Financial Intelligence

Peak Asset
MANAGEMENT

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Twenty Peak Years

by Terry Hefty

Twenty years ago, about this time in 1994, I was filing registration paperwork with the SEC in order to operate as an RIA (Registered Investment Advisor). This was the first step in launching Peak Asset Management, LLC. I was making a major personal commitment to a new business and career in wealth management, which had only been a sidelight for many years previously. Soon afterward, Gerry Witmore, a good friend and retired Digital Equipment Vice President, joined me and lent his considerable effort and expertise for several years to help launch the business.

When Gerry decided to re-retire, Noel Bennett merged his private portfolio management business with Peak to create a larger and stronger practice. In 2000, John McCorvie did the same, providing additional clients and know-how, along with being Peak's first CFA charter holder. Then Joe Glasman, who has earned not only the CFA designation, but is also a CFP and CPA, was recruited in 2006 following a ten-year career at Wells Fargo Wealth Services. Joe added additional and more comprehensive abilities to Peak's financial mix. Tara Hume was next in 2007, and she also completed the necessary requirements and earned the CFA and FRM (Financial Risk Manager) designations. Lastly, Terry Robinette joined Peak as a portfolio manager and equity researcher two years ago.

Twenty years ago it would have been hard for me to imagine that we could assemble such a distinguished team to serve the more than 200 clients (with over $300 million in assets) in the Peak Asset Management family. It has been, and continues to be, an extreme privilege for me to work and interact with these professionals along with our support staff: Debbie Harper, Angela Dwinal and Yvette Green.

Peak's philosophy continues unchanged over these 20 years, simplifying our clients' financial lives by implementing a customized plan for each, focused on the three distinct components: structure, strategy and discipline.

Since the beginning of this year you have no doubt noticed the new look of Peak Asset Management, LLC, which represents our move into the next twenty years and beyond. We have intentionally sought out younger colleagues who, along with providing a seamless transition of services for our clients and their families well into the future, also bring about change and refreshing new ideas. The updated logo, bright colors and soon-to-be-released website are a result of their influence.

Our intention is to consistently increase the range and improve the quality of services offered without sacrificing the personal touch and attention that you expect. An example of this is presented in the following article by Tara Hume. You will be hearing more about additional improvements as the year progresses.

We appreciate the trust that our clients put in Peak and we will strive to continue to earn that trust in the future. Thank you all for your past and continuing support.

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Finance Camp

by Tara Hume, CFA, FRM

Last fall I received a request from one of my clients asking if I would host a "Finance Camp", as she termed it, for her nieces and nephews, who ranged in age from 19 to 35. "Of course!" was my reply. I am always eager to share my passion about finance. Just ask my friends who make the mistake, usually only once, of asking me about the economy or the stock market. My client, who is quite financially sophisticated, and I began with a list of outline topics that we thought would be good to include in "Finance Camp." The list included: asset types; risk vs. return; opportunity cost; liquidity; portfolio theory; asset allocation; diversification; risk tolerance; volatility; total return; types of accounts; common benchmarks; trusts; and retirement planning. My client and I thought these were great topics to present, but how the students would respond was the big question…

My personal education in the world of finance started early because my father is a finance professional and provided me with a financial education throughout my life. I purchased my first stock, Johnson & Johnson, in middle school. I can remember attending a general assembly at school where some of the then current health issues were discussed. While I do not recollect the details of the presentation, I do remember that Johnson & Johnson was invested heavily in pharmaceutical research in an effort to combat some of those issues. I left the auditorium thinking that if Johnson & Johnson were successful, not only would the world be better off but the company would make a lot of money. I presented the idea to my father and in April of 1990 I purchased shares of Johnson & Johnson. Since that time, the company has indeed made a lot of money.

> "That first stock purchase fueled my love of finance and investing."

That first stock purchase fueled my love of finance and investing. I went on to obtain an undergraduate degree in finance, and then earned the CFA (Chartered Financial Analyst) and FRM (Financial Risk Manager) designations. I have now worked in the financial industry for over 15 years; first in interest rate risk management for a large multi-national bank, then performing public and private company valuations and now in portfolio management and wealth planning.

As I began to consolidate all of my learning and experience in finance into a single day's instruction, I realized that the outline topics we had created were focused on investing and portfolio management. While important to understand, these concepts are secondary to what the average young person really needs to learn, understand and practice with regard to his or her financial life. There will be no portfolio of assets if saving never occurred in the first place. More relevant questions are: How do you put money away for retirement when you "need" every dollar you make? Why do you want to plan for your child's college education when you are still paying for diapers? I realized that the camp needed to start with personal finance. After all, personal discipline needs to be in place before investing even becomes a possibility.

With all that contemplation behind us, my client and I decided personal finance topics would be more appropriate for the first half of camp. The outline for instruction included the following:

Control What You Can Control

Personal finance is the process of evaluating your present financial situation, identifying your financial goals, preparing a plan to achieve those goals and implementing your plan. In short, personal finance is learning to control what you can control. We all know one thing for sure: we can't control what the financial world throws at us!

Evaluating Your Present Financial Situation

Companies could not operate without an understanding of their financials. Where is the money coming from? How is it being spent? What debts are outstanding and what assets are available to pay down these debts? Individuals and families should have a similar understanding of their personal finances. However, few of us do. In order to make educated decisions about the future we must analyze our personal assets, liabilities, income, and expenses. The first step in taking control is calculating personal net worth. A net worth statement is a personal balance sheet which lists out all that you own and all that you owe.

Personal Assets - Personal Liabilities = Net Worth.

The next step is to understand income sources and what money is available for spending. A personal cash flow statement illustrates what money is available after all expenses are accounted for.

Income - Expenses = Free Cash Flow.

Expenses should be broken down further by categorizing what is a necessity and what is discretionary. By separating needs from wants, one is able to form a much clearer picture of his or her financial fitness and what changes he or she can make to become more financially fit.

Identifying Your Financial Goals

Financial goals are unique to each person or family and can vary through time. Someone just out of college may be worried about paying off student loans or saving for a home, while someone closer to retirement is concentrating on having adequate income once he or she stops working. Few people truly understand that the best time to start to invest in your retirement is with your very first pay check. For example, if you make at least $30,000 and invest 10% of your pretax income ($3,000 or more) in a tax deferred retirement account throughout your career you will retire a millionaire. Unfortunately, retirement is generally not at the top of the list of priorities when we are just starting our careers.

Preparing a Plan to Achieve These Goals

Armed with the knowledge of your present financial situation and financial goals, it is time to make a plan to achieve your goals. That's right, I'm going to say it: it is time to create a budget. The word budget conjures up some of the same feelings that homework or chores may have in the past. However, budgets help people avoid common traps including too much debt, too little savings and too much spending. Budgeting should evoke a feeling of empowerment rather than dread.

Carrying Out Your Plan

Tracking your budget can often be the hardest part, as it is easy to ignore and eventually quit. However, in my case following a budget allows me to feel good about what I am spending. I can even reward myself for coming in below my budgeted amount. For example, if I budget $700 to spend on groceries this month but I only spend $625, I now have an extra $75 that I can put in my vacation fund or get a relaxing massage. Finally, budgeting provides transparency and allows me to make appropriate adjustments when necessary.

> “ The word budget conjures up some of the same feelings that homework or chores may have in the past. ”

Financial concepts that everyone really needs to understand don't have to do with portfolio theory, but instead with our own daily financial management. The topics of finance camp needed to include things like: saving early and often; the power of compounding interest; the detrimental effect that debt can have if not used responsibly; the long-term cost of a daily Starbucks latte; why tax deferred accounts are important savings vehicles; spending less than you earn; personal risk management; and finally, achieving retirement goals. Retirement should not be based on hitting a certain age, but rather on achieving financial freedom, which can be defined as the ability to choose what you want to do, when you want to do it and for how long. With effective personal financial management, retirement may come sooner than you think.

Many people with whom I have spoken about “finance camp” have been personally interested or have a family member whom they feel would benefit from this type of a presentation. If you have an interest, please let me know. I would be happy to put together a presentation for your family or small group. While digging into the details of portfolio theory and investing is my first passion, spreading knowledge about personal financial health is quickly becoming my second.

Company Profile: PACCAR

by Noel Bennett

Twenty-five years ago I fulfilled a fantasy I'd harbored since childhood: riding cross country in a sleeper-equipped semi. It was an immaculate white Kenworth and we were in a convoy with an equally beautiful Peterbilt, transporting new BMW motorcycles from Reno to Colorado. Driving through the night, sunrise found us crossing the Bonneville Salt Flats. We kept up a steady 75 m.p.h. pace all the way to Grand Junction, and although I spent half of the time in the sleeper, by the end of 600 miles, several truck stop meals and nonstop music from the Oak Ridge Boys, I was eager to get back in a car. The liking for trucks has stayed with me, however, and in early 2010 we purchased shares of PACCAR for our Model Portfolio*. Its stock price declined by more than two-thirds from a high of $66 during the Great Recession, and sales of its Kenworth, Peterbilt and European DAF heavy duty trucks had dropped in half. Even more dramatic was the decline in its earnings, from $3.97 per share in 2006 to $.23 in 2009. Normally a drop that extreme results in the company's CEO departing “to spend more time with his family,” followed by a major restructuring and layoff of employees. But PACCAR's 2009 annual Letter to Shareholders from Chief Executive Mark Piggott showed barely a trace of concern. Was he in denial, or doing a slick PR job, or was he supremely confident that the company's products were so superior and desirable and his company's balance sheet so solid that the worldwide economic crisis was nothing to be worried about?

After our analysis of the company's financial strength (lots

Company Profile: PACCAR cont.

by Noel Bennett

of cash and little debt), its normalized owners' earnings (also very strong), and its profit margins (considerably reduced but in line with other good cyclical businesses), we purchased a position for our Model at $36 per share. Our timing could have been better since it had bottomed out a year earlier at $20, but we bought a piece of an excellent company at a reasonable 45% discount from its high. As is typical with our stock buys, years of waiting yielded an opportunity at a time when most investors were too spooked by the recent economic meltdown to invest in any company, especially a cyclical truck manufacturer.

In 2013, half of PACCAR's sales were generated outside the U.S., down from 64% four years prior, due to the recession in Europe. With the exception of Italy, Europe and Great Britain appear to be starting a recovery, meaning there will be pent up demand for its DAF and Leyland heavy and medium duty trucks. Increasingly stiff emissions requirements both abroad and domestically, the aging of truck fleets (the average age of North American trucks is seven years), combined with gradually improving economies on both continents means that unless there is a relapse into recession, the company's sales should rebound this year to levels last seen in 2006 when worldwide economies and commodity markets were booming.

What could go wrong with our investment? When buying into a cyclical industry, paying a low price and thus getting the all-important margin of safety is crucial, and we believe we achieved that in 2010. But a looming problem is increasingly strong competition from railroads, especially when transporting petroleum and coal. Railways are becoming more efficient, cutting costs and investing heavily in computerized improvements, and are able to transport both commodities and manufactured goods with far less diesel fuel used per mile traveled. Another negative is the unhealthy lifestyle and long hours of an over-the-road trucker, making it difficult for companies to find and keep qualified drivers. But truck routes remain far more flexible than rail, trucks are less subject to long delays at coastal container ports and in rail yards, and they remain able to deliver directly to loading docks anywhere in the country.

> "As is typical with our stock buys, years of waiting yielded an opportunity."

As I wrote in Financial Intelligence shortly after buying PACCAR for our Model, "Like another great American brand, Harley Davidson, its Kenworth and Peterbilt nameplates are universally admired, the best of breed for which owners and would-be owners are willing to pay a premium." Anyone spending a few hours driving the Interstate highway system today can confirm that the niche occupied by PACCAR in the world of cross-country trucking is as intact as it was twenty-five years ago.

*The Model Portfolio is not a real cash portfolio. It represents the core direction of our portfolio management strategies. Individual client portfolios are managed in accordance with the client's specific investment objectives and constraints.

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