

May 5, 2022

Dear PCM Clients and Friends:

In February we wrote that the “split” markets of 2021, with many but not all stocks down, had expanded throughout January with most stocks and all of the market averages beginning corrections. The January and February correction was triggered by inflation surging to 40-year highs and the Federal Reserve signally, almost promising, it would raise interest rates faster than previously thought. Later in February, the market’s primary concern shifted from monetary policy to geopolitics as Russia amassed troops on the Ukrainian border and invaded Ukraine in the early hours of February 24. These factors fueled a significant rise in uncertainty and have pushed an expanding list of stocks lower.

As we look forward into 2022 it appears, at this time, that several “big picture” concerns: Ukraine, China, the midterm elections, the Fed and interest rates, significant price inflation, supply chain disruptions and the effect of all of this on corporate earnings; plus, of course, Covid-19, as a pandemic or not, will continue as headlines for the rest of the year.

Looking back, during the past two years we endured, in several waves, the Covid-19 pandemic health crisis. There was also a bitterly partisan presidential election that didn’t end on election day with partisan politics continuing today. A volatile up and down stock market. The current inflation spike, which goes beyond just oil prices, and is likely not just “transitory.” And now, Russia’s invasion of Ukraine.

As investors it would be totally human and normal to feel somewhat exhausted by all of this.

Fortunately, we feel much of the impact of these concerns, uncertainties, or “worries” have already been discounted by the market’s correction which we are now well into; but not quite finished with yet.

No one can know or begin to predict exactly how these situations will resolve themselves; or precisely when. Fortunately, crises in the past have been the starting point for positive change. Today Russia’s tragic war on Ukraine has united western countries and is forcing the Western European countries to rethink their reliance on Russian energy. The current well-documented and quite severe supply chain issues have reinforced the need for U.S. domestic production of goods and services. We should not rely on China or other countries to the degree we do.

As we think back about past crises – and how our American companies have worked through them, regrouped, and then went on to new highs – the more inclined we should be to remember that in America it’s not just a market of stocks, it is a market of investments in companies whose employees are building businesses and that “This too shall pass.”

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INVESTMENT MANAGEMENT

THE MARKET SCOREBOARD

All major equity indices posted negative returns for the first quarter of 2022. The S&P 500 and the Dow Industrials saw only mild losses compared to the Nasdaq Composite, the Wilshire 5000 and Russell 2000. Investors sold growth-oriented, high-P/E technology stocks and bought into sectors with cheaper valuations and more exposure to the traditional economy. This risk-off rotation benefitted the big-cap economically diversified Dow Jones Industrial Average while the Nasdaq Composite suffered. This quarter also ended a seven-quarter streak of positive returns in the S&P 500.

The first quarter of 2022 was the most volatile quarter for markets since the depths of the pandemic in 2020, as numerous threats to economic growth emerged. This broader market volatility began during the second week of January as inflation readings hit multi-decade

Ranked by Q1 Return Indexes	% Return Q1 2022
S&P 500 Total Return	-2.72
NYSE Composite	-2.87
Dow Jones Industrial Average	-4.57
Wilshire 5000	-5.89
NASDAQ Composite	-9.10

highs, confirming that price pressures were still accelerating. That prompted multiple Federal Reserve officials to signal that interest rates would likely rise faster than markets had previously thought. The steep declines in the tech sector exacerbated market volatility in January. Additionally, while the fourth-quarter earnings season was solid, there were several large, widely held technology companies that posted disappointing results or forecasts. Finally, in late January at the FOMC meeting,

Fed Chair Powell clearly signaled that the Fed would be raising rates at its next meeting in March; confirming to investors that interest rates were going to rise much more quickly than had been assumed just a few months prior.

By market capitalization, large-cap stocks outperformed small-cap stocks in the first quarter, and that was to be expected given the geopolitical uncertainty and rising interest rates. Investors flocked to the relative safety of large caps amid the rise in volatility over the course of the quarter.

On a sector level, only two of the eleven sectors in the S&P 500 finished the first quarter with a positive return. Energy, up 38% in its best single quarter ever, was the clear standout as the sector benefitted from the increase in geopolitical uncertainty and subsequent surge in oil and natural gas prices in response to the Russia-Ukraine war. Utilities, a traditionally defensive sector, were modestly positive. Sector laggards included the communication services, internet technology, semiconductor technology, and consumer discretionary sectors. Most other sectors in the S&P 500 saw modest declines that did not stray too far from the performance of the S&P 500.

The market averages declined from early January until mid-March, rallied into the end of the quarter, then in April corrected again going back down to the February lows. The first four months of 2022 were the most volatile months for markets in several years.

STOCK MARKET OBSERVATIONS

A year ago, in our May 12, 2021 letter, we discussed market corrections when we posed and answered the question: “What should we expect in terms of a correction in stock prices?”

To answer that question, we presented the Ned Davis Research chart Mean Market Days Without a Correction which revealed that: “In bull markets 5% corrections come along every 84 days on average (3 or 4 a year), 10% corrections occur every 331 days (every year) and 20% corrections every 1105 days (every 4 years – the economic cycle).” We then stated that the current market was overdue for a correction.

So where are we at now in terms of these timelines? The S&P 500 and the Dow have completed 5% and 10% corrections and both have approached but not had a 15% or 20% correction in 450 days. The Nasdaq Composite, which is heavily technology weighted, has corrected significantly during the past year with over a 20% correction. From their highs the Russell 1000 Growth, NASDAQ, and Russell 2000 have all entered “bear territory,” being down -21%, -23%, and -23% from their highs.

What is interesting, and has been very difficult for us as investors who generally invest for growth, is that “growth stocks” have had dramatically greater corrections than what is referred to as “value companies.” Year to date, the Russell 1000 Growth stocks have had a negative return of -20.0% while the Russell 1000 Value stocks have had a negative return of -6.3%. In S&P stocks, the S&P 500 is down year to date -12.9%; but in terms of growth vs value, the S&P 500 Value is down -5% YTD through April versus S&P 500 Growth down -20%. In this down market, value has significantly outperformed growth.

The question on everyone’s minds now, like kids traveling in a car, is: Are we there yet?

The honest answer is that no one knows or has been shown to predict future markets with any certainty.

Looking at the past, the average maximum drawdown in the S&P 500 since 1990 has been -13.88%. To date, the S&P 500’s maximum drawdown from 1/3/2022 has been -13.05%.

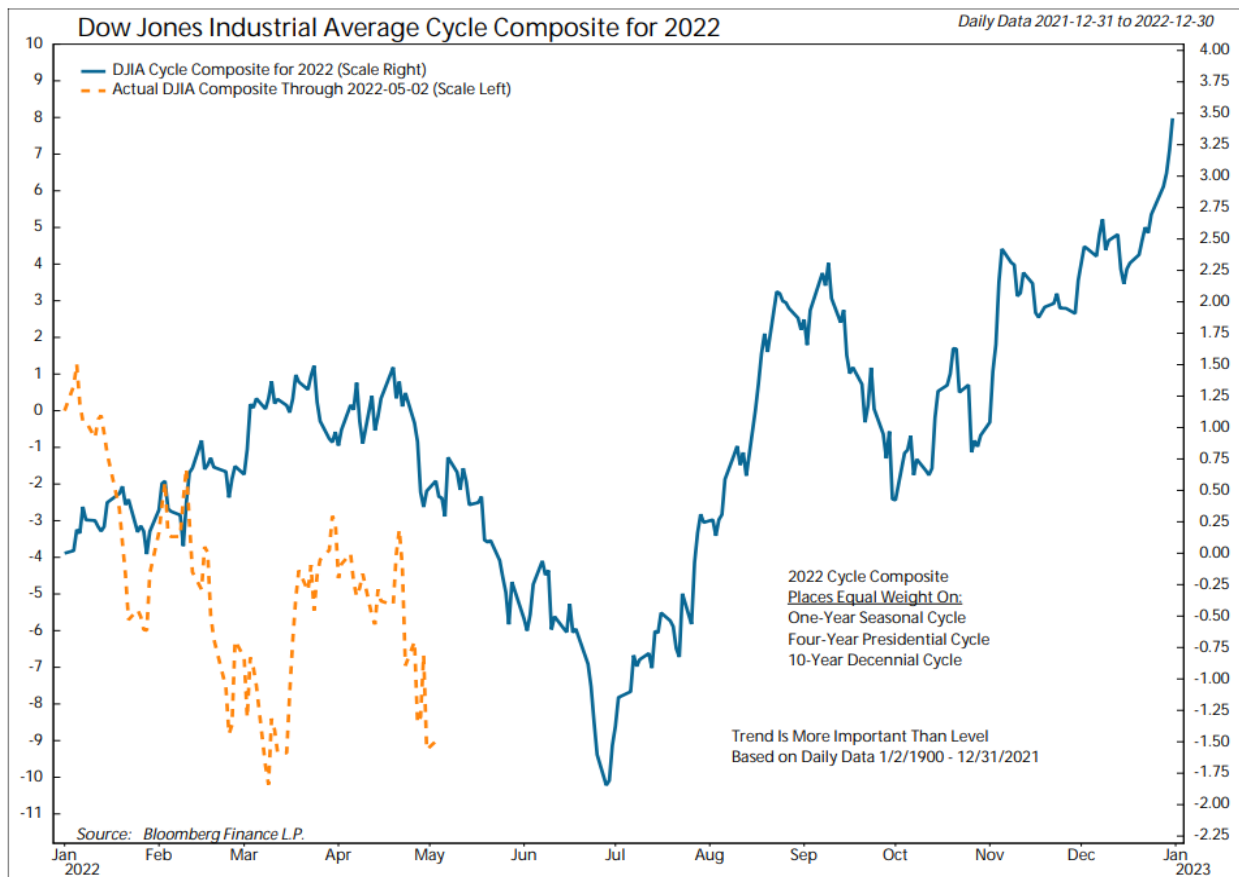
Our opinion regarding this correction, which we stated earlier, is that we are now well into it; but not quite finished yet.

In our quarterly letters, we have often included graphs of the important cycle work of Ned Davis Research. In our last letter we included the S&P 500 Cycle Composite for 2022, the Dow Industrials Four-Year Presidential Cycle for the next four years, and the Dow Industrial 10-Year Decennial Pattern. The Presidential Cycle predicts a low during this midterm election year and then a generally positive market until after the “honeymoon period” of the next first presidential year which is 2025.

Midterm years have been on average the weakest year of the four-year presidential cycle for the stock market. Midterm years have often been years with elongated corrections; often into Q2 or near to when the elections are resolved in Q3 before a Q4 rally.

Ned Davis Research has also indicated that drawdowns are bigger in midterm years on average. They wrote on March 29: “Consistent with lower returns, midterm years have experienced larger drawdowns, on average. Only 6 of the 30 midterm years have experienced maximum declines of less than 10% in the DJIA. The median midterm correction is 17.3% versus 13.2% for all years. The DJIA’s max drawdown year to date is 11.3%.”

This is shown below in the Dow Jones Industrial Average Cycle Composite for 2022.



The blue line shows the 2022 Cycle Composite (equally weighted composite of the One-Year Seasonal Cycle, the Four-Year Presidential Cycle and the 10-Year Decennial Cycle). The orange line shows the early decline of the Dow, its March rally, and then the year-to-date decline. NDR states that trend is more important than level. The trend could be lower into summer or we could have a rally now and then a retest. The good news for investors

is that the presidential cycle work turns positive prior to the elections; during the summer months or by the end of the third quarter.

As always, if you have any questions about your accounts, any of your specific investments, or any of the companies you are invested in, please give us a call. Or call in and ask to schedule a time to talk.

Now that we appear to be moving into a somewhat post-COVID environment, we have also had several clients come into the office again and we welcome this. We are always willing to answer your questions.

Sincerely,



Richard C. Perkins, C.F.A.
President
Portfolio Manager



Daniel S. Perkins, C.F.A.
Chief Operating Officer
Portfolio Manager

RCP:DSP/jah



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SOME LAUGHS FROM THE PAST:

HOW IS NORMA?

A sweet grandmother telephoned St. Joseph's Hospital. She timidly asked, "Is it possible to speak to someone who can tell me how a patient is doing?"

The operator said, "I'll be glad to help, dear. What's the name and room number?"

The grandmother in her weak, tremulous voice said "Norma Findlay, Room 302." The operator replied, "Let me place you on hold while I check with her nurse."

After a few minutes, the operator returned to the phone and said, "Oh, I have good news. Her nurse just told me that Norma is doing very well. Her blood pressure is fine; her blood work just came back as normal, and her physician, Dr. Cohen, has scheduled her to be discharged on Tuesday."

The grandmother said, "Thank you. That's wonderful! I was so worried! God bless you for the good news."

The operator replied, "You're more than welcome. Is Norma your daughter?"

The grandmother said, "No, I'm Norma Findlay in 302. No one tells me sh*t."

NEVER UNDERESTIMATE A LITTLE OLD LADY

A little old lady was walking down the street dragging two large plastic garbage bags behind her.

One of the bags was ripped and every once in a while, a \$20 bill fell out onto the sidewalk. Noticing this, a policeman stopped her and said, "Ma'am, there are \$20 bills falling out of that bag."

"Oh really? Darn it!" said the little old lady. "I'd better go back and see if I can find them. Thanks for telling me, officer."

"Well now, not so fast," said the cop. "Where did you get all that money? You didn't steal it, did you?"

"Oh, no, no," said the old lady. "You see, my back yard is right next to the golf course. On golf days, a lot of golfers come and pee through a knothole in the fence, right into my flower garden. It used to really tick me off. Kills the flowers, you know. Then I thought, why not make the best of it? So now, I stand behind the fence by the knothole, real quiet, with my hedge clippers. Every time some guy sticks his thing through my fence, I surprise him, grab hold of it and say, Okay buddy! Give me \$20, or off it comes."

"Well, that seems only fair," said the cop, laughing. "OK. Good luck! Oh, by the way, what's in the other bag?"

"Well, you know," said the little old lady, "not everybody pays."

NEVER USE COPIES

A young priest arrives at the monastery. He is assigned to helping the other priests in copying the old canons and laws of the church by hand.

He notices, however, that all of the priests are copying from copies, not from the original manuscript. So, the new priest goes to the bishop to question this, pointing out that if someone had made even a small error in the first copy, it would never be picked up! In fact, that error would be continued in all of the subsequent copies, allowing many chances for error.

The bishop says, "We have been copying from the copies for centuries, but you make a good point, my son."

He goes down into the dark caves underneath the monastery where the original manuscripts are held as archives in a locked vault that hasn't been opened for hundreds of years. Hours go by and nobody sees the old bishop.

So, the young priest gets worried and goes down to look for him. He sees him banging his head against the wall and wailing, "We missed the R! We missed the R! We missed the R! His forehead is all bloody and bruised and he is crying uncontrollably. The young priest asks the old bishop, "What's wrong, Father?" With a choking voice, the old bishop replies, "The word was "CELEBRATE!"

WHAT THE CHILDREN HAVE TO SAY

A little girl was talking to her teacher about whales. The teacher said it was physically impossible for a whale to swallow a human because, even though it was a very large mammal, its throat was very small. The little girl stated that Jonah was swallowed by a whale. Irritated, the teacher reiterated that a whale could not swallow a human; it was physically impossible. The little girl said, "When I get to heaven, I will ask Jonah." The teacher asked, "What if Jonah went to hell?" The little girl replied, "Then you ask him."

A Kindergarten teacher was observing her classroom of children while they drew. She would occasionally walk around to see each child's work. As she got to one little girl who was working diligently, she asked what the drawing was. The girl replied, "I'm drawing God." The teacher paused and said, "But no one knows what God looks like." Without missing a beat, or looking up from her drawing, the girl replied, "They will in a minute."

One day a little girl was sitting and watching her mother do the dishes at the kitchen sink. She suddenly noticed that her mother had several strands of white hair sticking out in contrast on her brunette head. She looked at her mother and inquisitively asked, "Why are some of your hairs white, Mom?" Her mother replied, "Well, every time that you do something wrong and make me cry or unhappy, one of my hairs turns white." The little girl thought about this revelation for a while and then said, "Momma, how come ALL of grandma's hairs are white?"

The children had all been photographed, and the teacher was trying to persuade them each to buy a copy of the group picture. "Just think how nice it will be to look at it when you are all grown up and say, 'There's Jennifer; she's a lawyer,' or 'That's Michael, he's a doctor.'" A small voice at the back of the room rang out, "And there's the teacher. She's dead."

U.S. NAVAL SHIP TRANSCRIPT WITH THE CANADIAN AUTHORITIES

Canadians: Please divert your course 15 degrees to the south to avoid a collision.

Americans: Recommend you divert your course 15 degrees to the north to avoid a collision.

Canadians: Negative. You will have to divert your course 15 degrees to the south to avoid a collision.

Americans: This is the Captain of a U.S. Navy ship. I say again, divert YOUR course.

Canadians: No. I say again, you divert YOUR course.

Americans: THIS IS THE AIRCRAFT CARRIER U.S.S. LINCOLN, THE SECOND-LARGEST SHIP IN THE UNITED STATES' ATLANTIC FLEET. WE ARE ACCOMPANIED BY THREE DESTROYERS, THREE CRUISERS AND NUMEROUS SUPPORT VESSELS. I DEMAND THAT YOU CHANGE YOUR COURSE 15 DEGREES NORTH. I SAY AGAIN, THAT'S ONE FIVE DEGREES NORTH, OR COUNTER-MEASURES WILL BE UNDERTAKEN TO ENSURE THE SAFETY OF THIS SHIP.

Canadians: This is a lighthouse. Your call.

RELATIONSHIP WISDOM FROM CHILDREN

HOW CAN A STRANGER TELL IF TWO PEOPLE ARE MARRIED?

You might have to guess, based on whether they seem to be yelling at the same kids.
-- Derrick, age 8

WHAT DO YOU THINK YOUR MOM AND DAD HAVE IN COMMON?

Both don't want any more kids. -- Lori, age 8

WHAT DO MOST PEOPLE DO ON A DATE?

Dates are for having fun, and people should use them to get to know each other. Even boys have something to say if you listen long enough. -- Lynette, age 8

On the first date, they just tell each other lies and that usually gets them interested enough to go for a second date. -- Martin, age 10

WHEN IS IT OKAY TO KISS SOMEONE?

When they're rich. -- Pam, age 7

The rule goes like this: If you kiss someone, then you should marry them and have kids with them. It's the right thing to do. - - Howard, age 8

EMAIL EXCHANGE OF LETTERS FROM A PROPERTY DISPUTE WITH THE MICHIGAN DEPARTMENT OF ENVIRONMENTAL QUALITY:

Dec. 17, 1997
Mr. Ryan DeVries
2088 Dagget
Pierson, MI 49339

Dear Mr. DeVries:

It has come to the attention of the Department of Environmental Quality that there has been recent unauthorized activity on the above referenced parcel of property. You have been certified as the legal landowner and/or contractor who did the following unauthorized activity: Construction and maintenance of two wood debris dams across the outlet stream of Spring Pond. A permit must be issued prior to the start of this type of activity. A review of the Department's files shows that no permits have been issued.

The Department has been informed that one or both of the dams partially failed during a recent rain event, causing debris and flooding at downstream locations. The Department therefore orders you to cease and desist all unauthorized activities at this location, and to restore the stream to a free-flow condition.

Sincerely,
David L. Price
District Representative
Land and Water Management Division

The reply:

Dear Mr. Price:

Your certified letter dated 12/17/97 has been handed to me to respond to. Mr. Ryan DeVries is not the legal landowner and/or contractor at 2088 Dagget, Pierson, Michigan. I am the legal owner and a couple of beavers are in the (state-unauthorized) process of constructing and maintaining two wood "debris" dams across the outlet stream of my Spring Pond. While I did not pay for nor authorize their dam project, I think they would be highly offended to hear you call their skillful use of natural building materials "debris."

I would like to challenge you to attempt to emulate their dam project. I believe I can safely state there is no dam way you could ever match their dam skills, their dam resourcefulness, their dam ingenuity, their dam persistence, their dam determination and/or their dam work ethic. As to your dam request – the beavers first must fill out a dam permit prior to the start of this type of dam activity – my first dam question to you is: Are you trying to discriminate against my Spring Pond beavers or do you require all dam beavers throughout this state to conform to said dam request?

As for me, I am not going to cause more dam flooding or dam debris jams by interfering with these dam builders. I seriously hope you are not selectively enforcing this dam policy – or once again both I and the Spring Pond beavers will scream prejudice!

Sincerely,
Stephen L. Tvedten