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# *Constant, Come What May*

It has now been eight years since the Financial Crisis and the Great Recession. But as bad as it was, our economy and equity markets are still the strongest in the world. The Standard & Poor's 500 index is up about 214% since the lows reached in 2009. Even an investor buying at its peak in 2007 would have earned a return of some 36%.

Credit markets now function, asset prices have recovered and enough jobs have been created to place the unemployment rate at levels that would normally signal great strength in our economy.

Yet, in spite of this success, it's also clear that all is not well. While unemployment rates are low, many people appear to have given up looking for work. Economic growth is positive, but muted. Inflation is low and many investors have dusted off their history texts to find the last time interest rates have been this low -- or even negative -- in key parts of the developed world.

In the midst of this begrudging recovery, investors of all stripes are faced with a series of unknowns that seems to increase every day. Does the United Kingdom's vote to leave the European Union signal perilous times ahead or could the global economy emerge stronger than before? Can the Federal Reserve continue to raise interest rates or are economic conditions more fragile than they appear? How will the next president of the United States affect business conditions and the investing environment?

One of the remarkable things about investing over long stretches of time is that while each period faces its own unique challenges, history is often able to provide a guide, or at least a template. The specifics may be different but the themes are frequently the same. As Mark Twain said, "History never repeats itself, but it does rhyme."

We thought this an appropriate time to review our investment philosophy and how constant it has remained -- not only since our firm's founding thirty-seven years ago, but going back to the early years of long-term growth stock investing.

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Growth stock investing is one of the oldest investment philosophies, developed in the 1930s and 1940s. David L. Babson and Thomas Rowe Price, Jr. are widely considered to be its founders and they developed the strategy separately at roughly the same time: Mr. Price started his firm in Baltimore, Maryland in 1937 and Mr. Babson his in Boston, Massachusetts a few years later in 1940. Both firms were investment counseling firms aimed at helping individuals as opposed to institutions, which was then the investing norm.

Our firm's founder, David Wendell, joined David L. Babson & Company in 1959 and by 1967 was the co-editor of the *Babson Staff Letter*. The Letter was directed to friends and clients of the firm and regularly discussed current economic conditions as well as investing in growing industries and markets. By 1972, David Wendell was the editor of the Letter. He established our firm in 1979.

The hallmark of the Babson investment philosophy was to take the long-range point of view. Instead of trying to predict which way the stock markets might go, the Babson firm instead focused on broad trends affecting the markets, economy and society. At its height, the mailing list for the Letter numbered 8,000 names, which at the time was huge.

An example of this long-term point of view can be seen in a Staff Letter written by David Wendell in 1974 entitled *Base Investment Policy on What You Can Predict*:

> *"One of the biggest obstacles to good investment results is the tendency to place too much emphasis on the short-range outlook. At times, the majority of investors seem to believe that the whole future is wrapped up in the headlines of the day. With all the attention it gets, however, near-term forecasting is usually not very rewarding. . .*
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> *The present is a case in point. The big imponderables of the moment -- the Mideast crisis, the oil situation, world finance, the power struggle in Washington -- are very important. Yet these concerns are just new versions of the unpredictables that are always in the picture, as illustrated below:*

| | ***The Perennial Unpredictables*** | ***Today's Version*** |
|---|---|---|
| 1. | *What stock prices will do next week, next month or next year.* | *Will the Dow Average end up the year below 700 or above 1000?* |
| 2. | *Which way the political winds will blow.* | *Will President Nixon resign, be impeached or finish his term?* |
| 3. | *When the economy will change direction and for how long.* | *Are we entering a brief slowdown or a deep recession?* |
| 4. | *Where the course of international developments will lead.* | *Can the Mideast powder keg be defused or will it blow up?* |

> *For as long as we can remember, the amount of effort spent on trying to predict the above unpredictables has been way out of line with the investment results it has made possible. In fact, we don't know of a single investor who has been successful over the years because of his ability to forecast short-term developments."*

Just for fun, we recently updated this list to reflect the current investing environment:

| | ***The Perennial Unpredictables*** | ***Today's Version*** |
|---|---|---|
| 1. | What stock prices will do next week, next month or next year. | Will the Dow Average end the year below 17000 or above 18000? |
| 2. | Which way the political winds will blow. | Who will be our next President, Hillary Clinton or Donald Trump? |
| 3. | When the economy will change direction and for how long. | Are we entering a brief slowdown or a deep recession? |
| 4. | Where the course of international developments will lead. | Can the Mideast powder keg be defused or will it blow up? |

We didn't need to make much in the way of changes, and it is clear that 42 years later the "Perennial Unpredictables" are indeed perennial!

To be sure, the challenges we face in 2016 are important. The near-term picture is unclear, especially with interest rates in negative territory in some of the world's major economies. All over the world, corporate earnings are softening, terrorist events seem to be on the rise and the global economy may be undergoing drastic changes. In the U.S., our national politics are as tumultuous as they've been in decades.

But looking back over time, we have adhered to the same investment philosophy for nearly four decades, through other periods of great challenges and difficulties. And through it all, we have strived to maintain a long-term point of view.

Central to this long-term point of view is our discipline of focusing on some of the best companies in the world. They tend to be the leaders in their fields. Their revenues, earnings and dividends per share are growing and with their experienced and capable management teams, they are more than likely to continue growing in the future. While these companies span many different industries and market segments, they tend to share a number of fundamental characteristics.

For example, two of the fundamental characteristics that we pay particular attention to are quality and financial strength. Quality is multi-faceted and one of several tools we use to judge it is Standard & Poor's ranking system. In this system, key elements of quality are the growth and stability of earnings and dividends.

Over time, a company's management team, its competitive position and its products and services feed into the growth and stability of its earnings and dividends. The rankings run from "A+" for the highest quality to "C" for the lowest and "D" for a company in bankruptcy or reorganization. It may take a while for newer companies to be rated by Standard & Poor's.

Financial strength is also important, especially so in the aftermath of the Financial Crisis. Value Line, an investment research firm, rates companies' financial strength by looking at their income and balance sheets, the amount of debt that is owed, and how the companies handle their finances in general. The most financially strong companies are rated "A++" while the least strong are rated a "C".

The chart below shows the most widely held companies among our firms' clients:

Top 25 Client Holdings

| Company | Standard & Poor's Quality Ranking | Value Line Financial Strength |
|---|---|---|
| Automatic Data Processing | A | A++ |
| TJX Companies | A+ | A++ |
| MasterCard | B+ | A++ |
| Ecolab | A | A |
| Nike 'B' | A+ | A++ |
| Colgate-Palmolive | A | A++ |
| Coca-Cola | A | A++ |
| ExxonMobil | A- | A++ |
| Johnson & Johnson | A | A++ |
| Stryker | A- | A++ |
| McCormick & Co. | A+ | A+ |
| Apple | B+ | A++ |
| Church & Dwight | A+ | A+ |
| McDonald's | A | A++ |
| Fiserv | B+ | B++ |
| Abbott Labs | A- | A++ |
| Stericycle | B+ | B++ |
| Celgene | B | A+ |
| Proctor & Gamble | A | A++ |
| PepsiCo | A | A++ |
| AbbVie | *Not Rated* | A |
| Walgreens Boots | A- | A+ |
| Microsoft | A- | A++ |
| United Technologies | A+ | A++ |
| Intuit | B+ | A+ |

As can be seen, these companies are some of the world's finest. Their quality and financial strength makes it very likely they will continue to grow their revenues, earnings and dividends per share over the years, come what may. And we will remain constant in our investment philosophy, continuing to focus on companies such as these in the years ahead, come what may.

*Neil G. Bleicken*
*Karen Wendell*