**SACAJAWEA & COMPANY, LLC**
**Economic & Financial Research**

**William H. Wrean Jr., M.A.**
**William H. Wrean, Ph.D.**
**148 Linden Street, Suite 204**
**Wellesley, Massachusetts 02482-7904**
**Telephone 781-237-9290**

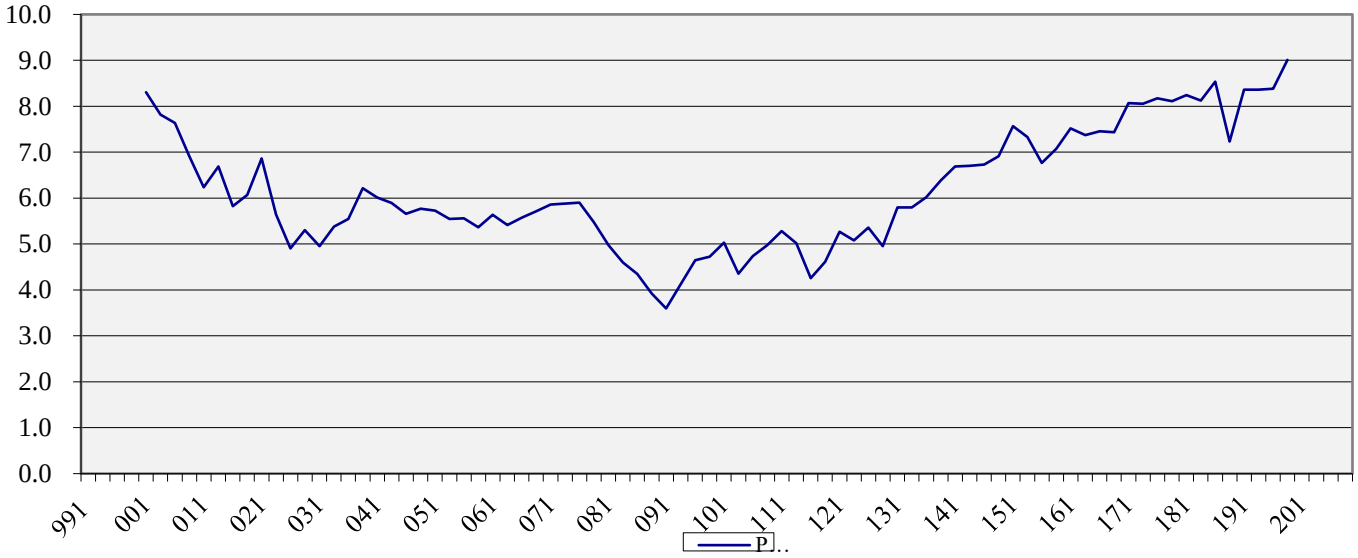
February 6, 2020

Hello,

Most years portfolio returns of 10.5% would make me happy. Unfortunately, not this year as the S&P 500 returned over 30%.

Last year's letter discussed several factors that impact the economy and the stock market. Much of that discussion is still true today. Unemployment is very low. The U.S. economy is growing, currently extending the longest period between recessions in modern history. Congress and our president are stimulating the economy with an eye toward the November elections. Interest rates remain low, therefore bonds are unattractive alternative investments and business and consumers can borrow money at a low cost. The 2017 tax law lowered corporate tax rates giving business money to spend. Finally, our president has continued to reduce regulations on large industries such as energy and banking, improving their future profitability. These factors are positive and have contributed to investors bidding up prices.

Below is a 20-year chart showing the quarterly closing price/quarterly sales (P/S) for the S&P 500 suggesting the market is dangerously overpriced. The last quarter (194) sales is a Barron's estimate.




The first question one should ask when looking at this chart is, have there been changes to the economy that can explain why the price/sales (P/S) ratio should be higher today? The paragraph above makes it seem reasonable. However, every positive in the economy has a negative counterweight. The economy is growing but only at 2.1% last quarter and it is expected to slow further. The fiscal stimulus tied with the tax cut has given us the largest budget deficit in history that is not tied to a recession and the deficit is expected to continue to grow even if our expansion continues. As a result, more of our tax dollars will go toward paying the interest on the debt and less to funding programs. Theoretically, a large deficit will also cause higher interest rates slowing growth and making bonds a better alternative to stocks. The change in the tax code could cause a

shift, but despite causing a brief increase in profitability, businesses have chosen to buy back their own shares rather than investing in themselves and improving future growth. Regulations come and go, nothing new there. One factor I do believe would cause a higher P/S ratio is the change in the composition of the index by including more technology companies. They are faster growing companies with generally higher P/S ratios. However, any boost from technology companies to the high current P/S ratio is likely due to their popularity driving up their prices and therefore their ratios from 3.67 to 5.91 over the past year, not the composition of the index.

Historically, our model has underperformed late in long periods of growth, such as the 90's and today. However, it typically outperforms in corrections and during the early stages of a recovery. Yes, I would have liked to do better in 2019, but I am confident that in the long run, our clients will do well.

Finally, I want to take a moment to discuss the current state of the world. We are now more polarized and confrontational than at any period in my lifetime. It is not the fault of President Trump, though he does not seem to be doing anything to reverse the trend. Democracy worldwide is in decline. According to Larry Diamond at Stanford University, the number of countries with democratic governments has dropped from 62% in 2006 to 51% in 2017. There is growing dissatisfaction with our governments and their ability to get anything done. One factor could be globalization. As international commerce and communication has improved, our economies are more interdependent. As politicians work to solve "national" problems, they may appear inept as these problems are now influenced by foreign economies they do not influence. This can lead to the desire for stronger leaders and a shift toward autocratic government.

A second, and I believe larger factor, is the Internet and the change in the way people gather their information. Previously, most of the information we received was from newspapers, magazines and television news. It was costly to produce, had editorial reviews and tended to be fact-based. With the growth of the Internet there has been an "information" explosion. People can now publish and reach a wide audience for free, therefore the breadth of available content has grown. However, there is no fact-checking required, and as a result the amount of inaccurate content has also expanded. In addition, the Internet also allows people to control what information they receive. Human nature being what it is, we read what appeals to us, often the more sensational the better, and we do not need to listen to the counter arguments. Therefore, we are more polarized than ever before. This is clearly depicted in who we have elected to congress and what they accomplish. Our frustration has led to the growing appeal for an autocratic president.

I finish with an appeal. You control what you read. Try to read fact-based information from different points of view. Then make an informed decision and vote! Democracy is worth the effort.

Sincerely,

Will Wrean