PORTFOLIO NOTES	**January 2020**

To our Business Partners:

- ***VALUE – INVESTING VS. SPECULATING.*** Following are highlights from a recent article that caught our attention. Written by Michael Lebowitz, CFA and Jack Scott, CFA of RIA Advisors, it captures the essence of the "value investing" approach (full article available on request).

  - Value investing is an "active" strategy that considers company fundamentals (type of business, sales, earnings, financial condition, etc.) and the valuation of the company's stock to acquire it below estimated value; it's a time-proven style clearly defined by Benjamin Graham, who said, "An investment operation is one which, upon thorough analysis promises SAFETY OF PRINCIPAL and an ADEQUATE RETURN. Operations not meeting these requirements are SPECULATIVE."

  - Yet, present-day "investors" have shifted away from this successful proposition over the last several years in favor of what we think is speculation in "passive" approaches like buying pools of money tied to a stock index or sector, or so-called "growth" companies which promise exceptional future revenue and earnings growth; while the value approach wins decisively over the long haul, growth stocks have outperformed for the last few years.

  - Yes, passive investment strategies, due to rock-bottom fees and high weightings of growth companies, have outperformed active investors; one could argue, however, that pure passive investing is highly SPECULATIVE by Graham's definition; the undisciplined low-fee buyer of an index fund will pay any price because he likely has not performed THOROUGH ANALYSIS and thus has no clue what the investment is worth, so it might or might not yield an ADEQUATE RETURN, and is totally ignorant of SAFETY OF PRINCIPAL.

  - The value investor who evaluates individual companies does so from the standpoint of the business owner; he knows the company, its business prospects, its financial condition, and can make a reasonable evaluation of what the business is worth and, most important, whether he can buy the stock in the marketplace at a price considerably below its estimated worth; therefore, this approach has high odds of meeting all Graham's tests of a successful investment operation: thorough analysis of all the relevant fundamentals), safety of principal (due to the margin of safety between price and worth), and an adequate return (as the stock price rises toward the company's underlying value).

  - Value investing is a long-term wealth-building approach, vs. the buy-at-any-price mentality of the growth or passive investor; we have no doubt that the value style will return to prominence, and passive investing will decline in significance in due course; Messrs. Lebowitz and Scott leave the reader with an interesting question: *Why do you think Warren Buffett's Berkshire Hathaway is sitting on (a record) $128 BILLION in cash?* (Buffett is, of course, an extremely patient value investor.)

- ***VALUATION.*** With stocks generally up in the month of December, they haven't gotten any cheaper.

- ***RECENT RESULTS.*** Stocks again rose in December, with the all the indexes returning 2-3.5%. For the full year there was a wide range of returns. Large-cap indexes rose 30-35%, while the small- and mid-cap indexes had returns of 17-24%. The "average" stock of those traded on the New York Stock Exchange was up 21%, which is about what our group of portfolio stocks gained in 2019, which is quite satisfactory.

Steve Nichols, CFA *Bill Warnke, CFA*

****The group of "portfolio stocks" -- our Equity Composite for the purpose of evaluating investment performance -- consists of 17 stocks that are held in our clients' accounts. Portfolios might hold some or all of these stocks, depending on investment guidelines unique to each client, the timing of purchases and sales, and start dates of accounts. The performance of this group of stocks is a good proxy for our equity performance but might vary widely among accounts. Of course, past performance is not necessarily indicative of future results.***