FROM SPECULATIVE CONTAGION TO THE GREAT RECESSION

A DECADE OF DELUSIONS

FRANK MARTIN

INTRODUCTION BY JOHN C. BOGLE

NATIONAL BESTSELLING AUTHOR

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of Delusions

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Frank K. Martin

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May the few who profit from this book be
mindful of the many who cannot.

Contents

Foreword

Frank Martin is one of the wise men of American finance. No, he doesn't have the public profile of the late Benjamin Graham and Peter Bernstein, or Warren Buffett, Paul Volcker, and Henry Kaufman, but he stands firm and tall with them in the pantheon of my heroes and mentors. This book, *A Decade of Delusions*, will make it clear both why I admire Frank and why I commend his wisdom to you.

The first thing you should know is that Frank Martin is the founder (and remains the intellectual leader) of Martin Capital Management, an investment advisory firm established in 1987 and located in Elkhart, Indiana. Yes, he manages "other people's money" (OPM). But what differentiates him from most other advisors (and nearly all advisors to mutual funds) is that he manages the wealth entrusted to his care by his clients under substantially the same investment principles and strategies as he manages his own wealth; he takes essentially the same risks with his clients' money as with his own. Investing under the principle of "my own money" (MOM) makes him more than an advisor to his clients; it makes him their partner in every sense of the word.

Those of us who have been plying the investments trade over the past few decades have been eyewitnesses to one of the most remarkable eras in U.S. financial history. We've seen the bubble in the "New Economy" of 1996 to 2000; the (inevitable) stock market crash that followed; the ensuing (likely inevitable) recovery; the ultra-speculative financial Bubble of 2005 to 2007; and the (again, inevitable) crash of our investment system, our economy, and our society. Frank Martin was one of us, but with a difference. He pondered each event, looked for causes, considered outcomes, contemplated resolutions, and drew both on the wisdom of the ages and on the fundamental mathematics of business and investing, turning information into knowledge, then into his own wisdom.

What was the author thinking and doing during those waves of hope and fear, during that environment of greed and speculation? Happily, we know the answer to that question. For he wrote (and wrote and wrote) about the saga as it unfolded in the markets. An assiduous chronicler of those events, Frank prepared annual reports to his clients that carefully described the thinking, the actions, the policies, and the strategies that drove his and his firm's investment decisions. These annual reports are lengthy and deeply detailed, but they provide precisely the kind of information that intelligent investors have a right to expect—no, to demand—from their own wealth managers. Were I not a financial professional with substantially 100 percent of my wealth invested in the Vanguard funds, that is exactly what I would expect from the manager of my own assets.

Commonsense Wisdom

I've read the Martin Capital Management annual reports for more than a decade now, ever since the 1998 edition. These annual reports, through 2004, were packaged together in Frank's first book, *Speculative Contagion*, published in 2006. Largely an anthology of his earlier reports, the book's publication immediately preceded the financial crisis that would soon unfold. I marveled not only at the book's prescience, but at the commonsense wisdom that helped to cut through the dense fog of infinitely abundant information that, paradoxically, has clouded our vision, and the intensity of emotion that has plagued investor behavior as we act on those eternal enemies of long-term investing—hope, greed, and fear.

Frank's philosophy of long-term investing in companies (not stocks as such, a critical distinction) minimizes such counterproductive behavior. After *Speculative Contagion* was folded into *A Decade of Delusions*, the new material takes us through the rest of the decade just ended. Some of Frank's chapter headings and subheadings will leave you little doubt about the direction and force of his opinions (in the interest of continuity, I'll omit the quotation marks): The Power of Popular Delusions. Only Fools Rush In. The Rogues Gallery. The Great Abdication of Fiduciary Responsibility. S&P 500 Earnings Dissected. Of Pawns, Guinea Pigs, and "Retail Investors." The Mathematics of Patience. The ARM-ed Robber. The Perfect Storm Redux. The Misalignment of Incentives and the Opaque World of High Finance. Back to the Age of Innocence? "This Time Is Different." If these excerpts suggest that Frank is fun to read—as well as stimulating—you understand my point.

But what I like most about Frank Martin's voluminous output is his penchant for quoting the words of others, always spot-on in relevance. Ben Graham and Warren Buffett? You'll meet them inside. Lord Keynes, Cervantes, Bertrand Russell? They're here, too. General Patton and Ted Williams? Sure. Bonhoeffer, Minsky, Leibniz? If you've not known them before (perhaps likely?), you'll meet them here and enjoy their timeliness in our world of today.

A Decade of Delusions is not only a wise book, it is a deep book—deep with sound philosophy—and a fairly long one (except when compared to my own recent tomes!). But all that heavy intellectual baggage—greatly simplified and made relevant to the average investor by Frank's deft touch—is easy reading. To lighten your journey, the book is interspersed with illustrations, cartoons (with biting satire), and charts of the ups and downs in the Standard & Poor's 500 index that show just where "the market" was as Frank was writing and as you are reading—clearly marked "You Are Here."

The Proof of the Pudding

As it is said, "The proof of the pudding is in the eating," and the investment returns earned by Martin Capital Management (MCM) for its clients over the years have been solid.

Especially during this past decade of delusions, MCM's performance record is impressive on balance. But its year-to-year variations have been wide—just what you would expect from a firm holding strong principles and convictions. Frank was among the few advisors who eschewed the euphoric buying frenzies that created recent equity Bubbles. His investors' allocation to equities was 30 percent or less in late 1999 and again in mid-2007. As a result of this flexibility—plus owning shares of corporations for their intrinsic value rather than, say, their price momentum—MCM earned its stripes. A timely and conservative posture offered excellent returns relative to the S&P 500 from 2000 to 2002, then lagged behind the powerful recovery of the index in the ensuing bull market of 2003 to 2007. But in 2008 and 2009, despite the sharp drop in the S&P 500, the MCM return was strongly positive.

There is a message here: Independent-minded money managers don't follow the crowd, aiming at high correlation with the stock market's shorter-term vagaries; they invest with the conviction and boldness required to take "the road less traveled by." Not only MCM but its clients must have the wisdom and the courage and (especially) the patience to focus on durable long-term values rather than fickle short-term stock prices.

No one can forecast with accuracy whether the MCM record will be similar, or better, or worse in the years ahead. But I am fully confident that—especially in the risk-infested world that we now inhabit—Frank Martin's investment principles are sensible principles (however implemented) for investors seeking to capture whatever long-term returns our financial markets are generous enough to provide for us, as well as to offer an anchor to windward against whatever short-term losses may be inflicted on us. I summarize these principles here:

- Performance goal: to maximize long-term portfolio returns, while strenuously avoiding the assumption of risks that might result in permanent loss.
- Investing in the basic asset classes: long-term, common-stock holdings; fixed-income securities; and cash equivalents, seeking the highest possible after-tax, risk-adjusted returns.
- Reasonable expectations: purchasing stocks as if buying into a private business.
- Minimizing risk and eschewing leverage.

- Minimizing conflicts of interest by having the firm's principals invest in substantially the same securities as the firm's clients.
- The firm's principals conducting themselves in their relationships with clients as if the roles could be reversed at any time, the ultimate ethical standard ("Do unto others . . .")—and striving for candor and forthrightness at all times.

So read *A Decade of Delusions* for wisdom, for insight, and for fun. I thoroughly enjoyed it, and I know you will, too.

John C. Bogle
Valley Forge, Pennsylvania
March 2011

Mr. Bogle, founder and longtime chief of The Vanguard Group, celebrates his sixtieth year in the investment profession on July 7, 2011.

Preface

S*peculative Contagion: An Antidote for Speculative Epidemics* was first published in 2006 and originated from my fascination with and skepticism about the widely embraced "Great Moderation," an economic era of predictable policies, low inflation, and tempered business cycles. The origins of the Great Moderation can be traced back to late 1987, when the economy barely flinched after the shock of the Dow Jones average's unprecedented and infamous 23 percent freefall on October 19. Quick intervention by Alan Greenspan, Federal Reserve chairman, who had been confirmed only two months before, likely stemmed the tide. But in doing so, he established an oft-repeated enabling precedent for what became known as the "Greenspan put," an implicit government guarantee against the consequences of financial and economic crises.

The original *Speculative Contagion*, its title a loud and clear warning bell, was published 18 years into the Great Moderation. Little did we know it was going to be a premonition of what two years later became known as the "Great Recession." During the prolonged spate of generally stable times, apprehensions about risk gradually faded as the economy—along with the market prices of popular asset classes of stocks, bonds, and real estate—continued to trend inexorably upward. The momentum of invincibility was so entrenched in the popular psyche that even the bursting of the "Great Bubble" in 2000–2002 did not restore an abiding respect for risk.

As *Speculative Contagion* was being published in 2006, it became evident that fallout from the Great Bubble's bursting was muted by monetary intervention and by a public all too willing to believe. The decline in stock prices did not rouse an aversion to risk but rather a cocksure belief that the economy and the capital markets were impervious to wealth-threatening, systemic calamities. The antidotes for speculative epidemics fell on deaf ears.

What was happening was fantasy. In 2002, leery of the near-term consequences of a possibly harsh but cathartic recession happening on his watch, the "second most powerful man in the world" once again took the path of least resistance. The Greenspan put was invoked. But it only bought some time—and ultimately at a huge social and economic cost.

The unintended side effect was a blitzkrieg of dubious, and sometimes extreme, financial innovations that became dangerously complex and interdependent. Investment banks, no longer structured as partnerships with open-ended personal liability, ratcheted up financial leverage until it spiraled out of control. This combination gave rise to a financial services sector whose high-octane incentives were so irresistible and so contagious that the epidemic could not be reversed except through self-destruction. The structured-finance products fabricated in this environment begot huge distortions in home prices and, to a lesser extent, those of marketable securities.

Flashing back to the latter half of the 1990s, market commentators more or less arbitrarily and, as it turned out, quite irresponsibly, asserted that a decline of 20 percent would constitute a bear market. This implied that investors and speculators alike need not anticipate anything worse. The approximate total market value of all domestic equity securities reached its apogee of $17 trillion, estimated from Wilshire 5000 data, in the spring of 2000. By the late fall of 2002, approximately $8 trillion of illusory, inflated value—roughly half of which can be attributed to the savaging of stocks making up the Nasdaq index—had disappeared into thin air as the Bubble burst. An antidote for a speculative epidemic? Not on your life. Retail investors' increasing home values soon compensated them for losses of the dot-com days. The financial wounds were salved, and the ever-more-dangerous disregard for risk morphed into a full-blown epidemic.

As a consequence, the bloodletting at the outset of the new millennium was only a prelude to the utter carnage between 2007 and 2009. The market value of U.S. stocks plummeted from $18 trillion to $7.9 trillion, but this time the disease migrated to other asset classes—and then to the economy at large. (Whether sustainable or not, another Fed-induced Bubble has spurred the market to regain 60 percent of the ground lost, and the aggregate value now stands, in November 2010, at $14 trillion.) According to Federal Reserve data, the market value of average Americans' most prized possession, their home, fell dramatically for the first time in modern history, from $22.7 trillion as of year-end 2006 to $17.1 trillion at the end of the second quarter 2010, a jaw-dropping 25 percent.

More worrisome, mortgages and home-equity loans actually increased marginally during the same time frame, from $9.9 trillion to $10.2 trillion. Even though the market value of U.S. stocks has at least partially recovered, the aggregate net worth of American households has sustained the most devastating body blow since the Great Depression. For that reason, the current economic contraction is unlike the typical "inventory" recession of the post-World War II era; in reality, what we are dealing with now is properly known as a "balance sheet" recession, which is significantly more problematic. As the three-year anniversary of the Great Recession approaches, it is becoming more and more apparent that when critical sectors of the economy are consumed with deleveraging their balance sheets, they are stubbornly unresponsive to government stimulus.

■ ■ ■

Speculative Contagion was a compilation of my published annual communiqués from 1998 to 2004. The concluding chapter, the 2004 annual report, left the reader in suspense, warning of an approaching tempest: A financial tropical depression had already formed and was gaining intensity. Two and a half years later, it raged into the worst financial and economic crisis since the 1930s. The prophetic section was titled "Marathon Endurance," the opening paragraph of which follows:

> The message throughout this report, summarized here, is that we are nearer the beginning than the end of the long secular transition from greed to fear, from exhilaratingly high prices to despairingly low ones, from irrational exuberance to level-headed rationality and perhaps (I say irrespective of how remote the possibility) from a financial economy to [a] real economy. Accordingly, we have, out of necessity, a heightened sense of vigilance, a pervasive but hopefully constructive skepticism.

Speculative Contagion was more than simply a chronicle of the first half of a decade of financial and economic reversals. Like the original work, *A Decade of Delusions* (the sequel) is anchored to mainstream historical data, events, and anecdotes that are analyzed and interpreted, real time, in terms of whether they confirm or impugn one of the observer's principal theses: that the foibles and follies of humanity are among our species' irrefutable constants. John Wiley & Sons' editors thought it a helpful study of how one might assemble from available evidence and data, and without benefit of hindsight, an accurate assessment that trouble is on the way. The devastating storm that uprooted our financial system and the economy during the last years of the decade had been visible on radar, but many chose to interpret the ominous blips as false echoes or simply ignore them altogether.

A Decade of Delusions aspires to capture a subtle shift in human behavior that may have undergirded what was outwardly manifested. Beneath what seemed like an increasingly reckless disregard for risk was *moral drift*, which may be remembered as the signature causative force of the "Lost Decade." Though I elaborate further on this important point in Chapter 7, allow me to say this much up front: The term *willful ignorance* is the desire for an action's intended result that is so all-consuming that one largely ignores the unintended effects. Of this transgression, many were conflicted but few convicted. Individuals and boards in positions of power and responsibility the past decade all too often sold their integrity down the river for financial gain.

■ ■ ■

This sequel builds upon the bulwark of the original. The 1998 through 2004 Martin Capital Management annual reports are largely intact. Most additions to the original text are bracketed; a modest number of changes to the original reports were added to improve clarity. In addition, substitutes were inserted without acknowledgment for duplicated pet words, phrases, or aphorisms; and the potentially annoying repetition of a number of key ideas or concepts (as might logically appear in seven discrete reports) was generally left unattended in order to maintain the flow of the text. Every effort was made to avoid omitting anything that might cast the narrative in a more favorable light than it deserves. Each annual report (organized in Chapters 1–7) told, in its own time and in its own way, how it felt to be pulled one way by the temptation to mindlessly join the crowd in its rush for paper gold and the other by the sometimes fragile convictions about what constitutes rational thought and behavior. *Speculative Contagion* concludes in Chapter 8 with insights gleaned from years on the front lines. More Darwinian than prophetic, they were presented as guideposts to help investors adapt to an ever-changing world, rather than predictions about just what those changes might be.

Chapters 9 through 11 draw from 180,000 of my words that were published during the second half of the decade in annual reports to clients, as well as in quarterly communiqués and other writings. I also use one of my FDR-esque "Fireside Chats" as the basis for the Epilogue. *A Decade of Delusions* thus embraces the entirety of 10 years of unrelenting speculative contagion. Chapter 9 includes the annual reports of Martin Capital Management from 2005 and 2006 when fundamental conditions deteriorated, even as housing and security prices continued their upward trend. The 2005 report is significant in its use of "The Perfect Storm" as a descriptive means of alerting clients to the dangers that likely lay ahead. It is a theme repeated and more closely analyzed in the 2006 annual report, culminating in Chapter 10, which is aptly titled "The Tipping Point." It might be said that in the 2007 quarterly communiqués and that year's annual report, the severe storm *watch* issued in preceding years was elevated to a severe storm *warning*. Here in the Midwest, residents of "tornado alley" are all too aware of the significant difference in these terms: A watch means conditions are right for the formation of damaging storms. A warning means the storm has been spotted and its arrival is imminent. Take cover.

Chapter 11 consists of annual reports from 2008 and 2009, which covered the early stages of a nation in the midst of a global financial maelstrom and ensuing meltdown. It was a time, hardly unexpected, of massive governmental intervention. However ill-conceived their actions, however ineffective their experimentations, however costly the ultimate consequences, government officials almost invariably feel compelled to intervene for political and social reasons. Centralization of control has enfeebled the once-free markets. According to the Business Cycle Dating Committee of the National Bureau of Economic Research (NBER), the Great Recession began in December 2007 and, apart from a possible easy-money-inflated bubble in risk assets, the economy remains unresponsive. As time passes, some will argue that if authorities had let the markets clear unimpeded, however terrifying in the short run, the consequences might have been a deeper but far shorter economic V. The point, however, is moot. To quote the chairman of the Federal Reserve Board, "There are no atheists in foxholes and no ideologues in financial crises." Was the massive Keynesian, monetary, and regulatory intervention part of the solution—or part of the problem? In short, were the financial crisis and the Great Recession the end? Or just the beginning?

For the record, on September 20, 2010, NBER determined that the recession ended in June 2009—after 18 months. It has been wrong before.

The Epilogue is intended to leave the reader with the notion that once the catharsis is complete, long-term investment will once again be recognized as the rational course. We won't know until long after the fact whether the speculative contagion has been purged. As baseball legend Yogi Berra once sagely observed, "It ain't over till it's over." Hard to argue with that logic. Consequently, the last word in this volume will undoubtedly disappoint those seeking a detailed and pinpoint forecast. Consistent with the rest of the work contained in *A Decade of Delusions*, the Epilogue represents the musings of an observer examining a single snapshot of the landscape in real time. The next frame in the larger motion picture has yet to be photographed and developed, and that is naturally cause for unease.

As an investment advisor prone to reflect on cause and effect, I came to work in the midst of the grand delusion every day of the past decade. I watched and wondered, sometimes nearly overcome with self-doubt, worrying that we as a firm were out of step with a new-era reality. At other times, I was modestly encouraged by some seemingly insignificant piece of evidence that gave us a sign, often little more than a fleeting assurance, that we had not lost our way, that our sense of historical proportion might eventually validate the vision we were pursuing for our clients and ourselves. It was a grueling experience.

It is hoped that the reader will discover a common thread woven throughout the book: Success is more likely to come to those who have some clue about the counterintuitive way that the thought processes and subsequent behaviors of crowds differ from individuals. There is a sound basis for the famous quote from the poet/dramatist Johann von Schiller, who once said, "Anyone taken as an individual is tolerably sensible and reasonable; as a member of a crowd he at once becomes a blockhead."

If one is to avoid the allure of the majority—or the mythical character "Mr. Market," as defined by Benjamin Graham in the pages that follow—one must have an understanding of the manic-depressive nature of this creature. One also should gain some awareness of an asymmetrical behavioral pattern common to the conduct of crowds as their collective state of mind tends to swing from extreme to extreme. I believe that there's a cyclicality to the world of finance that is more than mere coincidence and makes the study of history relevant. Books like *Extraordinary Popular Delusions and the Madness of Crowds* by Charles Mackay, LLD, put this propensity into a context that leaves the careful reader feeling that delusions are indeed endemic to the human condition.

Taken as a whole, *A Decade of Delusions* serves as my bully pulpit. I found it bordering on the unconscionable to live in close proximity to the latest incarnation of *Den of Thieves* (1992), James Stewart's chronicle of the Wall Street depredations of the 1980s, and not to speak out against the crimes and misdemeanors perpetrated by the "masters of the universe," aptly named by Tom Wolfe in *The Bonfire of the Vanities* (1987). Accordingly, throughout *A Decade of Delusions* the reader will encounter occasional tirades directed at the more flagrant violations of the standards of ethical conduct, rationalizing my outspokenness by turning to no less an authority than eighteenth-century Scottish economist and philosopher Adam Smith. The book that established economics as an autonomous subject and launched the economic doctrine of free enterprise, *An Inquiry into the Nature and Causes of the Wealth of Nations*

(1776), examined in detail the consequences of economic freedom, including the role of self-interest. As a moralist, Smith argued that the system of free enterprise was only as strong as the general ethical character of the society of which it was composed. Egregious ethical breakdowns, particularly the abuses of fiduciary trust and power at the highest ranks of corporate governance, frequently become the weak link in the economic chain. If the chain breaks, chaos is likely to reign. Dare I hold my tongue when the consequences of silence could be so dire?

Acknowledgments

Every tree that withstands tornado-force winds has unseen roots buried deeply in the soil. This book is the tree, but its roots nurture and strengthen it. Countless people are, collectively, the roots. Among those who bent their shoulder to the wheel to get *A Decade of Delusions* rolling, including those who critically read it: Keith Rockey and Bob Ellis; Adam Seessel, Zack Clark, and Jeff Robbins did blue-pencil editing; within my firm, analysts Aaron Kindig and Clint Leman, consummate, selfless team players, were invaluable in too many ways to enumerate, as was Gary Sieber, head of marketing, who, as a broadcast journalist, proved to be a man of letters as well. Kristen Myers-Smith, my assistant, ably played the role of juggler, keeping the pins aloft between and among all parties. Thanks to Lauren Silva, who, because of the high-tech digital world in which we live, provided impressive editing assistance without us ever having met face to face. Dan Shenk, proprietor of CopyProof, has left his indelible mark on every single page of the book: first by editing most of the missives when they were originally written, then proofing this manuscript with his characteristic attention to both detail and the big picture. And the good folks at Wiley demonstrated their professionalism at every turn as they took my sow's ear and turned it into a silk purse.

By chance in 1998 I happened across the work of cartoonist Bill Monroe. He was as pleased as I to have his artwork bring smiles to the faces of readers of a book that sought to treat the subject at hand as more than just the dismal science as it is often characterized. Still drawing at the age of 77, Bill would love to sell you fine art prints. See what he has to offer. His web site: www.monroeartist.com.

So that they aren't forgotten, the following acknowledgments appeared in *Speculative Contagion*.

> Al Auxier, Warren Batts, Edward Chancellor, Marks Hinton, Janet Lowe, John Maginn, Merle Mullett, Rich Rockwood, and Shirley Terrass, all of whom provided advice, support, and encouragement along the journey. A special thank you goes to Dennis Rocheleau, Mike Stout, and Larry Crouse who reviewed the manuscript with the same critical eye as if it were their own. Aaron Kindig and Tom Dugan, outstanding junior analysts with our firm, accepted with enthusiasm the many assignments thrown at them and produced results commensurate with their outstanding effort. Kristen Smith, who stepped into the project midstream, did a remarkable job getting up to speed in a heartbeat while assisting with the editing and keeping me focused on the task at hand. Stephanie Malcom, the formatting pro, packaged the prose. Wordsmith Dan Shenk once again helped me look good.

I cannot even imagine what my journey thus far might have been had a few exemplary gentlemen not showered their remarkable favors on one so undeserving as the undersigned. Among them was my dear friend Ted Levitt (1925–2006), the economist and Harvard professor who coined the term "globalization," and Peter Bernstein (1919–2009), known by many as author of *Against the Gods: The Remarkable Story of Risk* and by me as a man whose words of encouragement (and once or twice of richly deserved reproach) will never be forgotten. Jack Bogle, the 82-year-old founder of the $1.4 trillion Vanguard Group, reigns supreme as "Mr. Integrity" in the financial services world. He is the living epitome of what is good in our industry and a fearless critic of what isn't. Few realize that Bogle made a choice in the 1970s between putting the customer first and a personal fortune that likely would have put him on the *Fortune* list. Instinctively, he took the high road. I highly recommend two of Bogle's increasingly relevant books: *Battle for the Soul of Capitalism* and *Enough*. Warren Buffett, 80, with whom I have had the least face-to-face acquaintance of the four (we communicate mainly by letter and e-mail), but whom I most emulate, has cast the longest shadow of anyone I've known in my professional development. Once I realized the extent and durability of Buffett's genius, as both investor and thinker, I studied him with such singular focus that some have called me a sycophant. In relation to the Oracle of Omaha, I could have been called worse! All four men share similar traits, including:

- Intellectual brilliance
- Irrepressible drive and focus (65 was less a speed limit than a speed bump that they hardly noticed)
- Exemplary honesty and integrity, as well as a lifelong passion for learning
- An amazing approachability and likability

They were or still are humble giants. I believe I inherited at least two traits from them: I didn't even feel it when I blew by 65, and if my appetite for food were the equal of that for learning, I'd be 400 pounds and counting. My debt to these masters of my universe knows no bounds.

I have also drawn much strength and wisdom from clients (*friends* is a more fitting descriptor) with whom our relationship in almost all cases has been constructively candid and mutually respectful. Many are older and far more experienced, and their sage advice has often been vitally important, particularly when one's convictions are tested to the core day in and day out. Regular encouragement from virtually every client has kept my spirits high and my desire to persevere undeterred. Those words are not platitudes. There are few men or women alive who reach their potential without the support of caring others.

In the 2001 annual report (Chapter 4), I addressed the matter of attribution as follows:

> Sources for factual matter include the *Wall Street Journal*, *Barron's*, *Fortune* magazine, *Forbes* magazine, various Internet sources, Bloomberg, and others, along with a number of books. Considering the limited audience for whom this report is intended, the abbreviated production window, and the fact that most readers already are familiar with my ideas and writings, my words and those of others are freely mixed, sometimes without formal acknowledgment, particularly in the latter sections of the report. It is not my wish to put forth as original the ideas or words of others. To the contrary, I wish to save them the embarrassment of being associated with me! If you find a really great

> idea in these pages, and you're sure it could not have come from my semantically challenged synapses, give me a call, and I'll find the source and give credit where credit is due.

In reading *The Problem of Pain* by C. S. Lewis, I found he expressed the issue much more succinctly: "As this is not a work of erudition, I have taken [few] pains to trace ideas or quotations to their sources when they were not easily recoverable. Any theologian will see easily enough what, and how little, I have read." While I must read to compensate for my incapacity to think and reason (as Lewis did seemingly without effort), and *erudite* would not be the word to describe this far-from-scholarly exposition, I nonetheless have followed Lewis's lead and have not taken pains to trace all "ideas or quotations to their sources" (though permission has been received for the extensive references to copyrighted material from Ben Graham and Warren Buffett). As one observer suggested—with obvious reference to the quality of the effort (and therefore the need for *any* attribution, as well as the reason I sought solace from Lewis's book)—"Don't quit your day job!"

Enough

This book's purpose is not promotional. Rather it is personal. I hope that my experience—and account of events—can help future investors. I am a stickler for documenting in a profession where most people fear having their reputation indicted because of the paper trail. When I finally go to pasture and someone asks me what I did in my work life, I don't want to have to say, "Oh, I made a lot of money." How inconsequential, how pathetic. I've had the luxury of living through some of the most interesting economic times in modern history. And I've had the privilege of being able to record some of what I've observed. I would not be content keeping this exhilarating experience to myself.

As noted in the preceding paragraph, we are *not* soliciting new business through this book nor, accordingly, can we respond to inquiries from readers. Rather, the book is offered as a small contribution to the body of investment knowledge. We encourage readers to apply whatever insights they might glean to the management of their own investment assets or what they might look for in selecting a manager.

In Chapter 11 the reader will find a full account of the firm's investment performance history during the Lost Decade. Its purpose is to authenticate (or perhaps repudiate; be sure to read the fine print!) what might otherwise be perceived as just so many words. Pontifications from pundits are too often taken at face value. Although I'm not sure on which side of the line that separates crudeness from healthy skepticism readers might perceive me to be, it is my nature to discount whatever is said today unless corroborating (or, more often, contradicting) evidence from earlier pronouncements can be found and verified.

A Decade of Delusions, an indelible, and sometimes self-indicting, paper trail, reveals my foibles and fortes—and the investment record that exposes both. Warts and all, it is hoped that the contrast will be refreshing.

Finally, the opportunities for reflection and contemplation abound for a professional investor for whom success is not measured in dollar terms. It would have been a great loss if I had sped through the preceding decade in the pell-mell pursuit of the almighty buck and missed a lifetime of lessons that were there for the taking. Such ineffably sublime gifts are given to those whose senses remain attuned to the juxtaposition of the daily stream of anecdotal tidbits, like so many falling leaves, and the perpetually repetitious nature of the willful human mind. On an even more personal note, in the reckless rush for riches that characterized the Lost Decade, all too many were so consumed by the "more is better" mind-set that they seldom paused long enough to ask: "How much is enough?" I hearken to the thoughtful words of Kahlil Gibran in *The Prophet*: "And what is fear of need but need itself? Is not dread of thirst when your well is full, the thirst that is unquenchable?"

While I confess to being a contrarian, I will never submit to charges of pessimism. The great deleveraging likely ahead will be burdensome, to be sure, but it may yet have a positive outcome: helping Americans rediscover what it means to have—as Jack Bogle stated simply—"enough."

FRANK K. MARTIN
November 2010