Marble Harbor Investment Counsel, LLC
Excerpt from
Second Quarter, 2013 Letter

Dear Client:

While sitting in my office one rainy day as the market was roaring ahead, I began looking at the charts of companies held in our portfolios. With the exception of some technology companies that had flown to astronomical highs during the tech bubble of 1999-2000, most of the stock prices of companies in our portfolios were at 20, 30 and even 40 year highs. In some cases, these stocks lost as much as 50% of their market value during the Great Recession of 2008-09. So, in a relatively brief span of four years, not only did these investments recover their (paper) losses, they continued to new highs. Clearly, the benefit of long-term investing in high quality companies is evident. As the market began a bit of a swoon at the end of June, your companies proved to be more resilient than the market.

The term for these wide swings in stock prices is commonly called volatility and to some, it represents the risk of owning stocks. It is a popular misconception that owning equities is by definition risky. It's an even bigger misconception that risk can be measured by volatility. Volatility itself is not risk, but rather how we react to volatility is where the risk lies. Panicking and selling stocks when the market declines can lead to a permanent loss of capital, potentially unnecessary payment of capital gains taxes and loss of current and future income. It also amounts to market timing, which tends to be a fool's errand. Often when the price of a good company falls, it may be the time to step back and recognize that the market is just not pricing the stock at what it is really worth and may be providing a terrific buying opportunity. So, volatility can actually be your friend.

We often refer to our investment philosophy as investing in strong businesses rather than just buying and selling stocks. One way to evaluate these businesses is their ability to generate cash that can be either reinvested or returned to shareholders. Companies that can grow revenue and earnings during difficult economic times can also continue to raise dividends even when the price of the stock is declining. The stock's movements don't necessarily reflect the health of the *business*. This certainly bodes well for a rebound in the stock's price when other investors recognize how well the company is doing. It may be difficult to "keep your head when all about you are losing theirs" but that is just the time when consistency of philosophy pays off: The rebound in the market value of your companies reflects this discipline.

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