

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

For starters, the All-Terrain allocation strategy is up and running! Even better, every

client switched over to the new strategy which is an encouraging endorsement of the approach.

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I think the timing for this is good. The balanced fund benchmark, VBIAX, had a good July and August, but a very weak September. As I mentioned in both the [market review for the quarter](#) and in [Observations from 10/15](#), the investment landscape is becoming more complex. As the threat of inflation increases, the threat of a very different investment regime also increases. Further, that different regime is also quite likely to be hostile to traditional balanced portfolios.

For example, my current forecast for expected returns from stocks is about -6% per year for the next twelve years. This is based on methodology developed by John Hussman and is essentially a price/sales ratio for the broad market. As he has demonstrated, this measure has been extremely effective in forecasting *future* returns.

This is the analytical foundation for my extreme trepidation towards having a large exposure to stocks. If correct, it means

stocks will be worth a little less than one-half what they are today in twelve years. That would be devastating to retirement portfolios and is exactly what I am trying to avoid.

That said, I recognize the Fed and other major central banks seem to be on a mission to inflate asset values for as long as they can. However, that effort is going to be offset by tapering in the short-term and by the need to manage inflationary pressures in the longer-term. In other words, I view it as extremely unlikely that the Fed can perpetuate the illusion it can keep stocks afloat forever.

Two big implications arise from this. One is diversification is going to be more important than ever. And by diversification, I don't just mean small caps vs. large caps vs. international stocks. I mean securities that go up when the S&P 500 goes down. There are fewer and fewer of them but it will be critical to have them.

Another big implication is stocks and bonds are likely to endure some real turmoil. As a result, I do expect opportunities to increase exposure to stocks on a tactical basis.

Most of what is happening from a market standpoint is a transition from stocks benefiting from short-term cues to stocks benefiting from longer-term cues. As a result, the challenge of portfolio management is mainly one of daring to be different.

Superficially, taking a different tack isn't that hard to do in itself, but it does take some fortitude and it absolutely depends on the patience and trust of client investors. Because of this, I always try to be clear and

transparent in what I am doing and thinking - in order to earn that trust.

If you ever have questions or comments along the way, please always feel free to reach out - that's what I am here for.

As always, thanks for your support!

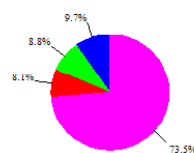
David Robertson, CFA
CEO, Portfolio Manager

Asset allocation

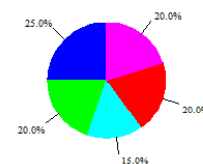
As I mentioned in the last Areté quarterly report, asset allocation is going to replace portfolio characteristics because it is more meaningful for understanding the All-Terrain strategy.

In the current actual allocation, cash is by far the largest position followed by stocks and gold. While the target allocation suggests several more transactions will be necessary, it is more useful to consider that allocation as a guideline than as a definitive target. For example, the target allocation is most indicative when valuations and opportunities among traded securities are generally in line with historical averages. Because those conditions do not hold today, the practical target allocation will have lower weights of financial assets.

Actual Allocation



Target Allocation



Another factor to keep in mind is the asset classes that are shown are not definitive or mutually exclusive of one another. As I have mentioned, gold mining stocks correlate more closely with gold than with stocks,

and some securities like the ETF, SPD, are literally a combination of stocks and inversely correlated assets.

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

Going forward, one of the top priorities will be finding attractive inflation hedges and deciding when to add them. Since commodities and energy have had huge runs, gold mining remains the single area with the most interesting ideas. There are a lot of things on the radar, however.

Transactions review

There were three transactions in quarter. First, the remaining position in DVA was sold. The stock was a great performer and exceeded target expectations. It was also vulnerable to rising rates, among other things, which made it an easy candidate for selling.

In addition, two more gold stocks, AEM and OR, were added. Gold stocks still look like one of the few fairly attractive areas in the market. These stocks, especially AEM, have been targeted for some time. The inception of the All-Terrain strategy and its greater baseline allocation to gold made these easy ways to increase exposure.

Performance review

As investment strategy transitions over to the All Terrain strategy, there will be some

changes in performance evaluation, but many of the general principles will remain the same.

For example, the search for undervalued assets will remain the same, although the scope of that search will expand significantly from the universe of US mid cap stocks to a much broader universe of publicly traded securities and funds.

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

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

The Areté All-Terrain Allocation (ATA) strategy really started at the end of August, but performance is reported for the entire quarter in order to provide continuity.

While the strategy was not fully implemented in September, it is still easy to see the potential benefit it provides over a balanced portfolio. In September, the ATA strategy returned -1.78% (net of fees) while VBIAX returned -3.12%. Clearly, it helped to have cash in a down market whereas VBIAX was hurt by losses in both stocks and bonds.

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

Areté Asset Management, LLC
All Terrain Composite
June 30, 2021 - September 30, 2021

Period	Gross-of-Fees Return (percent)	Net-of-Fees Return (percent)	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 (\$)
			Index Fund (percent)						
2021									
July	0.15	-0.10	1.49	2	NA	599,635	599,635	100%	1,185,806
August	0.66	0.66	1.67	2	NA	603,591	603,591	100%	1,192,535
September	-1.78	-1.78	-3.12	2	NA	592,841	592,841	100%	1,440,234
Q3	-0.99	-1.23	-0.04	2	NA	592,841	592,841	100%	1,440,234

Areté Asset Management All-Terrain performance composite disclosures follow:

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.

Areté Asset Management All-Terrain performance composite disclosures continued:**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” if its equity composition is greater than 90% of the equity composition of the composite. Each portfolio will remain in the composite until its equity composition becomes less than 90% of that of the composite. 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 allocation strategy 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.