ARM Holdings LLC Investment Theory

By

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The purpose of this document is to outline the core beliefs and associated methodologies that will be utilized to allocate the capital of the various partnerships of which ARM Holdings LLC is the general partner. I intend to casually walk you through some of the pitfalls that you may have unknowingly come across in the financial arena and illustrate our take.

Objective

Beat the market by buying undervalued, fundamentally strong companies with growth potential, minimizing downside risk and maximizing upside gain taking into account the market trends, as well as everything that could impact the stock price utilizing intuition.

Addendum: To do whatever it takes to maximize expected returns.

Strategy

We intend to achieve the above objective not by figuring out which companies to own, but by being adamant about not owning companies that we feel offer a poor risk/return situation. Many organizations inundate their employees with *bounded* (sector, business, industry, location) financial analysis, and lots of it --- on a few companies. Our advantage is being *unbounded*. Our scope includes every possible investment opportunity that we can find. We intend to spend more time eliminating companies from our investment scope than wasting time putting price tags on seemingly mediocre opportunities. Further, our framework for pricing companies will only come from individuals with proven track records of beating the market over extended periods of time. These legends include: Joel Greenblatt, Peter Lynch, Jim Cramer, Warren Buffett, Al Frank, Martin Zweig, Benjamin Graham, Joseph Piotroski, William J. Ruane, and Jesse Livermore.

Risk

In the land of insanity, risk comes from stock price covariance according to the Efficient Market Hypothesis. We believe risk in the investment arena comes solely from overpaying. We believe that stocks are not always priced efficiently and in fact, would argue that there are many irrational decisions that can drive prices beyond or below what's justifiable. Two examples of this: buying a bankrupt company is very risky as you are paying something for nothing. Further, paying what a company is intrinsically worth or more than the company is intrinsically worth is very risky as there is not much more upside potential.

Diversification

We believe that mutual fund companies as a whole encourage the diversification among companies at mediocre prices. 30 years ago, this was very helpful, as the transaction costs for the small guys were very high and this enabled them to lower their firm specific risk. Now that transaction costs are lower, we feel that sell-side asset management hurts the average investor. We believe that diversifying across select situations where companies are priced shockingly below where we value them will over time yield above average returns and more importantly reduce the possibility of loss of capital (risk).

Value vs. Growth

The first question you may have been asked by an asset manager is whether you'd prefer to invest in value or growth. We believe that looking at the two separately instead of as components of one another is ridiculous. We believe that companies that are growing and set to grow faster than other companies should come with a higher price than other companies. Hence, we put extra value on extra growth. We believe that we can capitalize on this core belief by finding and buying high growth companies at discount prices.

Limiting Factors

There are two limiting factors when it comes to the allocation of financial capital. When and Where. Where defines the companies or opportunities that are to be taken advantage of. When defines the time at which you allocate your capital into those opportunities. The saying, "Strike while the iron's hot" comes to mind. The trick is forward looking. In order to make money, you have to be allocated where a lot more money is headed before it gets there. You have to buy stocks that are at low prices before they are at high prices. "Buy low, sell high." Sounds easy enough, but you are fighting market dynamics that can push company valuations away from their intrinsic value for potentially forever. These are not limited to but may include: bear and bull markets, confirmation biases, herd mentality, panic buying and selling contagions. These result from: defective reasoning, sycophantic strategies and narrative fallacies, defective reasoning, short-sightedness, satisficing, and the winners curse.

Large vs. Small

To illustrate this point most effectively, imagine a 1 man company doubling in size. Now it's a team of 2. That was easy. Now, double the largest company in the world. Not so easy. We feel that there is more growth potential in smaller companies and that buying smaller companies that are on their way to becoming larger companies is a better approach than buying large behemoth juggernaut type companies.

Debt vs. Equity

We believe that equity tends to be more inflation resistant and that fixed rate debt which tends to be subject to real investment losses even though investors may see nominal gains. Also note that there have been more frequent and more severe bond market crashes. A book titled Stocks for the Long Run by Jeremy Siegel illustrates why we do not intend to invest in debt. If an opportunity presents itself that we find it difficult to match in the equity market, however, we will not be afraid to buy debt.

Lastly, we believe the best we can do is give you, the investor, the opportunity and the incentive to take it. The choice to take it is yours, and yours alone. At the least, I hope that reading this document makes you more concerned about your present investments and the associated strategy going forward.