April 11, 2016

I began to write a cover letter that accompanied quarterly portfolio reports to New West Investment clients 16 years ago after the first quarter of 2000 in an effort to explain the craziness of the tech, telecom and large cap stock market bubble of that time. It was not until last Friday, April 1st that I realized that many first quarter letters that had gone out since then were dated April 1st, April Fools day! As such I decided to wait a couple of days to write this version so that the content of the letter would not be confused with a joke or a bad attempt at humor.

While the recent quarter lacked the most absurd examples of market (mis) behaviors, it still managed to set a couple of historic records. We started off with the biggest equity market declines over the first 10 days of the year ever and proceeded to decline over 10% by February 11th only to rebound and finish up 1% for the period as measured by the S&P 500 index, also a first. I am reminded of the late Gilda Radner's portrayal of fictitious news anchor Emily Litella on Saturday Night Live, who would mishear or misunderstand a question and go off on a rant, only to be corrected by a fellow anchor and finish up with "Never mind."

So what was all the fuss about? If you believe the media has some divine insight into why market prices move, it was concerns about a weakening Chinese economy causing a drop in commodity prices triggering increased junk bond defaults by commodity producers thereby negatively impacting bank balance sheets exacerbated by hawkish Federal Reserves Board members threatening higher interest rates driving the U.S. dollar higher creating a headwind for corporate earnings. Or maybe it was just more sellers than buyers.

At any rate the quarter finished with commodity prices recovering with oil specifically bouncing off a $26 per barrel low to close where it started in the mid $30's, junk bonds rebounded, bank balance sheets were spared massive defaults, the Fed reversed course and talked down interest rate expectations which weakened the U.S. dollar, easing the pressure on corporate earnings. And what about the Chinese economy? That concern has dropped out of the news headlines. Maybe it was all about the Fed and interest rate expectations after all.

As stocks traded down in January, and I attempted to explain this market action to my wife, I was struck by the obvious notion that we need this kind of volatility to justify our reasoned approach to investing and to create opportunities to buy investments at attractive prices. Were it not for the fact that stocks, and sometimes bonds, can decline precipitously in price, we would be misguided to invest in a balanced portfolio. And price declines are equivalent to items that we purchase going on sale, not something that should make us unhappy and want to sell our holdings but instead prompt us to buy more. Quoting Warren Buffett "You want to be greedy when others are fearful. You want to be fearful when others are greedy. It's that simple." There was some fear in the first quarter.

New West portfolios outperformed most of the stock market indices by a small amount in the period after adding significant value for clients with a much smaller decline than risk assets during the heat of the selloff in the first half of the quarter. In fact I used the market selloff to add to some existing positions and purchase some new investments at attractive prices. I was never anxious the U.S. economy would fall into recession due to the strong employment situation and the boost to consumers created by cheaper energy costs. My 2015 expansion of intermediate U.S. Treasury holdings and municipal closed-end bond funds added to investment performance in the quarter.

Broadly speaking, going forward interest rates are too low at this point to entice me to add to any type of debt investment and stock prices have recovered to an extent that I am not tempted to add to those positions given the muddle along economic environment. I am therefore combing through investment ideas looking for single situations that appear attractive and trimming some holdings in order to simplify portfolios.

Finally, after I had completed this letter and was just waiting to print it out, I came across an article in Barron's weekly magazine, a sister investment publication to the Wall Street Journal, on a topic that is dear to my heart. I decided to share the following excerpt dated April 9th of this year:

> Last week, the Labor Department issued a new set of rules mandating that stockbrokers, insurance agents, and financial advisors must choose investments with their clients' best interests in mind. Sounds like a no-brainer, right? It should be, and for registered investment advisors, who have long been held to a higher standard, it is.
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> But brokers and insurance agents—along with other professionals you may loosely have referred to as "advisors"—had been beholden to a mere "suitability" standard. This meant that as long as the investment products weren't wildly inappropriate, brokers were free to sell clients whatever funds, annuities, private real estate investment trusts, or what have you that offered the broker the biggest commission.
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> The new rules mandate that anyone helping to manage your 401(k), individual retirement account, or other retirement plan be held to the higher, "fiduciary" standard. The change is a big deal. Now, your broker must truly be able to justify why a particular product is in your best interest—and not his. Often, that boils down to: "Is there a cheaper comparable product?" The new rules, which won't go into full effect until 2018, don't go as far as a draft promulgated a year ago, leading Wall Street analysts to call them "better than feared" and "less radical"—for the industry, that is.

New West Investment Management, Inc. has always been a registered investment advisor. The above states that "registered investment advisors, who have long been held to a higher standard," as if being a fiduciary were some kind of a burden. At New West Investment I have not "been held" to the standard, I have celebrated and embraced it for 25 years. In fact I left the brokerage industry in 1990 and started this firm because I could no longer tolerate what the article calls the "suitability" standard, maybe better titled the "buyer beware" standard. The idea of requiring investment salespeople to act in clients' best interests has been in the works since the 2008 financial crisis which raises two questions: Why did it take a crisis for regulators to act? And why has it taken so long to implement the rule change? I guess that is the nature of government.

Enclosed please find your most recent portfolio report covering periods from inception through March 31, 2016. Please contact me if I may be of assistance. As required by regulatory authorities, New West Investment Management, Inc. has updated Form ADV Parts 1 and 2, A & B for year-end 2015. There are no material changes to report. You can review the current versions at www.adviserinfo.sec.gov or contact our office, if you prefer that we send you a copy.

Best regards,

Peter V. Hedberg, President