

# THE ARETÉ QUARTERLY

## Welcome

As it becomes progressively more apparent that the investment landscape presents unique challenges, it is also becoming progressively more apparent that conventional investment approaches are not sufficient for meeting those challenges.

Areté is a unique organization for unique times. With an orientation to research and analysis, these activities are applied for the purpose of solving problems and helping investors do the best they can. Each investment decision and communication is made with the mindset of having skin in the game.

If you are interested in getting more (or different) investment insights, please take a look at our blog [[here](#)]. Content for the posts is selected and created on the basis of being important, relevant, and useful.

In addition, *Observations by David Robertson* provides a weekly collection of insights and analysis that are intended to be especially relevant for long-term investors. You can find the letters on the substack platform at: <https://abetterwaytoinvest.substack.com>

Finally, please always feel free to contact us with questions or comments.

## Business Update

The performance of the All-Terrain strategy composite in its first full calendar year was

good (see performance on page 5). It finished up a little over 2% whereas the Vanguard balanced fund finished down almost 17%. That's a big differential - and it happened for the right reasons.

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All-Terrain almost completely avoided mainstream stocks and bonds which were the biggest detractors from performance. In addition, it reached beyond more conventional asset classes to improve diversification and to supplement returns. In short, 2022 proved to be a terrific proof of concept for the new strategy.

The main challenge for the new year will be maintaining a strong performance edge, but I don't think that is going to require doing anything substantially different. A large proportion of investors have still not recalibrated to the new investment landscape. This means risk management will be the number one priority which means avoiding stocks and bonds.

The emerging challenge will be attracting new business and new assets to the strategy while there is still plenty of time to prevent a lot of anguish (and investment losses). Despite strong performance and a sounds

strategy, I still expect this effort to be an uphill climb. The reason is there is a lot of inertia regarding changing advisors. Most of the time people only switch *after* they have lost a lot of money.

Further, incumbent advisors don't like to lose business and normally go to great efforts to retain it. I know because I used to work for bigger shops that exerted a lot of effort to retain business.

Indeed, it struck me that more effort was exerted to retain business than to make difficult, but important investment decisions. This realization was a big reason I decided to start Areté. It's not that bigger shops don't have really smart people or large research budgets. It's that they tend to leverage those resources more to the business of gathering fees than to the outcome of making clients better off.

So, if you know someone is looking for a different/better investment service, please let me know - I would really appreciate it!

In the meantime, I will continue doing what I do - sharing my thoughts about markets and portfolio strategy with clients and other interested parties through the "[Observations](#)" newsletter. Look through the archives and it is easy to trace how my thinking has evolved from the start of the pandemic through to today. I also put out [The Areté Quarterly](#) to provide a more detailed analysis of the investment strategy.

Thanks! And please don't forget, if you ever have questions or clarifications, let me know at [drobertson@areteam.com](mailto:drobertson@areteam.com) and we'll get things straightened out.

David Robertson, CFA  
CEO and founder, Areté Asset Management

## Asset Allocation

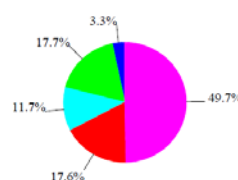
In the current allocation, cash is still the largest position and actually increased a little bit with some net sales in the quarter.

The Gold position increased partly due to performance and partly due to the addition of PAAS. The uncorrelated class weight declined partly due to performance and partly due to a sale.

With the exception of cash, all other classes are underweight relative to the targeted allocation. That said, Gold, Uncorrelated, and Inverse correlation are all relatively close. The only significant underweight position is equity.

The chart below reflects a representative account from the All-Terrain composite.

**Actual Allocation**



**Target Allocation**



As a reminder, the easiest way to think about the strategic priorities of the All-Terrain strategy is as an effort to get the most out of the valid market opportunities that exist. In other words, it is more about finding attractive assets and creating thoughtful diversification than about speculating which hot stock might do well.

The Fed's Quantitative Tightening (QT) program remains in full gear and that is clearly affecting markets. Further, the Treasury General Account (TGA) got whittled down in

the fourth quarter. That means if its target level of \$700B is to be reached, more than \$300B of liquidity will get pulled from the system. As a result, the primary goal remains to stay mostly clear of stocks and bonds. This explains the high cash levels.

From a high level, prices of stocks and bonds in general are still not cheap, and got worse in the fourth quarter. The main efforts are to avoid assets that depend on leverage or structured finance and to find ideas that can perform well independently of what the major stock indexes do.

## Transactions review

There were four transactions in the quarter. Three of these were sales of positions no longer considered core to the All-Terrain strategy. LE was never a large position. NRG proved incapable of producing consistent growth. GLPI, while sporting an attractive dividend yield, is also vulnerable to weakening consumer spending and credit conditions.

The lone new purchase was PAAS, a silver mining operation. This stock had been targeted for years and has swung wildly over that time. When it made an offer for AUY, the stock sold off and created a fortuitous opportunity to increase the weight of the Gold asset class.

## Performance review

With the All-Terrain strategy now being the sole focus, here are some of the general principles that guide its management.

The search for undervalued assets remains the same, although the scope of that search

expands now encompasses a broad universe of publicly traded securities and funds.

The overarching goal of providing attractive returns to investors on an absolute basis also remains the same. As many markets became significantly overvalued, this is especially important to keep in mind.

Finally, the major change features a greater emphasis on diversification. This new focus will elevate the importance of uncorrelated return streams and reduce the importance of individual security performance.

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For the fourth quarter, the ATA strategy returned 3.94% (net of fees) while VBIAX returned 4.91%. While ATA modestly underperformed in the quarter, it was encouraging that it managed to produce the vast majority of the upside in the quarter while also avoiding virtually all of the downside of the first three quarters.

Gold proved to be the standout performer of the quarter, staging a healthy rebound from a poor third quarter. Other than that, the only other notable performance was that of CTA which was unusually weak in the quarter. Many of the trends that had proven powerful most of the year seemed to get disrupted in the fourth quarter.

## Investment Philosophy

We firmly believe in the critical importance of a cogent investment philosophy for any investment operation. In order to emphasize this point, and to assist you in understanding how we work, we provide an abbreviated version of our investment philosophy here. The text of our investment

philosophy is also provided, in its entirety, in our Form ADV, Part II which is available upon request at any time.

### **Asset allocation is a key function of wealth management**

One of the most important functions for long-term wealth accumulation is to have access to certain asset classes when they are attractive and to be able to minimize exposure to other asset classes when they are extremely unattractive. In short, diversification moderates the long-term swings in portfolio performance and therefore significantly increases the chances of wealth accumulation over a reasonably long investment horizon.

### **Mispriced assets are an important source of performance**

One of the keys to investment performance is finding and exploiting market inefficiencies. While such inefficiencies can arise in the form of mispriced securities, they can also arise in the form of over- or under-valued industries or asset classes.

Identifying such opportunities begins with the assessment of underlying intrinsic value. When disparities with market prices exist and clear rationale for such mispricing can be identified, there are opportunities to take advantage of the differential.

### **Information management is a core skill of investment management**

Analyzing investment opportunities and developing portfolio construction is a dynamic exercise that involves a constant and ongoing process of gathering information, processing it, analyzing it,

developing knowledge, and applying it for the benefit of clients.

### **Execution is crucial for investment success.**

In order to create value, an investment strategy needs to be implemented continuously and comprehensively. Actions speak louder than words. We believe the most effective efforts focus on a few simple, but key concepts that work to ensure proper execution of a firm's investment strategy. This approach is notably distinct from the common practice of simply gathering assets.

The first key to execution is structural in nature and involves a firm's independence. By maintaining independent ownership, an investment firm eliminates agency effects which can present a conflict of interest between clients and certain of its ownership groups.

The second key to execution is temperament. The best investors tend to have a temperament that provides them the courage and initiative to act, often going against the grain, when opportunities arise. However, the same temperament provides balance such that decision-making is not simply a risk-taking activity, but a very conscious and targeted effort to engage in propositions with high risk-adjusted expected returns.

Finally, another important element of execution is simply doing what you say you do in your investment process. Too often, perfectly acceptable investment processes fail when actual investment activities bear little resemblance to the process described in the marketing presentation. We call this the "marketing gap;" the difference between what is said and what is done.

Execution is optimized when the marketing gap is minimized.

## Areté All-Terrain Composite (revised)

**Areté Asset Management, LLC**  
**All Terrain Composite**  
**August 31, 2021 - December 31, 2022**

Period	Vanguard balanced			Number of Portfolios	Internal Dispersion (percent)	Total Composite Assets (\$)	Composite Assets With Bundled Fees (\$)	Percentage of Composite Assets With Bundled Fees	Total Firm Assets (\$)
	Gross-of-Fees Return (percent)	Net-of-Fees Return (percent)	Index Fund (percent)						
2021	0.06	-0.20	2.22	3	NA	841,887	841,887	100%	1,460,255
2022									
January	-1.04	-1.27	-4.52	3	NA	831,184	831,184	100%	1,444,243
February	2.02	2.02	-1.96	3	NA	847,963	847,963	100%	1,470,743
March	3.64	3.64	0.84	3	NA	878,830	878,830	100%	1,520,047
April	-0.58	-0.83	-7.00	3	NA	871,564	871,564	100%	1,796,422
May	-0.88	-0.88	0.14	3	NA	863,873	863,873	100%	1,776,888
June	-3.23	-3.23	-5.66	3	NA	835,962	835,962	100%	1,725,958
July	-0.63	-0.88	6.50	3	NA	828,626	828,626	100%	1,708,959
August	-0.61	-0.61	-3.29	3	NA	823,581	823,581	100%	1,698,941
September	0.58	0.58	-7.27	3	NA	828,357	828,357	100%	1,714,003
October	2.56	2.31	4.27	3	NA	847,478	847,478	100%	1,748,946
November	0.97	0.97	4.63	5	NA	1,482,895	1,482,895	100%	1,767,897
December	0.60	0.60	-3.83	5	NA	1,491,824	1,491,824	100%	1,778,478
Q1	4.63	4.39	-5.60	3	NA	878,830	878,830	100%	1,520,047
Q2	-4.64	-4.87	-12.13	3	NA	835,962	835,962	100%	1,725,958
Q3	-0.66	-0.91	-4.50	3	NA	828,357	828,357	100%	1,714,003
Q4	4.18	3.92	4.91	5	NA	1,491,824	1,491,824	100%	1,778,478
YTD	3.26	2.26	-16.89	5	NA	1,491,824	1,491,824	100%	1,778,478

Areté Asset Management All-Terrain performance composite disclosures follow:

### Revision

This table was revised from the original to account for the inclusion of two portfolios that met the requirement for inclusion in the composite in the quarter. Gross performance for the quarter was revised from 4.19% to 4.18% and net performance was revised from 3.94% to 3.92%.

**Definition of the firm**

Areté Asset Management, LLC (Areté) was established in 2008 and is registered as an investment adviser in the state of Maryland. Areté is defined as an independent investment management firm and is not affiliated with any parent organization. Areté currently manages one strategy, the U.S. equity mid cap core strategy, which it markets to individual and institutional clients.

**Benchmark**

The benchmark is the Vanguard Balanced Index Fund Admiral Shares (VBIAX), and its performance is reported in U.S. dollars.

**Calculation methodology**

Portfolio valuations are calculated as of calendar month-end and are computed in U.S. dollars and performance is also reported in U.S. dollars. Time-weighted rates of return are used which adjust for external cash flows. Our smaller, retail accounts contain fee structures in which one flat, per-transaction fee is charged for trading expenses, and which embeds an implicit charge for custody. Since trading and custody charges cannot be directly segregated in these cases, they constitute “bundled fees”. Gross-of-fees performance returns are presented before management and custodial fees when custodial fees can be segregated from trading but are presented before management fees and after bundled (trading and custodial) expenses for our retail accounts. Net-of-fees returns are presented after management fees, trading expenses, and custodial expenses are deducted or after management fees and bundled (trading and custodial) fees for retail accounts. There are no instances in which management fees are bundled with trading or custodial fees. Returns are presented net of nonreclaimable withholding taxes when applicable. Areté does not use leverage or derivatives in the management of portfolios. Additional information regarding policies for calculating and reporting returns is available upon request.

**The composite**

This All-Terrain allocation strategy composite was created in August 2021 and includes all fee-paying, taxable and non-taxable, discretionary, long only, fully invested portfolios benchmarked to the Vanguard Balanced Index Fund. Every new portfolio is added to the composite in the first complete calendar month that it is “fully invested”. For purposes of composite construction, a portfolio is “fully invested” when it breaches the threshold of 90% similarity with core composite portfolios. Each portfolio will remain in the composite until its similarity with core composite portfolios falls under 90%. A complete list and description of firm composites is available upon request.

**Fee schedule**

The management fee schedule is as follows: 1% of AUM up to \$1 million, 0.75% on AUM greater than \$1 million, but less than \$5 million, and 0.65% on assets greater than \$5 million.

**Minimum account size**

There is no minimum account size for inclusion in the composite. Please note, however, the minimum initial account size accepted is \$100,000.

Areté Asset Management All-Terrain performance composite disclosures continued:

**Dispersion**

Internal dispersion is currently not meaningful as there are five or fewer portfolios included in the composite. In the future, we plan to calculate dispersion using the dollar-weighted standard deviation of all portfolios included in the composite for each performance period.

**Verification**

Areté has not been verified by an independent verifier for its compliance with GIPS.