

Investing for the Long Run

The fresh air, green trees and singing birds can all be savoured just a few strides from our office (well, in the summer that is). The rhythmic motion of ten thousand steps erases the cares of just an hour ago. I took up running in my early thirties to address the excesses of my youth. An investment in my future, of sorts. What started as a labour of necessity quickly became a passion; or more accurately, an obsession. My peace on a recent lunch run was interrupted as I contemplated the absurdity of running the California International Marathon, a 42.2 km race from Folsom Prison to California's State Capitol, one week from Sunday. A dozen or so serious contenders will compete for a payday. The rest of us will be there to experience some twisted combination of joy and torture. Is there a Black Friday discount for the suffering ahead? Running and investment careers are both measured over a lifetime, punctuated by moments of elation as well as defeat. There are a remarkable number of parallels between the two. Here are a few that we keep in mind for ourselves.

Staying healthy

Great results in running are achieved through continuity of practice and building on experience. Therefore, the most important thing in running is avoiding injury. Similarly, the most important thing in investing is avoiding capital impairment. Overpaying for an investment or purchasing a low quality business that fails to grow book value at a reasonable pace are injurious and therefore hindrances to achieving one's long-term investment objectives.

Patience is a virtue

We need to collect the facts in order to monitor our progress. Quarterly results and 5 km split times contain valuable information, but they should be given only the weight they deserve. We need to stick with our plan and not overreact to short-term distractions around us. Data from the NYSE reveals that average holding periods have declined from 8 years in 1960 to 8 months in 2015. Investors make a lot of decisions these days, and we postulate that there is an inverse relationship between trading frequency and decision-making quality. Computers and algorithmic trading account for some of

the decline in holding periods, but generally speaking patience is eroding in our modern culture. The overreaction to short-term results by other participants is therefore a tailwind for the steadfast.

Speed check

Running at the right pace is analogous to giving a business an appropriate weight in the portfolio. It's deflating to grind to a halt late in the race due to a poor decision made on the starting line. Being overly aggressive can potentially have huge payoffs, but the downside when an aggressive move fails is difficult to recover from. We are not infallible, so we've installed speed bumps into our risk management framework to curtail the effects of excessive optimism. A 6% maximum weight in our best ideas allows our clients to benefit from the conviction of our research, while limiting the consequences of a mistake or just plain bad luck.

Dealing with adversity

If a pain arises during a marathon it isn't always obvious whether the right course of action is to maintain pace or slow down. Is this just the normal discomfort of racing or am I injured? Sometimes the right answer is to speed up! Similarly, it's rare that every investment works out perfectly in accordance with our thesis. An investment starts to hurt when bad news is combined with selling pressure. Sometimes we have to reduce the weight in a business because it's looking an awful lot like an injury. It could be that a management team underestimated the challenges of integrating a new technology or a recent acquisition. In these cases we consider trimming our position or exiting altogether. On the other hand, adversity can also be an opportunity. We believe this was the case with Canadian Western Bank (CWB), a holding in the QV Canadian Small Cap Fund, whose shares sold-off with negative sentiment towards both the banking sector and Western Canada. We picked up the pace by adding to our investment in CWB at attractive prices.

Performance measurement and review

With every race and investment comes an opportunity to measure performance, uncover key lessons, or reinforce good practice. The big advantage that running has over investing, however, is that the post-race analysis involves burgers, fries, cake and ice cream.