

# Playing Chess, Not Checkers

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As the Chief Investment Officer of an asset management organization that relies on proprietary security selection, I find myself involved in many conversations about buy, sell, and hold decisions for the securities that comprise our client portfolios. Naturally, I very much welcome such discussions. However,

after nearly twenty-five years, I have realized that the biggest misconception I must explain is the difference between "playing" the market, trading stocks, and investing in companies.

We invest in the future growth and profitability of the companies that we own in portfolios, not a near-term outlook for a stock's price action. We invest very differently from how most retail investors are taught about how one invests in the market. Trading stocks and playing the market is an entirely different endeavor compared to investing in companies. Investing in companies involves understanding financial statement analysis, return on invested capital, industry/competitive analysis, macro-economic factors, and disruptive technology risks/opportunities. Trading stocks and playing the market requires monitoring market dynamics such as money flow, technical indicators involving price moving averages, and movement in quarterly earnings estimates versus the probability of beating or missing near-term analyst estimates.

The vast majority of what is written and broadcast on television and found on the internet about investing focuses on trading securities and playing the market. Occasionally the financial media will give time to investors such as Warren Buffett, Ron Baron, and Leon Cooperman. These well-known investors are focused exclusively on the long-term forecasting of a business' fundamental financial performance. However, for the most part, the financial media's attention is focused on minute-to-minute and day-to-day trading.

Because most of our clients are inundated with media discussion and analysis of trading dynamics and short-term market forecasting, we find ourselves explaining why our portfolio actions appear to conflict or are at least uncorrelated with the current market sentiment. We pay very little attention to short-term market dynamics or behavioral finance indicators such as sentiment, other than when weakening sentiment may give us a buying opportunity. We are not overwhelmingly contrarian investors, but we are willing to be contrarian if the opportunities are compelling bases upon our long-term fundamental outlook.

The most confusing thing about the stock market for most investors is the "why" question. Why did the market go up or go down today or this week? Why did X stock go down so much when the market did not? Why didn't you sell X stock when it went up over the last year? Why did you buy more of X stock two or three different times when it has mostly gone down?

The simple answer to most of these "why" questions is that markets and stocks go up and down for reasons that are not criteria upon which we base our decisions. Instead, stock prices, for the most part, are market-driven in the short term by sentiment, technical market structure considerations, and institutional money flow. Unfortunately, today's public markets and traded securities are dominated by day-to-day money flow derived from trading strategies that are not fundamentally driven; they are instead price-driven and value agnostic. We make our investment decisions on securities that are

unfortunately tethered to these non-fundamental and value agnostic markets. We accept that short-term price moves are mostly non-fundamentally driven. With that acceptance, we base our decision upon criteria that are unique, value-driven, and long-term in duration. In a way, most market participants are playing checkers, while fundamentally focused long-term investors are playing chess. Our moves are part of a long and interconnected multi-dimensional strategy. Winning our game requires vision, conviction, and patience. The checker players play a two-dimensional game at best; it is fast and more tactical than the multi-dimensional, deliberate, and strategic game of chess.

Therefore, most times, when we are asked a "why" question, we provide what sounds like a dodge. We typically admit that we don't try to answer the "why" question other than the effort we make to rule out a fundamental underpinning to a price move with as much certainty as possible. The reality is, most short-term market price action is background noise to us.

We are unapologetically long-term investors.

We do not set out to simply make money trading.

We set out to build durable wealth over the long term.

The reality of making money in the markets can be very fleeting if you are playing the market or trading stocks. Like everything in life, if something is acquired quickly and easily, it can just as quickly be lost.

Building durable wealth requires far less transactional risks in the form of time-dependent wagering, which is at the root of most trading strategies. Building durable wealth takes longer, is underpinned by intrinsic value factors, and benefits from the amazing power of compounding when executed properly.

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Disclosure:

Advisory services offered through CS Planning Corp., an SEC registered investment advisor.

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