

# Recent Comments from Our Sub-Advisors

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Madison

WEALTH MANAGEMENT

## Chris Davis – Portfolio Manager, Davis Advisors

- ~ “While hundreds, if not thousands, of people make a living as market and economic forecasters, there is overwhelming evidence that such short-term forecasting is impossible. As John Kenneth Galbraith observed, “The function of economic forecasting is to make astrology look respectable.” Although the media is now filled with fawning interviews with those strategists who correctly predicted the bear market, these are not the same strategists who were lionized for predicting the bull market. Reputations for astute forecasting tend to be short-lived. A dramatic example of the ephemeral nature of such reputations came in Alan Greenspan’s admission that “I’ve been in the forecasting business for 50 years, and I’m no better than I ever was, and nobody else is either.” (Now he tells us!).”
- ~ “Unfortunately, it remains true that people are pessimistic when prices are low and optimistic when prices are high. The result of having sentiment correlated with prices is that investors (aided by stock market promoters and certain financial media commentators) have incurred a significant self-inflicted penalty by getting in *after* prices are up and getting out *after* prices are down. The cost of this penalty over the last 20 years is estimated to be about 6.5% per year, a staggering figure that dwarfs any other investment expenses.”
- ~ “Although the turmoil of the last year was dramatic the fact that this year marks the 40<sup>th</sup> anniversary of the founding of our firm serves as a useful reminder that tumultuous periods in the market and economy have happened before and will happen again. We have always managed our firm, like our funds, to get through such difficult periods. We are private, employee-owned, frugal, and well capitalized. We are also among the largest shareholders in the funds that we manage and have not sold a share throughout this downturn.”

## Managers of Brandes Investment Partners

- ~ “Over the last 20 months or so, short-term stock market volatility has made it difficult for many investors to remain focused on the long term. In addition, the tendency we have as human beings to take action may be exacerbating market swings. Many market participants do not simply want to “buy and hold” They want to do *something* to feel they have control over the situation. We share a reminder that sometimes the best action to take may be no action.”
- ~ “Recently, we read a research report about soccer goalies facing penalty kicks that, we believe, has applications for investors. In a penalty kick situation, it’s just the striker and the goalie. The ball is placed 11 meters from the goal – so the goalies really don’t have time to *react* to the shot. They try to anticipate where the striker will kick the ball and often dive to that spot to try to make the save. In a study, researchers found that goalies dove either left or right 80% of the time – yet their save percentage was only 15%. The strikers kicked the ball to the left 1/3 of the time; to the right 1/3 of the time and - knowing that goalies tended to dive right or left – right down the middle the other 1/3 of the time. The researchers shared their findings with the goalies and suggested they could improve their save percentage if they simply stood in the middle of the goal rather than diving left or right. Each of the goalies listened to the evidence and the recommendation and said they wouldn’t do it. In essence the goalies said “You don’t understand. I play in a stadium in front of thousands of people. I can’t just stand there and do nothing.” Just like soccer goalies, investors have a strong desire to take action. Often it doesn’t feel comfortable when we see stock prices soaring or falling and we do nothing. Yet, sometimes doing nothing may be the best thing to do.”

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## **John Gunn – Chairman, Dodge & Cox**

- ~ “The developing world is likely to lead global growth. The powerful tools of increased computing power, the internet, and wireless communication enable the citizens in the developing world to plug into the global economy. Multinational companies in the U.S. will benefit from opportunities by increased demand from the developing world. The U.S. economy is resilient and has recovered from many past challenges. In the first 50 years of the S&P 500 from 1956 to 2006, corporate profits increased 25-fold. Behind that performance were companies innovating and achieving productivity gains. The pace of technological innovation remains rapid. Companies have the opportunity not only to create new products and services, but also to improve the old ones and cut costs through increasing productivity.”

## **Jody Johnson – London based Portfolio Counselor, American Funds**

- ~ “Investing in a company that’s outside the U.S. isn’t necessarily more risky, particularly as the world goes more global. All of the large companies we look at are operating globally anyway. They’re all doing business in the same end markets around the world, they’re all relying on similar customers, and so it’s not that relevant to just differentiate between companies based on where they’re headquartered.”
- ~ “In fact, we find that, for example, if you wanted to invest in the recovery of the U.S. auto industry, the best way to do it would be to buy Toyota or Honda, because the U.S. is a very significant market for them. All of the incentives to get rid of clunkers and buy new cars are being directed toward smaller cars, which they specialize in, and you really can’t invest directly in GM or Chrysler today. You can invest in Ford. So, often participating in recovery in one country isn’t best done by buying the stocks in that country. They’re best done by buying something somewhere else which has a large market share there.”

## **Cliff Greenberg – Portfolio Manager, Baron Small Cap Fund**

- ~ “Our stocks have participated nicely in the rally and for the most part performed very well. Our best performers were our companies whose earnings were down the most or had the most leverage – our most volatile holdings. This makes sense as one would expect that improving business conditions and financial markets would most benefit such companies.”
- ~ Generally, our holdings reported earnings results which were better than dire projections and forecasts of future earnings that were better than expectations. The improvements are primarily driven by cost cuts that have outpaced revenue declines. Many of our holdings were able to raise new equity during the quarter and refinance debt at ever more attractive rates, both important, positive continuing trends.”

## **Charles Royce – President and Founder, The Royce Funds**

- ~ “In the triage that happened in March, we were separating stocks that we thought could go up three times from the stocks that might only go up two times and ones that might only go up 50%. It was an odd moment of separating some extraordinary possibilities from just great possibilities. Going forward, what expectations should small-cap investors have? The big question is will equities ever give you the kinds of returns that historically were present to preserve wealth or increase wealth? Or has the world changed so dramatically because of last year? I come out on the former – that time was just a big bump in a long road. It did not change the dynamic that a well-managed corporation can compound wealth better than a fixed-income instrument.”

## **Bruce Berkowitz – Portfolio Manager and Founder, Fairholme Fund**

- ~ “Successful investing is about getting much more cash over time than you give. Buying cheap relative to expected cash flows is half the battle. Today, even though the market is up significantly from the March lows, the investments we own appear undervalued reflecting the market’s hangover from years of irrational exuberance.”