OUR FAMILY PERSPECTIVES

INSIGHTS FROM CANADA'S LEADING FAMILY OFFICE

First Quarter, 2018 - April 18, 2019

On the heels of the worst quarter for public equities since 2011, the first quarter of 2019 has sent the bears back into hibernation as the spring thaw caps off a double-digit rebound from Q4's painful sell-off. The last time global equities[i] delivered a first quarter return above 10% was in 2012, which precipitated a mid-single-digit second quarter decline followed by two consecutive positive quarters - ultimately finishing up with just under a 16% return for the calendar year. Though we're pleased to participate in this year's equity market bounce, caution is the watchword, as much of the run-up has been driven by mutliple expansion rather than earnings growth. At the time of writing, the S&P 500 Index is roughly 1% shy of it's all-time high reached on September 20th of 2018. So, although investors may be riding high on 2019's bullish surge, we're pretty much back to where we started approximately six months ago. Only now, the Fed funds rate is 25bps higher, 2019 corporate earning expectations are 5% lower, and weakening global growth forecasts have begun to surface.

So, what gives? How should investors position for the future against a backdrop of emerging risk factors? Those that know us well will not be surprised to hear the all-familiar refrain of downside protection above all, alongside a wholehearted embrace of the "defense wins championships" philosophy that forms the foundation of Our Family Office's investment program. Rather than attempt to predict or time short-term market direction, our focus is fixed on constructing globally diversified portfolios comprised of unique & resilient investment strategies with a proven ability to withstand both macroeconomic and market-driven headwinds. Governed by a thoughtfully formulated strategic asset allocation blueprint, our investment platform is designed to provide access to creative and flexible solutions across a wide range market verticals.

One topic that has commanded significant attention (understandably so) is the active versus passive management debate. Though both sides of the argument present interesting thought-work, we refute the binary divide that seems to want to push for exclusive allegiance to just one side of the fence. Said differently, our investment program is built upon the premise of sourcing the most competitive risk-adjusted returns on a net-of-fee basis across a broad spectrum of public and private markets. In some areas, passively managed strategies offer a higher degree of confidence in obtaining top-quartile long-term performance over their actively managed counterparts. In others, active management is our preferred path. And in private markets, of course, active management is the only option. By combining quantitative analysis of long-term data sets with informed judgment, our pursuit for out-performance aims to focus exclusively on opportunities where the probability of success is skewed in our favor. In other words, we try to identify which battles are the most winnable before sending out the troops.

Take the S&P 500 Index, for example – a broad proxy for arguably the most efficient market in the world. On average, there are 21.2 analyst ratings per stock within this index.[ii] Intuitively, it seems reasonable to question the ability for stock-pickers to consistently "beat the market" with so many eyeballs closely watching each company. But what does the data show? While there are countless ways to slice and dice the numbers, we reviewed periodic out-performance among active US Large Cap equity managers to get a sense of what the distribution looks like in recent years.[iii] In Q1 of 2019, 108 of 363 funds tracked outperformed the S&P 500 Index; for calendar year 2018, only 12 of those 108 prior out-performers beat the index; in 2017, 7 of those 12 outperformed; in 2016, 1 of those 7 outperformed; and in 2015, none outperformed. Though this very simple look-back analysis can be challenged or "enhanced" to consider risk-adjusted outcomes, the point we aim to make is that consistent outperformance is extremely elusive, particularly within crowded markets characterized by intense competition, high transparency, and democratized access to information. For these reasons, our large cap US equity portfolio footprint is structured to "be" the market, rather than attempt to fight a battle with very low odds of winning.

While it's unlikely that you'll find us turning over rocks in search of the next best superstar stock-picker, we do, however, spend considerable time hunting for opportunities where our expected "return on research" is high. More often than not, our interests gravitate towards areas that are either under-followed, less-liquid, or capacity-constrained. Though the landscape of interesting opportunities is continually evolving, careful and selective identification of what we believe to be mis-priced risk can provide fertile ground for capturing asymmetric returns. Simply put, we spend a lot of time searching for ideas where the risk of losing money is low, and the confidence in obtaining a positive return is high. As one would imagine, these types of opportunities are typically in limited supply, particularly in environments where capital is easily accessible and market participants behave in an undisciplined manner. For investors with geographic, liquidity, or asset class constraints, the ability to source unique and attractive investment ideas is limited to the "fishing ponds" where they are equipped with rod and reel. Our Family Office's investment program, however, is assembled in a truly unconstrained fashion, allowing us the full flexibility to explore and pursue strategies without restrictions. A close working relationship with our US affiliate, Ballentine Partners, expands sourcing capabilities, further enhancing the breadth of our investment platform.

By combining cost-effective, highly liquid exposures within efficient market verticals (i.e. "cheap beta"), alongside differentiated, unique opportunities within less-accessible corners of the world (i.e. "scarce alpha"), our goal is to participate in positive long-term directional trends (recognizing that short-term return patterns are highly unpredictable), while protecting against significant drawdowns that can prolong investors' ability to compound capital at attractive rates of return. The defense versus offense equation embedded within this stated portfolio design draws from both strategic and tactical asset allocation decisions. In today's investment environment, defensive positioning is readily apparent on both fronts, as we are much more concerned with protecting the gains many of us have generated during the longest bull market in post-war history than we are with eking out incremental upside. There will come a time when it makes good sense to play offense, which is likely to coincide with widespread asset sales clearing at economically irrational prices. We don't know what will cause this dislocation (though we have some ideas), but we know we'll be prepared to act. As always, we thank you for trust and confidence, and appreciate the continued support.

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[i] Performance data based on the MSCI All Country World Index (LCL)
ii Data sourced from Bespoke Investment Group
ii Data sourced from Morningstar Direct