NOVEMBER 2018

Resources Management Corp

MARKET COMMENTARY

INVESTING IN VOLATILITY

October proved to be a tumultuous month for both the equity and fixed income markets. The S&P 500 finished down 6.9%, while the Bloomberg Barclays US Aggregate Bond Index finished down 0.8%, for the month. While this feels like a large drop in the context of the current bull market, monthly drops of this magnitude are not at all uncommon throughout history. As such, it is important to recognize that our investment process continues to be business as usual. That being said, volatile times warrant the re-establishment of the core principles that drive our decision-making process as a firm.

At the center of RMC's investment philosophy is a keen focus on the fundamentals of the businesses that underlie the securities we invest in. This means that, rather than spending time focusing on the market movements of a stock, we are constantly evaluating trends in the business, industry and economy to understand how companies will perform over the long term. A track record of consistent earnings, high returns on capital, a strong balance sheet, growth in both revenue and net income and a highly competent management team are all qualities that we seek in our investments. Companies that exhibit these characteristics are far more likely to outperform over the long term as these are the key drivers of value creation in business. Our interest is in how these drivers are going to trend for years into the future, as opposed to just from quarter to quarter or even in an isolated year.

Once the quality of the business is well understood, the other major fact that needs to be established is the appropriate price that should be paid for the stock. While it may seem obvious that valuation would be a deciding factor in any investment decision, lack of discipline when it comes to purchase price is an extremely common occurrence, especially as it relates to good businesses. When a business fits the description given above, it is easy to think that there is not a price that is too high to pay. Price is, however, a critical determinant of the success of an investment, and our focus is on not overpaying for a stock. Purchasing undervalued securities is always our preferred option, but we view purchasing excellent companies at fair prices as more attractive than purchasing fair companies at excellent prices. This approach should allow for strong stock price returns over the long term.

At the end of the day, the goal of investment in stocks is the combined return received from price appreciation and dividend payments. While dividend payments can be reasonably predictable over the short term, stock price movements are not. Rather than attempting to guess something that is unknowable in the near term, our goal is to focus on the major drivers of value creation over the long term and invest when prices are favorable relative to these factors. Over time, we expect that this will produce results that are in line with each client's individual objectives. Market volatility similar to what was experienced in October will occur in public markets from time to time. Rather than viewing price movements like this as something to fear, we see this as both a healthy and normal occurrence that can create opportunities to purchase well run companies at discounts to their intrinsic value.

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