



Building a Portfolio, Due Diligence and "Les Trois Mousquetaires"

By Alan Snyder

With the holidays being a fun time of year, I pondered what persona an expert who has mastered due diligence and portfolio construction might exhibit. While the reindeer pranced, it was impossible to narrow the archetype to just one person. Alexandre Dumas' *Three Musketeers* wound up providing inspiration and rescue to my thoughts. Although to set your mind at ease, I don't claim to be D'Artagnan.

Our Athos, Porthos and Aramis:



MARCO POLO



"PEG LEG" SMITH



SHERLOCK HOLMES

Marco Polo, the 13th century Venetian trader and explorer, searched his world for treasure and became very wealthy in the process. Traveling the less beaten path, he sought unique opportunities with balanced diversification. He may have been one of the earliest investors in niche strategies with the patience to see them through.

"Peg Leg" Smith, a trapper and early western frontiersman, was possibly the most famous California gold prospector. He suffered great deprivation in his monomaniacal pursuit of this precious metal, but kept on going. It was a close contest in selecting Peg Leg over James Marshall, who discovered Sutter Creek and started the California Gold Rush, or Billy

Barker, who purportedly found the most gold yet died penniless from his wastrel ways. Yes, living in California created some bias. All three prospectors were indefatigable in their pursuits, a key requirement for finding the best investments when coupled with the requisite research to improve the odds of success.

Lastly, Sherlock Holmes becomes a clear-cut choice. While a fictional character created by Sir Arthur Conan Doyle, his sleuthing prowess knows no peer. His power of observation, deductive reasoning and uber skills across many cases prove he was not a one trick pony.

Wrap your mind around utilizing these talents to structure a sound portfolio, balanced between risk and return, and created with deep conviction stemming from thorough due diligence:

Global perspective
Open to new ideas
Seek highest value
Relentless pursuit

Deductive reasoning
Consider all clues/tells
Replicable intellectual process
Implacable patience

Would our three musketeers have avoided the recent debacle of Platinum Partners, definitely not eponymously named? Six Platinum executives were arrested and charged with fraud (among other things) in a 48-page criminal indictment. The partnership gated and then declared bankruptcy during late summer, claiming that there were more withdrawals than could be met, yet maintained that the portfolio would recover. Allegedly, \$1 billion has gone missing.

Platinum generated double-digit returns for years with shockingly little volatility. The investments were generally in loans. Shinnecock briefly considered a position in Platinum, but cursory diligence happily led us to believe it was “too good to be true.”

With a deeper dive, our troika would have noted:

1. Sketchy valuation policies
2. Portfolio illiquidity notwithstanding flexible withdrawal terms
3. Intercompany loans
4. Affiliates dealing among themselves
5. Asset blowups
6. Litigation
7. Dissatisfied borrowers

As reported in the press, the subsequently uncovered hidden payments encouraging independent investors to invest would not have been knowable beforehand by a diligencier. Possibly all seven of the issues above might not have been found. However, any one of them would have been a red flag.

In short, great returns should not mean a suspension of disbelief. Due diligence and careful portfolio construction takes time, money and hard work. Nevertheless, it is truly sad to learn of investors who lost all of their money in Platinum or Madoff.

Diversification protects against single-point failures. This critical portfolio consideration safeguards against the unexpected because ***no*** due diligence process or market forecast is perfect.

In our earlier missives, we have shared some of Shinnecock's process with more to come, which might be useful for our readers and investors to help avoid the calamity of a Platinum Partners. We strongly believe this should be applied to us and other investments (even if not with us, ha).

We wish all a great new year, which is guaranteed to have its own unique challenges. And, many thanks to our readers who offer comments, thoughts and suggestions.

Happy New Year and Happy Investing!