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As the stock market has behaved sickeningly over the past year and a month, I've had many conversations with investors that drive home a most important point. Investing and markets may be subject to massive amounts of mathematical analysis, but they are truly and basically about human behavior. That fact can make my job challenging.

Back in late 2002, as the stock market was most of the way through a 40% + decline over two years, I developed an idea for a portfolio based upon a favorite term of hedge fund management; absolute return. Those words are used to mean a positive return every year and some of those hedge funders claimed their target for that absolute return was 15%. Shades of Bernie Madoff! I am pleased to say that I immediately stated that 15% -a- year-every-year was unattainable. What I, in fact, had developed was a rather low risk stock/bond portfolio. And in the fall of 2002 the idea got its first taker because as the dot-com bubble was bursting folks were scared.

That portfolio rode out 2002 well and progressed into early 2003 with nice returns. That's where human behavior came in. The year 2003 is something in my hopes and dreams. After that two year drop of not just dot-coms that took the market down over 40%, it rebounded in 2003, rising over 26%. And, even though their conservative portfolio was performing nicely, the folks who had chosen it six months earlier came to me and said, "We'd like to get more aggressive with our portfolio." So I carried out their wishes.

I must emphasize here that I have never criticized that decision on the part of my friends. It is simply an example of how financial markets are all about human behavior and what a challenge that presents to investors and people to whom they turn for guidance. The first piece of advice I got, from a friend who, in 1973, was an institutional broker at E.F. Hutton, was, "The most important thing you have to do is determine your client's threshold of pain." And, he went on to tell me this was not an easy task.

There is one fascinating piece of mathematical data on markets that I recently saw in a piece from Davis Advisors; a New York investment firm. Over the past 20 years equity mutual funds had an average annual compound return of about 11.50%. However, a typical shareholder over that time received an average return of about 4.50%. The reason for this semi-astounding difference is, again, human behavior. There are very few people who have the courage to rely upon asset allocation as the bedrock of their investment strategy; especially in 2009. Yet, here is powerful evidence. The obvious reason for the difference between funds performance and that of their average client (7%) over 20 years is that the funds were always in the market and the customers weren't. And, it's obvious that for the vast majority of those customers, timing did not work.

Finally, I must add that those friends, who chose to get more aggressive in 2003, chose, in June, 2008, to get out of stocks altogether. I find the study cited by Davis Advisors to be a compelling argument, but I'm sure going to keep an eye on what these friends choose to do with their portfolio.