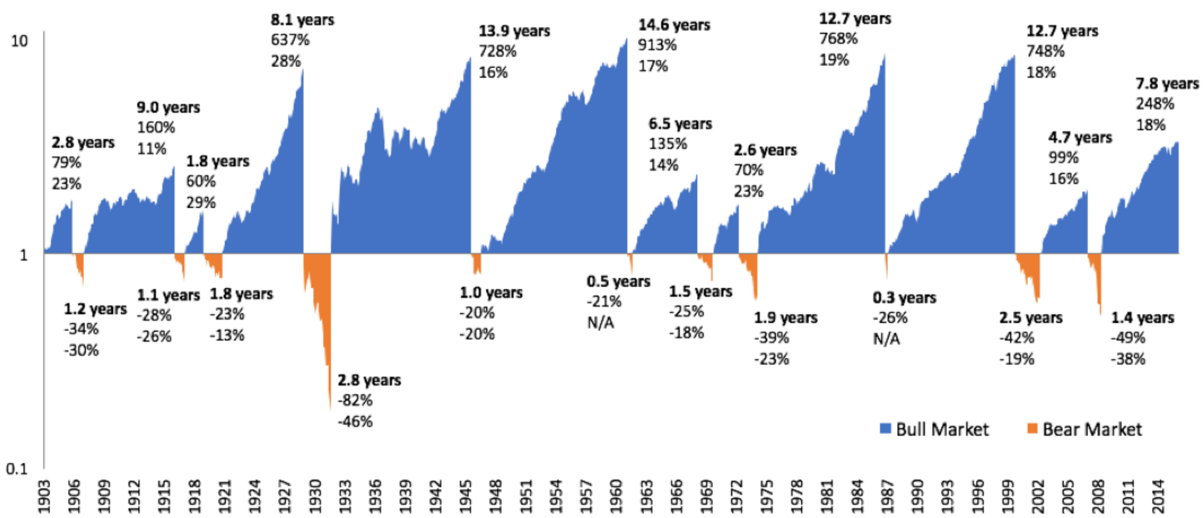
Frankie Says Relax

"Investing is the intersection of economics and psychology." ***–Seth Klarman***

It's become a common theme in our newsletters where we like to remind investors (as well as ourselves sometimes) to take a step back from the headline news to examine where we really are in the current Bull Market cycle. While the news is constantly talking about a pending market top and subsequent drop, history shows us that we need to stay calm and, as the popular 80's hit by Frankie Goes to Hollywood says, "Relax!"

In the below chart you will see that this current bull market has come off of the 2nd worst bear market drop ever. Even then, the subsequent recovery and charging Bull ranks in the middle of the pack. Out of 9 bull markets, the current bull ranks 5th in total return and 6th in annual return.

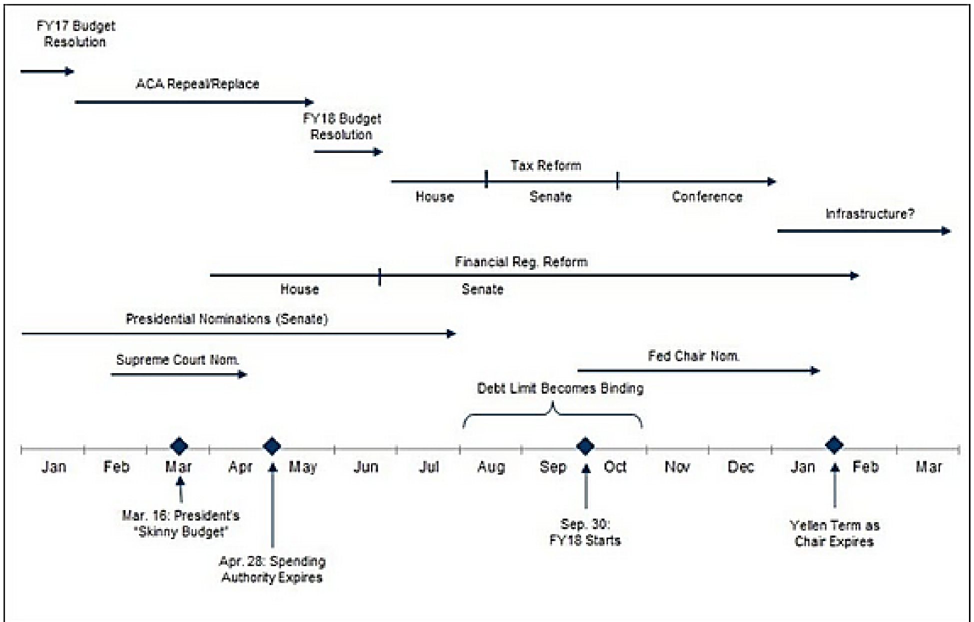
U.S. Bull and Bear Markets: 1903 to 2016



We always like to reference the famed Sir John Templeton's quote and will continue to do so as long as we feel it necessary: "Bull markets are born on pessimism, grown on skepticism, mature on optimism and die on euphoria." Optimism in the market coming out of the election has lost some ground to skepticism as Washington continues to face gridlock. Whether legistlation actually gets passed and optimism takes completely over, we don't know. The one thing we do feel confident about is that we are a long way from euphoria. Michael Harnett, Bank of America Merrill Lynch's Chief Investment Strategist, recently relayed this same sentiment, "My sense is there are too many people who want the market to correct, and so it's not going to correct. Many investors seem reluctant to embrace the view that the US can shift into third or fourth gear, and that's why I describe the consensus as reluctantly bullish." We agree, and we remain bullish for now.

Policy Uncertainty Takes Center Stage

The Trump trade was in full effect the first half of the quarter, but as the probability of legislation passing started to diminish, and the President's rhetoric began to deviate from his campaign promises, the excitement and optimism coming out of the election suddenly gave way to caution and uncertainty. The inability of Republicans to come to an agreement on Obamacare has shaken investors confidence in Washington's ability to get anything done, including stimulus efforts like tax reform and infrastructure spending. Goldman Sachs recently put together the below timeline to visually show investors the long legislative road that is ahead:



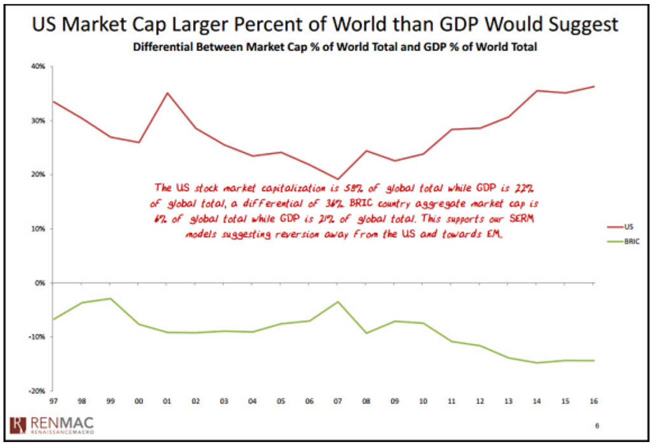
Source: Goldman Sachs Global Investment Research

Policy uncertainty is not just a domestic issue. The rise of populism worldwide has caused global uncertainty to rise to record levels. The Global Policy Uncertainty index, which uses data from 18 countries that make up 2/3rds of global GDP, currently sits at a 20 year high. That said, while markets and consumers may favor certainty, opportunities arise in times of uncertainty. We are finding some of those opportuntiies now and are allocating accordingly. But in order to capitalize on those, we must remain disciplilned and have the fortitude to invest even into the teeth of volatility. International markets are one of those areas of high interest which we discuss next.

Opportunities Abroad

We have always been investors in International Markets due to their diversification benefits, but, as of late, we have been increasing that allocation due to what we believe is great long term value relative to dometic equities. Europe's recovery has been long and slow, but recent economic activity indicates that things are turning around. Despite this uptick in positive news, Europe has greatly underperformed the US, and while volatility will continue as politics dominate the headlines, it is our belief that European equities offer tremendous value potential. The below chart shows the performance difference between the United States and Eurozone over the past 5 years. If you take it out over 10 years, performance difference gets even wider. Looking back 10 years from the end of this past quarter, SPY (an ETF tracking the S&P500) would have given you a total return of 104% while VGK (an ETF tracking FTSE Developed Europe) would have returned 9.9%.

In addition to European equities, we believe that the Emerging Markets offer up some of the most attractive value opportunities for investors. Like Europe, the return dispersion between the two has been incredibly wide coming out of the Global Financial Crisis, and only recently have Emerging Markets begun to outperform. This return differential has created an incredible imbalance between the two markets that is hard to ignore: The US stock market makes up 58% of the total global market cap while it's GDP is only



22%. On the flipside, the BRIC (Brazil, Russia, India & China) nations make up just 6% of the global market cap despite their collective GDP representing 21% of the global total (see chart above).

Within Emerging Markets, we continue to like Emerging Asia as the middle class continues to grow in those countries. After a recent slowdown, the largest of those countries, China, has started to see economic activity pick up again. This past quarter saw GDP, retail sales, industrial production and fixed asset investment all come in above estimates.

Client First!

This month we will be celebrating our 6 year anniversary and we want to thank our clients and partners for their continued support. Our goal when starting Canal Capital was to build a firm that truly served the client first, something that seems like a novel concept, but is not always found in the financial services industry. With each passing year we strive to continue to uphold this goal and are always looking for ways to better serve. Jeff Bezos, CEO and founder of Amazon, in his most recent shareholder letter described their commitment to a client centric culture and it's one that echoes Canal's same sentiment: "In my view, obsessive customer focus is by far the most protective of Day 1 vitality. Staying in Day 1 requires you to experiment patiently, accept failures, plant seeds, protect saplings, and double down when you see customer delight. A customer-obsessed culture best creates the conditions where all of that can happen." We are constantly striving to deliver to our clients a better experience. Our doors and phonelines are always open and we encourage our cleints to continue to help us achieve that goal.

As always, please don't hesitate to contact us with any questions or to discuss changes in your overall risk tolerance.