A View From Here - April 2019

"Courageous convictions will drag the dream into existence." â€• Neil Peart

March delivered another increase in our investment accounts and at the end of the first quarter, most portfolios are ahead - well into the double digits. We hope this isn't just luck as our investment holdings, including ones stuck in reverse, have been reporting strong year over year corporate developments that make our increased activity in the final quarter justified. We remained quiet in January and February as the value of our investments had a strong recovery, reversing most of the sell off from all-time highs. The markets are somewhat schizophrenic as sectors that have been ravaged over the past two years are still struggling to recover. I am encouraged by our out performance over this period and hope that it continues throughout 2019.

Looking back on the past six months, we saw excellent year-to-date performance weaken from September and year-end, only to strengthen again in the new year. It appears that more than ever, we are going to witness bouts of spontaneous volatility through the new reality of ETFs (Exchange Traded Funds) that have been dominating investor behavior for some time. These instruments mirror market components such as indices of the S&P 500 or the Russell 2000 as they buy and sell its components based on algorithms. This brings bouts of manic fluctuation that gets extreme at times and forces investors - perhaps more than ever - to know what and why they own any investment holding, so emotion doesn't get the better of them. This is one of the great secrets to successful investing... to differentiate between stock valuation and the underlying success of a business. I've yet to see the efficient market theory work except in the well followed business where most information isn't overlooked.

The Art of Looking Dumb

Our investment portfolios are run much differently than most of the financial services industry, which tend to farm out the actual investment management to third party managers. In my investment career, I have not seen this work over the long-term and continue to wonder why few look at their returns without greater scrutiny. As smug commercials about fees populate our TV screens, few notice that there isn't a solution backed by a track record showing in its place. What they also aren't telling you is what fee you might be paying - only insinuating that it is low. But you can bet that if they are outperforming, especially over a reasonable period, they are not doing it for next to nothing.

My basis of belief is to holistically hold a relatively small portfolio consisting of disparate businesses and be prepared to hold them until fruition or the thesis changes. While it often tests our resolve, the long-term track record suggests that the process works well. The main reason I believe we have achieved success is that we know each holding well, making us better equipped to take appropriate action when adverse conditions present themselves. Investing money is emotional and one can make poor decisions after reading a blog, watching a business program or even hearing someone else's opinion that sounds right in the moment. When we do not know why we are invested, it stands to reason that we are prone to the swing of emotion. That is why I can pretty much tell when clients trade my ideas elsewhere. They tend to show a lot more emotion...that is because they really don't understand why they hold a certain investment or the individual thesis. Those who have done the work and know how we allocate each holding in terms of managing a portfolio are far less prone to experience emotional knee-jerk reactions.

Despite our performance over the long term, there are times when peers, associates and clients question our methodology, intelligence and sanity. It is easy to look stupid in the investment world. That being said, I would argue that there is a distinct line between looking stupid and acting stupid, but they can look awfully similar at times. Most financial advisors and/or investment managers prefer not to look stupid in their own right. Given the choice, billions of dollars allowed to run right off a cliff without a whiff of remorse doesn't seem as bad as long as they go in a crowd. One year all the rage can be oil and gas, then its technology, followed by something else. Like a thundering herd of buffalo, investment money and its managers can rarely be blamed for moving in such an enormous mass. It is not that they are dumb; it's more likely that, whether or not they know it, they are invested in a trend while holding out hope that they can sell it all to a greater fool before a panic.

This herd mentality combined with the growth of index or passive investing through exchange-traded funds has led to an enormous amount of 'closet' indexing. This means an investment manager might have a portfolio with an almost 100% match to some index such as the S&P 500, Russell 2000 or TSX 300, pretty much guaranteeing that they will be within 2% - 5% of the index, yet charge 1.5% for the privilege of doing so. But like previous investment products - the fee seems to be pushed into the background, insinuated to be inexpensive and more importantly, so does the performance. Sounds like a bad deal. Ultimately, it is the performance that is going to rue the day.

Like the popularity of mutual funds before it, the structured product that is prevalent throughout the industry has a poor track record of adding much value to investors, which answers an important question about performance. If one is to look back over the past 5-years of performance and find that you are below what could have been achieved in a 5-year GIC, it's time to start asking some real tough questions. Where are the clients' yachts indeed?

Thanks for taking a look, and as always,

All Good Things,

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