

COMPASS WATCH

MARK S. HALVERSON

CHRISTOPHER C. KELLEY, CFA, CAIA

A quarterly newsletter of Compass Capital Management, Inc.

JAY M. JACKLEY, CIMA

LEIGH E. NIEBUHR

CHARLES M. KELLEY, CFA

MARK A. VITELLI, CFA

Volume 27, Number 4: Winter 2015

TAKING STOCK: A FEW THOUGHTS FOR TIMES LIKE THESE

Just nine months ago, U.S. stock indexes were hitting all-time highs as the bull market was passing its six year anniversary (from the March 2009 lows). Since then, the Federal Reserve has begun raising short-term interest rates, oil has continued its precipitous retreat (from its recent high, oil is down 68%) and emerging markets have teetered as a result of their dependence on higher oil prices and a more robust Chinese economy. In addition, fickle investors are now skeptical of long-term domestic growth opportunities in the current economic environment. No wonder many investors are confused and a bit exhausted.

What the beginning of 2016 has made abundantly clear once again, is that world-changing events are unpredictable. Therefore, one must not base an investment strategy on the ability to predict the future accurately. Market-timing, momentum investing and buying long-term bonds are strategies to avoid for this reason. Successful investing is not dependent on speculating about the future, but in taking advantage of mispriced opportunities in the here and now.

Since the future cannot be predicted with certainty, we believe an investment portfolio should emphasize high-quality, individual stocks and bonds. When the economy does weaken, it is vital to hold companies which will not only survive, but are likely to experience growth when the economy then recovers. A prudent investor should assume that volatility is likely to be an integral part of any long-term investment time horizon.

Here are a few things the Compass investment team have been thinking about and doing during these recent volatile times:

1. **Investment Policy Reviews:** Each account we manage has a written Investment Policy Statement (IPS), which is included in the report we send to clients after the end of each calendar quarter. Recent events support our strategy of reviewing these policy statements to be sure they continue to reflect current client return expectations, risk tolerances and income needs.
2. **Stocks:** We are a growth manager, but growth at a **sensible** price, not growth at any price. We view successful stock management as patiently and carefully selecting high-quality companies which exhibit sensible growth and risk characteristics for the long-term, rather than rotating rapidly into styles and sectors of which may be momentarily in fashion. For example, in 2015, the “FANG” stocks—Facebook, Amazon, Netflix & Google—combined to contribute over 3% to the total return of the entire S&P 500 Index return of 1.38% (therefore, on average, the remaining stocks were *negative* 1.62%)!
3. **Bonds:** High-quality bonds have been terrific performers as market volatility has picked up. Some investors are now worried that interest rates may continue rising and drive current bond prices lower. At Compass, we have been following a single discipline successfully since 1988. We construct our bond portfolios by equally-weighting our maturities 1-10 years. We “ladder” to mitigate risk and control volatility within the portfolio. **The primary goal of a laddered bond portfolio is to achieve a total return over various interest rate cycles similar to that of a longer-term bond, but with less market risk.** At Compass, managing fixed income portfolios (or as part of a larger balanced portfolio) is a significant piece of our total assets under management (approximately 30%). We also have the flexibility to customize our tax-exempt portfolios (i.e. purchasing state specific or national bonds depending if you are a Minnesota or California resident, for example).

It is true that the investment landscape is continually changing (market are moving up and down daily—sometimes by 1, 2 or 3%), new investment products are being introduced and economic/political forces are always shifting. Nevertheless, following certain time-tested investment disciplines is likely to continue to produce desirable results. Successful investing is not a matter of trying to determine the unknowable (such as the direction of the market in the short-term, interest rates or the economic growth of China). Rather, it is a matter of establishing a sound long-term investment policy and following sensible investment disciplines in implementing this policy. Once these are in place, much anxiety and distraction are eliminated, and the investment team at Compass can move on to the fun of looking for mispriced, quality investment opportunities and passing them on to you, our clients.

For more information regarding our company, disciplines and results; please call, write, e-mail or visit our website: www.compasscap.com

Compass Capital Management, Inc. * 706 Second Avenue South * Suite 400 * Minneapolis, MN 55402 * (612) 338-4051