

October 28, 2019

Dear PCM Clients and Friends:

The past three months have again come and gone quickly at PCM. We continue to very much be in our normal routine here. In our April tribute letter to Perk we wrote: "Then there were all the many years working together at PCM; as a team, as father and sons, but also as individuals with a contribution to make." We continue to work here as a team. Every team member does have a contribution to make toward our success for you, our client. All of us here do still think of Perk every day as we do our work. Our success will come from what we contribute as individuals and also accomplish as a team. A further thought of ours is that we need to ensure the important daily and weekly contributions Perk made to our success here at PCM continue. We are talking and thinking formally about what those important contributions were and making plans to ensure that his most important "work" contributions continue. For us this is less about our grieving and more about making sure Perk's contributions guide us in the future.



It seems like autumn comes and goes so quickly here in Minnesota. We are hoping for a little more fall -- the Indian summer that we do not feel we had. What we did continue to have was more of the rain this fall. On our fall hunting trips to western Minnesota and South Dakota you can still see it -- wet, muddy fields everywhere. The little lakes and rain-soaked fields which we described in July as impossible to plant. Now many of these same fields look not harvestable unless the farmer has one of John Deere's newest fanciest machines ... you could call it the Heli Harvester. Seriously, in many of the fields we drove past this fall we think it would literally take a helicopter to harvest them. That would be for the corn and maybe soybeans. The sugar beet crop in many areas is at risk of being frozen in the ground. We will have to wait and see what develops for the farmers' harvest over the next several weeks.

The Bomba Squad (aka The Twins)



We have good news and bad news as a follow up to our July letter segment: How about those Twins – Baseball Summer Excitement in Minnesota Again. First, the good news. The Twins did win the American League Central Division for the first time since 2010. More importantly, they did also set the all-time record for home runs by a team in a single season! They hit 307 home runs (**Bombas**)!! This was led by Nelson Cruz who hit 41 Bombas. It was also a team effort as they were the first team to have 5 players hit 30 or more Bombas (home runs) in a single season. The bad news is they did lose to the New York Yankees in the playoffs after having the bases loaded a couple of times

right when they could have used, yes, a Bomba. Oh well. It was an exciting season for Minnesota Twins fans and they can now say with quite a bit more enthusiasm than in previous years wait till next year; it will be a **Bomba!**

THE MARKET SCOREBOARD

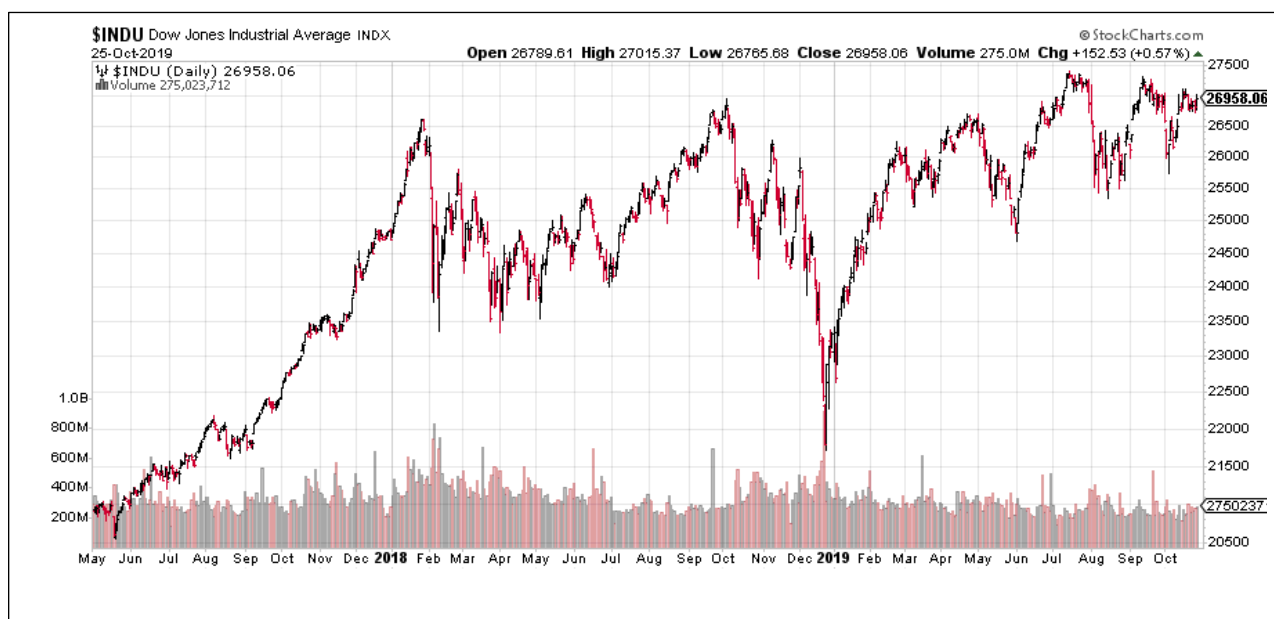
The third quarter of the year provided modest positive returns for many but not all stocks. The month of July was flat, a midsummer rest, then down sharply in early August, back up to briefly touch the highs at mid-September followed by a modest decline into the end of September, which continued into October. This was a rest after the strong first six months of the year which was positive across all asset classes and was the best start of a year since 1997; but there was more underneath the surface. Everyone participated in the first six months of the year while the third quarter was very different. In Q3 bigger was better with many of the larger companies having modest but positive returns. Many small and micro-cap companies had negative returns during the summer quarter. Q3 was also a quarter where many of the best first half performers gave back some of their gains. This could be seen in the performance of the health care sector where we at PCM have had many long-term healthy investments for clients; but in 2019, Q3 was a tough quarter for health care companies. According to Furey Research Partners, health care companies, in general as a group, fell -9% in Q3. They also noted that the health care industry group of companies in the Russell 2000 was down -15% compared to the entire index itself having a negative -2.4% decline. Piper Jaffray, in their October 2019 Informed Investor publication, looked at the health care sector returns by market cap. The Q3 performance of the 663 health care companies in Piper's Informed Investor universe very much followed the big was better theme with the 41 largest mega-cap companies (greater than 20 billion in capitalization) being down -3.04%, the next grouping of 60 companies in the 5 billion to 20 billion big-cap group was down -9.47%, followed by the mid-cap 2 billion to 5 billion down -8.33%. The two groups of smaller companies included 274 small-cap companies in the 250 million to 2 billion range down -14.69% and 218 micro-cap companies under 250 million in market cap down -19.28% on average during the quarter. Q3 was a tough quarter for health care.

Ranked by YTD Return Indexes	% Return YTD 2019
NASDAQ Composite	20.56
S&P 500 Total Return	20.55
Wilshire 5000	17.87
Dow Jones Industrial Average	15.39
NYSE Composite	14.33
S&P SmallCap 600 Total Return	13.46
Value Line Composite	10.23

Ranked by Q3 Return Indexes	% Return Q3 2019
S&P 500 Total Return	1.70
Dow Jones Industrial Average	1.19
Wilshire 5000	0.28
NASDAQ Composite	-0.09
S&P SmallCap 600 Total Return	-0.20
NYSE Composite	-0.34
Value Line Composite	-2.36

STOCK MARKET OBSERVATIONS

We ended last quarter’s Stock Market Observations section with the observation that “we feel the markets are strong; but not quite broad enough yet and strong enough today to move immediately dramatically higher.” We also said: “Our thought at this time is that we will continue to consolidate here and perhaps form another small V later in 2019.” This has been the market’s behavior the past three months. During the past three months we have experienced two “small Vs” with the averages declining twice then returning back to the area of its highs. This can be seen in the chart below:

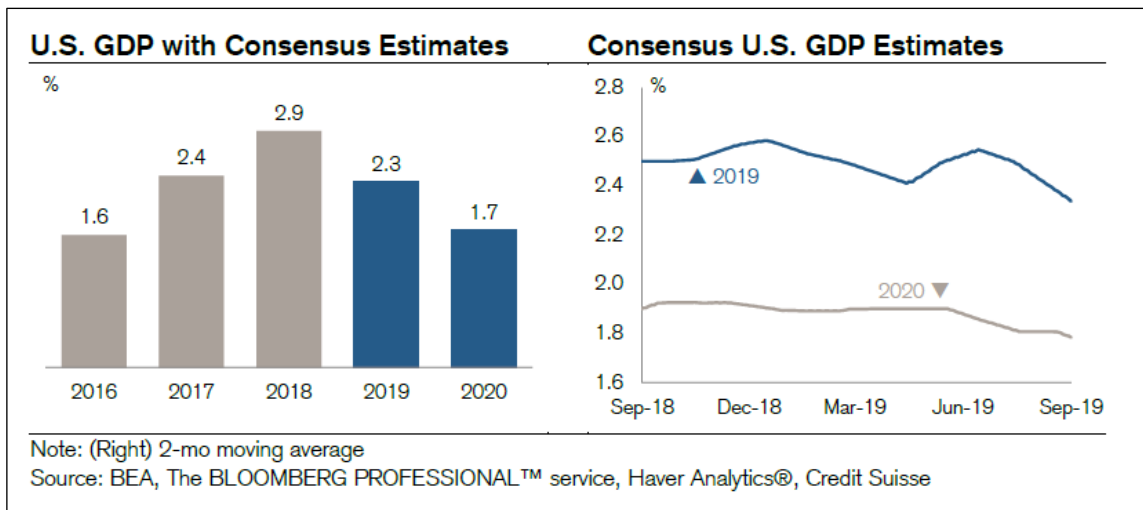


This has been the case with the Dow, the S&P, the NASDAQ composite, and the Dow Transports; with the Russell (the smaller stocks) lagging and not as strong as the other indices. Only the Utilities have moved higher and gone to new all-time highs during the past three months.

We see this up and down and sideways movement near the highs in the averages as a normal consolidation which is likely to continue for several more months now. We do not feel that the markets have the strength at this time to move to a sustainable new high. The key words here are: “at this time”. We also do not feel that we will have more than the normal V type of corrections we have been experiencing during the past 18 months. These are the 5% to 10% corrections which have occurred almost twenty times during the past 10 years. More sideways Vs for now.

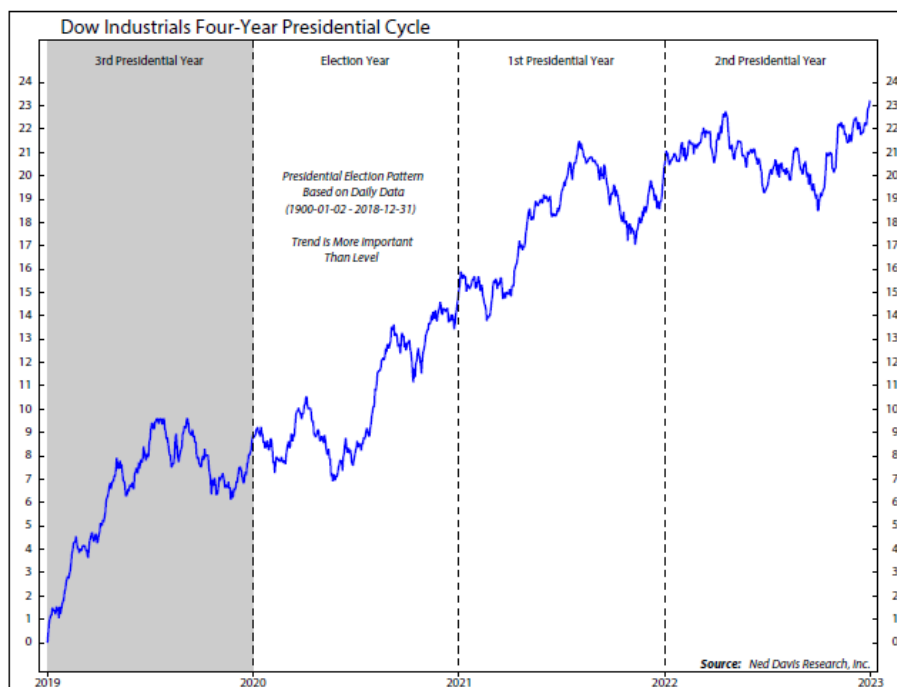
The most recent consolidation similar to what we are now experiencing lasted during most of 2015 and 2016. After this period the markets in terms of the averages moved up strongly -- about 40% -- after the elections in 2016 into the early 2018 high during a strong 2017. After every strong upward move in the averages, it is normal for a consolidation or sideways period as the market digests its gains. Periods of consolidation often follow periods of strength and are part of the long-term trend of market. This is what we feel we are experiencing.

Our “plow horse” economy continues with yet a little slower but still positive growth; around 2% now and going into 2020. Every day it seems there is a different economic statistic; some positive, some are not quite as good as earlier this year, but none at this time are negative. The news media continues to do its best to create angst and news by throwing out the recession fear; but at this time the economy continues at a more or less positive pace. Rates are low, the Fed is accommodative and all the fear of the future is at this time a “what if.” The news media also reminds us that the current economic expansion is the longest in US history -- ten years and running; implying that it cannot last forever. It, of course, will not last forever. Yet, with tax rate cuts taking effect, an accommodative Fed monetary policy, interest rates still extremely low, a President with a pro-business stance, more pro-business regulatory policies, and consumers employed and spending, we do not see anything derailing our plow horse economy anytime soon.



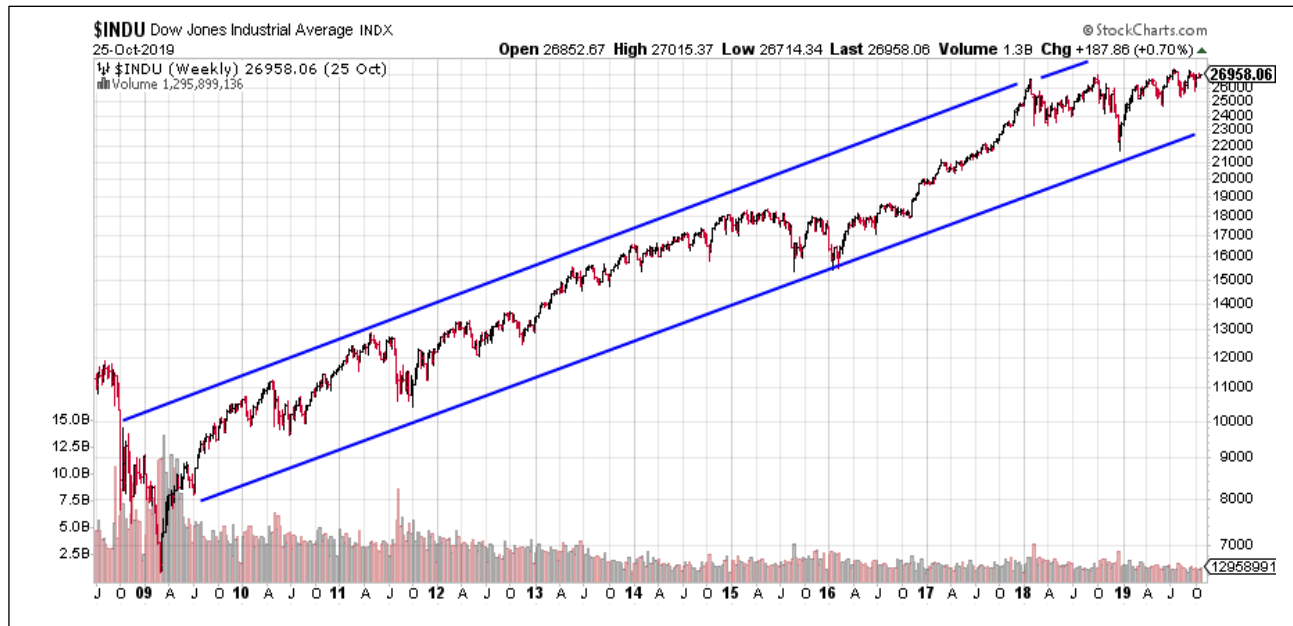
A very interesting piece of research by Ned Davis Research crossed our desk about a week ago entitled: “Presidential cycle choppy into mid-2020.” As our readers know we have regularly included the Ned Davis’ market cycle work in our letters and, though not perfect,

their work has been quite accurate over many years in predicting the market’s general direction and form. Their annual S&P 500 Cycle Composite is a one-third weighted compilation of the seasonal one-year market cycle, the 10-year decennial cycle, and the four-year presidential cycle. What was interesting was their analysis of year-end rallies during election years compared to non-election years. Their conclusion was that



while it is typical in most years for the stock market to correct in the fall before staging a year-end rally (your typical September/October correction) that in pre-election years the year-end rally has not tended to carry through into the early months of the following year. As shown in their chart of the Dow Industrials Four-Year Presidential Cycle (above) and as they stated: “... the four-year cycle has endured a trading range from early September of the pre-election year to mid-May of the election year.”

As we listen to the day-to-day chatter of the business news media as it reports the market as either up or down and for what reason, we run the risk of missing “the forest for the trees,” the risk of getting twisted up and forgetting what is important. One important long-term trend we are currently in is the 10-year uptrend since the multi-generational 2009 low in the markets. As displayed in the chart on the next page, the market has traded within an upward channel of higher highs and higher lows with sideways periods of consolidation since the 2009 lows. This is a fairly wide channel which in terms of up and down percentage is actually approximately 20% wide. Today the market average is about in the middle of this upward sloping channel; the point of which is that there is plenty of room for the market to go up as well as sideways and continue to consolidate within the long-term positive channel. There is room within the channel, with the market about in the middle, to correct down 5%-10% in terms of the averages without violating the upward trend of the market’s series of higher highs and higher lows.



In conclusion, our stock market observation is that the market will continue its sideways consolidation with a modest upward but fluctuating trend. We think the economy will continue to plow along and that we must always consider what the Fed is doing. An accommodative Fed helps the markets and this is often referred to as election “pump priming.” As shown in the Ned Davis Four-Year Presidential Cycle, this consolidation could continue until the market identifies the next likely winner of the 2020 presidential election. We continue to feel we are in an environment which is positive for investing in individual opportunities; companies who over time can show positive growth and results. There is also an opportunity for conservative investors to invest in high quality dividend paying companies whose yield and opportunity for increasing their dividend over time far exceeds the current interest rate investment returns.

Sincerely,

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

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

RCP:DSP/jah

The cartoon refers to Minnesota deer hunting season. If the "Deere Heli Harvester" shows up in the fields this fall Minnesota deer hunters will have to know their deer.



SIMPLE POINTS TO PONDER

If you have a bad cough, take a large dose of laxatives. You'll be afraid to cough.

You only need two tools in life - WD-40 and duct tape. If it doesn't move and should, use the WD-40. If it shouldn't move and does, use the duct tape.

How come you press harder on a remote control when you know the battery is dead?

Why are there flotation devices under plane seats instead of parachutes?

Whose cruel idea was it for the word "lisp" to have an "s" in it?

Tell a man that there are 400 billion stars and he'll believe you. Tell him a bench has wet paint and he has to touch it.

Why do banks charge you a "non-sufficient funds fee" on money they already know you don't have?

The easiest way to find something lost around the house is to buy a replacement.

Aging: Eventually you will reach a point when you stop lying about your age and start bragging about it.

A truly happy person is one who can enjoy the scenery on a detour.

Life and beer are very similar... chill for best results.

THE SUNDAY OFFERING

One Sunday a pastor told the congregation that the church needed some extra money and asked the people to prayerfully consider giving a little extra in the offering plate. He said that whoever gave the most would be able to pick out three hymns.

After the offering plates were passed, the pastor glanced down and noticed that someone had placed a \$1,000 bill in offering. He was so excited that he immediately shared his joy with his congregation and said he'd like to personally thank the person who placed the money in the plate.

A very quiet, elderly and saintly lady all the way in the back shyly raised her hand. The pastor asked her to come to the front. Slowly she made her way to the pastor.

He told her how wonderful it was that she gave so much and in thanksgiving asked her to pick out three hymns.

Her eyes brightened as she looked over the congregation, pointed to the three of the handsomest men in the church and said, "I'll take him, and him, and him."

THREE BLONDES APPLY FOR A JOB

Three blondes were all applying for the last available position on the Texas Highway Patrol. The detective conducting the interview looked at the three of them and said, "So y'all want to be cops, huh?" The blondes all nodded.

The detective got up, opened a file drawer, and pulled out a folder. Sitting back down, he opened it, pulled out a picture, and said, "To be a detective, you have to be able to detect. You must be able to notice things such as distinguishing features and oddities like scars and so forth." So he stuck the photo in the face of the first blonde and withdrew it after about two seconds. "Now," he said, "did you notice any distinguishing features about this man?"

The blonde immediately said, "Yes, I did. He has only one eye!" The detective shook his head and said, "Of course he has only one eye in this picture! It's a profile of his face! You're dismissed!" The first blonde hung her head and walked out of the office.

The detective then turned to the second blonde, stuck the photo in her face for two seconds, pulled it back, and said, "What about you? Notice anything unusual or outstanding about this man?" "Yes! He only has one ear!" The detective put his head in his hands and exclaimed, "Didn't you hear what I just told the other lady? This is a profile of the man's face! Of course, you can only see one ear! You're excused too!" The second blonde sheepishly walked out of the office.

The detective turned his attention to the third and last blonde and said, "This is probably a waste of time, but," he then flashed the photo in her face for a couple of seconds and withdrew it, saying, "All right, did you notice anything distinguishing or unusual about this man?" The blonde said, "I sure did. This man wears contact lenses." The detective frowned, took another look at the picture, and began looking at some of the papers in the folder. He looked up at the blonde with a puzzled expression and said, "You're absolutely right! His bio says he wears contacts! How in the world could you tell that by looking at his picture?" The blonde rolled her eyes and said, "Well, Helloooooooooooooo! With only one eye and one ear, he certainly can't wear glasses."