

October 18, 2018

Dear PCM Clients and Friends:

The August 24 issue of *Finance & Commerce* blew us away when we read that the Wayzata Planning Committee has approved yet another condo, a 16-unit condominium called Ventana (pictured here), which replaces the eyesore pink building owned by Brad Hoyt, who had painted it pink in a fit of pique after the city failed to approve his plans for a 148-unit condo project. Evidently, the city and Hoyt have buried the hatchet, and the pink building will be history.



Also approved was an office building next door to the Ventana condo; the builder is Pat Hughes, and it will replace an office building he owns. A two-lane driveway will be between the Ventana condo and the office building for access to a parking ramp which the city

plans to build. The Wayzata Blu condo of 18 units is under construction at the corner of Barry Avenue and Lake Street East. Also under construction is the Meyer Place 21-unit condo at the corner of Ferndale and Lake Street East. As Commissioner Peggy Douglas said "We're so happy to have this block finally taken care of," which is the long block from Barry Avenue to Ferndale. We are coining the name "Condoville" for Wayzata as there are about seven condominium buildings in the Wayzata downtown area, with the structures having at least 153 units. And now one more is planned, the possibility that a new building with condos and offices will replace the Boatworks building.

But wait! Wayzata could also be called Restaurantville, and more people are needed to keep all the restaurants busy. Starting at the west

end of town there is 6Smith in the old Wayzata Boatworks building. Moving east there is Gianni's Steakhouse in the middle of the block between Broadway and Walker Avenue, and Sakana is nearby. At the northwest corner of Broadway Avenue and Lake Street is

Wayzata Condominiums

Regatta Wayzata Bay Residence	58-Units
Wayzata Place Condominiums	50-Units
The Landing Condominiums	31-Units
Garrison Landing	9-Units
Meyer Place at Ferndale*	21-Units
Wayzata Blu*	18-Units
Ventana*	16-Units

*Under construction

McCormick's Irish Pub and Restaurant. Diagonally across the street to the southeast corner is CoV, the latest restaurant in the clock tower building, a Dean Vlahos venture. Further east and across the street is Bellecour, another venture by Gavin Kaysen. Further on is Crisp & Green, where they craft a fresh salad for you, and a short distance away is Wayzata Bar & Grill, owned by the city, housed in the same building as Wayzata Wine & Spirits, so the place is commonly called the Muni. A few months ago, we would be including the District Fresh Kitchen in the Quayside building, but they have closed, soon to be replaced by The Dough Room, a pizza and pasta eatery. Further on in the Landing Hotel is Ninetwentyfive, an upscale venue. There are many smaller venues, such as Baja Haus, Benedicts, D'Amico & Sons, Jade Fountain, Maggie's, Sushi Fix, and many others. Now you can see why Restaurantville is a good description of the new Wayzata.

So, Condoville meet Restaurantville, aka Wayzata.

A MESSAGE FROM PERK

Sunday evening, July 29, I got into a wrestling match with the Vermont Country Store bathrobe which Dana gave me for Father's Day. Well, the robe won the wrestling match, and the result was a fall right on my butt. The diagnosis at WestHealth ER was a compression fracture of the L1 lumbar vertebrae. That was on Tuesday, July 31, but since I didn't realize how serious this was, I didn't go to Abbott Northwestern Hospital until the



next Sunday, August 5. Then, into a room in the spine section where among other things I was fitted for a back brace, which I learned is a standard remedy to aid the healing process; it is to be worn whenever I am up. I had a little walking therapy there every day, and then on Thursday I was moved to a rehabilitation facility called Interlude Restorative Suites, which is owned by Presbyterian Homes and Services, except for 10% that belongs to Allina Health. It is joined to the Allina West Health complex. Allina Health, by the way is also

affiliated with Abbott. Interlude is called the Ritz Carlton of rehabilitation facilities, and I can see why. It is attractive physically, with an abundance of staff, but the best thing, believe it or not, is the food. And a small world it is, as it turns out the food director, Jillian Gessell, is the youngest daughter of Lyle Gessell, who bought Dumbbell Lodge and Lake from me years ago.

I'm writing this to assure my PCM clients that it is and has been business as usual, despite the restraints of not being at the desk. As I have done for many years, I review about a ream of charts of my client holdings, as well as other market indicators on Saturday, and then I review all accounts on Sunday. Although I missed two weekends, I have been able to review charts and accounts the other weekends, including the one prior to Labor Day. I went home Wednesday, September 19, which is about halfway through the expected three-month recovery time. This is being written to assure all of my clients that this mishap will not limit my time managing their accounts.

Back at the office all is normal, with Dick managing his client accounts and Dan the Perkins Discovery Fund, our mutual fund, with assistance from Dick and me. So each of us continues to handle our specific responsibilities while, as we always have, also working together and helping each other out as needed for the benefit of all of our clients.

THE MARKET SCOREBOARD

For the first nine months the small-cap stocks did very well, with the S&P 600 and the Russell 2000 near the top; the Wilshire 5000 and Dow Industrials were near the bottom. This order was reversed in the 3rd quarter. The message here is clear—small-caps have had a good run and now large-caps are joining in.

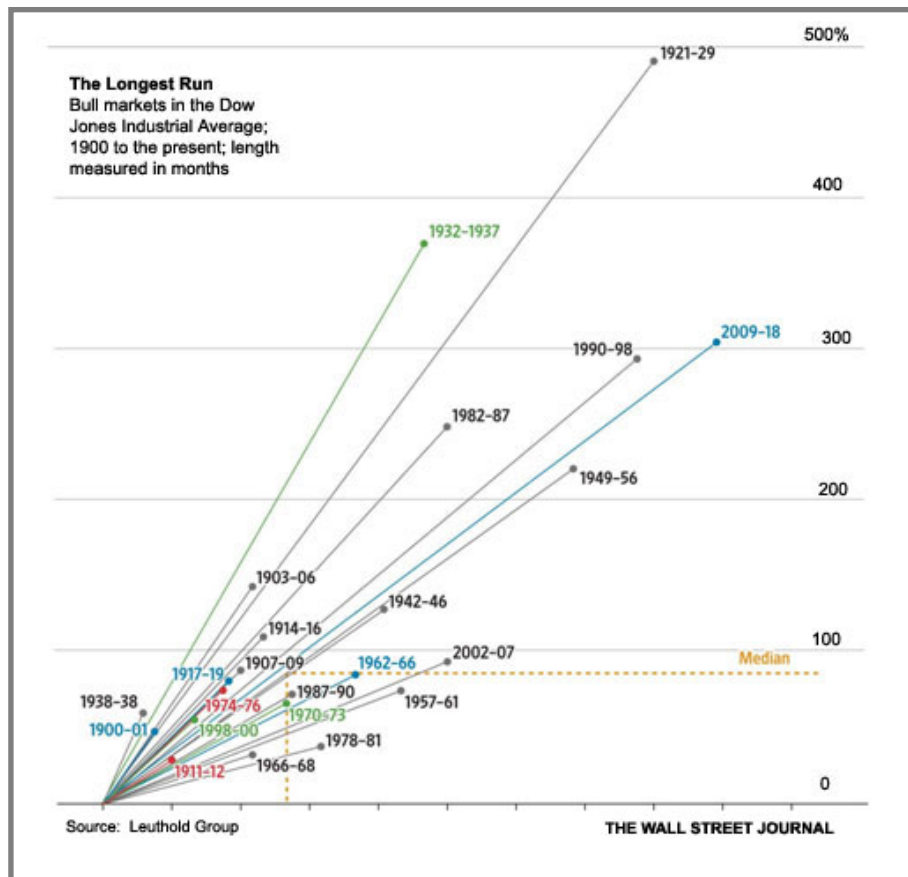
Ranked by YTD Return Indexes	% Return YTD 2018
NASDAQ Composite	16.56
S&P Small-Cap 600 Total Return	14.54
Russell 2000 Total Return	11.51
Russell 3000 Total Return	10.57
S&P 500 Total Return	10.56
Russell 1000 Total Return	10.49
Wilshire 5000	8.87
Dow Jones Industrial Average	7.04
Value Line Composite	3.65
NYSE Composite	2.14

Ranked by Q3 Return Indexes	% Return Q3 2018
Dow Jones Industrial Average	9.01
S&P 500 Total Return	7.71
Russell 1000 Total Return	7.42
NASDAQ Composite	7.14
Russell 3000 Total Return	7.12
Wilshire 5000	6.57
S&P Small-Cap 600 Total Return	4.71
NYSE Composite	4.62
Russell 2000 Total Return	3.58
Value Line Composite	2.32

OUR CURRENT VIEW OF THE MARKET

This is going to be similar to what we said in our July letter as our thinking about the market has not changed. The negative news continues—the tariff “war,” rising interest rates, the continuing immigration problem, etc., and more negatives are added each day, it seems. But the market is ignoring the negatives and instead is focusing on the good economic news. The economy grew at 4.1% in the second quarter and is expected to do

better in the third quarter at an estimated 4.3%, and unemployment is at the lowest rate since 1969. While there have been those that believe the economic recovery is in the late innings, others including us believe we could see a prolonged period of economic expansion fueled by tax cuts, a very strong labor market, and rising consumer confidence. But the debate continues about the end of this bull market and many believe that it has gone on too long, 9½ years according to a recent Wall Street Journal article. Below is a chart showing the length of bull markets from 1900 to the present. But it all depends upon



when you start counting. Ned Davis Research believes that the bear market indicator of a 20% correction is arbitrary, and therefore the current bull could have started later, much later than the count used to label this as the longest bull market. Our thought is that it is all academic anyway, as we own stocks in client accounts, and not the stock market, although in a bear market they go down in sympathy with the leaders of the decline.

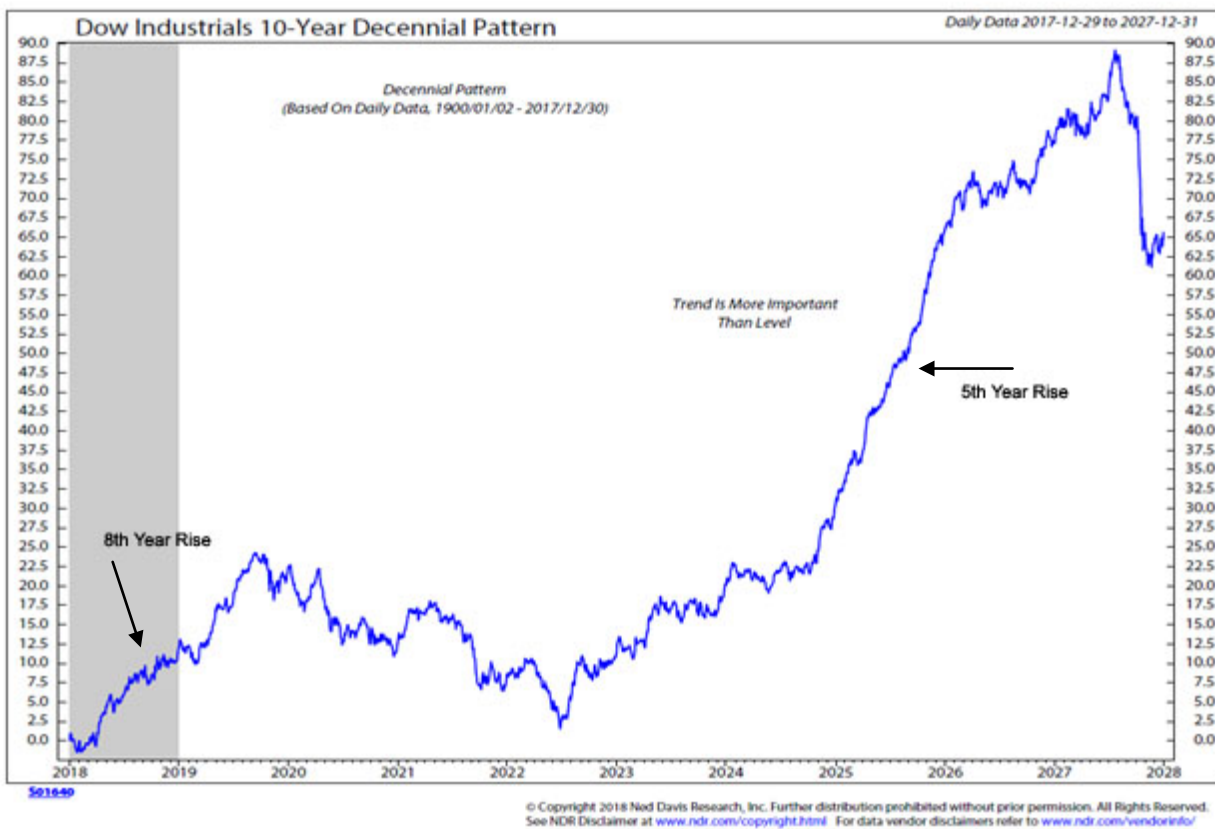
Nevertheless, the media has stressed the markets advance since 2009, by calling it the “Longest bull market on record,” and therefore, this means only one thing—it must go down. But we just got another clue that the opposite is more likely. We are talking about the magazine cover indicator which Paul Macrae Montgomery developed years ago, which took the view that magazine covers can be used as a contrary or reverse indicator. A famous example is the August 13, 1979 cover of *BusinessWeek* titled “The Death of Equities” when the Dow was at 833. The 1970s had been a bad period for the market,

and despite the negative implication, the *BusinessWeek* magazine cover of 1979 marked a turning point and stocks went on to enjoy a bull market for nearly two decades. Using the magazine cover indicator, *BusinessWeek*'s projection that equities were dead made it a contrary indicator it would become a buy signal. So now we have another, the *Bloomberg Businessweek* cover, on September 17, 2018 which should be looked at from a contrary viewpoint, namely that the market has not been up too long, as the cover implies, but rather the opposite or a continuation of the bull market.



Our readers know that we are great believers in the decennial cycle, in other words, the tendency of certain years to look quite similar to those years in the past. Looking at the Decennial Pattern, which was also in our January letter, at which time we pointed out the

5th year is the best year in the decade, followed by the 8th year which lasts into the 9th year. Then a correction until 2022 when the 40-year, 20-year, and 4-year cycles all bottom creating the 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 is here, and it shows the 4-year cycle bottoming in early 2018, and the continuation of that rise into the middle of 2019. See where we are now? Right in the middle of that rise.



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 drop out 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.

Despite the robust economy and the message from Federal Reserve Chairman Powell, in which he recently said that “This historically rare pairing of steady, low inflation and very low unemployment is a testament to the fact we remain in extraordinary times.” It would be unrealistic for us to expect the market not to have a correction from time to time. We appear to be in a bull market correction at this time, not the start of a bear market.

HEDGE(D) FUND OR ACTIVIST FUND?

Recently, hedge funds have been in the news more than ever as many of them have changed their tactics from the original concept of hedged portfolios to “activist” investing to achieve better performance. Before getting to that, however, let’s review how the hedge fund started. The original “hedged” fund was invented in 1949 by Alfred Winslow Jones when he and four friends formed A. W. Jones and Company as a general partnership. Jones was a sociologist who had turned into a writer; in 1949 he freelanced an article which reported on various approaches to the stock market. His research for that story convinced him that it was possible to make a living in the stock market and, therefore, the idea of a partnership was born. In the early years the partnership experimented with a number of investment approaches, including the idea of hedging investments by being both long and short and, therefore, being in a position to make money on both rising and falling stocks. It was from that humble beginning that the entire “hedged” fund concept was born, and as time passed employees of A. W. Jones who had learned from the master left to form their own hedged funds. But over time, the word hedged was shortened to hedge and numerous such funds were formed as limited partnerships. Two of the first were City Associates and Fairfield Partners, followed later by the Quantum Fund (George Soros) and Steinhardt Partners (Michael Steinhardt). The modern day hedge fund has made managers very wealthy, and for them is very likely the best invention since the wheel.

But recently, many hedge funds have become “activist” funds whereby a fund will make an investment in a “target” company, usually one that is perceived as a way to achieve big returns by seeking changes in the target company ranging from engaging in a fight to replace directors with their slate to the sale of the company or parts of it. Then the new directors could engineer changes that would be beneficial to the company which in turn would result in a higher price for the stock. Or they can go as far as to demand a sale of the company or at least break it up into parts for sale. As this tactic got more successful the activists got more daring by going for larger and larger prey. For example, Daniel Loeb’s activist fund, Third Point, recently took a 5.6% position in Campbell Soup, a much larger company than activists usually target. He likely sees an opportunity where some of the third and fourth generation heirs of John Dorrance, the founder, are likely to support his efforts creating this opportunity. We may not know the result for some time to come. Conversely, we know what happened when Nelson Peltz of Trian Partners took a position in Proctor and Gamble (P&G) and failed, but at least got one seat on the board. Also Barry Rosenstein of Jana Partners scored big when Whole Foods sold to Amazon, and Jana made \$300 million for its efforts in kickstarting the sale. Here in Minneapolis we have seen two successful activist efforts--Buffalo Wild Wings where Marcato Capital

succeeded by winning a bitter proxy fight and made a lot of money, and then SuperValu where Blackwells Capital won by stimulating the breakup of the company and sale of the pieces.

So today there are many different hedged strategies, but hedge activists are a larger portion now vs. years ago. The long-short hedged fund has not been as successful in recent years, prompting more to become activists and they are targeting bigger companies, presumably because the bigger they are, and if you succeed, the more you will make. Through the first half of this year there was a 66% spike in the number of activist campaigns, targeting companies with market values of \$10 billion or more.

Our closing cartoon is obviously referring to the hedge funds that have not done well in the market.

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

RWP:RCP:DSP/jah



JOKE PAGES FOLLOW →

A LITTLE PAYBACK

A wife was making a breakfast of fried eggs for her husband.

Suddenly, her husband burst into the kitchen. "Careful," he said, "CAREFUL! Put in some more butter! Oh my gosh, you're cooking too many at once! TOO MANY! Turn them! TURN THEM NOW! We need more butter. Oh my gosh! WHERE are we going to get MORE BUTTER? They're going to STICK! Careful, CAREFUL! I said be CAREFUL! You NEVER listen to me when you're cooking! Never! Turn them! Hurry up! Are you CRAZY? Have you LOST your mind? Don't forget to salt them. You know you always forget to salt them. Use the, salt! USE THE SALT! THE SALT!"

The wife stared at him. "What in the world is wrong with you? You think I don't know how to fry a couple of eggs?"

The husband calmly replied, "I just wanted to show you what it feels like when I'm driving."

AND IT CONTINUES

Two attorneys boarded a plane, one taking the window seat, and the other in the middle seat. A physician boarded and took the aisle seat. The three made small talk and thus revealed their respective professions. The physician kicked off his shoes, wiggled his toes and was settling in when the attorney in the window seat said, "I think I'll get up and get a coke." "No problem," said the physician, "I'll get it for you."

While the physician was gone, one of the attorneys picked up the physician's shoe and spit in it, and exclaimed "I can't stand those damn holier than thou doctors."

When the physician returned with the coke, the other attorney said, "That looks good, I think I'll have one too." "Again, the physician obligingly went to fetch it, and while he was gone, the other attorney picked up the other shoe and spit in it.

The physician returned and they all sat back and enjoyed the flight. As the plane was landing, the physician slipped his feet into his shoes and knew immediately what had happened. "How long must this go on?" he asked. "This conflict and jealousy between our two professions, this animosity and hatred...the spitting in shoes...and pissing in cokes?"

THE STRENGTH OF AGE

A young man at a construction site was bragging that he could outdo anyone based on his strength. He especially made fun of one older workman. After several minutes, the older worker had had enough. "Why don't you put your money where your mouth is?" he said. "I'll bet a week's wages that I can haul something in a wheelbarrow over to the other building that you won't be able to wheel back."

"You're on, old man," the young man replied. Let's see what you've got."

The old man reached out and grabbed the wheelbarrow by the handles. Then, nodding to the young man, he said with a smile, "All right, get in!"

PARROTS SAY THE DARNDDEST THINGS

A woman went to a pet shop and immediately spotted a large beautiful parrot. There was a sign on the cage that said \$50.00. "Why so cheap?" she asked the pet store owner. The owner looked at her and said, "Look, I should tell you first that this bird used to live in a brothel, and sometimes it says some pretty vulgar stuff." The woman thought about this, but decided she wanted the bird anyway. She took it home, hung the parrot's cage up in her living room and waited for it to say something. The bird looked around the room, then at her, and said, "New house, new madam." The woman was a bit shocked at the implication, but then thought "that's not so bad."

When her two teenage daughters returned from school the bird saw them and said, "New house, new madam, new girls." The girls and the woman were a bit offended, but then began to laugh about the situation.

Moments later, the woman's husband came home from work. The bird looked at him and said, "New house, new madam, new girls - old clients!"

There was once a magician on a cruise ship who performed mainly sleight-of-hand tricks. He had a regular spot on the ship's cabaret evening entertainment. He was actually quite a good magician, but his routines were regularly ruined by the onboard parrot that would fly around squawking out and giving away his secrets like: "IT'S UP HIS SLEEVE, it's UP HIS SLEEVE!" Or "IT'S IN HIS POCKET, it's IN HIS POCKET!" Or "IT'S IN HIS MOUTH, it's IN HIS MOUTH!" The magician was getting pretty sick of this and threatened to kill the parrot if it ruined his act one more time. That evening right at the climax of his act, just as he was about to disappear in a puff of smoke, the ship hit an iceberg and sank in seconds.

Amazingly, the magician and the parrot were the only two survivors. The magician was lying on a piece of driftwood in a daze. As he opened his eyes he could see the parrot staring at him out of its beady little eye. The parrot sat there for hours just staring at him and eventually said, "OK, I give up, what did you do with the ship?"

A woman's dishwasher quit working so she called a repairman. Since she had to go to work the next day, she told the repairman, "I'll leave the key under the mat. Fix the dishwasher, leave the bill on the counter, and I'll mail you a check." "Oh, by the way don't worry about my dog Spike. He won't bother you. But, whatever you do, do NOT, under ANY circumstances, talk to my parrot! I repeat, do not talk to my parrot!"

When the repairman arrived at the woman's apartment the following day, he discovered the biggest, meanest looking dog he had ever seen. But, just as she had said, the dog just lay there on the carpet watching the repairman go about his work. The parrot, however, drove him nuts the whole time with his incessant yelling, cursing and name calling. Finally the repairman couldn't contain himself any longer and yelled, "Shut up, you stupid, ugly bird!" To which the parrot replied, "OK Spike! Get him!"