

## IS THIS FOR REAL?

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*This newsletter was originally sent to you in an e-mail on November 9, 2009. We have provided a hard copy with your quarterly report for your convenience.*

The DOW passed the 10,000 mark.

The question of the month from clients is: So is this for real? We have no idea, and anyone who says they do has no idea what they are talking about. As we have said for over a decade, the market, in the short run, is completely unpredictable. If the last few months do not make you a believer, then nothing will.

The Dow Jones Industrial Average, a U.S. stock market index, dove 27.5% in the first 9 weeks of the year, adding to a nearly 34% 2008 loss. *The market is now up 60.09% since March 9<sup>th</sup>, with 42.1% of that coming in just 19 trading days.* I challenge you to find *anyone* that predicted the steep market gains (to this degree) in recent months. That person does not exist, despite all the talking heads making predictions literally every hour on cable, radio, and the internet.

***“When the recession is ‘over,’ it is too late to get in on the gains.”***

This rally could be the beginning of a new bull market, as the stock market traditionally recovers most of its losses well before recessions end. On the other hand, it could be a classic “bear market rally.”

For a sense of history, check out the market returns during the Great Depression. (No, I am not trying to scare you. I am just illustrating that even long bear markets have very high positive returns in the middle of them.) This example illustrates the rallies that occurred during the worst bear market in U.S. history:

06/24/30 – 09/10/30: +15.69%

12/16/30 – 02/24/31: +23.39%

07/08/32 – 09/07/32: +93.91%

02/27/33 – 07/18/33: +116.65%

03/14/35 – 04/04/36: +66.99%

04/28/36 – 03/10/37: +32.47%

03/31/38 – 08/06/38: +47.22%

The numbers are so incredible, I had the investment managers triple check them. Bottom line: this could simply be a bear market rally. The market could be wrong in its guesstimate

## IS THIS FOR REAL?

that the recession is ending.

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On the other hand, when the recession is “over,” it is too late to get in on the gains. The market historically recovers most or all of its losses well before a recession is officially declared over, with most of the recovery happening in the first few months of the market rally. The majority of economists and Wall Street strategists think the economy has bottomed, or is going through a bottoming process (for whatever that is worth). The market usually moves up in anticipation of a recovery.

As we have stated repeatedly, this is not the Great Depression. There are many differences that have been highlighted in previous newsletters. However, just because the market has gone up over 50% in the last few months does not mean that we are out of the woods yet.

The reality is that over the short run, the market is unpredictable, but over the long run it is very predictable (it goes up – over and over again). The stock market may be correct this time in predicting that we are on our way out of a recession, or it could simply be the third false start. This upward trend simply feels better because it has been a consistent climb rather than the wild swings that accompanied the last two upswings. This is why even though we were buying stocks during the market tumble into the 6000’s, we are not over allocating to stocks beyond the amount that is appropriate for your long term goals.

Strategists, as always, have strong predictions. The lead strategist at Goldman Sachs declared recently that we are currently experiencing a “sustained rally,” and that it is a great time to overweight stocks, at least for the next few months. The same week, the lead strategist at Morgan Stanley / Smith Barney declared that the market was overbought and due for another downturn, and advised investors to sell into the rally and underweight stocks.

The reality is neither knows the answer, and despite their confident rhetoric, they may as well flip a coin. Our position is simple: no one knows what the market will do tomorrow, next week or next month. However, over long periods of time, the outcome becomes predictable. The key to surviving bear markets is to stick with the plan and not be scared out of the market when everyone is fearful and to avoid getting greedy when everyone feels good. The best way to deal with market movements is not to attempt to time short term movements, but to follow, in a disciplined fashion, a coherent strategy. If you have a friend, family member or colleague still dealing with a broker that thinks they can time the market, we would love to meet them.

*“A prediction about the stock market tells you nothing about where stocks are headed, but a whole lot about the person predicting.”*

*-Warren Buffet*

The DOW sometimes passes a number and blazes ahead. During the Great Depression, the

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*“Our position is simple: no one knows what the market will do tomorrow, next week or next month.”*

DOW was at 24. Not 2400, but 24. At the time, 10,000 seemed unfathomable. On the other hand, the market can pull back often. When the DOW passed 10,000 on Friday, it did so for the 29th time in market history.

The market, as it always does, will sort itself out, leaving behind many of those who tried to time its short term movements. In the meantime, know that the more confident a market prognosticator, advisor or talking head is with their predictions, the less credible they become. Warren Buffet

had it right when he said *“A prediction about the stock market tells you nothing about where stocks are headed, but a whole lot about the person predicting.”*

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