ADKINS SEALE CAPITAL MANAGEMENT, LLC

Investment Commentary
April 3, 2018

Dear Clients:

"Whoever is careless with the truth in small matters cannot be trusted with important matters" – Albert Einstein

We can only speculate on how Mr. Einstein would evaluate the "truth purveyors" on the internet and through today's 24/7 news feeds, but we would bet his trust factor to be very low. Truth stretching claims to outright scams are unfortunately all too common in our world today where low single digit returns are the norm for marketable investment securities. From the investor's perspective, Einstein's admonition is a reminder of the importance of maintaining a careful and objective posture when considering important investment matters.

In the investment world, fact and opinion are clearly separate concepts but nonetheless linked in the investment decision making process. Known facts include the long term historical investment return data for US stocks, bonds, bills and inflation. This data, some of which is chronicled back to 1870, has been verified and scrutinized by academics and practitioners for the better part of the past fifty years and is generally taken as "gospel." Audited financial statements for issuers of exchange-traded securities are also considered factual despite the infrequent intentional misstatement of a material fact or two. Investors believe/hope the data coming out of various governmental statistical departments is factual, but the complexity of society forces these statisticians to rely rather heavily on approximations and derived results. Nonetheless, we generally consider the forgoing data as truthful and not subject to gross carelessness.

Less certain from a factual perspective are investment opinions. The reliability of investment opinions varies in direct proportion to the certainty associated with future events that impact the basis for an opinion. Expected returns from bonds issued by financially strong borrowers have a high degree of certainty associated with the yield to maturity (aka return). Bond issuers with weak finances offer far less certainty of future returns despite the contractual commitment in the bond indenture. Uncertainty of future investment returns is larger still for company stocks with such uncertainty generally higher for smaller companies and companies with a limited operating history. Formulating opinions on future returns on individual stocks is the most difficult investment exercise as the impacts of known unknowns and unknown unknowns can lead to actual outcomes quite different from the assumptions underlying the opinion. Diversification of risks and incorporating a margin of safety in valuation methodologies are the investor's means for managing uncertainty.

Einstein would almost certainly embrace the truism that "if something is too good to be true, it will not be" or Milton Friedman's admonition that "there is no such thing as a free lunch." If trust emanates from truthfulness, investors should rely most heavily on the facts. Actual results compared to relevant market indices are about as factual as is possible in measuring the effectiveness of investment opinions. Actual results trump opinion all day long. Of course actual results can deviate from opinion over a relatively short period and still not disqualify the original opinion. In this case, the truth will revealed in how the deviation is explained. Does the explanation ring true with the original pitch or does the story keep changing to fit the current narrative? As Mark Twain once said, "if you tell the truth, you don't have to remember anything."

Investment Market Returns as of March 31, 2018

The US stock market experienced a classic reversal in the first quarter of 2018. The US Total Stock Market Index (CRSP) generated a total return of 5.3% in January but finished the quarter with a negative return of -0.6%, including dividends, reflecting the impact of a negative -5.6% result for the February-March period. US small company stocks performed slightly better than large companies by losing less. International developed country stocks performed even more poorly, but stocks of issuers from emerging countries bucked the general trend by posting a positive 1.3%

return for the quarter. Seemingly, the prospect for rising interest rates combined with a growing concern about sustaining economic growth in the face of tighter credit conditions and unconventional rhetoric from the US Executive branch of government may have provoked a rise in the required return on stocks. As we have discussed with you in the past, higher interest rates usually cause equity yields to rise which lead to lower equity price multiples. Common stocks are very long duration instruments and are negatively correlated to longer term interest rates. In contrast to the quarterly result, twelve month returns for the broad US stock and non-US stock markets (FTSE) generated total returns of 13.9% and 16.7%, respectively, both of which remained above long term averages.

Returns on fixed income instruments (aka bonds) in the US unsurprisingly were also negative; the total return on the Bloomberg/Barclays ("BbgBac") US Aggregate Bond Index was negative -1.5% for the quarter, reflecting higher short term yields and wider credit spreads for investment grade corporate bonds. The big surprise for the quarter was the strength in the BbgBac Global Majors exUS Bond Index which recorded a positive total return of 4.7% despite a measly quarterly coupon of around 0.25%. A lower US dollar exchange rate probably accounted for 2.75% of the return but the remainder of the return reflected an apparent decline in yield. For the twelve month period ended March 31. 2018, US bond returns were less than 2%, while international bond returns exceeded 11%, as the falling US dollar added nearly 9.5% to the miniscule coupon from the Global Majors exUS Index. US investors benefit from holding foreign investments when the US dollar is weak.

The results from Alternative Assets were a mixed bag for the quarter and twelve month periods. The hedged equity positions lagged when stocks surged in January 2018, but performed reasonably well in the February-March period, experiencing about half of the downdraft in stocks. US REITs saw a negative return of -7.4% for the quarter as the prospect for higher interest rates was factored into the share prices. Commodity prices were generally flat for the quarter except for a slight rise in gold bullion; surprisingly, the higher price for bullion did not translate into higher prices for mining stocks. For the twelve months ended March 31, 2018, these assets were a drag versus equity assets and breakeven versus fixed income.

Our Look Forward

In our "opinion", investors should be prepared for continued modest, if not negative, returns from both US and international stocks. We believe international stocks have a slightly better outlook due in large part to a generally lower price to earnings multiple. This pricing advantage may be reflective of higher volatility near term, but as Benjamin Graham once said, "In the short term, markets are voting machines; in the longer term, markets are weighing machines." The realization of higher interest rates will also put a ceiling on stock prices, while at the same time bringing about a much needed lift in the reward offered for taking duration risk. These expectations lead us to sell equity assets to meet our clients' liquidity needs or reduce exposures above targeted levels, to maintain lower than average duration and higher than average quality in the fixed income segments, and to use alternatives and cash as funding reservoirs to take advantage of future opportunities.

In Closing

We look forward to visiting with each of you about your investment results and expectations for the future and to make sure your portfolios are aligned with your specific circumstances. We greatly appreciate the opportunity to serve as your investment adviser and pledge our best efforts to meet your expectations.

P. Michael Adkins, CFA
mikeadkins@ascm-llc.com

J. Richard Seale, CFA
dickseale@ascm-llc.com

Jay K. Binderim, CFA
jaybinderim@ascm-llc.com