April 2022

When is Enough Enough?

There is a lot of uncertainty that investors are grappling with these days. From the war in Ukraine to the direction of interest rates and inflation, to name a few. These are heavy topics. People of various backgrounds are weighing in and opinions and narratives abound. The deluge of information is overwhelming for investors who are trying to make sense of what all of this means for their investments. This is stressful. With so much uncertainty, people seek digestible opinions and definitive answers to feel comfortable. Investment writer, Morgan Housel, wrote:

“Uncertainty amid danger feels awful. So it’s comforting to have strong opinions even if you have no idea what you’re talking about, because shrugging your shoulders feels reckless when the stakes are high. Complex things are always uncertain, uncertainty feels dangerous, and having an answer makes danger feel reduced. We want firm answers when things are the most uncertain, which is when firm answers don’t exist.”

When there is an unusual amount of uncertainty and nervousness in the market, there is a tendency to reach for more – more data, more analysis, more answers. But having more is neither efficient nor effective. Time is a finite resource. And more information does not necessarily equate to better decisions. We cannot model every scenario, let alone every risk. One must determine the most relevant and important information, manage the most detrimental risks, and move forward cautiously.

"A model might show you some risks, but not the risks of using it. Moreover, models are built on a finite set of parameters, while reality affords us infinite sources of risks." – The Map and Territory

But when is enough enough? Knowing the answer to this question requires judgement. Our team’s collective experience, shared knowledge and history of recognizing investment patterns help us make this judgement. Determining that there is indeed a point when enough is enough is thoughtful in philosophy and deliberately optimal.

Preparation helps: understanding industry dynamics, advantages a company may have, management’s operating history and capital allocation tendencies, and most importantly, what a reasonable intrinsic value is for a company. In short, we do our homework in advance to be familiar with the crux of an investment thesis. So, when there is a dislocation in the market, we know what information we are looking for. In essence, this focused investigation greatly helps us determine when enough (research and analysis) is, in fact, enough.

With endless data at our fingertips, it is tempting to want more and more information. The idea is that more information and more research mean more accuracy and more certainty. More is comforting. More inspires confidence. But information gathering has diminishing returns. At some point, time and effort should be focused on areas where there are “bigger fish to fry”.

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Worse yet, an insatiable thirst for information can backfire. More information tends to lead to unjustified confidence in how the future will unfold. In reality, uncertainty cannot be minimized beyond a certain point. The result can be overconfidence and poor decision making. For example, overconfidence can lead to a portfolio with too large a position in a stock because someone knows the company "inside out".

A principal benefit of being able to identify the point of enough is speed of decisions and execution. As we saw in March 2020, the market can whipsaw at a breakneck pace. Attractive investment opportunities come and go. One must be ready, willing and confident enough with their preparation and the information at hand to act. Seeking out ever more information in the false hope of more certainty may mean that gaps between price and intrinsic value disappear.

Finally, it is important to avoid "analysis paralysis", which is the inability to act because of too much information and over-analysis. Note that inaction is completely sensible if it is deliberate inaction (which is, ironically, an action). We do not want to be frozen from making decisions because of the mirage that more analysis always means more certainty. Going beyond enough may make us unintentionally miss investment opportunities that have attractive risk and reward ratios. And this ratio is critical. Since there will always be risk, the goal is to seek a reward that justifies that risk. Put simply, our estimate of intrinsic value must project a return that compensates for taking on a certain level of risk.

At Sionna, we balance between seeking incremental certainty and gathering enough information to make good decisions. No information will give us 100% certainty as to how the future will unfold, but targeted and relevant information is very useful because it tilts the likelihood of investment success in our favour. Ultimately, we believe that having a feel for the point of enough makes us nimble, sets the stage for good decision making, and is additive to our overall investment performance.

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