Quarterly Review & Outlook

3Q Review

Despite slowing economic growth, ongoing trade tensions and a presidential impeachment inquiry, U.S. equities recovered in September to end the third quarter on a positive note. Year-to date, large-caps outperformed mid and small-caps, with the S&P 500 up 21%, while the S&P MidCap 400 and S&P SmallCap 600 gained 18% and 13%, respectively.

Even with the gains in September, international markets ended the quarter with losses while holding on to year-to-date gains, with the MSCI EAFE and MSCI Emerging Markets Index up roughly 13% and 8%, respectively.

For the first time in many quarters, Value outperformed Growth, but time will tell whether this reversal continues. Year-to-date, Growth stocks still hold a substantial lead

While rising Treasury yields hindered performance in September, U.S. fixed income managed to finish the quarter with gains.

Commodities recovered in September but still ended the quarter with losses.

DCP US All-Cap Review

Against this somewhat sanguine backdrop, we saw the US All-Cap Portfolio continue to participate in the upside. For the quarter the strategy advanced 1.26% bringing its year-to-date return to a very respectable 16.53%. While the strategy continues to lag the S&P 500, the underperformance is within the expected realm given the strength of the markets in 2019.

The underperformance was driven by our underweight to Financial and Consumer Staples sectors which turned in two of the strongest sector performances for the quarter. Positive contributions were made through our stock selection in the Technology and Healthcare sectors.

DCP International All-Cap Review

Our International portfolio outperformed its MSCI EAFE benchmark notching a return of 0.43% vs. a -1.00% return for said benchmark. The strategy is now more than 200 basis points ahead of its index for the year, ending the third quarter with a return of 15.66% vs. 13.35% for the MSCI EAFE.

The outperformance can be attributed to strong stock selection, particularly in the Consumer Discretionary, Healthcare, and Consumer Staples Sectors. Our underweight to the Financial and Technology sectors were the main detractors for the quarter.

Why Value Investing Works

Jack Schwager, the author of Market Wizards series, when answering a question on whether value investing works, turned to the wisdom of Joel Greenblatt, one of the foremost experts on the subject.

Schwager quoted this from his interview with Greenblatt –

Value investing doesn't always work. The market doesn't always agree with you. Over time, value is roughly the way the market prices stocks, but over the short term, which sometimes can be as long as two or three years, there are periods when it doesn't work. And that is a very good thing.

The fact that the value approach doesn't work over periods of time is precisely the reason why it continues to work over the long term.

You see, the biggest problems in the long-term practice of value investing are that –

1. It flies in the face of anything taught in business schools where most influencers/experts come from, and
2. It requires a painful degree of patience because it is only over long periods of time that the market eventually gravitates toward value.

As Schwager quoted Greenblatt –

It is very difficult to follow a value approach unless you have sufficient confidence in it. In my books and in my classes, I spend a lot of time trying to get people to understand that in aggregate we are buying above-average companies at below-average prices. If that approach makes sense to you, then you will have the confidence to stick with the strategy over the long-term, even when it's not working. You will give it a chance to work. But the only way you will stick with something that is not working is by understanding what you are doing.

This is a very important statement Greenblatt makes, that the *only* way you will stick with something that is not working (temporarily) is by understanding what you are doing.

Sadly, most people participating in the stock market **don't really understand what they are doing**. This is especially when making money gets quick and easy, and they are doing great at it.

Like Aesop's wolf in sheep's clothing, they play a role contrary to their real character, which often leads them to the slaughterhouse.

However, the lack of patience of such people to invest with a long-term horizon creates the opportunity for the few committed to long-term holding periods.

In the battle between impatience and patience, the latter wins.

All in all, Greenblatt's simple idea is so insightful. **Value investing works (over the long term) *because* it sometimes does not work (in the short term).**

With over fifteen years of practicing value investing with sincerity and with decent success (purely based on personal standards of success), as well as seeing a lot of my fellow investors drop out due to their disbelief in its continuity and now ruing their decisions, I can vouch for this powerful idea.

The team and I at Durand Capital truly appreciate your loyalty and trust. As always, if you have any questions regarding anything above, or just questions about the strategy in general, please do not hesitate to get in contact.

Sincerely,

Jim Tassoni
President/CIO
Durand Capital Partners