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3rd Quarter 2017 Investment Review

"*Valuations make sense with interest rates where they are*"

Warren Buffett, commenting recently on CNBC television

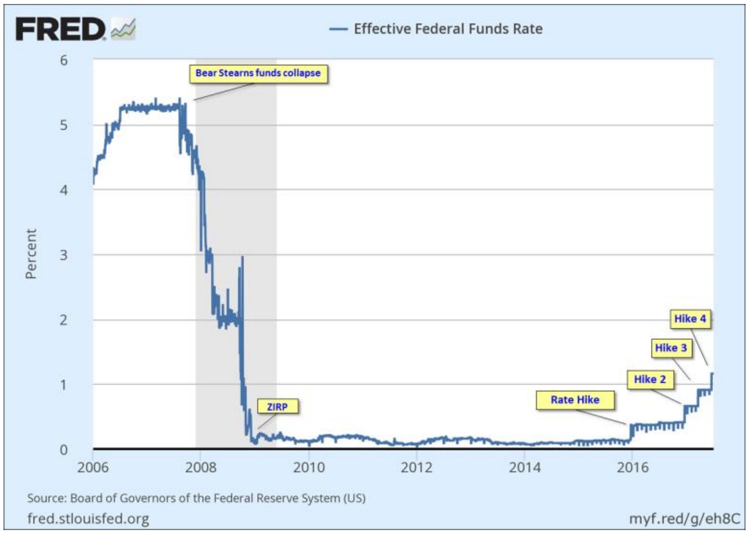
"*I am bullish about 2018 for activity. Money is still virtually free. The equity market has been very responsive to mergers and acquisitions. Prices are still high…that is very tough…but increasingly companies are looking at assets and saying, This is just strategic for me…I need to make a move.*"

J.P. Morgan Chase Investment Banker

Investment Thoughts

As the quotes above indicate, Mr. Market's party hat is still on. Mixing metaphors, there's seemingly no stopping the big rampaging bull. For investors, the past eight years has been one long stock market boom. Just buy an index fund, ETF or technology stock—Facebook, Amazon, Netflix, Google, Apple, Alibaba, Priceline, Tesla—then, sit back, relax and watch the money roll in. This stuff is easy, right? Yes, it's easy until it's not easy. As the chart below demonstrates, we're in the upper altitudes for both **stocks** and **bonds**, based upon historical valuation relationships:

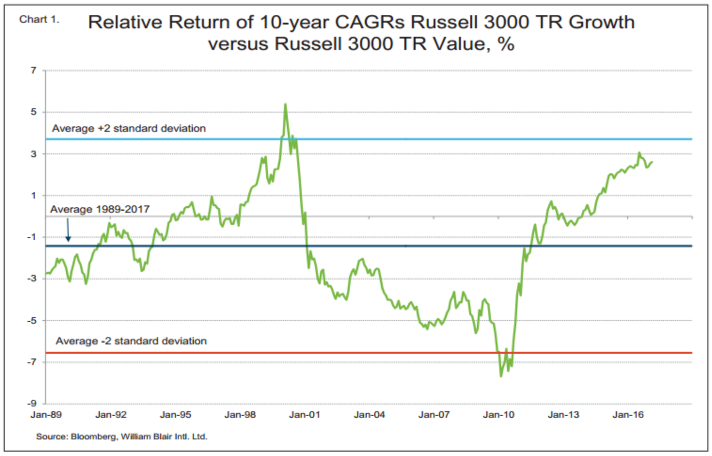
What's been particularly easy is money. Easy money made possible by a grant from your friendly Federal Reserve Board. It should come as no surprise that in the aftermath of the 2008 Financial Crisis that you'd have to go back the 1930's, in the wake of another financial earthquake called the Great Depression, to find a similar low-rate period:



In response to the Great Recession of 2008-2009 the Fed dropped interest rates to zero, where they've been until very recently. What's wrong with low interest rates? Aren't low rates good for the economy and stock prices? Even Warren Buffett seems to have recently dropped his customary caution and joined the "***maybe it is different this time***" crowd.

In our view, low rates are the magic elixir that's been responsible for elevating all manner of asset prices. Stocks, private equity, venture capital, bonds, commercial real estate, residential real estate, farms, collectibles, antiques, vintage cars, Bitcoin, artwork—you name it, it's up. Let's look at my favorite artist whipping boy, Mark Rothko, whose best known piece, appropriately and creatively titled, "*Orange, Red, Yellow*", sold for a whopping $86.9 million in 2012 to some "lucky" auction buyer. In my humble opinion Mr. Rothko's "stock" is overpriced. When rich people plunk down almost $100 million for art I could have done in second grade, you know there's too much money floating around:

The effects of sluggish growth and the resulting low interest rate environment are twofold. Those companies that have demonstrated above-average growth in the low-growth environment of the past eight years have had significant earnings growth. Investors have rewarded this above-average growth with above-average valuations, creating somewhat of a "growth stock" bubble. Sorry for the repetition, as we've shown this chart over the past few years, but the outperformance of Growth versus Value stocks is almost off the charts:



But it's not just higher growth in sales and earnings that's driving these companies and the overall stock market. There are multiple forces converging to elevate valuations toward historical highs. Low interest rates reduce borrowing costs for businesses. Companies often pay cash to acquire other companies, using cash on the balance sheet earning nothing, or borrowing from willing lenders at very low rates. In most cases, the purchase increases earnings given the low return on cash. Presto, an expensive acquisition looks good due to rock-bottom rates. As well, many companies have used cheap money to repurchase their own shares, further boosting earnings per share.

For large global businesses, especially technology and other "intellectual property" companies, the ability to dodge taxes by conveniently locating your most profitable subsidiaries in low-tax havens such as Ireland, Luxembourg and Bermuda has resulted in tax rates trending down over time, pouring more gasoline on the valuation fire.

Putting it all together, there's a multiplier effect at work. It creates an upward spiral, where investors reward higher earnings growth with higher stock market valuations. Put succinctly, investors might be placing peak valuations on peak earnings. It's happened before.

The $64,000 question? When does it end? We don't know, but over the past few years we've recycled client capital out of the more expensive merchandise. Instead, we've plowed further into the downtrodden, unloved, neglected, but still viable businesses. These companies sport valuations that haven't been puffed up by low interest rates and other temporary factors that have a chance of unwinding over the next few years, leading to heartburn for some investors.

As Chuck Prince, former CEO of Citigroup, said in July 2007, on the eve of the last Financial Crisis:

"*When the music stops, in terms of liquidity, things will be complicated. But as long as the music is playing, you've got to get up and dance. We're still dancing.*"

We're not dancing.

Economic Conditions

The good news is this economic cycle just continues to roll along, making it one of the longest on record. Europe has started to grow, and China seems to be gathering strength. The outlook seems positive for the next year, perhaps longer. The Federal Reserve has raised rates this year, and one more rate hike looks likely before yearend. More hikes are in the cards next year if the economy continues to grow, employment stays strong, and inflation remains subdued. Our concern? It probably doesn't get much better than this. And it could get worse. Employment could weaken. Inflation could pick up. Much higher interest rates would be a problem, especially for the overpriced stocks discussed earlier. We're paying close attention to signs of deterioration.

Investment Conditions

We always seek to buy a dollar's worth of value for less than a dollar. Much less than a dollar. We're not interested in buying a dollar for ninety cents. We'd prefer something closer to fifty cents for each dollar invested. Purchases at a significant discount to our estimated value provides a margin of safety in case we're wrong. Which we are at times.

Despite today's lofty valuations we continue to find enough good values to remain fully invested in client portfolios. We don't need hundreds of ideas, just a handful of new ones each year. The one thing we can count on is conditions will eventually change, which should provide more opportunities for us than is currently the case.

Within our portfolios, we have exposure to areas that should do well with further growth, including Energy, Industrials, Financial Services and Consumer stocks. We're light on Technology and Healthcare, two of the better performing areas over the past few years. Many technology companies seem richly valued to us, despite their good long-term prospects. The prospect for more government intervention and healthcare reform continues to make it more difficult to determine the winners in this area. We continue to research and wait for better opportunities in these areas.

Bond yields remain low due to interest rate suppression, and we're keeping our bond maturities very short-term while we await higher rates over the next few years. As with stocks, it requires patience and diligence to navigate a difficult fixed income environment.

While we've had positive results year-to-date, we've lagged the main market averages, as have many value-oriented investors. We believe our day will come. And it could happen relatively quickly.

Let us know of any changes to your financial situation that might suggest altering your investment portfolio and if you'd like a current copy of our SEC Form ADV Part 2.

We encourage your questions and comments. As always, ***your*** LOYALTY and PATIENCE remain our secret weapons. It's been tough over the past couple of years, but we believe brighter days are ahead.

We remain diligent, disciplined, and optimistic. And, we continue to eat our own cooking, which means investing alongside clients in the same securities—yes, even those that haven't necessarily gone up. It's the right way to operate.
Sincerely,

John

John Heldman, CFA

October 25, 2017

"Many shall be restored that are now fallen and many shall fall that are now in honor."

Horace

"Always do right. This will gratify some people, and astonish the rest."

Mark Twain

The securities discussed herein do not represent all of the securities purchased, sold or recommended for each strategy during the quarter. The reader should not assume that an investment in these securities was or will be profitable. Inherent in any investment is the possibility of loss. Past performance is no guarantee of future results.

Triad Investment Management, LLC claims compliance with the Global Investment Performance Standards (GIPS®). Triad has been independently verified by ACA Compliance Group for the period from the strategy's inception, April 30, 2008, through June 30, 2017. Triad is an SEC-registered investment adviser. The composite includes all fully discretionary separately managed accounts that follow the firm's Concentrated All-Cap Equity investment strategy, including those accounts no longer with the firm. Triad's strategy is to invest in a concentrated portfolio (usually holding 20 to 30 securities) of common stocks, unrestricted as to market capitalization, of both domestic and international companies. The U.S. Dollar is the currency used to express performance. Past performance is not a guarantee of future results, and there is a risk of loss in investing in equities. Results are presented net of fees and include the reinvestment of all income. Investments made by Triad for its clients differ significantly in comparison to the referenced indexes in terms of security holdings, industry weightings, and asset allocations. Accordingly, investment results and volatility will differ from those of the benchmarks. As of June 30, 2013, the Triad Equity Composite was renamed the Concentrated All-Cap Equity Composite. For more information or for a copy of the firm's fully compliant presentation and the firm's list of composite descriptions, please contact us at (949) 679-3991.

%	3Q 17	YTD	1 Year	3 Year	5 Year	Inception
Triad Concentrated All-Cap Equity	(1.1)	1.2	11.5	(3.3)	3.7	6.2
S&P 500 Index	4.5	14.2	18.6	10.8	14.2	9.0

As of September 30, 2017. Results presented net of management fees.