



Epsilon Theory

Notes From the Field: The Goldfinch in Winter

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I've learned that people will forget what you said, people will forget what you did, but people will never forget how you made them feel.

— **Maya Angelou (1928 – 2014), author of *I Know Why the Caged Bird Sings***

And in our business, people will forget what price targets you set, people will forget what funds you managed, but people will never forget how you impacted their personal account.

Longer summer means longer winter.

— **traditional Westerosi saying**

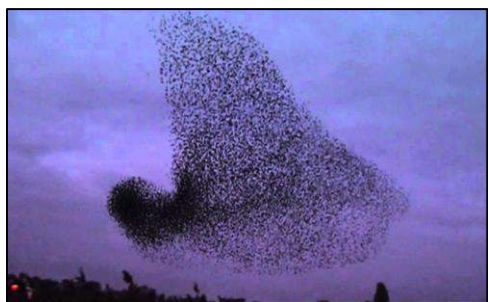
We've got a five acre field that I brush hog once a year if I'm feeling particularly industrious, and one day I suppose we may do something with it.

In late summer this fallow field of thistle and hay is one of my favorite spots, particularly in the early morning and late afternoon, because of the flocks of goldfinches that swoop in and around the field. The goldfinch is exactly as the name implies — a small bird with a bright yellow, almost tropical, plumage — and it looks out of place in the Northeast, like maybe it's an escapee from a gilded cage in Greenwich. But they love these Connecticut



summers, and it's not uncommon for me to count 30 or more flying around in a swarm that at times

seems to be the animal itself.



The flocks are never as big as the far more famous murmurations of starlings, which is a good thing, of course, but they generate that same sense of awe in that there is clearly some sort of order and method to the flowing chaos of all these birds moving together. Most unlike the starlings, however, is that the goldfinch flocks are absolutely beautiful. The glints of yellows and gold moving through the air like a living liquid, the morning sun piercing the flock ... it's a natural

poetry that has no good reason to exist, but does all the same.

I'm as much a dilettante birdwatcher as I am a dilettante farmer, so when the beautiful yellow birds stopped making their appearances over the field every fall, I just assumed that they were like the robin, flown south for the winter. I assumed this was the case for years, and in fact some goldfinches do migrate south every year, particularly the ones who set their breeding nests up in southern Canada.

But not our goldfinches. No, our field and its thistles, together with the nearby woods and the river that runs through it, is just too good of a home base to leave even for a season (I agree!). So they don't fly south. They don't go anywhere at all. They stay the whole winter, there in the field and the scrub and the forest all along.

Why didn't I see them in the winter? Because they change color, or at least the males do, exchanging their flashy yellow feathers for a quite pedestrian dull brown. Just an ordinary little bird, one you'd never give a second glance at, even if now you remember seeing so many at the bird feeders you set out when the snows come.

Yes, the goldfinches were there all along. I just didn't know where to look.



What's the investing lesson here?

Goldfinches are like Value investing. Or Growth investing or Momentum investing or whatever your investment style might be. They have a season where they seize the stage, blistering in their radiance. And then they recede. They don't go away. They just fade into the background and become a pedestrian little bird, until their appointed season returns — it always does! — and they seize the stage once more, zipping around in a glorious flock with some sort of fractalish order-in-chaos.

Unfortunately for us investors, though, the seasonality of investment styles is more like Westeros on *Game of Thrones* than Connecticut here on Earth. "Winter is here" on *Game of Thrones* today, but it took a long time coming ... summer lasted a good nine years this time around, and legends tell of a winter back in the day that lasted for an entire generation. **The winter currently being experienced by Value investors only seems like it's lasted for a generation.**

Not surprisingly, then, investors are always asking the same question: **is there a bird for all seasons?** Is there an investment style or process that can be more than just a pedestrian performer come winter, spring, summer, or fall, and no matter how long or how deep those seasons might be?

The answer, I think, is yes. The answer, I think, is *diversification*. There's your bird for all seasons.

But here's the problem with diversification, and it's a problem I've written about extensively in *Epsilon Theory*, most recently in "[It's Not About the Nail](#)" and "[It's Still Not About the Nail](#)", and in an oldie but goodie titled "[Don't Fear the Reaper](#)".

Diversification isn't a pretty bird. Diversification doesn't make my heart skip a beat like a flock of goldfinches in July. Diversification, *by design*, is going to have winners and losers simultaneously. Diversification, *by design*, is never going to look pretty doing its job, because if your portfolio is all working in unison, swooping through the market in a beautiful glint of gold ... well, you may be making money, but you sure aren't diversified. Diversification is undeniably effective, but it's effective like a rat is effective, wonderfully adapted to do pretty well in pretty much any possible environment without calling too much attention to itself. That's actually one of the rat's primary survival mechanisms. It's not flashy. It's not pretty. It's a freakin' rat.

Diversification doesn't make us *feel good* like a winning value or growth investment makes us feel good, and as Maya Angelou so brilliantly said, how you make people feel is ALL they remember.

I don't have an answer for the simple fact that diversification doesn't sing. I can't make a financial advisor's client *feel good* about diversification. I wish I could, because I would be ... umm ... a very rich man. But what I do know is that it's a mistake to gussie up diversification as something that it isn't. You can't sell diversification as a beautiful song bird. You have to be honest about what diversification can and can't do, not just for a portfolio's *performance*, but also for a portfolio's *experience*. The more years I spend in this business, the more I am convinced that how one lives with a portfolio, how one experiences its ups and downs over time, is more important for business success and business staying power than that portfolio's performance. And I'm not just talking about volatility, which is usually how we think about the path of a portfolio and its ups and downs. No, I'm talking about how a portfolio makes us *feel*. Most of us need those goldfinch moments of wonder and awe, even if they just last for a season, to feel good about our portfolios, and those are moments that diversification has a really hard time delivering.

To every thing there is a season, and a time to every purpose under heaven. That holds for portfolio construction, too.

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