

The US stock market ended higher for the third quarter, with international markets stabilizing and US strength narrowing. Trade tensions seemed to be easing during the quarter, taking some pressure off international stocks. The S&P 500 index was up +7.71% for the third quarter and +10.55% for 2018 year to date. International markets stabilized, up +0.76% (MSCI EAFE Index – USD) for the quarter but remain down -2.48% for the year. Bond markets continued to face headwinds from rising rates. New headwinds from fiscal stress in Europe helped to keep bond prices flat. The Barclay's Aggregate Bond Index was flat for the quarter (+0.02%) but is down -1.60% for the year. Strong US performance was good for investor portfolios and, where international stocks are included, strong relative performance from active management added value.

Stocks were strong. Incoming economic data revealed that the US economy had strengthened notably in 2018. This backdrop combined and the simultaneous strong earnings reports from health care, industrial, tech, and consumer companies gave investors' confidence in the sustainability of the market advance. Adding to the confidence, the US made significant progress on trade negotiations with North American and European trading partners while the negotiations with the Chinese seemed to be thawing. Investors were able look past increasing interest rates – growth takes care of that. And Growth companies strongly outperformed for the quarter, besting the more conservative Value companies by a wide margin.

As I write this letter, renewed trade tensions in October have triggered another round of downside volatility and a great deal of index gains from Q2 and Q3 have been reversed. So far, Value stocks have held up better than the broad indexes. We have commented on the change evolving in the equity markets for some time now, including a special note early in Q2 (see link to website http://ashdon.com/wp/wp-content/uploads/2018/10/2018_Investment-Implications-when-Index>Returns-are-Concentrated.pdf).

Quoting from that note:

“...we subscribe to both the view of the (changing) macro environment/market structure and the view that the solution isn't avoiding market exposure, but investing in companies that are far away from the "crowded" major market indexes and the "crowded" names that have, so far, dominated those trends in those indexes (think F.A.A.N.G. stocks - Facebook, Apple, Amazon, Netflix, Google/Alphabet). Our investor portfolios are exposed to these companies and have benefited. The F.A.A.N.G.'s are all amazing companies, but they are not forever immune to the economic forces changing consumer preferences, lagged, but progressing regulation (in multiple jurisdictions, no less), and ever evolving technologies introducing new competition.

The duration and extent of a bull market isn't predictable. The timing and depth of a correction isn't predictable. But we are confident that the best chance for investors to meet long term financial goals are by investing with:

- Companies with needed products/services,
- Companies run by capable management teams using prudent leverage, and
- Companies generating consistent profits

We have just returned from an annual trip to three Western financial centers: London, Edinburgh, and New York). We met with over 20 investment professionals during this trip. These professionals work across a broad spectrum of asset classes, geographies and investment styles. In addition to these one-on-one meetings, we attended two investment conferences where we heard presentations from CEO's, industry experts, and forecasters on a wide verity of topics important to investors. The most important takeaway is that our investors' assets are entrusted to men and women with the skills and character we desire. We understand that it is difficult to discern good from bad based on simple measures of investment return, comparison to trends in market indexes and the wide range of *Bull* and *Bear* opinion available in modern media. In meeting after meeting, we found deep dives into portfolios raised our confidence. There are many global companies who are led by hard working, shareholder-friendly CEO's. And there are great minds who are working to take the world forward.

We often focus on the more negative "what if's" to manage risk of loss:

- What if rates rise too fast?
- What if the tax cuts create an unsustainable deficit?
- What if the trade negotiations deteriorate into a trade "cold war"?

The perspective gained from our experience with these diverse professionals helps to keep the other side of "what if" in view:

- What if life-extending health care technology drives a new productivity miracle?
- What if technology advances drive the creation of entirely new economic segments?
- What if growth policy makers engineer a more sustainable global growth trajectory?

For sure, day-to-day, month-to-month and even year-to-year price changes will work to shake this confidence, but we believe that the best chance to meet goals will be to keep the balanced view.

As always, please contact us if you have any questions. Thank you for your confidence.