KONDRACKI ADVISORY

January 9, 2019

Quarterly Commentary and Opinion

Dear Clients of Kondracki Advisory,

We outperformed the market in 2018 with our composite total return of -4.23%. The total return on the S&P 500 was **-**4.40%. International stocks as measured by the EAFA Index were **-**13.4%. Importantly, as the stock market declined nearly 20% from its peak during the fourth quarter, our portfolios proved far more resilient and far less volatile, **overcoming a 7% performance differential during the final 10 weeks of the year**. In what was one of the most challenging quarters for the stock market in many, many years, we achieved our best relative performance in the history of our firm, and at the most important time for our clients.

During the fourth quarter, we saw the risks of a concentrated market that I discussed in our First Quarter Commentary, exposed. Technology and bank shares, representing nearly 40% of the value of the S&P 500, were hit particularly hard. Quarterly losses on many formerly high-flying and widely owned Mutual Funds, Index Funds, and Exchange Traded Funds, exceeded 20% to 30%. Although now more reasonably priced, markets do remain fairly concentrated and significantly influenced by the stock price gyrations of just a handful of technology companies and several large banks. This concentration, in combination with what I can only describe as "manufactured" activity and volatility from high-frequency and algorithmic and program trading, or, broadly speaking, quantitative and computer trading, will most certainly lead to additional periods of significant volatility and downside risk. Concerns about slowing economic growth, trade, and rising interest rates are all very reasonable, but alone, could never explain away the extreme intra-day volatility that we experienced in 2018. Markets could remain challenging for a while; but with challenges, come opportunities.

Over the years we have experienced many examples of the effectiveness of our investment approach. This was especially so during the volatile fourth quarter, and we are seeing it today. Our portfolios are **better protected** than the market, and our considerable **dividend income,** reinvested**,** is now purchasing more shares at significantly higher yields. In fact, our current dividend yield is **3.1%,** which is 19% higher than it was just 12 months ago, and 45% higher than the dividend yield of the S&P 500. Extreme market volatility has also led to some excellent **buying opportunities** for our portfolios. With our current cash and 1 Year U.S. Treasury Note position of 18%, we are in an advantaged position to be opportunistic, but without sacrificing downside protection. Over the course of the year I had been gradually increasing our cash and Treasury Note position as rates on the 1 Year Note approached 2.7**%**. It is possible that I will further increase our Treasury Note position if yields and market conditions warrant it.

Our balanced approach to downside protection and the achievement of reasonable returns has worked very well for us since the inception of the firm, having achieved a **9.3% average annual return through January 9th, 2019,** with just half the volatility of the market. I cannot find a single investment benchmark that comes close to our total returns that also matches our reduced level of volatility.

Ours really is an all-weather investment approach, and I think it is especially timely right now. Challenging markets are the true test of a portfolio and investment approach, and the best long term returns are usually realized not by achieving the highest return in up markets, but by holding onto gains, and losing less in down markets. The notion that investors must assume significantly more risk and endure extreme volatility to achieve superior long term returns has been proven false time and time again.

Markets and the economic and political environment do not always operate in a smooth fashion. Nonetheless, careful company and sector selection **can achieve** outstanding investment results during such periods. In fact, it is usually during periods of heightened uncertainty and volatility where the truly valuable, time-tested companies and investment approaches, shine brightest and demonstrate their considerable worth.

We are off to a very strong start in 2019. As always, I am closely monitoring our companies and will do everything that I can to help us to have the opportunity to grow our wealth as safely and effectively as possible.

Sincerely,

Chris Kondracki, Principal and Portfolio Manager
Brian T. Kondracki, CFA, Investment Adviser and Research Analyst