Long Term Success for Part-Time Investors

By Greg Lewin

Letter to Readers

I wrote this investment guide to help people. Very few are in the enviable position that they don't require returns on their capital to live the life they wish to live. For the vast majority we must invest to realize our wants and needs. Unfortunately, we are living in a period when the primary source of low risk returns, the bond or fixed income markets are no longer suitable for rational investment. As a result, we all must invest in riskier investments whether we wish to or not.

For those that find themselves in this position I want to help you better understand the task that lies in front of you. There are many ways to approach the investment problem. In this document I am trying to lay out the basic understandings you need to consider before you begin. These ideas can be of value whether you choose to invest on your own or give the money to another. I also believe this discussion can have considerable value beyond the confines of the investment world.

This investment guide was not written for the profit. My goal is to make it freely available to as many people as possible. If you find this writing of use, and possibly enjoyable, please send it to others and then ask them to do the same.

This investment guide is not intended as investment advice. Please consult with a professional financial advisor before investing.

Introduction

Investing is a sacred act. It is a mirror into the soul and a path to chase your dreams. I know this sounds a bit over the top but indulge me for a moment. Consider this, the money you invest is not the money you use to house, feed, clothe, educate and care for those you love. It is not the money you require for medicine, to help those in need, or to support your place of worship. Depending on your priorities, those dollars are the first dollars you earn. And not to diminish or wrongly characterize any of those things, perhaps those sacred things, if I may, those are not the things your dreams are made of. The dollars you invest are those dollars that you have earned that are unattached to those things you may consider obligations, demands or non-negotiables. The dollars available for investment are the excess you have struggled to acquire. They are the end product of your effort, discipline, and ingenuity. They are the reason that you studied hard, worked late, made the tough choices, and prioritized bigger goals over easier acquired pleasures. They are the product of your life's work and they enable you to pursue your dreams. They grant you choice in a world that is forever demanding. They offer you independence from the terms dictated by others. And they enable you to be patient and studied when day to day life rarely grants you the time to breathe. If the beauty of a life is captured by the privilege to stop and smell the roses or the space to pursue your dreams, then perhaps all the sacrifice that went into making this possible is worthy of the designation, a sacred journey. And given this context, how you choose to invest your precious capital is a very special responsibility, a sacred act.

How is it possible that a story told during dinner with friends, a brief interview on television, a column in a newspaper or a report that some well known investor bought a stock can possibly be sufficient to invest that capital. Shouldn't it be harder than a few keystrokes on a computer to spend something that effectively took you a lifetime to earn? Maybe you understand this intuitively and that is why you feel so much pain and loss when investments fail. And all that you are left with is the parade of backseat pundits explaining how they saw this coming all along. The business media and brokerage houses have hundreds of pundits with hundreds of opinions ready to parade in front of you with the expressed purpose of increasing their credibility. They are playing a game, they have their own agenda and they have little to no awareness or

attachment to the sacrifice you made to get your self in position to invest in the first place. I wrote this investment guide to honor the sacrifice you made and help you maintain and grow the advantage you worked so hard to achieve.

This guide is broken into two related but separable parts. Think of this as a 40 page book, each part approximately 20 pages in length. Part 1 is a discussion of the psychological preparation for investing. This part of the book focuses on the impact of stories and expectations on behavior, decision-making, and goal setting. Part 2 is a more methodological approach to the strategy and tactics of investing. The successful investor must develop a command of both the art and science of investing. This is intended to be a practical guide. You are encouraged to read the parts that serve you best.

PART I

The Art of Investing

First Things First:

Does anyone know the definition of a wealthy person? This is important stuff because if you don't know what you are chasing how can you possibly construct a strategy to get it. If I was your personal money manager and the S&P 500 was up 8% and you are up 10%, are you satisfied? If the the S&P 500 was down 10% and you were down 8%, is that okay? The answer to each of these questions and the hundreds more I could generate is always the same, maybe. We both think we know what was said and we may have even agreed in writing but does that matter if your best friend doubled his money over the same period; if the Nasdaq soared and the S&P lagged; if Amazon was up 300% and you didn't own a single share? I know we agreed but does that make you feel better? Of course the answers are no, no, no and no, because satisfaction is not a matter of logic and reason, satisfaction is a matter of perception.

For the majority of us investing is an exercise with meaning and purpose. We don't invest to generate a number. We invest to generate something far more important such as, peace of mind, security, ego, independence, or flexibility. When we touch on subjects such as these we are addressing the most important and complex parts of our human nature. That is why investing more closely resembles a Rorschach Test than an IQ test. In order for us to solve for success we must first define what success means to each of us. To do this we need to understand the stories that define our lives.

We are born storytellers. To prove this point simply watch children play. Whether alone or with others, children are constantly narrating their play, crafting elaborate stories to accompany what appears to be rather simple acts and gestures. Stories activate multiple senses in the brain and spark emotional associations that make it easier to imagine, comprehend, and recall. Adults construct stories just as children do, but awareness of social norms and customs have trained us to carry on these discussions in silence. Everyone knows the little voice that occupies a lot of valuable real estate in our heads. It is hard to recall a time when your mind was still and the voices quiet. Our narrators play many roles such as coach, advisor, protector and promotor, helping us envision great futures when we are riding high or shifting blame and deflecting criticism when failure visits. Perhaps, without our narrators feeding us endless streams of soothing stories, reality would be impossible to manage? Our attachment to storytelling and this incessant conversation droning on in our heads is clearly an adapted trait that is vital to some important feature of our human condition.

When professionals in the investment business share ideas, those ideas are almost

always referred to as stories. And sharing ideas is an incredibly important aspect of the business. For most of us these stories are literally the currency we trade to grow our networks and improve our odds for investment success. Storytelling is not a fictional account of life, it is life, and they are capable of catalyzing changes that fundamentally alter business prospects and change stock prices.

Let me tell you a story about the power of storytelling. A cleaver man had an idea. It was not a unique idea, but it was one he believed in passionately and with the generous support of his parents he started a company in 1994. He incorporated in 1995 and parlayed early success into a $8 million funding arrangement with a well known venture capital firm. In 1996 his business generated a little less than $15.7 million in sales and $5.8 million in losses. No small accomplishment but no small level of losses either. In 1997 he leveraged this early success into an IPO that created a public company valued at $438 million. His IPO prospectus contained the following warning, "The rate at which such losses will be incurred will increase significantly from current levels, and the recent growth rates are not sustainable and will decrease in the future." Fair warning. The company finished 1997 with $147.8 million in sales and $27.6 million in losses and now the big established resource rich companies in the business were coming to compete. In the first ten years of business the company kept its promises. Cumulative losses reached $3 billion and in year ten the company generated $5.3 billion in sales and recorded its first profit of $35 million. In that same year the business had more debt than cash and yet investors gave the company a public market valuation of $21 billion. In 2019 the company generated $280 billion of revenue, $11.6 billion of profit, and in October of 2020 the company was accorded a public market valuation of $1.6 trillion.

We all know the company, Amazon. And we all know of the riches created for management and shareholders. From a traditional stock market perspective the numbers simply never made sense, the investment shouldn't have worked, but it did, creating one of the most transformative businesses the world has ever known. The genius of Jeff Bezos was not the idea or the execution it was the story. Amazon thrived because of one simple truth, Bezos was able to convince a loyal and growing group of investors to disregard the traditional financial numbers that Wall Street demanded. Instead, he got them to buy into the story. This was no small feat. This was not some sideshow, the story was the show. It was his expertise as a gifted and trusted storyteller that enabled him to raise vast sums of cash at incredibly generous terms that enabled him to develop the infrastructure and brand reputation that enabled Amazon to compete with the big boys. Each quarter as the losses grew his investors signaled loud and clear, don't worry we have your back. Jeff Bezos is a remarkably talented man and I

have no doubt that he surrounded himself with equally competent managers. But without any doubt, it was his unique ability to weave a story for the first 20 years of his company's existence that enabled him to build one of the worlds great powerhouses. The story became the reality and consumer behavior changed forever.

Stories rule the world. Religion, capitalism, democracy, the US dollar, political parties, branding, stocks, bonds, Wall Street, culture, art, music, are all predicated on stories. None of us could go about our daily existence without leaning on the stories we have created regarding our health, talent, work ethic, smarts, morality, generosity, goals and dreams. They guide our behavior and dictate our choices. Stories aren't stories, they are the reality through which we live our lives, raise our children, work, play, pray and eventually meet our maker. French writer Anais Nin said it best, "We don't see things as they are, we see things as we are." Our perceptions are our realities and our perceptions come from the stories we have been told, the stories we tell ourselves, and the stories we tell others about ourselves.

So what does that have to do with me and my investments you ask? The answer is - everything. The stories you accept as your own change both your investment goals and your investment choices. Your goals are the single most important building block of your investment strategy. It's pretty simple. The bigger your goals the more risk you must accept to achieve them. A rational and honest appraisal of need versus desire offers the possibility of a reasonable balance of risk versus reward and that improves your odds for success. Rational and reasonable goals are a powerful advantage for investors. Unfortunately, honesty, reasonable, and rational are tough qualities to summon when the subject is money. It is a hard job peering within ones self to construct goals that both address personal responsibilities, mobilize discipline, and command motivation.

I wish creating goals and sticking to them was easy but the human spirit is far from simple. Our perceptions are in a constant state of change as we continuously reinvent ourselves by accepting new stories that change how we define our lives. As our stories change so do our wants, needs, desires, goals, choices, and behavior. If hypothetically you determined that you would be happy with a 5% annual return but all your friends were making a killing chasing Bitcoin, the FANG stocks, the flavor of the moment, can you stay the course or do you feel the urge to be a player? Without your clear and conscious awareness, that voice tells you it's time to turn up the volume on your investment choices and join the chase. Your story is changing and your needs, wants, and desires are changing to reflect your changing story. Suddenly you are investing with less research, less discipline, and without the context of carefully considered goals.

Before you know it investing more closely resembles gambling, eventually returns suffer, and you fall further behind the curve. The lure of wealth is the most powerful narcotic known to man. Simply imagining a different future can convince you to recklessly spend capital with little regard for all the effort required to earn it. **If you can't get a handle on your behavior any and all discussion of investment strategy and tactics is largely a waste of time.** I want to help you understand the real challenges you face and offer tools that can help you overcome and succeed. Investing is monumentally complex and it will require far more than a command of facts and figures to reach your goals. And if you choose to occasionally join the herd I want to help you make smarter decisions that offer a path to profits without risking all that you are fighting for. This is a deadly serious game and I want you to rise to the challenge and possibly become enriched by the journey.

The Man in the Mirror:

When we examine the arc of human behavior we begin with stories because stories manifest how we see ourselves fitting into the world we know now. From these stories come our expectations which frame how we see ourselves fitting into the world to be. Stories build our self-concept, expectations put that concept into action to chase our future wants and desires.

Let's drill down on these thoughts. Pretend you grew up in a family of successful lawyers, doctors, and business persons. Academic success is assumed to be in the blood and all the stories you have heard speak of Harvard, Yale and Princeton as a right not a privilege. Imagine the expectations that are fashioned from this environment. Performance is not an option and the time and effort demanded are accepted without reservation. You know what is expected of you and you never needed to be told because you expect no less of your self. Let's assume you make it through this gauntlet and find your way to a highly paying prestigious job that befits the family storylines. You begin to accumulate personal wealth and now recognize your need to capitalize on that wealth and grow your fortunes. Imagine the expectations you bring to the investment challenge. What return is good enough? What is your definition of a wealthy person? The family lore that informs your expectations is not necessarily consistent with boundaries and limitations. You expect to be rich and so you expect extremely high returns from your investments. After all, those are the stories you hear from your peers and there is absolutely no reason to expect anything less for your self. And so as markets rise and stories of higher returns fill the airwaves and dominate the

conversations you have with family and friends you naturally shift into overdrive and join the herd.

Unfortunately, your decidedly successful life may have failed to help you prepare for the disappointment, loss, and risk intrinsic to stock market investing. Volatility is not consistent with your storyline and its not hard to imagine the stress and frustration you are forced to deal with when an unexpectedly difficult market takes control and losses build. The skills and attributes that have served you so well in the past may not provide the answers and comfort you seek. This is when decision making suffers, fear overwhelms clarity, and temporary losses become permanent. My guess is your broker has heard from you more than a few times and they feel the pressure to respond to your pressing concerns rather than assert their better wisdom. Your performance failed to meet your unreasonably high expectations, trust failed, choices were poor, and performance suffered.

Stories build the plot lines of your life and the expectations that flow from those stories point you to the choices you believe you need to make in order for your stories to come true. This fundamental truth has not alluded the algorithms and social media engines that intrude on every aspect of your life. Yuval Harari shared in an interview that when the algorithms know the smallest amount more about you than you know your self, it's all over. So what is it that they want to accomplish? In simple terms, they want to set your expectations so that they can then fulfill them; selling you products, changing your vote, or directing you to service offerings they wish to promote. The algorithms are focused on your expectations because your expectations are not only predicative of your behavior and choices they are also predictive of your satisfaction with your behavior and choices. This is the holy grail of salesmanship and commerce. They get to tell you what you want and then tell you how you feel about it. It's Christmas everyday for corporate America. At least you get to carry the debt.

You are not happy because you got a $5,000 raise at work. You are happy because you were not expecting a raise or you were expecting a far smaller raise. Perhaps $5,000 would be very helpful for you and your family but if you were expecting $10,000 or you found out some colleagues got more without justification, in your opinion, how would you feel? Consider this example. You forget to study for your college calculus midterm, you walk into the classroom and expect to fail. The following day the grade comes back and you got a 75, you are elated. Then you notice all your friends got grades in the mid 90's and all of the sudden your joy turns to disappointed and anger. You know you are as smart as they are, but you were too stupid to keep track of your responsibilities. **So let's make this discussion really straight forward. You wouldn't buy a stock or give**

your money to a manager if you didn't expect the stock to go up or the manager to succeed! Therefore, the only questions you need to ask before buying a stock or giving your money are: "What am I expecting?" And "Why am I expecting that?" Are my expectations reasonable? Are they justified given what I know and don't know? Do they make sense in terms of my goals and willingness to take risk? Figure out your expectations or join the herd. Supposedly there is safety in numbers.

We measure, monitor, motivate and judge ourselves relative to our expectations. It is your expectations that lead you to judge a choice smart, an accomplishment meaningful, a connection trustworthy or a life well lived. It is your expectations that will inform whether you believe your self to be a wealthy man. Two thousand years ago, Marcus Aurelius said, "If you are distressed by anything external, the pain is not due to the thing itself, but to your estimate of it: and this you have the power to revoke at any moment." The great emperor and philosopher understood the power of expectations and he also knew that they are simply a creation of the mind, subject to change if you have the will and awareness. Our stories and our expectations are joined at the hip. Awareness that our stories and expectations are changing can help us anticipate that our goals and choices will soon be changing. Those insights are extremely valuable. With regard to the subject of investing we turn our focus from stories to expectations because our stories are more closely aligned with the past and our expectations are more closely aligned with the future. And investing is all about what happens next.

Let me make one thing crystal clear. You will not be a successful investor based on how you handle the expected. When everything you buy turns to profits there is little to think about. But when gains inevitably turn to losses, what's your next move? Your success will be entirely dependent on how you manage in these moments, the unexpected moments. I want you to begin to understand how your expectations influence your decision making. If you have a better understanding you will be better prepared to implement the tactics we will discuss later that will help you protect profits and reduce losses.

It is a statement of fact that we pay more attention to that which we expect and retain far more easily information that is consistent with our expectations. What this suggests is that your perspective of reality is heavily biased toward your prior beliefs rather than current experience and observations. Let me offer a concrete example. In 1999 there was a sensational video posted by Daniel J. Simons. Six basketball players, three dressed in white shirts, three in black were asked to move and pass a basketball around on a stage, the viewers were asked to make a silent count of the number of

passes made by the players in white shirts. After some time a man dressed in a gorilla costume walked to the middle of the stage, thumped his chest, then left. The gorilla was on the stage for nine seconds. When the exercise was finished only half of the audience noticed the gorilla. Mr. Simmons concluded that we are missing a lot of what is going on around us and we have no idea we are missing so much. Perhaps an alternative explanation is that our awareness is tied to our expectations and because we did not expect to see a gorilla many were unable to see a gorilla. This offers two very important conclusions. First, we don't see reality, we see the reality we expect to see. Secondly, we think we know what is going on in the world and we hold the belief that others are seeing what we see. Nothing could be further from the truth. William James said, "My experience is what I agree to attend to. Only those items which I notice shape my mind." We all live in very small worlds limited by the expectations through which we interpret our experiences. This limitation becomes increasingly problematic when you learn that many of the expectations you choose to accept may not be of your own creation.

In 1963 research psychologist's Bob Rosenthal and Kermit Fode constructed an unusual experiment. Twelve senior experimental psychology students were assigned the task of teaching common lab rats to run through a maze. Half of the rats were labeled bright maze runners and half the rats dull maze runners, when in fact they were all the same breed of common lab rats. After a week of training, magically the rats randomly labeled bright performed much better than those randomly labeled dull. The conclusion drawn was that the expectations of the students charged with training the animals actually changed the performance of the animals. Later that year Rosenthal took this same experiment into an elementary school where he demonstrated that the expectations of teachers changed the performance of their students. What is most significant about the Rosenthal experiments is the observation that the expectations of others can potentially have the same impact on your behavior, choices and performance as do your own expectations.

We collect expectations with great ease and unfortunately, with little awareness. There is clearly a warm embrace we all feel when we join with the expectations of others. But keep in mind that warmth comes at a cost. Every expectation you collect comes with its own set of blinders that keep you marching along an increasingly narrow path. Just as the growing depth of a rivers' channel increasingly fixes its path, your increasing collection of expectations fixes your intellectual path limiting your ability to process, adapt and change. You wonder why you double down on bad bets or defend the indefensible when confronted with better arguments, think expectations.

This habit of collecting expectations is amplified when we talk about the markets because the markets are about money and money is all about survival. The markets present us with a dynamic that can make the mythical challenge of Adam and Eve look like child's play. In one hand we have complexity, risk and loss and in the other the prospect of life changing wealth, all separated by a few keystrokes on the computer. If there was ever a time when you were likely to attach your self to the expectations of others, this surely would be it. And that is why the herd instinct on Wall Street provides such a powerful and comforting embrace. When things are this dynamic, offering the promise of easy to imagine riches, and the prospect of unknown risks, it clearly feels better to stand with others that are eager to reinforce your opinions. I am not suggesting that when you join the herd that you abandon all your principles or lose your sense of intellectual integrity. Instead, I believe you employ a far more artful device that makes falling in line easier. Your expectations don't stop you from seeing and thinking about your investments, rather they simply help you see what you would rather see. You comfortably accept the specific facts, observations, and logics that support your needs and desires and fail to register or easily dismiss those that would cause you to question your choices. I will be generous and say that although your perceptions include facts, they are driven by selectively chosen facts. And this can be as misleading as no facts at all.

Imagine two men standing at the same corner in Times Square. Think about the infinite amount of stimuli and information that is there for each to process. How do they choose what to consider and what to ignore? They actually don't. Their expectations choose for them. When Bill told his friends he was going to visit Times Square they went on and on describing the great energy and the beauty of the neon lights. As you might imagine, when Bill arrives at the corner all he sees is the beauty of the lights and the incredible performers entertaining people on the streets. Alternatively, when Ted told his friends about the trip they cautioned him about the crime, possibly even sharing a story about an unfortunate acquaintance. Predictably, when Ted arrives at the same corner he can't take his eyes off the sketchy guy standing across the street. The same data was available to both men but their expectations create two entirely different experiences. Both were fact based. But neither was truly factual.

We rely on our expectations to selectively attach ourselves to the data we judge to be relevant to the subject in question. We narrow what we look at and in fact we hold on tight to what we chose to see. If you buy a stock that later turns to losses you endow the price you paid with some magical properties that ensures that the stock will return to your original cost. In effect, you try to make static that which is dynamic in nature. You

wait for the stock to recover when circumstances may have changed. If your losses grow your disposition sours and your attitude unjustifiably changes your view of all your other investments. Don't worry your not alone. We hold on to earnings estimates when prospects change, charts when we never really cared about charts, and comments from famous investment managers without any awareness if they still hold the stock you later purchased. Data points become anchors and goals, processes, and strategies suffer.

Expectations are stubborn beasts. Not only do they frame your perceptions but once held they are very hard to change. These stubborn conclusions are referred to as our mindsets. Mindsets are neither good nor bad, they are simply unavoidable. They are a convenience we rely on to make the complex manageable. But that does not mean they serve us well. There are several characteristics about mindsets that are important to understand. First, they are very quick to form and very resistant to change. They are not well suited for the dynamic world of investing. Second, when we are trying to assimilate new information it first must navigate the rigid construct of our existing mindsets. Lastly, even when new and better information is presented we tend to be resistant to change until the data is overwhelming. In simple parlance, when it is likely too late.

In most cases we get along just fine living in our small worlds of selective facts. It doesn't cost you to carry a biased opinion in a casual conversation with friends who most likely share the same selective truths as you. But get out there in the big bad world of investing where nothing is static and half truths are likely to cost you dearly. The market can be a cruel arbitrator of accepted truth. Making proper compensation for your biases is not an option.

Connecting The Dots:

The markets where securities are traded and priced are nothing more than expectation engines. Every stock in the marketplace is assigned, by the consensus of those that trade and invest in the security, an expectation of its future prospects. Those prospects include all kinds of measurements such as product introductions, earnings, competition, general economics, quality of management, and financial health, that are then distilled into a single price at a particular moment in time. To simplify. All of these predictions ultimately boil down to an expectation of the cash the business will generate in the future. A product isn't a product, it's the sum of cash that product will return to the company over its useful life. Competition isn't competition, it's the impact

competing products will have on the cash a particular product will return to the company. Earnings aren't earnings. They are the cash such earning will generate for the company after all capital commitments are fully considered. It's all about the cash because cash is the real stuff that management can use to invest in the business and return to shareholders. As the company produces results those results will be measured relative to the expectations in the marketplace and if expectations are exceeded the stock will rise and if not the stock will fall. The two basic questions any investor is asked to answer when making an investment are: what are the current expectations embedded in the stock price and are those expectations optimistic, pessimistic or reasonable given all that they know?

Did you ever wonder why a company posted great earnings or introduced a wonderful new product and the stock price declined? The product may have been great and the earnings strong but from the markets' vantage point the price of the stock already included the expectations for a better product and better earnings. Investors aren't looking for the best company or best product they are in search of the greatest disparity between current price and the expected future value of the stock.

There are two basic ways to accomplish such a task. Either you can try to identify a change in the future that you don't believe the market has recognized or you can spot a gap in the current valuation assigned to a company's stock price relative to its current prospects and wait for the markets' expectations to reset. In both cases your mission requires an understanding of expectations. And so I must pose the obvious question: <u>If you are unaware of the expectations that you bring to each investment decision then how prepared are you to evaluate the expectations of the other investors that collectively determine the price of an investment on any given day?</u> Once you are able to better account for the biases, prejudices and limitations you bring to the table the better your chances will be for understanding the expectations and mindsets of others.

The Art of Investing:

Before we get to the details, strategies, principles and choices of sound investing I need to offer some direction that can help you observe, process and act with a greater clarity, discipline, patience, and curiosity. Only then will you be in position to pursue thoughtful goals, execute consistently, and endure. What I have tried to do is make this difficult task approachable. I want to offer a virtue, a tool and a strategy that can help you put the subject of expectations directly in your line of sight. They are not silver bullets. But I believe that these ideas, when considered deeply and applied sincerely,

intersect with many of the subjects that fundamentally impact behavior and compromise sound decision making. If you commit to explore this line of inquiry you have a great chance of becoming aware of the expectations that drive your investment behavior and change your chances for success.

In a seminar class given at the Stanford Business School in 1978 Warren Buffett said, "There is absolutely no correlation between hours worked or intelligence and money management success… There is a tremendous correlation between approach and temperament and investment success." The approach he advocated emphasized discipline and the temperament he valued was patience. **Patience is the virtue** that makes discipline possible. To paraphrase Buffett, "If you have the patience to wait for the right pitch, it is far less difficult to hit the ball." Patience is the quality that enables you to process information at a pace, to a depth, and with a level of intellectual humility that enables the investor to merge conviction with the right capital allocation. Patience enables you to walk away when real understanding is not possible. Patience gives you the strength to decline the possibility of outsized returns when the risks are too large to accept. And patience affords you the time to reflect on a particular investment relative to your unique goals and desires. And please - please don't misconstrue patience for laziness. Nothing can be further from the truth. The willingness to cut corners, to act with haste and chase dreams rather than deliberately build wealth, are the true signs of laziness. Josh Waitzkin, chess master, martial arts champion, and subject of the movie 'Searching for Bobby Fischer' said, "Not only do we have to be good at waiting, we have to love it. Because waiting is not waiting, it is life."

The following truths about our human nature are not subjects of debate. We are all built to act. Most of our senses as well as the biochemicals that course through our veins were placed there to facilitate fast and decisive action. We are pattern seeking beings that often jump to conclusions before the patterns are clear. We are easily bored and our attention spans are shrinking to the point where they are now being measured relative to the attention spans of fish. Compound this toxic brew with the constant barrage of updates and alerts bombarding us from social media and it is clear that the path of least resistance is action. This is a big problem. We act when action is uncalled for. We attribute cause to outcomes when the connection is tenuous. And we readily attach ourselves to patterns that are specious at best. We are perfectly primed for forecasting errors. Without any doubt, the discipline to do nothing is the far more difficult path. Patience is active, because patience takes effort and discipline. Patience is thoughtful because patience is often paired with analysis and investigation. And finally patience is more closely aligned with humility which demands that we always test our

assumptions and challenge our conclusions. My best advice is: do less, read more, challenge your assumptions, and learn to enjoy the wait. It will definitely be more profitable and you may even live longer. But I warn you, this is very hard to do.

Active Listening (AL) is the tool that I want you to consider. It is extraordinarily easy to explain, difficult to master, and infinitely broad in its applications and implications. AL is a technique for listening in which the listener listens to another person with the singular intention of truly understanding what the other person is trying to say. This simple objective has everything to do with managing expectations. The human brain has evolved to recognize patterns more than any other single attribute. We are not great at processing logic, remembering facts, or even making calculations. But when it comes to pattern recognition we operate like a sophisticated massively parallel computing machine. It is perhaps our greatest core competency.

This skill comes with both advantages as well as some notable disadvantages. When we listen to another person we don't patiently wait and focus on what they have to say. Instead, we listen until we believe we have gathered enough information to be able to predict what is left to be said. From that point forward we stop listening and turn our energy toward constructing a clever response. **We don't listen to listen, we listen to act.** There is sound logic behind this uniquely human behavior. Thinking consumes a lot of energy and listening demands that we think. Therefore, if we can predict what is going to be said we can shut down thought and preserve our precious fuel. We listen, in the broadest sense of the meaning, to protect ourselves. The sooner we can guess what comes next the faster we can react, and in theory keep ourselves safe. And we listen, or more accurately participate in conversation, to gain the favor of others, build our networks, and grow our strength and influence. We instinctively believe that the faster we can demonstrate comprehension and offer a clever response the more attractive we will appear in the eyes of others. It is not unreasonable to believe that conversation is just another medium for advancing our self interests. The problem is, human beings are so anxious to leap to conclusions that our predictions tend to be rather inaccurate. We seem to be overly geared to speed and action at the expense of depth and accuracy. Have you ever watched two high level chess players studying their next move? That's not us.

Kevin Sharer, former Chairman and CEO of Amgen said, "My conversations were all about some concept of intellectual winning and I'm going to prove I'm smarter than you." In this regard he is not alone. We all participate in this form of competitive dialogue. We jump to conclusions because we enter every conversation with expectations about both the speaker and the subject matter and as soon as we can align

what we expected with what was said, we stop listening and turn our attention to scoring points. Breaking this pattern does not require that you stop your brain from generating expectations, that won't happen. Your goal is simply to become aware and when that voice in your head begins to talk, redirect your attention back to the speaker.

AL isn't just a tool for learning to listen to others, it is also a tool to help you learn how to listen to your self. If you can apply the patience and attention you use when actively listening to others inward, you give your self a better chance of understanding the triggers that catalyze emotion and change behavior. We are fairly transparent beings. We often declare out loud our expectations using phrases such as, I expect, I bet, I hope, I believe, I think and I imagine. If you can become more aware of what you are expecting, and possibly challenge those expectations, then perhaps the unexpected will become less challenging.

If you are not listening to the sound of your voice then listen to the voice in your head using the very same words and expressing the same intentions. And if the sound of your public or private voice is not loud enough then all you have to do is pay attention to the changes coursing through your body. When the unexpected begins to reveal itself your heart beats faster, your skin tingles, your muscles tense, you get hotter, a bit more agitated, your mind moves faster, you may raise your voice and even scream just to release some steam. The interesting thing about risk, the possibility or probability of the unexpected, is that you feel it. If you can develop the ability to actively listen to what you are feeling, and then pause to ask "What am I expecting" and "Why am I expecting that," you put your self in position to deescalate the situation and make better decisions. Your body keeps score and you can take advantage by actively listening.

Awareness of language, feelings and even the voice in your head can alert you to moments when things are beginning to drift in an unexpected direction. And if you can simply acknowledge what you hear, see, and feel, you will diffuse the circumstance. If you inquire further you put your self in position to carry on from a position of strength. When you learn to be more aware of your self it becomes increasingly easy to be aware of others. It makes perfect sense, when you lose some measure of control all of your attention is turned inward and all that is happening around you increasingly escapes notice. And so it is logical that if you are less preoccupied with your self then things beyond your self may increasingly come into view.

AL is not the answer. AL is one really interesting tool to begin the journey of living a life with fewer and better curated expectations. Conventional wisdom in the investment business says that investing is half art and half science. I can tell you with great conviction that nothing is further from the truth. We will get to the science of investing

soon enough. But if art refers to all that is not subject to calculation, then from my experiences and observations those things trump science far more than fifty percent of the time. And because the investing problem is unbounded in scope, infinite in complexity and endlessly dynamic we all must develop processes that help us bound the problems, limit the complexity, and allow for adaptability when faced with that which was not foreseeable. These are the moments when emotions overwhelm science and clarity, discipline, and patience are required to steer a steady course. You can be great at the science of investing but if you have not constructed a solid personal foundation to deal with all that is beyond calculation (the unexpected) then your chance of success is greatly diminished. And that is why we began with the subject of expectations. Because expectations occupy prime real estate in that space I classify as the art of investing.

Patience is the virtue, AL is the tool, now for the strategy. This is a big topic and I am going to keep it very simple. You have to learn to create more separation between you and your phone. Your phone is the tool used by others to provoke you to act and be impatient. Your phone is the tool others use to relentlessly push their expectations on to you. The phone is the tool that enables others to distract you, to lose your focus, to shorten your attention span, and make you feel bored. Your phone stifles curiosity because it spoon feeds you exactly what others believe you should be curious about. The phone is where others generate expectations and then trick and taunt you into making them your own. The phone is a direct assault on everything you wish to achieve through patience and AL. **Put down your phone is the strategy.** These three things feed on one another. Distraction, boredom, anxiety, and impatience make listening, learning, and deliberation impossible. And without the thoughtful reflection of your assumptions and a careful examination of the facts and circumstances, successful investing is an untenable proposition. Break out the charts and start trading.

Great expectations would come from stories that resonate in the present rather than stories you reflexively attach your self to from the past. Great expectations would come selectively from others after thoughtful deliberation. And great expectations would be adaptable rather than cast in stone. It would be a worthwhile project to put in writing the values and goals you wish to hold close and then share those thoughts with people you trust. That is a conversation worth having. Then you may begin to understand what you want and why you want it. If that is possible then so is the construction of an investment strategy that really works for you. You will have constructed some boundaries on this boundless problem and that puts you far ahead in the game. Always remember that the more you want the more you must risk and risk changes you down

to your bones. And if you want to keep your head about you when others are losing theirs it may not be best to see capital earmarked for your kids college education or mortgage payments go up in smoke. One piece of advice. Very few things truly matter. And those things that matter, matter far more than you understand. Look deeply, curate carefully, and don’t be afraid to change with time, understanding, and circumstances.

PART II

The Science of Investing

Getting Started:

I made this investment guide for everyone. As my investment career evolved from novice to professional, traditional fund manager to hedge fund manager, and then back to a private investor, my goals changed, my resources changed, my tactics changed, but my passion for performance never changed. I have always liked to compete and for me investing was no different than sports, a puzzle I needed to solve given an objective appraisal of my strengths and weaknesses, as well as the strengths and weaknesses of my opponents. My goal with this guide is to simplify all that I have learned to help you become better competitors in this very serious game with its very serious purpose. Whether you choose to manage your own assets or turn them over to another, I want you to have a better appreciation of what is required to succeed.

I am going to focus on the strategies that work best for me in my current circumstance as an individual investor. I no longer have the resources at my disposal that I once had as an institutional investor. But I have learned that a lack of resources does not necessarily translate into a disadvantage. I had access to the most highly regarded research analysts on Wall Street, I regularly met with CEO's of major companies, and I spoke with trading desks from all the brokerage houses that helped me understand the near term money flows that changed stock prices. But I also learned that far too many analysts were not interested in performance, too many CEO's had agendas different than my own, and too much information was oftentimes a bigger distraction than useful guide. I learned that I prefer fewer resources at my disposal in exchange for a single set of thoughtful performance expectations. <u>I have learned that fewer resources does not necessarily mean less resourceful</u>. And I have learned that I can be more successful today than I was in the past. This is my singular perspective and I hope it inspires you to learn more.

<u>Investing is not about right or wrong, that just happens. Investing is about cultivating a balanced mindset, crafting reasonable goals, and following disciplines that play to your strengths and protect you from your weaknesses</u>. Investing comes at you from a million different directions every single day. <u>Very little of what happens is predictable but how you handle what is thrown at you is predictable</u>. Performance is created when the unexpected visits. If you own companies that are financially strong, selling at attractive prices, run by smart investor oriented managers, then your

investments have a fighting chance in all market conditions. If you are riding the hot stocks ignoring the relationship between fundamental business values and price then best of luck. If you are using leverage and are trying to maximize the moment, your margin for error is slim. However, if you remain vigilant about both risk and reward for each of your investments, if you keep your goals clearly in mind and don't fall pray to goals of others, if you can figure out your wheelhouse and resolve that it is a good place to live, and if you have a growth mindset that wants to learn, then the unexpected is nothing to worry about. The only two questions you need to ask are: "How did I conduct my self?" and "What did I learn?" Investing is about clarity, discipline, patience and curiosity. Putting that all together leads to good decisions, sound behavior, and a sense of satisfaction with your efforts. Developing such a process and disposition will help you with everything you do.

Just One Thing:

Investing is a boundless problem. The scope of what you don't know is far bigger than what you do know and the way you deal with the unknown will have a lot to do with how things turn out. An investor can rationalize complexity by buying a low cost index fund that is representative of a big portion of the market like the S&P 500. This has been a terrific strategy since they became popular in the 1980's followed by ETF's in the early 1990's. But don't mistake a broad index for risk aversion. All the large funds and ETF's are by definition diversified products. As such they tend to reflect general market conditions and performance. But market conditions don't necessarily equate with profits and performance. We are in a most unusual time. The largest traditional sector for investment dollars is the bond market, but the governments' of the world have decided that the bond market is no longer a rational place for investor dollars. Average worldwide yields for quality securities have tumbled well below 1%. For most investors this means that the primary source for safe returns is closed for the foreseeable future. As a result, if you want to generate returns on your wealth you better get acquainted with risk taking, because risky assets are all that remains. Buckle up.

I am not suggesting that you shouldn't buy an index fund. I have invested clients assets in these vehicles since the early 1990's. I am saying, don't confuse indexing with risk reduction, because if you bought an index and the markets they mirrored declined in value for the next two years I would not be of the opinion that you protected your self from risk. The only people that shelter themselves from risk with any large diversified investment product are those who manage them for a living. It was your

choice and they delivered as promised. But that doesn't necessarily put money in your pockets. Over the past 40 years these products have generally outperformed most actively managed offerings when costs and taxes are considered. But be aware, these are by no means normal times. And just remember, everyone who speaks publicly about investing and investments has never seen anything like the investment world we now live in. All of us need to invest but we better do it thoughtfully and carefully because none of us knows what comes next.

Whether or not you choose to invest in these large diversified products is not the most important decision. The important decision is, what portion of your investible assets do you choose to invest in them. Capital allocation is the number one tool for managing risk and capitalizing on potential rewards. It is the most important decision you will make in solving the investment problem. Capital allocation is how you compensate for the known and the unknown. Counting the number of winning and losing stocks will not help you understand how you are doing. Counting winning dollars versus losing dollars will give you the answer. The job of a good investor is to align the most capital with securities offering the most attractive risk/reward ratios and the least amount with those securities offering less attractive ratios. Creating a rational structure for executing this allocation is our next task.

Knowing:

Wise investors look down before they look up. Understanding risk is far more important than understanding reward. Psychological studies have proven that investors regret loss over two times as much as they value similar sized gains. The importance of this fact should not be under estimated because the only thing you bring to the table is the stuff between your ears. If past losses impact future decisions then you really don't have a chance. Another important reason why risk should occupy more of your attention than gain is the mathematics of investment returns. Markets may act irrationally but math does not. For example, one years loss of 50% can wipe out 9 consecutive years of 8% annual gains. In the last 48 years there have been four times that major market indexes have declined 50% or more. None of us are exempt from the risk of large losses. Large losses change your attitude and preferences for stock selection and capital allocation. In general there are two directions you can go psychologically after taking a big financial hit and both are bad. When you operate with balance and you are not playing from behind your chances of success skyrocket. If you stay committed to measuring risk before considering potential rewards your long term

portfolio returns will pleasantly surprise.

In my investment experience, there are a million things that can go wrong all the time. However, few are worthy of your effort to predict. Fortunately, when markets decline there are two things that can help an investor weather the storm and they are both somewhat predictable. The first thing you must learn to follow is the cash and cash generating capabilities of a company and the second thing, which is the more important of the two, is you must find businesses run by managers you can trust.

The basic financial exercise challenges an investor to analyze a company's ability to generate cash. First the investor must clearly understand the dollars required to run the business efficiently and effectively for the foreseeable future. If the business is likely to generate cash beyond its needs the investor can then speculate how the management team may choose to deploy those excess dollars to maximize investor wealth. The analysis requires a thoughtful appraisal of current financial conditions and a forecast of future performance. Those figures are assigned different values based on assessments of risk. And the number one risk is time. The shorter the forecast period, the more accurate the forecast is likely to be, and therefore the more value assigned. Eventually the present value of all the future cash streams are measured against all the debt holder obligations and the number of stock holders who are entitled to share in the cash. Understanding the cash needs versus cash generation per share relative to the price of a stock is the most reliable measure of stock price value. The manner in which the company chooses to save, spend, invest, and return cash to shareholders will have a lot to do with how the stock performs in good times and bad. Turning you into sophisticated financial analysts is not my purpose. There are many resources available to help you along that path if you so desire. My interest is to help you find a practical path to reaching roughly similar answers..

One thought I want you to keep front of mind. As a shareholder you are only interested in your per share ownership of the wealth. The more people that share in the wealth the lesser is your opportunity for gain. A rising share count is the most predictable path to shareholder wealth destruction. Be very mindful of a company's willingness to issue shares to finance their needs and wants. Poor custodianship of shareholder capital is an absolute deal breaker. This job is too hard to waste your energy on companies that don't fully embrace this fundamental truth.

I am not advocating one style of investing over another. Roy Neuberger once told me,"There are a million ways to make money. The only way that does not work is the jack of all trades." Find a style and stick with it. I believe this to be true. But regardless of style, I do believe every investor must be able to measure and monitor risk using

methodologies that are somewhat consistent and reliable over time. Roy was a stock trader. I am a long term fundamental investor, a style that I believe to be much more suitable for part-time investors. From the perspective of a long term investor, I believe that measuring and monitoring free cash flow is the most reliable way to track risk.

Every business must ultimately measure up against this free cash flow calculus, but there is a catch. In most cases this calculus is dominated by prediction, and more often than not prediction is a matter of art not science. Although financial analysis is wrapped in the warm embrace of math, don't be fooled. That math is supported by some very un-mathematical guesstimates. If you are a growth investor you generally invest in companies trading at high multiples, to defend these multiples with free cash flow estimates you must make a lot of assumptions and predict far in the future and that is very risky. Alternatively, if you are a value investor, and you purchase a money center bank you must explain to me how you value hundreds of business lines and thousands of different financial products, supporting hundreds of thousands of individual and corporate loans across all industries placed all over the world, leveraged with financial instruments that are often too complex to definitively measure, that are syndicated to other financial institutions with equally complex financial structures. Banks may sell at low valuations but I challenge anyone to tell me what they are worth. Recent decades have proven that estimates of true bank worth are wildly overstated when inevitably the ___ hits the fan. Every business is unique and every strategy comes with its own challenges.

Value, intrinsic value, book value, worth are matters of perspective. Beauty lies in the eyes of the beholder and a disproportionate amount of that which is claimed to be of value is predicated on forecasts that are subject to the bias and flaws of the beholders eyes. The problem is really complicated, but failing to meet the challenge of calculating economic worth puts the investor at risk of loss when times get tough. I have a few suggestions that can help you turn this very difficult research exercise into one that is manageable and potentially profitable for the individual investor.

I imagine the idea that an individual investor can successfully compete with professional investors is hard to believe. But in fact you can. You have more real advantages than you might be willing to believe. One powerful source of advantage is expectations. We spoke extensively about the importance of rational and reasonable expectations. We referenced the advantages of putting boundaries on this boundless problem. Well reasonable and rational expectations are not something Wall Street operators have for themselves nor are they found in abundance with the wealthy and powerful clients that pay for their services. This creates a culture that is exceedingly

short term results oriented. Unfortunately, short term and results are two objectives that are not natural allies. This very unhealthy friction between manager and client oozes through every pore of Wall Street's anatomy. This offers the individual a significant advantage if they have learned to turn expectations into an advantage.

People that actually manage client capital are under constant pressure to perform. There are so many alternatives and so many clients chasing returns that the center of gravity naturally draws the vast majority of participants toward the short term. Greed is a powerful elixir. And my observations suggest that the more you have the more you seem to want and believe you deserve. This culture permeates the entire corporate food chain with rising pressure and consequences as you move down the pecking order. The analysts that are paid to support the portfolio managers that attend to client demands work with little room for error. In response, they spend an inordinate amount of energy on the short term where forecasts are generally subject to smaller risks. By doing so, they tend to sidestep the riskier venture of making the longer term predictions that ultimately drive business value and stock prices.

Unfortunately, predictions, forecasts and assumptions are the part of the investing exercise that present the greatest challenges. And although individual investors are not obliged to the unforgiving judgements of clients and portfolio managers, they are not immunized from the forecasting errors inherent in the process. So how do you make this task more manageable and predictable for your purposes? You begin by keeping your focus on the long term where the intellectual landscape is less crowded. You further improve your chances by unburdening your self from the obligation of being specifically correct, instead, you are looking for businesses generally headed in the right direction. In one way or another stock prices follow profits. Rising rates of profits drive prices higher and declining rates of profits drive prices lower. However, if trends are favorable, even when earnings miss estimates the penalties are generally far less penal. When an investor chases short term profit they are really just playing a game because short term profits have very little to do with long term worth. To judge worth investors need to examine long term trends.

In my opinion, the most reliable source of information to help you judge business trends and company worth is the companies themselves. No one knows more about a particular business, its competitors, prospects, obligations, and intentions than the management team. And if you suspect they don't your research ends there. But if you can identify a business that interests you and is managed by capable and qualified executives who are fully transparent, prudent custodians of capital, whose interests are clearly aligned with shareholders, and whose stock price is trading at a reasonable

relationship to free cash, then your prospects are bright. Keep in mind most of life involves compromise. With every investment you will have to make your fair share. It is your job to choose your compromises wisely and to monitor them closely. **But one compromise you must never make is trust in management, because they hold all the cards.** That does not necessarily mean they have all the answers. They are subject to the same forecasting errors as the rest of us. They simply know more and have access to far greater resources. But that does not mean we turn over our independence. They must constantly earn your trust. Misplaced trust is a dangerous thing. And the list of examples from Bernie Ebbers to Bernie Madoff is evidence enough that anyone is capable of anything. It is your job to monitor carefully and in the best case dispassionately. Reading all that is published and listening to all that is said by the management team is the best route to identifying trends early. And the longer you follow a company the better you are at interpreting their messaging. Josh Waitzkin is right when he says "Depth of knowledge beats breadth of knowledge everyday."

In our new era of regulatory disclosure a company's website should tell you a great deal of what you need to know. It is in the company's best interest to help shareholders understand their business and become thoughtful and loyal shareholders. Informed shareholders can be a powerful ally to a well managed public company, just ask Amazon. Any indication that they are unaware of this fact is cause for concern. I like to begin by reading and listening to all the quarterly earnings releases for the past two years. Understanding how a company communicates, its priorities, its disclosure and openness to questions, the accuracy of its forecasts, and the manner in which it addresses failure are essential measures for building trust.

If they think their stock is cheap I want them to explain why. I want to see executives buy stock rather than receive compensation awards that don't connect them to the same risks shareholders accept. I am not looking for perfection, in 40 years of investing I have never found it. But I am looking for a powerful ally that is willing to share their vision of what comes next, is capable of adapting skillfully when circumstances change, and makes smart decisions with their capital. And I need to see these results translate into financial gain and stock price appreciation. Management needs to be effective communicators to their customers and the investing public. Valuation, the multiple of earnings assigned to stocks by investors, is an important part of the art of investing as well as the art of running a public business. Management teams that are good at the art of storytelling can create valuation advantages that translate into rich sources of capital that drive business prospects. If they don't have these skills, they should be willing to buy them. And if they don't understand that this is important, then I think it is fair to

question their judgement.

I often follow companies for years before I buy them. They may have interesting products and great management teams but the stock price is wrong, so I wait. I may follow companies because they compete with my investments or because of trends in the economy or consumer behavior that interests me. It is not necessary for me to invest capital in these thoughts, nor does it occupy a lot of my time, it simply helps me build my knowledge base and hopefully speeds the process when circumstances and prices change. When a topic is interesting it is easy to maintain your attention and focus. Anything that makes research easy will inevitably reduce risk. I prefer long term investing because it seems logical that my significant investments of time, energy, and dollars should correspond to longer holding periods and my expectations for outsized rewards. This does not mean that I don't trade stocks, study charts, and on occasion speculate. But those things are done with far less capital and with far more rigid disciplines regarding both gain and loss. It is useful when trying to visualize risk to translate percentages into absolute dollars. It helps make the entire exercise far more personal.

Always remember capital allocation is everything. It is the job. It is your final appraisal of risk and your willingness to pursue reward. When risk, reward and valuation are somewhat understandable and attractive you invest more and when compromises are required you invest less. Simple enough. The far more challenging appraisal involves understanding the difference between what you believe you know versus what you need to know. This is where **experience** plays a critical role. With that in mind start slowly and allocate conservatively. It is far better to make less with your successes than to lose more with your failures. Capital allocation will be the reason why you remain calm when others are not. And it is the reason you will stay focused on your goals rather than chase the flavor of the moment. **It is the single most powerful tool separating success from failure**.

Putting the pieces together:

At this point in our dialogue I think it would be useful to share a real-time example. Before we start I must make one thing crystal clear: THIS IS NOT AN INVESTMENT RECOMMENDATION OR ADVICE. I chose a current example, with personal capital at risk in the market, because I believe it would be intellectually dishonest to examine a hypothetical or older thought that offers the writer a level of clarity and perspective that is unavailable to the investor in the real world. Investing is not an academic exercise.

Therefore, to exclude the prospect of loss would not serve the reader well. The investment I am going to share is still in its infancy. The outcome is still far from known. The intention of this example is to give the reader a perspective on process rather than a recitation of the facts and figures that support my work and decisions.

In May 2021 a friend brought to my attention an interesting potential investment posted on a public investment website. The following initial observations were sufficient for me to start a small investment in Gannett Co (stock symbol: GCI):

(1) Many years ago I invested in Gannett. It is a powerful national brand anchored by USA Today and approximately 250 local newspapers in the US and UK. Real brands are rare and wildly expensive to build. The prospect of aligning these assets with new management, strategies, and technology was a compelling prospect.

(2) In November of 2019 the assets were acquired by a management team that I knew and respected. Following the takeover the new chairman made a large personal investment in the shares at prices considerably higher than current prices.

(3) A quick review of publicly available sources informed me that Wall Street analysts had largely abandoned the stock. Only three analysts covered the stock and all three held negative opinions of GCI because of their shared conventional view that traditional publishing was dead. A lack of Wall Street support is not necessarily a bad thing. If everyone is expecting the worst and the worst does not happen a stock can rise substantially. A wise investor should take comfort in low hurdles. They are very easy to jump over.

(4) The company's website highlighted the following accomplishments in the 18 months prior to my investment: (A) total outstanding debt was reduced from $1.8 billion to $1.4 billion; (B) the rate of interest on the remaining debt was reduced by almost 50%; (C) annual operating cost were cut by over $300 million; (D) longterm liabilities were restructured; (E) non-core assets were sold for significant sums; and (E) the digital rollout was ahead of schedule. Management was working quickly to return this company to a path of profitable growth.

In the following weeks I read every document submitted to the SEC and published for investors since the takeover. I listened to all public conference calls, spoke with various members of the management team, exchanged notes with other informed investors, and read numerous trade and industry articles germane to Gannett's businesses. My research was supportive of a larger investment. With this work completed I want to share some important observations.

The basic tension that an investor is challenged to resolve at this stage in the company's development is the trajectory of revenue growth or decline for the company

as its traditional print businesses shrink and digital businesses grow. The rate of decline of the print businesses is the number one risk the GCI investor must monitor. My optimism stems from my fundamentally derived belief that the digital businesses that account for approximately one third of 2021 revenues, will grow in excess of 20% and the remaining traditional businesses will decline at a rate of less than 10%, for the foreseeable future.

Underlying these assumption is my view that USA Today and the approximately 250 local newspapers they own represent one of the largest big data platforms in the media business. Big data is one of the most powerful trends in business today and I believe Gannett will benefit from this trend far beyond the expectations of Wall Street. Gannett has a digital audience of 179 million unique monthly page views per month. They have over 600 quality journalists creating unique content for their loyal local audiences as well as the only national media product (USA Today) that remains to its core both neutral and balanced. A very rare bird in our highly polarized country. Big data, unique content, and a broad platform give Gannett the ability to modulate product design, content, and marketing strategies on a daily basis to maximize sales and profits. This incredible agility resonates through every single business line in their digital portfolio, and will also work to the advantage of their print businesses.

The idea of big data, whether we are talking Google, Facebook, or Amazon, is about having enough information about a potential customer's preferences and intentions to dynamically create products at a cost and price point that maximizes business outcomes. Every single day the producers of a digital newspaper have access to your wants, desires, and interests. Are you clicking on stories about football or basketball, are you looking at betting odds, advertisements for new or used cars, reading recipes, buying tickets to a concert, or exploring travel options? Everything you read reveals something intellectually or emotionally salient about your intentions.

Using this data to continuously adjust content, explore and prioritize new offers, and experiment with different pricing strategies helps Gannett build products that meet or exceed customer expectations. Users of big data don't have to guess. They already know the answers the customers are seeking. And they get to adjust those answers daily as customers provide incremental information. In the traditional publishing model providers knew little beyond a customer's address. A digital platform is synonymous with low cost and dynamic change. In the case of Gannett the fixed costs are the journalists and the cost of technology. The production and distribution costs that slowed change and dominated costs are essentially nonexistent. This gives management options that the publishing industry could never have previously imagined. One could

argue that a publisher, in this new technology driven world, with a recognized brand, large audience, and unique content, is not only leaving the dark ages but entering a golden age of possibilities.

Data and analytics will not only accelerate growth, offering more products that customers desire, but will also help slow the attrition of Gannett's 2.4 million print subscribers. If a a subscriber spends $5.00 per month on a daily print copy of USA Today and Gannett wants to protect that subscription from attrition they could offer the print subscriber the same product in digital form for a lower price to the subscriber and a lower cost to Gannett. Alternatively, they could offer the USA Today subscriber a digital subscription for their local paper for an additional cost of $1.00 per month, saving the customer $4.00 per month on the local subscription standalone price, while increasing the subscribers total spend to $6.00 per month. At first this may not appear ideal for Gannett, but you must consider that the print edition of USA Today includes a lot of national advertising that is priced based of circulation size and the digital version of the local newspaper they offered the subscriber essentially costs Gannett nothing to produce. The math and strategies that optimizes outcomes for Gannett are fluid. The important point to appreciate is the versatility the platform offers the company to optimize short and long term outcomes. Mass customization presents the sophisticated user of big data with unprecedented opportunities. And the Gannett franchise generates big data.

What is truly exciting for the Gannett shareholder is the understanding that the product rollout has just begun. This suggests that the power of data analytics for this company is in its infancy. Dozens of new products will translate into infinite amounts of new information at the company's disposal to leverage journalistic talent, increase customer reach, and increase customer satisfaction. Digital sports packages, cookbooks, crossword puzzles, reviewed products, restaurant guides, ticket services, and travel booking services are just the beginning. The list is only limited by the creativity of management and the size and quality of the journalists. Neither of which, in my opinion, will be a gating factor. If you think of Amazon as the marketplace for goods, it may one day be possible to think of the Gannett platform as the marketplace for experiences and services. As the customers and products grow in number so will the data that can then be analyzed to increase customer interest, customer loyalty, and the prices Gannett can charge. A virtuous cycle that increases advantage and profits.

This value proposition that marries data with customized products benefits the advertising customers as well as the customers of Gannett's digital marketing services platform (DMS). DMS is Gannett's largest digital business. The DMS business already

generates large recurring revenue streams for over 15,000 customers while boasting retention rates well in excess of 90%. The DMS platform offers customers the tools, services, and support for all web based and mobile platforms that small businesses require to reach and support their customers. Digital marketing is no longer an option. And returns on investment are very large when executed effectively. Unfortunately, most small businesses suffer because they fail to embrace this truth and adequately invest in this new business paradigm. Gannett is rapidly ramping up its software and service offerings to accelerate penetration of this enormous market opportunity. Their are over 30 million small business in the US and most need help. Gannett's visible presence in over 250 local markets through their local newspapers gives them a large structural advantage over the loose collection of undercapitalized local and web-based players vying for market share. Ironically, this huge business opportunity is structurally too cumbersome for the larger players in this business to target. I believe this business is overlooked and has incredible potential for Gannett. The following is a summary of my investment thesis:

(1) I have a very different view of the future of this important brand in this changing industry. Wall Street analysts see this company near its end, I see it at its beginning. I believe that new management, technology investments, and significant free cash flow will propel this stock to higher growth rates and greater profits than we have seen in the recent past.

(2) In the year 2022 I estimate the company will generate over $200 million of free cash flow. In the years that follow I expect free cash flow to continue to grow as the conversion from print to digital accelerates and new software and services at DMS gain traction. With an enterprise value (the sum of all debt + stock market value - cash) of less than $2 billion, a shareholder of GCI can expect a 10% free cash flow return in the near term. Much higher returns are possible in the later years as obligations (debt and equity) are retired and the company continues to invest without the need for additional capital. THIS STOCK IS AN OUTSTANDING VALUE.

(3) If my analysis proves generally correct and my appraisal of management accurate, then this business will soon enter a period of sustained fundamental acceleration. In my experience nothing is more important. Managing a business with the wind in your sails makes decision making simpler and mistakes easier to navigate. I believe the transition to a period of sustainable revenue and profit growth will happen in the next 18 to 24 months. WHEN THIS IS EMBRACED BY INVESTORS I EXPECT VALUATIONS FOR THIS BUSINESSS TO RISE SUBSTANTIALLY. It is my job to anticipate this transition and invest when others are unwilling.

(4) This is fundamentally a data analytics business. It gains advantage with scale. This means, if management executes thoughtfully, THIS BUSINESS IS DURABLE AND ITS COMPETITIVE ADVANTAGES SUSTAINABLE. This grants me the privilege of patience, knowing mistakes will be made and the unexpected will present challenges from time to time.

(5) THE INTERESTS OF MANAGEMENT ARE ALIGNED WITH SHAREHOLDERS.

All of the information and observations described above are subject to change. And this is as it should be. The only truth about the stock market is that change is constant. Your only viable response to this condition is constant research and the willingness to adapt as fundamentals, market conditions, valuation, and personal goals change. Any other posture is sure to fail. At this time, these are my working assumptions and expectations for my investment in GCI. I do not believe there is a sound way to invest in this company, or in any other you might chose, without doing your own work. I never said investing was easy.

Not Knowing:

Research comes with a unique set of problems. Intrinsic to all research are forecasts, and all of us tend to bias our forecasts positively when we own a security or wish to buy one. The truly dispassionate investor is hard to find. Investors tend to hold on to forecasts they like and have difficulty processing information that undermines their ideas. If you have a lot of money invested in the markets you tend to listen more carefully to bullish commentators and dismiss the bears with ease. Quite simply, the more you want something to be true the more likely you are to believe it so. There are countless well written books on this subject. The only thing that merits consideration for our purposes is that we concede these statements to be true and build systems that protects us from ourselves.

Forecasting bias is just the tip of the iceberg. That which the typical investor knows is dwarfed by that which they do not know. A mentor and great investor once told me, "50% of a stocks move is attributable to the market, 30% to the industry (a bank stock is part of the financial industry), and 20% to the stock itself." Again experience has taught me that he is far closer to the truth than not. One of the reasons I have chosen an investment strategy that focuses on individual stock selection is because the complexity of a problem is generally proportional to the scale of the problem. An individual

company is a more manageable undertaking than is an industry or the market as a whole. With increasing complexity comes increasing forecasting errors. But that does not immunize me from industry and market risks. In fact, recent market developments are making this problem more pronounced. ETF's are relatively new products that are capturing an enormous amount of investor capital. They offer an easy way for investors to make industry and market bets. Unfortunately the ease of the bet seems to be disconnected from the underlying complexity of the bet and that is dangerous.

The health of a market should fundamentally mirror the health of the general economy. And the greatest source for general economic knowledge comes from the businesses that drive the economy. When investors are close to companies their business intelligence is more reliable and their understanding of true business worth is far more secure. This fundamental connection invariably leads to more rational investor behavior. As ETF's, indexes, and algorithms have exploded in popularity investors have increasingly lost their connection to this valuable source of knowledge. This is very dangerous. As a result, baskets of stocks are increasingly traded like commodities and individual stock volatility has risen dramatically. It is not unreasonable to speculate that short and intermediate term stock price movements will increasingly be detached from core investment truths. Fortunately, all is not lost. This new investment landscape may offer smart and disciplined individual investors more frequent opportunities to both buy and sell securities whose stock prices do not accurately reflect business reality. Markets are going to be extremely challenging in the future. **That is okay, because we are not trying to build the best stock or best strategy we are trying to build the best you. Your discipline, patience, clarity and curiosity are the qualities that will ensure durable returns.**

To cope with the new era of elevated volatility you need to incorporate disciplines that help you manage your decisions when you feel you are in control, and more importantly, when you feel you are not. Let's assume you have $200,000 to invest. If you are relatively new to investing I would recommend you personally invest no more than 50% of your capital and invest the other half in an indexed product or actively managed mutual fund. I generally believe that when all costs and taxes are considered ETF index funds are the best choice for passive investing. The reasoning for my view is fairly simple. If an actively managed fund does well it inevitably attracts more assets. As assets grow the fund has no choice but to become increasingly diversified. And with increasing diversification portfolio performance inevitably tends toward the mean (the average market return). Average results minus relatively higher fees, costs, and taxes lead to suboptimal performance for the individual investor. But there is an exception to

this rule that may offer you an advantage.

Let me share a trick used by people that enjoy investing their own money but have too much to manage themselves, aka rich people. If you give some of your assets to an active portfolio manager who has a record of success you generally get periodic views of their portfolio holdings. There are ways to do this without a direct investment but sometimes the disclosure from a fund investment offers more than just a simple list. Periodically fund managers may send fund holders updates that include more revealing summaries of their favorite holdings and their views on the market. This can provide you with an effective screen for potential new investments while simultaneously offering you a better understanding of those who manage your money, for better or worse. If this sounds interesting then look for managers or management companies that communicate with their investors and also share a process, style, or holdings list that suit your interests.

Now I want to share with you the specific disciplines I have used to protect my capital and keep my head in the game. These disciplines have worked for me. They suit my disposition for acceptable capital risk as well as the promise of satisfying rewards. **Use them as a guide to build disciplines that suit your unique investment disposition:**

(1) I never use leverage (borrowed funds). This business is hard enough, and the underlying volatility is more than sufficient to drive very attractive returns. It is important for you to understand that the entire financial system, including many of it's most powerful players, are using unprecedented levels of leverage and more complex derivative structures than ever before. This has connected small changes in stock prices and core economic variables with wildly overstated market moves. The system is more fragile than it has ever been. And the expectations for returns have rarely been greater. Proceed with caution. Things are far less predictable than they appear to be.

(2) I prefer a concentrated number of positions. I generally find it hard to collect a large number of interesting investments that are consistent with my disciplines. I also like to have the feeling that there is a lot riding on each decision. Risk is not a bad thing. A reasonable level of risk heightens your focus, attention, and endurance. It creates a sense of urgency that drives my appetite for research. Surprisingly, it also has a calming effect because in my opinion, the best way to truly mitigate risk is through understanding. Risk is an ally that helps me make better choices, as well as choices that I feel better about regardless of outcome. **Most look to avoid risk, I look to lean into risk.**

(3) The following numbers apply to your total funds invested, regardless, if you choose to invest some of your assets with a professional investor or invest all the funds your self. I don't allow any position, measured by cost, to exceed 7.5% of total capital. In this example I am investing $200,000 of total capital, therefore no position should cost more than $15,000. In general, I buy my positions slowly in an effort to marry better prices with more knowledge. I never allow a position to exceed 15% of total portfolio value. If I was fortunate enough to invest in a big winner I cap the position size at $30,000. Once reached I force myself to sell enough shares to reduce the position size back to $15,000 and then treat the position as new, with the current price as the new cost. I always measure from beginning year capital. For the current year all measures are based on $200,000. And years are always calendar years to account for tax considerations. One of the reasons I cap appreciation is because when positions grow too large they become the portfolio. I become overly preoccupied and miss new opportunities.

(4) Maximum loss permitted for a single position is 20% of a full cost position. In our example, a full position at cost is $15,000, therefore maximum dollar loss is limited to $3,000. If I take a full position, when the stock is down 20% I must sell the entire position. But if I chose to take less than a full position, I give myself the latitude to hold a position that is down over 20%. If a position is sold for a loss, those lost dollars are subtracted from the new maximum position size if I choose to invest in that security again in the same calendar year. Additionally, any position that is sold for a loss can not be revisited for one month. I don't want to compound errors without giving myself the time to reflect on what might have gone wrong. Lastly, if I lose money in the same position in a single calendar year I can not buy it again that calendar year. Something needs to be in place to let me know that I have this one wrong. I try to put myself in a position where no single loser can ruin my year but a single winner can make it.

(5) If I choose to manage my money through indexes or funds these rules do not apply. Passive investing is not about about timing and protection. If I choose an active manager I review their progress at the end of each year. Promises in general are vague. But I don't invest without some reasonable expectations regarding style, discipline and performance.

(6) At the end of each calendar year market values become the new cost values for all positions. I think in terms of 12 month time frames and I make an effort to create performance every year.

General Observations:

(1) Goal Setting: You must first be aware of the importance of compounding interest. Compound interest refers to the mathematical fact that relatively small differences in annual returns can have a very large impact on your final value over long periods of time. For example: If you deposited $1,000 in an investment that grew 5% per year for 10 years, at the end of year 10 you would have $1,629. If it grew at 7% you would have $1,967 and at 10% then $2,593. If you contribute an additional $10 each month the numbers would grow to $3,138, $3,625, and $4,506 if interest is compounded annually. In each case, the numbers grow very large if the performance is consistently positive and the time frame expands. Reflect on these numbers before you set goals. Think in terms of absolute needs and wants. You may not need to shoot for the stars to live a life that will make you happy. Remember, the bigger your goals the more risk you must accept and the harder it is to avoid losses. **Your goals change the nature of the investment problem you are trying to solve. The more reasonable you are the better your chance of actually getting what you need and want.**

(2) I definitely emphasize loss avoidance over chasing gains. My most obvious attribute is patience and I am generally willing to wait for outsized opportunities. I find it hard to identify small advantages. I am looking for really big gaps between price and fundamental business developments and I am willing to hold positions for many years.

(3) I tend to look at smaller stocks that large investors ignore. This makes it easier for me to create a differentiated point of view. It has been my experience that small company management team's are more entrepreneurial by nature and are willing to invest their personal capital along side my own. And the added volatility of small market cap investing provides me with very attractive opportunities when prices are discarded in general market declines.

(4) I try to write down my expectations for each stock I own on a single piece of paper. I try to outline my thesis (the story), highlighting the 3-5 greatest opportunities and risks (my expectations). I also record all my position changes and the rationale for those changes. I want a record of my thinking so that I can evaluate my performance from many different vantage points. I want to get better and this offers me a path. There is always so much to learn.

(5) I have a science oriented background and I enjoy chasing speculative stocks that are trying to innovate. These stocks come with the potential of outsized gains as well as outsized losses. They are voracious users of capital so free cash measurements are meaningless. As a result I am very conservative with capital allocations, rarely

exceeding 3% of capital.

(6) I like looking at charts relative to fundamental developments to gauge market expectations. Charts are a tool, not a strategy. Every investor should use every tool at their disposal.

(7) In a financial world starved for income I caution you against chasing dividends. In my experience equity volatility will easily consume dividends paid. If a company generates free cash I would rather smart managers use the cash to the shareholders advantage rather than be obliged to pay it out.

(8) For the past forty eight years, with few exceptions, market timing has been a fools errand and cash has been a real drag on performance. I am not advocating market timing. But I do believe in following a disciplined approach to investing that does not chase stocks when valuations are extended and is willing to sell a stock and sit with cash when the risk versus reward is no longer attractive. I am a bottoms up fundamental investor. I buy when I can identify stocks that make sense and I wait for new ideas that fit my disciplined approach. I do not consider cash a burden and I don't chase marginal (small) returns while I am waiting. I believe the current market environment is very risky and I am quite content sitting on cash rather than taking unnecessary risks chasing incremental returns. The hardest part of marching to your own discipline is getting comfortable with lagging returns when others seem to be enjoying so much success. **In my experience, the harder thing is often the right thing to do.**

(9) Finding ideas is hard work. You need to process a large number before you find those that are suitable for your capital commitments. I wish there was an effective system, but in my opinion there are none. You can screen stocks for all kinds of financial metrics but in my experience those screens are not terribly productive. My only suggestion is read as much as you can and begin to network. You will find that lots of people like to talk about stocks because lots of people like making money. Learn to bring up the subject more often than you might expect to be polite and learn to listen. Just because you talk about a stock does not mean you have to buy it. A conversation is a place to start not finish. I assure you, the longer you do this the easier it becomes. I also must point out that there are a million places to investigate new ideas online. Many of them cost money. Choose wisely. But know this. The value of one good idea typically far exceeds the cost of any individual service. Alternatively, the impact of a bad idea or worse, a market view, would make all the money spent a colossal waste of money.

(10) Capital allocation should dominate all of your decision making. I use it to balance my sense of understanding of a company and my willingness to take risk. I

have generally found that it takes me about a year of following a company before I feel I really know what makes it tick. I still may buy a stock if I believe the company is interesting and the stock price is attractive. I just pace myself until I acquire a sense of confidence. Capital allocation is also a way for me to express my feelings about a market and my goals. Let's say I want to make 5% per year and I have achieved those goals early in the year. I may choose to simply lighten up some of the positions that helped create that performance. Or perhaps I feel the market seems a bit extended, I may sell small portions of my holdings to reduce risk until I feel more confident. Rather than chasing stocks I don't know to participate in a rising market or shelter myself from risk I stay in my wheelhouse increasing and decreasing holding size in securities I understand. Caution, there may be tax consequences. But I like to pay attention to my instincts. This is a simple and sensible approach that is not filled with drama. It keeps me in the game without taking me out of my comfort zone. **Capital allocation is everything.**

One of the truly interesting things about the investing exercise is that it is one of the few things that resembles the complexity of life. Living a good life can be a tough road. There are endless obligations, lives depend on you, and the unexpected is the norm. Everything is always on the line. Investing is no different. The complexity is overwhelming, the skills are hard to develop, the discipline required will challenge your basic instincts, the process can take a lifetime to learn, and the unexpected is the norm. And because we are talking about money, everything is on the line all the time. You need to be thoughtful, emotionally strong, and physically ready to endure. I know this doesn't sound welcoming. **But another perspective can suggest that the investment process is a wonderful training ground for living a better life. Learning to live with less bias, to see without blinders, to stay calm when others are not, to make sound choices, to connect more effectively with others, and most importantly to learn more about your self is an awfully rich education. I would hope this is enough to inspire and sustain your curiosity. And if you choose to make the effort the rewards may be far greater than money. You may actually become a wealthy person.**

Good Luck

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This investment guide is not intended as investment advice. Please consult with a professional advisor before investing.