Can This 1 Simple Trick Increase Your Investment Returns?

Description

One of the things I like most about investing is there isn't always a direct correlation between hard work and success.

Take many prominent hedge funds as an example. These firms are filled with the smartest minds in the business who have access to the world's best data. And yet, many of these funds have long periods of underperfomance, although some of that can be attributed to fees.

I also know individual investors who did incredibly well over the years buying and holding some of Canada's most boring blue chips, all while reinvesting dividends. Investing doesn't get much simpler than that.

There's another simple metric I prefer to look at–one I think will help me get excess returns. Here's why I'm following the money, so to speak.

The rich get richer

It's an unfortunate reality, at least for some of us: the rich keep on getting richer.

It's an expression so overused, it's practically become a cliché. It's also the basis of what I believe to be a powerful view of investing.

If someone has become a millionaire or even a billionaire by starting a company from scratch and growing it to a dominant player, they're pretty smart. That kind of growth isn't a fluke. It's an indication that a smart person is in charge.

If that person made intelligent decisions in the past, chances are they will make similar decisions in the future. After all, the rich get richer.

I'll admit, this revelation is hardly ground breaking. I don't have any data to back it up, either. All I know is, I'd rather bet on a smart founder than a mediocre management team any day of the week. It's a simple theory. It's also a powerful one.

Reitmans

There's another wrinkle to my theory. It isn't just enough to buy a stock with high insider ownership. I also want to load up when shares are cheap.

Reitmans (Canada) Limited (TSX:RET.A) fits the bill. The company is cheap on a number of metrics, including price-to-sales and price-to-cash flow. The company has took its medicine and closed more than 100 underperforming locations, including axing its Smart Set banner completely. Its balance sheet is also debt free with more than $163 million in cash. The company also pays a generous 3.1% dividend.

And, perhaps most importantly, the two Reitman brothers own a substantial stake in their own company, which has been in the family since 1926. Insiders own a combined 7.644 million shares, or more than 10% of the company.

Fairfax Financial

Another example is **Fairfax Financial Holdings Ltd.** (TSX:FFH)–a company almost legendary among value investors in Canada.

Prem Watsa, the man in charge of Fairfax, has done a terrific job replicating Warren Buffett's success here in Canada. Fairfax's many insurance subsidiaries deliver plenty of capital for Watsa to invest in undervalued securities. In fact, Fairfax is one of Reitmans's largest shareholders.

It's been a winning formula over the years. Since Watsa took over in 1985, Fairfax has grown book value by more than 20% per year, at least until the end of 2015. While 2016 has been a little disappointing, shares are trading at only a fraction above their book value, so now is a fantastic time to pick up Fairfax shares at a bargain-basement price.

Oh, and Watsa is Fairfax's largest shareholder, owning approximately two million shares–a stake worth approximately $1.2 billion.

The bottom line

I don't think investors can outperform the market by looking just at insider ownership. Execs of many failed companies went down while owning stock that was once worth millions of dollars.

But at the same time, I think insider ownership can be a valuable part of an investor's toolkit. Betting against rich people is usually a sucker's bet, especially those with a demonstrated history of success.

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TICKERS GLOBAL

1. TSX:FFH (Fairfax Financial Holdings Limited)

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