Gore Capital Management

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Earnings season yet again nears its close, and it's been an awfully good one. Through the middle of August, about 90% of S&P 500 companies have released their 2nd quarter earnings reports. Of that group, about 3/4ths have reported positive revenue and earnings surprises, both of which are above their respective five-year averages. The average earnings growth rate is just under 25%, which is the second-highest rate since 2010 (data from Factset). The technology sector remains a bright spot, with companies like Apple, Microsoft, and Google reporting stellar results. Conversely, the energy sector had the greatest number of negative earnings surprises as the price of oil fluctuates wildly on geopolitical tensions around the world.

The disparity in performance between the stocks of large companies and small/medium-sized companies continues to be a story to watch, though the coin has flipped in 2018. Through the end of July, the Russell 2000 small cap index is +9.3% year-to-date, while the S&P 500 large cap index is +6.1% over the same timeframe (data from Morningstar). Smaller companies tend to pay higher average tax rates than larger ones, but the Tax Cuts and Jobs Act has given them a huge leg up on profitability potential and their stock shares have been rewarded handsomely this year. Small companies also do most of their business inside the United States; a strong domestic economy means more business, meaning more revenue, meaning more profit (especially when combined with lower taxes). This is a double-edged sword, however, and if (or when) we enter the next recession, those smaller companies will suffer the effects of slowdown more than their larger peers. Another reminder of the importance of disciplined diversification and rebalancing.

In other stock-market related news, Apple became the first publicly traded company to cross the trillion-dollar market capitalization valuation threshold. Amazon, the second-most-valuable stock, is nearly 10% behind at a measly $900 billion. Exxon Mobil, the most valuable company a decade ago, currently has a market cap about a third of the size of Apple's. Although the "trillion dollar mark" doesn't really mean much in and of itself, it is a stark reminder of the increasingly prominent role technology plays in our lives as well as the influence the sector has on the stock market as a whole. Assuming we define Amazon as a technology company (as opposed to a retailer), the five most valuable companies by market cap, and thus the five largest components of the S&P 500 index, are all now tech names: Apple, Amazon, Alphabet (Google), Microsoft, and Facebook.

News of the quarter

We are pleased to announce that Ben has passed all three levels of the Chartered Financial Analyst® program. In addition to the rigorous academic aspect, earning the CFA charter demonstrates a commitment to the highest ethical standards of practice. It is estimated by CFA Institute that less than 20% of those who begin the CFA program are able to complete it and earn the right to use the designation.

Market Statistics	2Q 2018	YTD (as of 7/31/18)	2017	3-Year Annl.	5-Year Annl.
S&P 500	3.28%	6.13%	21.10%	11.23%	12.72%
Dow Jones Ind. Avg.	1.26%	4.07%	28.11%	14.07%	12.96%
Russell 2000 (Small Cap)	7.66%	9.33%	14.21%	10.52%	12.02%
MSCI EAFE (Foreign)	-1.24%	-0.36%	25.03%	4.90%	6.44%
MSCI ACWI (Global)	0.53%	2.57%	23.97%	8.19%	9.41%
MSCI Emerg. Mkts. Equity	-7.96%	-4.61%	37.28%	5.60%	5.01%
Barclay's Aggregate Bond	-0.16%	-1.59%	3.54%	1.72%	2.27%
S&P GSCI Gold (Spot)	-5.48%	-5.78%	13.68%	2.30%	0.50%

Source: Morningstar

Looking at the broader economy, the US printed a 4%+ GDP figure in the second quarter for the first time since 2014. The first quarter estimate was also revised higher to 2.2%. Consumer spending on goods and services, as well as business investment, printed higher than last year's averages. Looking forward, the Federal Reserve believes the rest of the year will play out similarly, making 2018 "the best calendar year since 2005" (source: Wall Street Journal, 7/27/18).

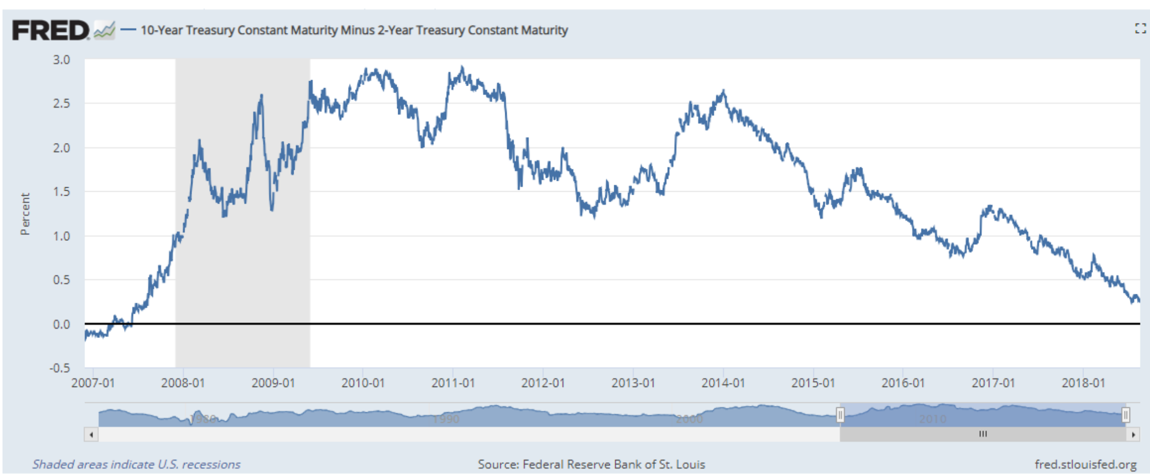
It should be noted, however, that not all signs point to clear skies ahead. Analysts use the difference in interest rates between long-dated bonds and short-dated bonds, commonly called the "spread," as a predictor of economic slowdown. Historically, recessions are preceded by a narrowing and even inverted spread (meaning shorter bonds actually pay higher yields than longer bonds) as the Federal Reserve raises short term rates in response to inflation, but investors demand longer-dated, higher-quality securities. The accompanying chart from FRED (the Federal Reserve's economic research arm) shows the steady decline in spread between 10-year bonds and 2-year bonds over the past 11 years. The spread is currently hovering around its lowest level since late 2007. It is a gross oversimplification to merely state, "spreads are narrowing, thus a recession is imminent," without considering a number of other data points and indicators, but it does raise a cautionary flag suggesting that this expansion could be near its end.

In politics, mid-term elections are fast approaching and we don't have the foggiest clue which way the winds are blowing. FiveThirtyEight is predicting that the GOP will lose the House but it is likely that they will keep their majority in the Senate. Legislative gridlock seems to be par for the course now, regardless of who controls what portion of our government. If anything, we wouldn't be surprised to see the partisan gap widen further during the next Congressional session as intra-party disunity seems to be affecting Democrats and Republicans alike. We are seeing a number of younger, non-career politicians entering House races around the country, some of whom are having success against incumbents. It will be interesting to see how they fare in November.

We hope you had a wonderful summer and we wish you a cool, calm autumn.

All the best,

Peter, Ben, & Keri



GCM's Top Holdings	2Q 2018	YTD (as of 7/31/18)	2017	3-Year Annl.	5-Year Annl.
PIMCO Income (PONPX)	-0.46%	-0.22%	8.49%	5.22%	5.81%
FPA Crescent (FPACX)	0.32%	3.31%	10.39%	5.79%	6.89%
Litman Gregory Masters Alt (MASFX)	-0.03%	0.60%	4.51%	2.82%	3.43%
Vanguard Mega Cap Value (MGV)	1.20%	3.55%	16.79%	10.35%	11.45%
First Eagle Overseas (SGOIX)	-1.88%	-1.59%	14.37%	4.33%	5.67%
T Rowe Price Blue Chip Grwth (TRBCX)	5.71%	14.13%	36.55%	17.16%	18.76%
Dodge & Cox Stock (DODGX)	2.76%	5.60%	18.33%	10.95%	12.81%
Virtus Seix Floating Rate (SAMBX)	0.50%	2.75%	3.87%	4.02%	3.84%

Source: Morningstar

Ben's Corner

For my birthday this year, my poor, poor wife agreed to accompany me to Bristol, TN for a NASCAR race. The town of Bristol, which actually straddles the border of Virginia and Tennessee, is home the third largest sporting venue in the United States: Bristol Motor Speedway. In NASCAR's heyday, the Speedway would easily sell out all of its 160,000 seats and the noise level would exceed 140 dB as the unique shape of the stadium actually intensifies the cacophony. We estimated it was about 50% capacity for our race, a sign of sinking attendance that plagues not just auto racing but several other major professional sports leagues as well.

Outside of NASCAR and Formula 1, my wife and I don't follow many sports (yes, she likes racing more than she will admit). We watch the occasional football or ice hockey game and the big tennis tournaments from time to time, but that's about it. And it seems like we are slowly becoming the norm rather than outliers. Disney has been reporting lower revenues from its basket of ESPN channels, TV ratings for major sporting events are generally on the decline, and ticket sales aren't what they used to be. So what's going on? The blame is often laid on Millennials for simply not being interested in sports, but that may not be the full story.

Consulting firm McKinsey released an interesting article last October suggesting the problem is not that Millennials don't follow sports, but that they watch sports in different ways. Rather than sitting down for a full 3-hour football game, Millennials will check Twitter for score updates or quick clips of the exciting plays. They'll watch recaps on Youtube that condense the game into a 5-minute highlight reel, effectively skipping not only the boring parts of the game but also the ceaseless series of ads for razors and Doritos. They'll play fantasy football with their friends, the sports version of social media. They're still invested, but in ways that traditional ratings metrics do not capture accurately.

There's also the trend of "cord-cutting," or eliminating cable television subscriptions in favor of internet-only packages and a-la-carte services like Netflix and Hulu. From this perspective, I do think Millennials (as well as members of other generations who have cut the cord) are less engaged because there simply aren't many sporting events available to watch without network television or the big cable stations. We cut the cord for about two years, only returning because Cox gave us an offer we couldn't refuse, and watched very few sporting events during that period of time. I'm not sure why major sports leagues haven't jumped on "the whole internet thing" sooner, but it seems like they're all behind the 8-ball when it comes to attracting the cord-cutting crowd.

I admit the argument is far more nuanced and complex than can be fully captured in a few hundred words on a single page, and I can appreciate that it's difficult to simultaneously attract the traditional TV fanbase and the younger internet fanbase, but there has to be a way to do it. It's simple math – make sports more accessible to more people and more people will watch them.

Market Movers	2Q 2018	YTD (as of 7/31/18)	2017	3-Year Annl.	5-Year Annl.
Alphabet (GOOGL)	8.88%	16.50%	32.93%	27.88%	13.97%
Amazon (AMZN)	17.44%	51.99%	55.96%	57.62%	43.67%
Apple (AAPL)	10.76%	13.25%	48.24%	15.29%	28.17%
Chevron (CVX)	11.85%	2.65%	10.03%	13.06%	4.54%
General Electric (GE)	1.85%	-20.52%	-42.12%	-15.41%	-5.11%
JP Morgan Chase	-4.74%	9.06%	26.30%	17.56%	16.48%
Microsoft (MSFT)	8.50%	24.99%	40.22%	32.71%	25.01%
Verizon (VZ)	6.44%	0.91%	3.51%	7.06%	4.08%
Visa (V)	10.90%	20.29%	47.03%	26.02%	24.24%

Source: Morningstar

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