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"Question Number One"

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To Focused Compounding members:

Warren Buffett famously said: *"Rule number one in investing is: never lose money. Rule number two is: never forget rule number one."* A good rule, sure. But, *"never lose money"* is an outcome rule – not a process rule. To improve as investors, we need to focus first on process and outcomes will follow. So, what investing ***process*** rules can we think of? And which would be rule number one?

We publish a lot of stock idea write-ups on Focused Compounding. Some I like a lot. Some I like a lot less. And I was recently asked why that is. What separates a stock write-up I like from one I don't? That's easy. The amount of time, effort, analytical thinking, and just plain old investigative journalism expended on answering one simple question: *"Is this a business we want to be in?"* Most stock write-ups focus on things like a low stock price, an upcoming catalyst, and a variant view. Those are all wonderful things to have. But, they tend to be either: a) potentially short-lived and/or b) difficult to be sure of. Most low stock prices turn out not to be that low if you've badly misjudged the business's competitive position, the industry's microeconomic structure, or the inherent economics of whatever product or service they sell. A price-to-book ratio of one is super cheap for an auto insurer with a good competitive position and yet it's not cheap at all for a life insurer. When analyzing a life insurance stock, the question I want answered first is: *"Do we actually want to be in the life insurance business?"*

My write-up of **Keweenaw Land Association (KEWL)** – a stock Andrew and I hold in the managed accounts – focused on whether timberland as an asset class is or is not attractive in the long-run. At the time – there was an ongoing proxy battle (since won by the dissident), there were plans to convert the company to a REIT, there was a copper mine planned on land KEWL controls, and there had just been an upward re-estimate of the amount of actual timber on company lands. Yet, I chose to focus mainly on whether timberland is an asset investors should hold for the long haul. Why? The investment case for Keweenaw has always been the stock's price versus the most recent appraisal of the company's timberland. As I write this, the price of a single share of Google and a single troy ounce of gold are roughly the same (both about $1,200). If you were distributing either asset to me – and I planned to sell that asset in the open market right away – I'd be pretty indifferent to which asset I liked better and would simply take the market's current appraisal of each: about $1,200. However, if I was – as value investors often find themselves – going to be stuck holding one asset or the other for the long-term, I'd much rather be given $1,200 worth of Google than $1,200 worth of gold. Wouldn't you? The market's appraisal of each asset is the same. And yet the compounding power of an advertiser supported media company is so much greater than that of a precious metal. So, the first investment ***process*** question to ask is: *"Do I actually want to be in gold for the long haul?"* or *"Do I actually want to be in Google for the long haul?"* Only after you've answered what you want to own does it make sense to ask at what price you want to own it.

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