Warnke/Nichols Ltd.
Investment Management

William R. Warnke, CFA
Steven R. Nichols, CFA

PORTFOLIO NOTES **FEBRUARY 2022**

To our Business Partners:

- ***WHEN "MR. MARKET" MELTS DOWN.*** Vitaliy Katsenelsen is a value-oriented money manager and prolific investment commentator. In his latest "Contrarian Edge" blog, he writes eloquently about "How to Build a Portfolio for Today's Crazy Markets." He wrote the following in response to a question about a plan to protect clients' portfolios if the market goes into a panic free fall:

  "Answer: There is absolutely nothing we can do to *fully* "protect" the portfolio … (T)he best protection against stock market declines is to make sure the businesses you own are worth a lot more than what you paid for them.

  "Let's try a new analogy. Let's say someone insults me. My first instinct is to get upset and react. But then I'm reminded by the Stoic philosopher Epictetus to 'Remember that the person who taunts or hits you does not insult you, but your opinion about these things as being insulting does. So whenever somebody upsets you, know that it is your own opinion that upsets you. Accordingly, first strive to not be carried away by the appearance. For if you take the time and pause, it is easier to control yourself.'

  "Why should I be upset at Mr. Market for calling our stocks ugly and taking them down 30%? That's just his opinion. Once Mr. Market sobers up, he'll change his mind. There is a saying, 'Don't take criticism from someone who you wouldn't take advice from.' We work very hard at analyzing and valuing each company we invest in so that we don't have to take advice from a deranged Mr. Market.

  "So how do we protect your and our portfolio if the market goes into free fall? By playing a very different game. By not trying to protect the portfolio from temporary declines. Yes, you read that right. What does it matter if on any given day moody Mr. Market coughs up the opinion that our portfolio should be priced 30% lower? That's just Mr. Market in one of his depressed moods. We don't need to do anything about it. The value of businesses we own has not changed by 30%, and that is all that really matters in the long run. *Long run* is the key term here.

  "If you don't have a long-term time horizon you should not be in stocks, period. If your personal situation doesn't allow you to tolerate a 30% decline of the portfolio, please give us a call. We'll need to discuss allocating a portion of your portfolio to cash. If you'll need some funds over the next three to five years, you'll need to set them aside in cash. These funds should not be in stocks."

- ***PORTFOLIO VALUATION.*** Due to falling prices recently, along with a review of our intrinsic value calculations, the aggregate price-to-value of our group of stocks* has fallen to 87%. It's still not good enough to become more aggressive stock buyers.

- ***RECENT RESULTS.*** Year 2022 is off to a crummy start, with all the popular averages down in the 3% (Dow) to 8% (NASDAQ) range. The large-company indexes, still driven by a few very large companies, are still way ahead of smaller-company stocks over the past twelve months. For the year-to-date and trailing year, our group* has trounced all the popular averages. The market has been very kind to "value" stocks since late 2021! It's been a long time coming.

Steve Nichols, CFA *Bill Warnke, CFA*

The group of "portfolio stocks" -- our Equity Composite for the purpose of evaluating investment performance -- consists of 18 stocks that are held in our clients' accounts. Portfolios might hold some or all of these stocks, depending on investment guidelines unique to each client, the timing of purchases and sales, and start dates of accounts. The performance of this group of stocks is a good proxy for our equity performance but might vary widely among accounts. Of course, past performance is not necessarily indicative of future results.

We hereby offer to deliver to you without charge a copy of our current Form ADV Part 2, in accordance with the U.S. Securities and Exchange Commission's "Brochure Rule." Please contact us if you would like us to send you a copy.

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440 Wells Street, Suite 203 Delafield, WI 53018 262–303–4113
Fax: 262–400-3030 E-mail: value@warnkenichols.com www.warnkenichols.com