

Matarin Capital Management, LLC aspires to be a symbol of stewardship within the investment management industry. We are dedicated to delivering above benchmark risk adjusted investment returns through insight, passion, and diligence. We aim to build strategic alliances with our clients based on the highest ethical standards.

Investing in Innovation

There is a rising call for corporations to make investments for long-term benefit, rather than simply focusing on short-term returns. But there is an outstanding question about what kinds of capital allocation decisions management teams should focus on. At Matarin, we shy away from companies that are “[Empire Builders](#),” where company management is more concerned with acquiring control over a larger domain than optimally allocating company and stakeholder resources. This empire building manifests itself in excessive spending on capital expenditures or M&A that may prove, at the end of the day, to have been little more than expensive vanity projects. So what kind of capital spending will truly lead to long-term gain?

One area of investment that can benefit both the corporation and society is research and development. At Matarin, we like to invest in companies that are today’s innovation investors and tomorrow’s innovation achievers, investing in research and development (R&D) today, with the future in mind. During Q3’19, we have added a new indicator to our stock selection models within the People concept to reflect this idea.

Innovation is an increasingly important part of the global economy, and R&D intensive companies represent a rising share of the overall market. The chart on the right shows that the revenue share of the industry groups which Matarin considers to be meaningfully driven by R&D has increased from roughly 44% to roughly 51% over the last 10 years. Therefore, it’s important for investors to get this right.

Investing in R&D is attractive to us because we are long-term investors. For a short-term investor who’s merely focused on the next quarterly results, companies investing for the future may be viewed negatively. The R&D expense will decrease short-term earnings and cash flow. As a result, in the short term, these companies may look less fundamentally attractive.

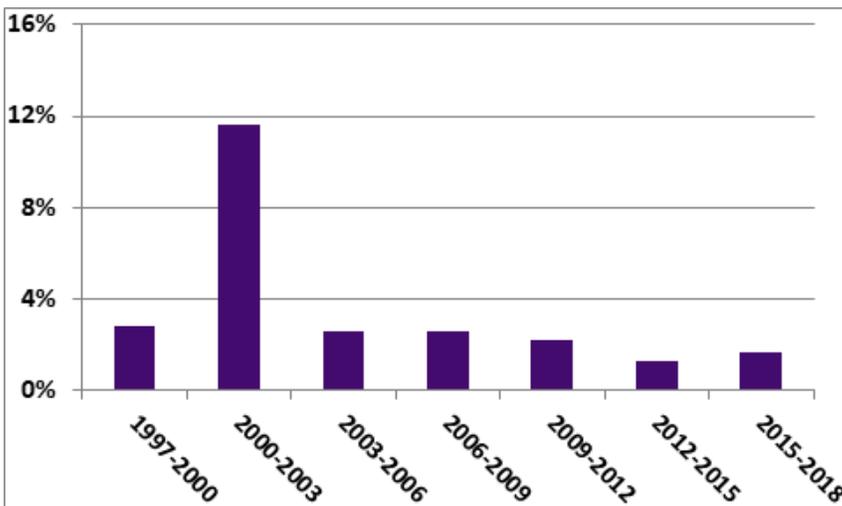
But in the longer term, spending on innovation should lead to better business results. The following table demonstrates that when compared with stocks in their own peer group, the highest R&D spenders tend to show greater improvement in 3-year sales per share growth than companies with the lowest R&D expense, by anywhere between 1% and 12% over the last 20+ years. These companies’ stocks also tend to outperform over multi-year periods.

As investors, if we are willing to focus on longer-term ideas such as innovation, and stick with them, we should be able to earn a patience premium that will benefit us both as shareholders of leading businesses and stakeholders in a bright future.

Revenue Share of R&D Intensive Industries



Difference in Sales Growth Change for High vs. Low R&D Spenders



Sources: Compustat, FactSet, Standard & Poors Data as of September 30, 2019