Taking Stock with SAM: A Market Discussion - March 2022

This webinar will touch on:

- The current state of the economy and markets
- Geopolitical events, including Russia's invasion of Ukraine
- Inflation and interest rates

Jonathan Satovsky:

I have a fire in the background because my intention was to actually do a fireside chat, but clearly, this is... If I start burning the house down someone please, put in a chat box that I've gone overboard. We're here on March 14th, 2022. And we wanted to take stock at SAM and give a little update on our perspective and lens on the state of the world. March 2022, it's interesting, just a quick reflection—it happens to be March and the last 25 years have been very pivotal points in history for some reason. March of 2000 was a moment in time when the clock changes of Y2K, they were worried about the leap year, the time change, and it sort of was the beginning of the decline in the Nasdaq.

And then, of course, March of 2009, was the turnaround in the financial markets. In March of 2003, we had an invasion, a war that started 19 years ago. And now March of 2020, we had, of course, COVID. Now, we're in March of 2022. So we wanted to take a little stock and have a little discussion with Avi, our new chief investment officer in the past year, to let the SAM community get to know Avi a bit, and hear our perspectives on some of the issues that are top of mind to people. So we'll just jump right in.

I suppose I should give homage and respect to the situation at hand. There's clearly a tremendous amount of pain in humanity and in culture and society with Russia invading Ukraine and two million refugees plus being displaced from their homes and traveling into Europe. And even for our clients and our clients' parents and family, this brings back a tremendous amount of trauma and experience from World War II. And 70 years ago, some similar experiences that many people have many stories to share, so it's painful on many levels.

And similar to Viktor Frankl, I would pay homage to Thich Nhat Hanh who had passed away this year, who was a tremendous peace activist over the last 90 years of his life. And similar to Viktor Frankl, who wrote, "Man's Search For Meaning," I thought this quote was apropos for the moment, "Hope is important because it can make the present moment less difficult to bear. If we believe that tomorrow will be better, we can bear a hardship today." So pause for a minute and just have the moment of silence to have a deep reflection for the people that are suffering and send a little bit of hope and positive energy for healing in the world for the moment.

Today, in recognizing the moment of what's happening in the world, SAM has made a contribution to support some of the relief efforts in Ukraine, and we try to make a contribution represented of a day of revenue for just paying homage to the situation and trying to be supportive in whatever way that we can. So now, obviously, it's a little less... Sorry about the smack. Sorry about the crackling fire. My bad, fireside chat isn't so good if the fire is crackling louder than my voice. I know that there are a lot of financial matters that are top of mind for people, geopolitical, interest rates, the Federal Reserve is meeting on Tuesday and Wednesday, inflation, there's just... I feel a tremendous amount of angst that a lot of people have coming out of COVID. And finally, people are excited to get some relief and get out and start socializing out of isolation in the world, and now, we're going through something different. So we'll try to dig into give you some statistics and information and ground in some evidence to give some perspectives that may help ease a little bit of weight and a little bit of attention, give some perspective of our views looking forward.

So I'll pass it over to Avi Berg. For those of you who don't know, Avi joined us. They say you're supposed to hire people smarter than you, so we've been blessed to have Avi join us in the last year.

Avi went to the Michigan of the East, which is Crimson (Harvard) in the Northeast quadrant of the United States, as an undergraduate, went to graduate school at Columbia Business School, and taught value investing at Columbia Business School and has a tremendous pedigree in the financial field, worked at Goldman Sachs, Fir Tree, Jennison, some hedge funds, and had a lot of experience in financial markets the last 25 years. But more importantly, more important than his intelligence and his knowledge of markets, his emotional intelligence, as you'll see in a short half hour, is maturing me quite a bit. So thank you, Avi, and I'll pass the baton.

Avi Berg:

Thanks, Jon. Look, we know these are the big three things that are on people's minds. And look, it's very hard to talk about some of these things when there's other stuff that Jon was speaking about going on in the world, but I know this also creates anxiety, so we thought it'd be helpful just to kind of give our view of how this might impact people's portfolios, et cetera. So let's start with the beginning with geopolitical events. So this is a kind of a laundry list of various kinds of geopolitical events that have occurred over the last 50, 70 years actually, going the whole way back to Pearl Harbor. And I think there are a couple of things that I want you to get out of this slide, okay?

The first one is that the knee-jerk reaction is always down, which makes sense. And then it kind of continues to go down for a little while longer, but it usually doesn't take long for the markets to bottom and then for recovery to happen, so you can see the average number of days before the market bottoms is 22, so that's only three... well, it's four weeks of trading days and 47 days to recover. Now, clearly, there's a wide range of outcomes here, so there are no promises on any particular one event, but I'd like to just point out that, in the past, things have actually recovered reasonably quickly from these kinds of events.

So let's talk a little bit about inflation because that's the second thing that people are concerned about. Now, look, inflation is bad for the markets. That is true. As you can see from the slide, the markets have done better when inflation is falling and when inflation is low. On the other hand, what I want you to get out of this slide is that markets are still good when inflation is high and when inflation's going up. And so, if there is one message that I'm going to leave you with, it is that I'd rather have low inflation and falling inflation, but markets tend to perform okay when inflation is higher, when it's going up, and there's a reason for that. And that is that companies are able to price for inflation, usually with a lag, to recover their cost inflation. And so therefore, profits tend to recover over time and that's why it works.

So let's talk about the third one and that is interest rates. Now, this is a very busy slide. So I just want to kind of walk you through what this says. These are all the instances since 1950, where the 10-year Treasury has gone up 1% or more. And you can see from the very right column, which is the S&P 500, is that in almost all of those cases, the markets were actually up. There were two instances where they were down, basically marginally, almost flat. So why is that? So the reason is because interest rates go up when the economy is good, that's why interest rates are going up. And so yes, over time, eventually cycles do occur. Interest rates go too high. The economy slows down and the market rolls over, okay?

We haven't gotten rid of economic cycles, but what we want to say here is that we haven't even started raising rates, and people are already nervous. And you can see from the starting yield column and the ending yield column is that interest rates have gone up often two, three, sometimes as much as five or 6% before the market rolls over. And that's because, again, the economy's strong, and until the economy kind of rolls over, it looks like the economy's rolling over, the stock market does okay. So I think the idea is not that interest rates aren't something to be concerned about. It's just a little too soon to worry about it.

And the last thing I want to say is, and this will be on the next slide, which I'll just forward right now, is look at the starting point from where we're starting from. We're starting from historically low levels of interest rates. And so I guess my thought here is that it's likely that it'll take even more interest rate rises, not less to cause the economy to kind of roll over, that's a conjecture on my part. We don't really know. We've never been here before, but at the very least, it seems logical that it wouldn't be fewer.

Okay, so let's move on to a little discussion about fear and volatility. And I know Jon has talked to many people about this. The VIX is a measure of market volatility, determined by bid-ask spreads on options, okay? And so the higher the implied volatility in the options, the higher the VIX. Now, historically, when the VIX goes north of 30, you'll see here, which doesn't happen very often on balance in all observations, right? The VIX is over 30, about 8% of the time. And what we see here is that when the VIX is over 30, a lot of people are nervous if you just hold your nose, and look at the market six months later, and 12 months later, you'll see that the returns are way better when the VIX is over 30 than during all the observations when the VIX is under 30.

And I think even more important than that is the hit rate. So when I say the hit rate, what I mean is that the percentage of times where in six months, it's up. Or in 12 months, it's up. And you see that the hit rate is over 80%. So 80% of the time, historically, if you just held your nose, when the VIX is over 30, you'd be up in six months. And 87% of the time, you'd be up in 12 months. And right now, actually, as of last week was at 31.27, we're now at 31.77 as of the close today. So the upshot is that, look, it's not a guarantee, but what we're trying to do when we invest is make the probabilities in our favor. And there's very little that has this kind of probability in investing in my experience, and I've been in the markets for 25 years.

Jonathan Satovsky:

I'll just throw in... This is, often, a question of... A lot of people ask, "Are you not paying attention? The markets are falling. It's a terrible time." Half-jokingly, for the last 25 years, if there was one statistic that really was salient as Avi pointed out, you can really throw a dart at the wall and you'd make money, but I don't want to tell people to throw caution to the wind that everything's fine as just like the data about the war, just like the data about interest rates, just like this data. It's not 100% certain, and we don't know how long and how prolonged the current interest rate and Fed tightening cycle could be, or the invasion in Ukraine could be, and how far and wide this spreads and how it plays out, but we show this to give you hope, to give you hope and optimism to realize that when everyone is fearful, it's good to be greedy. And we're going to highlight some slides about Berkshire Hathaway to use it as a proxy to remind people about an ideology and a methodology and philosophy about investing to be calm when others are greedy and be greedy when others are fearful.

Avi Berg:

That's a good segue. Perfect. So let's talk a little bit about Berkshire. And I think Jon gave a perfect segue into Berkshire. We own it for some clients and it really tries to remind us that investing is a process for a lifetime. So if you look at this slide, you'll see... And I'll just highlight a few of the data points on the top, the bar charts on the top. In 2015, Berkshire actually underperformed... It went down actually and underperformed the market. And then 2019 and '20, underperformed pretty dramatically in the S&P 500.

And so, but if you had sold in 2020, you would've missed out on the fact that if you look at this year, in 2022, it's massively outperforming the market by about 20 percentage points. And so look, from a financial planning perspective, what we can learn from that is that there's no path that's right all the time. And if you, philosophically, agree with the path that you're on and you like the assets that you're in, eventually, if you stay the course and resist the temptation to succumb to, "Oh, my God, I'm underperforming. I'm going to dump it when it's low," you'll be better off.

Jonathan Satovsky:

The other thing to highlight is there are two big financial planning things to highlight here. One is around cash, which Avi will talk about in a second. Holding cash and not being fully invested at all times is not because we're not trying to make the most money for people, it's to calibrate to someone's risk tolerance so that they can sleep at night. They aren't ever a for seller of assets, and the principles of Buffett and Berkshire and Charlie Munger have really helped reinforce that lesson. And also, the ideas that we're going to talk about in some of the subsequent slides about value investing, investing in profitable businesses, ignoring the crowd, not coveting the high flyers and the lottery tickets, trying to get rich quick, and throwing Hail Marys as Tom Brady's coming back out of retirement. I guess he must have seen his portfolio the last month, he decided to come back to work next year. He's had great execution on surveying the field and finding pockets of openings. So I'll digress, but we'll get into more of that. But the principles and philosophies of investing with a margin of safety toward cheap, small, and profitable businesses are something that Buffett is the godfather of, so to speak.

Avi Berg:

Yeah. I mean, and that really sums it up. And I just wanted to kind of highlight a couple of things on the bottom charts here, which a lot of... Jon mentioned the fact that you want to own enough stable assets to be able to weather any storm. I mean, that's what Buffett says all the time. And a lot is made the fact that he has now about 144 billion of cash on the balance sheet, that's his sort of level at the moment. But if you look at Berkshire's cash as a percentage of total assets, you'll see that it's been pretty consistent over time. So while he says that he would like to invest more, and I'm sure at times, he will be below that level, his actions have really been...over the last decade, you can see his actions have really been keeping cash at, basically, a flat level to his total assets, which basically is the same lesson that Jon was mentioning before, which is we should have enough stable assets to be able to weather any storm, and I think that's really the other lesson that we take away from this.

Jonathan Satovsky:

What's fascinating is he talks about the ideas. Ideally, he'd like to have 100% in equities, but he's really had about 85% of his portfolio invested at all times if you look, by and large, just visually the average sort of turns out to be about 15% of his portfolios held in cash, just interesting.

Avi Berg:

Yeah. So I thought I would just take a step back here and talk a little bit about what we do research-wise and kind of how we're evolving. Since I joined Jonathan as CIO, I've worked with the team to try to really discern whether there are ways to improve the portfolios, both on a risk and excuse me, on a return perspective. And I think look, philosophically, Jon and I are very much in alignment on how we view investing. And so you shouldn't expect wholesale changes in the portfolio, really, this is working around the edges, trying to figure out whether we can take advantage of things to improve slightly people's performance, and so based on kind of what we see but also on clients' risk parameters.

So look, some of the things that we've done that I'd like to highlight over the last few months since we've been here, we did rebalance certain portfolios, and we do that consistently when we get out of line. We had a very strong equity market last year, so we took a little bit of that to add equities and reallocated to fixed income. That's actually helped us a little bit this year as the market goes down. And if the market continues to go down, we'll be doing it in the other direction. We'll be rebalancing into equities because we want to match people's risk tolerance, but also take advantage of market movements. The second thing we've done is for many portfolios, portfolios that have fixed income exposure, we swap a broad bond market exposure to buying some short-term TIPS. So TIPS is an acronym for treasury inflation-protected securities. And what's unique about them is that if inflation goes up, the interest rate that it pays goes up. So it's basically pegged on inflation.

And so our view there was two-fold. Really, the first was that if there was persistent inflation, which it does seem like there is actually happening, that we would actually get high-interest payments from the TIPS. And the second thing was that we shortened the duration. So they're short-term TIPS because we were concerned about interest rate rises, and so we wanted to shorten the duration of the portfolio, and this was a way to do that. And so far that's been actually a pretty good trade, it's outperformed the rest of the bond market by significant margins, since we made the trade. And the last thing that we've done is we have... For new money only, we've replaced one of the ETFs that we were historically buying, which was pegged on the S&P 500 to the overall stock market. And that not only broadened exposure, but it also gave us a little bit more exposure to small caps, which directionally, we kind of like, and I'm going to talk a little bit about that in more detail. So those are some of the things that we've been doing. We continue to try to think diligently and thoughtfully about how to just tweak clients' portfolios to improve the probability of success.

So Jon had mentioned this earlier, and I just wanted to kind of reiterate it with a slide that certain factors have historically proven to do better than the average of market over long periods of time. Now, you'll see from future slides that it will show you that doesn't happen all the time, but those factors are, as Jon said, smaller size. Smaller companies tend to outperform larger companies, and this happens across the world. All the factors work all around the world. Cheaper stocks tend to outperform more expensive stocks and higher profitability companies or companies that have higher profitability outperform stocks with lower profitability. Now, we've been very focused on the profitability one, in part, because of the persistency, and I'll show you that in a minute, of the factor. It's done extremely well, and it's been more consistent than the other ones, but we also think there's an opportunity in small cap, and we'll talk about that a little bit in a minute.

Jonathan Satovsky:

The other thing to point out is that profitable companies, if you own a profitable company and interest rates rise, you're less dependent on the capital markets to finance your operation. So it gives you a little bit more of a margin of safety, a little bit more cushion, and you're self-sustaining, regardless of interest rate changes or capital market changes, by and large.

Avi Berg:

Yeah, excellent. So what this chart shows you is the 10-year rolling average returns of the most profitable companies in the world, in the US markets, I should say, less the least profitable, okay? So you can see that over a 10-year period, almost in every 10-year period, except for a few in the early 1980s, higher profitable companies have outperformed low profitable companies, so that makes sense, right? They should over long periods of time. And so we have a very high... We have some exposure to this factor in many different portfolios. This is the same chart, rolling 10-year premiums for small cap minus large cap. Now, you can see that over long periods of time, small-cap, most of the time, outperforms large cap, and often by very large margin. You could see in the early 1980s on an average 10-year period, it outperformed by almost 15 percentage points, which is incredible.

Jonathan Satovsky:

I want to just opine, not that this is a perfect correlation, but in the '70s was the last period where we had of geopolitical tension, high oil prices, and inflation pressure and rising rates at the same time. And you can see sort of visually that this is a period where small companies outperformed by a material margin. Obviously, we're not expecting past performance is not a guarantee of the future, but there's a good indication that leaning in this direction could be valuable.

Avi Berg:

Yeah. And so what we've seen and one of the things that I just wanted to reiterate, and I think... Thanks, Jon, for mentioning that. But one of the things I wanted to reiterate is you can see from the very end of the chart, and if the chart was extended to 2021, it would also be as bad, is that we're basically at almost a historic low for how badly small caps have done relative to large caps. So it's a very unusual period where large caps have really outperformed. And so therein lies the opportunity, and that's why we're going to lean in that direction. Now, an interesting question someone can ask is, what happens to small caps during wartime? And one of the things that we sort of looked at is, in fact, during wars on average with a lot of variability, but on average, small caps have actually done better than large-cap stocks. Now, that's true overall throughout the whole period, but even better during wartime. So I'm not sure what that means for today, but it's surely not a red flag for us if we're going to do it today.

Jonathan Satovsky:

I was just going to chime in and say that the thing that really stuck out to me here is that during all periods, historically, from 1926 to now, the stock market in the US averaged 10%, and the small-cap markets averaged 11.6. But in all war times, on average, the markets actually perform better, which is kind of fascinating. Just a minor thing to point out, which we'll talk about later, but it's not lost is the idea that the point here about the increased return also comes with increased volatility. And people think volatility is risk. It's only risk, obviously, when someone sees something volatile down, but the volatility can happen up as well. So the range of outcomes day to day, week to week, month to month will widen when you have more small companies. So people have a tendency during times of war to gravitate toward the familiar names. So the risk spread or the volatility spread also widens. So you get paid more for owning small companies, but it comes with a little bit more heart palpitations along the way.

Avi Berg:

Yeah. And just to kind of reinforce that, I mean, that's one of the reasons why we would never move the whole portfolio in small caps, right? I mean, it's really something on the margin that we'd like to do to enhance performance, but without creating an enormous change in the risk profile of portfolios. And one of the things that I thought was interesting in doing some research on this was even within small-cap, we think there's an opportunity for value. So if you look on the right two-bar charts, you'll see that on average, the 2000 value, which is the commonly used small-cap value index has outperformed the Russell 2000 growth by a significant margin over 300 basis points a year since 1978. But in the last five years, and that includes, by the way, your last year, where the Russell 2000 value outperformed by a significant point, has underperformed by about 500 basis points a year, which their end, I think, lies an opportunity for us in the market. And so even within small caps, we're kind of looking for opportunities where there may be some mispricing.

And I think one of the last things about small-cap, which I wanted to highlight is that small caps have been one of the few asset classes that have outpaced inflation in every decade. That's not in every year, but in every decade. And so even in the '70s, you can see, when inflation on average was over 8% that small caps were up. The inflation was up almost 15%. And so as an inflation hedge also stocks in general are good inflation hedges, but small caps are also good inflation hedges. So this is the same chart that we saw before on small-cap and high profitability, but this is value minus growth. And you can see, we're actually at a historic low of value, underperforming growth over a rolling 10-year period.

Now, we have been tilting in that direction, even our high profitability, quite frankly, tilts a little bit value, but we've been tilting value to lean into this. And I think as we look at small-cap, we're also going to be leaning into this. So I think these are the kinds of the things that we're going to lean a little bit more into. But again, we want to create enormous amounts of tracking errors so that people react to underperforming. So we're trying to do this in a thoughtful way to balance the kind of opportunity with the potential for higher returns.

And I think just the last thing I just wanted to kind of point out is... And look, I don't want to make any... I would hate to be quoted at any time, trying to make a little too much of two and a half months' worth of performance, okay? So with that as the caveat, I just wanted to point out that if you look at what's happened in the market today, it does look like the value indices are starting to outperform growth. We've seen it in the Russell 2000 value, which we already said, and that's the small-cap, but also in large-cap, where the growth indices have underperformed. And look, there's lots of speculative assets that are doing way worse than what we're seeing on this screen, right?

I mean, we approximately half of the Nasdaq companies are down 50% from peak. And we are just reading actually an article that NFTs are now down 70% from where they were, we're not playing in those areas. We're not trying to speculate with your or our money, quite frankly. We invest the same way you guys do. We are really trying to be deliberate and thoughtful and improve the probability that we're going to have success over long period to time and not kind of chase kind of performance or Feds or what have you, and that's kind of how we think about the portfolios. And look, we're constantly trying to find areas where we can improve. We've got a lot of research projects that are going on now, so who knows? Stay tuned, there may be some more, but that's kind of what we're thinking at the moment.

Jonathan Satovsky:

The other thing to point out is we answer some of the questions that have come in, and certainly, if you have additional questions, you can throw them in the chat. And to the extent, time permitting, we'll jump into it. We only allotted us... We want to make this sort of a short update. We didn't want to take up too much people's time, but thank you, Avi, for sharing a lot of the background and perspectives. One of the key points that is often lost on people is the idea of execution risk. And what I mean by that is it's not just being right, it's being right persistently.

So a lot of the data that Avi shared with you is based on research around cheap, small, and profitable companies that can be executed on in a robust, persistent, and sustainable manner. And that's important because if we are turning things over to fervently, there's also a tax implication. Most of our clients are taxable investors and we're balancing qualified and non-qualified assets. So we have to be sensitive to the fact that there are tax consequences if you're turning a portfolio over too frequently. So in trying to control the controllables, we want to make sure that we're sensitive to that factor as well.

So jumping into a couple of questions, I think we might have addressed many of the questions already, but I want you... If you don't mind, Avi, go back to that slide that refers to the wars, if you don't mind because this sort of hits on a lot of the questions that maybe some people have had. So one of the things I wanted to point out to because people are like, "Well, what are you doing to protect money? I don't want to lose money." Of course, no one wants to lose money. As Buffett said in his famous Salomon testimony in the '80s, he said, "Lose me money, I'll be tolerant, but lose me a shred of reputation, I'll be ruthless." So I'd rather... We're trying to build multi-generational relationships. And fortunately, in some cases we're working with third and even fourth-generation families. And so it's important to be able to make sure that we're thoughtful about thinking beyond the short term.

And oftentimes, we tell someone, even if they retire at 60, that if you have a 40-year timeframe ahead, we're pretty much certain as we've talked about before that during the 40-year time that someone might need to have their money sustain their longevity because the history is that people experience stock market declines of 5%, three times a year on average... This goes back to 1800. 10% once a year on average, and 20% every two and a half years on average, that means that during a 40-year period of someone's retirement, we have to be able to create a planning and investment structure that is going to enable them to be calm, not to try to predict those moments, but to be calm, to be able to get through those moments for a 40-year period, knowing that you're going to have some pretty material speed bumps.

And right now, we're in one that could be mild. It could be a lot larger and bigger, but it is where it is at the moment. But the point that I want to make about not losing money is all about timeframe. Avi showed a lot of things around the timeframe about large and small companies. Obviously, stocks outperforming bonds, and you can see in this chart, let me highlight this for a second to... This may tackle a lot of questions that people have. This is the history of the data. Of course, the past is no guarantee of a future. Historically, inflation has run at 3%. Cash has historically run at three and a half percent.

Right now, cash yields are more emblematic of World War II, where cash is paying virtually nothing, and the inflation run is running similar to World War II at a much higher rate. So you can keep your money in cash and you could say, "Well, I'm not losing money," but you are losing money because you're losing purchasing power every day. Every day, every year, every month, your ability to buy goods and services is going to decline and that's dangerous for longevity risk and that's something that people lose track of. But in that realm, when someone says, "I don't want to lose any money," they're talking about volatility. The good thing about cash is there's no volatility.

So going back to the Buffett story, the first line in planning when we go through someone's balance sheet is we want to know how much liquidity in lines of credit someone has so that they are mentally prepared to weather any storm. And they're not ever going to be put in a position to be a for seller because you don't know... As Buffett says, "You never know when the hundred-year flood's going to come, but you want to be prepared for the hundred-year floods." So that's the only way to ensure that your money is stable and it's not deteriorating to a great degree.

But if you're really trying to protect money over 40 years, you want to protect money from the invisible risks. And the invisible risks are inflation, taxes, and spending, and those things are going to go up over time. So in order to outstrip three to 5% spending generally for most retirees, like an endowment, three to 5% inflation, plus one to 2% taxes, you somewhat have to accept the notion that you're going to have to have more equity-oriented assets that are going to give you a chance. Forgive my scribbles. That are going to be a chance to outstrip and maintain your purchasing power over time. So the safest thing to do is own profitable businesses that have sustainability to it.

Now, that discrepancy between large and small companies, even in World War II, you could see a massive spread almost 70% more volatility, but double the return in smaller companies. So we're doing what we can to be mindful of protecting people, not just from... We're not trying to insulate someone from recession. We're not going to mitigate any loss whatsoever. Of course, we want to be mindful, we don't want to have too deep of drawdowns. We're looking for assets that can generate a good risk return attribution, but that's never certain as you saw, even if you go back to the Buffett chart and the Berkshire chart for one second.

Avi Berg:

Yeah, hold on.

Jonathan Satovsky:

You can see back to... Yeah, if we go back to this chart, you can see that even in 2015, if we didn't, but if we had all our money in Berkshire Hathaway and a client was looking at their portfolio and just reviewing performance, and they said, "Wait a second, the market was up 1%, you were down 12. You're an idiot, you're fired." Tracking error, that's something called tracking error. If we expose someone to too many tracking errors, people are going to throw up on themselves also. Of course, no one complains about tracking errors in this direction where you're up 10%, and markets are down 10. We're not expecting perfection. We just want to make sure that we have a process and progress that aligns with the way that people are thinking about things. Someone asking the question about inflation or the impact of the supply chain across the global economy. Avi, I don't know, opine on that.

Avi Berg:

Yeah. There are a couple of questions, so let me answer this one first, and thanks for asking the question. We had supply chain problems last year, particularly in semiconductors if you remember, and these supply chain problems always fix themselves, right? Because at the end of the day, when there is an issue with supply, then people will figure out how to create supply in the place where it needs to be because there's money to be made there. And so already, you're seeing... In semiconductors, you were seeing war supply coming on in various parts of the world that were going to fix the supply chain problem. And it was already kind of getting fixed.

Now, the war has created a bunch of other supply chain problems, right? So Russia and Ukraine, they don't have a major impact on the world economy, except for in certain commodities for Russia, particularly oil and nickel, and there are a bunch of other commodities. And so there's going to be an adjustment period if this situation maintains itself, but ultimately, supply chain problems are very fixable and are never sustained because when there's money available to be made, people will figure out a way to make it. So I don't usually get very concerned about supply chain problems in the very long term. And in fact, even in the medium term, they get fixed. It's only very much in the short term where this can be a problem. There were a couple of other questions that people put in.

Jonathan Satovsky:

I'll jump. Before you get the next, I'll just jump in. Tax hit has been tough this year because people had pretty big gains last year. So taxes are coming in at the time that portfolios are taking a little bit of hits, so people are feeling like a double whammy a little bit. So there have been a long stretch of times where the tax... We're able to eliminate taxes altogether, but yes, it is a good problem to have, to have some gains. And that's the trade off we have to make in rebalancing and trimming some of equities over time. During very robust periods, some of the equities that we trimmed last year had tremendous gains, not just last year, but over the last 10 years. And so trimming them back a little bit did cause a bit of a tax hit. The offset of that is some of the assets that we trimmed are down 20% or more in 2022. So the tax cost relative to the rebalance actually net met has worked out better. It's not a guarantee it will always work out that way, but directionally, we are quite mindful of trying to mitigate taxes to the greatest degree possible. And yes, directionally, we are leaning a little bit more towards smaller, cheaper, and profitable factors. So yes, that was clearly highlighted.

Avi Berg:

The other thing I just wanted to mention on the tax issue is we are actually looking to tax loss harvest where we can. We have some losses embedded in the portfolios. So we're going to look to take those tax losses and put them in assets that are pretty similar. So that's another thing that we're actively doing, we've done some already, and we're going to do some more.

The other couple of questions were... let's see. Recession, I think we touched on recession exposure and protection strategy. I mean, part of protection is not being exposed to one market or one factor, making sure that we spend a lot of time. I think it's sort of lost. Think about it like a doctor's checkup, part of the idea of sitting down with your financial planner. Part of the idea of financial planning, which no one values, everyone wants to know what are your fees and what is your performance. But I've been doing financial planning since 1993, so now close to 30 years, and I never understood how people spend so much time on investing. It's sort of like planning a vacation, but not planning their finances.

Financial planning is so much more important than investment planning in many respects because it's very rare that someone takes them inventory of their balance sheet and cash flow to be able to make sure you're calibrating decisions. And part of the idea is to build a trusted relationship with an advisor over a lifetime to look at that balance sheet and objectively analogies to having a doctor where you're looking at the x-ray and making sure that he's not operating on your knee when you have a hip problem or whatever the case may be. So I think looking at someone's balance sheet objectively and understanding the danger points, a balance sheet, cash flow, assets, liabilities where income can get disrupted, that's where the greatest protection can come from to make sure someone's insulated from the unknown unknowns, and to protect you from getting over your skis and making any irreparable damage.

This is a silly example. I won't spend too much time on it, but a year ago now, there was a fund manager that had gone from $200 million to $70 billion because of very good performance in 2020. Well, that particular investment manager is down 60% or more from February of 2021 at a time when everyone piled in and ended up with significant losses. People are still adding to it because they're like, "Oh, I'm fearless." Well, they're adding... You don't just add to something because the price is volatile, you have to know what you own and know that there's margin safety, that people aren't just throwing darts and Hail Marys. I think Tom Brady has been more successful because of the diligence of his process. Unfortunately, I'm from Detroit, just putting anyone on the field isn't going to make a winner, which leads to sort of a good lesson now that we're we're into March madness. So for those of you that have some joy around college basketball, there was a moment, a painful moment for me as a Michigan Wolverines fan, but I think it's a good lesson for investors and for everyone, and this is a good way to sort of end this session to keep it under an hour. Michigan was up by 17 in the second half of a Big Ten Tournament on Wednesday of last week. And they still had chance in the game. They were down by two with 17 seconds to go and you can play this and then I'll opine and comment on it. Go ahead. Indiana, yeah. So Indiana takes a shot. Freshman Diabate gets the rebound. I don't think it's playing very clearly, but you could see it in slow motion. He gets the rebound, hustles, does a great job, but instead of relaxing, he quickly gets it out of his hands, and throws the game away. He got the rebound. They played defense. They locked down the defense. They did what they needed to do. They locked down the defense and yet he made too quick and too rash of a decision. So the lesson I want you to take away from this is that you don't need to react with first level principles. Of course, everyone's like, "Well, Russia invaded the Ukraine, got to buy oil!" And of course, oil prices went parabolic. And then as expected people pile into oil prices, and then now, prices, I think the last several days have been down sharply.

Just because everyone's doing something in a moment in time doesn't mean you have to do it. At the moment, the safe haven...someone asked about gold. We've owned gold on, on and off over the last 25, 30 years, and it's a good... Historically, it's been a protection from chaos or inflation and that's the same theory of why people are buying cryptocurrencies, and NFTs, but it doesn't always function particularly well. But certainly, when people are frightened, they move into things that they perceive to be safety. And then when they're no longer frightened it... I heard many years ago that gold is the inverse of trust in the financial system. So when people don't trust the financial system, gold goes up. But if you look at the cash flows into gold, what's interesting is now that it just crossed 2,000, I think it dropped below 2,000 a day. The money flows again, go up when the prices are up, and then when they're down, it's no good. I mean, even the UK central bank who had held it as their reserve in the '80s, 1982, in 2000, when it had declined significantly from 1982 when inflation was high, it declined for 18 years into 2000. And then of course, they cut their gold reserves in 2000 just in time for it to rally again. So you don't have to make rash decisions. We are trying to be very diligent, thoughtful... Avi's calming me down to not react and be like, "Sell it all, buy it all," relax, slow down, you have a persistent process. You're planning for 40, 50, 60, a hundred years. Even Buffett, who's 90, and Charlie Munger, who's 99, who have a conference at the end of this month, in April, or the beginning of April, they're investing for multiple generations. They're still looking beyond their lifetime to multiple generations of investments. They're not making investments saying, "I'm 90. I could die in two years. Let me put everything in a pile and curl up in a corner and wait to die." They're still looking out on the horizon.

So, I would encourage you. And hopefully, thankfully somehow Michigan got into the tournament they're playing in for Thursday. But hopefully, Diabate will learn from the experience. And when he gets the rebound, instead of quickly getting it out of his hands, he can relax, survey the landscape, maybe pass it forward to DeVante Jones, and maybe, Michigan will win a couple of games. That'll be my hope for the Big Ten Tournament, even though, obviously, no one here really cares about my Wolverines. It was just my paying homage to the Wolverines.

Thank you all for your trust, confidence, and for enabling us to steward your resources for multiple generations of families and for, God willing, another 25 to 50 years, we'll be able to continue to build out a team and technology and people to support you and your families and anything that we can do. Call, and talk to an advisor. If friends or family value our perspective or need advice, and our stewardship, we welcome the opportunity to help. Thank you again.

Avi Berg:

Thank you, everybody. Thank you for listening.