
*Tocqueville Asset Management L.P*

## THE REAR LONG VIEW

***Although the purpose of this paper is not to discuss performance per se, please make sure you read the disclaimers at the bottom.***

Tocqueville's largest account has recently been approaching the $1 billion landmark. I have managed or co-managed this account since the end of 1974: first with my partner Christian Humann at Tucker Anthony, then alone and, since 1992, with the help of my partners at Tocqueville Asset Management.

It is the only account for which we have audited statements going back thirty years and, although I always remembered it being worth around $12 million when we took over its management, the audited record showed it multiplying by less than 38 times from the end of 1976 to the end of 2006. Until recently, something did not gibe: 38 times $12 million is "only" $444 million. Then, while doing some file cleaning, my secretary uncovered an old, hand-made (un-audited) performance analysis, which included the years 1975 and 1976.

Indeed, the account *was* worth less than $12 million at the end of 1974. But in its first two years it gained a touch over 78%, as the world's stock markets rebounded spectacularly from the depths of the 1973-1974 bear markets. When the measuring period is lengthened to cover the thirty-two years since the end of 1974, instead of the thirty years since 1976, the portfolio is shown to have multiplied by a bit more than 67 times, which after adjusting for capital received and disbursed is generally consistent with both my recollection and the auditors' work.

A look back at the thirty-two year record calls for some remarks:

**A dollar ain't what it used to be.** In fact, thirty-two years ago one dollar used to purchase roughly four times what it does today. Our client's *true wealth,* as opposed to his "paper worth", therefore increased by 17 times – not 66 times – over 32 years..

**The miracle of compounding.** Albert Einstein once stated that "the most powerful force in the universe is compound interest". Nothing *relative* about this: he was right on the button! (This is the only finding of Einstein's I am in a position to confirm).

Over 32 years, our largest account grew at an average compound rate of 14.1% (after charging management fees). This sounds pretty good but, in fact, it is only 0.8% more per year than the 13.3% achieved by the S&P 500 index when the index's dividends are assumed to be automatically re-invested.

Was a mere additional 0.8% per year worth all our efforts? Judge for yourselves: over thirty-two years, $12 million growing at 13.3% per annum will become $652 million,

whereas if it grows at 14.1% per annum, it will become $817 million – a $165 million difference on an initial $12 million investment!

**Performance is uneven.** There will always be some great stock market years, followed by mediocre or even negative ones.

Surges like the one in 1975-1976 have not been that exceptional. There were other outsized gains throughout the period: for example, 70% in 1979-80; 65% in 1982-83; 105% in 2003-06. It is thus very important not to miss on these periods of large gains.

But, to average to 14.1% per year, there must have been some more subdued years – and there were (see the appendix). One satisfaction we take from our long-term record, however, is that actual *down* years were few and rather mild: -5.3% in 1977; -1.4% in 1984; -1.0% in 1990; -4.1% in 2002.

**The calendar makes it look better.** That being said, customarily used annual performance figures can be misleading. A well-known mutual fund manager, whose sixteen-year streak of beating the S&P 500 index every year was finally interrupted in 2006, once commented that at least some of his extraordinary record was due to the vagaries of the calendar. In many *interim* periods, he pointed out, his fund had performed poorly or actually declined. The same could probably be said of most managers with superior long-term records, including us.

It is good to remember that, as I argued in an earlier paper, "volatility is not risk". Risk comes either from shaky investment fundamentals, unforeseen outside factors ("black swans") or gross discrepancies between stock prices and companies' values. From that perspective, short-term or medium-term volatility (unless extreme) is mostly "noise" to be largely ignored. As Warren Buffet is fond of saying, "time is the investor's friend and the speculator's foe".

**Timing or not timing the market: that is not the question.** I don't know of any investment manager who has made a lot of money over a significant period of time (several major cycles) by timing the market. In fact, various studies stress the opportunity loss of being un-invested during market advances that, generally, are near-impossible to forecast – at least in their timing. One such study,from Townley Capital Management and the University of Michigan, covers thirty years. It shows that $100 invested in the stock market in 1963 would have earned $2,333 by 1993. But missing the best 90 days of that period (*an average of 3 days a year*) would have cut the earnings from $2,333 to just $110.

Some of my partners feel a responsibility to be more or less fully invested at all times. I don't feel as strongly about this. But all of us always give precedence to stock picking over economic or market considerations. We follow contrarian-value criteria to identify and select stocks globally: If we find compelling new ideas, we buy them regardless of our market views; if we don't, we do not buy and cash tends to build up as other stocks in our portfolios reach full value and are sold.

Differences among us really better qualify as nuances about the definition of "compelling idea", especially when we view stocks as generally overvalued. But interestingly, in the particular case of the account that is the object of this nostalgia trip, and for which we use several in-house managers, my observation is that, though our individual performances have diverged at times, they show a surprising convergence over the longer term.

**Catch a rising star.** Receiving fresh cash to manage in a rising market constitutes a conundrum.

Whether you invest before or after a stock market surge makes a big difference. As we observed at the start of this paper, investing at the end of 1974 yielded an average annual return of 14.1 % over the 32 following years, while investing at the end of 1976 (after a two-year surge) yielded an average annual return of only 12.9% in the following 30 years. Even though we cannot "time" the market, there are some guidelines we can, and do, follow.

At any particular point in time, our existing portfolios typically are made up of 1) cheap stocks at or near their buying point; 2) stocks that have moved up, but are neither dirt-cheap nor excessively overpriced; and 3) stocks that are approaching our selling target price. For a new account, stocks in the first category clearly can be bought immediately and those in the third category should not. For stocks in the second category, however, the decision is more difficult. Often, we will buy some partial positions but, sometimes, we will just wait for a better opportunity.

In such situations, some view of where we stand in the market cycle can be helpful. A glance at the table below, derived from a study by Crestmont Research, makes it fairly clear that it is generally better to buy when prevailing price/earnings ratios are low than when they are high.

| 87 Twenty-Year Periods Ending 1919-2005 | | |
|---|---|---|
| **20-Year Total Return Average** | **Average Beginning P/E** | **Average Ending P/E** |
| **3.2%** | 19 | 9 |
| **4.9%** | 18 | 9 |
| **5.3%** | 12 | 12 |
| **5.6%** | 14 | 12 |
| **6.7%** | 14 | 14 |
| **8.3%** | 17 | 18 |
| **9.2%** | 15 | 17 |
| **10.4%** | 11 | 20 |
| **11.7%** | 12 | 22 |
| **13.4%** | 10 | 29 |

This observation, though not perfect, is consistent with our contrarian-value approach. We cannot "time" the market but we can identify periods when the ratio of perceived risk to potential return augurs poorly for future stock market gains. In such periods, (usually ones of high price/earnings ratios), I believe that "constructive inaction" is the best response: keep actively looking for new, compelling ideas and, until you find them, buy nothing. On the other hand, if you do find them, forget about the "market" and buy them.

**If you are so smart…** As value-contrarian investors, we do worst when the market is carried away from its fundamentals by a strong upward momentum. In the technology and Internet bubble of the late 1990s, for example, our selected account badly trailed the S&P 500, advancing 101.3% from 1994 to 1999, while the index surged 251.3%. Fortunately, before our clients lost patience with our "discipline", the bubble burst and the market suffered three consecutive years of decline while we kept plodding along. As a result, the account finished the 1994-2003 cycle up 97.1% against the 82.1% chalked up by the S&P 500 – with a lot less volatility.

After this episode, over lunch, another client recalled: "I knew all along this was crazy, but I must say that, quite a few times I wished François were a bit crazier. Now I know why I stayed with Tocqueville."

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Upon reading a draft of this paper, one of my younger partners claimed to be surprised: I seldom mention performance and, in fact, advocate that we not publicize it too much, because "performance chasers" seldom turn out to be very desirable clients. I answered him that doing so once every thirty-two years is acceptable, and that when I do it next, he probably will be retired.

In fact, this article was not about "relative" performance and the futile competition that our industry tends to engage in. It really was about putting wealth protection and growth into historical perspective, and drawing from that exercise some pearls of wisdom. So, here they are:

*There are no miracles or magical black boxes in investing for the long term.*

*Patience, discipline and common sense will always prevail over restlessness and "genius".*

*For the rest, we can trust compound interest.*

**Francois Sicart**, in Paris
June 25, 2007

*This article reflects the views of the author as of the date or dates cited and may change at any time. The information should not be construed as investment advice, nor is there any guarantee that any projection, forecast or opinion will be realized.*

*The returns discussed in this article are based upon the annual returns for each of the last thirty-two years for fully-discretionary accounts managed by Tocqueville Asset Management and François Sicart, founder and Chairman, for its largest client. {Also referred to as the "Multi-Strategy Core Private Client Account".} The client account predates the formation of Tocqueville on January 1, 1990, and was managed by Mr. Sicart initially as an executive of Tucker Anthony, R.L. Day, Inc. beginning in 1974 through the formation of Tocqueville. Other accounts were managed by Mr. Sicart during the same period, and may have had different investment objectives and achieved different results. A new account with similar investment objectives and style may not achieve similar results.*

*Performance data quoted represents past performance and does not guarantee future results. The Total Return of the client account, other than for the first two years, is calculated in conformance with the AIMR-PPS methodology. With the exception of the first three years, it is audited, but is not covered by the report of independent accountants. The US equities account segment of the client account is neither audited nor covered by the report of independent accountants. The returns were calculated using a time-weighted monthly rate of return formula and are presented net of advisory fees, commissions and other expenses and, assumes reinvestment of capital gains and dividends. The accounts are valued monthly and transactions are recorded on a trade date basis. Dividend income is recorded on a cash basis. Cumulative rates of return for multi-year periods are calculated by linking the annual rates with such periods. The annualized rate of return is equivalent to the annual rate of return which, if earned in each year of the indicated multi-year period, would produce the actual cumulative rate of return over the time period.*

*The client account includes investment in foreign securities which involve greater volatility and political, economic and currency risks and differences in accounting methods. The S&P 500 Index is a market-value weighted index consisting of 500 stocks chosen for market size, liquidity and industry group representation. The S&P 500 Index returns include reinvestment of dividends. The volatility and other risk characteristics of the S&P 500 Index may be greater or less than those of the client account. You cannot invest directly in an index.*

# Appendix

| Year | Tocqueville Asset Management (%) | S&P 500 Index (%) | Tocqueville Cumulative Returns (%) | S&P 500 Cumulative Returns (%) |
|---|---|---|---|---|
| 1975 | 36.34 | 31.51 | 36.3 | 31.5 |
| 1976 | 30.59 | 23.57 | 78.0 | 62.5 |
| 1977 | -5.30 | -7.41 | 68.6 | 50.5 |
| 1978 | 12.70 | 6.39 | 90.0 | 60.1 |
| 1979 | 35.50 | 18.20 | 157.5 | 89.2 |
| 1980 | 25.50 | 32.27 | 223.1 | 150.3 |
| 1981 | -0.40 | -5.01 | 221.8 | 137.7 |
| 1982 | 30.00 | 21.44 | 318.4 | 188.7 |
| 1983 | 27.30 | 22.39 | 432.6 | 253.3 |
| 1984 | -1.40 | 6.10 | 425.2 | 274.9 |
| 1985 | 27.30 | 31.57 | 568.5 | 393.3 |
| 1986 | 2.50 | 18.56 | 585.3 | 484.8 |
| 1987 | 4.50 | 5.10 | 616.1 | 514.6 |
| 1988 | 20.90 | 15.80 | 765.8 | 611.7 |
| 1989 | 14.60 | 31.69 | 892.2 | 837.3 |
| 1990 | -1.00 | -3.10 | 882.2 | 808.2 |
| 1991 | 12.80 | 30.47 | 1008.0 | 1085.0 |
| 1992 | 14.30 | 7.62 | 1166.4 | 1175.3 |
| 1993 | 21.90 | 10.08 | 1443.7 | 1303.8 |
| 1994 | 2.03 | 1.32 | 1475.1 | 1322.4 |
| 1995 | 22.95 | 37.58 | 1836.5 | 1856.9 |
| 1996 | 19.35 | 22.97 | 2211.3 | 2306.4 |
| 1997 | 14.06 | 33.36 | 2536.2 | 3109.1 |
| 1998 | 2.57 | 28.58 | 2604.0 | 4026.3 |
| 1999 | 17.25 | 21.04 | 3070.4 | 4894.5 |
| 2000 | 5.68 | -9.10 | 3250.5 | 4440.0 |
| 2001 | 1.79 | -11.89 | 3310.5 | 3900.2 |
| 2002 | -4.14 | -22.10 | 3169.3 | 3016.1 |
| 2003 | 43.12 | 28.68 | 4579.0 | 3909.8 |
| 2004 | 10.14 | 10.88 | 5053.4 | 4346.1 |
| 2005 | 11.94 | 4.91 | 5668.8 | 4564.4 |
| 2006 | 16.58 | 15.79 | 6625.2 | 5300.9 |
| 2007 | 9.93 | 5.50 | 7293.0 | 5598.0 |
| 2008 | -33.08 | -37.00 | 4847.4 | 3489.7 |
| Annualized | 12.16 | 11.11 | | |
| Shaded = Periods of out Performance | | | | |

Note : The article, written in June 2007, reflects data up to 2006.