Rich Morgan, RIA Channel Interview with Brian Yacktman
Transcript

Rich: Hi. This is Rich Morgan of RIA Channel, and contributor to Forbes. I'm here with Brian Yacktman, President and Chief Investment Officer of YCG. Brian, welcome. Thanks for joining us.

Brian: Thanks for having me.

Rich: So tell us a little bit about you and the firm you're running currently.

Brian: Sure! So, the name is Brian Yacktman. A lot of people just instantly assume that I work for Don Yacktman at the Yacktman Funds. Don is my father, but I'm actually at a completely separate firm. So, several years ago I used to work with him, but then in 2007 their minimum was so high I said to him, "Why don't you lower your minimum? There's got to be people who don't have fifty million that want to be managed in a Yacktman style." And he said, "That's a great idea, just don't do it here."

Rich: So, you took all the trade secrets and you started your own firm.

Brian: Yeah, exactly. No, basically it was, the intent to start a separately managed account business, and then when he closed his mutual fund, we decided to open a mutual fund called – we changed our name from Yacktman Capital Group to YCG, the initials, to avoid the confusion that was constantly coming up.

Rich: So you're known for owning a lot of stable, and some might say boring stocks and, you know, where do you find the opportunity to seek alpha and upside in that kind of portfolio mix?

Brian: Yeah, that's a great question. So, typically people think of you need to take on a lot more risk in order to be able to outperform the stock market. And what's interesting is when you look at studies, high quality has actually proven for decades to outperform lower quality counterparts. And I think a lot of that, in my assessment is, based on three kind of ideas. One is we all tend to be overconfident, so if you put all of us in a room and you say, "who's an above average driver?" Everybody, or ninety percent, say, "I am." And so we all tend to think, even though high quality outperforms, we think, well but I'm not going to do it quickly, so second is that we're impatient, and then they think I'm overconfident enough to know that I can pick it. And then third, we're just greedy. So that greedy, impatience, and overconfidence I think leads to a constant, systematic underpricing of high quality. In other words, you almost get paid a premium to be willing to own boring stocks. But then there are times where that will totally change. In periods of catastrophe, where people's aversion to loss overwhelms those principles, and all of a sudden low quality really outperforms from there. So during those times, we might have something different, but in this environment we're finding that you're not getting paid much to take on a lot of extra risk. And so, we're finding comfort just compounding in some stable, steady eddy companies.

Rich: So, specifically, around kind of the strategies that you employ, are there any in particular that you would highlight as kind of setting you off as unique?

Brian: Yeah, sure. We implement what we call an option enhancement strategy. The concept behind that, it's similar to the same thing where people want to make a quick buck, and so I think that's why I get paid a premium to own boring businesses. Well, in the options market, there have been studies that show that the writers of options tend to make more money than the owners of the underlying stocks themselves. And I think it comes back to that same thing, that people want to make a quick buck, so it's almost like they overpay for options. So what we'll do is we'll write options on businesses that we want to own. Not with leverage, it's just cash secured puts on things we want to own, and sell covered calls on things that we want trim out of. It's sort of like putting in limit orders, and you get paid handsomely for being willing to write these options to put in limit orders.

Rich: Sure. So, let's talk about 2016 a little bit. Obviously, two macro headwinds that we're walking into. One is the election, and the second, probably more important to you, is what's the Fed going to do with rates? A lot of would say maybe 25 basis points in November, or excuse me, in December, uh maybe some follow-on raises. What do you think's going to happen next year?

Brian: So, to be perfectly honest, I haven't a clue. I would say...

Rich: At least you're honest!

Brian: Yes! I feel like it's fruitless for me to attempt to predict these things because I feel like if I make decisions based on that, I'm going off on a limb, and who knows? So, my crystal ball is broken, let's put it that way.

Rich: Are there any particular stocks that you would highlight as maybe opportunities from an ownership perspective you see out there?

Brian: Absolutely. Actually, it's very fitting that we're here at the Charles Schwab conference. Schwab, and as you bring up Fed funds, you know if they were to raise rates, Charles Schwab is actually priced inside of some sort of like dormant on the money market and on the margin loans that they make, they're sitting dormant in their earning power. So like right now, if rates were to go back to like a 2006 level, which wasn't any egregious time in interest rates by any means, to a 2006 level Charles Schwab's earning power would triple. I mean, literally triple. So, but if interest rates were not to rise, it's still a fantastic business that's continuing to collect assets, growing at around eight to nine percent a year. So, with no rates you're looking at like an eight/nine percent-type rate of return. If interest rates raise, I mean, just depends on how far they go, but you could have some serious compounding.

Rich: You heard it here, Schwab, 2016 stock to own, Brian Yacktman. Brian thanks for being with us, I appreciate it. Thanks.

Brian: Yeah. I appreciate it.