

Forest Capital – Market Commentary

July 20th, 2018

Q3 2018 Notes

“It takes five years to learn how to make money. It takes twenty-five years to learn how to not lose it.”

- Nassim Nicholas Taleb

Successful investing is a function of making educated decisions (mapping probability) on where you are adequately compensated for taking risk. More often than not, at Forest Capital that means finding unique positions that are not present darlings of the financial world. We prefer boring, consistent, and stable cash flows and assets. A difficult task as most are more comfortable within the herd of the consensus (FYI - 4 stocks are responsible for 80% of stock market returns in 2018).

There are a host of poor outcomes (Dotcom 1.0, real estate 2006, Bitcoin 2018 (-70%+)) we all remember...but investors continue to make the same behavioral mistakes. Being late can be catastrophic - or the land of opportunity. After all, the 2nd mouse gets the cheese. Being patient is often the hardest part. Our job: Where is Value Today? The Major themes driving our outlook include:

- Strong US \$Dollar (improving US purchasing power)
- Growth Slowdown (China + Europe – currency moves exacerbate)
- Yield Compression in US (short rates up, long rates down = flattening yield curve)
- Watching US Growth & Inflation Rates (more likely to slow, than grow, on the margin in 2019)

Our job is to navigate macro trends (per above) and locate where the best RISK-ADJUSTED decisions/positions can be owned or purchased. Then wait. In order to protect against the uptrend in short-term rates we have held fixed to floating rate securities of firms that benefit (i.e. improving balance sheet) from rising rates.

Through Q2 2018 this decision has protected capital as the broad bond markets have had horrific relative (we are income people at heart) returns. The YTD (6/30/18) investment grade index is -4.4% (historically terrible!). Net, net we have favored America for many years, and will continue for as long as these trends remain strong.

While possible the economy could further accelerate, a moderating interest rate environment and robust corporate earnings will provide a solid backdrop for our Total Return oriented portfolios.

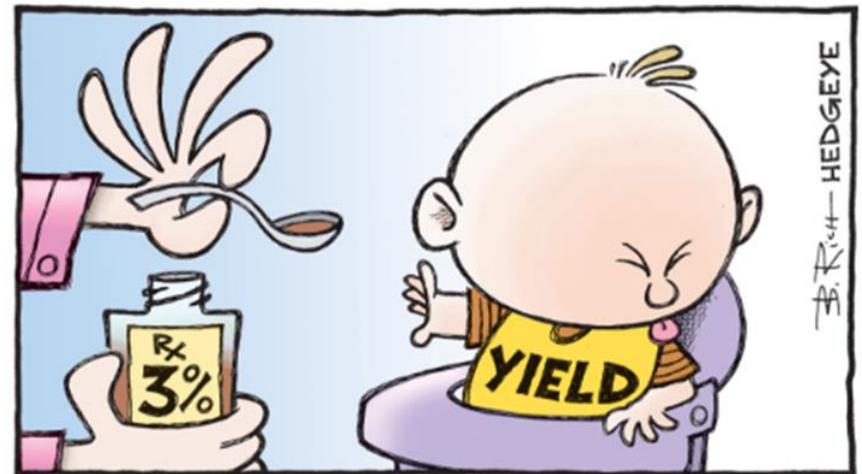
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For additional information on portfolio positioning, please contact Forest Capital directly at jbooth@forestcapital.net

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Market Commentary (*continued*)

Even after the financial media hyperbole/hysteria of “Rates Rising”, the 10-Year Treasury bond has been unable to break 3.0%. This is likely indicating a yield threshold where nominal economic growth will settle in the current cycle, yet another example of the interest rate markets being far more astute than the non-stop talking heads.



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