July 15, 2015

It was a pleasant surprise to read in *Barron's* recently that in its ranking by investors of the top 30 most respected companies worldwide, we and our clients own 17 either directly or in our pharmaceutical ETF (Exchange Traded Fund). Better yet, our Model Portfolio* holds shares in the top 4 ranked businesses: Apple, Walt Disney, Berkshire Hathaway and VISA. *Barron's* went on to say that its survey shows ethics being weighted more than business performance for the first time since 2010, and that poll respondents now highly value "social responsibility, 'proper treatment' of employees, suppliers, and customers; and a positive impact on the community." We all live in or near Boulder, Colorado—one of the most socially concerned and green communities anywhere. Each of us has his or her own environmental or socially responsible leaning. Mine happens to be biophilia, loosely defined by an ethologist friend as "our natural tendency to be attracted to animals and nature." Given the amount of effort and money being directed toward such causes by large foundations and wealthy individuals, including our own clients, it makes sense for us to continue to focus attention on investing in businesses that do good in addition to doing well.

For a long time, however, socially responsible investing (SRI) has been a conundrum at Peak. When our company was founded in 1996, SRI didn't exist. Since that time it has evolved and matured into a large niche business for investment advisors such as ourselves. According to the fund company TIAA-CREF, "SRI originally involved excluding companies that make products or engage in behavior with negative social consequences. Since then it has evolved into an investment strategy that seeks to have a positive impact on the world by providing funds for projects that offer solutions to social and environmental issues, such as alternative energy, affordable housing and clean water facilities." Aside from the conviction that we would never invest in tobacco companies, our original reluctance to participate in SRI stemmed primarily from the fact that making money consistently for clients is difficult enough without putting such constraints on our investment process. Also, we were looking at multinational public corporations possessing a wide range of products and services, often with subsidiaries in places with names like Pune, Xiangyang and Sao Paulo. So it was a challenge to find ones that we could confidently say did not make any environmentally damaging products or participate in activities with negative social consequences. After all, to quote one of our partners, "Stuff happens."

The Chairman's Letter in the annual report of nearly every one of our Model Portfolio companies contains at least one page that is titled something like, "Being a Power for Good." It typically goes on to promote the company's support for solutions to world hunger and its commitment to community development, minimizing waste and nurturing top employee talent. I fast-forward past this section and focus on "Management's Discussion and Analysis" of the facts and figures of the past year, which is where an investor begins to find what he needs to know. For example, British Petroleum (which we do not own) had several paragraphs in that part of its 2009 annual report touting its "safe, reliable and compliant operations." So in 2010 when an explosion on one of its oil platforms in the Gulf of Mexico spilled the largest amount of oil ever into U.S. waters, resulting in an additional $18.7 billion settlement last week, the accident laid waste not just to the Gulf of Mexico but also to BP's public relations efforts for years to come.

Changing topics, another question we have been debating recently is whether the steady six year advance of the stock market has put us into "Irrational Exuberance" territory. Robert Schiller, the Nobel laureate who wrote a book with the same title, says a bubble is "a period of enthusiastic bidding up of prices by a growing group of enthusiastic investors that goes on too long and is carried away by its own momentum." He states that the stories people tell themselves and others during such times become part of the culture and reveal much about what creates and sustains booms and bubbles. The late 1990s were a time of excitement about a New Era. In 2007 we had what Schiller calls the Ownership Society Bubble, in which there was a belief, supported by the banks, that everyone deserved to own his or her own home, whether or not they could afford it. Interestingly, he notes that today, in 2015, the elevated stock market valuations appear to be driven largely by fear, and we agree: the Federal Reserve is afraid to raise interest rates too quickly lest it plunge the country into a Japanese-style deflation that lasts for decades. The average investor worries about what else he can do with his money if he sells out of stocks. Long term bonds don't look attractive, real estate is approaching 2007 levels and gold is a questionable investment, given the strength of the U.S. dollar.

It's not obvious whether or not today's market is approaching bubble levels, but a fear-based overvaluation seems less likely to harm our clients' assets in a downturn than a greed-driven one. Either way, we subscribe to Warren Buffett's Owner-Related Business Principle Number 14, in which he writes that he prefers to see the share price of his company over time gravitate to a fair level than a high level: "…(By) our policies and communications, we can encourage informed, rational behavior by owners that, in turn, will tend to produce a stock price that is also rational." The best result for us and our clients in the long run would be for the earnings of the 500 companies in the S&P Index to spend the next few years catching up with their share prices, arriving at an equilibrium of fair valuation.

Best regards,

Noel F. Bennett

**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 clients' specific investment objectives and constraints. Historical results are available upon request.*