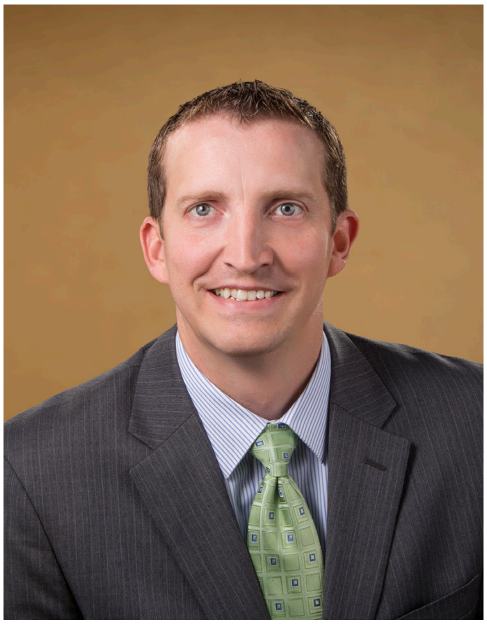
THE TRUST COMPANY

INVESTMENT & WEALTH MANAGEMENT UPDATE

JANUARY 12, 2018



CHANGING OUR BEHAVIOR TO CHANGE OUR INVESTMENT RESULTS

Michal Emory, CFA, Vice President & Chief Investment Officer

I am going to say from the outset that this is not your typical "2018 Outlook" article. And that is because I believe that examining our behavior is more important than correctly guessing, I mean forecasting, what will happen in 2018. In October, I said I would have a blog post later in the month about how successful investing is more of a behavioral exercise. I decided to hold off until now to be able to expand more on the topic.

When we encounter something that we do not understand, our mind immediately scrambles to construct a mental model that enables us to "understand" what is before us. Our mind is so great at taking these complex situations or problems and constructing these mental models that we usually do not realize that it is happening, much less that the mental model may not be accurate.

Sometimes, these mental models are a great help. When we are trying to catch a ball, we do not stop and do the math to figure where to run or how fast to run or what angle to hold our hands. We just look at the ball and run to it. Sometimes, though, these mental models can trick us.

We often don't know what we don't know, and that can severely hamper our investment results. When we hear or see something that we do not understand, our mind immediately (and unconsciously) forms this mental model to help us "understand" what is before us. Or our mind will eagerly accept a mental model thrust upon us by those in the financial news. Our mind uses mental models to handle the problem of "we don't know what we don't know."

Take my three-year-old son, Cole, as an example.

He knows that every morning, he gets in dad's truck and dad drives him to preschool. Then dad drops him off to play with his friends while dad goes to work. Eventually, dad will return to pick him up and take him home to see mom and big brother.

His mind cannot comprehend why dad goes to work, what dad does at work, or how that work allows him to have a bed to sleep in and food to eat. His simple mental model tells him that mom and dad have food for him when he is hungry. That dad (or mom) always comes back to pick him up after he has played with his friends at preschool. That his family is always ready to give him a hug. And that at the end of every night, he will have a

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CONTACT US

800 Poyntz Avenue, P.O. Box 1806
Manhattan, KS 66505
785.537.7200

4210 Philips Farm Road, Suite 109
Columbia, MO 65201
573.876.7000

333 West 9th Street, Suite A
Lawrence, KS 66044
785.371.9555

908 Broadway, Suite B
Marysville, KS 66508
785.562.2344

5960 W. Parker Rd., Box 278-124
Plano, TX 75093
972.342.6643

THETRUSTCO.COM
800.285.7878

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warm bed that mom or dad will tuck him into.

He cannot understand the why or how all this happens or that some kids are not so lucky. In his mind, this is what happens every day unless mom or dad tell him it is the weekend. His mind has developed a mental model that makes his routine make sense to him even though that mental model is not accurate. He, also, cannot comprehend that his mental model may have shortcomings.

Investing is a precisely imprecise endeavor. It is precise in that we can precisely measure how a company (not the company's stock) performed by looking at their bottom-line results. It is imprecise in that we cannot precisely predict how markets will react to those precise results. Because of this imprecision, our mind develops mental models that try to insert precision where precision is not possible. Our mind, also, develops these mental models to protect us from feeling as if we did not know something that we "should have" known. That is, essentially, what the saying "hindsight is 20-20" is alluding to. Looking back on 2017, our mind can construct many reasons why it was easy to see that the stock market would not have even a 3% pullback. If we are honest though, we would admit that if our 2017 self could go back in time and tell our 2016 self that the stock market would not have even a 3% correction, we would not believe it.

> "We often don't know that we don't know, and that can severely hamper our investment results."

Here is an example to illustrate this. Company A has a negative $8.56 earnings per share (EPS) over the last 12 months. This compares to a negative $6.45 EPS over the previous 12 months and a projected negative $10.20 EPS over the next 12 months. Company B has a positive $4.38 EPS over the last 12 months. This compares to a positive $2.73 EPS the previous 12 months and a projected positive $6.22 EPS over the next 12 months. Company A is also burning through cash at an astounding rate and is not expected to be cash flow positive until 2020, while Company B is seeing good growth in their cash flow.

Which company do you want to invest in? One stock was up almost 46% in 2017 while the other was down almost 10% in 2017. Which stock was up, and which stock was down? It seems easy, right? Most of us would assume that Company A was down, and Company B was up. Would you believe me if I told you that Company A was up almost 46% despite losing more money than the previous year and with the expectation that it will

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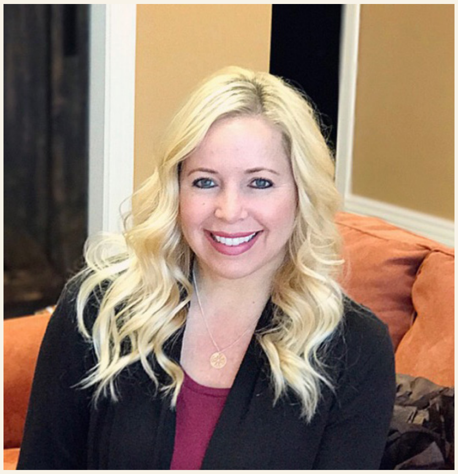
COMPANY NEWS

Chelsy Parsons Earns CFP® Certification

Chelsy Parsons, Account Administrator on Katie Seay's team in Manhattan, has been authorized by the Certified Financial Planner Board of Standards (CFP Board) to use the CERTIFIED FINANCIAL PLANNER™ and CFP® certification marks in accordance with CFP Board certification and renewal requirements.

Chelsy joined The Trust Company in 2016. She is a 2011 K-State graduate with a B.S. in Personal Financial Planning. We are proud to have such a dedicated and caring professional among us. Congratulations, Chelsy Parsons, CFP®!



Meet Jenny Hayes

Jenny Hayes is the newest addition to our staff, having joined our team in Columbia as Account Administrator.

Jenny has an extensive background in human resources and office administration. She is a member of the Society for Human Resources Management (SHRM), and is certified as a Professional in Human Resources (PHR). A California native, Jenny holds a Bachelor of Science from California Polytechnic State University.

Jenny commented, "The client relationships here are exceptional. This level of customer service is wonderful to be a part of." Likewise, we are glad to have Jenny's enthusiasm and passion for helping others. Please join us in welcoming Jenny!

Market/Index	2016 Close	As of 9/29	2017 Close	Month Change	Q4 Change	2017 Change
S&P 500	2238.83	2519.36	2673.61	0.98%	6.12%	19.42%
Nasdaq	5383.12	6495.96	6903.39	0.43%	6.27%	28.24%
DJIA	19762.60	22405.09	24719.22	1.84%	10.33%	25.08%
Russell 2000	1357.13	1490.86	1535.51	-0.56%	2.99%	13.14%
Global Dow	2528.21	2907.67	3085.41	2.38%	6.11%	22.04%
Fed. Funds	0.50%-0.75%	1.00%-1.25%	1.25%-1.50%	25 bps	25 bps	75 bps
10-year Treasuries	2.44%	2.33%	2.41%	0 bps	8 bps	-3 bps

ANNUAL MARKET REVIEW

Overview

The year 2017 was eventful, to say the least. President Trump and Congress tried, without success, to repeal the Affordable Care Act, known as Obamacare. However, the new year-end tax law included the elimination of the individual health insurance mandate.

The U.S. economy started slowly but picked up steam as the year progressed. The gross domestic product expanded at an annual rate of 3.2% in the third quarter. The unemployment rate fell from 4.7% to 4.1%, while upwards of 2 million new jobs were added. The Federal Reserve, based on the strength of the economy and labor market, began to roll back its stimulus program and raised interest rates three times during the year.

The stock market reached several historic highs in 2017. Consumer income rose and purchases increased, but inflation remained stubbornly below 2.0%. Business investment expanded in 2017 and is expected to surge in 2018. The year ended with the passage of sweeping tax reform legislation.

The Markets

Equities

The stock market saw several benchmark indexes reach record highs throughout 2017. Strong corporate profits and a general upswing in domestic and global economic growth helped push equities to new highs. Market volatility was historically low throughout the year, as the benchmark indexes saw very few weeks of negative returns.

Bonds

Interest rates moved incrementally higher, while the demand for long-term bonds was marginal. Yields on 10-year Treasuries were volatile for the second straight year, ultimately falling below their 2016 year-end totals. The yield on the benchmark 10-year Treasuries closed 2017 at 2.41%, down from the 2016 yield of 2.44%.

FOMC/interest rates

The Federal Open Market Committee raised interest rates three times during 2017. Following each rate increase, the Committee expressed the expectation that the labor market would remain strong and the economy would continue to expand, while noting that inflation has not risen as quickly as anticipated.

Eye on the Year Ahead

The year 2018 is off to a rousing start, with the passage of major tax overhaul legislation that could impact consumer and business income and equities. The U.S. economy, which got off to a slow start in 2017, picked up steam throughout the year and enters 2018 in pretty good shape. The U.S. economy as well as major world economies are expected to continue to grow this year. The Fed has indicated that it expects to raise interest rates three times this year despite stubborn inflationary expansion.

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lose even more this year? It seems to be an imprecise reaction to a precise result, right?

Now what if I told you Company A was Tesla and Company B was Celgene (a biotech company that makes products for cancer and arthritis treatment). Does that make it easier to believe that Company A was up 46% last year? But why does it make it easier? Is it because our mind has a mental model built around Tesla? And that mental model

tells us that Tesla is an innovative company and because of that, a return of 46% seems reasonable regardless of their precise results? But if we step outside that mental model, we can start to have questions. Now, I am not trying to bash Tesla. I think Elon Musk is a true genius and I would not bet against him. But I can like a company and not like the stock.

I have no idea if Tesla shares are going to $1,000 or going to $0. But I do know that too many investors (both professional and otherwise) get tricked by their mental models and do not stop to ponder whether Tesla (or fill-in with any company) can be a great company AND be a bad stock at its current price. They do not ask, "What if I don't know what I don't know about Company X and I am wrong?" The ability to hold these competing thoughts and question if we know what we think we know is very important in investing. How does this impact how you and I should think about investing?

One, accept the imprecision of an expectation versus wanting the precision of a forecast. There is a difference between expecting a correction in 2018 and forecasting that it will hit in January 2018. The former allows me to prepare for the inevitability of an event even though I imprecisely know when it will occur. Meanwhile, the latter dictates action at a precise moment. The former acknowledges that I don't know what I don't know, while the latter assumes I am clairvoyant.

Two, be willing to step outside the mental models forced upon us either internally or externally. Ask more "what if" questions. Our mental model may tell us that markets are too high, and we need to get out. But what if the markets keep going up? How do we know to get back in? Or what if we do have a 10% correction? Does that truly change our ability to reach our investment goals?

Three, focus more on our behavior than on the noise around us. In the decade of the 2000s, the CGM Focus fund was up more than 18% annually. The average investor in the fund, though, lost an average of 11% per year in the fund. How is that possible? The fund had a great year in 2007 and investors' mental models were telling them they did not want to miss out and rushed into the fund. Then in 2008, the fund was down dramatically and now the mental models were telling investors to rush out of the fund after they had big losses. If investors had focused more on their behavior, then maybe they would have avoided the whipsaw.

As we begin 2018, let us endeavor to focus more on our behavior and less on getting trapped by our mental models. Thanks for enduring through my lengthy thoughts. At The Trust Company, we look forward to our continued relationship with you and thank you for allowing us to partner with you in reaching your financial goals.

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