WINDWARD CAPITAL

Risk Averse Asset Management

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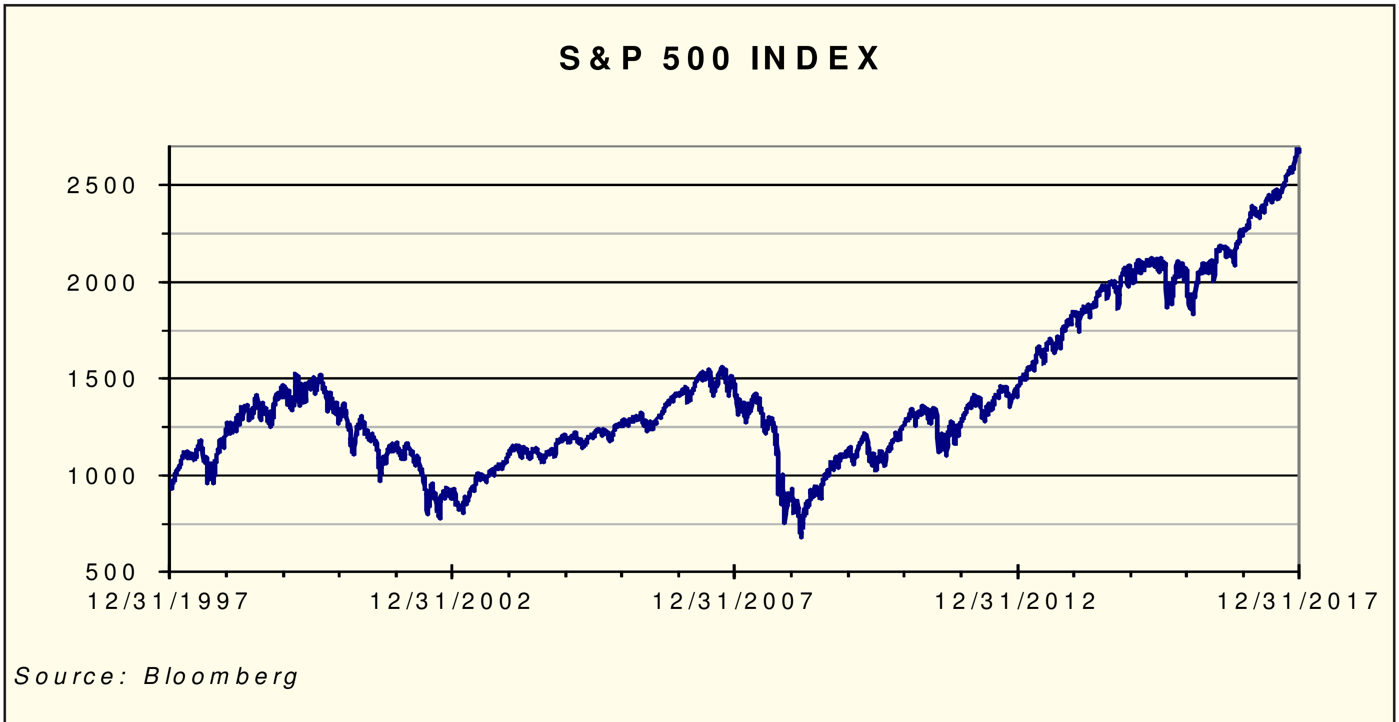

Whataboutism

"Bull markets are born on pessimism, grown on skepticism, mature on optimism, and die on euphoria."

—Sir John Templeton
American-born British Investor, Fund Manager, and Philanthropist

The major U.S. equity market indices continued their advance during the Fourth Quarter of 2017, with the Standard & Poor's 500 Index (S&P 500), Dow Jones Industrial Average (DJIA), and NASDAQ Composite Index (NASDAQ) increasing +6.64%, +10.96%, and +6.57%, respectively, for the period. For 2017 as a whole, the S&P 500, DJIA, and NASDAQ returned +21.82%, +28.11%, and +29.73%, respectively.

The equity market advance appears to be primarily related to accelerations in corporate revenue and earnings growth. For the Fourth Quarter of 2017, year-over-year S&P 500 Revenues and Earnings are expected to increase +6.7% and +10.5%, respectively. As a result, after three years of relatively flat corporate revenue and earnings growth, the S&P 500 is expected to finish 2017 with annual increases of +6.2% and +10.2%, respectively. For 2018, the consensus anticipates further year-over-year increases, with estimates of S&P 500 Revenues and Earnings growth of +5.7% and +13.1%, respectively.

The recent equity market gains have continued into 2018 and, besides reflecting a positive corporate revenue and earnings outlook, also appear to be related to a variety of other factors, including: consistent but moderate economic growth, a weak U.S. Dollar, optimism regarding the positive impact from "tax reform," liquidity effects, reemergence of the "reflation trade," and momentum. Some of these factors necessarily raise concerns regarding market valuation: among other metrics, the forward 12-month S&P 500 Price-to-Earnings (P/E) ratio is currently 20.8x. This P/E ratio is significantly above both the 5-year average of 15.9x and the 10-year average of 14.2x. Although we share this valuation concern and believe that the equity markets may be "overbought" on a technical basis in the short term, we believe that this risk is mitigated in *Windward* portfolios to a large degree by the fact that we are invested in "high quality," dominant, financially-strong, leading companies with best-in-class managements, high incremental returns on invested capital, and business models with sustainable competitive advantages.

As we have discussed before, based upon the (by historical standards) unprecedented degree of uncertainty associated with the Trump administration's ultimate policy agenda/directives (and their domestic and international ramifications), we believe that near-term financial market movements may continue to be unpredictable. Donald Trump's campaign rhetoric was far-reaching, wide-ranging, vague, and, oftentimes, contradictory. From an economic perspective, he has (among other issues) advocated policies of trade protectionism and immigration reduction, individual and corporate income tax cuts, infrastructure investment, and the deregulation of financial services, healthcare, and energy policies. In our opinion, there remains too much uncertainty and lack of details associated with the policies and directives of the Trump administration to be able to confidently make any definitive assertions regarding their impact on the geopolitical and global macroeconomic outlook, much less the financial markets. Until there is further clarity, we can only be confident that the investment environment will continue to exhibit greater uncertainty and increased volatility.

Indeed, what part of Trump's America-first political campaign policy rhetoric will translate into reality and what are the details as to how it will be implemented? Although no one knows, the first year of the Trump Presidency appears inconclusive.

For example, the potential for a positive economic impact from the recently-enacted Trump administration tax policy remains unclear, raising more questions than answers. Some of these questions include:

- ✓ What is the fiscal rationale for incurring over $1+ trillion in unfunded tax cuts that accrue primarily to upper income taxpayers and corporations at a time when the U.S. economy will enter the ninth year of an economic expansion, growth in Gross Domestic Product (GDP) is probably nearing its upper limit, and unemployment is at a 16-year low ("full employment")?

- ✓ What amount of corporate U.S. Dollar shifts will occur, if any, under the offshore Dollar repatriation scheme, and how will corporations utilize those repatriated funds?

- ✓ What effect will the tax bill have on the global currency markets, and will there be any geopolitical ramifications?

- ✓ Will the fiscal impact of the tax bill elicit a response from the U.S. Federal Reserve via a monetary offset policy, and will potentially higher interest rates dampen any positive economic impact from the tax bill?

- ✓ In order to address the increase in the Federal deficit caused by this tax bill, will the current Administration pivot toward cutting spending on welfare, entitlement programs (such as Social Security and Medicare), and other parts of the social safety net? If so, how will this impact U.S. economic growth?

These types of uncertainties surrounding the tax bill—which does not appear to have been crafted in either an intelligent or innovative manner and does not represent true tax "reform"—may, ultimately, limit its broader economic benefits/efficiency.

As investors, we remain politically agnostic in evaluating the economic and corporate impacts of public policy. That is the reason why we would prefer to analyze the actual legislative mandates and policies that are enacted and determine their corporate beneficiaries before considering major changes to the current investments in *Windward*'s portfolio strategies. As a result, in the interim, our strategies may underperform to the upside relative to the market indices over the short-term given the degree to which other market participants make ungrounded assumptions, and/or high-frequency trading and algorithmic "investment" strategies engage in daily financial market trading based upon such things as Trump's "tweets" (as an example). Regardless of the policy initiatives ultimately enacted by the Trump administration (and despite ongoing financial market volatility), we believe that we will, however, continue to be successful in making profitable long-term investments for *Windward*'s portfolio strategies.

As always, we continue to monitor domestic and international political and economic developments as they unfold. As a result, from our long-term perspective, ongoing equity market volatility continues to revolve around numerous global macroeconomic and geopolitical risks that we have elucidated upon in the past. As noted in our previous *Quarterly Review*s, some of these risks include:

- ✓ Central bankers' aggressive monetary policy antics since the 2008 Financial Crisis have only produced subpar global economic growth. Zero interest-rate monetary policy (ZIRP) has borrowed consumption from the future, underscoring the challenge of future economic growth and resulting in a global dearth of demand and surfeit of supply, with concomitant deflationary risks.

- ✓ No one knows the consequences of an extended period of ZIRP. (Indeed, if there were no consequences to ZIRP, interest rates could have been held at zero forever—in the past, as well as into the future.)

- ✓ Monetary policy overkill (in duration and in the level of interest rates) continues to produce adverse consequences of malinvestment and has resulted in the hoarding of cash and reduction in spending by the disadvantaged savings class.

- ✓ The "exclusive prosperity" of the "haves" (versus the "have nots") is politically unstable, leads to more uncertainty (and unexpected outcomes), and will likely have a negative and more volatile impact on social systems, the global macroeconomy, and the financial markets. As a result, global macroeconomic growth becomes uneven and less predictable.

- ✓ The world has never been more "flat" (i.e., more networked and more interconnected). As a result, country-specific actions have the potential to quickly lead to global consequences.

- ✓ The viability of the European Monetary Union (EMU) remains uncertain.

- ✓ The economies of the BRICs (Brazil, Russia, India, and China), previous drivers of global macroeconomic growth, are slowing—in some cases, quite dramatically and uncontrollably.

- ✓ An increase in U.S. interest rates will have significant negative ramifications for those developing world economies that have dramatically increased their U.S. Dollar-denominated debt over the last decade.

- ✓ High-frequency trading, algorithms, and the pervasive use of ETFs, combined with overall financial market illiquidity, is a recipe for increased volatility.

- ✓ Demographically, the aging of the populations of the developed world will have important implications for future demand growth and entitlement costs.

- ✓ Terrorism (including cyber attacks), religious radicalism, and geopolitical instability are increasing and will be more of a threat in the future than in the past.

- ✓ Global political and economic coordination is at an all-time low, and isolationism/protectionism seem likely to be a mainstay in the time ahead.

- ✓ With monetary policy no longer providing extraordinary stimulus to domestic growth, the U.S. needs intelligent, innovative, and aggressive tax and fiscal policies to shoulder the responsibility of catalyzing economic activity. It still remains uncertain what progress, if any, will be made on these fronts.

We closely monitor these, as well as other, risks when managing Windward's portfolios of investments. Since we take a long-term view, we typically do not react to short-term financial market fluctuations driven by near-sighted market participants. However, should there be a change in the global macroeconomic indicators and/or corporate fundamentals that we monitor, we are prepared to take whatever action is necessary to protect our clients' capital.

As you know, *Windward*'s goal is to protect our clients' capital and mitigate market-related risks by investing in specific, high-quality businesses that have long-term, secular growth opportunities. Indeed, we prefer to take a proactive approach to managing risk by investing in specific companies that are taking advantage of the changes in their operating environment to create long-run opportunities for their businesses. Our long-term performance results demonstrate the success of this disciplined investment approach.

Binge and Purge

We do not predict, nor does your *Windward* portfolio own, "the market." We believe that "market timing" is a generally useless exercise—especially given that we are long-term investors who purchase high-quality businesses for our clients' portfolios. Indeed, despite frequent corrections and the occasional "bear market," equity markets generally follow the direction of global macroeconomic growth—which, over the long-run, is, and will continue to be, up. However, the recent geometric advances of the major U.S. equity market indices to historic highs has heightened interest regarding the potential risk of an equity asset bubble—especially given the context of the significant, relatively recent, market corrections experienced during the 2000-2002 and 2007-2009 periods (as well as the earlier, historic, 1929, 1972, and 1987 examples).

Overall, for a variety of reasons that we have discussed with you in the past, the underlying global macroeconomic fundamentals since the Financial Crisis have been relatively disappointing from a historical perspective due to structural issues/limitations (i.e., dearth of demand/surfeit of supply). As a consequence, financial market participants, far from being euphoric, have instead been climbing the proverbial "wall of worry" associated with many past market advances—additionally fueled by unprecedented liquidity delivered by central bank policymaker largesse via ZIRP. Despite these factors, on a cyclical basis economic fundamentals *are* continuing to gradually improve: the global macroeconomy is in sync for the first time in a dozen years, and global profit margins are at a high. For the U.S., this is currently the third-longest economic expansion since 1850: job growth has been persistently strong, inflation remains subdued, the economy is effectively at full employment, and Real GDP is now more than +12% higher than its pre-recession peak. Despite the uncertainty associated with its broader ramifications, a corporate tax cut is also on the way, which, in today's highly monopolistic world, is unlikely to be quickly competed away but will more likely further increase the corporate share of GDP—a positive for equity markets.

In our view, a combination of financial deleveraging and greater investment in fixed capital formation are critical to restoring full health to the world economy. Although these important issues remain unresolved, there is no sign yet that the worldwide cyclical recovery is slowing down. Market attention is now turning to the outlook for activity in 2018. Will the world economy maintain its strong cyclical growth rate, leading to a second year of upward revisions to consensus forecasts for GDP growth in the major economies? Could there be some improvement on the supply side, with fixed investment and productivity growth beginning to recover? Or will the buoyancy of 2017 prove to be the exception, with the major economies slowing towards their lower trend growth rates in the next 12 months--or worse, into recession?

Like many other advanced economies, the U.S. is confronting several secular shifts. These include technological change that is reshaping labor and product markets, low productivity growth, rising skills premia, and an aging population. Even with high per capita income and one of the most flexible, competitive, and innovative economies in the world, the U.S. model appears to be having difficulties adapting to these changes. Most critically, relative to historical performance, growth has been too low and too unequal, resulting in a decline in most measures of living standards compared to other Organisation for Economic Co-operation and Development (OECD) members.

Within this context, we certainly do recognize that this is one of the highest-priced equity markets in U.S. history. In addition to the market valuation metrics that we noted above, the 10-year cyclically-adjusted Shiller P/E (CAPE) for the S&P 500 is currently over 33x—higher than it was on Black Tuesday of October 1929. (The CAPE is defined as price divided by the moving average of ten years of earnings, adjusted for inflation, and is principally used to assess likely future returns from equities over timescales of 10 to 20 years.) However, although we have found that extreme overvaluation plays a significant role in the subsequent "popping" of asset bubbles (it is, in fact, a necessary precondition), the degree of overvaluation and timing of the subsequent bursting are *not* predictable.

In fact, when examining the great investment bubbles of the past, we find that the classic examples are not just characterized by higher-than-average prices. Among other factors, indicators of extremes in emotional "euphoria" appear coincident with, but seem much more important than, valuation. Based upon our analysis of statistical and psychological factors from previous eras, each bubble is very different (so much so that most of the information available is not easily comparable). Therefore, we believe that whether or not the equity markets are currently showing signs of entering the "blow-off" or "melt-up" phase of this very long bull market is, ultimately, a judgment call. In looking for signs of late bubble behavior, then, we have to recognize the fact that no two bubbles, even the classic ones, are the same. They share many signs of investor euphoria (sometimes approaching the "madness of crowds" level), but the combination of psychological and technical indicators has been different each time. The investment historian has to emphasize the bigger picture: In general, are investors clearly "getting carried away"? Is price momentum accelerating? Is the market leadership narrowing? And are at least some of the other early warnings from previous bubbles becoming apparent?

In our view, beyond price momentum acceleration, two other technical factors have been effective warning signs of a late-stage asset bubble: (1) increasing concentration, and (2) unusual outperformance of quality low-beta stocks.

- ✓ "Concentration" is the essence of escalating financial market euphoria. In the late-stage of a market cycle, many buyers are fixating on "winners," with the purchase motive being further stock gains (price momentum), rather than any logic related to long-term intrinsic value. Therefore, as the market soars, attention is increasingly focused on those stocks with the largest earnings and stock price gains, and interest in secondary participants (laggards) declines. This concentration effect usually favors larger companies and is typically measured by the "advance-decline line" (the number of advancing stocks minus the number of declining stocks), whose value *declines* as concentration *increases*.

- ✓ The outperformance of quality low-beta stocks in a rapidly-rising market appears counterintuitive as an asset bubble warning sign but seems to us to be a reflection of the "fear-of-missing-out-on-continued-market-gains" conundrum, whereby asset managers who do not feel comfortable purchasing the momentum-driven (usually speculative) "concentration" stocks instead purchase alternative names that are perceived as higher quality with lower growth

> but still participants in an overly-exuberant economic sector (*Microsoft* versus *Pets.com* in the Technology sector in 2000, for example).

We have already discussed valuation of the current level of the S&P 500, which, in our opinion, appears high. In contrast, the S&P 500 advance-decline line has *risen* along with the index (perhaps helped by the rising percentage of index and ETF purchases), indicating no warning sign with regard to the concentration issue. Quality low-beta stocks, on the other hand, *outperformed* the S&P 500 in 2017 and are signaling a potential warning. With regard to the more difficult-to-measure, qualitative factors, the market experience of 1999 and early 2000 was a classic primer on those signs. We know the current market is not there yet, but we can perhaps see some early signals: increasing vindictiveness toward market "bears," speculative frenzy for cryptocurrencies (Bitcoin, Ethereum, etc.), and the increasingly optimistic tone of media coverage regarding the markets.

Overall, however, Wall Street does not currently appear to be exhibiting signs of true euphoria. Although the pace of the rally has picked up recently, it has not reached wild acceleration. Rather, the financial markets continue to climb a "wall of worry." Technical indicators are mostly well-behaved. What is missing is the "primal scream" of divergence. Market bears list an impressive number of structural stress points under the surface of the economy and the financial system. Perhaps they are correct, as were some early warnings in 1929 about deteriorating fundamentals. Certainly, some of their points will turn out to be at least partially correct. But for an equity asset bubble to form from here, we believe that there needs to be a greater confluence of both quantitative and qualitative factors.

To us, rather than an asset bubble, the greatest risk of an equity market correction continues to revolve around the numerous global macroeconomic and geopolitical risks that we have elucidated upon in our introduction and that we have discussed over the years since the onset of the 2008 Financial Crisis.

Of these, the most imminent risk lies with projected central bank policy actions, which currently imply a bias toward further tightening. Despite a low U.S. unemployment rate, inflation has remained quiescent, confounding central bankers who set in motion a tightening cycle on the expectation of firming prices. This leaves the U.S. Federal Reserve (the Fed) stuck in a quandary: either transitory factors are restraining inflation only temporarily, or inflation expectations have sunk below the Fed's 2% target. If the former is true, the Federal Open Market Committee (FOMC) can continue along the current path of gradual rate hikes. But if the latter is correct, maintaining the current plan risks causing excessive economic slowing and a possible recession. In our experience, global economic expansions (and bull markets) do not die of "old age:" outside of geopolitical conflict or violent energy shocks, they are invariably murdered by central banks fearing inflation.

Inversion Conversion

As expected, Fed officials followed through on an interest-rate increase in December 2017 while modestly raising their forecast for economic growth in 2018. The 7-2 vote for the rate move, the Fed's third in 2017, raises the benchmark lending rate by a quarter percentage point to a target range of 1.25-1.50%. In other moves that tighten monetary conditions, the Fed maintained a projection for three more hikes in the coming year and confirmed that it would step up the monthly pace of shrinking its balance sheet, as scheduled, to $20 billion (from $10 billion) beginning in January 2018.

In our opinion, the following considerations surround the appropriate path of U.S. monetary policy:

1) The U.S. unemployment rate is likely near or below a level consistent with full employment.
2) The U.S. economy currently operates at a pace sufficient to maintain further downward pressure on the unemployment rate.
3) The natural rate of unemployment (and, likewise, potential output) is, however, an unob-

served variable and, as such, estimates of its value are subject to nontrivial amounts of uncertainty.

4) The low wage growth and low inflation of the past year look inconsistent with an economy operating at full employment.
5) The reasons for (4) above may be mismeasurement of the natural rate of unemployment, a change in the inflation-setting mechanism (such as declining inflation expectations), or simply the result of lags in the time between reaching full employment and experiencing an impact on wages and inflation.
6) Given persistently low inflation, not just this year but also since the recession ended, the appropriate course of action is to delay further rate hikes until there is more clarity on the inflation story.
7) Moreover, the tendency of the Fed to err on the side of too high unemployment over too high inflation also argues for caution.
8) If rate hikes are delayed now, it is with the understanding that they may need to be adjusted upward quickly in the future or endure a period of above target inflation in a low unemployment environment.

Within this context lies the backbone of the Fed's monetary policy decisions: essentially, in the Fed's view, the U.S. economy currently operates at or near full employment, the current pace of activity will take the economy well beyond full employment, and, therefore, the economy must slow in order to prevent overheating (i.e., inflation). As a result, the Fed's projected path of an additional three 25 basis-point rate hikes in 2018 sets the stage whereby short-term interest rates could become higher than long-term interest rates—i.e., an inversion of the yield curve.

Historically, the yield curve flattens during monetary tightening cycles, a pattern repeated this cycle. Continued flattening and subesquent inversion is fairly unusual, however. In this cycle, long-term rates have remained relatively stable since the Fed began tightening: a result of a low neutral real interest rate, low inflation expectations, and a low term premium. Meanwhile, short-term rates (directly controlled by the Fed) have moved steadily higher. Assuming long rates remain suppressed, just a handful of short-term rate hikes—as the Fed anticipates—could invert the yield curve.

We doubt that the Fed would have expected the yield curve to flatten to this degree, foreseeing instead more of an *upward shift* of the *entire* yield curve. The failure of such an upward shift to materialize has significant policy implications. First, it suggests that the Fed's longer-run rate projection, or the terminal rate of the hiking cycle, remains too high. In other words, the central bank has less room to move the short end than it currently believes. Failure to recognize this could cause the Fed to overtighten, pushing the U.S. economy into recession. Second, the Fed should be wary of embracing the idea that the stubbornly low long rates reflect easy financial conditions that require central bankers to correct via substantially higher short-term rates. This would become essentially an effort to force longer rates higher and would invite the Fed to invert the yield curve from the short end. Again, this would likely constrict financial conditions and have recessionary implications. Finally, the Fed needs to guard against the possibility of declining inflation expectations—a significantly negative outcome that, as we have discussed in the past, could have severe long-term economic ramifications.

Although it would seem that the relatively weak U.S. inflation data would prompt a stronger reevaluation of current monetary policy (arguing against continued rate hikes), the Fed remains undeterred. For more than two decades, the central bank has erred on the side of higher unemployment over faster inflation. There is no reason to expect this cycle to be different. Some policymakers (such as Chicago Federal Reserve President Charles Evans) believe the Fed should explicitly allow for inflation in excess of 2% in order to shore up expectations. Yet such a suggestion is difficult to reconcile within the Fed's inflation targeting framework, in which the central bank does not attempt to make up for past inflation deficits (that is why central bankers aim to hit the target *from below*, not above). In fact, for years the Fed has undershot its 2% inflation target, risking a sustained drop in inflation expectations that inhibits monetary policy effectiveness in the next economic downturn and erodes their credibility if they should want to later claim that they intend to overshoot the target in the next recession.

Of course, facing an environment of persistently low wage growth and inflation, the Fed could determine that the natural rate of unemployment, or the non-accelerating inflation rate of unemployment (NAIRU), is sharply lower. The reduction of the Fed's estimate of NAIRU in recent years is a step in that direction. Further reductions, if they happen soon, could lessen the Fed's commitment to near-term rate hikes and slow, or stall, the rise in short rates. Still, we tend to believe that the Fed would hesitate to veer from its current path as long as the economy continued to post solid numbers consistent with further declines in the unemployment rate.

The one-two punch that could help steepen the yield curve and avoid inversion would consist of a sharp downward reversion to the Fed's estimate of NAIRU combined with more explicit allowance of above-target inflation. This could lower expectations for rate hikes, and would depress the short end of the yield curve. It would, at the same time, create greater uncertainty over the path of inflation, thus lifting the term premium and, with it, the long-end of the yield curve.

Similarly, if U.S. economic growth unexpectedly slows, market participants might reasonably anticipate the Fed would switch gears and *ease* policy. This would take pressure off the short end of the yield curve, allowing for steepening. Or perhaps the opposite happens: activity accelerates on the back of productivity, boosting the neutral rate, while the Fed retains its current rate path. That could steepen the curve from the long end. Finally, another path to avoiding inversion is if the Fed simply pauses rate hikes after flattening the yield curve.

Each of these scenarios serves to highlight the fluid nature of the variables impacting the current interest rate-setting environment—which is why reading the economic data and setting monetary policy are likely to become more difficult in the years ahead. During a "typical" recession, the policy choice is obvious: cut interest rates. At some point during the recovery, the policy choice again becomes obvious: begin raising rates. But in the aftermath of an economic downturn caused by a global financial crisis—during which unprecedented levels of monetary policy measures were deployed—a subsequent economic recovery with moderate growth, full employment, *and* lack of inflation presents central bank policymakers with special challenges.

A Market of Stocks

Although the equity markets have recently exhibited significant strength, the potential for a correction always remains possible given the risks we have noted above. However, the U.S. economy continues to grow, and we do not foresee a recession in the near term. To us, that means that the long-term upward bias in stock prices should continue. We believe, therefore, that potential market volatility can create an exceptional opportunity to take advantage of the misunderstandings of myopic market participants and purchase high-quality businesses that meet our investment criteria.

Our investment process utilizes a combined top-down/bottom-up approach whereby, based upon our analysis of the components of global macroeconomic GDP, we identify a variety of investment themes, both secular and cyclical, that drive further fundamental analyses of individual businesses that meet our investment criteria. Currently, some of our investment themes include:

- ✓ *Rise of The Rest*
  Globalization and the development of the middle class in emerging markets is a long-term secular trend.

- ✓ *Disruptive Innovation*
  Companies that are disruptive innovators are well positioned to outperform their peers in the current economic environment.

- ✓ *Regulation*
  Financial Services regulation, Healthcare reform, and Climate Change policy are all currently areas of government focus, and the economic sectors within these areas may, therefore, be subject to challenges or opportunities based upon how successful the government is in implementing its programs.

- ✓ *Continued De-leveraging*
  De-leveraging and the shrinking of private and public balance sheets will be a multi-year process that will restrain global macroeconomic growth.

- ✓ *The Great Unwind*
  The eventual "normalization" of monetary policy may result in unforeseen and unintended consequences.

- ✓ *China Rebalancing*
  The rebalancing of China's economy from investment- to consumer-driven has significant global macroeconomic ramifications.

- ✓ *Supply and Demand*
  Global macroeconomic growth remains anemic due to a surfeit of supply and a dearth of demand.

- ✓ *Demographics*
  Demographically, the aging of the populations of the developed, and some developing, economies will have important implications for future demand growth and entitlement costs.

As you know, we do not predict, nor does your *Windward* portfolio own, "the market." Instead, we seek to mitigate market risk and generate excess returns by making long-term investments in individual businesses with the following underlying fundamental characteristics:

- ✓ *Quality*
  Dominant, financially strong, leading companies with best-in-class managements, high incremental returns on invested capital, and business models with sustainable competitive advantages

- ✓ *Growth*
  Companies with predictable and sustainable above-average growth in revenue, earnings, and free cash flow

- ✓ *Value*
  Companies that are undervalued on either an absolute or relative basis, based upon our projections of future cash flow and earnings

Windward's portfolios of individual businesses, with their own company-specific fundamental dynamics, are continuing to thrive and prosper. In the short term, this fact may be obscured by "market action"—which results in highly-correlated security price movements during periods of increased volatility—and/or the negative influences of ETFs, asset allocators, and algorithmic traders—whose focus is on baskets of securities or on stock symbols, not on underlying business model fundamentals. However, financial history has proven, time and again, that, over the long term, investors are ultimately rewarded by being owners of these type of companies.

We have been investing this way for decades, and have successfully navigated a variety of historic market environments.

We believe that the "indices" will become less relevant as time goes on and that successful wealth creation and capital preservation in the years to come will become increasingly dependent upon the identification and ownership of those businesses that, although possibly impacted by exogenous events in the short run, remain relatively immune to these global macroeconomic issues over the long run due to their own underlying growth dynamics.

We remain exceedingly optimistic on the prospects for the individual companies that we own in *Windward* portfolios and encourage you to contact us should you have any questions or concerns.

Sources:
Bank for International Settlements
Bloomberg
Congressional Budget Office
International Monetary Fund
Organisation for Economic Co-Operation and Development
U.S. Bureau of Economic Analysis
U.S. Bureau of Labor Statistics
U.S. Department of the Treasury
U.S. Federal Reserve

HAS YOUR FINANCIAL CONDITION CHANGED?

Portfolio decisions are based on an individual's income requirements, tax bracket, time to retirement, risk tolerance, and other characteristics. If your financial condition has changed, or is about to change, please call us. We strive to prepare a portfolio that meets each investor's objectives, and the more information we have, the better the job we can do. If you have any questions regarding your portfolio, your asset allocation, or any investment within your portfolio, please let us know.

THE FUTURE IS NOW

As you may know, we post a weekly commentary on our website every Friday afternoon. We only mail some of these comments out when markets are particularly unsettled. Please be aware that these notes will continue to be available on-line, and we want to encourage you to sign up to receive a password for access to our secure web-site.

Our website provides the capability for clients to review their portfolios, their year-to-date realized capital gains, and income and expenses. Clients also have access to our weekend market comments. These reports are updated after 8:00pm each Friday, and are available to clients who have requested access. Clients may also request that their accountants and/or attorneys have access to the same information. We hope you will visit us at www.windwardcapital.com.

If you have interest in these capabilities, or if you would like to receive a copy of our Form ADV Part II free of charge, please email Steve Pene at: spene@windwardcapital.com, or call Mr. Pene at our main number: (310) 893-3000.

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