



**CROWELL WEEDON ASSET MANAGEMENT
MONTECITO INVESTMENT PORTFOLIOS**

1Q 2018

Dear Fellow Investors,

Volatility is back. 2017's steady march higher was abnormal from a historical perspective. As we forecast in our January 2018 Annual Letter volatility and corrections have returned! Take heart investors in the knowledge that there is a difference between price volatility and long-term, fundamental value accrual. As Benjamin Graham said a long time ago ***"In the short run, the market is a voting machine but in the long run, it is a weighing machine."***

On a short-term basis stock prices are influenced by emotional reactions to "Headline News", momentum focused traders, black-box algorithm strategies, Index and ETF rebalancing, and many other influences that can cause exaggerated price movements. While the last trade may price the entirety of a company at that moment in time, it doesn't always represent what the entirety of the business is truly worth. When the short-term emotions subside, the real fundamental value will drive the price of the shares.

When we talk about fundamentals, for the sake of simplicity, we're largely talking about valuing a company based on how much money they make, or their earnings. In our January 2017 Annual Letter we showed that long-term stock market returns are highly correlated to earnings. This makes sense. If a company makes more money, it should be worth more. Conversely, when earnings decline, so too should their value. To illustrate this point, we remind investors ***two of the most severe earning declines in stock market history occurred during 2001 (-51%) and 2008 (-78%)!*** Prior to 2001, the average earnings decline for the stock market was 15%. We all witnessed how these severe changes in fundamentals negatively impacted the stock market.

Fortunately, when we analyze the fundamentals of today we see a much different picture than just a few short years ago. Technology continues to advance at a rapid pace making what seemed like science fiction actual reality. Pro-business moves have been made such as slashing the corporate tax rate and reducing costly regulations. Interest rates remain low but finally getting back to a state of normalcy. In our opinion, the main ingredients are in place to see the next major boom in growth. However, these fundamentals tend to be boring, long-term drivers for the stock market. Keep in mind, the media can't sell boring. This is why, from time-to-time, these drivers of growth will be completely forgotten and instead replaced with headlines of the next "Major Fear". Rest assured, we don't invest according to the headlines. ***We invest according to our analysis of fundamentals and continue to believe fundamentals remain sound.***

As always we want to thank you for your continued confidence and the opportunity to manage your investments. We take very seriously our responsibility and will always endeavor to be responsive to your questions and concerns. We welcome and encourage your comments as well.

Sincerely,

Blake Todd, CWS
Portfolio Manager

Jarrett Perez, CFA
Portfolio Manager

Important Disclosures

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- Source for Earnings per Share calculations: <http://www.multpl.com/s-p-500-earnings/table>
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