SHAKER investments

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Dear Investor,

The fourth quarter of 2018 was difficult for US equity markets with sharp declines across all segments. Our accounts were down more than the S&P 500 Index due to greater exposure to small-cap, high growth stocks. This part of the market underperformed during the sell-off in the fourth quarter after having outperformed during the first nine months of the year. The small cap growth index (Russell 2000 Growth) declined 21.65% in the quarter. Declines of this magnitude often (but not always) foreshadow an economic recession, but most leading indicators are only pointing to a slowdown in growth.

We continue to believe that our core strategy of identifying high quality, high growth companies will generate excess returns over time, but we recognize that such companies can be more volatile in periods of market turmoil. However given the uncertainty in the Fourth Quarter, we made adjustments to your account to better position it for the potential of slower economic growth in 2019.

Periods of high volatility and market declines can be challenging as an investor, but it is important to remember that these events also create opportunities. When the market sells off sharply like it has over the last several months, both good and bad companies can fall significantly. We relish the chance to buy high quality companies at steep discounts to fair value and are actively looking for opportunities to upgrade our holdings. Though we have positioned your account more conservatively today, we are not deviating from our strategy of buying good companies at attractive valuations.

As always, your actual investment returns, including your statement of realized gains, are enclosed. The following is a summary of returns for selected major indexes for the fourth quarter, year-to-date, and last ten years:

	3 Months Ending 12/31/18	**12 Months Ending 12/31/18**	**Annualized Returns for 10 Years Ending 12/31/18**
S&P 500 Index	-13.52%	-4.38%	13.12%
Russell 3000 Index	-14.30%	-5.24%	13.18%
Nasdaq Composite Index	-17.29%	-2.84%	16.76%

Discussion of Fourth Quarter Performance

In the fourth quarter, virtually all of our investments were down with the market. Other than our energy investments, the biggest losers by dollar amount were our largest holdings, the same stocks that had been the biggest winners for the prior nine months.

For the year, our largest winners were Trade Desk (TTD), Abiomed (ABMD), Dexcom (DXCM), Insulet (PODD), CoStar Group (CSGP) and Paylocity (PCTY). Our largest losing investments were our collective investments in energy, homebuilders, and building material companies. In addition, Facebook (FB), Universal Display (OLED) and IPG Photonics (IPGP) underperformed expectations.

Investment Outlook for 2019

The investment environment for equities in 2019 is markedly different than in 2018. Investor psychology has gone from positive to negative, which is reflected in the price-to-earnings ratio of stocks. At the start of 2018, the S&P 500 traded at 19.0x forward earnings. Today it trades at 14.5x forward earnings, a 24% decline. Small cap stock valuation multiples have declined even more than those of large cap stocks.

We continue to believe that a recession is unlikely in 2019 given the strength of most domestic economic indicators, but we do expect economic growth to moderate in 2019. Since the beginning of the fourth quarter, global economic data has continued to indicate further slowdowns in growth. In January we received information that suggests international economic weakness may be impacting the domestic economy. The Institute for Supply Management (ISM) Manufacturing Purchasing Managers Index (PMI), a closely watched monthly survey that tracks US economic activity, declined from 59.3 in November to 54.1 in December. Declines of this magnitude in one month are rare, but it should be noted that the latest reading remains above 50 which signifies growth. Most other domestic indicators, such as employment and consumer spending, are still signaling solid economic activity and growth. The major downside risks to the outlook are a potential worsening trade war with China and the partial Federal Government shutdown. The negative economic effects of the shutdown will accelerate as its duration lengthens.

We have made small additional investments in January, but we still have more than normal cash in the portfolios. We will reinvest if we see attractive opportunities. Our largest investments are in the following companies:

<u>Technology</u>
Paycom Software (PAYC)
Broadcom (AVGO)
Alphabet (GOOG L)

<u>Health Care</u>
Dexcom Inc. (DXCM)
Abiomed Inc. (ABMD)
Insulet Corp. (PODD)

<u>Consumer Discretionary</u>
The Trade Desk Inc. (TTD)

<u>Producer Durables</u>
Costar Group (CSGP)
Paylocity Holding (PCTY)

<u>Financial Services</u>
Axos Financial Inc. (AX)
PayPal Holdings (PYPL)
Visa (V)

Stocks got to be very oversold in the Fourth Quarter, which typically results in a rally off of the lows. Even with that expectation, the market has rebounded strongly since December 25th. Rallies of similar strength and speed in the past have often resulted in significant further gains in the following 12 months. We have seen these uncertainties before. We are confident in the investment process we have in place, and Shaker Investments is prepared to take advantage of the opportunities in individual stocks as they unfold.

We look forward to updating you further as the year progresses.

Sincerely,

The Shaker Investment Management Team

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