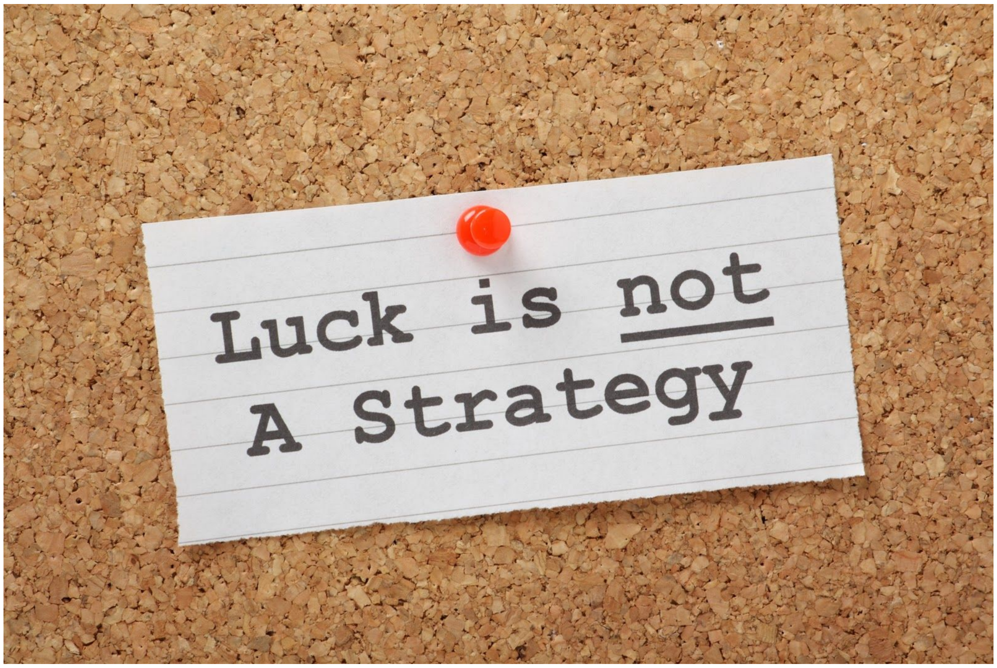
Investor Values

June 2018



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"*Purpose of the margin of safety is to render the forecast unnecessary.*" – Ben Graham

There was recently an op-ed in the Wall Street Journal written by Jamie Dimon and Warren Buffett that argued short-term earnings per share guidance was harmful[1]. They reasoned from their experience that quarterly guidance leads to an unhealthy focus on short-term profits at the expense of a long-term strategy. However, they did not disagree with the actual reporting of returns on prior quarters. They simply had issue with the predictive, future component.

This same methodology can be applied to your "personal company". Having prior portfolio performance data is important for investors. Individuals can use that information to measure progress against their goals. However, we believe trying to predict the next quarter based on the prior quarter is not at all helpful. Like companies, individuals can lose focus on the long-term when trying to predict the short-term.

Rather than focusing on short-term market movements, investors should be more concerned with revisiting their values and measuring progress toward their goals. To that end, here is some food for thought.

Value of Money:

We talk about the value of money everyday with clients. It means different things to different people.

- How hard is it to earn?
- How much can it buy?
- How free does it make you feel?

Learning what money means to you is a difficult but important first step in the wealth management process. The earning, spending, saving, and investing decisions should be directly correlated to the value individuals and families place on their money. To make things more difficult, these values might change with time so need to be consistently revisited.

Pathway to Goal Achievements:

Law of Averages:
Living in the Midwest is always a great reminder on the role of averages. Look at the weather forecasts for a spring day and you might see an expected 58° day. However, everyone in the Midwest knows that this is only the beginning when making preparations for the day. The morning activity (i.e. walk in the neighborhood, work in the yard, watch youth sports game) can start out much cooler than 58°. The middle of the day can bring something much warmer than 58°. For example, on April 30, the high in Milwaukee was 80°. The low was 37°. Just your average 58° sunny day!

This lesson in averages is helpful for investors when monitoring portfolio growth in relation to one's goals. Based on historical data and assumptions about economic activity, planning requires the use of long-term average returns. The actual yearly returns (like the weather) will look and feel much different along the way. Midwesterners that have the best outdoor experiences are the ones with the best expectations and preparation. They know there will be changes and they plan accordingly. They give themselves the best probable chance of reaching an outcome that achieves their goals (never being too hot or too cold). Just like investments, individuals have different preferences for temperature. The important part is planning ahead and knowing there will be variability around the average.

Value of Compounding:
We all know Warren Buffett, age 87, is incredibly wealthy. This can be attributed to many things. However, the argument can be made that the most important reason is time. Per published reports, over 99% of his current wealth was earned after his 50th birthday[2].

Pulling this apart even more, you could attribute his overall net worth to:

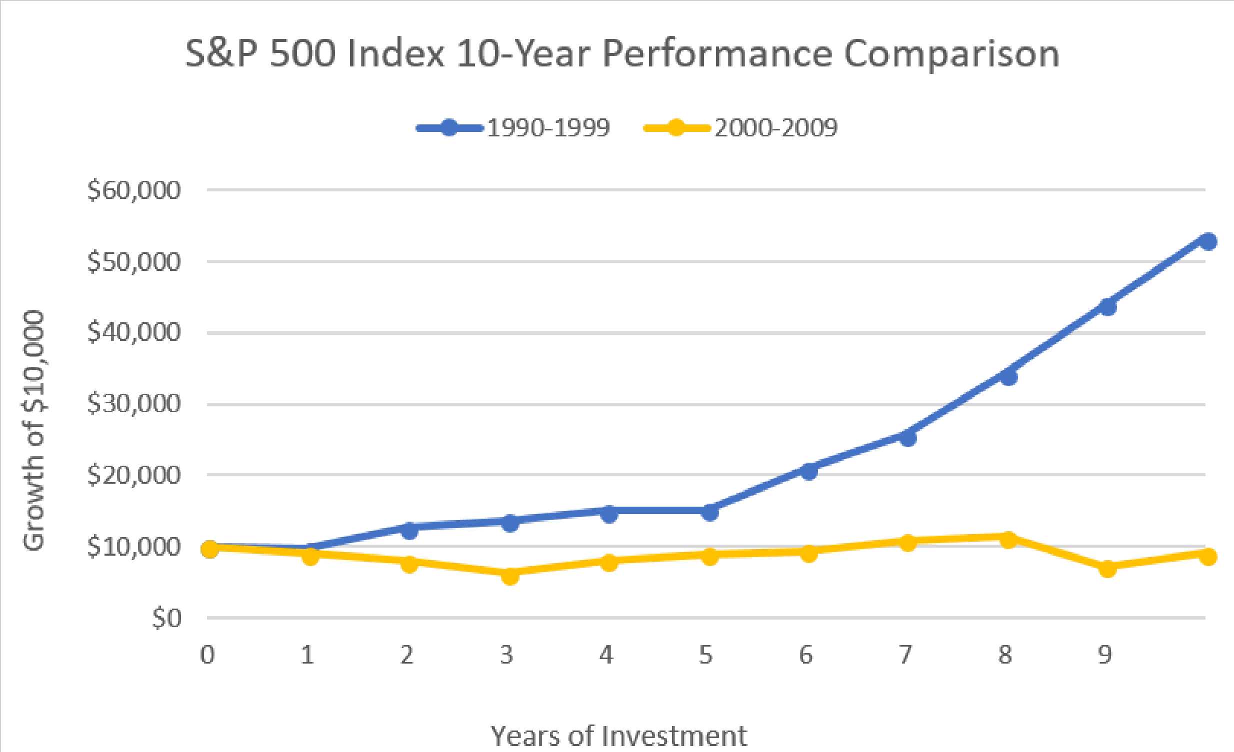
1. Investing early in his career
2. Good investment returns along the way
3. Long time period of compounding returns

By far, #3 is the biggest driver of his wealth. Per Bloomberg, his wealth in the last twelve months has increased $5 billion[3]. For perspective, that one-year increase is more than his total wealth was at age 60 when he was already one of the wealthiest people in the world.

The lesson here is not to be Warren Buffett, but extreme examples help to understand concepts. The takeaway is compound interest is powerful. The longer the time horizon, the more powerful it becomes. This should be kept in mind when individuals are thinking about spending, saving, and investing decisions.

Luck Versus Skill:
As investors, we often get caught up in the comparison game. We want to judge our investment portfolio against others in a quest for bragging rights over others. We worry about underperforming our neighbors, when the larger concern should be what the market is going to return.

Here is a simple example that some investors can relate to. Below is a chart showing the ten-year performance of the S&P 500 for two different time periods.



Source: Dimensional Fund Advisors
Past performance is not indicative of future results. This chart is provided for informational purposes only and should not be relied upon when making an investment decision. Indices are not available for direct investment. Index performance does not reflect the expenses associated with the management of an actual portfolio.

Someone starting out in 1990 had a drastically different investing experience than someone starting out in 2000. Unfortunately, people cannot choose what decade they decide to invest. The timing is driven by their stage in life and goals. When individuals can earn more than they spend, they decide to invest. It's usually nothing more complex than that.

Investors who underperformed the market by 2% from 1990-1999 were drastically better off than if they outperformed the market by that same 2% from 2000-2009. The timing of the investment matters, and before investors start to think that they can time the markets, they should think again. The investor graveyard is full of people who tried and failed that game. The lesson here is to understand the role of luck in your particular investment experience and worry less about the "skill" in trying to outperform the market.

Takeaway:

Values and goals are constantly changing as we move through life. In addition, progress to the attainment of those goals is moving too. Just as Jamie Dimon and Warren Buffett wrote, checking in on those goals is recommended and necessary. However, knowing what traps are hidden in that analysis is just as important. The path is never easy. Sometimes just recognizing that is the knowledge that many people miss.

If someone you care about would benefit from this newsletter, feel free to pass this along. Our goal is to work with a small group of families with whom we can have a big impact. Seeing clients make informed decisions about their wealth so they can achieve all that is important to them is something that gives our team great satisfaction.

From the entire McCarthy Grittinger Group team, have a great start to the summer!

[1] https://www.wsj.com/articles/short-termism-is-harming-the-economy-1528336801
[2] https://www.marketwatch.com/story/from-6000-to-67-billion-warren-buffetts-wealth-through-the-ages-2015-08-17
[3] https://www.bloomberg.com/billionaires/profiles/warren-e-