A long, long time ago my wife and I were invited to the races by some friends. We had never been to a horse track and had absolutely no idea how to evaluate a race form or interpret the information available on the race sheets in order to make our bets. I can remember studying the data, taking input from our friends as to what was important, making calculations based on all the available data, and choosing a horse. Gail, my wife, had a different process for making her selections. She simply waited for the horses to show up on the track before each race and then decided which of the jockey’s outfits and colors she liked best. I am sure you know where I am going with this…she did the best that day. By the time the last few races came up we were all looking to her, waiting for her to review the parade of colors and make her choice. The fact that there was neither rhyme nor reason to the process was a secondary consideration to the results she had been able to achieve. Somehow her process had become unimportant to us because it had generated positive outcomes…albeit over a very short time period.

Of course we were all just having fun with it that day at the track, but I see a similar scenario play out time and time again in the equity markets. We have written on the concept of process versus outcome in the past, but in our view it is one of the most important themes for investors to understand and refer back to over the course of their investing lives. Over short time periods a poor process can produce positive outcomes. A shot from half court might go in during a basketball game, but that does not mean it was a good decision to take the shot. A stock purchased solely because it has been going up or because it is popular in the media does not incorporate a good process…even if you make a profit on it. Over longer time periods, such as the complete market cycles or even the decades that most of our clients will be engaged in the equity markets, a sound process is much more important than short term results.

In our view, there are periods during which the broader environment seems to favor poor processes, or at least it does not punish them. We believe the current extended period of very low rates have enabled what we would classify as lower quality companies to be more competitive than they would otherwise be, taking share from companies that might be better managed. If company x borrows as much as they can and lever up their balance sheet without regard for the long term consequences they may be able to stay in business longer than they otherwise would. In the short run, they may even sell more products (probably at lower margins) than a more conservatively managed competitor who is focused on the longer term. We often see the stock prices of these types of companies rising as investors who are also focused on short term results drive the prices up. The process (simply buying what is going up) is not sound at all, but is justified by the outcome of a rising price.

Ultimately we believe these issues get sorted out. Regardless of what one is doing, there is usually a right way and wrong way to do it. If Gail picked horses every day based on her method the process would soon fail leaving her followers to search out the next shortcut to success, but not before they had lost back what they had previously won (and maybe more) based on her random selections. In our view, the biggest impact we have in this regard is when a consistent process can be aligned with the specific goals, objectives, and risk parameters of each individual client as opposed to simply buying what is hot or trending. It is important to note that having an established process in place is no guarantee of success on each investment, but we believe it should increase the likelihood of successful outcomes over time while reducing the reliance on luck or randomness. Luck and randomness are not words we like to use when discussing our clients hard earned money.

As always, thanks for your time and for your trust. Please call on us anytime.
Introducing Denison Kummrow, CRPS®

I am happy to be the newest Financial Advisor in the Riverwood Group. Although I am new to the team, I am not new to Morgan Stanley. I look forward to meeting you, whether it is in the office or over the phone!

I was born and raised in Waukesha, WI and attended the University of Wisconsin – Madison. There, I graduated with a double major in Economics and Political Science.

My wealth management career began in 2001 at A.G. Edwards & Sons. In 2007 I changed firms and joined Smith Barney, which ultimately became Morgan Stanley Wealth Management. While I am new to The Riverwood Group I have had the pleasure to work in the same branch as Mark, Sara and Jeff for the past ten years. As a member of the Team, my focus will be on supporting the day to day management of our clients’ portfolios. Primarily I will be responsible for all forms of research, analysis and evaluating money management strategies.

I currently live in Oconomowoc with my two sons, Noah (12) and Brady (8). When away from the office I enjoy fishing, reading, traveling, playing sports and watching my sons numerous athletic events. It’s a safe bet that you’ll find me on a sideline most weekends of the year…but I enjoy every minute of it.

Dennison Kummrow, CRPS®
Portfolio Manager
Financial Advisor

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