MONTAG

Viewpoints

FOURTH QUARTER 2017

*The New Year brings a NEW LOOK for our newsletter, now called "**Viewpoints**". We plan to share our views on markets and investment topics in these pages each quarter. We hope to inform, enlighten, and entertain. Welcome to **Viewpoints**!*

HAPPY NEW YEAR FROM MONTAG — *Ned & John Montag*

With the turn of the calendar comes a time to reflect on the ending of a year gone by as well as looking forward to the New Year. It's a time to look at ourselves and our accomplishments but most importantly to thank those around us that have helped us to get where we are today.

As we often do in the welcome note of this newsletter, we want to say thanks to each of you for taking the time to read this letter. Thank you, to our clients, supporters, and friends, who have helped us grow and make MONTAG a successful, multi-generational family owned business. Thank you to the 25 wonderful professionals who work at our firm, all of whom are dedicated to our core beliefs of outstanding client service and providing thoughtful solutions to our clients' individual needs.

We look forward to continued success and growth and appreciate all of you who have joined us and are a part of this journey. **Wishing you all the best for 2018!**

Inside This Issue

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MARKET OBSERVATIONS — *John Montag*

The fourth quarter was a continued uphill march for the major indices as the calendar year came to an end. For the quarter, the returns were 11.0% for the Dow Jones Industrial Average, 6.6% for the S&P 500 Index, and 6.5% for the NASDAQ. The returns for these three indices for the year 2017 were 28.1%, 21.8%, and 29.6%, respectively. For the Dow Jones in particular, over the calendar year we saw the index set, and break, its all-time high throughout the year, surpassing the 20, 21, 22, 23, and 24,000 marks all in 2017. 2017 returns were also somewhat strengthened during December as the market started to price in the expectation, and eventual passing, of major tax reform into law. This tax reform simultaneously eased the corporate tax burden for businesses, thus potentially spurring companies to reinvest in their businesses and the labor market, while giving investors a sigh of relief that a major piece of promised legislation could be accomplished by the White House.

So where does that leave us as we begin 2018?

The markets are at all-time highs as previously stated, and the bull market, now 2,000 plus days in the making, doesn't appear to be slowing down. At MONTAG, while we recognize that valuations appear to be getting extended, **we still believe the equity markets offer the best investment opportunities at present.** Two reasons come to mind.

First, the market reflects earning expectations, as in the future cash flow opportunities of the companies in which we tend to study and invest. The expectations for the market continue to look strong, particularly given the passage of tax reform legislation, as previously mentioned. Companies will be facing a lower tax environment, continued low interest rates, and a more advantageous path to repatriate some (or all) of their foreign cash reserves than they've had in many years. Regardless of whether the repatriated cash is used for capital expenditures ("Capex") or share repurchase, the balance sheets of these companies have every opportunity to remain strong.

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Second, we repeat the ongoing refrain: There Is No Alternative (TINA). Interest rates remain low, and this represses both the return on cash as well as fixed income (i.e., bond) investments. To give you some idea of how this has changed over the tenure of my time in the investment field, when I started here in the mid-90s, a cash allocation in a portfolio would yield 5%. As of this writing in late 2017, investors are fortunate to find a tenth of that yield in a similar cash allocation. The equity markets simply offer a better return than any other liquid investment out there.

In our view, the continued setting and breaking of equity index highs has been more interesting to us because what it reveals is a strong investor sentiment that "all ships rise with the tide" and folks are more eager to participate in this market than sit it out. This has, therefore, created a herd mentality amongst these investors and tamped down fear, as measured by market volatility. And in our experience, markets don't typically move in a straight line like they did in 2017. As such, our expectations for 2018 are for a continued rising market, with an increase in volatility.

At MONTAG, we pride ourselves on constructing portfolios that are uniquely suited and driven by the client's investment objectives. Because each portfolio is different, we strive to craft an answer that is right for you in the ongoing management of your portfolio. For example, a key question that surfaced in many client meetings during the last quarter of 2017 was "Given my portfolio and these expectations, is it appropriate to change my asset allocation?" When asked this, the answer for many was "yes," and for others the answer was "no." These conversations are specific to each of you and **we encourage you to reach out and let us know what is on your mind** whenever you feel like discussing your personal situation. M

John Montag is President & Chief Investment Officer

The market reflects earnings expectations... Our own expectations for 2018 continue to look strong, with an increase in volatility.

SELL DISCIPLINE AND THE S&P 500 — *Kent Shaw, CFA*

Buying a new stock can be fun and exciting. Almost like driving a new car off the lot. Some stocks may even have that new stock smell. Ahh, money. The promise of vast profits ahead. Surely, my new stock pick is the next Apple or Facebook or.... You get the idea. However, selling is often more important than buying and can be quite a bit more difficult. Especially if you are selling a stock that is down from where you purchased it. The rule or method of exiting a stock at a loss is often referred to as a "sell discipline" among professional investment managers, and we will examine sell disciplines, and their differences, in this article.

Looking at the S&P 500

Thinking about what a sell discipline means can sometimes use some context. In that regard, let's look at a measure of market performance that most people are familiar with.

The S&P 500 Index is the most widely followed equity index for US investors and represents the 500 largest US stocks by market capitalization (that is, a company's stock price multiplied by the number of shares outstanding). The index is rebalanced every year, sometimes several times, and when a rebalancing occurs, some stocks are removed from the index for various reasons and others are added. If a company is acquired by another company it may be removed. If the stock falls too far and is no longer large enough to be included in the index it is also removed.

This periodic review of the index serves as a kind of sell discipline for poorly performing stocks, because if a company's market capitalization is going down, implicitly the stock price of that company is falling.

How a sell discipline may be different for an individual investor

The S&P 500 "sell discipline" described above is based on a simple rule, which is that if a company is no longer one of the largest 500 companies as defined by market capitalization, it is automatically removed

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Selling is often more important than buying… especially if you are selling a stock that is down from where you purchased it.

DID YOU KNOW?

What blockbuster Hollywood motion picture premiered at the Loew's Grand Theater, which once stood on the grounds now occupied by MONTAG's office in downtown Atlanta's Georgia-Pacific Center? *(Answer on Page 4)*

A. Driving Miss Daisy

B. Gone with the Wind

C. Deliverance

D. Ben-Hur

E. Fried Green Tomatoes

Loss aversion may result in underperforming stocks staying in an investor's portfolio longer than they should.

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from the index. However, selling a stock for an individual investor can be a bit more complicated due to non-rule based biases.

One of the reasons sell disciplines receive such little attention is the human tendency to avoid losses. The idea of *loss aversion* was first proposed by Daniel Kahneman and Amos Tversky in an academic paper published in 1979. Their research showed that they emotional pain felt by a loss was twice as great as the joy felt from a gain of a similar dollar amount. As a result, many investors would prefer to allow the "paper loss" to remain in the investment account and hope that the stock will one day recover rather than selling the stock and realizing the loss. This and other work by Kahneman and Tversky became the foundation of what is today referred to as behavioral economics, the study of psychology related to economic decision making.

Return Required to Recoup Losses

Loss Incurred	Return Required for Breakeven
10%	11%
20%	25%
30%	43%
40%	67%
50%	100%
60%	150%

Every investor experiences losses; it is simply part of investing. However as we've just described, the concept of loss aversion for investors may result in underperforming stocks staying in your portfolio longer than they should, and this can be a major determinant of long term returns. The table above shows the return required to breakeven on an investment after experiencing moderate to very large losses. A loss of 10-20% can be recouped and stocks often make such moves but a loss of 50% requires the stock to double just to breakeven. Stocks very rarely double. If they do, it can take quite a while.

What ever happened to those stocks dropped from the S&P 500?

We took a look at all stocks removed from the S&P 500 between 2009 and 2016 that were not acquired (i.e., were removed from the index due to poor performance). There were 59 such stocks during the period. For our purposes, these stocks serve as a proxy for what underperforming stocks in a client portfolio might look like.

We compared the performance of those stocks to the index during the one-year and two-year period after they were dropped from the index. The median performance was -14.5% over one year and -16.8% over two years. In the sample reviewed, 71% of the stocks performed worse than the S&P 500 in year one and 76% performed worse over the full two-year period after being dropped from the index. In other words, the stocks that were removed from the index were appropriately dismissed, as they continued to underperform, indeed at an accelerating rate, after being removed.

Conclusion

The S&P 500 Index's sell discipline is based on a market capitalization rule. By exercising this simple mathematical procedure, the S&P removes stocks from the index that have underperformed, and show accelerating underperformance going forward. This is a sell discipline that helps mitigate losses and therefore lowers the threshold for stocks to recoup their losses.

Stocks can be sold for a number of reasons and our sell discipline is more complex than what is illustrated in this article. At MONTAG, we believe a sell discipline is an important step to protecting our clients' capital and generating long-term returns that enable our clients to reach their financial goals. M

Kent Shaw, CFA is a Portfolio Manager

COMPLIANCE MATTERS — *Stacey Godwin*

Protect Yourself from E-Mail Phishing

E-mail phishing attacks are increasingly on the rise in this new age of cyber fraud. You may wonder how to protect yourself against these constant threats and clever schemes. Here are some best practices for e-mail use:

- Don't click on links or reply to messages asking you to verify any type of personal information. If contact verification is required, look up the customer service e-mail address or phone number of the entity and contact them directly yourself.
- Don't reply to unsolicited e-mails, click on browser pop-ups or respond to phone calls warning that your computer has been compromised. These are almost always fake and responding in any way can put your personal information and finances at great risk.
- Be extremely cautious when clicking website links or ads sent via e-mail, unless you are absolutely certain they are from a legitimate source. Criminals are notorious for sending coupons and ads with malware embedded in these links.
- Be suspicious of (as in don't open or simply delete) e-mails from unknown senders, even if they appear to be personalized. Direct as much unsolicited e-mail traffic through your spam filter. M

Stacey Godwin is Chief Compliance Officer

UPCOMING EVENTS

EXECUTIVE BREAKFAST SERIES — **Tuesday, February 6, 2018** ***(7:30am — 9:30am)***

MONTAG hosts the next in our series of breakfasts when Christine Quillian, CFA/CFP, one of our Portfolio Managers, will make a presentation titled "Consumer Deliberations: Same Same, *But Different*". For more information, contact Steve Whittington — *Business Development Director*, at 678-539-8245 or via email at stevewhittington@montagwealth.com

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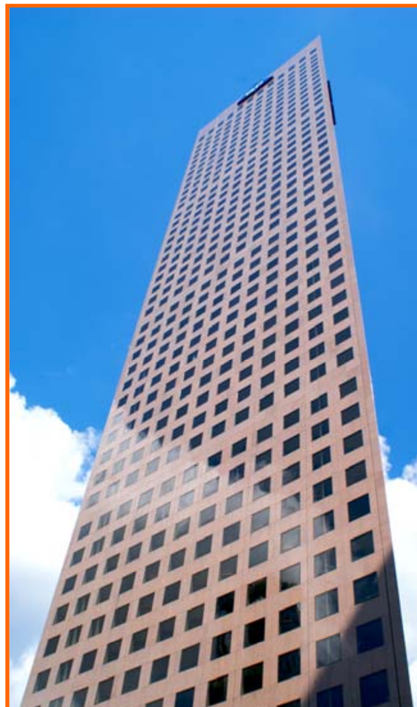
FACTS AND FINANCES FOR WOMEN — **Wednesday, April 11, 2018** ***(9:30am — 1:00pm)***

Please join us for a morning of presentations from MONTAG staff members, subject matter experts from outside firms, and remarks from an area non-profit organization. To reserve your place, contact Bill Lee — *Director of Marketing Operations*, at 678-539-8243 or via email at billlee@montagwealth.com

Location: 103 West, 103 West Paces Ferry Road NW, Atlanta, GA 30305



DID YOU KNOW? *(from page 3)*

Answer: B. *Gone with the Wind*, staring Clark Gable (Rhett Butler) and Vivian Lee (Scarlett O'Hara), premiered in December, 1939. Based on the best-selling novel by Atlanta author Margaret Mitchell, the movie version received 10 Academy Awards, including winning the Oscar for Best Picture.

The Loew's Grand Theater was heavily damaged by fire in 1978. Not long thereafter, construction began on Georgia-Pacific Center to be the company's headquarters. MONTAG relocated its offices to the 25th floor here in 2006.

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