

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

As I mentioned last quarter I thought the timing for starting up the All-Terrain

Allocation strategy was good and I continue to believe that. While the benchmark VBIAX fund had a very strong October and a fairly strong December, its weaknesses were laid bare late in 2021 and early this year. With both stocks and bonds getting hit as long-term bonds rose, it is clear to me that the notion of a 60/40 index as being “safe” is going to get sorely tested.

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On a similar note, I believe the prospects for Areté are as strong as they have been in quite some time. As I have mentioned many times in the past, market opportunities that Areté are well suited to exploit correlate closely with business opportunities. Further, an environment in which investing is more difficult places higher value on the experience and expertise Areté brings to the table.

When the market goes down, or gets volatile, or surprises investors in other unpleasant ways, people want answers and explanations, not just statements with red ink and a busy signal from a customer “support” desk.

In addition, since the financial crisis in 2008/9, common trends in the market have

been extraordinary monetary policy, the proliferation of passive investing, modest inflation, and a strong upward trend in both stocks and bonds.

In such a benign environment, the most successful actions have been to ignore risk and take on maximum exposure to financial assets. Many investors have done exactly this. There has never been a better time to completely ignore investment fundamentals.

Until now anyway. The big honking problem with completely ignoring fundamentals is that it relies entirely on the intent, and ability, of others to keep asset prices artificially afloat. By definition, that cannot last forever.

Now, with inflation emerging, the game is changing. Approaches that have worked so well in low inflation are going to confront headwinds of similar magnitude with higher inflation. Just as huge infusions of liquidity propelled asset prices on the way up, reductions in liquidity will cause asset prices to falter.

It will take time for investors to realize this. There will be ups and downs along the way. What will become increasingly clear, however, is that many investor portfolios will not only not be gaining any more, they will be falling further and further behind.

In addition, the advisor community will have a hard time migrating clients quickly enough. Most investors are uncomfortable with change and that discomfort poses a business risk. Advisors can choose between recommending big portfolio changes to adapt to inflation (but losing clients in the process), and changing the portfolio slowly,

(but underperforming and eventually losing clients in the process).

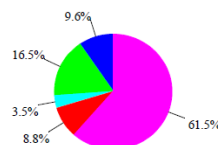
These are going to be tough times for investors and I suspect there will be a long process of digesting this reality. Many people will be ticked off and many will refuse to change. For those who are curious and recognize the need to adapt, however, Areté will be there to help.

David Robertson, CFA
CEO and founder, Areté Asset Management

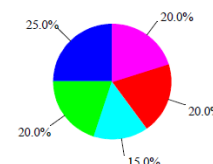
Asset Allocation

In the current actual allocation cash is still the largest position followed by gold and then stocks. Relative to last quarter, the cash portion is smaller as funds were deployed to increase positions in the gold and inverse correlation categories.

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 about finding attractive assets and creating thoughtful diversification rather than about speculating which hot stock may do well.

As a result, in an environment in which monetary remains extremely accommodative, but in which liquidity conditions are likely to become far more

problematic, it makes more sense to be patient than to chase ideas.

As with last quarter, the top priorities remain the same, namely finding attractive inflation hedges and deciding when to add them. Since commodities and energy have had huge runs, gold mining remains the more attractive area for now. I expect slowing growth to create some opportunities in the next several months, however.

Transactions review

There were three transactions in quarter. Two involved adding to gold at a time when gold prices are still attractive. This has been an ongoing theme and gets the sector weight close to its longer-term target.

The third transaction involved a new ETF from Simplify Asset Management which is an interest rate hedge. This is interesting because interest rate risk is one of the biggest risks in the market right now and it is unusual to be able to hedge it relatively easily. Being able to do so, however, also contributes greatly to portfolio diversification. Finally, the hedge is attractively priced. As a result of volatility being so low, the options used in the fund are priced attractively.

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.

Since the Areté All-Terrain Allocation (ATA) strategy started at the end of August, performance is reported from that date.

For the fourth quarter, the ATA strategy returned -0.2% (net of fees) while VBIAX returned 2.22%. The underperformance was driven primarily by the months of October and December during which VBIAX had strong performance on the back of stocks hitting new all-time highs. Due to the large cash position, the ATA strategy did not benefit materially from these moves.

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

Arete Asset Management, LLC
All Terrain Composite
August 31, 2021 - December 31, 2021

Period	Gross-of-Fees Return (percent)	Net-of-Fees Return (percent)	Vanguard balanced Index Fund (percent)	Number of Portfolios	Internal Dispersion (percent)	Total Composite Assets (\$)	Composite Assets With Bundled Fees (\$)	Percentage of Composite Assets With Bundled Fees	Total Firm Assets (\$)
2021									
September	-1.78	-1.78	-3.12	2	NA	592,841	592,841	100%	1,440,234
October	0.51	0.26	4.03	2	NA	594,348	594,348	100%	1,443,316
November	-1.03	-1.03	-0.75	3	NA	822,082	822,082	100%	1,431,088
December	2.41	2.41	2.18	3	NA	841,887	841,887	100%	1,460,255
Q3 (Sept)	-1.78	-1.78	-3.12	2	NA	592,841	592,841	100%	1,440,234
Q4	1.87	1.61	5.51	3	NA	841,887	841,887	100%	1,460,255
YTD	0.06	-0.20	2.22	3	NA	841,887	841,887	100%	1,460,255

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.