

The financial markets have worn many masks this year. Like a ping pong ball, wide and powerful swings from Fed pronouncements, movements in the dollar, and the price of oil have contributed to violent and swift changes in mood. Perception and reality are almost entirely a function of macroeconomic news, but for the very brief period in time each quarter when company specific news arrives in the form of earnings season.

Given the active and at times, no doubt, necessary involvement of the Fed in our markets for the past few years, we've slowly and silently been experiencing outcomes that one might expect in a period of greater government. Similar to trends in Little League where everyone gets a trophy regardless of play, passive investing and the rising popularity of exchange traded funds bearings gifts of "exposure" have risen to the forefront of investors' psyches. Like the preference for renting rather than owning anything in a "sharing" economy, we've become numb to both the opportunity and stewardship that ownership affords.

Fortunately, the tides may be turning.

For the first year in quite some time, our results on a year to date basis are substantially ahead of the indices. While our focus on companies that can and do grow in a world where economic growth is scarce certainly helps, it can't explain everything, as we've had this approach for years. What has helped, we believe, is the increasing likelihood that the Fed may finally become less involved in the financial markets as employment and inflation reach "normalized" levels. As the financial markets have started to discount less involvement by the government in its affairs, we've slowly started to feel the faint heartbeat of a market that wants to reward winners rather than everyone who shows up to play.

Like the proverbial frog that boils to death in a slowly warming pot of water, even the most diehard of capitalists have been taken hostage by Fed involvement in the markets in recent years, by declaring the market vulnerable to calamity, given the lack of breadth and participation in this year's results. In other words, with just a narrow set of companies driving the overall market's gains this year, the environment is viewed by some as neither sustainable nor healthy. While these strategists and market technicians could be right, they are likewise suggesting, at least to me, that the only way a market and economy can be healthy is if everyone gets a trophy, otherwise perhaps, no one should.

Similar to the love for all things Fed, stock markets around the world also seem to take their cue from oil prices both above and below \$42 per barrel. Low prices of oil are generally viewed as a positive for the economy and the consumer, but only as long as they don't go too low – apparently the low 40's according to Mr. Market.

To some extent, this makes sense, as some jobs are indeed tied to the health of the oil patch. Lower for longer is a good thing, but too low only accelerates the need for reorganization in the energy, materials, and industrial sectors, which gives rise to systemic concerns over the trickle down effects into other areas of the economy, particularly the financial sector. Just as we can't stand it when only a few areas of

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the economy are doing well, similarly, it seems we can't stand it when just a few are doing poorly. Signals from the stock market, Lord forbid, tempt the Fed to both action and inaction, in an almost schizophrenic, data dependent fashion, as has been the case in the past six weeks.

In addition to a focus on the Fed and oil, we've also heard a great deal about the dollar this year. But I suspect, for most investors, the idea of the dollar and what affects its relative value is a rather nebulous concept. What does it really mean to have a strong dollar? Aside from interest and growth rate differentials across the nations of the globe, what, at its core, does the dollar truly represent? Why are enemies of our State, like Saddam Hussein, discovered in foxholes carrying buckets of U.S. dollars?

I would suggest that at its core, the value of the dollar reflects a belief in the stability and sustainability of the United States as a sovereign nation, founded on the principles of individual freedom and hopefully, responsibility. We are a nation which permits public disagreements that don't have to lead to physical violence or the jailing and decapitation of former leaders with a change in power. The founders of this country were obsessed with the notion of checks and balances, tired, perhaps of rule by royalty, where birth played a role more important than merit in outcomes. Even our Fed, has a dual mandate, one favorable to labor and the other capital.

Ours is an economy that allows the private sector to restructure as needed, and innovation to create new jobs even at the expense of the old. Very few places in the world have areas like Silicon Valley, where the proverbial Wild West gives birth to new ways of doing things at a destructive and at times also very self-destructive pace.

The United States, as offensive as it may sound to some, may enjoy a coveted currency because we permit micro-revolutions on the job and industrial front, revolutions which enable us to maintain our position in an increasingly global competitive environment. Countries around the world believe in our future. If oil represents the past and the dollar is a symbol of innovation and thus, the future, perhaps it should come as no surprise that there is such an inverse correlation between the two. While the last economic crisis may have required greater government involvement, we should also be careful to permit failure, lest we lose the opportunity for its polar opposite, success, to be born.

In recent days, many retailers, including Nordstrom's, have reported lackluster results. Nordstrom's, commenting in its recent earnings call, indicated the traffic to its stores started to slow dramatically in August, a trend which continued in September and October. The weakness was across the board, both at the Rack and core Nordstrom's, along with all merchandise types. At the same time, however, its ecommerce results were up strongly, in the double digits, testament to a "changing preference in the way consumers choose to shop."

Technology has revolutionized the way the consumer wants to shop and be entertained. Through our new demand preferences, we are forcing old guard merchants, programmers, and advertisers like Nordstrom's and Disney, to change how, when and where we are served. Facebook, Google and Amazon are doing well, while others remain slow to change, clinging to business models that may no longer be longer term. Personally, I love it when an old boy network comes crashing down, unleashing creative, undiscovered talent in new mediums of reward like YouTube.

While it may be true that the market has narrowed this year, it is also true that it has been more discriminating, rewarding only the few, perhaps, that deserve it rather than the many simply because they exist. A narrow market can be a dangerous thing, particularly when carried to extremes, but only nine months in, cries over its near term demise would appear premature. If 1994 is a decent benchmark, and I believe it is, we could have some Fed rate normalization followed by a several year

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period where the productivity gains of recent technology shifts finally manifest themselves in the overall economy as further capex gains take hold.

Narrow at first, but perhaps more broadly down the road. So no, we don't believe everyone deserves a trophy. But if done right, everyone should eventually benefit.

Kindest Regards,

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