QUARTERLY COMMENTARY

THE WALL

An ice wall in Antarctica (a "real life" version of The Wall from Game of Thrones) source: sun-surfer.com

As most of our clients and friends are aware, we do not make stock market forecasts. In fact, we believe short-term market prognostications are almost always unworthy of the time spent to produce or consume them, as we do not think anyone can reliably predict gyrations in asset prices in advance. That said, we can and do provide our clients with some insight into how we are approaching the investment environment. From a valuation perspective, we see the broader equity market as being reasonably valued. At roughly 18x forward earnings, the S&P 500 is currently valued at a slight premium to its average forward multiple of 16.9x since 1990. By this same metric, the broader market has been valued as highly as 26.7x (December 1999), and as low as 10x (November 2008).

While it is obvious with 20/20 hindsight that stocks were "too expensive" in late 1999 and "too cheap" in late 2008, we do not think today's valuations contain much predictive value. About the most we can say is that stocks remain attractively valued relative to, for example, Treasury bonds. At a current yield of 2%, an investor in 10-year U.S. Treasury notes will pay 50x earnings for an asset that is guaranteed to return nothing more than par value at maturity. By way of contrast, an investment in the S&P 500 can be made at less than 20x forward earnings and offers a dividend yield of almost 2%/year, along with the potential for long-term capital appreciation. Although investors in the S&P 500 have no guarantee that they will not lose principal over the next decade, we think they are highly likely to fare much better than an investor in Treasuries between now and 2029. We readily admit that this statement, even if proven true, says nothing about whether U.S. stocks will be higher or lower over the next several months. On that score, we think the current state of investor sentiment may offer a bit more in the way of clues (see chart on next page).

INTRODUCING JOANN SEAGREN & MIKE KIMBAROVSKY

Managing Director, JA Glynn Private Wealth

Managing Director & Portfolio Manager, JA Glynn Private Wealth

We are pleased to welcome JoAnn Seagren and Mike Kimbarovsky to our team. JoAnn and Mike have opened JA Glynn Private Wealth in Chicago, where they provide customized separate account investment management and financial advisement to clients across the United States. They share JAG's investment philosophy, which has long been grounded in active portfolio management, flexibility, and the capability to respond decisively to economic shifts and new market opportunities. Like all of us at JAG, JoAnn and Mike believe this approach is critical to preserving principal and generating long-term out performance.

JoAnn and Mike bring decades of experience in making sound, enduring investment decisions for high net worth families and individuals. Their professional background includes many years running their own firm, where they served as investment advisors and financial advocates for their clients. In addition, Mike is a Portfolio Manager with JAG Capital Management, and oversees multiple investment strategies which complement and substantially expand JAG's strategy offerings.

Please visit **www.jaglynnpw.com** to learn more. JoAnn and Mike welcome a conversation with you at any time!

As background, we digress to note that the HBO series "Game of Thrones" ended its highly acclaimed 8-season run on May 19. The show drew millions of fans through its vivid depiction of violent dynastic struggles among a fictional realm's leading families for control of the Iron Throne. Cast with dozens of recurring characters, great acting, and compelling storylines, Game of Thrones won 47 Emmy Awards and is regarded as one of the most-acclaimed television series ever aired. Ironically for such a character-rich drama, one of its more pivotal recurring roles was played by The Wall, which is an inanimate object. Towering over 700 feet high and spanning 300 miles, The Wall was built to protect the southern inhabitants of the realm from the barbaric "wildings" that inhabit it in the frigid north.

The subject of formidable man-made barriers reminds us of an old investment proverb: "Bull markets climb a wall of worry." We think the current market environment brings this saying to life. Although the S&P 500 has gained almost 20% through the mid-point of 2019, many market participants and pundits seem steadfastly committed to hand-wringing over any number of potential roadblocks that stand in the way of further progress for the economy and stock market.

This dynamic has its roots in investor psychology. Over the past few decades, Behavioral Finance researchers have found that humans tend to dislike a given amount of losses roughly twice as much as we enjoy the same amount of gains. This tendency is called myopic loss aversion by academics, and it works with other parts of our psychological wiring to increase our sensitivity to signs of danger in the investment markets.

"You seem troubled, Brother Timothy. Is anything worrying you? I mean besides the sins of the world, the vanities of mankind, and that sort of thing."

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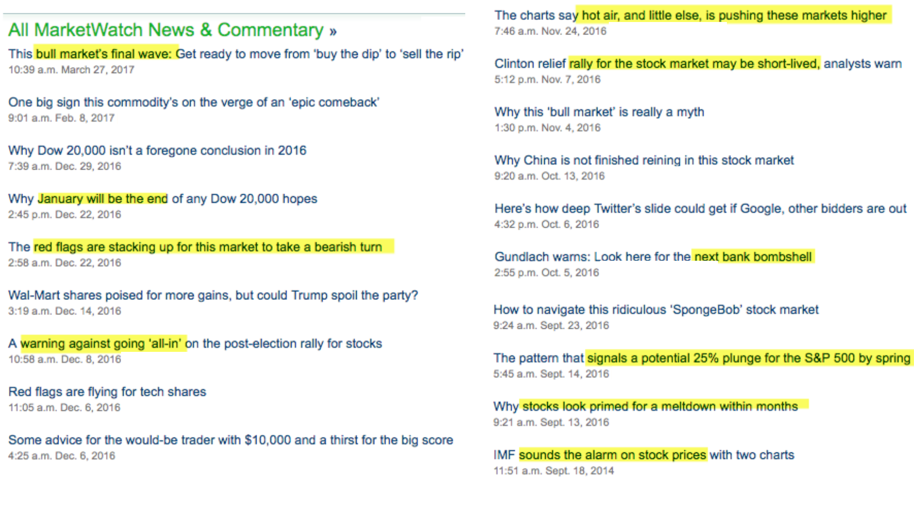
There is always a reason to be bearish



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Source: Urban Carmel

This is why most people are much more likely to "click" through and read an online news article that loudly warns of an approaching market calamity than one which advocates a calm, goals-driven, long-term approach to portfolio management. The normal attraction to negative headlines creates a feedback loop between media content creators and consumers, in which bearish pronouncements on the investment markets receive more attention from readers and viewers, who in turn become more bearish and fearful themselves, thus building a more-receptive audience for scary articles. To the extent that some investors react to their fears by selling stocks, or by maintaining lower levels of investment in equities than they would otherwise, widespread pessimism – "the wall of worry" - helps keep marginal investor dollars out of the stock market. This "dry powder" can provide fuel for future buying, which tends to occur as bull markets persist over time. This is part of why bull markets often run farther and longer than most people expect.

The June 2019 Bank of America/Merrill Lynch (BAML) Global Fund Manager Survey describes how investment professionals currently view the market environment. The 179 survey respondents are (for better or worse) sophisticated professionals, collectively overseeing more than $528 billion of equity and fixed income assets. As a group, these gurus are quite cautious. In fact, according to its authors, this was the "...most bearish survey of investor confidence since the Global Financial Crisis." A few highlights:

- 87% describe the global economy as "late cycle," which is the highest reading ever.
- 74% are bearish on both the global growth and inflation outlook over the next 12 months.
- Collectively, respondents are now 21% net *underweight* to stocks, which represents their lowest allocation to equities since March 2009.
- Collectively, they have raised cash in client portfolios to the highest level since August 2011.

The legendary investor Sir John Templeton had a wonderful way of describing how investor sentiment ties into stock market cycles: "Bull markets are born on pessimism, grown on skepticism, mature on optimism, and die on euphoria." The fact that professional investors are more worried now than they have been since the Great Financial Crisis implies that their dominant emotion is caution, not confidence. Moreover, signs of optimism and euphoria – which as Sir John noted tend to mark the end-stages of a bull market - are notably absent. We suspect that these signs will become evident eventually, but probably not until stocks trade to higher levels. And while it is anyone's guess as to when investors will finally become ebullient, the timeframe between now and the onset of the next bear market could very conceivably be measured in years. While this information alone cannot provide us with any specific insight on the short-term path for stock prices, it helps us enter the back half of 2019 in a constructive frame of mind.

"Sometimes they get frustrated and punch the wall."

Norm Conley
CEO & CIO

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JAG
CAPITAL MANAGEMENT LLC

9841 Clayton Road | St. Louis, MO 63124
800.966.4596 **www.jagcapm.com**
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