

A t h e r e a n

Wealth Management, LLC

121 Newark Avenue, Suite 531
Jersey City, NJ 07302
Ph: 347-409-1499
cgettingh@atherean.com
<http://www.atherean.com>

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Dear Atherean Wealth Management client:

Enclosed is your portfolio summary report for the quarter ending September 30, 2019, as well as an investment advisory fee statement for the fourth quarter of 2019. The portfolio summary report shows the holdings in your accounts as well as an overview of your portfolio asset allocation as of the close of the third quarter of 2019. It also provides a summary of your investment objectives, time horizon, and risk tolerance as per our records. It is important that you review this information and let us know if any of it is incorrect.

Equity and Fixed Income Market Performance

We saw volatility return to global equity markets in August, with the S&P 500 experiencing several high volume, significant down days. We believe that much of this was a response to recession signals that the bond market was sending earlier in the summer, which we discussed in detail in our last quarterly letter. The U.S. treasury yield curve continued its downward shift across all maturities, and many bond market indices outperformed most equity indices again in the third quarter. Year to date the S&P 500 index is up 20.4%, the Russell 2000 small cap index is up 14.1%, the MSCI EAFE (Europe, Australasia and Far East) index is up 13.3%, the MSCI US IM Real Estate 25/50 Index is up 28.2%, and the Barclays U.S. aggregate bond index is up 8.3%, as of the end of the third quarter, on a total return basis. It is worth noting that many real estate indices have outperformed most equity indices so far this year. While real estate investments are not suitable for all investors, the outperformance of the asset class serves as a reminder of the importance of portfolio diversification across asset classes.

In September, we witnessed several trading days during which value stocks significantly outperformed the broader U.S. equity markets. While the S&P 1000 value index has for the most part underperformed the S&P 500 index over the past few years, we anticipate mean-reverting behavior of under-priced equities as this subset of the equity asset class has consistently outperformed the broader market over long time periods. This "value" factor, along with the "size" (market cap) factor, and the original "beta" factor of the capital asset pricing model, is one of the few "factors" which have been found to generate excess equity market returns over long time periods. In the next section we will discuss what "value" means to us as investment managers as well as more traditional definitions of "value" which we hear discussed from time to time in the financial media.

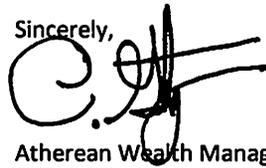
Portfolio management process: absolute value versus relative value, value stocks versus growth stocks

As we have discussed in recent quarterly letters, we primarily utilize a top down, asset allocation based approach in managing your portfolio. We generate exposure to asset classes via “passive”, market index tracking instruments in some cases and via individual security selection in other cases. Although we typically do not attempt to time the market with respect to making portfolio management decisions, we do from time to time attempt to purchase securities that are trading at discounts to their intrinsic values. In other words, we seek to purchase securities that are undervalued on an absolute value basis. Absolute valuation involves determining what an equity security is worth based upon the present value of estimated future cash flows. Once we have an idea of what we believe the security is worth based upon the valuation models that we build, we can determine whether or not the security is “on sale” or “undervalued”.

Much of the discussion in the financial press about “value” stocks revolves around relative valuation models, which involve purchasing securities which are priced at discounts relative to their peers. Relative value can be measured in several ways including the price/earnings ratio, price/book value ratio and the enterprise value/EBITDA ratio. “Value stocks” are stocks that are trading at levels such that their valuation ratios are attractive, or “cheap” compared with those of their peers. Although we do not use relative valuation explicitly when analyzing and selecting securities, we have found that the portfolios which we manage tend to be more heavily weighted toward “value” stocks than toward “growth” stocks. We see this as a confirmation and validation of our approach as there is much empirical evidence to suggest that “value” stocks have outperformed the broader market over long time periods, as discussed in the previous section.

Let us know if there are any changes to your financial profile or investment objectives. If you would like to review your portfolio and/or financial plan in greater detail, have any tax planning or tax advice concerns, or have any other questions or concerns, feel free to contact us.

Sincerely,

A handwritten signature in black ink, appearing to be 'C. J. Atherean', with a stylized flourish extending to the right.

Atherean Wealth Management, LLC