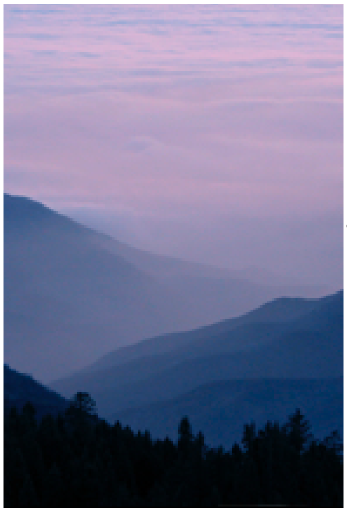


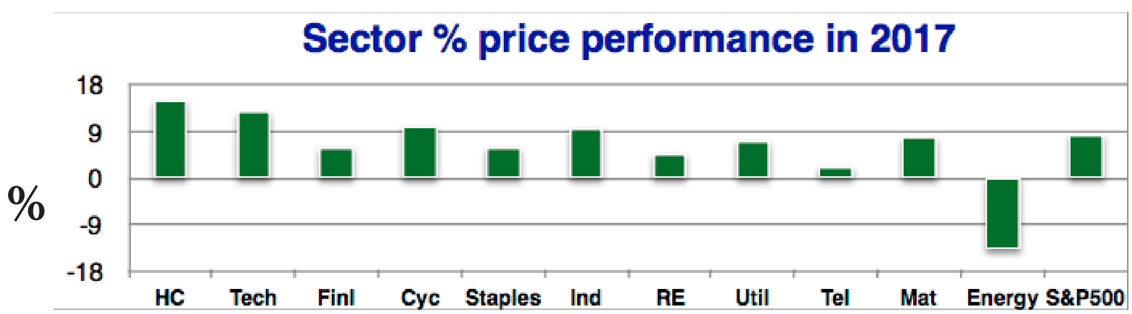
Quarterly Investment Report
June 30, 2017

Dear Investor:

With half the year completed and stocks up 9% while having made 24 new all-time closing highs, it's tempting to imagine that stocks can only go up up up. Though we believe that stocks are vulnerable to any excuse, legitimate or not, for an extended sell-off, there is good reason to believe that at this time stocks can stay this course or at least not take a dangerous dive.

S&P 500 IS UP 9% YTD ON A TOTAL RETURN BASIS (PRINCIPAL & DIVIDENDS)

Healthcare and Technology stocks are the best performers YTD
Energy is the only sector with negative returns



Stocks are discounting machines, their prices today anticipate and discount expected future earnings. After surprisingly strong earnings in the first quarter, investors are expecting continued earnings strength in the second quarter. Additionally, companies are increasing their spending and hiring. We'll need a few more quarters to make a clearer trend, but the signs are encouraging. Corporate spending is necessary to stimulate economic growth, and it signals an expectation for continued consumer demand.

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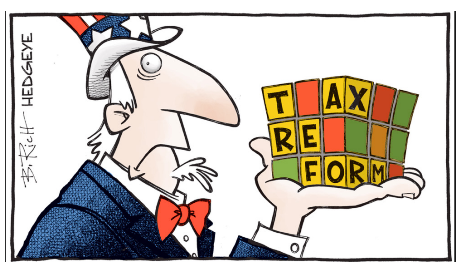
Technology and healthcare companies are traditionally the leading sectors for economic growth as so much of our innovations are in those two realms. Healthcare reform measures are coming out from the shadows just a bit. A bill may possibly see daylight in the coming weeks and as disappointing as it is that Medicaid dollars may be severely reduced, investors are reacting favorably to the possibility that Obamacare fees that were levied on pharmaceutical and medical device companies may soon be repealed. In addition to lower fees, investors remain hopeful that deregulation and trade renegotiations could boost not only healthcare and technology sectors, but the economy overall.

Today tech stocks make up 23% of the S&P 500 which is substantially higher than the historical average of 15%. That may smell like the start of a bubble but to put that into perspective, at the height of the tech-bubble peak back in 2000, technology's weight was as high as 34%. And back then a majority of tech stocks were of poor quality, whereas today the sector is highly liquid with solid and sustainable profit growth. Having said that, we sense the beginnings of a crowded trade, that is, too many investors crowding in to buy the sector at any price.

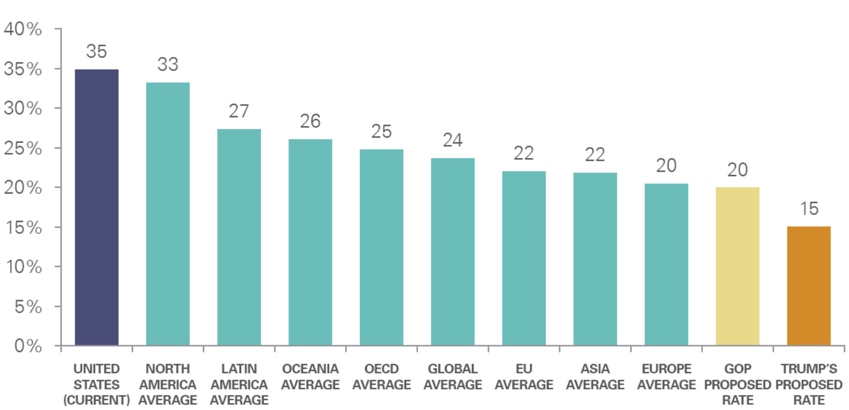
Expectations for healthcare and trade reforms, deregulations, and especially tax reform are driving this market. Republicans can hardly wait to get healthcare reform out of the way so that they can sink their teeth into tax reform. Expectations for reduced corporate tax rates have played a large role in the post-election stock market rally and contributed to an increase in business and consumer confidence.

The optimism rests on the belief that corporate tax cuts will provide a significant boost to corporate earnings. Approximately 56% of S&P 500 company earnings are domestic. At the current 35% tax rate, S&P 500 companies are paying an average effective rate of 23% and leaving approximately $2.5 trillion in cash parked overseas. A cut in the statutory tax rate to 20% would imply more than an 8% reduction in the effective corporate tax rate, lowering it to 15%.



The Current Statutory Corporate Tax Rate is 35%
The GOP Tax Proposal is to lower it to 20%

National Corporate Tax Rates



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The Federal Reserve's balance sheet strategy should also help stocks. After announcing their latest rate increase, the Fed announced that they will soon start selling $6 billion per month in Treasury securities and $4 billion per month in mortgage backed securities. They also stated that they would eventually unload $50 billion a month in assets. Their plan is to be gradual and avoid "creating market strains and to allow the market to adjust to a very gradual and predictable plan". Based on that Fed statement the 10-year Treasury bond sold off and the yield rose to 2.17%.

The Fed can't control long-term rates but it is trying to tilt the yield curve higher and counter the flattening trend we've been having in 2017. A flattening yield curve means that short and long rates are similar. It indicates that investors aren't demanding higher long-term rates to make up for an erosion in bond value that would be expected from inflation, and that they expect that the Fed still has some increases in store for short-term rates.

Flattening yield curves frequently signal that bond investors fear an economic slowdown is on the horizon and higher interest rates aren't necessary to slow things down. On the other hand, periods of robust economic expansion tend to be associated with higher long-term rates. But a flattening yield curve doesn't always portend a slowdown. Another way to look at things is that the economy will continue to chug along and that the yield curve is simply reacting to the deflation in the energy patch caused by the oil glut. If treasury bond yields stay low it can help stocks remain attractive for investors.

Bear in Mind

But before we get too giddy that we're in a "goldilocks" time for stocks, we can't lose sight of the fact that stocks are likely closer to a pull back. This bull market is the second longest in history and trading at high valuations. Anything - from failed domestic policies to surprising inflation spikes to unexpected war - can set off a market correction.

When one is literally in bear country the rules are to stand your ground, make yourself appear as large as possible, speak loudly, and above all to not panic or run. You can't outrun a bear (they can run 30 miles per hour) and running marks you as vulnerable and can potentially trigger a predatory chase and attack response. The rules are pretty much the same in metaphorical bear country. When hungry bears have been hibernating for too long it's best to own stocks that are "large and loud" in their industries, ones that can most ably stand their ground when the bear crosses ones path. That means you don't sell and run, but rather wait for the bear to lumber off…as long as it takes.

Happy Fourth of July!

Sincerely,

Ellen P. Le, CFA
President

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HAPPY 10TH BIRTHDAY, iPHONE!

(10th anniversary of its first sale on June 29, 2007)

It's astonishing to think that before 2007 our world looked like this…

Fast forward 10 years as capabilities have rolled into one ubiguitous device...

...and shareholders have been richly rewarded.