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Berkshire Hathaway's Annual Letter to Shareholders: Singing Harpswell's Tune.

Below is an exert from Warren Buffet's annual letter to shareholders. Mr. Buffet has always been critical of those investment advisors with high fees and has also regularly sung the praises of a Vanguard-centric portfolio. His example, below, refers directly to endowments and we feel the Oracle of Omaha is spot on! Harpswell, as you know, strives to minimize all fees (including ours) and we also see the virtue of having a healthy dose of low-fee passive funds in our portfolios!

"Let's put numbers to that claim: If my $114.75 had been invested in a no-fee S&P 500 index fund (in 1942), and all dividends had been reinvested, my stake would have grown to be worth (pre-taxes) $606,811 on January 31, 2019 (the latest data available before the printing of this letter). That is a gain of 5,288 for 1. Meanwhile, a $1 million investment by a tax-free institution of that time – say, a pension fund or college endowment – would have grown to about $5.3 billion. Let me add one additional calculation that I believe will shock you: If that hypothetical institution had paid only 1% of assets annually to various "helpers," such as investment managers and consultants, its gain would have been cut in half, to $2.65 billion. That's what happens over 77 years when the 11.8% annual return actually achieved by the S&P 500 is recalculated at a 10.8% rate." – ***Warren Buffett***

Fund Focus - Parnassus

Harpswell prides itself on our team's investment depth that comes with decades of experience working on the institutional side of the finance industry. Our team's institutional foundation was set at some of the world's most well-regarded mutual funds, hedge funds and global endowment/family investment advisors, and it is this experience that differentiates us from our retail brethren. This level of experience gives us a valuable perspective that translates into an ability to assess and analyze prospective fund managers. In fact, Harpswell has been day-one investors for five funds over the last six years (and we are happy with all five). This highlights Harpswell's investment process which focuses on people and a sustainable process rather than simply screening for past performance (which generally isn't sustainable).

Last year we added a unique fund to our roster of investments, and it proved to be quirky timing as the fund was experiencing one of its worst relative performance drawdowns ever. The fund came to our attention from our Advisory Board; however, we also do our homework and base a decision off of well-reasoned and objective analysis. The fund was an institutional offering from Parnassus and we were intrigued even prior to our manager interviews. The firm places a high regard on corporate governance and sustainability—two factors Harpswell values—and its internal policies fostered almost nonexistent turnover among its investment team. In performing our due diligence, our initial focus was on the team and then we turned to assess the sustainability of returns given their particular focus and style.

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Great first quarter of 2019!
What should we expect for the rest of 2019?

The markets had a considerable bounce in the first quarter coming off an atrocious fourth quarter of 2018. With respect to small and midcap stocks, the quarter ranks as the sixth best over the last 40 years. As we look ahead to the remainder of 2019, we reflect on ten of the best first quarters over this time horizon and frame our expectations. Historical returns are hardly a predictor of future performance; however, it is interesting to look at where we are in the context of this bounce and current market valuations. We will note that Harpswell bases our investment views on fundamentals rather than on market technical. However, we also recognize some element of a mean reversion in long-term returns.

While a very limited data set of ten offers little statistical significance, we would note the March P/E ratio for this year is 19.1, well above the median for the years cited. Furthermore, the dispersion in performance for the remainder of the years—bifurcation among high P/E and low P/E years—was significant in these years. To summarize, we should take the instances noted below with a grain of salt; but, historically, in years where the first quarter performance was noteworthy, the remainder of the year's performance was negative when valuations (P/E) were above 16.5X (March 2019 = 19.1).

Russell 2000 (Small/Mid Cap) Best 1st Quarter Performances

Best 1st Quarter	First Quarter	Next 9 Months	Full Year	March P/E
1Q91	29.7%	12.6%	46.0%	14.4X
1Q87	24.2%	-26.6%	-8.8%	16.7X
1Q88	19.1%	5.0%	25.0%	12.2X
1Q83	17.4%	10.0%	29.1%	10.9X
1Q79	16.9%	22.4%	43.1%	6.6X
1Q19	14.6%	?	?	19.1X
1Q86	14.2%	-7.4%	5.7%	14.8X
1Q06	13.9%	3.9%	18.4%	18.8X
1Q85	13.9%	15.0%	31.0%	10.5X
1Q12	12.4%	3.5%	16.3%	15.8X
1Q13	12.4%	26.5%	38.8%	16.4X
Average	17.2%	6.2%	24.5%	14.2X
Below Median P/E	19.4%	13.0%	34.9%	10.9X
Above Median P/E	15.3%	-0.6%	14.1%	16.5X

Source: Jefferies, FactSet, FTSE Russell

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Advisory Board – Q1 2019

Harpswell met with its Advisory Board on March 25, 2019 for the Board's quarterly review and conference. We feel exceptionally grateful for the expertise and insight of our Board, Mauricia Geissler, Chief Investment Officer for Amherst College, and Gus Sauter, former Chief Investment Officer for the Vanguard Group. The conference began with a review of firm updates, including new clients joining us this year, and the calendar-year performance and asset allocations across the firm.

Harpswell and the Advisory Board also discussed the active portfolio managers at length as part of our ongoing review process. One active manager in the domestic large cap space had a difficult year, but Harpswell is still comfortable with the overall strategy and process in place and believes they are a high-quality manager that will continue to add value long-term. One of our active emerging markets managers outperformed their peer group, while those with larger exposures to Asia struggled to stay close to their benchmark, as China had a difficult year. We continue to monitor our managers closely and look for any changes to process, people and stated mandate.

Harpswell closed the meeting with a discussion of market insights. Ms. Geissler noted that sometimes the hardest part of this kind of market is to "do nothing." Mr. Sauter feels the markets are soft, and we could see more moderate equity returns moving forward. For a deeper discussion of current markets, please contact Jack Moore.

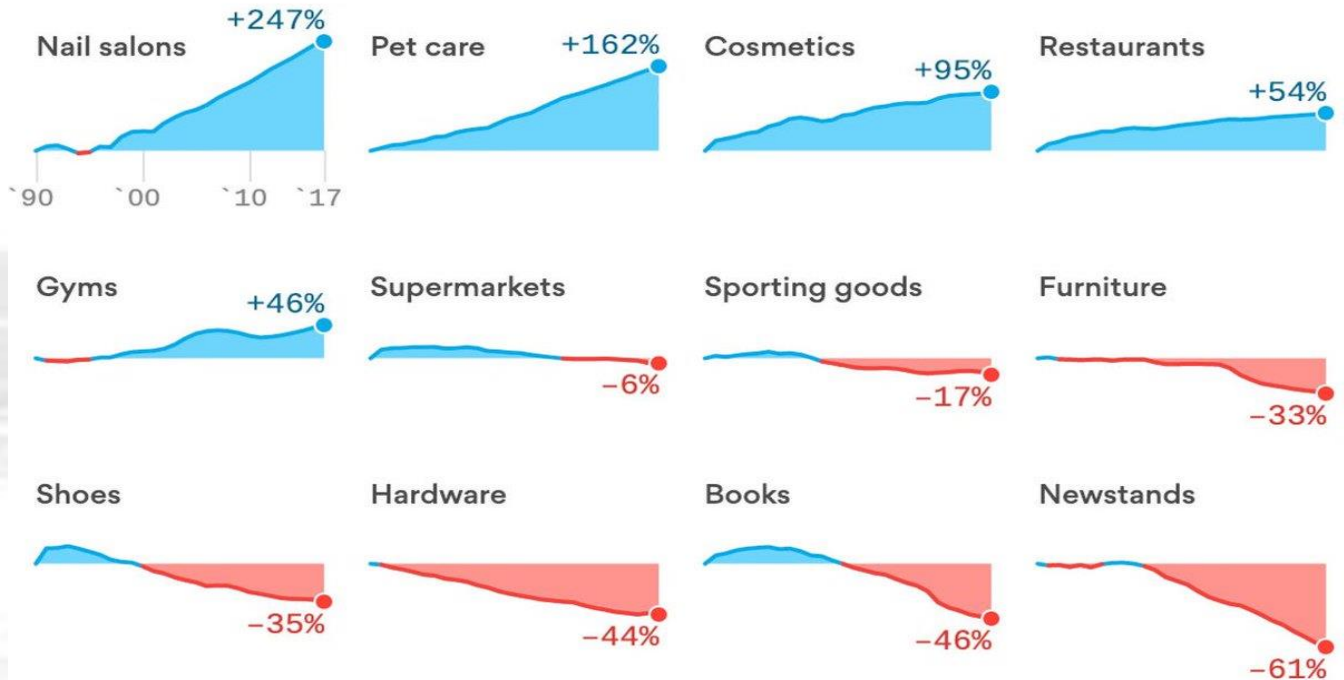
The Changing Face of Retail

Harpswell is fascinated with global economic and technological evolution that periodically shifts into high gear (or warp speed, as it seems today) and fosters change at a remarkable pace. Historic instances where change occurred at a similarly disruptive pace as today certainly include the agricultural era of the 1920s, when the tractor replaced thousands of field workers, as well as the industrial revolution. While those periods differed in many ways, the result was an enormous population being displaced by technology. A silver lining today might be the notion that we now have a much better safety net in place.

Ground zero for destruction in these eras of rapid change tends to be where the debt levels are highest and the shift in business results in the displaced businesses dragging investors down with them. Disruptive entrants recognize the opportunities associated with liability-ridden industries and target them because their lack of financial flexibility precludes them from effectively reacting to a new threat. Examples of this tactic occur across a number of industries and are exemplified in the healthcare sector. Hospitals are experiencing a headwind as drug stores offer various services (*e.g.,* dialysis, flu shots, diagnostic tests, *etc.*) where barriers are low and margins are high. Hospitals, over many years, have built up their facilities (frequently utilizing leverage) and now face an unforeseen dynamic where their margins are chipped away by new entrants. The retail sector is clearly one space where the impact of unforeseen "e-competition" is extraordinarily disruptive as the "Amazon effect" is far-reaching. Harpswell feels we are in the third inning of repercussions associated with the proliferation of e-competition and the impact will certainly extend beyond retail to real estate, finance and technology (where there will be some big winners as well as many losers).

The Changing Face of Retail *(continued from page 3)*

A massive transition in the real estate world associated with economic evolution has been occurring for years and is certain to continue to evolve. Up until now, we feel the shift in real estate associated with e-commerce has been relatively benign as old economy businesses are slowly replaced by higher margin service-oriented business. The visual below highlights several of the casualties and beneficiaries of these trends.



Source: Goldman Sachs

The shifts in real estate demand have efficiently ushered in new entrants who can better support real estate costs with higher margin services or products. Merchants paying for retail space have clearly become susceptible to either e-commerce or larger players with scale, lower costs and lower prices. These two trends are exemplified by shoe stores and Zappos, as well as local hardware stores and Home Depot.

Looking ahead, e-commerce penetration is expected to continue to grow and investors' concerns are growing as well. Investors' fear comes from the fact that the pace of e-commerce penetration is growing faster than new entrants can step up. Below is a chart from a recent UBS study which suggests e-commerce penetration is expected to grow by 64% between 2019 and 2026, and the impact will be over 83,000 store closures.

The Changing Face of Retail *(continued from page 4)*

	Estimated Online Penetration - 2019	Number of Stores Current	Est. Ecom. Penetration 2026	Ecom Growth 2019-2026 (%)	Number of Stores 2026 (est)	Est. Net Store Closures
Clothing & Accessories	23%	122,693	36%	57%	101,979	20,710
Consumer Electronics	35%	45,148	45%	29%	35,307	9,840
Home Furnishings	21%	47,552	35%	67%	39,125	8,430
Sporting Goods	20%	23,243	30%	50%	17,358	5,890
Gen. Merchandise	10%	64,282	18%	80%	58,568	5,710
Office Supplies	20%	7,608	30%	50%	5,682	1,930
Home Improvement	4%	69,366	12%	200%	68,747	620
Auto Parts	8%	57,620	15%	88%	57,557	60
Groceries	2%	89,530	10%	400%	82,221	7,310
Total Retail	14%	829,376	23%	64%	746,359	83,020
	Source: UBS					

As lower interest rates over the last ten years have encouraged both leverage and risk taking, the next chapter of closures, particularly those for shopping malls, may be more painful. The Bangor Mall, for example was valued at over $125MM in 2007 before its owner took out a loan for $80MM. The mall just this year, in default, sold for $14.95MM. Harpswell recently attended an institutional real-estate forum at Harvard and met with professionals who specialize in transforming malls into senior living and healthcare facilities. Clearly Bangor's demographics would not support such an undertaking; however, it does highlight the dawn of a new bifurcation of winners and losers associated with our evolving economy.

Source: UBS

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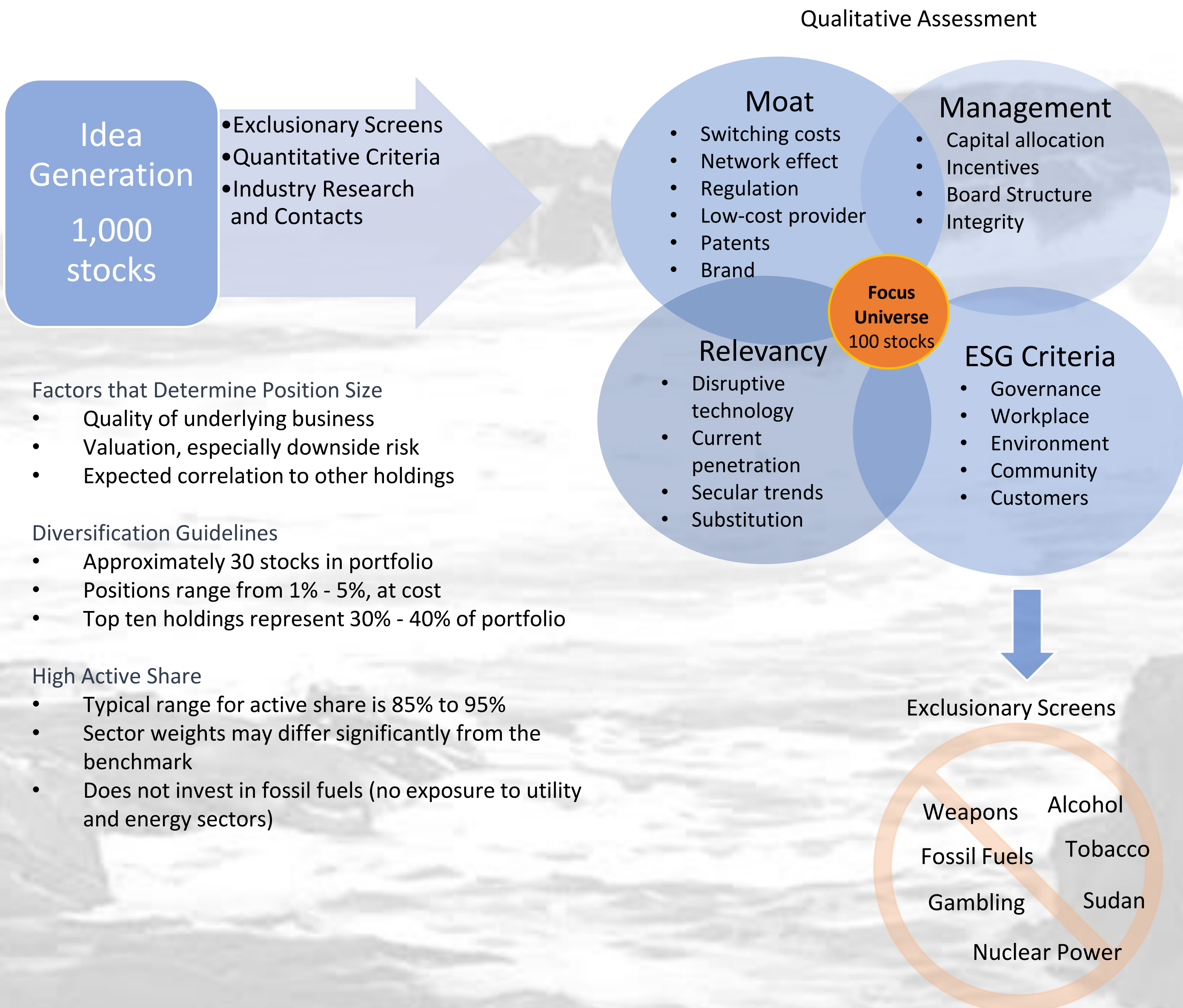
Fund Focus – Parnassus *(continued from front page)*

The fund is quite concentrated (*i.e.*, has a very limited number of holdings) and one would, therefore, expect periods of meaningful tracking error relative to their benchmark (we favor funds which are not simply trying to replicate their benchmark). We felt the origin of the recent poor performance was not the byproduct of a firm issue but merely a mistake that is expected to occur on occasions Our conclusion enabled us to make a timely investment in a firm that was coming out of a difficult period, and we were happy to take the place of the performance-chasing investors who were exiting the fund.



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Monthly Flash Report March 2019

Overview: GDP increased at a 2.2% annualized rate as reported by the Commerce Department in its 3rd reading of 4th quarter GDP growth. This was down from the 2.6% pace estimated in February. The revision reflected markdowns to consumer and business spending as well as government outlays and investment in homebuilding. The Federal Reserve did not raise rates at its March meeting and implied that no rate increases are likely in 2019. The Fed also announced that it will slow its balance sheet reduction program in May and then end it at the end of September.
UK lawmakers rejected PM May's Brexit deal for a 3rd time on Friday, moving the country into political turmoil. The agreement was defeated by a 344 to 286 vote which came on the same day that the UK was originally supposed to leave the EU. The new deadline is April 12.

Equities: The S&P 500 returned 1.9% in March, ending the quarter with a 13.7% gain. The dovish shift by the Fed and optimism concerning trade negotiations with China have contributed to the market's gains. Growth stocks significantly outperformed Value across all markets YTD. Energy, Technology, Real Estate & Industrials were the leading sectors while HealthCare lagged. Markets rose despite expectations that the quarter will show a 3.9% year-over-year decline in earnings for the S&P 500.
The Russell 2000 index lost 2.1% in the month but gained 14.6% this quarter, reflecting increases of 17.1% for Growth and 11.9% for Value stocks.

EAFE increased 0.7% in March where the stronger Dollar lowered gains by 0.7% versus local currency returns. EAFE earned 10.1% in the Qtr. The UK pound fell nearly 2% as Brexit negotiations stalled. Hong Kong (15.6%), Italy (14.7%) and Switzerland (13.5%) were the leading countries YTD for the international developed markets. Japan (6.9%) & Germany (7.0%) had the lowest gains for the same period.
The Emerging Markets increased by 0.9% in March. The strong Dollar detracted approximately 0.5% from local currency returns. The markets rose by 10% for the quarter. China increased 2.4% for the month for a YTD gain of 17.7% as trade negotiations remained optimistic. India posted an impressive 9.2% return in March ending the quarter with a 7.2% gain. Russia had a strong start to the year with a 12.2% return.

Fixed Income: The 3-month T-bill yield fell modestly by 5 bps to 2.38% as the Fed held rates at its March meeting. The 10 Year Treasury yield declined markedly in the month by 30 bps to 2.41%. The yield curve remained inverted from 6 months to nearly 10 years. A narrow yield spread of 43bps between the T-Bill and 30 Year Treasury remained at month's end. The 30 Year Treasury yield declined by 27bps to 2.81%. Yields fell as concerns about a slowdown in global growth intensified. The 30Year Municipal yield fell by 34bps, closing at 2.72%, 9bps lower than the 30 Year Treasury. The 1Year Municipal yield ended the month at 1.51%, an 8bps decline from Feb, maintaining the yield spread discount compared to the 1Year Treasury at 37%. The spread discount declines with longer maturities until yields for both municipals and Treasuries are almost equal at 30 years.

German rates declined in Mar ending with a negative 0.6% yield for the 2Yr Bund and a negative 0.07% for the 10Yr, a 25bps drop in the month . In the UK, the 10Yr Gilt yield moved down 31 bps to a 0.99% despite ongoing concerns regarding the Brexit implementation. The Japanese 10Yr Gov't bond yield fell another 7 bps for the month, yielding a negative 0.1%, while the 2Yr closed at negative 0.19%. High Yield bonds moved up in March by approximately 0.9% with an average yield of 6.2%. The High Yield market has shown resiliency this year given the losses realized at the end of 2018.

	1 Month	3 Months	YTD	1 Year	3 Years	5 Years
Domestic Equities						
Dow Jones	0.2%	11.8%	11.8%	10.1%	16.4%	12.2%
S&P 500	1.9%	13.7%	13.7%	9.5%	13.5%	10.9%
Russell LG Value	0.6%	11.9%	11.9%	5.7%	10.5%	7.7%
Russell LG Growth	2.9%	16.1%	16.1%	12.8%	16.5%	13.5%
Russell 2000	-2.1%	14.6%	14.6%	2.1%	12.9%	7.1%
NASDAQ	2.6%	16.7%	16.7%	10.5%	17.9%	14.3%
MLP Index	3.4%	16.8%	16.8%	15.1%	5.7%	-4.7%
REIT Index	4.2%	16.7%	16.7%	19.5%	8.0%	9.8%
International Equities						
EAFE	0.7%	10.1%	10.1%	-3.2%	7.8%	2.8%
EAFE Small Companies	0.2%	10.8%	10.8%	-9.0%	7.9%	4.8%
Emerging Markets	0.9%	10.0%	10.0%	-7.1%	11.1%	4.1%
China	2.4%	17.7%	17.7%	-6.1%	16.2%	9.7%
Fixed Income						
US Agg	1.9%	2.9%	2.9%	4.5%	2.0%	2.7%
US High Yield	0.9%	7.3%	7.3%	5.9%	8.6%	4.7%
Municipal Bonds	1.6%	2.9%	2.9%	5.4%	2.7%	3.7%
Currencies						
EURO	-1.4%	-2.0%	-2.0%	-8.8%	-0.6%	-4.0%
British Pound	-1.8%	2.1%	2.1%	-7.1%	-3.3%	-4.8%
Japanese Yen	0.3%	-1.2%	-1.2%	-4.4%	0.6%	-1.3%
Commodities						
Bloomberg Commodity	-0.2%	6.3%	6.3%	-5.3%	2.2%	-8.9%
S&P GSCI Crude Oil	4.7%	30.7%	30.7%	-4.3%	9.4%	-18.8%
Gold	-1.6%	0.9%	0.9%	-2.8%	0.8%	-0.4%

Commodities: WTI Crude Oil closed higher to $60.14/barrel, a $2.9/barrel increase in Mar. YTD price increases are the result of supply concerns associated with sanctions levied against Iran and Venezuela. Also, OPEC exports have declined to 4 year lows in March. Gold prices fell again by $18/oz to $1298/oz in the month. Gold has been pressured this year as inflation remains quite low and the Fed has delayed its rate increases for at the least the early part of 2019.

DISCLOSURE

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Risks

Harpswell invests in stocks, bonds, mutual funds and sometimes alternative investments. Each asset class, along with each individual investment, carries varied degrees of risk of loss. Harpswell analyses investments from a long-term fundamental perspective and aims to engineer portfolios that have an attractive risk and reward balance. Despite a strong bias for diversification, all Harpswell portfolios do carry risks of losses, particularly in times of escalated market volatility. Harpswell does focus on capital preservation yet extraordinary markets can potentially generate material losses.

Our investment decisions and recommendations are based upon our professional judgment. We do not guarantee the results of any of our investment decisions or recommendations, the future performance of your Assets or Accounts, any specific level of performance, the success of any Independent Manager, investment decision, strategy or recommendation made by an Independent Manager, or the overall success of the Account. Past performance is not indicative of future results. Investments in your Account may go up or down in value depending on market conditions.

Alternative investments are designed only for sophisticated investors who are able to bear the economic risk of losing all of their investment. Alternative investments: (1) often engage in leveraging and other speculative investment practices that may increase the risk of investment loss; (2) can be highly illiquid; (3) are not required to provide periodic pricing or valuation information to investors; (4) may involve complex tax structures and delays in distributing important tax information; (5) are not subject to the same regulatory requirements as mutual funds; and (6) often charge high fees.

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Market index information shown herein, such as that of the S&P 500 Stock Index, is included to show relative market performance for the periods indicated and not as standards of comparison, since these are unmanaged, broadly based indices which differ in numerous respects from the portfolio composition of the Fund. Market index information was compiled from sources that Harpswell Capital Advisors believes to be reliable. No representation or guarantee is made hereby with respect to the accuracy or completeness of such data.

Index Definitions

The S&P 500 Stock Index is an unmanaged market capitalization index of 500 US equities generally considered to be representative of US stock market activity. The Morgan Stanley Capital International World Index is a market capitalization-weighted equity index of over 1,500 stocks traded in 22 world markets. The NASDAQ Composite Index measures all NASDAQ domestic and non-U.S. based common stocks listed on the NASDAQ Stock Market. The Index is market value-weighted. The SB World Bond Index is a market capitalization weighted index of 18 Government bond markets composed of sovereign debt denominated in the domestic currency. The Lehman Aggregate Index is a benchmark index made up of the Lehman Brothers. The Hennessee Hedge Fund Indices® are calculated from performance data obtained from publicly available information, internally developed data and other third party sources believed to be reliable. MSCI EAFE is a stock market index that is commonly used as a benchmark for the performance of major international equity markets. The MSCI Emerging Market Index is an index created by Morgan Stanley Capital International (MSCI) that is designed to measure equity market performance in global emerging markets. The Russell 1000 seeks to track the investment results of an index composed of large- and mid-capitalization U.S. equities. The Russell 2000 seeks to track the investment results of an index composed of small-capitalization U.S. equities. The Russell 2500™ Index measures the performance of the small to mid-cap segment of the U.S. equity universe, commonly referred to as "smid" cap. The Barclays Capital Global Aggregate Bond Index is designed to be a broad based measure of the global investment-grade, fixed rate, fixed income corporate markets outside the United States. The Barclays Capital US Gov/Credit bond Index measures the performance of U.S. Dollar denominated U.S. Treasuries, government-related and investment grade U.S. corporate securities that have a remaining maturity of greater than one year.

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