Ely Prudent Portfolios

Being Obsessive-Compulsive is a Good Thing

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If you double-check something and get the same result, most people would assume it's right. I assume it is wrong twice and check it again. I do this because I am obsessive-compulsive, which is a good thing for my clients but not for me. It's good for my clients because I am always trying to figure out what can go wrong with their portfolios and how to prevent it. It's bad for me because I obsess about everything and I am compelled to constantly perform an illogical counting ritual that serves no purpose but to appease the dysfunctional portion of my brain.

In his book, Talking Back to OCD, John March describes the detrimental effect that this brain malfunction had on my education. "Obsessional thoughts can take center stage in a kid's mind, shoving what's going on in the classroom into the wings." Since I couldn't pay attention in school, I had to take my textbooks home and tutor myself in the material that the teacher had presented that day. That wasn't all bad, because the ability to figure out things on my own has become a very useful skill to possess.

Learning to compensate for a handicap by enhancing other skills is a normal thing. The blind develop a keener sense of hearing and the deaf acquire better visual perceptual skills. In my case, being oblivious to the obvious I have become acutely aware of the obscure. While this may not seem useful, it is actually highly beneficial in today's complicated investment climate. Back when I first got into the investment business, limited partnerships were the latest and greatest thing. People would actually beg me to invest in deals that promised high returns and big tax breaks. However, I never sold a single limited partnership because, as I told my clients, "There are three people involved in a program, the general partner, you, and me, and I know two of us are going to make a lot of money." I knew that because I was compelled by my obsessiveness to read and decipher the convoluted and purposefully vague language in the plan prospectuses.

Since then, the computer age has ushered in a whole new generation of incredibly complicated alternative investment products. This complexity not only leads to confusion, but it can also hide unsubstantiated valuations, deceptive accounting, poor liquidity, inadequate transparency and excessive fees. In his 2003 annual letter to shareholders, Warren Buffett warned that these highly complex financial instruments are "...ticking time bombs and 'financial weapons of mass destruction' that could harm not only their buyers and sellers, but [also] the whole economic system." The result of this complication, according to the March 20th-26th, 2010 issue of the Economist, is that risk doesn't end up being held by those "...best qualified to hold it...[but instead] it seems to have ended up in the hands of those least able to understand it." Amazingly, this includes some of the most sophisticated institutional investors in the country. Just like the investors in limited partnerships of the early 1980s, present day managers for endowments, municipalities, and public employee pensions have been begging to get into alternative investments, which unfortunately, appear to conform to the same old "two out of three" rule I observed 25 years ago.

Recently a psychologist said he could cure my obsessive-compulsive behavior. I thought about it for a while and decided not to take him up on his offer. While I don't like the personal hell it can cause me, I don't want my clients to go through the "hell" that Mr. Buffett compares the alternative investment business to, "... easy to enter and almost impossible to exit." Since escaping this financial purgatory is so difficult, you need to avoid entering the eternal damnation of alternative investments in the first place. You do that by hiring an advisor who is obsessive about due diligence and compulsive about counting costs.

Ely Prudent Portfolios, LLC is a fee-only investment advisory service working with individuals in or near retirement and non-profits. The firm is accepting new clients with a minimum AUM of $1,000,000

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