

The second quarter is now in the rear view mirror, with the S&P 500 climbing to a fraction below its all-time high and the U.S. economy gradually expanding without a corresponding rise in the inflation rate. In spite of the good news, there is a surprising amount of cautionary sentiment in our investment committee meetings here at Peak. Much of it may be that we have been taught for too long to be fearful when everyone else is greedy and to be greedy when everyone is fearful. We are also determined not to risk the hard-won gains of the past eight years in our and our clients' accounts after watching the economy climb out of a deep, self-inflicted and nearly disastrous hole. Commenting on this rebound, Gene Sperling, one of the President's economic advisors, recently said, "If we were back in early 2009—when we were coming to work every morning with clenched stomachs, with the economy losing 800,000 jobs a month and the Dow under 7,000—and someone said that by your last year in office, unemployment would be 5 percent, the deficit would be under 3 percent, AIG would have turned a profit and we made all our money back on the banks, that would've been beyond anybody's wildest expectations."

A look at the long-term picture may explain some of our caution: graphs representing bond yields and returns in the stock market over the past 40 years show a period of simultaneous wealth-building in both asset classes that is historically unprecedented and probably never to be repeated. Since 1976, according to Janus funds' Bill Gross, investment grade bonds have provided a remarkably consistent and steady 7.47% compound return. Stocks have returned 3% more, including dividends, although with much more volatility. Since a safe assumption is that the next forty years will not be as profitable as the last forty in both the stock and bond markets, we investors need to weigh more carefully the amounts of money we are willing to commit now in return for the cash flows we assume we will receive in the future. This also means that simply investing in broad market indices, as people are increasingly doing, may not work well during a lengthy period of flat or rolling returns. The discipline required to pick the right securities and sectors may become all-important, which will be positive for business at Peak, but it will almost certainly necessitate working harder, smarter and with greater focus on the fundamentals.

Luckily for us, we were born in a country that values freedom and the rule of law, one that rewards initiative and innovation. The companies in our Model Portfolio* such as Microsoft, Stryker and Berkshire Hathaway thrive in this environment. The CEO of Xamarin, a business that was recently acquired by Microsoft, said, "Big companies are much more exciting places to be now than they were five or 10 years ago. They've learned to be agile. They've learned to be innovative. They've learned not to take their customers for granted. In many ways, the best big companies have learned the tricks of the startups." This flies in the face of the often-heard lament that working for a large corporation means increased pressure to perform and constant worry about being laid off or replaced by a computer, a robot or a Chinese assembly line. According to outplacement firm Challenger Gray & Christmas, U.S. companies have cut more jobs so far in 2016 than at the same point in any year since 2009. So who do we believe? Is working for one of the companies we own in our Model more rewarding than ever or is it just the opposite?

We continue to look for bargains in sectors of the economy that are experiencing the hardest of times (energy, metals and luxury goods) and are likely to avoid new investments in those that have recently risen to the top (technology, health care and financials, although the biggest banks remain relatively attractively priced). We also have focused on changes in the balance sheets of our companies, particularly those that have taken on large amounts of debt to buy back shares, causing us to shed Home Depot early in the year. Overall, however, there has been very little turnover in our Model Portfolio in the past two years. We continue to heed Warren Buffett's advice that being "slothful," i.e., patient, produces a better result than being hyperactive. In our case, patience also involves maintaining historically large cash reserves and short term bond positions to take advantage of new opportunities as they arise.

Few of us at Peak predicted that the British would vote to withdraw from the Euro Zone, and we are currently perusing scholarly articles on what Brexit might mean to us and the rest of the world. Our own country is going through a similar political upheaval driven by feelings of disenfranchisement and anger toward the established order in Washington. Donald Trump seems to have effectively harnessed this upwelling of discontent, resulting in surprise and dismay among the well-educated liberal elite, also similar to Britain. What is most interesting, however, is the degree of outrage and vituperative name-calling toward him from normally staid conservative columnists like George Will, David Brooks and Charles Krauthammer. Trump has obviously struck a nerve. But our citizenry has survived and even prospered under various styles of leadership in the past twenty years (Jesse Ventura in Minnesota and California's Arnold Schwarzenegger, for example), and I have no doubt that the United States as a whole is resilient enough to do it again. But this is not a prediction.

Best regards,

Noel F. Bennett

**The Model Portfolio is not a real cash portfolio. It represents the core direction of our portfolio management strategies. Individual client portfolios are managed in accordance with the clients' specific investment objectives and constraints. Historical results are available upon request.*