The Most Important Thing (Mr. Market Revisited)

The **most important thing** in investing is to make decisions based upon what you know (or what you can know) rather than what you don't know (or cannot know). And never ever let something you don't know override those things you do know. This is easier said than done, which is why only a very small percentage of people have been able to accumulate meaningful wealth investing in publicly traded securities during their lifetime.

Trying to make investment decisions based on geopolitical and macroeconomic events is not only unproductive, but it can actually be destructive. Understanding this is the foundation of our entire investment process. Geopolitical/macroeconomic events are ensnarled in a complex global system of practically infinite variables all moving in different directions. In economics, there is an almost universal "law of unintended consequences." When you push on one side, something (often unpredictable) always pops out on the other side to counter-act whatever you might be focused on. And yes, certain events will have a negative impact on the overall economy, but you will never be able to predict exactly what will trigger a relevant economic impact or when.

Both the media and the financial services community have a vested interest in amping up the news of the day. The media benefits from stoking the flames of fear and anxiety to increase viewership, and the financial services industry benefits when large sums of money move around due to emotionally charged buying and selling activity. And they know that geopolitical and macro events are almost always wrapped up with emotion. But your emotions are your worst enemy in investing. People always react to geopolitical and macro events like *oh, this is so obvious, it's different this time*. But as Sir John Templeton says: "The four most dangerous words in investing are: 'this time it's different.'"[1]

And there's another important twist. Publicly traded security markets have many of the same characteristics of a pari mutuel betting system; like the racetrack, where the favorite horse has the lowest payout. So, even if a so-called "obvious" event occurs as predicted, markets often move in the opposite direction from what investors expect. Yet most investors continue to make predictions about the stock price impacts of geopolitical and macroeconomic events, even though they are almost impossible to predict, and even though those events (when they do occur) often do not correlate to the price movements of a given stock.

By making investment decisions based on geopolitical and macroeconomic factors, most investors (both large and small) are playing a nonsensical loser's game. Our efforts to remove ourselves from this chaos have enabled us to compound capital at meaningful rates for decades, building real wealth for scores of families as a result, throughout a never-ending string of various political, economic, and global news and events. When it comes to investing your capital for long-term compounding, **avoiding spending time on what we cannot control is "the most important thing in investing.**"

I began to accept this brutal truth over forty years ago, when I first read Ben Graham's groundbreaking book *The Intelligent Investor*; specifically, Chapter 8 entitled *The Investor and Market Fluctuations*. You **need** to read the enlightening attached article by Warren Buffett that perfectly summarizes Graham's ideas about "Mr. Market" from that chapter. Contrary to the irrational stock market environment (that is even more irrational today with endless 24/7 media and marketing), *The Intelligent Investor* was the first book to explain the easy-to-understand, but hard-to-practice concept that buying stock is simply a way to purchase an ownership interest in a business. Understanding both the economics and competitive advantages of that business and what represents a fair value to purchase that ownership stake are completely knowable variables. And the knowledge one accumulates about what gives one business an advantage over its peers is cumulative, and such knowledge will compound over time. By contrast, knowledge gained from focusing on geopolitical events does not help an investor predict the next geopolitical event or (more importantly) its effect on future stock prices.

Ben Graham was Waren Buffett's primary mentor, and Buffett recognized early he needed to create a working environment and business structure that insulated himself from the noise and emotional turmoil perpetuated by the financial community, the media, and public opinion around these events. Working from the confines of Omaha and creating a totally insulated structure at Berkshire Hathaway enables Buffett to be almost completely detached both from the noise of Wall Street and even from his own shareholders, other than the famous, annual Berkshire shareholder meeting. This optimal working environment liberates him to become a learning machine to understand what it takes for a business to develop long term competitive advantages and to be able to identify and boldly act upon opportunistic purchase entry points to accumulate its stock that will enhance long term compounding. In fact, there is a common characteristic shared by the few truly exceptional investors with track records that have withstood the test of time: They have figured out how not to be distracted and influenced by the noise and pressures to conform to the irrational forces of traditional geopolitical/macroeconomic investment industry thinking.

We believe the way to protect ourselves from that which we do not control is to put 100% of our effort into what we do control. Over the years, our ability to see the investment world through the lens of owning outstanding businesses at attractive prices has grown in clarity and as such our focus has become increasingly narrower. We believe this maniacal focus has materially improved our work and your/our performance. The downside of this disciplined approach is that I have become even more protective of what we perceive to be this enormous competitive advantage (to be able to see the investment process unencumbered by emotion). Our responsibility is to compound the capital that has been entrusted in us at meaningful rates over long periods of time, and in many cases that means deflecting the emotional distractions that can cause us to lose our cherished focused approach.

We understand we might come across as uninformed, dispassionate, or unsympathetic about the current news cycle. Quite the contrary, we each have our own strong morals and beliefs. And outside the confines of managing your hard-earned capital, we can be quite passionate about what we perceive to be injustices that regularly occur in various places on the planet. One area where we believe our rational investment approach can help promote

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[1] Sir John Templeton (1912-2008) is a legend of value investing, and he is one of the few investors whose track record has withstood the test of time, with an investment career spanning 70 years from before World War II until his death in 2008. In 1999, *Money* magazine called him "arguably the greatest global stock picker of the century." Templeton's investment performance reportedly beat his indices by 3% per year on average throughout his career. Notably, Templeton spent the majority of his career based in the Bahamas, effectively insulating himself from much of the Wall Street noise.

justice is in the workplace. We are passionate about the societal and economic benefits we can achieve by identifying and partnering with companies that create fulfilling, empowering, and collaborative work environments for all of their employees. We believe that by supporting great employee empowerment companies, we can do good for the largest number of people within the reach of a small boutique investment firm in Missoula, Montana, and, as we think we have demonstrated over multiple decades, it is simultaneously our most reliable way to compound your capital at meaningful rates over long periods of time.

If you have not already done so, we encourage you to read our last letter "The Lean Advantage". This letter explains our process, our passion and our fascination with identifying and partnering with companies that strive to unleash human potential by creating empowering and collaborative cultures. We believe over the past forty plus years we have become incrementally better at understanding the variables that are under our control, and as a result we have never been more excited about our future prospects.

Thank you for your patience and continued confidence.

Sincerely,

The Front Street/Tarkio Team

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"Mr. Market"[2]

Long ago, Ben Graham described the mental attitude toward market fluctuations that are most conducive to investment success. He said that you should imagine market quotations as coming from a remarkably accommodating fellow named Mr. Market who is your partner in a private business. Without fail, Mr. Market appears daily and names a price at which he will either buy your interest or sell you his.

Even though the business that the two of you own may have economic characteristics that are stable, Mr. Market's quotations will be anything but. For, sad to say, the poor fellow has incurable emotional problems. At times he feels euphoric and can see only the favorable factors affecting the business. When in that mood, he names a very high buy-sell price because he fears that you will snap up his interest and rob him of imminent gains. At other times he is depressed and can see nothing but trouble ahead for both the business and the world. On these occasions he will name a very low price, since he is terrified that you will unload your interest on him.

Mr. Market has another endearing characteristic: He doesn't mind being ignored. If his quotation is uninteresting to you today, he will be back with a new one tomorrow. Transactions are strictly at your option. Under these conditions, the more manic depressive his behavior, the better for you.

But, like Cinderella at the ball, you must heed one warning or everything will turn into pumpkins and mice: Mr. Market is there to serve you, not to guide you. It is his pocketbook, not his wisdom that you will find useful. If he shows up some day in a particularly foolish mood, you are free to either ignore him or to take advantage of him, but it will be disastrous if you fall under his influence.

[2] *Excerpts from the 1987 Berkshire Hathaway Inc. Annual Report*