

January 17, 2018

Dear PCM Clients and Friends:

Minnesota is thought of as the nation's icebox. Who would ever want to live there? That is the usual expression we hear from anyone living in any of the other 49 states. Well, yes it can get very cold and it is 10° below zero Fahrenheit as this is being written, and it may



very well get to -20° or more by the time this cold snap is over. It does get very cold, for sure, but there are benefits which we will talk about later, but right now we are thinking about the disasters of the past year in other states, and Puerto Rico. We did not have a Harvey or Irma, which Texas and Florida had, nor have we had fires devouring thousands of acres, hundreds of homes and countless helpless animals in California. And, no blizzards of epic proportions as in the Eastern states, although sometimes we

do get a taste of it. So looking at the past year, we consider living in Minnesota one of the best places to be, despite the cold. There are benefits from the cold—frozen water, commonly called ICE. Remember, Minnesota is the “Land of 10,000 Lakes” per our automobile license plates, but there are actually about 13,000 lakes. And with the cold, therefore, we get frozen lakes and fishing through the ice begins with miniature cities popping up on almost every lake. The scene above is one of the bays out on Lake Minnetonka near our office. The fish houses are placed where fish (sunfish, crappies, and walleye) are known to congregate—for example, near an underwater structure that is conducive to populations of fish. Thus there are pop-up villages dotting the lakes in certain areas of the lake. Of course, some areas are more productive than others, and since many of the houses are on wheels they move to what might be a better location, drill new holes in the ice and get right back to the business of fishing. Many of these fish houses are quite elaborate, including a stove for heat as well as one for cooking, two, or maybe even three, holes in the ice to



accommodate several fishermen, plus bunk beds for a nap. Yes, you guessed it, some fisherman are so nuts about the sport that they may stay for several days and nights watching television or playing cards with their buddies when the fishing is slow. The previous picture is the interior of one of the more elaborate houses which, as you can see, has four fishing holes with the black covers on them. Even a gas fireplace! No need to worry about the fish spoiling, just toss them out the door to keep them frozen. Sometimes, of course, some of the smaller pan fish are cleaned and fried for a meal of fresh fish. Yes, Minnesota is cold at times; there will be pleasant days to just drill a hole and fish. Not so bad, actually.

A MESSAGE FROM PERK

Now that we have had a stretch of cold weather, the prediction is that there will be a “January thaw” or what we called “case weather” in Vernon County, Wisconsin, where I grew up. The “cash crop” for dairy farmers was raising tobacco. A typical farm in the area had enough cows to get a paycheck for daily living from the milk, but the annual “bonus” was a check for growing tobacco. For some reason, the land in Vernon county and a few neighboring counties, had the unique soil and weather to grow leaf tobacco, which was in demand for cigar wrappers. The farm where my mother, her twin brother and two sisters were raised was typical, and so as a young boy growing up I often visited the farm. As it

was only five miles away, I bicycled it. Raising—growing—tobacco is a very labor-intensive crop, so I was needed to help. To begin with, the little plants had to be grown from seed like a tomato plant, for example. The plants grew in a covered area to provide warmth and retain moisture and when they got to be about six inches tall they were replanted in the “tobacco field” which had been meticulously prepared to be receptive to the young plants. The planting was done by two people sitting on seats near the



ground at the back of the planter, which held water which dispensed as each plant was put into the ground. Monotonous job. Some of the plants didn't make it, so hand replanting was necessary. As they grew, hand hoeing got rid of the weeds, and when the tobacco plants grew it was necessary to pick off worms about the size of your little finger as they would eat holes in the tobacco leaves, which would make them less useful as this tobacco was raised to be used for cigar wrappers, a very specialized use. Picking worms was an icky job, but necessary, and as the plants grew taller they had to be “suckered” and “topped” so that the nutrients would get to the leaves and not to the unnecessary parts of

the plant. The so-called suckers that grew where the main leaves attached to the plant and the top of the plant were not necessary and so were eliminated. Finally, the plants were ready to be harvested by chopping them down and spearing them onto a lath, five or six per lath which were then transported on a special wagon to the tobacco shed where they would hang until “case weather” appeared, otherwise known as the January thaw, which was pretty predictable. That was the time when the moist air would fill the shed and allow the leaves to become pliable, rather than brittle. Then the leaves could be stripped from the stalk and carefully placed into the tobacco case, hence, case weather. Those foggy damp days were the final thing needed to harvest a crop that was very labor intensive and took a half year to grow.

Now, what has this tobacco story to do with the stock market? Quite a lot, actually, as the market encounters many difficulties on its path to growth, somewhat like the tobacco worms and pruning the plants along the way. The market encounters many of the same things that need to be dealt with, and we won’t know if we have a successful crop until it is in the case waiting for a tobacco buyer to make an offer for your crop. And so it is with the stock market. Prices vary along the way just like the tobacco prices, and at times you want to accept the bid and sell too soon, and then at other times, you wait and it is too late as the bid no longer exists. Sound familiar? Growing a tobacco crop, or buying a successful investment takes hard work; including knowing when to sell.

THE MARKET SCOREBOARD

Clearly, an inspection of these tables shows that large-cap stocks were the leaders for the year and fourth quarter. And quite clearly, small-caps were at the bottom. It was quite a year for performance as all segments did well even if at or near the bottom.

Ranked by Q4 Return	% Return Q4 2017
Indexes	
Dow Jones Industrial Average	10.33
S&P 500 Total Return	6.64
Russell 1000 Total Return	6.59
Russell 3000 Total Return	6.34
NASDAQ Composite	6.27
Wilshire 5000	5.95
NYSE Composite	4.91
Value Line Composite	4.26
S&P Small-Cap 600 Total Return	3.96
Russell 2000 Total Return	3.34

Ranked by YTD Return	% Return YTD 2017
Indexes	
NASDAQ Composite	28.24
Dow Jones Industrial Average	25.08
S&P 500 Total Return	21.83
Russell 1000 Total Return	21.64
Russell 3000 Total Return	21.13
Wilshire 5000	18.65
NYSE Composite	15.84
Russell 2000 Total Return	14.65
S&P Small-Cap 600 Total Return	13.23
Value Line Composite	11.09

STOCK MARKET OBSERVATIONS

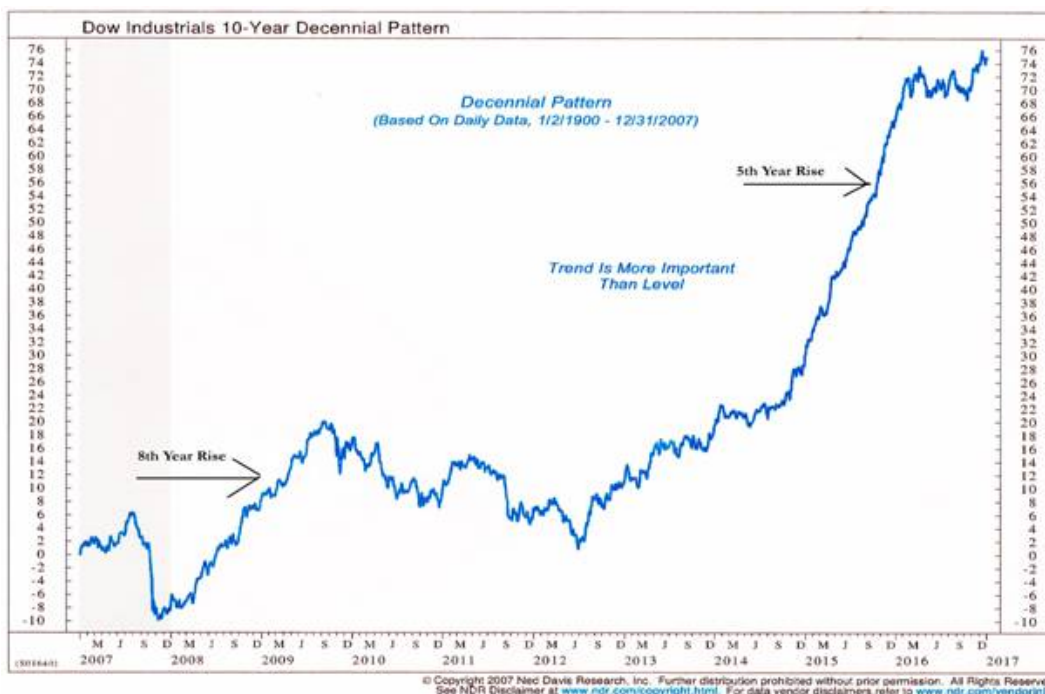
This has been a longer bull market than expected by most observers, but as shown in the chart from The Leuthold Group, the gain in the S&P 500 makes this the best bull market since 1950, surpassing the other three by a small margin. The question now is whether it



can continue. As usual, there are reasons both pro and con. Markets are said to climb a wall of worry and we started one a little over a year ago when Trump was elected president in November 2016. The expectations were very negative should he win, but you all know the story of the futures turnaround in the middle of election night when it became apparent that he was going to become president. Since then the Dow has risen by over 35% resulting in one of the greatest bull market runs in history, quite the opposite of expectations by the majority. We were optimistic, and have been, but not nearly enough in hindsight. When the market went up instead of down it was given a name: The Trump Rally. It should have been The Trump Bull Market, as it has continued, and continued, and continued. True, the Fed had a lot to do with it because of its “liquidity until infinity” loose money policy, but there is more to it than that. We think a big one is restructuring by elimination of many of the “rules & regs” that have shellacked many small businesses in America, and which was made worse by Obama. It is a one-sided affair—look how the tax bill passed without one democrat vote! We don’t want to get too political here, but when will the leaders of the left, Chuck Schumer and Nancy Pelosi, understand the disservice that they and their compatriots are doing for their constituents?

Looking back at recent letters, such as July 2017, we wrote about the likelihood of the 7th year decline, which we and many others thought quite likely, based upon history. But, as

Gerald Loeb famously said, "When you think you have found the key to the stock market, some SOB comes along and changes the lock!" That 7th inning stretch could easily have been postponed to early 2018, even though there is no precedent for that. The chart of the 10-Year Decennial Pattern (shown here) shows the 5th year is the best in the 10 years



followed by the 8th year rise, which in the past has lasted well into the 9th year. Then it is downhill until 2022 when the 40-year, 20-year, and 4-year cycles all bottom creating that launching pad for the next bull market as happened in 1942 and 1982; the 20-year cycle bottoms are in the other years ending in two as in 1922, 1962, and 2002. The chart showing this was also on page 5 of the October letter, and it shows the 4-year cycle bottoming in early 2018, so maybe we will get that 7th year decline after all, just a little late. If that happened it would be, in our opinion, a great buying opportunity as the majority will doubtless think it is the end of the bull market.

One of the services we pay for, and find invaluable, is Lowry's Market Trend Analysis which measures supply vs. demand, resulting in their Buying Power Index which has, since 1925, consistently shown the beginning of a top in a bull market. During the last four to six months, of a final high, this index shows weakness as some individual stocks dropout much like the leaves falling off trees in autumn, a warning of winter coming. As they point out, others are warning about the market because of a high P/E multiple, which will result inevitably in a bear market. They said recently that this is reminiscent of studies that show that it is impossible for a bumble bee to fly because of small wings, and a big body. Not knowing this, however, the bumble bee just keeps on flying; similarly, they say the P/E ratio may be relatively high, but a high P/E can actually be a sign of confidence and not the opposite. As they recently said, price-earnings ratios do not cause prices to

rise or fall, only buyers and sellers do. Sounds like the NRA—guns don't shoot people, people do. To close on Lowry's, at this time they have no tangible evidence of the kind of weakening investor demand that precedes a change in trend.

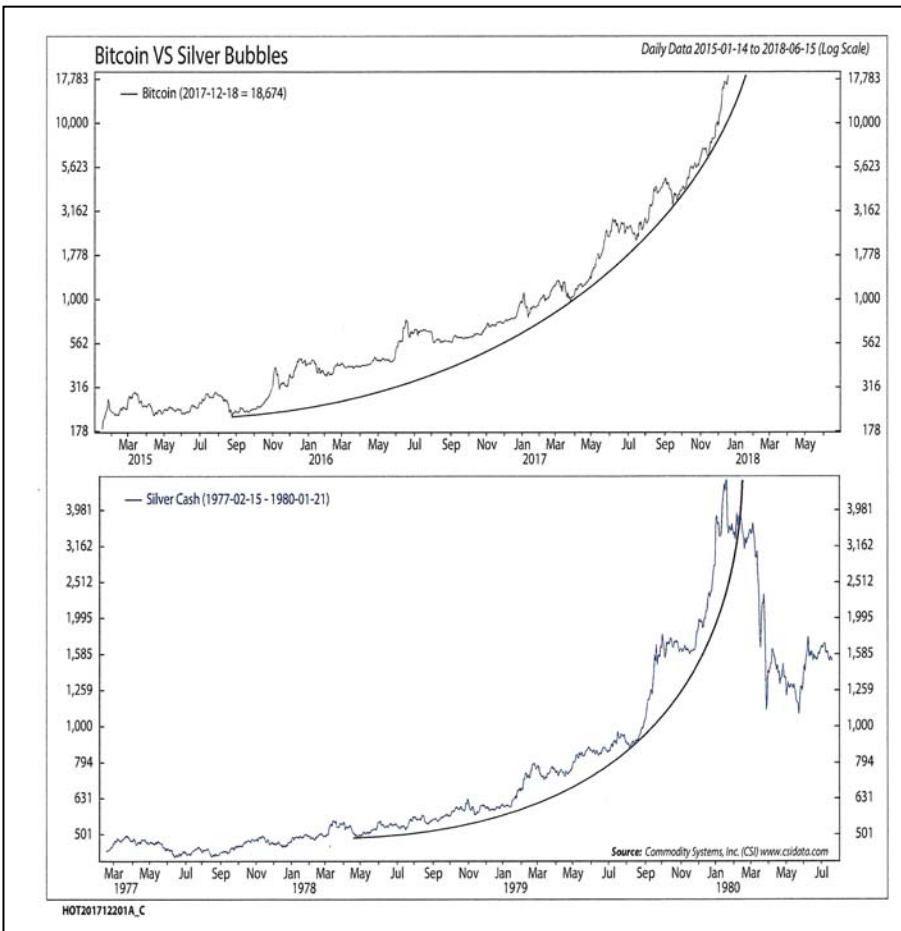
Undoubtedly, the tax bill has been a good thing for the market, and the economy, but its detractors look at its future estimated cost rather than the benefits to corporations and those who work for them, nearly everyone other than government employees. Most bull markets die by the sword of the Fed, as interest rates are raised to slow down an "over heated" economy to avoid inflation, but so far the Fed's interest rate hikes have been modest, and we do not have an overheated economy, but rather one that has been hoped for and it's finally here. Why look a gift horse in the mouth? Consumer confidence is strong, and employment is finally where we have wanted it. So no wonder the market is strong as well. There are negatives to be sure, such as a record margin debt, the result of the Fed's loose money policy. Those naysayers who are looking for a recession, which is long overdue, are overlooking that sign of a recession, a—flattening or inverted yield curve, when long rates fall below short rates. However, as Barron's recently pointed out, "investors should understand that while recessions are always preceded by an inverted yield curve, not all inverted curves are followed by a recession." Certainly, we agree with those who say the exuberant market has to a large degree been dependent upon the Fed's loose money policy, but the result has been a growing economy which provided the jobs. We agree that there will be a future time when the market will suffer, but that is not here yet, and we continue to expect a good market in 2018 and part of 2019, before we have to "head for the hills." We have had a good January so far, again putting the January barometer into play, which contends that if the first five days are up, January will be up and if January is up, then the year will be up. The famous technician, Allen Shaw, modified this adding that if the end of January is higher than the 5th day high, there is a 94% chance that the year will be up. Since 1900 this barometer has been activated 35 times and 33 were up years. Let's hope this January is one of those.

THE BITCOIN BUBBLE?

Is it possible that we are witnessing a true mania or price bubble in bitcoin, the popular cryptocurrency? We don't understand it very well, but here is some of what we know. It all started in late 2008 when Satoshi Nakamoto published a paper on a technology protocol called blockchain, whose purpose was to provide a record of exchange for a new digital currency he called bitcoin. Bitcoin could not exist without the blockchain technology, but blockchain can exist without bitcoin and it continues to be developed for use in many types of transactions. It is a distributed ledger system, which does not require a centralized server to support it, just as email does not as it runs on the Internet technology. Blockchain today contains 140 billion bytes of information, and every new transaction increases its size by adding another "block" to the chain.

Do not confuse bitcoin and blockchain; they are not the same thing. Blockchain is a technology that makes bitcoin or any other cryptocurrency possible. Blockchain technology exists without bitcoin but not the reverse. Think of bitcoin as a kind of

application that runs on the blockchain, much as the internet enables websites or email. The reason there is discussion of a bitcoin bubble or mania is that there will be a fixed supply of bitcoin as only 21 million will ever be created or “mined” and there may be less as some have been lost due to forgotten passwords. So their value is what the market for them determines—anything between zero and ????. This is what happens when there is a fixed amount of something, but a demand that cannot be estimated. Thus bitcoin itself has fluctuated from six cents at the beginning ten years ago to as high as \$20,000 in 2017. This gives you a reason to think of it as a bubble. Yet others have gone up more! The market action of bitcoin has been compared to the Dutch tulip bulb craze of the years 1634-1637 when tulips contracted a virus, which while it didn’t kill tulips altered them causing flames of color to appear upon the petals, and the color patterns varied widely increasing the rarity of each flower. And thus, people began to bid the price up according



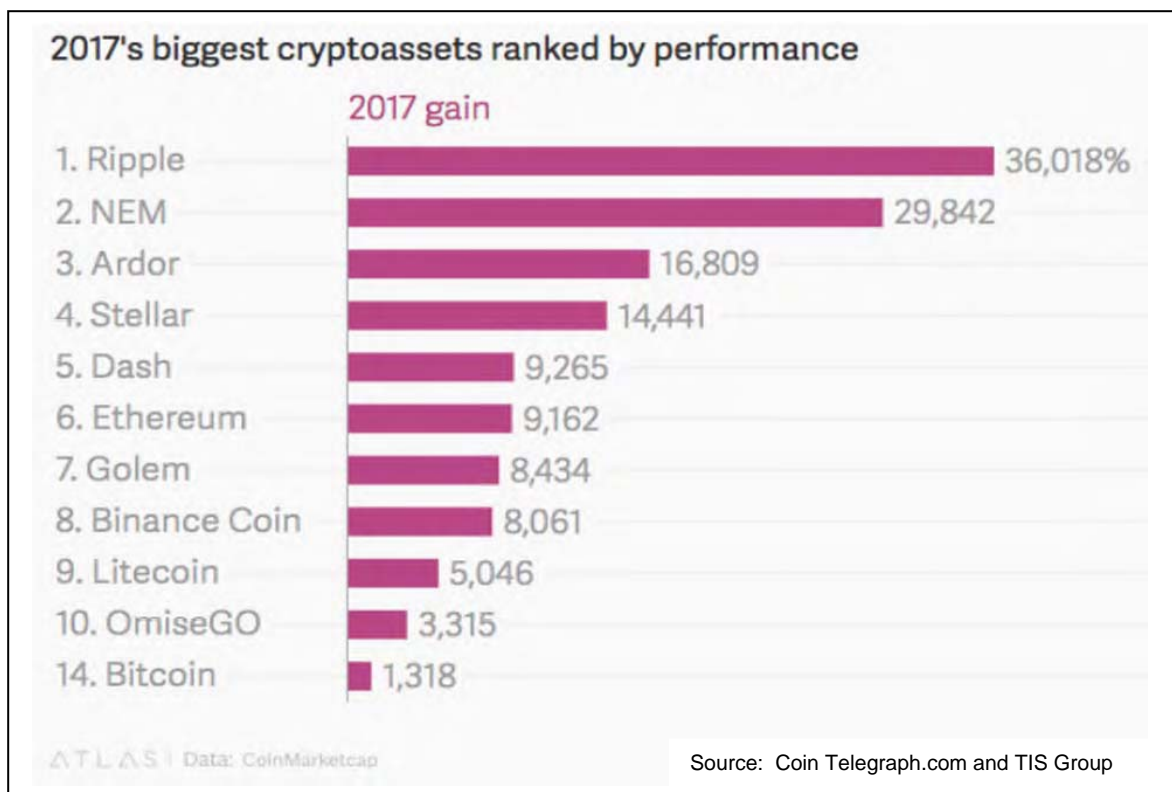
to the unique colors they saw and the speculation began. It was believed to have no limits until, of course, the amount of supply exceeded the demand. Ned Davis, of *Ned Davis Research*, has compared the bitcoin bubble to the silver bubble of 1977-1980 when the Hunt brothers of Texas had accumulated about one-third of the world’s supply of silver, and nearly went broke when the bubble was pierced by a new Comex rule, which in effect put restrictions on silver which caused it to drop dramatically. Thus a big margin call for the Hunts, but a consortium of banks provided the

credit to meet the call. While they lost over a billion dollars, they survived, although their net worth went down considerably. The Davis charts shown here indicate that although similar, the parabolic curve on silver is steeper, which may mean that bitcoin has yet to achieve that steep curve and a potential top. Only time will tell for sure.

But you can count on the fact that bitcoin will be like the tulips and silver, demand vs. supply, and when demand is greatest, prices will rise until supply overwhelms demand. We are wondering when that will happen and what the maximum amount of demand will

be vs. the 21 million or less of ultimate supply. Will the demand be there for just that particular cryptocurrency, because there are others as well. Actually, the bitcoin appreciation in 2017 was modest compared to others, as shown in the table. Each of these digital currencies seeks to do different specialized jobs. Think of them as an application for your cell phone. This is essentially what happened during the recent dot-com bubble. Today there literally is a stampede to “get in” on the craze, so companies that aren’t doing well are changing their name to benefit, such as Riot Blockchain, which had earlier been called Biopix, a pharmaceutical company that had limited success until it changed its name to Riot Blockchain and its business plan to investing in and operating blockchain technologies, including bitcoin. The stock doubled in value in the year or so before the name change, and afterwards went from \$7 to as high as \$41.75 on December 20, 2017. Others have done the same with dramatic price gains. All of this is very remindful of the dot-com days from about 1997-2001 when any company with a .com suffix went up regardless if they had any business or not. There are many examples like Riot today. Norris Communications became e.Digital Corporation in January 1999 when the stock was only a few pennies per share, but it went to an ultimate high of \$24.50 one year later. The same was true of eToys.com, Pets.com, and many more. Many of the dot-com stocks were viewed negatively, but went up anyway, killing a lot of shorts along the way.

Cryptocurrency Performance in 2017



But all of this hoopla about bitcoin and other cyber currencies hides the true value of the blockchain technology which could become a world changer way beyond digital currencies. It is being used already in financial institutions and governments, as well as foreign countries, much of which is detailed in the January issue of *Scientific American*, which we used in helping us understand this potential bubble. The January 8, 2018 issue of *IBD Weekly* also has a very good explanation of other uses for blockchain.

In light of our discourse in the beginning of this letter on ice fishing, we thought it might be fun to include a cartoon from a recent edition of *Outdoor News*.

Sincerely,



President
Senior Portfolio Manager



Executive Vice President
Portfolio Manager



Executive Vice President
Portfolio Manager

RWP:RCP:DSP/jah



JOKE PAGES FOLLOW →

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IF NOAH BUILT THE ARK TODAY

The Lord spoke to Noah and said: "In six months, I'm going to make it rain until the whole earth is covered with water and all the evil people are destroyed. But I want to save a few good people, and two of every kind of living thing on the planet. I am ordering you to build an Ark."

And in a flash of lightning he delivered the specifications for an Ark. "OK," said Noah, trembling in fear and fumbling with the blueprints.

"Six months, and it starts to rain," thundered the Lord. "You'd better have my Ark completed, or learn how to swim for a very long time."

And six months passed. The skies began to cloud up and rain began to fall.

The Lord saw that Noah was sitting in his front yard, weeping. And there was no Ark.

"Noah," shouted the Lord, "Where is my Ark?" A lightning bolt crashed into the ground next to Noah.

"Lord, please forgive me!" begged Noah. "I did my best. But there were big problems. First, I had to get a building permit for the Ark construction project, and your plans didn't meet code so I had to hire an engineer to redraw the plans. Then I got into a big fight over whether or not the Ark needed a fire sprinkler system. My neighbors objected, claiming I was violating zoning by building the Ark in my front yard, so I had to get a variance from the city planning commission.

Then I had a big problem getting enough wood for the Ark because there was a ban on cutting trees to save the Spotted Owl. I had to convince U.S. Fish and Wildlife that I needed the wood to save the owls. But they wouldn't let me catch any owls. So no owls. Then the carpenters formed a union and went out on strike. I had to negotiate a settlement with the National Labor Relations Board before anyone would pick up a saw or a hammer. Now we have 16 carpenters going on the boat, and still no owls.

Then I started gathering up animals, and got sued by an animal rights group. They objected to me taking only two of each kind. Just when I got the suit dismissed, EPA notified me that I couldn't complete the Ark without filing an environmental impact statement on your proposed flood. They didn't take kindly to the idea that they had no jurisdiction over the conduct of a Supreme Being. Then the Army Corps of Engineers wanted a map of the proposed new flood plain. I sent them a globe.

Right now, I'm still trying to resolve a complaint from the Equal Employment Opportunity Commission over how many minorities I'm supposed to hire, the IRS has seized all my assets claiming I'm trying to avoid paying taxes by leaving the country, and I just got a notice from the state about owing some kind of use tax. I really don't think I can finish your Ark for at least another five years," Noah wailed.

The sky began to clear. The sun began to shine. A rainbow arched across the sky. Noah looked up and smiled. "You mean you're not going to destroy the earth?" Noah asked, hopefully. "No," said the Lord sadly, "Government already has."

INNER PEACE

If you can start the day without caffeine,

If you can always be cheerful, ignoring aches and pains,

If you can resist complaining and boring people with your troubles,

If you can eat the same food every day and be grateful for it,

If you can understand when your loved ones are too busy to give you any time,

If you can take criticism and blame without resentment,

If you can conquer tension without medical help,

If you can relax without liquor,

If you can sleep without the aid of drugs,

Then You Are Probably, the Family Dog!

THE BATHTUB TEST

During a visit to the mental hospital, a visitor asked the director what the criterion was which defined whether or not a patient should be institutionalized.

“Well,” said the director, “we fill up a bathtub, and then we offer a teaspoon, a teacup and a bucket to the patient and ask him or her to empty the bathtub.”

“Oh, I understand,” said the visitor. “A normal person would use the bucket because it’s bigger than the spoon or the teacup.”

“No.” said the Director, “A normal person would pull the plug. “Do you want a bed near the window?”

THE CAN OF PEAS

An 80-year-old woman was arrested for shoplifting. When she went before the judge he asked her, “What did you steal?” She replied, “A can of peaches.”

The judge then asked her why she had stolen the can of peaches and she replied that she was hungry. The judge then asked her how many peaches were in the can. She replied “six.” The judge then said, “I will then give you six days in jail.”

Before the judge could actually pronounce the punishment, the woman’s husband spoke up and asked the judge if he could say something. The judge said, “What is it?” The husband said, “She also stole a can of peas.”

DISORDER IN THE COURT

ATTORNEY: "What was the first thing your husband said to you that morning?"

WITNESS: He said, "Where am I, Cathy?"

ATTORNEY: "And why did that upset you?"

WITNESS: "My name is Susan!"

ATTORNEY: "What is your date of birth?"

WITNESS: "July 18."

ATTORNEY: "What year?"

WITNESS: "Every year."

ATTORNEY: "This myasthenia gravis, does it affect your memory at all?"

WITNESS: "Yes."

ATTORNEY: "And in what ways does it affect your memory?"

WITNESS: "I forget."

ATTORNEY: "You forget? Can you give us an example of something you forgot?"

ATTORNEY: "Now doctor, isn't it true that when a person dies in his sleep, he doesn't know about it until the next morning?"

WITNESS: "Did you actually pass the bar exam?"

ATTORNEY: "Can you describe the individual?"

WITNESS: "He was about medium height and had a beard."

ATTORNEY: "Was this a male or a female?"

WITNESS: "Unless the Circus was in town, I'm going with male."

ATTORNEY: "Do you recall the time that you examined the body?"

WITNESS: "The autopsy started around 8:30 p.m."

ATTORNEY: "And Mr. Denton was dead at the time?"

WITNESS: "If not, he was by the time I finished."

ATTORNEY: Are you qualified to give a urine sample?

WITNESS: Are you qualified to ask that question?

ATTORNEY: "Were you present when your picture was taken?"

WITNESS: "Are you shitting me?"

THE BEST WITTY ANSWERS

It was mealtime during an airline flight. "Would you like dinner?" the flight attendant asked John, the passenger. "What are my choices?" John asked.

"Yes or no," she replied.

A lady was picking through the frozen turkeys at the grocery store but she couldn't find one big enough for her family. She asked a stock boy, "Do these turkeys get any bigger?"

The stock boy replied, "No ma'am, they're dead."

The police officer got out of his car as the kid who was stopped for speeding rolled down his window. "I've been waiting for you all day," the officer said.

The kid replied, "Yeah, well I got here as fast as I could."

A truck driver was driving along on the freeway and noticed a sign that read: Low Bridge Ahead. Before he knows it, the bridge is right in front of him and his truck gets wedged under it. Cars are backed up for miles.

A police car drives up and the cop gets out of his car and walks to the truck driver, puts his hands on his hips and says, "Got stuck, huh?"

The truck driver says, "No, I was delivering this bridge and I ran out of gas."

A man asks a farmer near a field, "Sorry, sir, would you mind if I crossed your field instead of going around it? You see, I have to catch the 4:23 train."

The farmer says, "Sure, go right ahead. And if my bull sees you, you'll catch the 4:11 one."

A prisoner is finally released, after many years in jail. He stands at the pavement, yelling, "I'm free! I'm free!"

A little kid walks up to him happily and joins, "I'm four! I'm four!"