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"In Part"

October 8th, 2018

To Focused Compounding members:

I recently read David Einhorn's 3rd quarter letter to clients. In it, he wrote: *"As we recount the (Apple) story and think back to the spring of 2013 as our largest position moved sharply against us, it basically feels the same today – but now the market appears to be rejecting our entire strategy of value investing..."*

This is a common feeling among value investors who are underperforming or who fear they soon will be underperforming. In 1967, Warren Buffet – then a hedge fund manager of sorts himself – wrote: *"Mushrooming interest in investment performance…has created a hyper-reactive pattern of market behavior against which my analytical techniques have limited value."*

I've only been running managed accounts for one quarter. But, performance in that quarter was bad. And that is, of course, in part because the performance of the S&P 500 was so good over these last 3 months. But, only ***in part***. The other part is my own fault. It is tempting to blame the underperformance of one's own portfolio on the irrational and incorrect perceptions of the crowd. After all, paper losses are the result of other investors setting the bid and ask prices of the stocks in your portfolio. Einhorn's positions in **General Motors (GM)** and **Brighthouse Financial (BHF)** are not marked to business results each quarter. They are marked to the perceptions of other investors. These perceptions are often wrong. And they often stay wrong for far longer than a quarter. But, your underperformance can also be caused ***in part*** by your own mistakes. The difficult thing in measuring portfolio results is that good and bad quarters in terms of price performance are not synchronized with good and bad quarters in terms of you own analytical performance. In investing: you do get helpful and ultimately objective feedback about whether you are right or wrong. It's just that – unlike when shooting a foul shot or telling a joke – the feedback is not immediate. It can take years to get a final verdict from your expert trainer ("the market"). Often, you will do the right thing and get punished for it today. The key is to neither: a) learn too much from your underperformance nor b) fail to admit your underperformance is ***in part*** due to your own decisions. So – if you have underperformed recently – take some time to dissect that underperformance and ask what part is due to the quarterly whims of the crowd and what part is due to your failure to be the best stock picker you can be.

To learn about our managed accounts, email Andrew at info@focusedcompounding.com or call or text him at 469-207-5844.

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