



January, 2018

## Long Term Optimists

As we enter 2018, our optimism on the economy and corporate profitability contrasts with our outlook regarding returns from the financial markets. We currently see an expanding global economy, acceleration in profit growth heightened by US tax reform, expansive fiscal policy, moderate global monetary tightening, and expensive valuations across most asset classes. Price momentum and investor sentiment are reaching peaks not seen since the 1999 tech mania.

We know two things for certain: first, sentiment and valuation are poor timing tools. Second, forward returns will be muted from this era of low fixed income rates and expensive asset valuations. For us and our investors, it is time to lower both our risk profile and our future return expectations.

This year brought both personal and professional milestones. KLCM turned 25 and a couple of us reached significant age landmarks. Given these events we have chosen to be a bit more concise and reflective on the key long term drivers of the economy and markets, knowing full well that our primary charge is to make investment decisions that are relevant for long term investors.

Our optimism has absolutely nothing to do with the current economic or business cycle, valuation of stocks, or our view on interest rates. This optimism is rooted in a longer term historical perspective and the observations we have made about free markets and our system of capitalism. Perhaps it has taken nearly a full working lifetime to fully appreciate this system and the human spirit that drives it. This recognition, while tardy, is best described by Churchill, **“There is no limit to the ingenuity of man if it is properly applied under conditions of peace and justice.”** While far from perfect, conditions globally are better positioned today for economic growth and personal freedom than at any other time in human history.

Today, there are more open societies providing basic human rights to individuals than at any time in history. We live in an age of personal and economic freedom enhanced by an ever expanding base of knowledge and capital. It is this backdrop and the facts of economic well-being, literacy, life expectancy, and a myriad of other objective data points that support our view. This has been a golden period. Our responsibility as a society is to first understand our good fortune and then guard the principals that make this prosperity possible.

Our rhetoric may sound a bit pollyannaish, for that we apologize. We know that growth and the fruits of this growth are not linear, nor are they shared equally. However, if history teaches us anything, it is that growing the economic pie is far more important to the human condition than how the growing pie is sliced. It is incumbent on those of us that happen to be in the right place at the right time to understand our good fortune and share it with others. Hubris and greed are unappealing character traits.

It has been a good run, we recognize and appreciate that we inherited a system that makes these opportunities for growth and prosperity possible. We must nurture and protect these liberties if we are to pass on this prosperity to future generations. We control our own destiny. **We are Long-Term Optimists!**