

July 31, 2021

Fellow Investors:

In my first letter, written last quarter, I explained my motivation for writing a newsletter and also outlined some views of the stock market and valuation analysis. Judging by the many responses I received, it appears the letter was appreciated. Thank you for your continued interest and support.

In reflecting on the previous letter, I feel there are several additional important questions that should be addressed. This letter is an attempt to address these questions. I hope you will find them as interesting to read as I did to write.

Why have I chosen to be an investor?

All of us have certain proclivities in life; tendencies or activities we are drawn to almost impulsively. Ever since I started in finance over a decade ago, my mind has never ceased thinking about investing. I have spent many thousands of hours reading and pondering on financial theory, history, and practice, particularly around valuation and business strategy. I often spend my free time building models and reading about new companies. Investing is where my thoughts habitually trend. For me, investing has been an endlessly fascinating endeavor that continually challenges me and also satisfies my curiosity. I simply love it.

Additionally, several of my family members and friends have recently come into some money and have reached out to me for investment advice. As I look around and consider the other options available to them, frankly I find very few that I could recommend with confidence. Too many managers charge high fees for poor results. I feel I can provide them a much better service than what they would likely find elsewhere. You've probably heard the old quote: "Luck is what happens when preparation meets opportunity." In that sense, I am lucky to be able to help my family and friends.

How can I hope to be successful?

Merely being interested in something does not mean you will be any good at it. And a very large segment of the financial world seems to sincerely believe that it is impossible to be better than average anyway, so why try? What makes me think I can succeed in this business? The answer to these questions is a combination of both personality attributes and the characteristics of the portfolios.

The most notable personality attribute needed for investment success is independence of thought. Following the investing consensus, at best, leads to average results. This independence of thought is a core attribute of my life. At times it makes me an awkward guest for a dinner party, but it does make me a better investor.

Furthermore, as alluded to in my previous letter, after many years of study and practice, I feel I have a strong knowledge of how to identify good investment opportunities. These two characteristics, independence and competence, combine to form the essential personality required for superior investment results.

Several characteristics of the accounts will also provide a unique advantage in investing.

- 1) **Small Size:** The relatively small size of the current client accounts allows me to take advantage of opportunities that larger investors either can't or don't want to do. Large investors are limited to only large dollar opportunities. Being small allows for a broader investment universe.
- 2) **Stable Capital:** All of the current clients are family and friends. The existing basis of trust, and the longer-term nature of the relationships, should result in a more stable and longer-term capital base. And long-term, dependable capital can be a portfolio advantage.
- 3) **Flexibility:** I am free to invest in nearly anything, anywhere, and anytime I find it attractive to do so. Most professional investors have strict limitations on the funds they manage. This flexibility can be a great advantage as it allows me to adapt to whatever market environment and opportunities may be present.

- 4) Alignment of interest: I am personally invested along with you. While the client portfolios are not identical, they are broadly similar. I personally own most of the stocks held in any portfolio.

For the sake of clarity, let me here add a few areas of potential investment success where I will not have an advantage.

- 1) Speed: My results will in no way be dependent on speed of information acquisition or of trade execution.
- 2) Inside Information: Apart from being illegal, I also want to state that I claim no special connections or relationships to people that could provide such “tips.”
- 3) Sheer Brilliance: I make no claim of being materially smarter than others, and I don’t feel it is required to be successful. High IQ scores don’t count for much if investors are distracted by incorrect assumptions or hindered by policy.

As stated above, many people, perhaps even a majority, believe it's impossible to achieve better than average investment returns. They often cite the number, brilliance, and speed of the competition in the markets as arguments against the possibility of above market returns. However, if said competition is conventional (which it usually is), lacking proper analytics (which they often are), or constrained (which they nearly all are), then there will remain ample opportunities in the markets for those few of us able to overcome these obstacles. As I look around and examine the competition, I remain undaunted.

This brings to mind another well known saying often attributed to George Bernard Shaw: “People who say it cannot be done should not interrupt those who are doing it.”

Why should someone choose me instead of a traditional financial advisor?

I am not a traditional financial advisor. Most such advisors (e.g., employees of Edward Jones, Fidelity, Wells Fargo, etc.) actually know relatively little about investing. They work for large firms that are considered trustworthy and offer a wide array of services such as tax advice, retirement planning, trust management, etc. The core skill of these advisors is relationship management. They are very likable people. They act conventionally and primarily focus on

not being wrong or doing anything questionable. Their goal is usually asset gathering: having as much money under management as possible, from any source. Most offer only generic investing advice and often do not even support investing in individual stocks but rather allocate assets to overly diversified funds as recommended by their firmwide committees. Their results are also typically generic. (After all, when has a committee ever made a bold decision?) Sadly, their clients usually end up paying high fees for poor performance.

Contrariwise, I am an independent investment analyst and portfolio manager, similar to how Warren Buffett's early partnerships were run. My sole specialty is investment analysis aimed at achieving high investment returns over the long term. I do not offer any other services. I will likely make many investments that others, especially traditional financial advisors, will consider too risky. I accept that I will occasionally be wrong, but that openness to being wrong is a necessary condition to being right. And in investing, a few right choices can more than compensate for many wrong choices. I have no committees to please and act at my sole discretion. I will therefore also bear sole accountability for the performance.

These differences should be well understood by all clients. I believe my position as an independent investor provides the greatest possibility for strong investment returns, despite the difficulty of establishing myself without institutional assistance.

How will the portfolios be managed?

The portfolios will be focused on stocks, with a long bias, and long-term orientation. But I remain open to the possibilities of short selling and investing in bonds or options or anywhere else I see value. I may also comment on these markets from time to time.

Despite all the advantages outlined in this letter, I must also state that investment results are impossible to predict with accuracy. Therefore, I cannot tell you when returns will be realized. Furthermore, I also cannot guarantee that losses will always be avoided; however, avoiding losses is my goal. Lastly, because the strategy is unique, it will likely not correlate with the general market.

Closing Thoughts

If you want a simple update on your portfolio or are curious about the positions, you can log in and view all the information anytime at the Interactive Brokers website. All required tax documents are also available there, as well as the ability to make changes to your account (updating an address, adding or removing funds, etc.). I do not have access to do any of these tasks for you.

Lastly, in a world where so many investment scams exist, allow me to reassure you that I have only trading access on your accounts. I do not personally have access or ownership of any of your funds. I cannot withdraw the funds and run away to the Bahamas. If I die, you will have uninterrupted access to your funds, but, of course, you will have to start making your own investment decisions.

Regards,

Todd Niemann, CFA