



Investment Philosophy

SilverCross Global Small-Cap Fund invests in a portfolio of 25-35 high-quality smaller companies. It invests in companies with defensible business models across global developed markets.

The Manager applies four core principles in its stock selection. Its aim is to drive attractive long-term investment returns in excess of the benchmark while keeping portfolio turnover low.

Core Selection Principles

Create Value with a sustainable business model.

Compound Growth thanks to a scalable business model.

Undervaluation implies an asymmetric risk / reward profile.

Insider Ownership ensures alignment with management.

About The SilverBullet

A silver bullet refers to a straight-forward solution perceived to have high effectiveness. With this newsletter we aim to offer a mix of thought-provoking research and small-cap insight.

Why we are not 'specialists'

What do Charles Darwin, Vincent Van Gogh and Roger Federer have in common? Besides becoming icons in their respective professions, they often sought insight and skill sets from seemingly unrelated fields. Federer would play other sports and not just tennis. Darwin was not just a biologist, he studied geology, philosophy, medicine and so on... This let him solve problems in a way specialists couldn't.

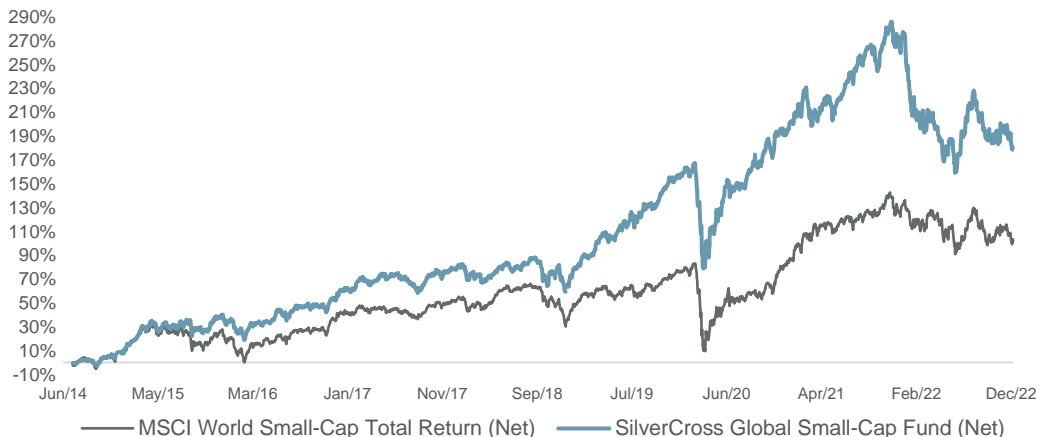
We are often taught the importance of becoming a specialist early and how the '10,000 hour rule' of repetitive practice is required to be successful. We agree that in investing, learning early and accumulating experience provides a massive advantage. But to succeed it also requires us to have a differentiated insight. To achieve this, we consider ourselves as analysts with a generalist approach at SilverCross. It is because of the two distinct learning environments we face. Let me explain.

Kind and Wicked environments

Psychologist Robin Hogarth identified two types of learning environments¹. On one end is a kind environment. All the necessary information is available; the possible situations are constrained by rules and feedback is immediate. This means for one action you can expect a similar result however many times you do it. By practicing you can achieve more consistent results, since it requires almost no human behavior aside from yours. An ideal environment for specialists. Activities like golf, or chess would be towards this end of the spectrum. Many famous people we know and hear of excel in this type of environment.

The other end of the spectrum is described as a 'wicked' environment. This is when not all the information is available; the rules are unclear or incomplete; there may or may not be repetitive patterns and these may not be obvious; the feedback loop is not immediate and perhaps incomplete. Situations are more complex as it involves other people's behaviors. George Soros described this previously as 'reflexivity.' This is the type of environment that white collar professionals often face. Unsurprisingly, it is the environment we face in **investing**.

Performance (EUR)



As of 22 December 2022	YTD	1-Year	3-Year ¹	5-Year ¹	Inception ¹
SilverCross Global Small-Cap TR Net	-25.8%	-24.3%	2.8%	9.3%	13.0%
MSCI World Small Cap TR Net	-13.2%	-11.8%	4.5%	5.8%	8.7%

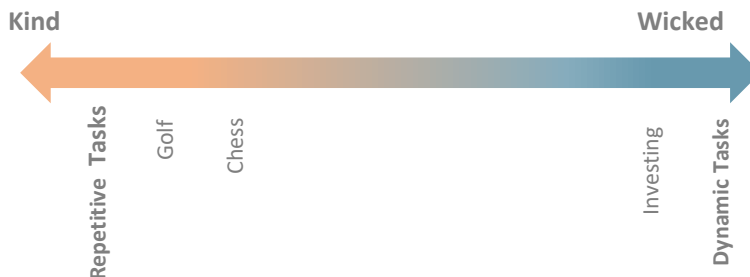
¹Annualised



Fund Details

Managers since July 2014:	David Simons & Chris Andrews
Inception date:	30 July 2014
Currency:	EURO
Share Class:	A
Management Fee:	1.15%
Total Expense Ratio:	1.40%
Minimum Investment:	100,000
ISIN code:	NL0010832242
Bloomberg:	SCGSCFA NA

Learning Environment Spectrum



In the book *Range* by researcher and journalist David Epstein², he discusses why generalists are better suited than specialists in a wicked environment.

The problem with specialists is that when taken out of a familiar situation, they fall victim to poor decision making. They tend to apply the same framework to try and solve every problem, caused by tunnel vision.

As Mark Twain once said: *“To a man with a hammer, everything looks like a nail”*

Generalists tend to approach problems more flexibly. Not only do they incorporate knowledge from their current profession but find patterns in seemingly unrelated fields to assess the situation. In many cases it comes from their personal interests and even hobbies. In doing so, they can depict a more accurate representation of reality.

Specialists	Generalists
<ul style="list-style-type: none"> • Deep knowledge in chosen field • Best when possible outcomes are finite • Can apply a more systematic approach to problems • Suited for kind environments • High repetition 	<ul style="list-style-type: none"> • Knowledge applicable to various fields • Better suited when potential outcomes are unclear • Employs more creativity • Suited for wicked environments • Low repetition

A crowdsourcing platform called Innocentive shows how easily you can get trapped by specialist thinking. On this global online platform, well-educated specialists from all fields can post a highly complex problem and anyone can attempt to find a solution for a reward. Problems they have been stuck on for months, sometimes get solved by non-specialists within weeks or even days!

Even in science: compared to other scientists, Nobel laureates are much more likely to have had training in more than one discipline and developed intensive hobbies. They are 9 times more likely to have training in crafts like metal work and fine arts than the average scientist.³ As strange as this sounds, pursuing other activities outside your dedicated field provides you with a different perspective.

It's no different in the way we operate at SilverCross. This is why an analyst is not confined to specializing in one sector. Many of us also have hobbies outside work. We like to learn about psychology and eastern philosophy. We practice singing, vegetable gardening and even poker! We also share a passion for food, which includes cooking and endless experimentation with ingredients. It creates opportunities to connect dots from apparently unrelated activities that sometimes help us to make better decisions.

Superforecasters

Philip Tetlock, a leading researcher in the field of psychology, political science and organizational behavior found a similar conclusion when it came to forecasting.⁴ He set out to find if specialists are better at predicting the future than amateurs. How did the specialists do? In his own words: “Roughly as accurate as a dart throwing Chimpanzee.” Overall, no better than an amateur.

What's more interesting however was that there was a small group of amateur forecasters who consistently outperformed specialists over the years. He named them ‘*Superforecasters*’ in his research. What did they do differently?



Perhaps to no surprise, they took a generalist approach to the challenge. Their backgrounds didn't relate to much of the forecasting problems they were solving. For lack of specialist knowledge, they made up with the way they processed and weighed information. Superforecasters considered facts and data from different sources, held multiple perspectives and found patterns from seemingly unrelated fields. They were also more willing to challenge their own views than specialists. If they found facts that contradicted their beliefs, rather than ignore this as an outlier, they were not afraid to change their minds.

As mentioned earlier, investing belongs in a wicked environment. If it were as simple as repetitive practice, investing could be automated and SilverCross wouldn't exist. We are often asked if each analyst specializes on a sector or an industry. The short answer is no. At SilverCross we are all generalists, we avoid specializing in a single sector. Some of us have a deeper understanding of a particular sector, but are also always developing in-depth knowledge *of multiple other sectors* to avoid tunnel vision.

The freedom to research various sectors provides us with more sources of information. This helps us assess a company in a differentiated light and identify potential risks that others may not have considered. To be clear, investing is a profession requiring time and practice. In pursuit of excellence, we still strive to understand each business and its industry as best we can – but in our fact-finding mission we are willing to explore beyond its domain and incorporate lessons from other sectors and fields.

There are certain biases that unfavorably influence the decisions of specialists:

- 1) Specialists are paid to have strong opinions, not tentative ones.
- 2) Sunk cost: As they have spent much time and effort, they can't afford it to be untrue.
- 3) More to lose: changing their minds will damage their reputation. So why should they?
- 4) They can only choose from a smaller opportunity set.

Even if a forecasting outcome is wrong, the ambiguous nature of wicked environments makes it hard to say with complete certainty the specialists are wrong. This makes it easy for them to explain the outcome without having to change opinions. Indeed, what Tetlock found was that even when specialists are wrong, they continue to believe they are correct.

As the saying goes:

"An expert is one who knows more and more about less and less" – Nicholas Butler

Seeing things differently

So as much as we try to acquire useful detailed knowledge to assess a business, our emphasis is on constantly refining our way of thinking. In other words, *it's not about the information that we have, but what we do with it.*

As generalists at SilverCross, we strive to foster a culture of humility, curiosity, and open mindedness. It helps us understand that our investment case is fallible. For each investment in our portfolio, we regularly test our existing hypothesis, find new perspectives to analyze from and challenge one another as a team. Humility is important as this helps us remain vigilant and admit when we are wrong.

By keeping an open mind while sticking to our principles, we are able to step outside what is familiar to find new opportunities. At times we may find patterns from a completely different industry when researching a company to identify both opportunities and risks. When we analyzed EM systems, a Japanese software company, we also studied real estate to verify the hidden value of its property that was not reflected in its valuation. As this example shows, we believe our culture leads to improving investment decisions, whether that is to buy or sell a stock.

Our generalist ethos not only applies to stock specific research. Taking a step back, we are open to refining our investment process by gaining new perspectives. Finding new 'tools' for our toolbox so to speak. By taking hints from different fields, it helps us improve the efficiency and effectiveness of our investment process. In a previously published [Quarterly report](#), Chris Andrews wrote about how we try to understand the irrationality of the markets. In the article he drew lessons from behavioral psychology and how cognitive biases affects us as investors.



About the author

Hayato Nakayama is an investment analyst at SilverCross Global Small-Cap Fund. SilverCross is an asset manager based in Amsterdam, The Netherlands. It is focused on managing a high-conviction global small-cap equity portfolio.

To be an investor is to be a lifelong learner

In conclusion, in our work as professional investors, we are continuously trying to improve our process of investing. In this pursuit, we believe it requires a generalist approach in our analytical process rather than having each analyst become a sector specialist. We feel this is a source of creativity that leads to insights others might not see and it can make us better investors. This is an important component of our research process in a time where information is readily available to everyone thanks to the internet.

We think there is also a secondary effect. For every unfamiliar company we analyze, we learn how to be beginners again, *we are learning how to learn*. Each time we do, we are able to learn more efficiently. This again, helps us become better investors over our lifetime and keeps us humble.

Lastly, it teaches us that it is never too late to start learning something new. Through these articles we look forward to sharing more 'tools' that we hope to acquire over the years.

"Progress is impossible without change, and those who cannot change their minds cannot change anything."

- George Bernard Shaw

Sources:

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- ³Root-Bernstein, Michele & Root-Bernstein, Robert. (2022). Polymathy Among Nobel Laureates As a Creative Strategy— The Qualitative and Phenomenological Evidence. *Creativity Research Journal*. 1-27. 10.1080/10400419.2022.2051294.
- ⁴Tetlock, P. E., & Gardner, D. (2016). *Superforecasting: The art and science of prediction*. Broadway Books.

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