HAAS
Capital Management LLC

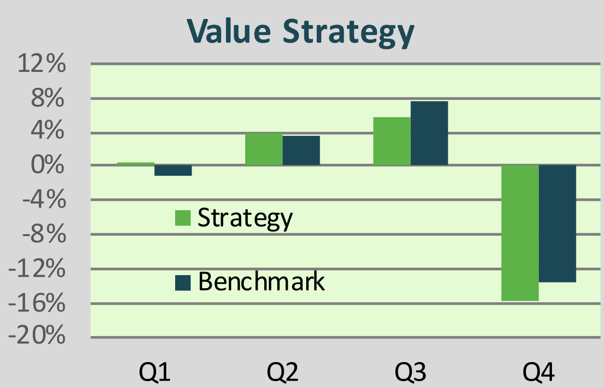
Fourth Quarter 2018 Performance Review

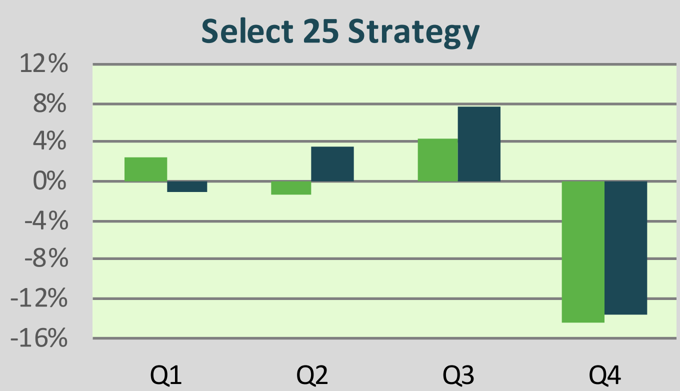
The last quarter of 2018 was a difficult one. All major US indexes reported double digit losses, and foreign stocks did little to help. Bonds added important diversification in the quarter and produced a slight positive performance. The Value strategy faced significant headwinds from the very poor performance of small stocks (Russell 2000 down 20%), and even the Select 25 strategy felt the impact of not owning the largest companies in the market. The Foreign Value strategy fared better, significantly beating it's benchmark and although it reduced the impact of poor US performance, it did not offset it.

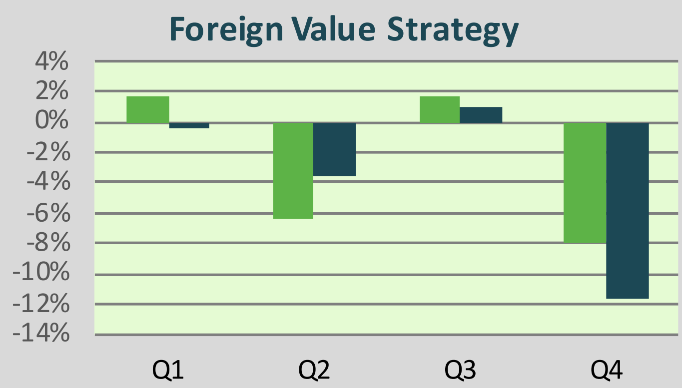
	Q4 2018	Benchmark	**Outperformance**	Prior 12 months	Benchmark	**Outperformance**
Foreign Value Strategy	-7.9%	-11.6%	**3.7%**	-11.0%	-14.3%	**3.3%**
Select 25 Strategy	-14.5%	-13.5%	**-1.0%**	-9.7%	-4.6%	**-5.1%**
Value Strategy	-15.7%	-13.5%	**-2.2%**	-7.3%	-4.6%	**-2.7%**

Strategy returns are before fees

Quarterly Returns January 1, 2018 - December 31, 2018







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Winds of Change

2018 was a poor year in the market and 2019 is an unknown. What seems more certain is that the US market is ending an era of relatively calm steady growth. December has shown us that investors are once again capable of a pessimistic view. Markets swung wildly, down several days and then up, then down. Why?

What a Stock is Really Worth

Like anything of value, a stock is only worth what someone is willing to pay for it. Sometimes investors are willing to pay for a stock in order to buy the entire company (we've had several take-overs in the last few years), sometimes the dividends that a stock pays makes owning it worthwhile, and much of the time a stocks value comes from high expectations for future performance.

Takeover Targets

In order for one company to buy another, they must buy most of the shares of stock. In order to entice stock owners to sell they typically must pay significantly more than the current stock price. A premium of 20% to 30% isn't unusual. This makes owning stock in a company that gets taken over a lucrative endeavor. Although I don't seek to buy stocks in the Value Strategy for their takeover potential, the types of stocks that the strategy owns (profitable and inexpensive) are attractive

Although news of a potential takeover can move a stock's price substantially, takeovers come slowly, one or two at a time. Therefore, this type of activity, or the expectation of it, doesn't typically move the entire market.

Dividends

Dividends are how investors receive a portion of a company's profits. Stocks that are bought for their dividends tend to rise when either the dividend is increased, or interest rates (a competing investment) fall. In the fourth quarter, utility stocks (the largest dividend payers) actually rose slightly, bucking the greater market. Changes in interest rate expectation don't explain the quarters poor performance.

Expectations for Future Performance

Buying the stock of a company that grows quickly over many years is exceptionally lucrative. Companies such as Microsoft, Walmart, and Apple have made many stockholders rich. It is the prospects of this growth that makes many investors willing to pay a high price for a stock that pays no or little dividends and is a poor takeover target. For example, investors currently consider Tesla to have about the same value as GM, in spite of the fact that GM sells more than 10 times the number of cars that Tesla does. The comparison between Walmart and Amazon is equally relevant. Walmart has about double the sales of Amazon but Amazon is worth about three times Walmart.

If either Tesla or Amazon stops growing then their stock should be worth significantly less than GM or Walmart. A drop of 50% to 90% wouldn't be unprecedented. For example, Facebook's stock has declined about 35% just since July and Chipotle Mexican Grill's stock declined over 60% from 2015 to 2018. Growth is notoriously difficult to estimate, but those paying high prices for companies such as Tesla and Amazon are forced to try. Since growth companies are highly valued, even a small change in growth expectations can justify a large change in stock price.

Valuations Matter

What we saw in December was largely a result of expectations for future growth becoming less bright. At the end of the day, these expectations are largely a "wet finger in the wind" and everyone is looking to everyone else for guidance. Hence, the "herd" can take over and panic selling/buying prevail over patient investing. But it's patient investing that has been the winning strategy in the past, and I expect that will hold true in the future. So while the stocks in my strategies may get caught up in the "herd", I'm still hopeful that they will perform better than average over the long term.

Rob Haas January 2, 2019