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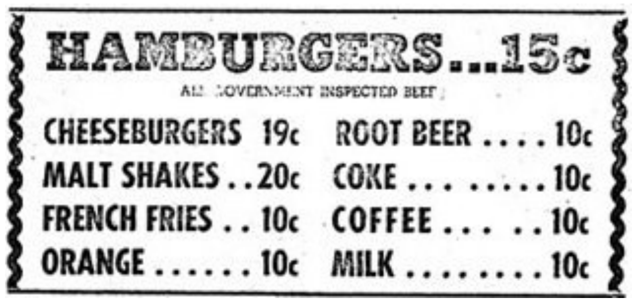
The Art and Power of KISS

Chart of the Month - March 2018

Ray Kroc, the longtime force behind McDonald's, is credited with managing the company on the principle of KISS – **K**eep **I**t **S**imple, **S**tupid. Kroc, at the age of 52, was making the rounds as a Prince Castle Multi-Mixer salesman when he came across a small hamburger shop run by Richard and Maurice McDonald. He was struck by the simplicity and efficiency; the menu consisted of hamburgers, fries, drinks and shakes. He later bought out the McDonald brothers for $2.7 million and credited the KISS philosophy – Keep It Simple - as a key in building a global powerhouse.

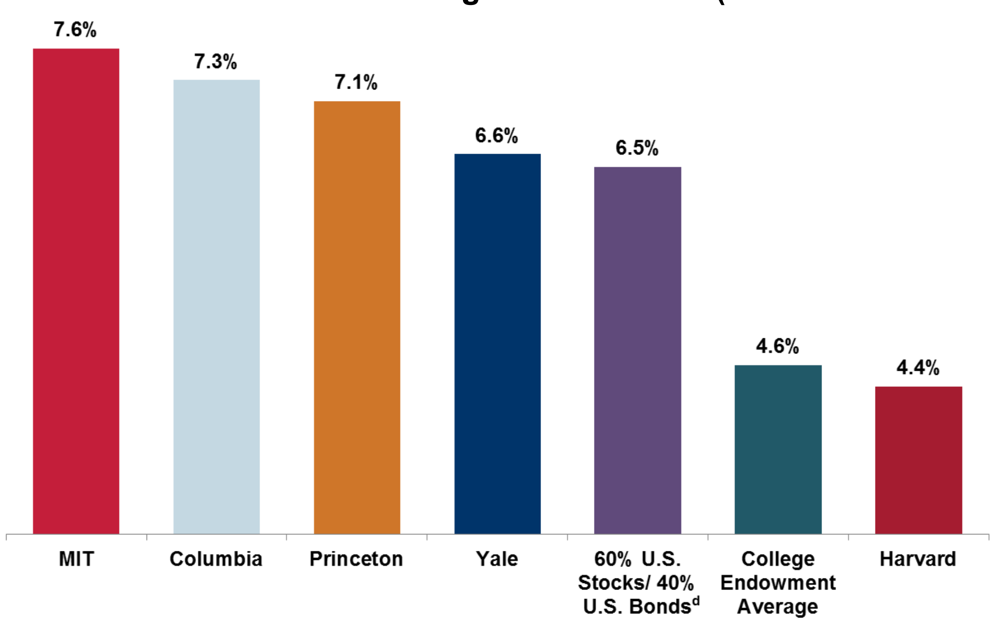
McDonald's Menu circa 1955[a]



We see other examples of elegant simplicity that dominate their fields – the uncluttered Google landing page, Dyson vacuum cleaners and almost anything that Jony Ive (Apple) touches. And In-and-out Burgers has built a thriving business by virtually copying McDonald's original formula.

It's a case of stripping away the superfluous until you're left with the essential. We're reminded of Ray Kroc as news comes out of Harvard's disappointing investment returns. A recent Bloomberg Businessweek article[b] points to Harvard taking steep losses on far-flung investments such as an Australian cotton farm, a eucalyptus plantation in Uruguay and timberland in Romania. These, and other alternative investments such as hedge funds and private equity, have delivered disappointing returns over the past ten years.

Annualized Performance of College Endowments (7/1/2007-6/30/2017)[b,c]



a. Kottke, Jason, "Early McDonald's Menus", 3/18/2013 (https://kottke.org/13/03/early-mcdonalds-menus).
b. Michael McDonald and Tatiana Freitas, "Harvard Blew $1 Billion it Bet of Tomatoes, Sugar, and Eucalyptus", 3/1/2018 (https://www.bloomberg.com/news/articles/2018-03-01/harvard-blew-1-billion-in-bet-on-tomatoes-sugar-and-eucalyptus).
c. National Association of College and University Business Owners, "Educational Endowments Report Decline in 10-Year Return Despite 12.2% Return for FY 2017, Up Significantly from -1.9% Reported for FY2016 - Large Institutions Lead Increase in Effective Spending Rate", 1/25/2018 (https://www.nacubo.org/-/media/Nacubo/Documents/EndowmentFiles/2017-NCSE-Press-Release--FINAL.ashx?la=en&hash=80ADECD43606B800223D45E4CF32DC47F7C1576D)
d. U.S. Stocks are represented by the S&P 500 Total Return Index. U.S. Bonds are represented by the Bloomberg Barclays U.S. Aggregate Bond Index. A 60%/40% blend of these indices, rebalanced annually, would have resulted an a 6.51% annualized return from 7/1/2007-6/30/2017. Past performance is no indication of future results. Investors cannot invest directly in an index.

This underperformance isn't unique to Harvard. It's noteworthy that a simple blend of 60% U.S. equities and 40% U.S. bonds returned nearly 2% per year more than the average of college endowments participating in a recent study[e]. If the same returns were repeated for the next ten years, Harvard's $37 billion endowment would trail the 60/40 index blend by over $12 billion[f].

There is certainly a place for alternative investments and their turn to shine may very well be on the horizon. But it's worth noting that a broadly diversified portfolio, at a low cost in a very tax efficient structure, can deliver returns which may rival, and many times surpasses, the complex approaches of the most revered universities. Harvard's new endowment chief is hearing calls to pivot and changes are being considered.

Market Performance[g]

Index	February 2018	Year to Date (1/1/18-2/28/18)	One Year (3/1/17-2/28/18)
S&P 500 Index	-3.7%	1.8%	17.1%
MSCI EAFE Index	-4.5%	0.3%	20.1%
Barclays U.S. Aggregate Bond Index	-1.0%	-2.1%	0.5%
JP Morgan Global Aggregate Bond Index	-1.0%	-0.2%	5.4%
Bloomberg Commodity Index	-1.7%	0.2%	1.6%
Gold ($/oz)	-2.0%	1.2%	5.6%

e. 809 U.S. colleges and universities participated in the 2017 NACUBO-Commonfund Study of Endowments®. Average annual return is displayed net of fees and expenses.

f. As of 6/30/2017 Harvard's endowment was $37.1B (Source: Harvard Management Company). In ten years, a 4.4% annual return with a $37.1B starting value would result in an ending value of 57.1B. In contrast, over the same time period the 6.51% annual return of a blend of 60% U.S. Stocks/40% U.S. Bonds would have resulted in an ending value of $69.7B. Past performance is no indication of future results. Investors cannot invest directly in an index.

g. Source: Bloomberg. Total Return indices.