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Charles W. Fish
Chairman and Chief Investment Officer

April 5, 2018

Letter from the Chairman…

"Life isn't about waiting for the storm to pass.
It's about learning to dance in the rain." – VIVIAN GREENE

When I first read this quote about life, I was struck by how appropriate it was for portfolio management. Financial storms are inevitable to be sure. Accurately predicting them, their directions, and their impact is unachievable. And then there's the fact that just because a storm passes, doesn't mean another isn't just around the corner. To paraphrase John A. Shedd; Ships aren't designed to sit safely in the harbor. Hopefully they are constructed to handle all kinds of sea conditions. Collectively, interest rate forecasters, including those at the Fed, have been wrong more than half the time. Sitting in cash or their equivalent for long periods costs too much. The chances that interest rates will leap to high enough levels for one to catch up with those skilled at dancing in the rain (and happy to do so) are miniscule.

Compare an investor earning 3% annually for 10 years to one who, fearing the storm, stays very short earning only 1% on average for the 5 years. To catch up to our first investor, they would need to earn 5% in each of the subsequent 5 years. If they continued to stay short for 2 more years, 7.75% would be required in the remaining 3 years to catch up. Like geography, credits, coupons, call features, legal structures, etc., maturities need to be diversified. Staying 100% in the short end of the market, like being all in the long end, presents huge risks and will deprive a portfolio of the flexibility needed to optimize returns. A reasonable guideline for an individual municipal bond portfolio in today's market would be to deploy 30% to 40% of one's positions 5 years and under, with a total of 70% maturing within 12 years.

Considering all the global tensions and the recent tax legislation that went into effect only days after becoming law, the municipal market has behaved remarkably well. Its' stability is in stark contrast to the volatility witnessed in the stock market recently. The yield curve continues to flatten, there is plenty of demand for new issues, and real-disposable income is slowly growing. The bond bears are quick to point out the Fed's plans for rate hikes and portfolio unwinds, the Treasury's plan to issue $500 billion more debt this year than last, and that wage growth is poised to surge, pushing inflation well beyond the Fed's target. Bond bulls, on the other hand, point out that the velocity of money has declined to its' lowest level since 1949, saving is at its' lowest level in 10 years, growth in employment is poised to decelerate, that corporations' post tax legislation windfall will mostly go to M&A and stock repurchase programs, while trade tariffs presage a global recession. Each side has dozens of supporting arguments to offer, but the one certainty that emerges is that polarization looms larger than at any time since the Civil War and is poised to intensify as mid-term elections approach. It seems only a national emergency can bring all sides together. Regrettably, once the emergency passes, someone will fire three shots* and the warring sides will be at it again.

**It is tradition at American military funerals that a three-shot volley be fired. This tradition dates from our Civil War when both sides would agree to a ceasefire for a few hours so the dead could be cleared from the battlefield. The firing of a three-shot volley indicated that the task was completed and hostilities could resume.*