Dear xxxx;

“The New Normal” is a phrase that financial analysts, economists, and pundits have all begun using to describe a period that would normally be strange or abnormal but is now more usual or expected. To us at GA Pincus Funds, as it relates to the US and global economies, macroeconomic policies, and politics, the third quarter of 2019 felt more like “The New Normal” than anything else. While there were ups, downs, and roundabouts during the quarter, we couldn’t help but feel like the outcomes were scripted.

Before discussing the events that shaped the quarter, it is important to understand the overall performance of the market during the last three months. The four major indices that compose the public financial markets: US Stocks (+0.63%), International Stocks (-2.50%), Commodities -4.18%), and Fixed Income (+2.27%), all finished off the highs they reached during early September. This letter will provide an analysis of the major geopolitical and financial events that shaped the quarter.

Jerome Powell & The Federal Funds Rate

Rather than use economic data to determine the Federal Funds Rate, Jerome Powell and the rest of the Fed seem to be making decisions to appease the stock market. The stock market’s recent performance has been largely driven by the US-China trade war. Thus, Chairman Powell seems to be making decisions that work to benefit the US stance in the war. Had there not been a trade war, the US economy would likely have continued to grow, and the Fed would not have needed to cut rates. Rate cuts aren’t necessary in a growing economy, they harm savers, benefit corporations, and can cause bubbles to form. Rate cuts in a bull market also limit the tools the Fed has available when the next recession hits.

During the previous quarter, seemingly bowing to market and political requests, the Fed voted to cut rates twice. Today, the target Federal Funds rate is 1.75-2.00%. Current indications point to an additional quarter-point cut at the Fed’s fourth quarter meeting. We hope the Fed will remain strong, not bow to pressure from the market, and keep rates steady.

Yield Curve Inversion

We’ve spoken extensively about the yield curve, a yield curve inversion, and what they mean for the broader economy and stock market in prior quarterly newsletters available on our website. To summarize, an inverted yield curve is one where shorter-term debt pays more than longer-term debt. This inversion signifies that people have become skeptical that the market will continue to expand over the long-term.

At the close of business on August 14th the 10-Year Treasury yielded 1.527% while the 2-Year Treasury yielded 1.496%, representing an inversion of -0.031%. Over the next two months the value of the 10-Year minus the 2-Year bounced around zero producing both inverted and non-inverted curves. By August 27th, the yield of the 30-Year Bond reached an all-time low of 1.905%. The silver lining of these low yields were the rising prices of bonds. By the beginning of September, US long term bonds were up 11.8% on the quarter and 21.6% for the year.

While the yield curve inversion is likely to precede a recession, it won't cause the recession. We believe the market will push higher from here and events like the recent inversions may continue but they won't have the same dramatic market reaction.

Commodities

Two events shaped the performance of the commodity market in the third quarter. The US-China trade war, coupled with the yield curve inversion spooked investors enough that gold finally spiked, hitting a high of $1,551.40 on September 4th. Gold hasn't been this high since 2011-2013 when it was being used as a post-crash safe haven. Gold is a great hedge, and a useful part of any large portfolio, but it's taken 6 years to show signs of recovery.

On a very high level, the Middle East is comprised of a bunch of countries that have drastically different religious viewpoints and are prone to using violence to maintain order in their countries and to impress their views on their neighbors. Wars and fighting in the Middle East have become so common they are no longer commanding the same media coverage as in decades past. That was until September 14th when someone, presumably Iran, used a drone to attack a Saudi Arabian oil refinery. When people think of Saudi Arabia, they usually think of oil, however, the US is actually the largest oil producer. The initial shock of the drone attack caused oil prices to spike by almost 15%. However, once the world realized that the attack was just a "routine" or "normal" middle eastern conflict, oil prices settled back to their pre-attack levels.

Private Equity Impact on the 2019 IPO Scene

Over the past 15 years, private equity (PE) funds on average have outperformed the S&P 500 by 3-5% depending on the data source used to determine PE returns (Cambridge, Bain, etc). Large investors like pensions, endowments, countries/sovereign wealth funds, and wealthy individuals love these returns and use them as a catalyst to pump additional funds into PE. This has helped new PE funds grow into the billions if not tens of billions or even 100 billion dollars. Larger funds equate to larger investments which equate to larger valuations. If a PE fund invests in a company at a $400 million valuation and then invests again in the same company a year later at a $4 billion valuation, the PE fund can show a 1000% gain (gross of fees) to their clients. Company founders and early employees see the paper growth of their stock and realize they can either sell their company outright or IPO their company to realize their gains and spend their newfound wealth.

In 2019, 114 companies entered their public market through an initial public offering (IPO). While 63 of these companies have had positive returns, some of the more well-known companies (Slack, Uber, Lyft), which were also heavily owned by PE companies, have seen the value of their companies drop. Since most newly listed companies restrict early investor selling until 3-6 months after the IPO date, these precipitous declines in assumed value can have negative implications for PE investors and early employees.

An IPO can only have two outcomes, a good one or a bad one. In 2019, the good ones have outweighed the bad ones, but the bad ones have been littered with spectacular falls from grace. While still a private company, Uber, was thought to be worth as much as $100 billion, as a public company it is now worth half that. SmileDirectClub is also down about 50% since its IPO. We Work has been pumped up so much by PE that it had to pull its IPO because the public markets weren't interested in paying anywhere near the most recent PE valuation. To be fair, there were some great stories too; Beyond Meat was initially valued at just under $1.5b and is now worth almost $9b and Zoom Video Communications is up 111% since its April IPO.

Dramatic moves up or down after an IPO are not altogether surprising. As you look for your next investment, we suggest that you seek out the companies with the least PE funding, those that expect full year profitability, and those with a single class of stock.

US-China Trade War

Unsurprisingly the US-China trade war continued to drive the performance of almost all financial markets this quarter. We would summarize the third quarter as follows: President Trump threatened to do something or did something protectionist and the market went down; Trump took back his threat or reversed his protectionist policies and the market went up. It's important to note that when President Xi says or does something, he doesn't walk it back to appease his people, the market, or the pundits. Rather than go into the details of each tit-for-tat move made by Trump and Xi, we can sum up the quarter by saying, the trade talks are still ongoing, tariffs are still in place, we are no closer to a deal than we were three months ago, and the entire world is getting sick of it.

Conclusion

The economy and stock market bounced around in the third quarter largely due to one-off events, comments, and investor sentiment. However, looking back at the quarter, it seems that the general trend saw the US economy grow; unemployment remained low, wages and spending remained strong, and fears were short-lived. This letter purposefully did not comment on the elephant in the room - President Trump's impeachment proceedings - because they were a non-event for the market.

The Fed rate cuts, the yield curve inversion, the conflicts in the Middle East, the IPO scene, and the trade war, all played out as if their outcomes were expected. The initial news drove the market up or down, investors took time to process the news, then the market reversed its course. The news flowed into the background and the market continued trending higher. Realistically speaking, this is what we believe will happen with the latest Trump saga. We remain bullish on the market leading into 2020.

Client Referral Network

One of the oldest and most successful methods to grow a business is through word of mouth. GA Pincus Funds has been fortunate and has grown substantially due to referrals made by you and your fellow clients. We would like to use our future quarterly newsletters to return the favor to our clients. We plan to dedicate a section of our newsletters to our client's businesses. Rather than list your name or company name, we will instead indicate the category of business and location where you operate. For example, Real Estate Professional in Chicago, or Employment Lawyer in Georgia, or Public Relations

Professional in New York, etc. If you would like to participate in this program, please let us know. This referral program is **free marketing** for your business. **We will not accept payments for these referrals.**

Performance Calculations

The performance of your accounts is calculated daily, taking into consideration daily deposits and withdrawals, and those daily returns are combined to form your quarterly, YTD, and since inception returns. When we round off this enhanced precision it may shift your performance by 0.01-0.02% when compared to the calculation ((end date value – start date value)/start date value). Please note, the performance figures on your statement are accurate and are GIPS (Global Investment Performance Standards) compliant.

It is impossible to predict whether and by how much the market will increase or decrease. Our algorithm rebalances your accounts according to changes in the relative weightings of the securities you hold. As one security becomes too heavily weighted the algorithm sells shares in that security. Conversely, as one security becomes too lightly weighted, the algorithm purchases shares of that security. Instead of rebalancing based on time (as most managers do), this algorithm rebalances based on a securities' relative weighting in the portfolio. This gives GA Pincus Funds a long-term advantage. No matter what the market does in the future or has done in the past, if your time horizon is long enough (>1 year), this algorithm has proven itself to be successful.

I am always available to answer any questions you may have.

Best wishes for a happy and healthy 4th quarter of 2019,

Gabriel

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