

Northstar Notes

Standing on the Shoulders of Giants

“There are no shortcuts to any place worth going.”

– Beverly Sills, Soprano

As we move into the second half of the year, we wanted to take a few moments to share some perspectives with you. This short commentary is not meant to encapsulate our world view, our political leanings, or heaven forbid, our predictions about stock prices. Instead, we want to explain our learning process.

Every day, we humans have to make choices. We make these choices using the best information we have, though often it may be incomplete or even incorrect. And if that weren't challenge enough, our instincts often take us in the wrong direction. Teenage children and spouses are quick to point out this deficiency, but thankfully, the field of behavioral economics tells us that it's not completely our fault. It turns out that during the evolutionary process, our brains have become hardwired to take shortcuts that can lead us to ignore the right decisions in favor of the wrong ones.

Examples of these shortcuts might include people preferring meat that is “90% fat free” (healthy) over meat that is “8% fat” (yuck), in the same way that patients are more likely to choose a treatment with a “90% survival rate” (wonderful) rather than one with a “9% mortality risk” (mortality=terrible). Do the math, and you will see that the latter example in both cases is really the more favorable one. Most of us, according to Nobel laureate Daniel Kahneman, are wired first to avoid losses, and will process stimuli with a strong, automatic bias against negative information, which can often lead to making poor choices.

As advisors, we make choices about how to put your money to work in a way that will best secure your financial future. Obviously, we want to make the right decisions and avoid the shortcuts that lead to wrong ones. To do so, we remind ourselves of these mental shortcuts every day, so that we can avoid them when it matters most.

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Reacting to short-term, media-induced static is one of the most common investment shortcuts, and one of the hardest to resist. The news is filled with distractions, faulty logic, and alarmist sentiment, just begging us to make a move. In 2011, for example, many investors took their money and moved to the sidelines until the United States government returned to a semblance of normal functioning. After all, Congress was dysfunctional, the country was defaulting, our credit rating was downgraded, the sky was falling! Wasn’t that reason enough to seek shelter in safe, cash-like investments? As it turned out, most of those millions of investors who liquidated holdings of fine companies are still waiting for politicians to return to rational behavior, while the shares they unloaded have soared to record heights.

Over time, we’ve found that when we step back and focus on long-term outcomes, the right decisions become more apparent. Instead of careening from crisis to crisis, we choose to stand on the shoulders of giants. We own shares in magnificent businesses with the expectation that their future cash flows will be greater than the near-zero returns from cash instruments. First-rate companies have a proven ability to navigate myriad obstacles and changing landscapes. Their thousands of employees are working every day to widen the moat around their businesses’ castles. They exemplify the qualities that are required for a durable business: integrity, sound management, efficiency, and the ability to adapt.

Not coincidentally, we try to exhibit the same kind of excellence at Northstar. Just as a Fortune 500 firm's adherence to these qualities is reflected in its share price, it is our belief that our dedication to rational principles and ethical practices should be reflected in our relationship with you.

Over the past few years we have benefited from a bull market in America. That's terrific. Yet, while we're glad that investors have growing confidence in the prospects for American businesses, it's easy to be lulled into thinking that market turmoil only exists in our rear view mirror. Basking in the glow of fresh market highs, the 19% decline of the summer of 2011 seems like a mere memory, doesn't it? Counterintuitively, it is precisely at moments like this that we have to remind ourselves that corrections are inevitable and inescapable. They will come again. And no, we're not afraid of them, because they have little to do with the characteristics of the businesses we invest in. They're more often simply the result of the collective hive-mind of investors across the world.

"If a man had £20 a year for his income and spent £19, nine shillings and sixpence of it—he would be happy but.....if he spent £20 and one (penny) he would be miserable." —Mr. Micawber in "David Copperfield" by Charles Dickens

So, choosing companies is one part of what we do. Choosing people is another. In order to do the best work for you, we have enlisted the help of three new faces around the office. We are happy to welcome Joshua Garcia, Bobby Asher and Stephen Colacurcio to the Northstar Group. It is likely that if you've called our office in the past few months you've spoken to at least one of these young men. Joshua, who joined us last September, graduated from Brown University in 2012 with a degree in Ethnic Studies. Stephen, also a Brown graduate with a degree in Economics, joined us in January. Bobby is currently working on his master's degree for Sports Management at NYU.

July 31, 2014

The Northstar Group, Inc.

And another important member of our team is Jenna Kastner. We have known Jenna for many years, and first came to rely on her when she did fantastic work for Royal Alliance's back office. She is our "go to" person on our larger, complex client service projects.

It is our hope that as a team, we will constantly remind one another that shortcuts don't work, that there is lasting value in a great business, and that the best way to succeed is to stand on the shoulders of giants.

Henry Asher and Linda Ray
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