

As We See It

Given Frank Lawson's recent passing, we have been reflecting on the ethics and timeless wisdom upon which Frank and Ken established our firm. The quarterly As We See It was but one avenue from which they imparted their unique insights to clients and numerous other professionals. In that spirit we are sharing one such piece where Frank and Ken laid out part of their investment process and discipline in early 1990. Their process is as relevant today as when it was written. It stands as another light post to guide our investment process and discipline for clients moving forward.

The Greenhouse Effect

(Originally published April 1990)

Naw! Not the carbon dioxide that is accumulating in the atmosphere and making things hotter down here on earth. We are thinking of a real, honest-to-goodness greenhouse with a glass roof and lots of growing plants—and how it can help illustrate a point about investment portfolios.

At any time during the year, a greenhouse has many plants in various stages of development. In December when the poinsettia's bracts have turned red in time for the Christmas market, tomato seeds may just have been planted so that the starter plants will be ready for spring planting. Later, the flowers for the Thanksgiving table are being started. Planting, growth, and harvest are ongoing and concurrent in the greenhouse.

A similar process takes place in a well-managed portfolio. There are new ideas or *plantings* (last year we added Briggs & Stratton to many of our portfolios), there are stocks that have been held for some time and are still *growing* (M. A. Hanna and Sonat for example), and there are stocks which have reached *maturity* or sell time (such as Goodyear).

The greenhouse analogy—a portfolio at any time has investments in various stages of development—may in part explain something we observed about our various portfolios last year. Many of our newer portfolios did not do as well as our older, established ones. The explanation, we believe, may be likened to the problem of a new greenhouse being started in November. There is no point starting poinsettia plants then because they will not mature in time for December sales, so it starts with plantings that will mature further into the future. Last year some of our older ideas came along very well while our newer ones were in the process of development.

The analogy can be carried too far. Stock investments cannot be counted on to mature for the Christmas selling season as can poinsettias. The holdings in a portfolio move according to their own dynamics. While we cannot plan the timing of how stocks in a portfolio will develop, it has been our experience that a well-diversified portfolio will function much like the greenhouse. As managers of the greenhouse, our challenge is to *harvest* when appropriate and *plant* new issues with promising prospects.

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