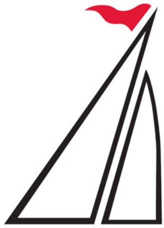
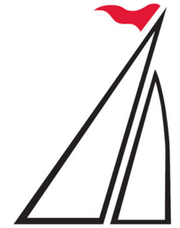


WINDWARD CAPITAL

Risk Averse Asset Management



2022 Fourth Quarter Review

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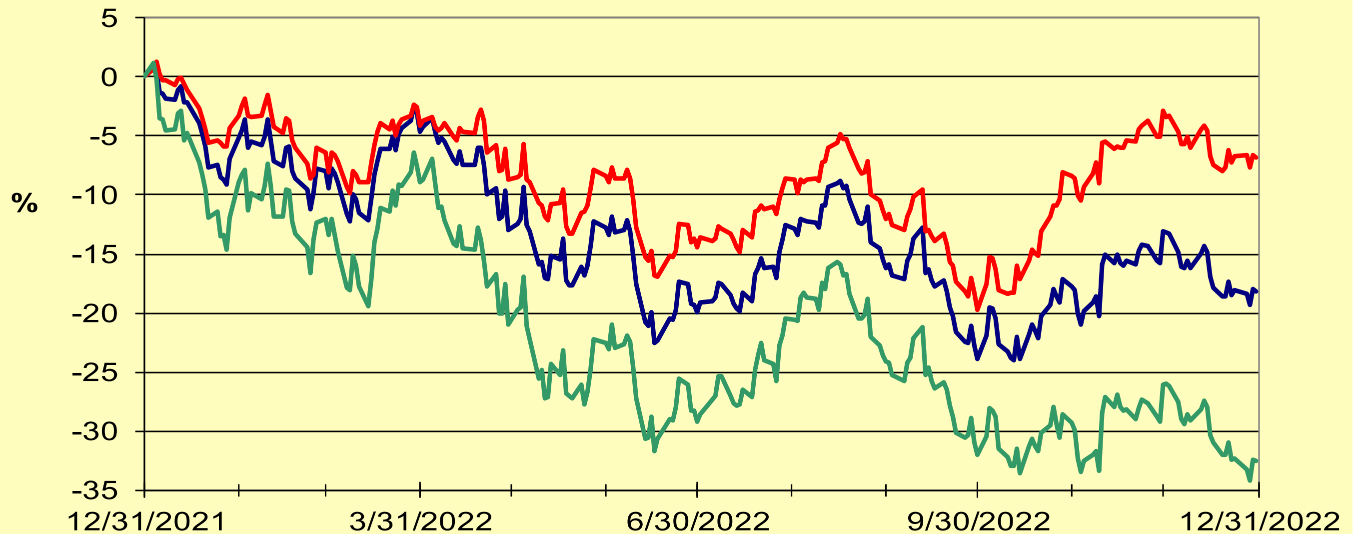

Perspective

"Patience is a conquering virtue."

— *The Canterbury Tales* (1392)
Geoffrey Chaucer (c. 1340s - 1400)
English Poet, Author, and Civil Servant

After reaching new annual lows in mid-October 2022, the major U.S. equity market indices rebounded and ended the Fourth Quarter with the Standard & Poor's 500 Index (S&P 500), Dow Jones Industrial Average (DJIA), and NASDAQ Composite Index (NASDAQ) returning +7.55%, +16.01%, and –0.78%, respectively, for the period. As a result, for 2022 Year-to-Date, the S&P 500, DJIA, and NASDAQ returned –18.13%, –6.86%, and –32.51%, respectively.

We believe that it is important to view the recent equity market declines within a broader context:

After posting three successive years of positive returns from 2019 through 2021—which culminated in a cumulative total range of returns of +66% to +142% during the period—the major U.S. equity market indices corrected in 2022. Despite the recent declines, however, as of December 31, 2022, the major U.S. equity market indices are still anywhere from +55% to +64% higher than December 31, 2018, from +59% to +89% above their 2020 coronavirus pandemic lows, and from +9% to +20% above their pre-pandemic highs, demonstrating significant resilience given the historic—and unprecedented—global events of the last few years.

Among other things, the current ongoing financial market volatility appears to be related to significant uncertainty regarding the impacts of tighter monetary policy, inflation, and geopolitical conflict on the global macroeconomy and the resultant effect that these issues could have on the corporate revenue and earnings outlook. Although the extent and duration of these impacts remain unknowable, based upon recent economic data it seems that at least some of these issues may either be in the process of moderating or have peaked. Until there is greater clarity regarding the ultimate resolution of these uncertainties, however, we believe that the current inter-, and intra-, day financial market volatility may persist. It is important to remember, though, that financial markets usually discount any positive (or, conversely, negative) outcomes before they actually occur.

Fortunately, despite expectations for a near-term tightening of financial conditions and concomitant slowdown in growth, the U.S. economy remains in a relatively strong position and continues to be supported by factors that we have discussed in the past, which include: employment-driven increases in household income, substantial net worth of the household sector, and a high level of savings accumulated during the course of the pandemic.

Predictably, some of the factors providing underlying support to the U.S. economy over the last few years have also had the unintended consequence of creating speculative excesses in specific areas of the financial markets. Recent examples include trading activity in near-bankrupt companies, microcaps, penny stocks, cryptocurrencies, non-fungible tokens (NFTs), special purpose acquisition companies (SPACs), and thematic ETFs, among other financial instruments. Liquidity effects, excessive leverage, and momentum "investing" have combined with high-frequency trading, algorithms, the pervasive use of ETFs, and a variety of social media-driven commission-free retail trading platforms to exacerbate this trend. In addition, economic sectors with generally-suspect long-term business fundamentals (e.g., Energy, Materials, and Financials) have traded in and out of favor based upon an unwinding (via higher yields) of the extraordinary bond market rally of mid-2020, projections of substantive and sustained inflation, and expectations regarding a renewed commodity supercycle.

As we have noted in the past, the ultimate unwinding of these speculative excesses and rotational sector moves may result in increased volatility and, potentially, a near-term market correction. We do not believe, however, that these factors represent a systemic risk to the overall financial markets. In addition, we believe that the risk associated with any resultant financial market volatility is mitigated in *Windward* portfolios—especially over the long run—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.

Historically, periods of excessive ex-ante savings, combined with demand that is too weak to justify investment, cause certain areas of the financial markets to become driven by the speculative rearranging of portfolios rather than by the underlying business fundamentals (like return on capital investment). We are not "traders;" we are investors. As such, it is irrelevant to us whether or not "the market" agrees with us over the short term. For speculators, on the other hand, daily market affirmation remains essential.

Although our strategies may underperform 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 speculative financial market trading, we believe that we will continue to be successful in making profitable long-term investments for *Windward*'s portfolio strategies. In our view, one of the best ways to accumulate wealth over the long term continues to be by investing in high quality businesses—especially during periods of financial market volatility when investors can take advantage of valuation discounts to purchase such businesses "on sale."

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.

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. 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.

Holding Tight

The relatively rapid increase in monetary policy tightening during 2022 was in response to the ongoing persistence of global inflation. By the time many global central bankers gathered at Jackson Hole in August 2022 for their premier annual conference, the mood had shifted decisively towards the greater action that is now being played out around the world. As a result, to date, monetary policymakers from 10 large developed economies have now raised rates by a combined +2,740 basis points in this tightening cycle.

On November 02 and December 14, 2022, the U.S. Federal Reserve (Fed) continued to tighten monetary policy by raising the short-term Federal Funds (Fed Funds) interest rate by +75 and +50 basis points, respectively, to a range of 4.25-4.50%—in line with the projection we made in our *Windward Capital 2022 Third Quarter Review*. As you will recall, in response to sustained inflationary pressures and a strong labor market subsequent to the coronavirus pandemic, the Federal Open Market Committee (FOMC) initiated the current monetary policy tightening cycle by raising the target range for the Fed Funds rate off of the zero lower bound to 0.25-0.50% at its March 2022 meeting. FOMC participants are currently projecting a range of 4.9-5.6% for the Fed Funds rate during 2023—the highest since the 2008 Financial Crisis. In addition, with regard to the Fed's balance sheet, the FOMC ceased net asset purchases in early March 2022 and subsequently began reducing its holdings of U.S. Treasury securities and agency debt and agency mortgage-backed securities in June—currently at a rate of $95 billion per month.

As we have noted in the past, it is important to remember that monetary policy works with long and variable lags. At some point, therefore, as the stance of monetary policy tightens further, it will become appropriate for central banks to slow the pace, while they assesses how their cumulative policy adjustments are affecting their economies and inflation.

Unfortunately, central banks have moved so rapidly that, as they put these rate hikes in place, there really has not been enough time for them to judge what the feedback effects are on the global macroeconomy, and an increasing number of economists think that monetary policymakers are now being excessive in their actions to raise interest rates and that the effect of all of this tightening will be a global recession.

Indeed, based upon real-time forward, rather than lagging, indicators, some economists believe that the Fed has already over-tightened. For example, certain economists (e.g., monetarists) monitor current changes in the global money supply because they believe that such changes affect the price levels of securities, inflation, exchange rates, and the business cycle. Under the monetarist approach, the fact that several "narrow" and "broad" money supply indicators have been contracting for many months suggests that inflation risks are already fading fast and that further monetary policy tightening is unnecessary.

Certainly, a primary consideration for monetary policymakers is judging how responsive economic activity is to the rising level of interest rates. This responsiveness is likely to be dynamic, changing over time and with the state of the economy. In addition to domes-

tic matters, the interplay of global macroeconomic and geopolitical factors must also be noted. Despite these uncertainties, we would not underestimate the Fed's commitment to restoring price stability.

As such, restoring price stability will likely require maintaining a restrictive policy stance for some time, because the historical record cautions strongly against prematurely loosening policy. Although reducing inflation is likely to require a sustained period of below-trend economic growth and softening of labor market conditions, restoring price stability is essential to set the stage for achieving maximum employment and stable prices over the longer run.

Disinflationary

Several recent economic and industry-specific indicators suggest that U.S. inflation may have peaked in the near term as a result of tighter financial conditions, ongoing progress in matching supply/demand imbalances, a moderation in economic growth, and demand destruction, among other factors:

- ✓ Declining global freight rates (as well as other measures, such as excess retail industry inventories) indicate that global supply chain disruptions continue to resolve. The Federal Reserve Bank of New York's Global Supply Chain Pressure Index—which is based upon global transportation cost, delivery time, backlog, and purchased stocks data—has declined –73% from its December 2021 peak, pointing to an easing in global supply chain pressures (even though they remain at historically-high levels).

- ✓ Although crude oil prices have recently bounced somewhat after a –30% decline, many other commodities (e.g., natural gas, copper, aluminum, lumber, cotton, wheat, etc.) still remain approximately –20% to –60% off of their previous Spring/Summer 2022 highs, and several are now trading at 2021 levels.

- ✓ Higher mortgage rates have slowed U.S. home price growth and eased housing industry supply chain shortages/imbalances. Over time, this should contribute to lower Owners' Equivalent Rent (OER), which is a significant component of certain inflation statistics.

- ✓ Despite ongoing strength in U.S. employment, Nominal Average Hourly Earnings growth has moderated on a year-over-year basis, and the rate of change in broad-based measures of overall wages that adjust for compositional changes in the labor force, such as the Employment Cost Index and the Atlanta Fed's Wage Growth Tracker, show no indication of a "wage-price spiral."

Although many components of inflation appear to have peaked, overall inflation remains well above the Fed's +2% longer-run goal: over the 12 months ending in November 2022, total Personal Consumption Expenditures (PCE) prices rose +5.5% (down from the June 2022 peak of +6.8%); excluding the volatile food and energy categories, core PCE prices rose +4.7% over the same period (down from the February 2022 peak of +5.4%). Price pressures remain evident across a broad range of goods and services. Importantly, however, the trend rate of price growth is no longer *accelerating* but is, in fact, *moderating*.

Despite elevated levels of current inflation, longer-term inflation expectations appear to remain well anchored, as reflected in a broad range of surveys of households, businesses, and forecasters, as well as measures from financial markets. This indicates an expectation that the Fed will be successful in its efforts to ultimately control inflation.

In November, Fed Chairman Jerome Powell discussed how the Fed monitors inflation by breaking core inflation into three component categories: (1) core Goods inflation, (2) Housing Services inflation (which measures the rise in the price of all rents and the rise in the rental-equivalent cost of owner-occupied housing, or OER), and (3) inflation in core Services other than Housing (the so-called "supercore" inflation).

- *Goods*
  Core Goods inflation has moved down from very high levels over the course of 2022 as supply chain disruptions and other related supply/demand imbalances have mostly been resolved, post pandemic. If current trends continue, goods prices should begin to exert downward pressure on overall inflation in coming months, in our opinion.

- *Housing Services*
  While Housing Services inflation has risen rapidly, this type of inflation tends to lag other prices around inflation turning points because of the slow rate at which the stock of rental leases turns over. The market rate on *new* leases is therefore a more timely predictor of the direction of overall Housing inflation over the next year or so. Because measures of 12-month inflation in new leases rose significantly during the pandemic but have been falling sharply since about mid-2022, we would expect Housing Services inflation to begin falling sometime during 2023.

- *Services ex Housing*
  As the largest of the three categories (constituting more than half of the core PCE index), this may be the most important category for understanding the future evolution of core inflation. This is a large spending category that covers a wide range of services—from health care and education to activities as varied as travel and recreation, legal services, and hospitality. Because wages make up the largest cost in delivering these services, the labor market holds the key to understanding inflation in this category. We discuss the current inflation issues surrounding the U.S. labor market in further detail in the following section (see "*Laborious*" below).

Over the coming months, the Fed will be looking for compelling evidence that inflation is moving down. We anticipate that the Fed will continue to raise short-term interest rates, and that the pace of those increases will continue to depend on the incoming data and the evolving outlook for the U.S. economy. The Fed's overarching focus is using their monetary policy tools to bring inflation back down to their +2% goal and to keep longer-term inflation expectations well-anchored.

As always, financial markets remain vulnerable to economic and monetary policy uncertainty and have whipsawed recently in an effort to digest both slower growth prospects globally, but also emerging financial stability concerns. While there have been some increased volatility and liquidity strains in financial markets lately, overall we believe markets are operating effectively. Actions by banks and financial regulators in recent years have greatly strengthened the financial system. Banks are well capitalized, and the functioning of the U.S. Treasury, equity, and commodity markets remains orderly.

Given the current state of the U.S. economy—with inflation at a 40-year high and the unemployment rate near record lows—moving expeditiously to a restrictive stance of monetary policy is appropriate, in our opinion. At the same time, monitoring risks and the responsiveness of economic activity to interest rate changes will be important guides in adjusting the pace of that transition.

The resolution of pandemic-induced supply/demand disruptions and the lagging impact of tighter monetary policy should contribute to an easing of inflationary pressures via the resultant moderation in economic growth. In the meantime, a monetary tightening cycle is always fraught with challenges. However, the rationale for removing accommodation is obvious when inflation is high, demand is strong, and the labor market is tight. Under those conditions, an economic "soft landing" is probable but not guaranteed—and the risk of recession still exists. While an outlook of easing supply constraints and moderating demand growth is consistent with inflation stepping down even as the labor market remains strong, less favorable outcomes are certainly possible. In the event high inflation persists while demand turns down and the labor market falters, monetary policymaker resolve may be tested—but should never be doubted.

Laborious

Overall, the U.S. economy continues to slow from the historically high growth rates of 2021, which reflected the reopening of the economy following the pandemic recession. Recent indicators point to modest growth of spending and production. Growth in consumer spending has slowed from 2021's rapid pace, in part reflecting lower real disposable income, tighter financial conditions, and the waning fiscal impact of the American Rescue Plan Act. Activity in the housing sector has weakened significantly, in large part reflecting higher mortgage rates. Higher interest rates and slower output growth also appear to be weighing on business fixed investment, while weaker economic growth abroad is restraining exports. Although moderating, the U.S. economy continues to grow, however, and a recession does not appear imminent: in the Third Quarter of 2022, U.S. Real GDP grew at an annualized rate of +3.2% (compared to +5.7% in 2021), and tracking estimates now suggest that the U.S. economy grew at an above-trend rate in the Fourth Quarter as well.

Despite the slowdown in economic growth, the U.S. labor market has remained extremely tight, with the unemployment rate near record lows, job vacancies near record highs, and wage growth elevated. Indeed, viewed from a historical perspective, the current U.S. labor market situation is unprecedented, with measures of labor demand significantly exceeding measures of labor supply.

Currently, the U.S. unemployment rate is near 50-year lows at 3.5%, and job openings exceed available workers by about 4 million—that is about 1.7 job openings for every person looking for work. Although job openings have fallen by about 1.5 million in 2022, they still remain far higher than at any time before the pandemic, and the overall U.S. labor force participation rate (at 62.3%) remains well below pre-pandemic trends. Although part of this labor supply shortfall is due to slower growth in the working-age population, recent research by Fed economists finds that the participation gap is now mostly due to excess retirements—that is, retirements in excess of what would have been expected from population-aging alone. Unfortunately, the data so far do not suggest that excess retirements are likely to reverse: older workers are still retiring at higher rates, and retirees do not appear to be returning to the labor force in sufficient numbers to meaningfully reduce the total number of excess retirees. Combined with lower birth rates and immigration, the effects of waning labor force participation over the long term could be significant and result in lower potential economic output and a rising dependency ratio, over time.

As we noted previously, trends in U.S. employment data are critical to the Fed in determining its outlook for future monetary policy tightening actions as it relates to core Services ex Housing inflation. From that perspective, although still strong, some of the data contained within the most recent December 2022 monthly employment report are very encouraging:

- ✓ Employment grew by 223,000 jobs for the month

  This is the lowest number in a year and a marked deceleration of the previous eleven months' average of 416,000. Although job gains have been strong—with employment rising by an average of 254,000 jobs per month over the last three months through December 2022 (compared to an average of 372,000 jobs per month over the last three months through September 2022)—these monthly gains have now moderated for the last six months in a row. While it is unclear when the pace of job growth will reach a longer-term sustainable rate that accommodates population growth over time (less than 100,000 per month, by many estimates), it appears likely to continue to slow in the months to come.

- ✓ Wages rose just +0.3% for the month

  This rate of growth was below consensus expectations and lower than the previous two months. In addition, combined nominal wage levels and monthly wage growth rates in October and November were revised lower. Overall, annualized wage growth over the last three months of 2022 was just above +4%—substantially lower than the +6% growth rate in the last three months of 2021. Year-over-year, nominal wage growth declined to +4.6%, the lowest yearly rate since August 2021.

With the full economic impact of the Fed's monetary tightening measures yet to be realized, a continuation of recent trends should lead to further moderation in these employment statistics, in our opinion.

We believe that these December employment statistics should weigh heavily on the Fed's monetary policy decision at its meeting on February 01. Given the deceleration in both top-line employment and wage growth, the Fed may choose to slow its pace of rate hikes next month, perhaps to +25 basis points from the +50 basis points increase in December. Indeed, under this scenario, trends in the jobs and inflation data continue to suggest that we may be approaching the peak in the Fed Funds policy rate.

If, on the other hand, Fed Chairman Powell looks through this data and believes that there is a structural labor shortage (as indicated by the labor participation data), then the Fed may remain on track for additional interest-rate increases as officials seek to lift borrowing costs high enough to soften the labor market further and ease inflation pressures more definitively. In that case, interest rates would have to be held higher for longer, and the risk of an economic recession would increase.

The Fed, through its rhetoric and policy moves, has indicated that it remains committed to holding rates at a restrictive level for an extended period of time to create sustained downward pressure on the labor market. And the guidance in their Summary of Economic Projections with regard to the unemployment rate and real GDP growth in 2023 look very much like they are forecasting a recession as a result. If the current disinflationary trends that we are seeing in the recent economic data persist, the Fed's hawkish reaction function (i.e., commitment to driving the unemployment rate higher than necessary) may become less defensible and could become the key monetary policy concern of 2023.

We continue to monitor the economic data on an ongoing basis.

Letting It Rip

The great Chinese zero-COVID policy experiment has finally—and suddenly—ended.

The government's recent about-face is a sign of its intractable unwillingness to acknowledge policy errors and undertake a course correction until left with no choice. Phasing out zero-COVID is not a strategy to end the pandemic—it is recognition of the policy's long-term ineffectiveness and an attempt to converge China with the rest of the world as soon as possible. As the Chinese population lacks the herd immunity that others have built up in the past three years, it still faces massive waves of infection to catch up. China's economy, which was until recently languishing under severe pressure from restrictions designed to keep the virus at bay, is now grappling with the impact of a sudden reopening and spiraling outbreaks in major cities. Given the high transmissibility of the Omicron variant of the coronavirus, combined with the upcoming mass migration associated with the Chinese Lunar New Year (Spring Festival), we expect that herd immunity will be reached earlier than the consensus anticipates, however. At that point, China's pandemic situation will then resemble that of other countries.

Initially, China's zero-COVID policy had its benefits—especially in holding down the death rate, which now looks likely to rise dramatically higher. But it had major costs as well. The policy is likely to leave long-lasting scars on the economy by setting back the government's intention to rebalance growth. The erratic and draconian lockdowns disrupted all types of economic activity, but hit household consumption and the services sector especially hard. Industrial activity held up reasonably well until recently; but employment growth has lagged behind, and the unemployment rate has risen noticeably.

The Chinese government's long-anticipated retreat from its zero-COVID policy briefly lifted domestic stock markets amid increased optimism about China's growth prospects. Although this policy reversal was welcome news, it still leaves unresolved the major impediments to healthy secular economic growth that

we have discussed in the past.

As we have discussed in detail over the years in previous *Windward Capital Quarterly Reviews*, China's current economic growth model is unsustainable, in our opinion. In our view, the surge in China's debt burden in the past decade, among the fastest in history, is a result of the economy's overdependence on nonproductive investment in property and infrastructure to balance out its structurally-high savings rate and to bridge the gap between genuine growth and the central leadership's GDP growth target. The longer it takes for Beijing to make the decision to rebalance its growth model, the more economically-difficult and politically-disruptive the ultimate adjustment is likely to be.

For decades the system functioned by forcing households to subsidize capital costs which, in turn, benefited manufacturers, local governments, property developers, and banks. Much of the supply side of the economy has been built around these subsidies. That is why it is much easier to *propose* policies that boost the household income share of GDP than it is to actually *implement* those policies: boosting the household share of GDP means reversing the growth model around which the economy was built.

This is a systemic problem. Beijing cannot directly boost household income until is willing to accept the costs to manufacturing of reversing subsidies equal to several percentage points of GDP. So far that remains unlikely. The household share of GDP is not astonishingly low simply because Beijing forgot to boost it. It is low because that is the result of a process by which the household sector has effectively been subsidizing the supply-side of the economy for decades. China, in other words, cannot raise the household share of GDP—and, with it, the consumption share—without reversing a process that has been at the heart of Chinese growth; and this almost certainly means a rapid reduction in growth before the economy is rebalanced. That is why we have to be very skeptical when Beijing proposes that it will rebalance domestic demand while continuing to subsidize manufacturing and investment in order to maintain high growth rates.

Beijing has a long-term plan to shift towards greener and high-tech industries, generate domestic innovation, and become technologically self-reliant. But this will require a better financial system that directs resources to more productive parts of the economy, private enterprise that can operate without fear of arbitrary government intervention, and a strong human capital base of workers proficient in new technologies. Unless China commits to pursuing comprehensive structural reforms and building a more complete market system, its current flaws will become obstacles to achieve the economic dynamism and sustained growth that it desires, in our opinion.

The Long View

Our strategy during the current investment environment remains consistent with the investment strategy that we have followed in the past—essentially: to invest in high-quality businesses at the right valuations and hold them for as long as they remain high-quality businesses. In addition, we continue to believe that the long-term secular investment themes that we have previously identified remain intact.

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

Information Technology regulation, Healthcare reform, Infrastructure investment, 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

Our goal, as always, is to identify those companies and invest in them for your *Windward* portfolio. Our risk averse approach to managing your investments causes us to take a more measured and unemotional view of extremes in bullish or bearish sentiment and find ways to outperform the market with less volatility by focusing on specific companies' fundamentals. Our results over the course of various market cycles demonstrate our success.

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, speculators, 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 types 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:
- Bloomberg
- Congressional Budget Office
- Council of Economic Advisers
- Federal Reserve Banks of Atlanta, New York, and St. Louis
- International Monetary Fund
- Organisation for Economic Co-operation and Development
- Reuters
- U.S. Bureau of Economic Analysis
- U.S. Bureau of Labor Statistics
- U.S. Congress
- 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 website.

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 at 8:00 pm 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 or Form CRS 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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