



Staying the Course is Hard Work

Why Aren't We Benefiting From The Recent Moves In The Stock Market?

Recently, several clients asked me why we are not benefiting more from the recent stock market gains. To one I responded: "You are NOT benefiting from the current run up in the stock market for a good reason. What you ARE benefiting from is having a very conservative portfolio that will not be taking a -20% to -30% in the next few years when this irrational exuberance has run its course."

One of the hardest lessons for most investors is to stay the course during times when it is temporarily out of favor in the markets. Particularly if some other strategy or asset class seems to be making money easily and safely. For most of my clients, at our ages and with our assets, there is no sane reason why we should take any unnecessary risks.

Most of us are at the age where a huge loss might negatively affect our lifestyles. If we keep our investment portfolios safe – even if they earn very little for a while – we still have enough assets to live a comfortable life.

In my judgment (and in the judgment of many othersⁱ) we are late in a bull market that has run for 10 years, now approaching the longest run up in history boosted by an extended period of the lowest interest rates in history.ⁱⁱ These are NOT ordinary times from an historical perspective. In addition, the stock market is currently aided and abetted by tax cuts paid for with money borrowed from the future. In my judgment it is never a sound investment practice to enter into highly speculative market fueled by borrowed money unless I also know how I can get out quickly enough when market sentiment changes and a crash comes. With respect to bonds, I do have such a method. With respect to stocks, I do not have such a method and I don't know of any other investment manager who does.

One of my favorite managers (now retired) was Jean-Marie Eveillard. He had the best record for 27 years in global funds up to 1999. He was a "value manager", meaning he only bought stocks that he thought were underpriced. However, in 1999 he began to lose clients because most mutual funds were doing far better than his that year. He was asked by a reporter if he would "change his strategy" because he was losing customers. His reply was, "I would rather lose my customers than lose my customer's money."ⁱⁱⁱ (It took us several more years to recognize and rename 1999 as the "Dot Com Bubble".) When the crash came in 2000-2002 Jean-Marie Eveillard's existing customers made money when almost everyone else lost a lot.

Rising Interest Rates Affect Conservative Asset Classes First

So far this year, we are making almost nothing in our conservative portfolios due to the Fed raising interest rates. When the Fed raises interest rates bond portfolios are negatively affected in the short run, even though higher interest rates should lead to a healthier bond market over the next couple of years. At the same time, as we saw earlier this year, higher interest rates can cause sharp breaks in stock markets. Even though the stock market has recovered from the February setback, margin debt in the stock market has climbed even further into record territory.^{iv}

Successful investing is difficult precisely because times when it looks like money is extremely easy to make are often times of the greatest danger for huge losses. Be patient. At this stage of life most of you need safety much more than you need a quick, but dangerous runup. The joys of the short-term profits can quickly evaporate in a sharp downturn which might take away much more than just the recent profits; downturns can also take away some of your other hard-earned money as well.

Feel free to call me or email me with any of your specific questions or schedule a phone appointment for a more complete review.

Michael Coleman, Ph.D.

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ⁱ <https://www.forbes.com/sites/baldwin/2018/07/17/three-metrics-of-stock-market-overvaluation/#237f66df7fff>

ⁱⁱ <https://www.businessinsider.com/interest-rates-5000-year-history-2017-9>

ⁱⁱⁱ <https://www.valuwalk.com/jean-marie-eveillard-resource-page/>

^{iv} <https://seekingalpha.com/article/4150526-2018-year-margin-call>