ALTIUS Financial
Empowered Future Report
Short term thoughts about long term matters

February 7th, 2014

Quote of the Day:
"The majority of men meet with failure because of their lack of persistence in creating new plans to take the place of those which fail."--Napoleon Hill

Defense Wins Championships?

I know many of us are just beginning to recover from this past weekend's debacle in New Jersey and I'm not trying to rub salt in the wound but I think it's worth pausing to extract a few lessons from the Broncos defeat in the Super Bowl. First, and it's been said often but it bears repeating: Peyton Manning truly demonstrates the virtues of persistence and professionalism. Thankfully, I'm not quite as emotionally invested in the team as I was back in the '90s before they won back to back championships and so when Manning was acquired I wasn't fully aware of how much he overcame just to play again, let alone at such a high level. But all the medical treatments and grueling physical therapy and emotional pain of leaving his team and home in Indianapolis did not deter him from his goals. I don't know if he'll take the Broncos back and win the big one next year but our culture is often bereft of character and leadership and so it's inspiring to have him try.

Those of us who follow professional team sports have heard it before "defense wins championships" and Seattle provides more evidence. We've seen it in other sports too – "Lord if we could only have that deep cadre of pitching, the Rockies would take us to the promised land…" Is the cliché actually true and more importantly, how does it relate to investing? While the sports pundits study and debate championship games, it seems the more thoughtful ones always come to the conclusion that while having a great defense is *necessary* for success, it isn't quite sufficient by itself. In other words, it takes being good on both sides of the ball. Having a balanced approach that recognizes the nature of the game and it's not different when we invest.

When Warren Buffet says that Rule #1 in investing is *don't lose money* and Rule #2 is, *don't forget Rule #1*, I think it's expressing the same thing. It's not that Buffet's always playing defense or never loses money but the more I study the great investors, the more consistent is their message: take care of the downside and the upside will take care of itself. It can be boring and frustrating to just focus on the fundamentals, whether it's blocking and tackling or actual and realistic earnings and consequent valuations. However, for those who approach their plan with level-headed and balanced attention to such fundamentals there can be great rewards.

Want to know more about the nuts and bolts of our approach to Value Investing? I'd highly encourage you to come to our next workshop (see below).

Calendar Planning

Here's what's coming up:

> **February 18th** **"Value Investing"** – Our analyst - Mike Rivers, CFA – will be making a presentation regarding our overall investment philosophy and taking questions from the audience.
>
> **May 13th** **Save the Date – we have something special planned for our next quarterly get together and will be announcing it soon.**

Add those dates to your calendar and think about who you'd like to bring and introduce us to. We always appreciate meeting new people and this is often a good format to have someone you know come see and hear us.—MM

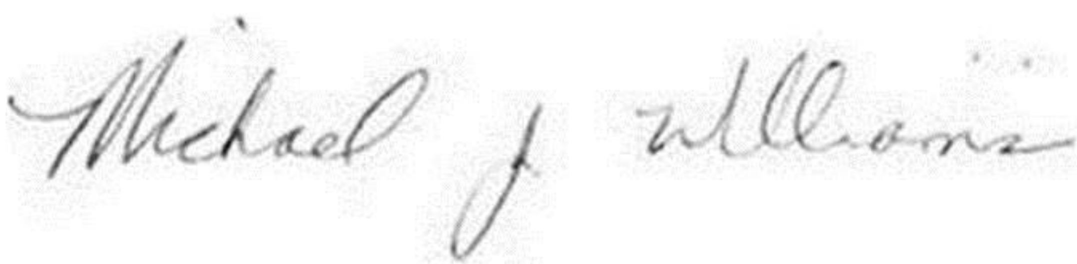
What's a Hedge Fund…and why you probably should avoid them…

I had a client ask me about "hedge funds" recently and whether she should be looking at them so I thought I'd explain a little bit. The term hedge fund is mainly a historical relic in the sense that the original investments called by this name were designed to hedge against downside risk. Today they are more likely an aggressively managed portfolio of investments that uses advanced investment strategies such as leveraged, long, short and derivative positions in both domestic and international markets with the goal of generating high returns (either in an absolute sense or over a specified market benchmark).

The fee structure for most hedge funds is heavily weighted toward the manager. This is presumably because they attract more talent (a dubious assumption when you look at the overall track record) - they often set up what's called a 2/20 agreement where the manager gets ongoing fees of 2% of the assets being managed PLUS 20% of all gains. Legally, hedge funds are most often set up as private investment partnerships that are open to a limited number of investors and require a very large initial minimum investment. Investments in hedge funds are illiquid as they often require investors keep their money in the fund for at least one year. Between 1998 and 2000, hedge fund fees totaled $440 billion versus $9 billion total profits for investors (Source - *The Hedge Fund Mirage – The Lesson of Big Money and Why It's Too Good To Be True). This result does not even take into account survivorship and reporting bias. Since hedge fund performance reporting is voluntary – they don't have the disclosure requirements of the rest of the industry - the data are bound to be missing hedge funds with bad returns and hedge funds going out of business. By the author's estimate, if these biases are accounted for, investors actually lost $308 billion in hedge funds, while the industry made $324 billion in fees.

Hedge funds and funds of funds, could make you very wealthy but they also can be a giant wealth transfer scheme from ordinary investors looking for the hot or special deal to hedge fund managers who market to this desire. This is not to say that "hedging" is a bad idea and we strive to incorporate such risk management ideas into our portfolios.

Stay Warm!



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