

April 20, 2017

Dear PCM Clients and Friends:

Weather has often been a subject on the first page of these quarterly letters, especially in the spring, when the subject is often the morel season or that special season in Minnesota that starts in spring and lasts until fall, called road repair. This year our subject will be “ice-out” of Lake Minnetonka, which is that large 14,500-acre body of water that we look at every day. Each March and April the subject in our office and many others, we are sure, turns to the question of when the ice will be out and the office pool on that subject begins. Minnesota is the Land of 10,000 Lakes, and the same question arises about the lake that is near every city or town. Here the Freshwater Society holds an annual fundraiser to coincide with the departure of the ice and the return of the loon, the Minnesota state bird. That event is going to be held April 9 of this year, but certainly that does not coincide with



ice-out which was earlier. Determining ice-out over the years has varied from visual observation to the ability to take a boat across the lake from one point to another. For a while, years ago, it was when a junker car placed on

the ice fell through. We remember this was still done on Minnetonka in the early years when we moved here. This year the Hennepin County Sheriff's Office and the Freshwater Society finally declared ice-out on Minnetonka, which now is when a boat can navigate through all the channels and into all the bays. Early in March it became quite warm and there was speculation that a new record could be set for ice-out, or at least beat last year which was second earliest on record. But no such luck, as the weather turned cold again and it didn't happen until Monday, March 27, placing this year 5th together with 1910 and 1981. The earliest date was March 11, 1878 and last year was the second earliest on March 17. We can be pretty certain about the accuracy of last year, but how it was determined in 1878 is anyone's guess, so it certainly is possible that last year was first. Nevertheless, March 27 is among the earliest considering that the median over all the years from the beginning of records is April 14. Many other lakes in the metropolitan area are smaller and set their own records this year. Perk says that Long Lake, which his house overlooks, was ice-free on March 7. There is a debate this year, however, regarding some lakes which had seen ice-out, but then froze over again during the cold spell and saw a second ice-out—so the question is which date to use.

A MESSAGE FROM PERK

One of Trump's campaign promises was more jobs here in America, all part of making America great again. He bashed Carrier, the air conditioning company, for its plan to close their Indiana factory and move the work to Mexico. Governor Pence of Indiana (now the vice president), may have had some influence as United Technologies (Carrier's parent) decided to stay in Indiana with the help of \$7 mil in tax incentives. Then they said there would be a \$16 mil investment in automation to lower costs. The United Technologies CEO told CNBC that although it would have been cheaper to move to Mexico, the Indiana plant will be made competitive through automation, and that as a result, ultimately, there would be fewer jobs. So, in the end, automation (robots) wins. The same story is told over and over in other countries, not just in the U.S., but worldwide, including China of all places. The writing is on the wall; the Boston Consulting Group says, "As U.S. factories adopt advanced manufacturing technologies, demand will surge for higher-skilled, white-collar workers who can quickly adapt to new technologies and processes, and demand will lessen for blue-collar workers who are trained in specific skills."

This all sounds dire, but the truth is automation does not steal jobs, because it improves efficiency and creates wealth, which in turn creates more jobs over the long term. Consider first the invention of the printing press about 750 years ago by Gutenberg, which morphed into an era of mass communication which permanently altered the structure of society worldwide. The Classic modern evidence to this dates back to the early 1800s when textile workers listened to Ned Ludd, and burned new textile looms that reduced the need for their labor as hand weavers. In truth, after hundreds of years of innovation, people are not massively unemployed by machines. Think about the horse. Yes, the horse. When the tractor was invented horses were not needed in agriculture, but everyone benefited and even farming continues to automate making food cheaper and more plentiful. Now crops, such as lettuce, are being harvested in California by machines which require fewer workers, but benefit the consumer by having fresh lettuce in the store sooner and cheaper. Ditto for the automobile, as horses were outmoded for transportation upon the advent of the automobile and the truck. What Henry Ford started with the first moving assembly line is today factories of robots literally building cars. Try to imagine what a Ford would cost today without robotic automation. The Luddites, i.e., non-believers in automation, are now vastly outnumbered by the optimists that see the benefits. Supply creates its own demand. Robots and automation increase supply, just as the tractor did, which lowered the price of some goods and services leaving consumers with more remaining income to spend on other items. There are countless situations like the loom business; someone's ox always gets gored. Likely, blacksmiths and buggy whip manufacturers were not happy about the automobile, but it was all part of technological change that in the end has benefited all of us whose living standards are higher than they would be otherwise. Most of the robots are made in other countries, but as time passes more will be made here. The next big thing will be the self-driving truck, which could leave thousands of drivers unemployed. Self-driving cars will really help the aged who need that mobility, as well as reduce deaths from accidents. But in the end, someone has to design the robots and manufacture them—presumably using robots with people supervising; we hope that will be here.

THE MARKET SCOREBOARD

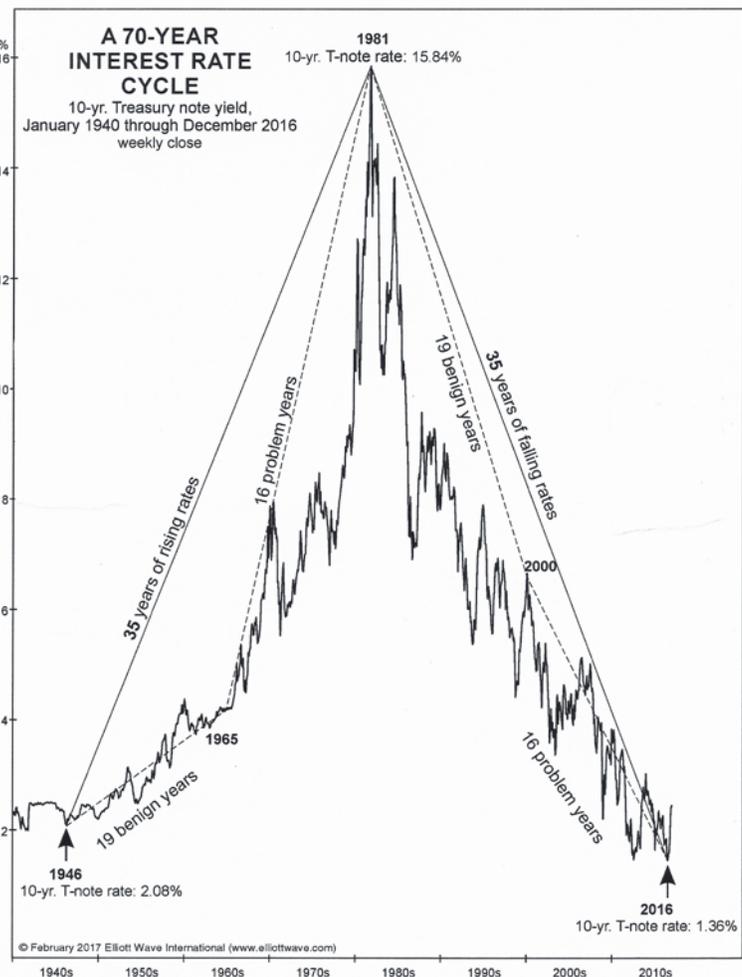
Ranked by Q1 Return Indexes	% Return Q1 2017
S&P 500 Total Return	6.07
Russell 1000 Total Return	6.03
Russell 3000 Total Return	5.74
Wilshire 5000	5.12
NASDAQ Composite	4.82
Dow Jones Industrial Average	4.56
NYSE Composite	3.94
Value Line Composite	3.74
Russell 2000 Total Return	2.47
S&P Small-Cap 600 Total Return	1.06

The first quarter returns for the averages we use in the scoreboard did not surprise us as we were well aware, as were our clients, that small-cap and micro-cap stocks in our portfolios were underperformers. Those small-cap stock averages are at the bottom of the table. The averages comprised of large-cap stocks such as NASDAQ, the S&P 500 and the Russell 1000 which were on top while those averages with a mixture of large and small, such as Value Line and the Wilshire 5000, were in the middle. The low return of the Dow is puzzling to us as the component stocks are all large.

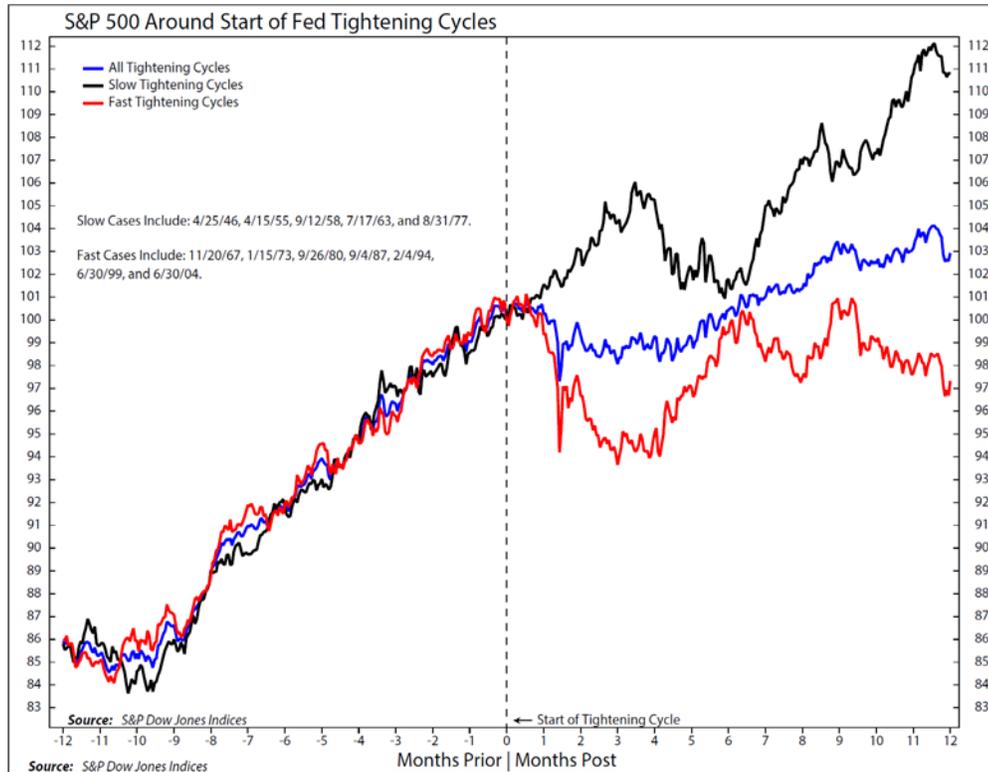
THREE STEPS AND A STUMBLE?

As expected, the Fed raised the Fed Funds rate 25 basis points or 0.25%, on March 15. The previous increases, both also 0.25%, were on December 14, 2016 and December 16, 2015. The previous increase was long ago on June 30, 2004 when rates went from 1% to 1.25% starting a string of rate hikes to 5.25% on June 29, 2006. But that was it, and rates started their downward spiral to 0% on December 16, 2008 and stayed there until the December 15, 2015 increase from 0% to 0.25%, seven years at 0%—the years of ZIRP or zero interest rate policy and QE—quantitative easing.

Interest rates, as shown in the chart, have been in a long-term decline for 35 years from 1981 when the 10-year Treasury topped out at nearly 16% and fell to a low of 1.36% in 2016.

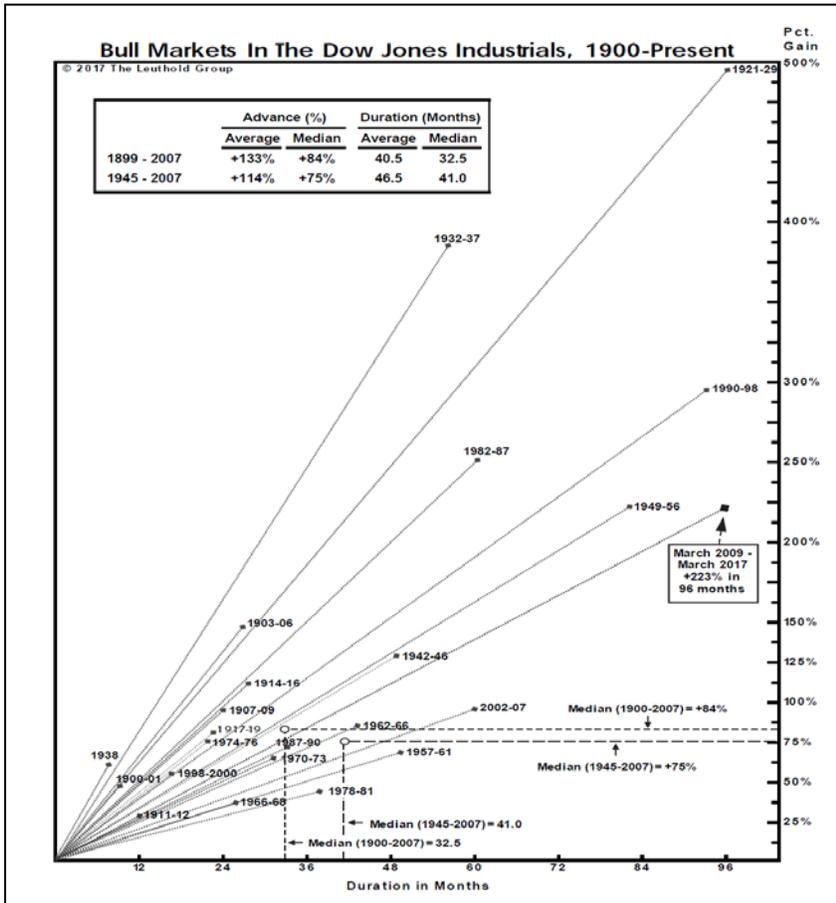


This bear market in interest rates, and bull market in bond prices, has been an amazing mirror image of the rise in rates and bear in bond prices from 1946 to 1981. Look at the chart on page three. Copy it and fold it down the middle to see that mirror image. Now three rate increases gives rise to the expectation that we are in a new bear market in bond prices and bull market in rate increases, which could put an end to the unprecedented stock market rise since 2009, starting just six months after the 0% ZIRP. As we will discuss in the next section on the stock market, we are in new record territory in terms of a secular bull market. So the three rate increases at the end of 2015 and 2016 and now in



March 2017 brings to the minds of many the Three Steps and a Stumble rule of the famous market analyst, Edson Gould, who held that when the Fed increases rates or uses another of their tools such as an increase in margin rates, three times over a short time frame, there will be a “stumble” in stock prices. Perk knew Edson Gould in the “old days” when he traveled to New York and Boston as an investment manager at the Mayo Foundation. As he has said before, the Mayo name was magic allowing access to prominent banks, bankers and advisors, such as Gould. Perk had boxes of Gould’s writings, but they got thrown somewhere along the way, probably at Piper Jaffray. While we think it is important to listen to what Gould said, our long time advisor, Ned Davis, who considers Gould to be his mentor, is of the opinion that this was in different times when rates were higher and that this time rates have gone up very slowly. The above chart, from Ned Davis Research, shows how the S&P 500 has performed during various tightening cycles. We are in a slow tightening cycle now, so while a market correction could be seen along the way, it is unlikely to be the so-called stumble. The Leuthold Group in their analysis says, “Three Steps and No Stumble, this time.”

A SECULAR BULL MARKET?



March 9, 2017 marked the eighth anniversary of the 2009 stock market low, making this market advance longer by one month than the previous advances since 1900. The chart shows all of the market advances by both duration and length. So while this market is longer it has not achieved the percent gain of the other bulls. This is shown in the following table and although this data was as of March 1, it is still reasonably accurate other than the number of months, which now would be 97; and the percent gain to March 31 would be 215.6%.

We experienced our first real correction in a while starting on March 20 when the S&P 500 declined 1.24% breaking

a streak of 109 days without a 1% correction. The table on page six shows previous streaks of days over the years without a 1% correction and market results one week, one month, and three months after the streak is broken, which has usually represented further gains ahead in the future. Of course, market circumstances were different in each of those streaks, but there still is some predictive value here. That 1.24% correction was not much, and often we will have a 5% or 10%, or perhaps even a 20% correction within a long bull market. It is a necessary

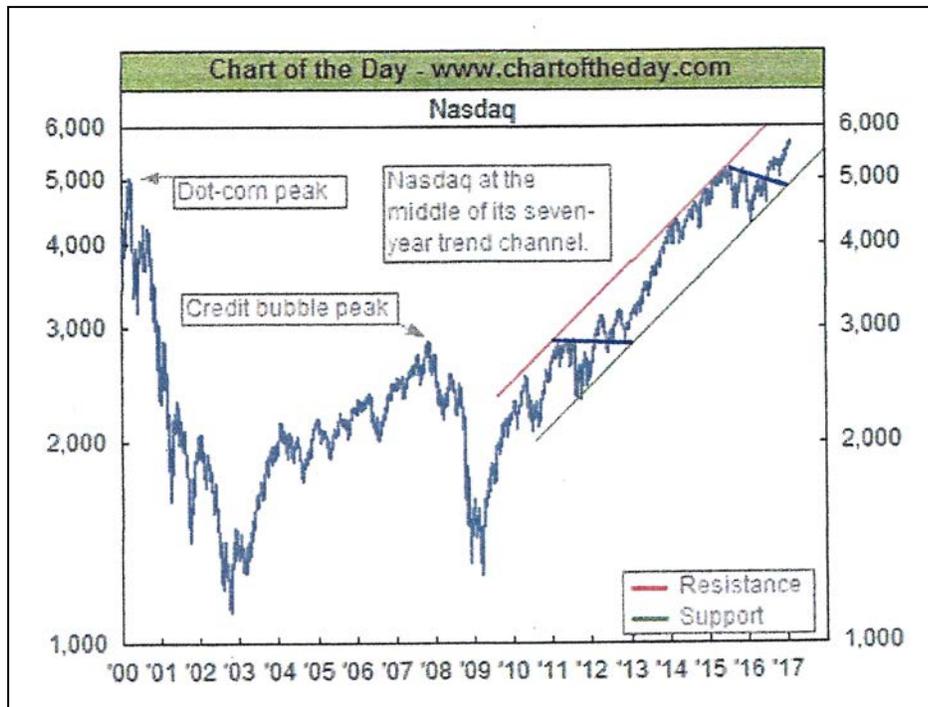
Dates	Gain (%)	Duration (Mos.)
August 24, 1921 - August 30, 1929	495.2 %	96
July 8, 1932 - March 10, 1937	371.6	56
October 11, 1990 - July 17, 1998	294.8	93
August 12, 1982 - August 25, 1987	250.4	60
→ March 9, 2009 - March 1, 2017	222.5 ←	96
June 13, 1949 - April 6, 1956	222.4	82
November 9, 1903 - January 19, 1906	144.3	26
April 28, 1942 - May 29, 1946	128.7	49
July 30, 1914 - November 21, 1916	110.5	28
October 9, 2002 - October 9, 2007	94.4	60
November 15, 1907 - November 19, 1909	89.6	24
June 26, 1962 - February 9, 1966	85.7	44
December 19, 1917 - November 3, 1919	81.4	22
December 6, 1974 - September 21, 1976	75.7	21
October 22, 1957 - December 13, 1961	75.1	52
October 19, 1987 - July 16, 1990	72.5	33
May 26, 1970 - January 11, 1973	66.6	32
March 31, 1938 - November 12, 1938	60.1	7
August 31, 1998 - January 14, 2000	55.5	16
September 24, 1900 - June 17, 1901	47.8	9
February 28, 1978 - April 27, 1981	38.0	38
October 7, 1966 - December 3, 1968	32.4	26
September 25, 1911 - September 30, 1912	29.1	12
AVERAGE	136.7 %	43
MEDIAN	85.7 %	33

and expected happening, like taking two steps forward and then one backward. Thus, a greater correction at some point would not surprise us, but when is not predictable. As shown in the January letter, the decennial cycle is clear in that the second year in the decade marks a market bottom in conjunction with the 20-year and 40-year cycle. Likewise, the 7th year has often been associated with a low, as in 1987 for example, although in a few cases that low has been postponed until early in the 8th year. Every bull market

S&P 500 Trading Days Since Last 1%+ Decline						
Last Day of Streak	Length of Streak	First 1%+ Decline	% Chg on 1%+ Down Day	% Chg Week After 1%+ Down Day	% Chg Next Month	% Chg Next 3 Mths
6/7/54	142	6/8/54	-2.24	1.73	5.65	6.81
7/26/57	115	7/29/57	-1.09	-1.38	-6.91	-15.00
5/13/58	102	5/14/58	-1.15	1.00	4.41	11.73
4/21/61	123	4/24/61	-2.08	1.20	3.54	0.71
11/20/63	184	11/21/63	-1.30	2.85	3.28	8.38
6/3/64	131	6/4/64	-1.03	1.35	5.48	4.02
2/28/66	154	3/1/66	-1.27	-2.09	-1.42	-3.32
10/31/67	104	11/1/67	-1.27	-1.21	2.58	-0.51
6/12/85	112	6/13/85	-1.22	0.76	3.99	0.85
5/17/95	110	5/18/95	-1.42	1.73	4.93	7.50
12/15/95	105	12/18/95	-1.55	1.23	0.24	5.71
3/20/17	109	3/21/17	-1.24	?	?	?
Average				0.65	2.34	2.44
Median				1.20	3.54	4.02
Avg. All Periods				0.17	0.61	1.79

has corrections; that is inevitable. At the moment, our best guess is after new highs in the averages there could be a correction late this summer or fall.

In our final letter last year we had a chart of the Dow which indicated it had plenty of room



to run. Here is a similar chart, but of NASDAQ, which shows the same picture, and clearly shows the first four waves of a five wave up sequence. We think there is ample room for significant new highs yet this year, with a correction late in the year.

We also want to give you a little bigger picture by utilizing a chart showing the interpretation of Bob Dickey, technical

analyst at RBC Capital Markets, which shows we are in a new secular bull market. We disagree somewhat with his placement of the last green box as we believe this bull started, as we said earlier, in March 2009. Nevertheless, it puts market phases in a different perspective.

Long-term market cycles 1925–2016

SSPX S&P 500 Large Cap Index Index
31-Jan-2017

The longer-term secular bull market trend is intact, and likely still early in its development, if history can serve as a guide. The two most important things we follow on forecasting are the trend and the sentiment, with investor opinions still far from any kind of euphoric state. We expect to see a time when the economic, international, and investor opinions are all much more optimistic than they are currently, and we believe the stock market will be at much higher levels before that happens.

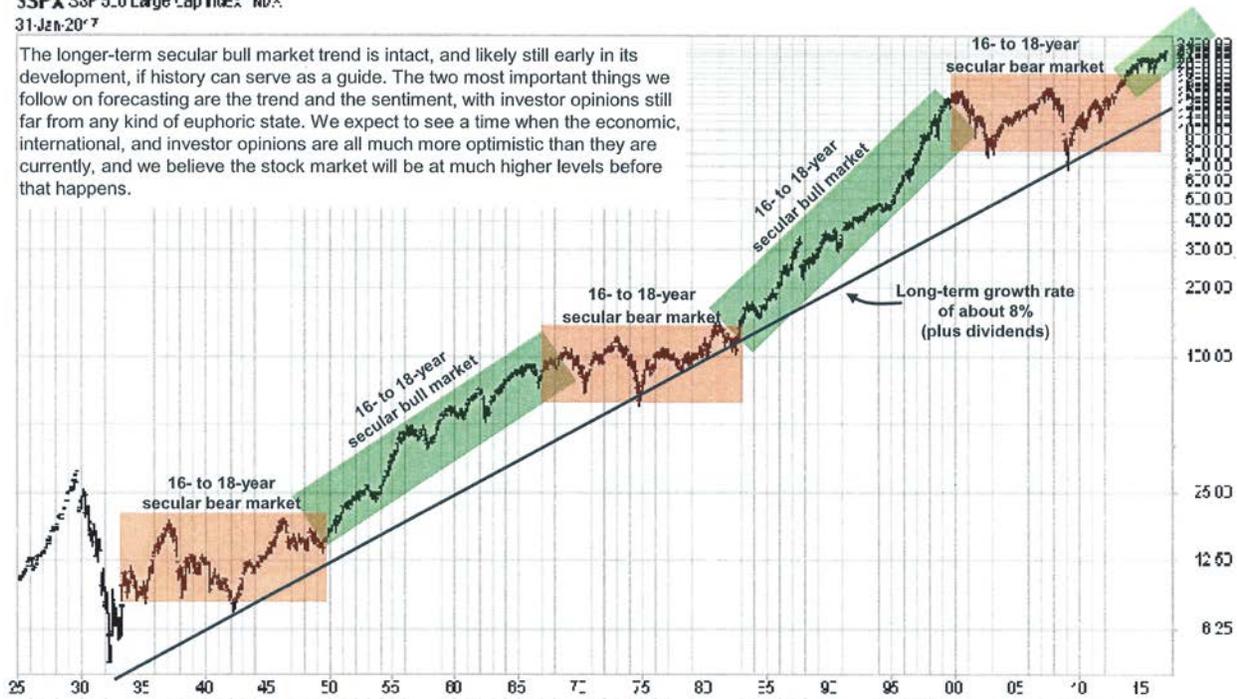


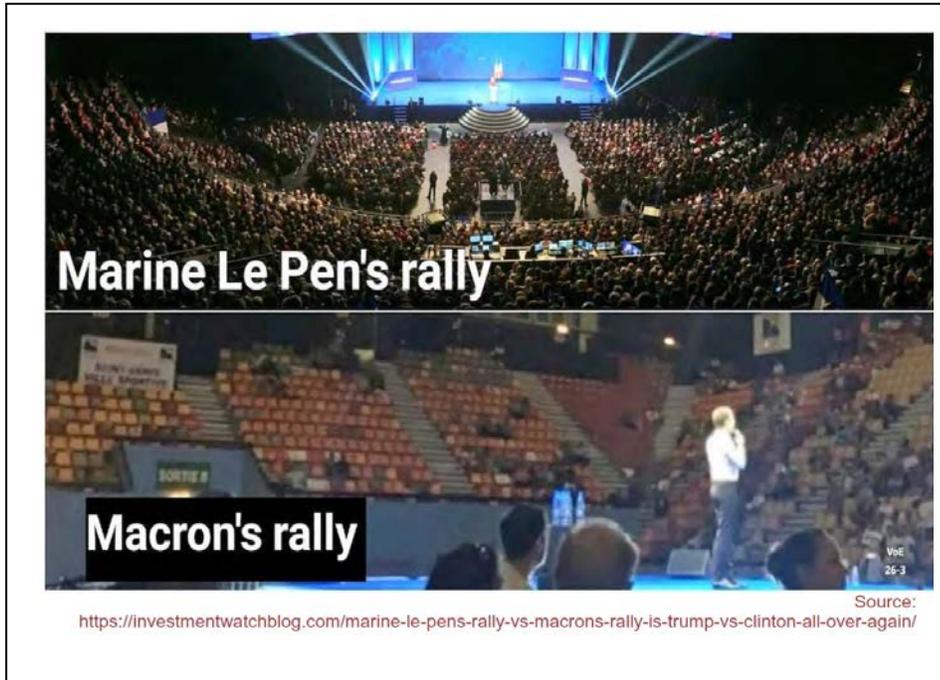
Chart courtesy of StockCharts.com and RBC Wealth Management; past performance does not guarantee future results

EUROPE’S CHALLENGING TIMES

Today, the European Union is facing multiple challenges, starting with the complicated job of negotiating Britain’s exit from the union. The Brits voted last year to exit from the EU, that famous Brexit vote. Despite the vote, some thought it would not happen and that Parliament would intervene, or there would be some other kind of divine intervention. But Prime Minister Theresa May has said “Brexit means Brexit.” It will be negotiated in Brussels by the EU under terms of Article 50, which provides rules for countries to leave the union. Recall that the Scots voted disapproval and now are planning a vote on Scottish independence in order to stay in the EU.

In the Netherlands, Geert Wilders, thought to be the leading candidate for prime minister, lost his bid in the March 15 election; he was contemplating an exit from the EU (Nexit) accusing the EU of taking away the Netherlands’ identity via acceptance of immigrants, especially Muslims. The incumbent Prime Minister Mark Rutte got the most votes, but none of the parties won a majority. But, as we know, it isn’t over ‘til it’s over. The next big thing is on April 23 when the French election is held, with another vote on May 2 between the two winners on April 23. National front leader Marine Le Pen is expected to be one of the winners and then win in the May run-off for president. She wants France to leave the

EU (Frexit) and to build an alliance with Great Britain and other countries that leave the EU. For her it is very much an immigrant problem and she is campaigning under that banner. A March survey revealed that 60% of French citizens do not feel safe anywhere



in the country, and 88% want to deport foreigners who are criminals. She was rated as the person who will do the best job of protecting the country against terrorism. Great Britain, the Netherlands, Italy, and countless others are afraid of losing their identity. The French Muslim community is the largest and fastest growing in Europe. No other European nation experienced

such a dramatic change in its ethnic and religious makeup, even if some of them—Germany, Belgium, the Netherlands and the Scandinavian countries—are not far behind. There are eleven candidates running, but only three are given a chance to get enough votes for the runoff election. Emmanuel Macron and Francois Fillon are the candidates given the best chance, with Fillon a distant third. With Le Pen's anti-immigrant stance and desire to expel convicted immigrants, all it would take is another successful terrorist attack somewhere in Europe, not necessarily France, for her to win. All this is very mindful of the Clinton and Trump battle, and the large crowds Trump got when he campaigned. The picture here of the crowd at a Le Pen rally compared to a Macron rally brings all of this back clearly. May the best crowd win!

The Russians have played their part in this election too, as Le Pen traveled to Moscow to meet Putin, while we are still debating the Russian interference in our election. It has been said that Russia actually contributed campaign money to her. What a topsy-turvy world we live in!

Success is not built on success. It's built on failure. It's built on frustration. Sometimes it's built on catastrophe."

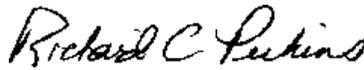
--Sumner Redstone

Failing to find a good political cartoon, and realizing that with the ice gone the fishing season begins, we thought this cartoon was appropriate. Besides, we knew that there are schools of fish, but never knew what they did in schools.

Sincerely,



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

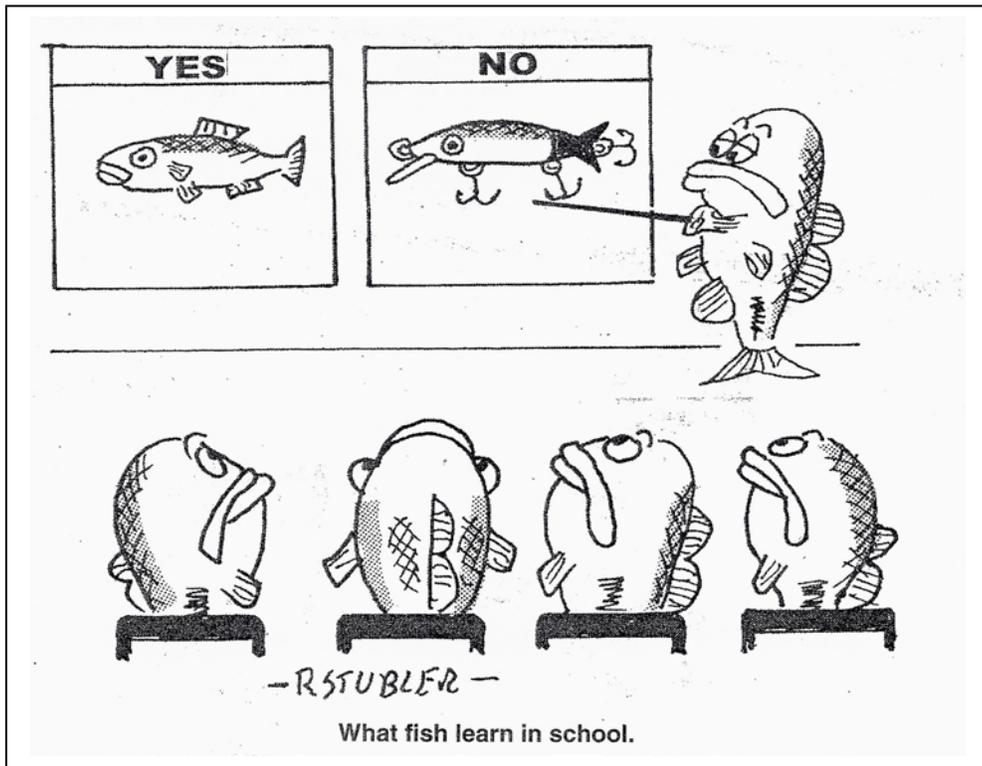


Richard C. Perkins, C.F.A.
Executive Vice President
Portfolio Manager



Daniel S. Perkins, C.F.A.
Executive Vice President
Portfolio Manager

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JOKE PAGES FOLLOW



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GOOD OLD HUMOR

A little boy was waiting for his mother. As he waited, he was approached by a man who asked, "Son, can you tell me where the post office is?" The little boy replied, "Sure! Just go straight down this street a couple blocks and turn to your right."

The man thanked the boy kindly and said, "I'm the new pastor in town. I'd like you to come to church on Sunday. I'll show you how to get to heaven." The little boy replied with a chuckle; "You're kidding, right? You don't even know the way to the post office."

Gallagher opened the morning newspaper and was dumbfounded to read that he had died. He quickly phoned his friend Finney. "Did you see the paper?" Gallagher asked. "They said I died."

"Yes, I saw it," Finney replied. "Where are ye callin' from?"

Bubba walked into a doctor's office and the receptionist asked him what he had. Bubba said: "Shingles." So she wrote down his name, address, medical insurance number and told him to have a seat.

Fifteen minutes later a nurse's aide came out and asked Bubba what he had. Bubba said: "Shingles." So she wrote down his height, weight, a complete medical history and told Bubba to wait in the examining room.

A half-hour later a nurse came in and asked Bubba what he had. Bubba said, "Shingles" So the nurse gave Bubba a blood test, a blood pressure test, an electrocardiogram, and told Bubba to take off all his clothes and wait for the doctor.

An hour later the doctor came in and found Bubba sitting patiently in the nude and asked Bubba what he had. Bubba said, "Shingles." The doctor asked, "Where?" Bubba said, "Outside on the truck. Where do you want me to unload 'em?"

Shortly after take-off on an outbound evening Air Lingus flight from Dublin to Boston, the flight attendant nervously made the following painful announcement in her lovely Irish brogue: "Ladies and gentlemen, I'm so very sorry, but there has been a terrible mix-up by our catering service. I don't know how this has happened, but we have 103 passengers on board, and unfortunately, we received only 40 dinner meals. I truly apologize for this mistake and inconvenience."

When the muttering of the passengers had died down, she continued, "Anyone who is kind enough to give up their meal so that someone else can eat will receive free, unlimited drinks for the duration of our 5-hour flight." Her next announcement came about 2 hours later: "If anyone is hungry, we still have 40 dinners available."

UNSCRAMBLE THE WORDS

PRESBYTERIAN: When you rearrange the letters: BEST IN PRAYER

ASTRONOMER: When you rearrange the letters: MOON STARER

DESPERATION: When you rearrange the letters: A ROPE ENDS IT

THE EYES: When you rearrange the letters: THEY SEE

THE MORSE CODE: When you rearrange the letters: HERE COME DOTS

DORMITORY: When you rearrange the letters: DIRTY ROOM

SLOT MACHINES: When you rearrange the letters: CASH LOST IN ME

ELECTION RESULTS: When you rearrange the letters: LIES – LET'S RECOUNT

SNOOZE ALARMS: When you rearrange the letters: ALAS! NO MORE Z'S

A DECIMAL POINT: When you rearrange the letters: I'M A DOT IN PLACE

ELEVEN PLUS TWO: When you rearrange the letters: TWELVE PLUS ONE

THE DOCTOR IS ALWAYS RIGHT

The Doctor asks: "What's the problem?"

The woman says: "Doctor, I don't know what to do. Every day my husband seems to lose his temper for no reason. It scares me."

The Doctor says: "I have a cure for that. When it seems that your husband is getting angry, just take a glass of water and start swishing it in your mouth. Just swish and swish but don't swallow it until he either leaves the room or calms down."

Two weeks later the woman comes back to the doctor looking fresh and reborn. The woman says: "Doctor, that was a brilliant idea! Every time my husband started losing it, I swished with water. I swished and swished, and he calmed right down! How does a glass of water do that?"

The Doctor says: "The water itself does nothing. It's keeping your mouth shut that does the trick."

BAGPIPER

Recently, I was asked by a funeral director to play at a graveside service for a homeless man. He had no family or friends, so the service was to be at a pauper's cemetery in the Kentucky backcountry.

As I was not familiar with the backwoods, I got lost and being a typical man I didn't stop for directions. I finally arrived an hour late and saw the funeral guy had evidently gone and the hearse was nowhere in sight. There were only the diggers and crew left and they were eating lunch.

I felt badly and apologized to the men for being late. I went to the side of the grave and looked down. The concrete vault lid was already in place. I didn't know what else to do, so I started to play. The workers put down their lunches and began to gather around. I played out my heart and soul for this man with no family and friends. I played like I've never played before for this homeless man.

And as I played "Amazing Grace," the workers began to weep. They wept, I wept, we all wept together. When I finished I packed up my bagpipes and started for my car.

Though my head hung low, my heart was full. As I opened the door to my car, I heard one of the workers say, "I never seen nothin' like that before, and I've been putting in septic tanks for twenty years."

FIRST DAY

One evening, a family brought their frail, elderly mother to a nursing home hoping she would be well cared for.

The next morning, the nurses bathed her, fed her a tasty breakfast, and set her in a chair at a window overlooking a lovely flower garden. She seemed ok, but after a while she slowly started to lean over sideways in her chair. The attentive nurses immediately rushed to catch her and straighten her up.

She seemed ok, but after a while she started tilting to the other side. The nurses rushed back and once more brought her back upright. This went on all morning. Later her family arrived to see how their mother was adjusting to her new home.

"So, Mom, how is it here? Are they treating you all right?"

"It's pretty nice," she replied. "Except they won't let you fart."

TO BE EIGHT AGAIN

A man was sitting on the edge of the bed, watching his wife, who was looking at herself in the mirror. Since her birthday was not far off, he asked what she'd like to have for her birthday. "I'd like to be eight again," she replied, still looking in the mirror.

On the morning of her birthday, he arose early, made her a nice big bowl of Coco Pops, and then took her to Adventure World theme park. What a day. He put her on every ride in the park; the Death Slide, the Wall of Fear, the Screaming Roller Coaster, everything there was.

Five hours later they staggered out of the theme park. Her head was reeling and her stomach felt upside down. He then took her to a McDonald's where he ordered her a Happy Meal with extra fries and a chocolate shake.

Then it was off to a movie, popcorn, a soda pop, and her favorite candy, M&M's. What a fabulous adventure. Finally, she wobbled home with her husband and collapsed into bed exhausted.

He leaned over his wife with a big smile and lovingly asked, "Well dear, what was it like being eight again?"

Her eyes slowly opened and her expression suddenly changed. "I meant my dress size, you moron."

The moral of the story: Even when a man is listening, he is going to get it wrong.

