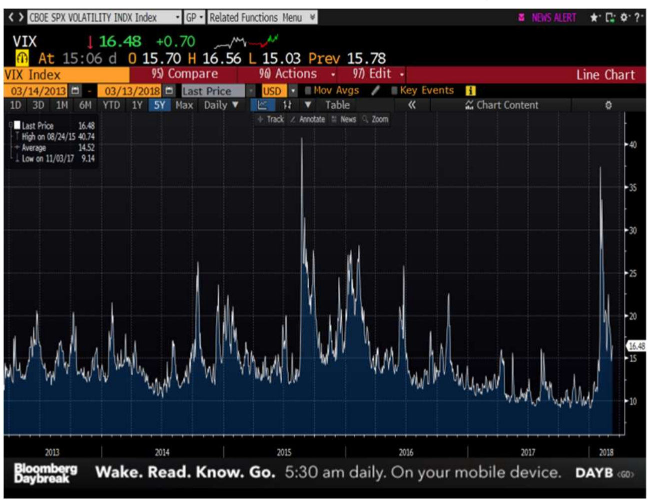
David W. Griffis, CFA   Andrew B. Hartline, CFA   First Quarter 2018

VERO BEACH GLOBAL ADVISORS

Registered Investment Advisor

> "Whenever you find yourself on the side of the majority, it is time to pause and reflect."
> Mark Twain, Author

As if on cue, we have noticed client angst ratchet higher as daily swings in the stock market have increased in magnitude. The chart below is the Chicago Board Options Exchange Volatility Index, commonly known as the "VIX." The VIX is a widely recognized volatility benchmark that pulls together option pricing data over a set period of time. It tends to be an accurate barometer of the level of diverging stock prices and a common flashpoint for market pundits discussing equity risk.



A visible trend from the VIX chart is the distinct period of moderation, or lull, during 2017, followed by February's recent sharp spike. Looking back, the VIX Index finished last year with the lowest average daily level on record, along with hitting an all-time low of 9.1 on November 3rd.* With a multi-year perspective, we view recent heightened volatility as the harbinger of a return to normalcy rather than a deviation from the norm. In other words, investors should be prepared for market price variability and adjust temperaments or asset mixes accordingly.

While the VIX reflects equity price variations, bond prices also adjusted in the first quarter. As pointed out in our year-end report, bonds were poised to decline in value, as interest rates were set to rise. That scenario has unfolded with bond prices adjusting down as the domestic economy continues to strengthen. Regarding the Mark Twain quote above, it gives us pause and forces reflection as our bond portfolios are currently aligned with the "majority" toward further rate hikes. With due respect to Mr. Twain, his time was well before the axiom of "don't fight the Fed..."

That said, we continue to move our client bond portfolios to the lower end of the duration curve in anticipation of the opportunity to reinvest at higher interest rates in the future. Disclosures from the recent Federal Reserve meeting indicate the U.S. economy is closer to achieving the 2% inflation rate they target. This gives a higher probability the Fed will raise its benchmark federal funds rate five more times before the end of 2019. This expectation, coupled with a historically low unemployment rate of 4.1%, should result in higher long-term interest rates. Though this has yet to materialize due to extraordinarily high demand for fixed income, we will continue to monitor this closely on behalf of our clients.

On the equity side of the house, we continue to invest in undervalued companies with strong balance sheets who have a documented history of sharing profits with investors in the form of above-market dividend yields. While some clients may not necessarily feel it, this has allowed our equity portfolios to experience much less volatility than the aforementioned discussion on the VIX may indicate. Constant cash flows from dividends allow our clients to meet spending needs or provide additional capital for us to invest at new market valuations. In addition, the value discipline we employ, by definition, will place our portfolios at lower valuations than the overall market. If history is any indication this will result in better returns on a relative basis should the markets further correct. Vero Beach Global Advisors also continues to take advantage of its relative size to find opportunities in smaller companies which meet our exacting standards and may fall below the radar of the behemoth money managers. As our name indicates, we are searching for "global" holdings which means we are not limited to investing in the United States.

To enhance and expand our global opportunity set of potential investments David made a research visit to the United Kingdom earlier this month. The purpose for this trip was to assess the current economic landscape there, and meet with some of the businesses we currently follow, as well as a few companies currently under consideration. While there we met with the UK's largest carbonated beverage company, a home builder, diversified technology/industrial company, a retailer, a global satellite company, an emerging market investment manager, and an aerospace and defense contractor. It was a very diversified group all having, as we believed going in, different economic perspectives and experiences. Their revenue sources were very diverse from a geographic perspective, in fact the aeronautics and defense contractor produces most of their revenue outside of the UK, while the retailer and beverage companies' revenues are almost exclusively internally generated. This allowed for a very interesting perspective about the local economy, Brexit implications, and currency issues. From a macro perspective there are a large number of cranes dotting the landscape, indicating a great deal of large scale builiding, especially in London proper (Zones 1 and 2). Coming away from a visit with the number one homebuilder in the UK we have greater confidence in the housing market, and the associated government support through their "Help to Buy" program. In fact, Prime Minister Theresa May's number two stated at-home priority (behind combatting terrorism) is home ownership in the UK. Generally the outcomes of the meetings were very positive and we came away with what we believe are contiued compelling reasons for owning most of the companies visited, as well as a couple of potentially new opportunities for our clients. Under a separate paper we will share with you more specific observations from this trip. In addition, this year our analysts will also visit both Hong Kong and India.

Note & Sources:

*Bloomberg Markets, "Why Is Volatility so Low?" Feb/March 2018, Brandon Kochkodin