

I Can See Clearly Now...

By Mariko Gordon

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Choosing a weird name like Daruma for our company has had a couple of unexpected bonuses.

For one, it's memorable. You don't forget what you can't pronounce. (And yes, you Japanese speakers, I know it should be "DA-roo-mah" not "Da-ROO-mah," but I'm not going to torture my fellow Americans any more than I have to.)

For another, the name Daruma came bundled with a prefabricated New Year's ritual. That's because in Japan, it's a tradition to set goals for the coming year with the help of a papier-mâché Daruma, filling in one eye when the goal is set, and filling in the other when the goal is reached.

At year-end, regardless of success, the Darumas are returned to temples where they are burned and new ones are purchased. (Very clever this - a consumable, recurring revenue stream keeps both temples and papier-mâché artisans swimming in yen!)

Here in New York City, we Darumaites fill in an eye on the first work day of the new year, write out our individual goals for the year to come, and seal them in an envelope. Since day one, my goal has always been the same: beat the benchmark by at least 500 basis points (anything less makes me extremely cranky).

And the same way all Darumas (failed or successful) return to the temple every year, we go through a performance postmortem annually as well, whether we beat our benchmark or not.

This year, however, I had a cunning plan for enhancing this process: since we have a GIPS verification and a periodic third-party compliance review performed, why not have an *investment process review* performed by a disinterested party as well?

After all, an outsider's perspective has proven to be valuable in those other parts of the business. Being introduced to new tools and best practices and benchmarking ourselves against similar firms ensures that we will bring our best game in those areas.

One problem: unlike the established fields of GIPS verifiers and compliance auditors,



"investment process auditor" is not a card-carrying profession. It's not easy to find a trustworthy person who is a proven stock picker, a continuous improvement data geek experienced at picking apart performance, and someone who knows the interaction effect of an investment team.

Enter my buddy Dan S. who not only fit the bill perfectly but whom I've known since we worked together back in the Pleistocene. He conveniently had some downtime in between gigs and was getting underfoot at home so, much to his wife's relief and mine, he signed on to help with our year-end review.

Now mind you, it's not easy having someone rummage through the investment equivalent of your underwear drawer (is that a purple sequined thong?!). But when you're in the trenches, it can be hard to shift perspective and see the bigger picture.

And while we had a lot of data to prove what we did well and what we needed to work on (thanks to having had every investment decision made since July 28, 1995, tracked and tabulated by the fine folks at [Cabot Research](#)), it was harder to see the *qualitative* reasons for those strengths and weaknesses.

Our intention in tapping Dan's expertise was to add an outside perspective to our many working hypotheses regarding how we came by our numbers - I wanted to be sure we weren't drinking our own Kool-Aid.

So what did Dan discover? Lots. Much of which we intend to share in future editions of this newsletter.

For today, however, the message is simply this: there is a lot to learn by bringing in an objective third party to weigh in on one's investment process. Specifically, Dan's analysis showed that:

1. Disinterested parties bring a detached perspective that is impossible to come by in-house.

They don't know what the sacred cows are and they can ask the obvious, "I'm an alien from Mars" questions that hold all the answers and that don't even occur to us in the first place (because we are so in the weeds).

2. Old data can contain fresh insights.

We've sliced and diced our performance, trading and characteristics data time and again. Every time we do so we find something new to ponder. An outside "auditor" brings this to yet another level, if only because they haven't lived the data and told themselves stories about it. An outsider comes up with a fresh narrative.



3. Pictures help with pattern recognition.

While Dan is a superb stock picker, always well-grounded in the fundamentals, he also uses charts to source ideas and to monitor what's baked into a stock price in terms of supply and demand.

"Seeing" our performance and trading data overlaid onto stock charts allowed us to more easily understand our patterns. It's not just slicing and dicing data but also presenting the data in more than one format that's useful.

Bringing Dan in has shown me a lot, both in terms of our investment process and about the value of an outside perspective. And while I know that when I pick up the Sharpie to fill in the eye of the 2012 Daruma my goal will still be to beat the benchmark by at least 500 basis points, now I will do so with fresh insights.

May 2012 be happy, healthy and prosperous for you!

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