

In an era where broad diversification is a widely accepted tenet for mitigating risk, we ask a critical question: What risk are you mitigating? We define risk as the permanent impairment of capital, not volatility or being out of step with a benchmark. In fact, over-diversification may introduce a different risk — the risk of diluting our best ideas — and so, we take a different approach.

Our Micro Cap portfolio, comprising approximately 30 carefully selected stocks, represents a deliberate concentrated strategy designed to generate differentiated returns. This approach reflects our genuine, fundamental belief that proper risk management stems from a deep understanding of what you own, not from owning a little bit of everything.

The Empirical Case for Being Different

Now relatively commonplace within the investing vernacular, the term “active share” — which measures the percentage of a portfolio that is different from its benchmark — was coined as part of an [influential paper by Martijn Cremers and Antti Petajisto](#) published in 2009, which provided empirical evidence that over a decade-plus period, the highest active share funds outpaced their benchmarks and their overdiversified counterparts.

Also in the study, managers with low active share — often referred to as “closet indexers” who charge active management fees for index-like (or worse) performance — were shown to consistently underperform over various time periods.

Fast forward to today, and their research remains influential in shaping how investors think about differentiation and conviction in portfolio construction. Active share is widely used as a tool to help identify true active managers and to distinguish them from closet indexers, many of whom have lost market share over time.

Looking different from the benchmark is a necessary, but not sufficient, condition for outperformance. Managers need conviction, and academic research consistently supports patient, concentrated investing as a pathway to superior returns. Some of the most persuasive evidence comes from a [2020 Harvard study](#) examining managers’ high-conviction positions, or “best ideas.” The researchers concluded that these positions outperformed both the market and other portfolio holdings, delivering annual excess returns of approximately 2.8% to 4.5%.

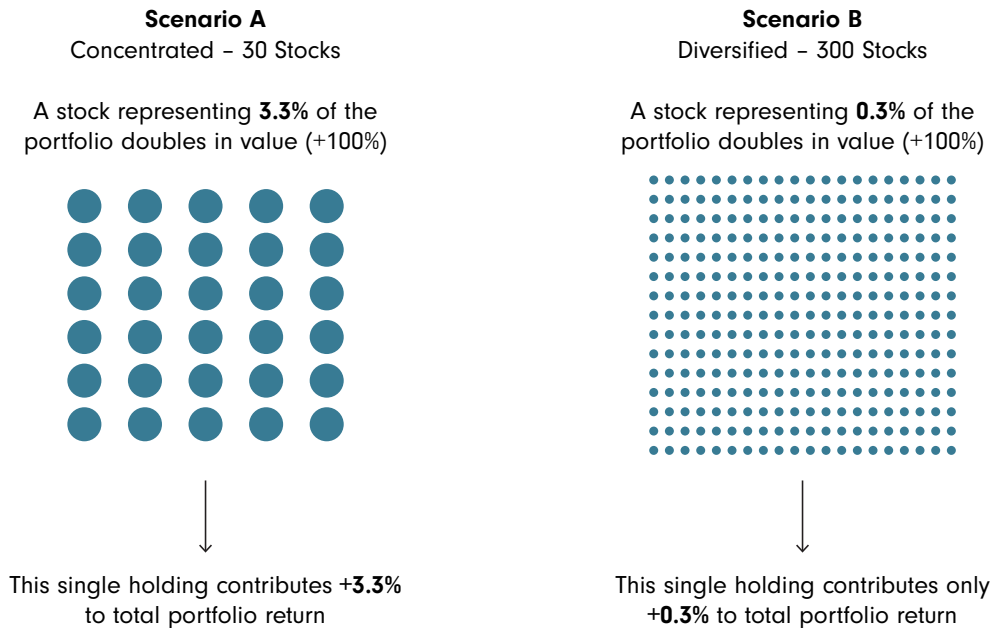
Concentration has the potential to magnify the contribution of successful investments, rather than diluting the best ideas with lower-conviction holdings that mainly serve to reduce tracking error. To that end, when we examined the contribution to return within our Micro Cap strategy, we found that roughly 80% of our overall return since inception has been driven by our top five contributors -- reinforcing the notion of leaning into our best ideas.

The Competitive Advantage of Focus

Beyond the empirical evidence, concentration makes intuitive sense: good investment opportunities are genuinely scarce. Managers diligently searching for opportunities within their circle of competence in efficient markets may only find a few compelling investments each year. When such opportunities are discovered, it makes sense to hold substantial positions rather than dilute conviction through excessive diversification.

Warren Buffett captured this concept in his 1996 Letter to Shareholders: “What an investor needs is the ability to correctly evaluate selected businesses. Note that word ‘selected’: You don’t have to be an expert on every company, or even many. You only have to be able to evaluate companies within your circle of competence.”

Concentration provides the ability to take advantage of this notion. The ability to focus on a smaller number of companies, in our view, creates a competitive edge versus more diversified funds. Deep research is our primary risk management tool — we prefer to know everything about 30 companies rather than a little about 300.



Source: For illustrative purposes only. Not indicative of actual performance, and not a guarantee of future results.

This focused approach aligns perfectly with our view of risk. While a widely diversified portfolio may feel “safer” as it closely tracks the market, it won’t necessarily protect principal or grow wealth. We believe the way to truly manage risk comes from understanding what you own: the quality of the business, the strength of its competitive position, the capability of its management, and the attractiveness of its valuation.

The rigorous research required to maintain conviction in concentrated positions creates a steep hurdle that we believe adds value. Each position in our portfolio has undergone multiple layers of analysis, from initial screening to ongoing monitoring. This process ensures that we’re not just diversifying away risk by diluting the impact of our best ideas but actively managing it through superior knowledge.

Conclusion

Concentrated investing isn’t about taking bigger risks — it’s about taking more informed risks. By focusing our research efforts on a select group of high-conviction ideas, we believe we can achieve a deeper understanding of our investments and better position ourselves to generate differentiated returns.

The academic evidence supporting concentration is compelling, but the logic is even more so. In a world where good investment opportunities are scarce, particularly in the micro-cap space, spreading capital across too many positions dilutes the impact of our best ideas. We would rather build wealth through a focused portfolio of thoroughly researched, high-conviction investments than achieve market-like returns through diversification.

Our approximately 30-stock concentrated approach represents a deliberate choice to prioritize conviction over comfort, knowledge over diversification, and long-term performance over short-term tracking error. In the micro-cap universe, where information inefficiencies create the greatest opportunities for skilled investors, concentration isn’t just a strategy — it’s a competitive necessity.

Active Share measures the difference between portfolio holdings and the benchmark. The higher the active share, the greater the risk.

Tracking Error is the difference in actual performance between a position (usually an entire portfolio) and its corresponding benchmark.

The views expressed are those of the author as of September 2025 and are subject to change without notice. These opinions are not intended to be a forecast of future events, a guarantee of future results or investment advice. Investing involves risk, including the possible loss of principal. Past performance is not a guarantee of future results.