

Lake County Contractors Association Professional Practice Report

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TWELVE LESSONS LEARNED FROM VOLATILE MARKETS

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In conjunction with Lincoln Financial Advisors

"Experience is the name everyone gives to their mistakes." Oscar Wilde

As such, there has been a lot of talk about the experiences learned from the volatile markets this past year. What's often said is that we should, "learn from our mistakes." To assist you in learning from 'mistakes made' due to the volatile markets, here's a list of 12 lessons that may help you in planning your market strategies in the future:

1. There is no such thing as "short-term investing." The term "short-term investing" is an oxymoron. Put bluntly, a short-term financial focus is speculation, not investing. Investing is a fundamental commitment of your capital to the pursuit of the greater goals in your life – a dignified and independent retirement, the education of your children or grandchildren, a legacy for your heirs or your community.
2. Valuation still matters. If you begin to believe "it's different this time," you are wrong – it's not. When valuations are far above their historic levels, there is good reason to be concerned. Good companies may remain good companies, but they may not continue to be good stocks. When this basic principle of investing is ignored, you will eventually pay the price.
3. Markets go through cycles. Effective investing during market cycles requires decisions that may be uncomfortable. When markets are most optimistic and exuberant, we should be cautious and ask "why?" When they are most pessimistic, we should see opportunity for the long-term investor. At all times, we should have a written plan as a discipline to guide our decisions and help us through the tough times. Sir John Templeton, one of the founders of modern international investing, believes that the real buying opportunities are at the time of maximum pessimism – "when the blood is in the streets."
4. Asset allocation is a diversification strategy that works. It cannot offer a guarantee against short-term market losses, but it is an effective investment risk management tool. Sector concentration, no matter how attractive the sector may appear, no matter how compelling the arguments, is still speculation.
5. There is no opportunity for return without some risk. If you don't see or understand the risk, keep looking. It's there. Once you find it and understand it, it may be acceptable. But until you identify the risks, they are unacceptable.
6. Most dollars flow into high-performing investments AFTER the performance has occurred. The single most abused tactic is for investors to chase last year's performance. A disciplined investment plan and investment selection criteria are critical if you want to avoid making this mistake.
7. Market indexes can tell a very distorted story. They don't really measure "the market." The success or failure of your investment plan should not be measured against any single index. The success or failure of your plan should only be measured by whether or not it is meeting your long-term goals over a full market cycle. If it is, it's succeeding. If it is not, it may be failing.
8. A well-balanced portfolio should be diversified among the major asset classes. Cash. Fixed Income. Large and small companies. Growth and Value. Domestic and international. The only guarantee is that some of these areas will periodically disappoint you. But

you never know which ones or when. Your plan will succeed only if you stick to your plan and remain invested across several asset classes.

9. Years of high returns can be completely reversed by one bad year. That's why you shouldn't use short-term criteria to judge long-term results. That can lead you to unknowingly creating a very high-risk portfolio. Ultimately, consistency is more important than an occasional "home run."

10. The traditional rules of investing are still true. While they can be adjusted periodically to fit some of the finer points of the current economic environment, we should never abandon the core principles of diversification, sound values, patience, following a sound plan and maintaining a long-term perspective. Know the rules and know when you are breaking them.

11. Raw information is not knowledge – and just knowing the facts won't necessarily make you any wiser. The financial media in all of its forms – television, radio, newspapers, magazines and the Internet – survives on stimulating emotion and fostering the

belief that "every second counts," that the ability to react and trade instantly is an improvement over patience, discipline and a sound investment plan. Warren Buffett, the well-known value investor, believes that the daily movements in the stock market don't reflect the true value of companies, but rather the emotional temperature of investors.

12. Market timing doesn't work. Moving into and out of markets based on any anticipated changes in price as opposed to fundamental changes in value is speculation – not investing. Peter Lynch, the former manager of The Fidelity Magellan® Fund believes, "Far more money has been lost by investors preparing for corrections or trying to anticipate corrections than has been lost in corrections themselves." This review has reaffirmed and strengthened our basic investment planning process. It has also strengthened our resolve to remember and apply these lessons in the future. Investing clients' serious money requires discipline, patience, objectivity and a clear, documented investment policy that is focused on their personal needs and values. As financial planners, this is the minimum standard to which we should be held.