

It is our distinct pleasure to bring you the following interview with Marc Batlle Mercadé of [ELCANO SICAV](#), a Spanish investment firm with offices in Madrid and Barcelona.

Prior to ELCANO SICAV, Marc worked at Merrill Lynch in London as a financial analyst in the telecommunications sector, responsible for European securities coverage. Previously he was an analyst of financial institutions for a hedge fund in New York specializing in arbitrations. Marc holds a degree in Economics from Pompeu Fabra University and is a Chartered Financial Analyst. Marc brings financial analysis skills and knowledge of investment and business strategy to his leadership role at ELCANO SICAV.

Please tell us about your background and how you became interested in value investing. What events or people shaped your investment philosophy the most?

When I was at college I came across *Security Analysis* and I was trapped by the concept of profiting from uncovering bargains through analysis. Investing fills my natural curiosity and thirst for knowledge to the point I would do it without getting paid. I view the market as a laboratory where your knowledge and judgment will be tested, and this is quite uncommon in the business world.

After college I worked for some years in order to gain experience and reputation, while at the same time kept developing my knowledge base through self-study. When I felt I was ready we launched ELCANO SICAV.

With time you get better through experience and study, but the basic concept has to stick in your mind since day number one, or probably it never will.

What other firms do you look up to, and why?

I think there are many good firms out there. There are many ways of making money.

But let me answer with what I do not like: money supermarkets with a large repertoire of funds, employing an army of analysts, PMs and salespeople and with little money invested alongside their clients.

In my opinion, employee-owned firms that are focused and not too large are in a better position to add value to their clients.

Please tell us about the founding of ELCANO SICAV. What operating principles have guided the firm since its founding?

We launched ELCANO SICAV at the end of 2009. It was mainly our own money.

The principles have remained the same: thorough analysis, independent thinking and emotional control, buying quality at a discount and keeping a concentrated portfolio. With our investors we try to communicate candidly and we are fully committed with all our assets invested in ELCANO.

We keep our firm expenses low, outsource all the non-core processes and focus on the long

run.

What are key success factors to intelligent investing? Similarly, what traits should an investor have to be successful?

You need knowledge and the right mindset. Knowledge is built through study and experience. Learning is tough, so a passion for the trade is absolutely critical. Money is not a strong enough motivator given how demanding this job is.

Psychologically wise, if you cannot control your emotions and endure difficult periods you are not fit for investing. Having a balanced life is very helpful in this sense. It has been proved that optimal decisions are made under the right amount of pressure, neither above nor below.

If you are intelligent, willing to work hard over a lifetime and capable of controlling your emotions, you should definitely succeed. How much will depend on many other factors, some of them outside your control.

Why does ELCANO SICAV have an edge? How will you maintain or expand this edge over time?

In my opinion, ELCANO SICAV's outperformance is due to the combination of our investment principles, our analytical approach and our firm set-up.

Our investment philosophy can be summarized as putting a lot of money in a few exceptionally attractive ideas we know well. Most investors do the opposite thing.

Our integrated analytical approach is based on the lessons and experiences of players and authors from a variety of fields: industrial organization, economics, trading, innovation, management, distress investing, psychology, M&A, etc. Furthermore, we believe that by being generalists touching many sectors we are able to see more.

Our set-up is characterized by the lack of investment committees, the flexibility to invest in situations where large funds can't due to their size, and the psychological benefits of being the largest investors in the fund and having a lean structure so we don't have to worry about business survival during difficult periods.

We try to get better everyday by learning from experience (particularly from our mistakes and this includes missed opportunities), by constant study and by improving our methods.

What sources of opportunity have you found over the years? Where do you look at?

Drawing on the knowledge we have built about many industries, we try to think where the opportunities are given the current fundamentals and expectations. We do not waste our time looking for bargains in sectors that are either inflated or with impaired fundamentals.

We also systematically analyze special or difficult-to-understand situations, such as spin-offs, litigation or turnarounds, as these are generally ignored by the general investment

community.

We keep our knowledge base of companies and industries updated, as this is our most important source.

Where are you finding opportunities today, in a market environment that generally is not cheap?

We think that after the industrial recession that started in mid 2014, caused by the overcapacity created everywhere in the aftermath of the GFC, fundamentals have stabilized and are starting to move towards a new cyclical peak maybe by the end of the decade. Capacity has been shut down, inventories cleaned up, demand is improving and further expansion will be tempered by the recent memoir and tighter credit conditions.

All this represent excellent conditions for the asset owners.

If you combine these fundamentals with the fact that investors have prioritized yield and stability, we conclude that cyclical are a great place to look for bargains.

Are there investment areas that you are purposefully trying to avoid? What are mistakes you either have made or seem others make, and what have you learned from the experience?

The surest way to lose money is by not knowing what you are doing, overpaying, taking too much debt and buying poor quality. So we stay away from these elements. We avoid sectors that are growing very fast as they often attract competition, or industries that are inherently unstable (eg. fashion retail). Buying into declining industries is often a bad idea, although there are exceptions.

Experience has taught a few important points. Everything takes time, usually much more than expected. The market gives you plenty of time as it is slow to adjust. So do not rush. Avoid the losers and stay with the winners: the trend is your friend. Buy very cheap. Bet strongly and infrequently. Do not overestimate management and business quality, as most of things prove to be cyclical.

What is your take on portfolio concentration, and how does it reflect your philosophy on risk? What is the ideal number of holdings for ELCANO SICAV?

We normally hold about 15 stocks. When we find an outstanding opportunity we bet up to 10% of the portfolio.

By increasing the number of holdings you obviously become closer to the market, so your chances of outperforming come down. We study opportunities with great detail and only act when the odds are overwhelmingly in our favor. Once invested, we follow the position as if we had all our net worth in it.

To be able to concentrate you should keep a cool head, understand what you are doing and act only when all the factors are aligned.

How do you protect your portfolio from permanent loss of capital, and what is your take on holding cash?

We act under two premises. Firstly, a paper loss and a realized loss are the same. Secondly, we always consider opportunity costs. Staying with the losers is a big mistake in this sense, and one value investors often make.

As I pointed out before, we treat every investment as if we had 100% of our money in it, so we need to understand it, have an ample margin of safety and be of good quality (business, management and balance sheet). It is easy to lose money if you buy low quality companies, expensive ones or you get involved into situations you don't fully understand.

Secondly, and this is something we have learned through experience: we try to listen to the market. We are very reluctant to make a commitment when momentum, both fundamental and market, is negative.

If we don't find opportunities, we just do not invest. So cash is treated as a residual. We always invest in liquid stocks, so we don't need a buffer.

How do you assess the quality and incentives of management, and what CEOs do you admire most? To what extent do you engage with the management teams of the companies you own?

In our experience, the economics of a business are way more relevant than who is leading it in a particular moment in time. It is also true that management has a bigger influence in some industries than others.

Something that has a direct impact on performance is firm's culture, so we take it into consideration before making a commitment. There are exceptional leaders who are capable of changing culture. To us they are the heroes of the corporate world. Jeff Clarke from Kodak is someone we admire, as he is transforming the company into a high performer. Meg Whitman from HP has proved to be exceptional as well.

We try to have a fluent dialog with management and always express our views if we disagree. If we don't like what we see, we move somewhere else.

Can you recommend a few recent books that have given you new insights into the art of investing?

I'd rather place a sure bet and recommend some classics. In Economics, [Man, Economy, and State](#) by Murray Rothbard. Austrian Economics is very useful in understanding cycles. I believe investors should have a framework that links economics and business so I would recommend [Industrial Organization](#) by Paul Belleflamme. Everything written by Peter Drucker is top drawer. As for general investment and trading principles, I would recommend [The Aggressive Conservative Investor](#) and [Market Wizards](#) by Jack D. Schwager.

