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A Case Study on Sticking With Our Strategy

> "Be like water making its way through cracks. Do not be assertive, but adjust to the object, and you shall find a way around or through it. If nothing within you stays rigid, outside things will disclose themselves"
>
> Bruce Lee, *Martial Artist*

This is absolutely the last Bruce Lee quote we will use but we found it while looking up the one used in our Q1 letter about keeping an open mind. This month's topic, in light of a market sell-off, is about sticking to our strategy when faced with adversity. Again we feel Mr. Bruce Lee is spot on in his Zen approach to conflict, which can also be applied to the mental challenge of stock market investing.

What we know about the stock market is confirmed by the Dalbar market research group in their report titled *Qualitative Analysis of Investor Behaviour 2015*. In summary, over the last 30 years the S&P 500 had compounded annually by 11.1%. But the average investor has only compounded at 3.8%. Through this period inflation was 2.7% so the average investor's real return was only 1.1%. The conclusion of the research is "**The overwhelming driver *of this poor performance* is bad timing by investors. This is worst during extreme events"***

The usual approach to short term stock market investing is to guess whether the security is going to go up or down. Given all the factors involved, predicting is almost impossible to do successfully over time. Many people can get it right for a while but then fail to notice a major change in the market direction. By the time one can acknowledge that the direction has, for arguments sake, turned down and that a decline in earnings is obvious, the opportunity to sell is lost and that is often the time when you should be thinking about buying.

Instead, at Avenue we ask two simple questions: is this a good consistent business and are the shares trading at a reasonable price? For us, a reasonable price gives us a fair chance of compounding at 8 to 10% over the next ten years. If markets run up, we can sell a bit and if they come off we can add. The key idea behind getting a consistent return is to own consistent businesses throughout the up and down cycles. You cannot capture the 8% compounding if you do not own the stock for the long term.

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*John Authers, Emotions get in the way, Financial Times, 23 April 2015
Dalbar, Qualitative Analysis of Investor Behaviour 2015
https://www.bellmontsecurities.com.au/wp-content/uploads/2015/04/2015-DALBAR-QAIB-study.pdf

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Getting there together