

Brad Brain: How to create wealth

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Brad Brain: "As I have been analyzing various investment opportunities, my core beliefs have been reinforced. Fundamentally, in order to accumulate wealth you need to own assets that increase in value."

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Last year I launched my own investment fund as Portfolio Manager. Consequently I have been spending significant time mulling over various investment ideas.

I have kicked the tires on a lot of potential investments. I have even taken second and third looks at ideas that I have previously dismissed for individual clients, thinking that perhaps they might have a specific role to play in a larger investment pool.

Some of the things I have looked at are fairly exotic. But when it comes right down to it, despite the innumerable things you can do with your money, there are only a handful of reasons why you would own an investment. The most common ones are growth, income, liquidity, capital preservation, diversification, or even speculation. At least those are objective reasons.

When it comes to investing the most important thing is to make decisions that are consistent with your financial objectives. Nothing else even comes close.

As I have been analyzing various investment opportunities, my core beliefs have been reinforced. Fundamentally, in order to accumulate wealth you need to own assets that increase in value. As my friends at Value Partners Investments say, the most certain way to create wealth is through the ownership of profitable businesses

Owning profitable businesses might seem like something that is good in theory but hard to accomplish, but it is actually very simple. You can purchase shares of publicly traded businesses through the stock market, and you can do this easily with mutual funds or exchange traded funds. So let's not worry about the "how" for now, and focus on the "why".

The most profitable businesses are difficult to live without, difficult to compete with, difficult to replicate. I will use some examples to illustrate. Let's say that you have a choice between investing in a Canadian bank, or a marijuana company.

The first criteria is whether the business is difficult to live without. Could you live without a bank in your life? It would be hard. Banking is how we receive money, and how we pay it out. It's where we go to borrow money when we buy a house. It's where our savings account, and chequing account, and line of credit, and car loan, and credit card, and foreign currency exchange, and mortgage all live.

The second criteria is whether the business is difficult to compete with. How would a competitor compete with a Canadian bank? I am not sure. There are international banks, but they don't have the same presence in Canada. There is technology, but Canadian banks are embracing technology too. Canadian banks are 800-pound gorillas. Pretty hard to compete with.

The third criteria is whether the business is difficult to replicate. Canadian banks have billions of dollars in assets, coast-to-coast infrastructure, and are federally regulated. It would be extremely difficult for a new entrant to take away market share.

Let's contrast the Canadian bank with a marijuana company. Can you live without marijuana? For millions of Canadians the answer is yes. Is it difficult to compete with? Not at all. Most of the market share is still on the black market. Is it difficult to replicate? Nope, you can grow your own.

So guess what the implications for profitability are? No surprise, the Canadian banks are making billions of dollars in profit, while the marijuana companies are losing money.

This is what we look at to define what makes a good business. But our work is not done yet. What makes a good business a great investment is the price that you pay. Get these things right and you are on your way to creating wealth.

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