JANIAN
INVESTMENT ADVISERS, LLC

February 4, 2019

Dear Clients and Friends:

2018 INVESTMENT REVIEW

STRATEGY	2018 Rate of Return*	Comparable Index Return
Hedged Securities (Taxable)	-9.6%	-6.9%
Hedged Securities After Tax (Estimated)	*-10.5%*	
Unhedged Securities	-12.2%	-5.3%
Fund Selection - Equity Benchmarked	-5.2%	-5.3%
Fund Selection - Bond Benchmarked	-1.2%	-0.1%

* Average Client Account, Net of Fees

We incurred a low level of estimated net taxes[1] in the Hedged Securities strategy, as on average realized long-term gains were only somewhat offset by realized short-term losses. Given client inflows during the year, we do not have the necessary data to calculate the after-tax results for the Unhedged Securities strategy.

The stock market has roared back from 2018's 4th quarter's fall, with the VTSMX[2] +8.6% in January 2019. Janian's Hedged Securities strategy was +3.4% on average, we estimate, with the Unhedged Securities strategy +11.0%, the Fund Selection - Equity Benchmarked strategy +7.6% and the Fund Selection - Bond Benchmarked strategy +2.0%.

A brief discussion of each strategy's 2018 follows.

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1 Please contact us if you'd like an explanation of how we calculate after-tax returns.

2 VTSMX = Vanguard Total Stock Market Index Fund Investor Shares.

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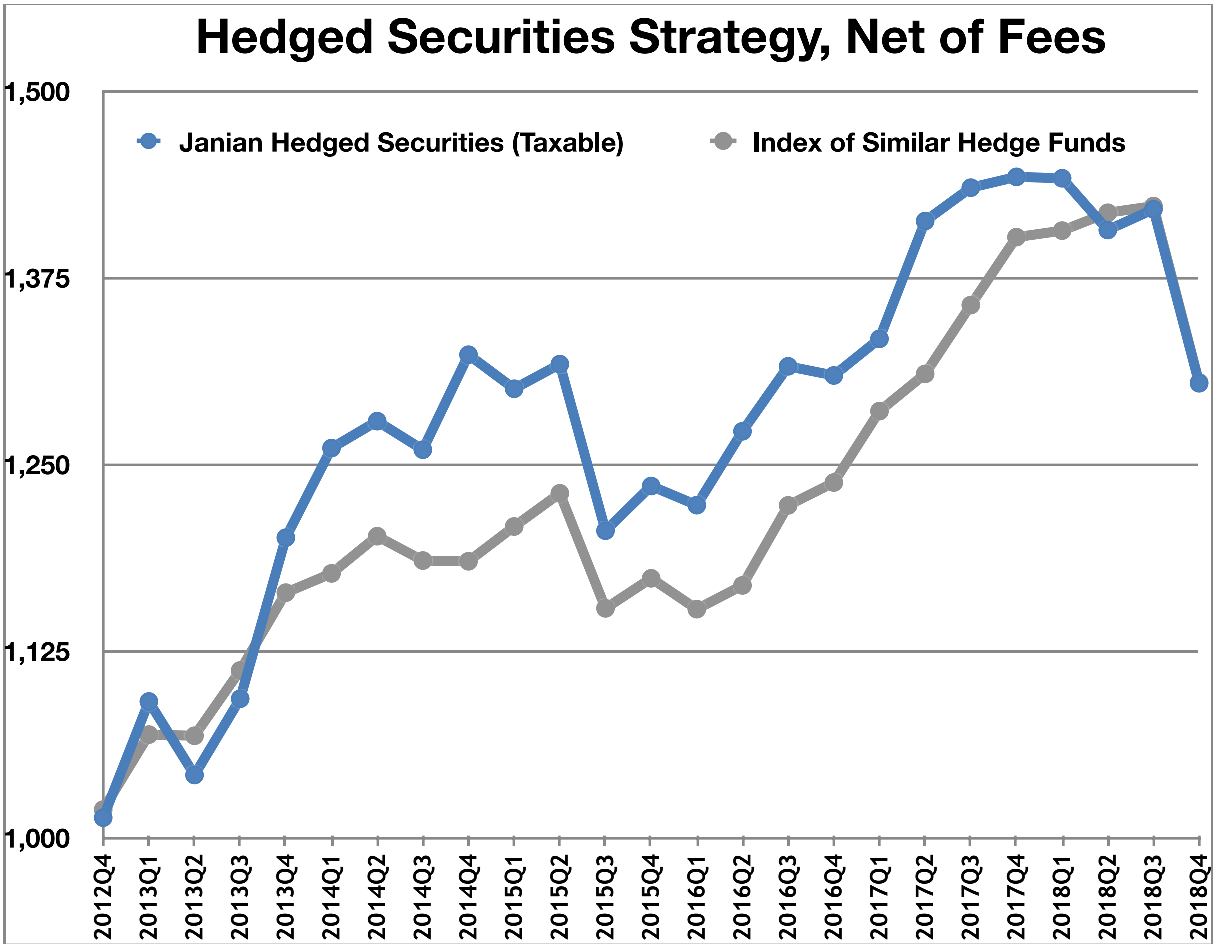
Hedged Securities

Over the last six years we have delivered the same returns in taxable accounts as the average similar strategy[3]. The returns in non-taxable accounts have been very slightly higher.



2018 was, generally, a tough year for hedged strategies. The index of similar hedge funds referenced above suffered a loss worse than the market's, and many well-known hedge fund managers posted poor returns[4].

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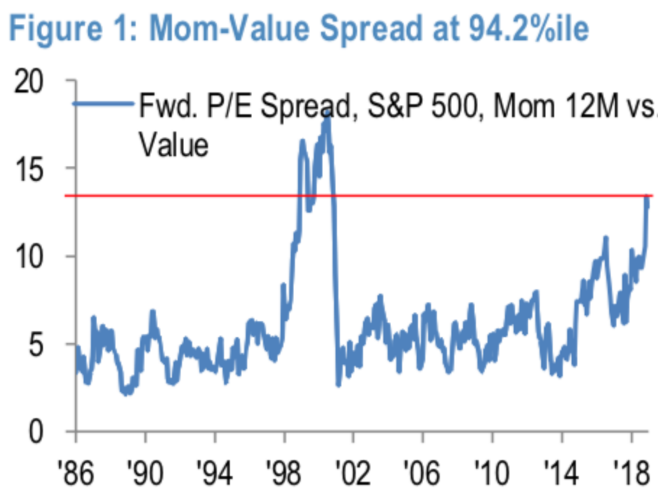
[3] A critical additional point is that the average hedge fund has much more gross leverage, and thus more risk, than Janian. We have produced better relative risk-adjusted results than shown here. A second important point is that our tax costs have been lower than the average hedge fund's.

[4] See https://www.bloomberg.com/news/articles/2019-01-09/hedge-fund-performance-in-2018-the-good-the-bad-and-the-ugly or https://www.bloomberg.com/news/articles/2019-01-11/-extraordinary-month-heaps-further-pain-on-hedge-funds.

For Janian, the loss was driven by the failure of the long portfolio to keep up with the market's bull run in the 2nd and 3rd quarters. For the year, the long portfolio's return on invested capital was lower than the stock market's. Meanwhile, the short portfolio posted a profit for the year and thus reduced the damage, but it was not enough to overcome the mid-year relative underperformance of Janian's longs.

As has been the case for several years, Janian's long portfolio did not fall in with the cool kids. Our exposure to 'momentum' was low and 'value' was high. This was counterproductive, as the 'spread' of valuations for "Mom[entum]" less the valuations for "Value" reached tech-bubble-like levels[5]:



Janian sees our job as selecting for you investments in a businesslike and rational manner. Betting on momentum continuing regardless of the prices that one is charged is not businesslike or rational. History has demonstrated very, very clearly that a value-driven investment process has had higher returns than a momentum-driven process over the long term, and so despite the headwinds that we have been facing we will not adapt a more momentum-driven approach[6].

Our position-level risk control was solid. The biggest long winner's contribution to total returns was approximately +2.2%, long loser -2.3%, short winner +1.4%, and short loser -0.9%. This underscores the point that our year was driven not by security selection, but by 'momentum' versus 'value' selection.

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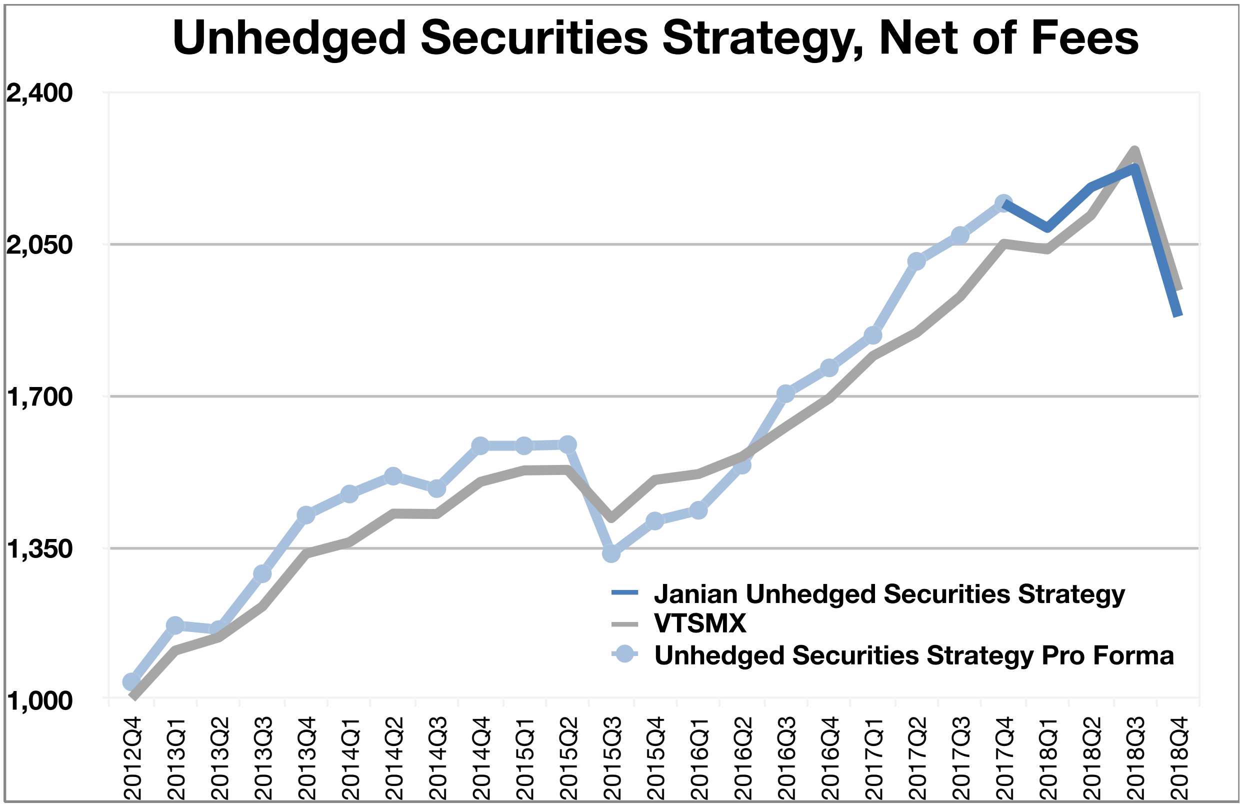
[5] Thanks to J.P. Morgan for the chart, which was published in "US Style Positioning" by the Equity Strategy and Quantitative Research group on January 9, 2019.

[6] Our patience might not be rewarded for some time or perhaps not at all, as pointed out in https://www.themacrotourist.com/posts/2018/10/16/factors/.

Unhedged Securities

Like the long side of the Hedged Securities strategy, the Unhedged (i.e., Long) Securities strategy[7] had a loss worse than the stock market's for 2018.

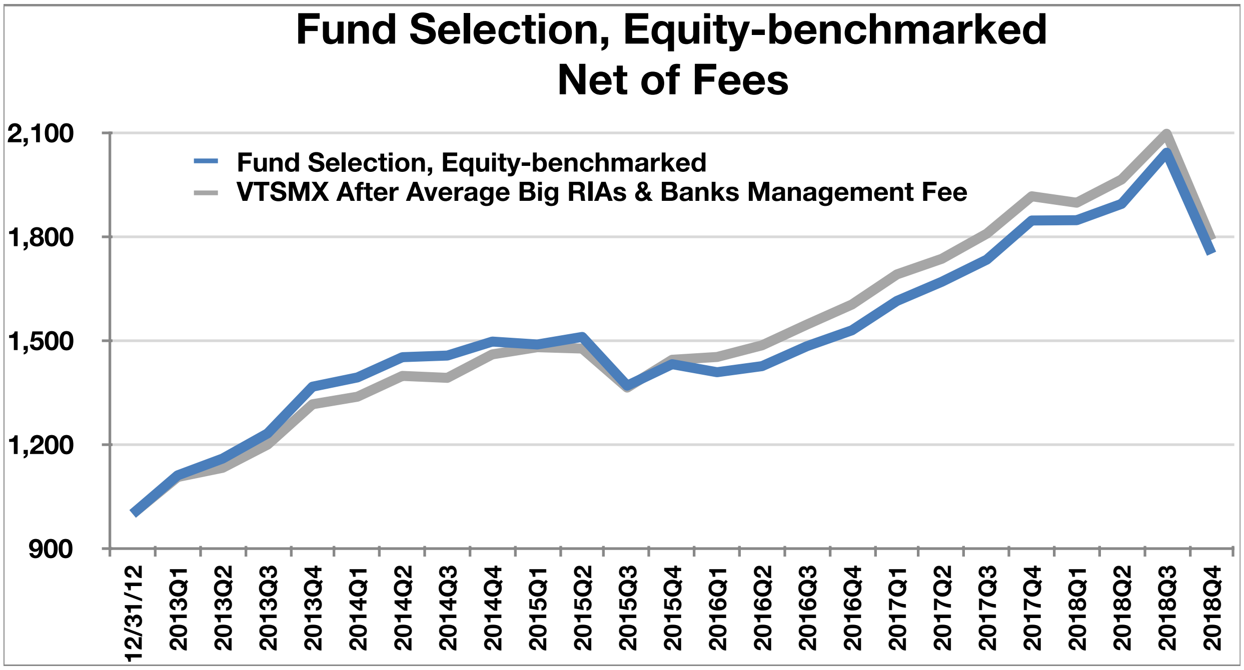


	Unhedged Securities Strategy	VTSMX
2013	37.12	33.35
2014	11.24	12.43
2015	(10.96)	0.30
2016	25.08	12.53
2017	21.54	21.05
2018	(12.19)	(5.27)
Annualized %	11.64	12.25

[7] Shown net of a 1% Management Fee; the actual fee level starts at 1% and goes down at various higher levels of assets under management per client. The Pro Forma results are calculated as the actual gross Return On Invested Capital of the long portfolio of the Hedged Securities Strategy, adjusted for a 1% Management Fee, for October 2012 - December 2017.

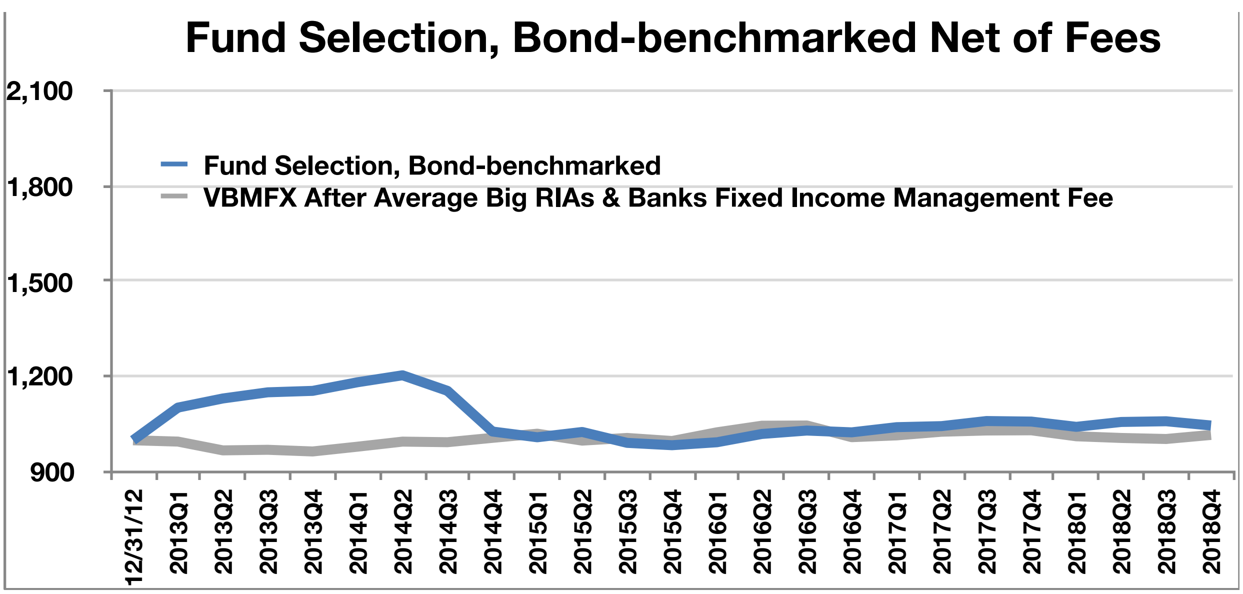
Funds – Equities

This strategy, which aims to match the stock market over time, performed as intended in 2018.



Funds – Bonds

This strategy[8], which aims to match or beat the bond market over time, performed as intended in 2018.



[8] VBMFX = Vanguard Total Bond Market Index Fund Investor Shares.

JANIAN RUMINATIONS

Macroeconomic Outlook

As Yogi Berra said, "It's tough to make predictions, especially about the future." We are not familiar with anyone who has been consistently successful over a reasonably long time at making correct one-year-forward macroeconomic predictions. We certainly haven't been. However, having a framework of views in order to shape guesses at probabilities is something that we do attempt. Here's our current views:

Stock market bulls point mainly to three items:
(a) Consumer confidence, although recently weakening, "suggest[s] that the economy will continue expanding at a solid pace in the short-term[9]," and unemployment remains low;
(b) Price/Earnings ratios fell meaningfully while the S&P 500's Operating Earnings Per Share grew 26% in 2018[10]. History suggests that the S&P 500 is currently attractively valued[11]; and
(c) Equities already fell sharply in 2018's 4th quarter[12], perhaps 'baking in' a future business slowdown.

Stock market bears point to more items, including:
(i) The Federal Reserve has indicated that it is considering raising interest rates further[13], although the timing of this is uncertain and appears to be on pause[14,15], and some observers think that "the delayed effects of past rate increases are starting to bite[16];"
(ii) The central banks of Canada, India, Indonesia, Mexico, South Korea, Turkey, and the United Kingdom also recently raised rates;

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9 https://www.conference-board.org/data/ConsumerConfidence.cfm

10 https://us.spindices.com/indices/equity/sp-500

11 https://am.jpmorgan.com/us/en/asset-management/gim/adv/insights/guide-to-the-markets

12 http://www.kkr.com/global-perspectives/publications/outlook-2019-game-has-changed

13 Better late than never: https://www.project-syndicate.org/commentary/federal-reserve-right-to-raise-interest-rates-by-stephen-s--roach-2018-12

14 Some think that it won't pause for long: https://www.themacrotourist.com/posts/2019/01/08/fed/

15 Deutsche Bank published an interesting piece entitled "The History (and Future) of Inflation…" Please let me know if you'd like to read it.

16 https://www.marketwatch.com/story/stock-market-bulls-look-to-shake-off-the-selloff-and-party-like-its-2016-2019-01-08

(iii) Economies around the world are slowing[17,18,19];

(iv) The concessions that China is likely to make to allow Presidents Trump and Xi to have a 'win' are very likely to incrementally slow growth in China;

(v) Brexit is likely to be a messy process and perhaps damaging to the U.K. economy and worldwide animal spirits[20];

(vi) Business confidence in the U.S. "has significantly slumped at the start of 2019[21];"

(vii) The TCJA is behind us and there is no further government stimulus on the horizon in the U.S.[22];

(viii) The Mueller investigation's results seem likely[23] to provide some degree of upsetting headlines and uncertainty about the ability of the U.S. Federal government to focus on actual governance; and

(ix) Some types of consumer debt in the U.S. have reached levels as high or higher than in 2007, suggesting that consumers' ability to grow consumption at rates similar to those of the recent past may face some constraints[24].

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17 https://app.hedgeye.com/insights/72174-global-growthslowing-the-bear-market-data-keeps-coming?type=macro, https://app.hedgeye.com/insights/72638-did-you-make-the-move-to-treasuries?subtype=macro&type=hedgeye-tv

18 https://www.zerohedge.com/news/2018-11-13/latest-shock-beijing-chinese-credit-growth-lowest-record

19 For a very specific example, an investment bank estimated that year-on-year sales of smartphones in China in 2018Q4 will be down 20% on a unit basis.

20 https://www.jpmorgan.com/jpmpdf/1320746642220.pdf has a wealth of interesting comments about a variety of economic and financial matters, including Brexit.

21 https://www.economy.com/dismal/indicators/releases/usa_dsbc

22 Instead, we had (and may have more of) https://www.newsweek.com/heres-how-much-government-shutdown-could-cost-786073, which, among other things, prevented the timely publication of U.S. economic statistics, which in turn added to uncertainty and thus bearish sentiment regardless of one's political opinion.

23 We are not predicting what the investigation will result in. Rather, we believe that the publication of articles such as https://www.politico.com/magazine/story/2019/01/14/trump-obstruction-collusion-russia-223978 suggests that even if the investigation concludes with no 'real' grounds for further litigation by the Justice Department against employees of the Trump campaign or administration, upset and uncertainty is likely to be stirred up by those who wish for more. And, we predict, if the investigation concludes with more than that, there's clearly an appetite for unleashing a wrenching drama.

24 Check out https://apps.urban.org/features/debt-interactive-map/?type=auto&variable=autoopen_pct for a fascinating visual examination of consumer debt in the U.S.

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We believe that a bearish spell in equity markets is more likely than was the case at the beginning of the last several years, and so for the time being Janian intends to:

(1) Keep net long exposure <60% in the Hedged Securities strategy;
(2) Be quicker rather than slower to reduce exposure in the Long Securities and Funds - Equity strategies; and
(3) Maintain a very large cash position in the Funds - Bonds strategy.

The Tax Cuts and Jobs Act of 2017

Last year we wrote about our skepticism that this will work out to be a net positive for the overall U.S. We can't resist two follow-ups. One: on the day before Halloween 2018 Janet Yellen, perhaps now free to say what she really thinks, put on her scary face and lamented the buildup of our national debt, a liability that she described as "unsustainable[25]." Two: a few days before that, the Federal Reserve Bank of New York dissed one of the main selling points of the Act by publishing a research paper that it summarized as "We find that the U.S. effective tax rate was already below the average rate abroad prior to enactment of the TCJA, and that it is now well below the rate in most countries."

[25] There are those who probably think that Ms. Yellen's favorite cartoon character is Caspar Milquetoast: see the 2019 Open Letter at www.macromavens.com

Acting Ethically in a Sea of Sharks

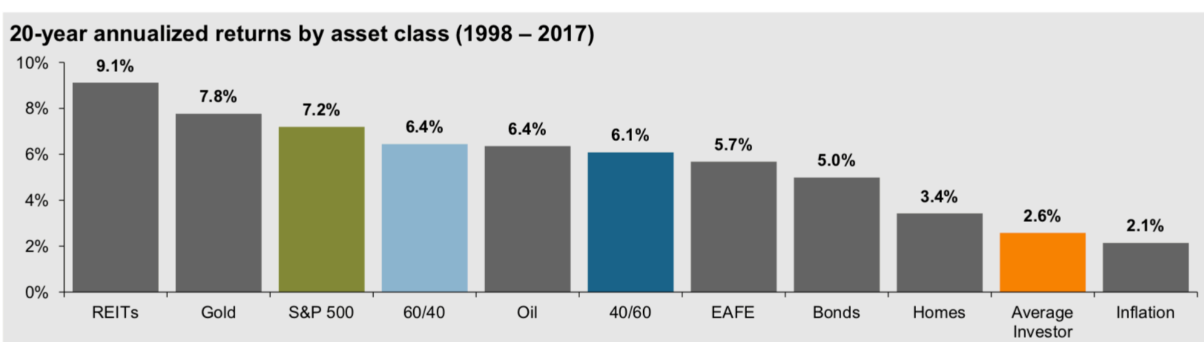
Last year we read the first academic paper that we've seen focused on U.S. Investment Advisor misconduct[26]. It contained the following:

Table 5: Firms with the Highest Incidence of Misconduct

Rank	Firm	Firm CRD#	Misconduct	# Advisers
1	OPPENHEIMER & CO. INC.	249	19.6%	2,275
2	FIRST ALLIED SECURITIES, INC.	32444	17.7%	1,112
3	WELLS FARGO ADVISORS FINANCIAL NETWORK, LLC	11025	15.3%	1,797
4	UBS FINANCIAL SERVICES INC.	8174	15.1%	12,175
5	CETERA ADVISORS LLC	10299	14.4%	1,432
6	SECURITIES AMERICA, INC.	10205	14.3%	2,546
7	NATIONAL PLANNING CORPORATION	29604	14.0%	1,760
8	RAYMOND JAMES & ASSOCIATES, INC.	705	13.7%	5,495
9	STIFEL, NICOLAUS & COMPANY, INCORPORATED	793	13.3%	4,008
10	JANNEY MONTGOMERY SCOTT LLC	463	13.3%	1,394
11	MORGAN STANLEY	149777	13.1%	23,618
12	SAGEPOINT FINANCIAL, INC.	133763	12.1%	2,063
13	WELLS FARGO ADVISORS, LLC	19616	12.1%	26,308
14	FSC SECURITIES CORPORATION	7461	11.6%	1,373
15	PURSHE KAPLAN STERLING INVESTMENTS	35747	11.4%	1,224
16	ROYAL ALLIANCE ASSOCIATES, INC.	23131	11.4%	1,975
17	RAYMOND JAMES FINANCIAL SERVICES, INC.	6694	11.2%	5,176
18	WOODBURY FINANCIAL SERVICES, INC.	421	10.9%	1,377
19	AMERIPRISE FINANCIAL SERVICES, INC.	6363	10.4%	13,549
20	INVEST FINANCIAL CORPORATION	12984	10.1%	1,425

Note: Tables 5 displays the firms in the U.S. with the highest employee misconduct rates as of May 2015. Firms are defined by their Central Registration Depository (CRD) number. Misconduct measures the percentage of advisers working for a firm that have been reprimanded for misconduct in the past. We restrict the set to the 100 firms with at least 1,000 advisers.

The level of misconduct in Janian's industry deeply angers me. Particularly given the need for better advice to individual investors[27].



[26] https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2739170

[27] https://am.jpmorgan.com/us/en/asset-management/gim/adv/insights/guide-to-the-markets

Janian remains committed to helping clients build a better future by capturing more of the opportunity offered by financial markets.

Sincerely,

James W. Hague

James W. Hague
Founder
Janian Investment Advisers, LLC