

DON'T FEED THE BEARS

NOVEMBER 2007

My daughter is afraid of bears. I am still trying to figure out where it comes from because she is downright terrified of them. Even songs that mention the word bear get her nervous. I have tried in earnest to explain that bears don't live in Florida and that she has no need to worry. Investors, like my daughter have an irrational fear of bears as well. The hysterics and irrational behavior of investors at the slightest sign of a bear market is something to behold. Fear is the most powerful and driving force on Wall Street. Whether it is fear of market downturn or fear of missing an opportunity, fear sets the trap.

This past year was a perfect example of the futility of timing markets. We started the year going like gangbusters, full speed ahead, only to be derailed by some statements made by the Chinese government in February, where we saw an 8% correction. Then from March through mid-July the markets raced ahead from 1380 on the S&P to 1540. Then the credit crunch reared its ugly head and we were in the midst of an all out freefall, dropping 10% in three weeks. The Federal Reserve stepped in and the market did an about-face, and away we went all the way back. Halloween comes and goes, and the month of November turns out to be credit crunch II, and another 10% correction. The only discernable pattern from this is the reaction from the media pundits. It is amazing to watch the keg party atmosphere when the bulls are running and contrast it with the sky is falling; we are all going to be homeless eating government cheese attitude when the bear comes out of his cave. Any kind of perspective is ignored; the mania of the here and now is all that matters. For example: CNBC ends every trading day with one of its female reporters asking *"It's 4:00, do you know where your money is?"*

There is an old saying, "A stopped watch is accurate twice a day." That phrase comes to mind every time I see one of these ridiculous know it all stock procrastinators on the financial shows. ***"Here is Bob Jones, he called it! He said that the market was due for a sell-off in November...Hi, Bob; I bet your feeling pretty good right now."*** Do a little research on Bob and you will often find that he just happened to guess right. I met an interesting gentleman this past month who told me a story about his adventures in setting up a Palm Beach based mutual fund back in the summer of 1987. Due to the snail-like pace of the SEC at the time he was unable to get the fund up in running until November; so all the money sat in cash. His clients were furious, and threatened to sue him. We all know what happened in October of 1987. What is hilarious, yet unsurprising, was the fact that this fund was sitting in cash only because of regulatory issues. The fund managers were heralded as conquering heroes in the press for having the foresight to be out of equities, when it was nothing but blind luck.

Have you had enough yet?

Does your portfolio rely upon, even in the slightest of ways on the "Mad Money/Fast money illusion of your brokers, James Cramer's, or fancy trading software's ability to time the market?"

Are you sick and tired of chase the latest fad hamster-wheel?

There a lot of people out there who bought the mood dujour and got their head handed to them this year. Even in the late 1990's I cannot recall an atmosphere like today where investors have the ability to be so wrong so fast on so many occasions in less than twelve months. The "best and brightest" minds running these fancy hedge funds are getting destroyed in record numbers, with a body count worthy of the last scene of Arnold Schwarzenegger's film *Commando*. The reality is that you can quit you job tomorrow and instead spend 120 hours a week studying the market and the economy. You can have every business channel and receive every business

periodical. You can have the most “advanced” trading software available anywhere and you still will not be able to tell what the market is going to do.

Nick Murray states that, “*Forecasting the market thus appears to be a vicious cycle. But like all addictions, it actually turns out to be a downward spiral.*” Market chasers are no different than casino gamblers. Eventually he or she will leave all of their money at the casino; no matter how long it takes, or no matter how often he or she is momentarily “*right.*” I am no mathematical genius, but if one keeps sitting at the blackjack table, or keeps pulling the slot lever, that person **will be** broke, busted and disgusted.

Jonathan Clements of the *Wall Street Journal* writes, “*Stocks will make fantastic investments over the next 30 years if only we can just get through tomorrow. We take the market’s decline and extrapolate it into the future. We fret feverishly over our losses, even though the Dow industrials are still up 79% since 2002’s low. Our confidence ebbs away, and we grow increasingly risk averse.*”

Basic things investors need to know about the market...

The market will continue to reflect the growth of the world’s leading companies in the most innovative, flexible and transparent economy on the planet. Due to its unpredictability/volatility it will provide significantly higher returns than other asset classes. You pay yourself and invest regularly, without concern of market direction. If it appears as if the sky is falling today, and the economy is going to hell in a hand basket, you will have wished ten years from now that you would have invested in it every dollar you had. When markets correct and quality companies go on sale, investors should get as excited as my wife gets when she gets those 40% off coupons for *Saks Off Fifth*. The bottom line is that if you are not excited by the current market correction, you don’t get it; and should start reading this article from the beginning again. When markets race through the roof you should get nervous.

We discussed the importance of goal-oriented investing in our article *Financial Planning Reality*. Successful investors are those who have their portfolios managed in the service of their life’s goals, instead of trying to *beat the market*. We understand the trap. The toxic drumbeat of materialism coupled with lyrics of:

“YOU CAN BEAT THE MARKET... DOUBLE DIGIT RETURNS... PROVEN TRADING SOFTWARE...FINANCIAL GURU EXPLAINS HOW...LATEST TRADING SOFTWARE...ETC.”

All of these are temptations that are difficult to ignore. We always try to bring the highest level of returns, for our clients, however, we realize that out-performance is desirable but is not the goal. Funding a long retirement is a goal; paying for your children’s education is a goal; leaving a lasting legacy for your family is a goal. Goal oriented investing is simply about accumulating and growing ones assets to meet ones goals. The portfolio is always the servant of ones goals. A goal oriented investor acts. A market driven investor reacts.

Out-performing the market is not a difficult thing for us to accomplish over time.

If you decided to invest in the Dow Jones Industrial Average in January 2000 as of April 2006 you will have put together a gain of 12% including dividends. However, if you decided to invest \$100 in the Dow every month from January 2000-April 2006 your return according to Morningstar would be 23%. **Dollar-cost averaging** like we just described is one example of how it is done. **Compounding** is another. We always take advantage of the best safe yields we can find, and stick with them. It might be boring, but it works. **Always look for value**. Asset prices move in long patterns. Wait until an asset goes on sale so you get more for your money. Last but not least is **asset allocation**. Asset allocation, diversification and rebalancing we believe are responsible for at least 95% of a portfolios performance. Timing and selection is the rest. The reason why you never hear the financial journalists or pundits discussing these items is because

they are not **news**, but truth. They want you watching their programs and buying their magazines. Once you understand the truth, you no longer have any use for their **news**.

We are not stock pickers, mutual fund handicappers or fortune tellers. We are financial planners; we deal in reality and understand the truth about our profession. What it is, what it can do for people, and what our limitations are. Truth of the matter is there is not a soul alive who can tell what direction the markets are going to go, or how a stock is going to trade over the short-term. If you are looking for someone to guess where XYZ Corp. is going to be trading next month look elsewhere; and might we suggest a casino.

After further thought and reflection about this bear fear thing, I realized that my daughter's fear is much more rational than investor's fear of them. On the one hand, real bears show no similarities to Winnie the Pooh or Bear in the Big Blue House. They are a lot more like the Grizzly in the movie *The Edge* that I wished would have eaten Alec Baldwin. Bears can kill you.

On the other hand, stock market bears can put a lot of money in your pocket and will only devastate you if you do something irrational. My daughter's fear is instinctual which helped to keep our hunter-gatherer ancestors alive for thousands of years. However, that flight instinct, getting out of harms way when faced with danger can ruin a portfolio. Investors are essentially programmed as human beings to do the wrong thing.

Our job is to keep you focused on your goals, not the bears.