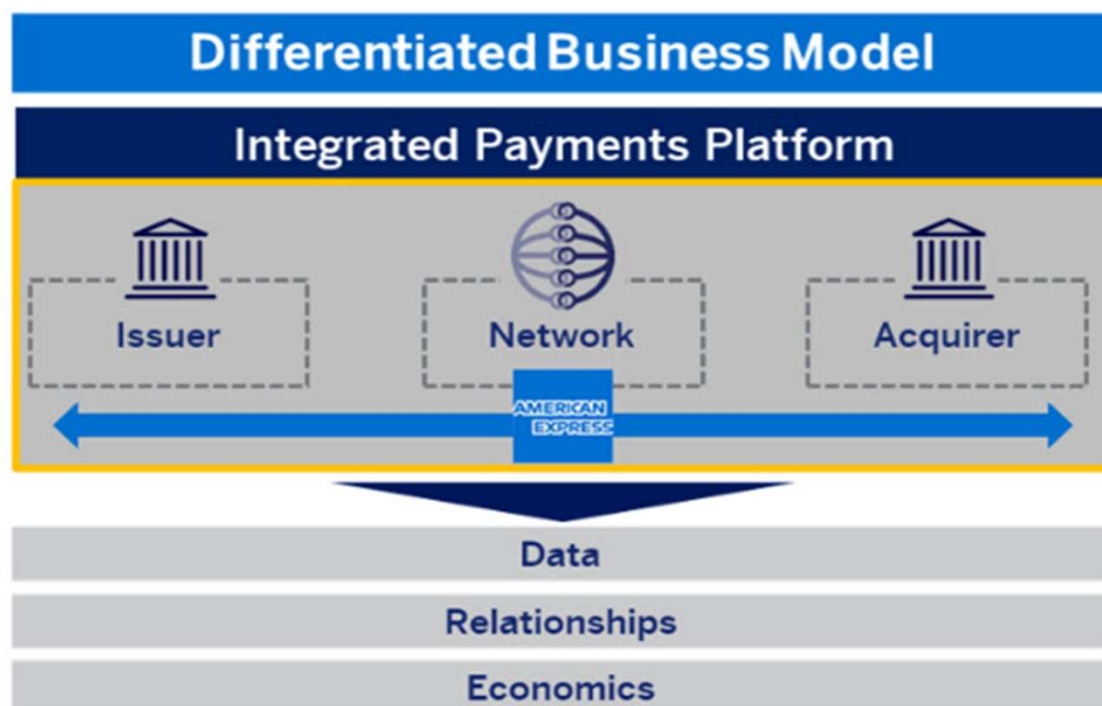
The following is a summary intended to review various elements including; an overview about the company and management, what are its competitive advantages, and price versus estimated intrinsic value.

### BUSINESS OVERVIEW

American Express (Amex) operates a credit card-based payments network. It maintains direct relationships with credit card users (as the card issuer) and with merchants (as the acquirer), creating the American Express network. The business model is “spend-centric” which focuses on generating revenue primarily by driving spend on cards and secondarily by finance charges and fees. Amex connects several partners to the integrated platform primarily in the Travel and Entertainment sectors including Delta and Marriott. The business model is differentiated since it has direct relationships with both the card user and merchant. The below image from its annual report provides an illustration of its business model.

**INTELLIGENT  
INVESTING**  
Hi-Line Capital Management, our intrinsic value-based investing is best viewed over the long-term. It incorporates the need for an in-depth analysis, long-term thinking, risk reduction, proper temperament, and independent thought and conclusions. We believe our investments have an employable competitive edge, and our insight papers, *Intrinsic Value Analysis*, provide a summary of some of the various elements crucial to our analysis and investment thesis.

**ABOUT HI-LINE CAPITAL  
MANAGEMENT**  
Hi-Line Capital Management, LLC (“HLCM”), based in Watertown, SD, provides investment management and advisory services for institutional and individual clients. The firm founded in July 2009, became a registered investment advisor (RIA) with the U.S. Securities and Exchange Commission (“SEC”) in March 2010.



### THE PEOPLE

Stephen Squeri has been CEO since 2018 succeeding long-time leader Ken Chenault, the originator of the spend-centric business model. Squeri’s recent contributions have been pursuing younger users and seeking parity with other networks regarding merchant acceptance which is progressing well.

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**COMPETITIVE ADVANTAGES**

American Express's business model of working with both the card user and merchant creates a closed loop network. This is differentiated from other networks that only issue cards, acquire merchants, or offer a payment network. A closed-loop network and integration of a payment platform allows Amex to analyze information on spending, improves the underwriting of new products, and reduces fraud and charge-offs while providing better targeted marketing methods. A second advantage relates to its ability to intentionally price its network discount rate higher than competitors but then pass the additional revenue to card users in the form of rewards, benefits and perks. Collectively, the network possesses more affluent cardholders resulting in more spend per account with lower write-offs. Amex is the 4<sup>th</sup> largest general purpose card network globally and is well positioned to offer continued value, reputation, and security to users and merchants relative to competing and emerging payment networks.

**PRICE VS INTRINSIC VALUE**

The business economics start with the 100+ million credit card accounts spending \$11,000+ per year resulting in at least \$1.1 trillion flowing through the network. Amex receives 2.25% of every dollar totaling \$25+ billion per year in revenue. Amex distributes nearly 80% of revenue to card users in the form of rewards, benefits and marketing efforts. Amex generates secondary revenue from financing, card fees and other sources for which 80% (average over time) is allocated to salaries, fixed expenses, and loan write-offs. Collectively, Amex generates 20% pre-tax margins largely with a variable expense base and with revenue protected from inflation. Since 2019, the network spending has increased even though 35% of pre-covid spend was based in the travel and entertainment sector, which is still below pre-covid levels. The successful efforts of pursuing younger users, increasing its on-line and global presence and seeking to achieve merchant parity has collectively contributed to more spend despite covid related headwinds. During the last fiscal year, owner's earnings exceeded \$7 billion based on the 20% pretax margin expectations to be achieved over a full business cycle. The current intrinsic value exceeds \$150 billion which is 50% higher than its current market capitalization. Regarding growth, it is expected that revenue will grow at least high single digits with earnings per share increasing double digits based on its willingness and ability to buyback shares outstanding when priced lower than long-term intrinsic value.

**IN CONCLUSION**

Owner's earnings are largely protected from negative inflationary effects and cashflow is counter-cyclical to recessions. Its ability to grow revenue while allocating at least 70% of owner's earnings via dividends and share buybacks adds value over time. Amex continues to operate in a good industry, from an economic perspective, with competitive advantages and priced significantly below estimated intrinsic value.