

Nils Herzing Sums Up His Investment Philosophy

This article is authored by MOI Global instructor Nils Herzing. Nils is an investment professional at Active Ownership Capital, a partner-managed investment company that acquires significant minority stakes in publicly listed, undervalued small- and mid-size companies in German-speaking countries and the Nordics.

This Investment Philosophy frames the general thinking about investing and describes my investment style. It is not a fixed set of rules, it is more an evolving collection of thinking patterns.

The aim of my investing is to generate long-term outperformance (over a time period of more than 5 years). Thus I don't aim for a low volatility or other fancy things; the sole goal is to maximize the performance in real money terms.

I don't believe in efficient markets, as I think that markets are "Voting Machines" in the short-term but "Weighing Machines" in the long term. I believe that the highest irrationality in stock prices, especially in the short run, exists in small- and mid-capitalized enterprises which have a low free float. Furthermore, I believe that an undervaluation in the long run can occur in large-caps, as most investors only think within a timeframe of 3 years. By taking a long-term investment approach which exceeds 3 years and thinking in time frames of 5, 10, or even 20 years, you are able to outperform the market even in large-caps.

I don't believe in over-diversification, or in holding more than 20 stocks as it doesn't add value and destroys performance. On the opposite, I believe that it is possible to get an investment edge via the two following ways:

- a.) Informational edge – More information than every normal market participant has. This means doing field research, visiting companies and speaking with customers and competitors.
- b.) Behavioral edge or "longer time horizon" – by taking a time horizon of more than 3 years, investors can see the value of long-term growth and are able to go against short-term pressure / noise / "pain".

To participate from short-term irrationalities, it is necessary to have an investment process which is focused on the long-term value creation of a company, thus the value of growth is essential for my investing approach. To pursue this type of investment strategy, it is necessary to find long-term capital and co-investors who think like owners.

The only possibility to increase my returns towards a level of above 15%, which I would like to achieve in the long-run, is in my opinion:

- a.) Have a less diversified portfolio of only 8 to 15 companies.
- b.) Avoid a permanent loss of capital, which can be achieved by using quality filters such as good management, strong balance sheets and the use of "Owner Earnings".
- c.) Use a higher discount rate and thus have fewer potential investment candidates.
- d.) Shorten the time frame of value realization, e.g., until the undervaluation is uncovered and the

market price reaches the fair valuation of a business

e.) Take a long-term view of more than 5 years and invest in real compounders, which have an outstanding management / capital allocator, really early in their life.

Last but not least, I would like to achieve this goal by investing in an ethical and sustainable manner. I believe so, as I think that sustainability and ethical thinking is equal to a rational view on the long-term time axis.