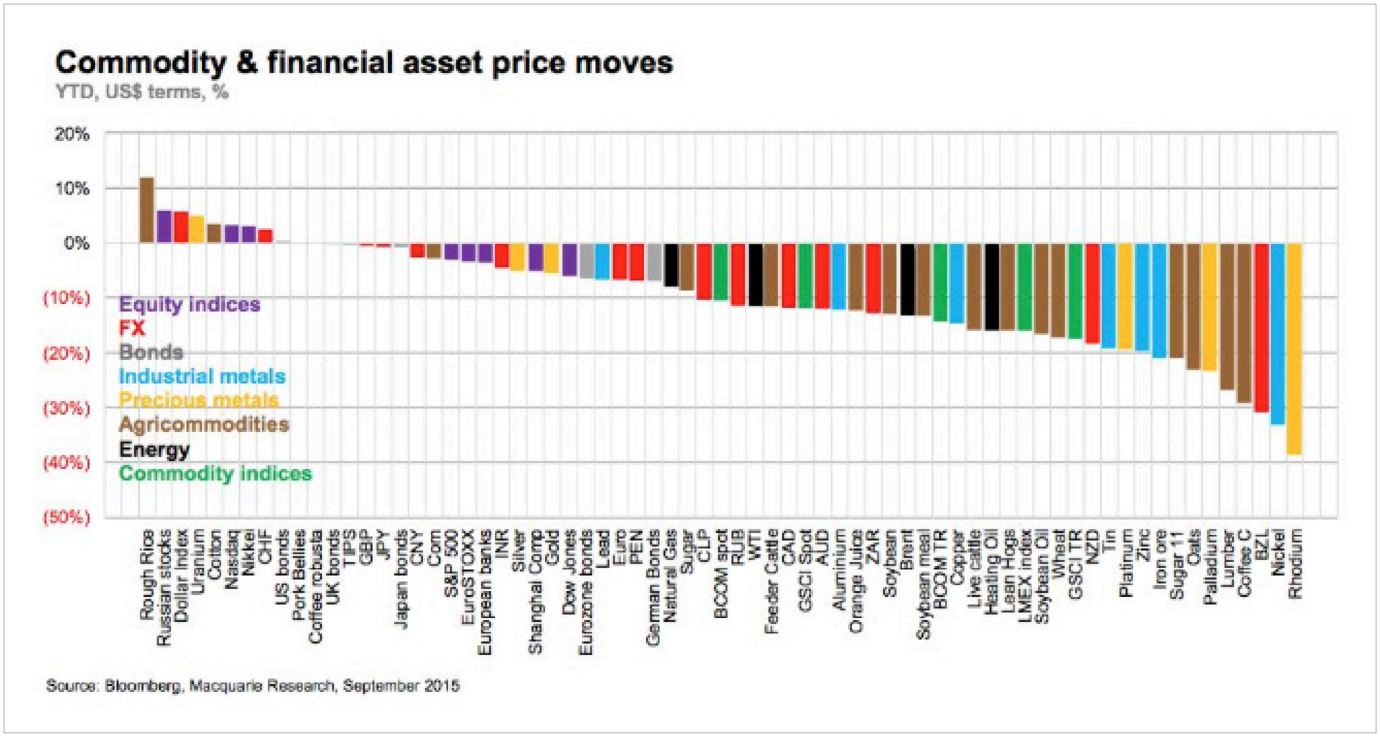
"Some argue that holding significant cash is gambling, that being less than fully invested is akin to market timing. But isn't a "yes" or "no" decision the crucial one in investing? Where does it say that investing means always buying something, even the best of a bad lot? Why should the immediate opportunity set be the only one considered, when tomorrow's may well be considerably more fertile than today's?" – Seth Klarman

Cash is King

- By far our largest investment has been in cash aka "money market funds." It just so happens that the "Dollar Index" (another name for it) has been one of the best performing asset classes year to date. This was not through any real stroke of genius on our part. In response to struggling to find investment situations that made sense to us, we defaulted to cash as a placeholder while we waited for better opportunities. Fortunately, it's proven to be a smart move.



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- In the game of chess, success comes from managing time, space, and "material" (your chess pieces on the board). As the game progresses, one seeks to optimize these three factors to be in a position to strike when a definitive advantage presents itself. There are clear correlations between chess and managing a portfolio. We seek to manage material (our chess pieces are money), not for short-term results, but to have the pieces in place to engage at peak effectiveness. Playing this longer strategy means forgoing mediocre opportunities now for the capacity to strike definitively later in the game. We believe the cash we've retained will be worth significantly more because of the potential prices we'll see in the future.

- Charlie Munger's assessment of Berkshire's performance is instructive:
  "If you took our top fifteen decisions out, we'd have a pretty average record. It wasn't hyperactivity, but a hell of a lot of patience. You stuck to your principles and when opportunities came along, you pounced on them with vigor."

- With China's intense use of commodities inevitably slowing down (Fun fact: China used more cement from 2011-2013 than the US did during the entire 20th century!), there has been some pessimism rightfully creeping into the stock prices of many commodities companies, especially oil and metals. This kind of cratering is exactly what value-minded investors like us look for, as market sentiment tends to overshoot economic reality, both high and low.

- Patience is still required. Since WWII, the typical bear market has lasted 14-15 months while falling 33% on average (it's even worse if we look back farther and include the Great Depression). Everyone remembers the dramatic headlines that punctuated October 2008, but the market actually peaked in October 2007 and didn't reach bottom until March of 2009. It took a full 17 months for the index to be cut in half (-57%) and start its eventual pendulum swing back.

- To summarize: our cash has been a top performer and leaves us perfectly positioned for the recent volatility. But it's still in the early innings and now's not the time for itchy trigger fingers.

"Rather go to bed without dinner than to rise in debt." – Benjamin Franklin

- Debt levels are a serious cause for concern. There's a common misconception that everyone has been "deleveraging" (paying down debts) since the 2008 crisis. This was largely true for the US consumer who, feeling relatively poorer after realizing their house wouldn't continue rising in price like an untethered balloon, quite-rationally cut back their spending and closed the HELOC ATM they were over-utilizing.

- Unfortunately, the world at large has actually added about $57 trillion (with a T!) in the last 7 years. Most of that debt has come from corporations increasing leverage to buy back their own stock (+$18T) and governments borrowing in attempts to goose their economies (+$25T). It's hard to see how much of that borrowing has added to the productive capacity of the world.

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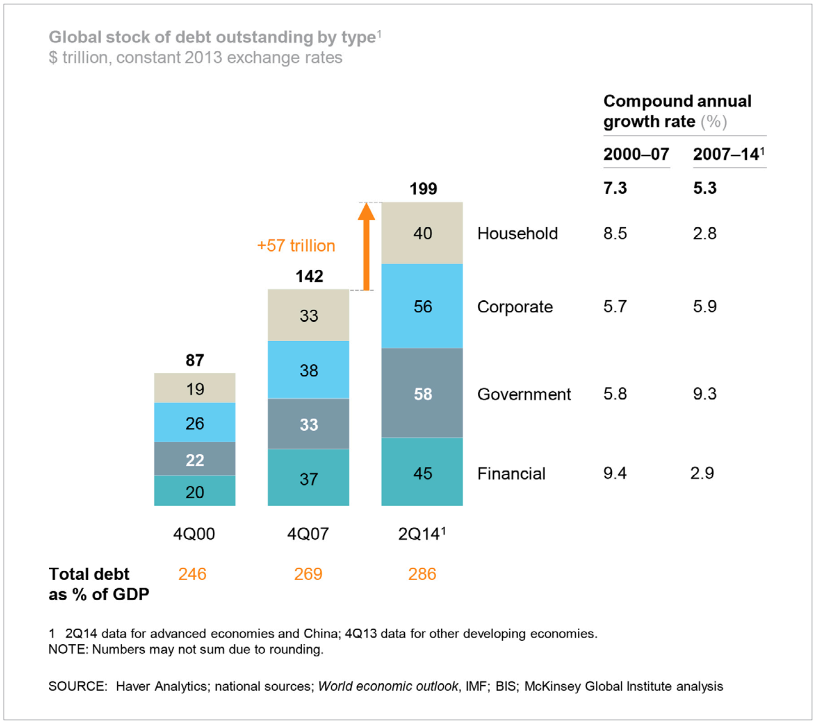

- Debt has been growing much faster than GDP. In the book *This Time is Different: Eight Centuries of Financial Folly*, authors Reinhart and Rogoff catalog myriad examples of crashes and draw clear correlations between swollen Debt/GDP levels and eventual depressions. It's interesting to note this dynamic applies to any organization: sovereign countries, individual businesses, or even families. High debt burdens + falling incomes = bankruptcy. (This concept even works biologically. As any fallen rock star shows, borrowing fun from the future via substance abuse (a form of leverage), while your general health is receding (lower income), equals "bankruptcy.")

- We are lacking the crystal ball that tells us what and when the exact consequences are of all of this debt, but it's definitely troublesome. Even worse, any concerns don't seem to be baked into today's rather euphoric prices. This is an unsustainable trend...

As always, we're thankful to have such great partners in this wealth creation journey.

Jake & Lonnie

Performance since Jan 2008*

FSI (after all fees)	+56.2%
S&P 500 (w/ dividends)	+54.9%

* Based on auditable track record of our flagship fund The 5505 Fund formerly named RCM Partners Fund.

It should not be assumed that recommendations made in the future will be profitable or will equal the performance of the securities discussed. Fund results may differ significantly from separately managed accounts. Individual SMA results may differ due to timing of purchases, account size, and portfolio strategies.

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