

MORNING OBITUARY— BUY AND HOLD INVESTING

Based upon what I have been hearing via the market pundits, it appears as if the funeral procession for buy and hold investing has recently left the chapel. Without question the recent turmoil in the markets left most buy and hold followers wondering whether they were lemmings foolishly following the pack over a cliff. That maybe so depending upon your viewpoint, but I am not so sure I am ready to jump on the bandwagon and write it off just yet. First of all, "Buy and Hold is Dead" because it was never really born to begin with. It was never meant to be interpreted as buy and ignore which is what it had become. "Buy and Hold" was intended to be a phrase for promoting patience with an investment. Somehow this patience turned into a deep sleep as the go-go years of the past two decades proved that anyone could make money, even those who were asleep at the wheel. Because the markets were rarely challenging, over time investors became accustomed to consistent above-average returns. They learned with Pavlovian-like response that they could just throw their money at the market with no real strategy and their dreams of massive wealth would come true. Unfortunately, we learned this past year that things can change in an instant.

First it is important to understand a few things:

1. Unlike trading where you are jumping in and out of the markets based on short term trends and trying to make a quick buck, "buy and hold" refers to an investment strategy that involves buying investments and holding them through the up's and down's of their inevitable price fluctuations. This is done on the theory that doing so will be more profitable than the pointless efforts of market timing and oft hyped and oversold stock-picking strategies. This assumes the investments chosen continue to warrant holding until an underlying fundamental change takes place that threatens the businesses success.
2. Despite the near absence of a pure buy-and-hold strategy, in every bear market, like clockwork, attention and money driven market pitchmen across the country take the stage to administer holy rites and declare that "buy and hold" is dead and they have found the way to the fountain of eternal riches. This is in an attempt to capture the enormous number of disgruntled investors who have lost money and are looking for a new and foolproof way to make them rich.
3. Like most things in life, a "buy and hold" strategy really doesn't exist in its purest form. Most advisors I know who followed the buy and hold mantra were taught to rebalance their client's portfolios periodically to manage portfolio risks and capture diversification benefits. Additionally, advisors would adjust portfolio allocations to account for changes in a client's life circumstances or when their research led them to the new idea or useful new investment products (such as ETF's). The idea was to not actively trade a client's account but rather make strong up-front investment selections and hold until a compelling event signaled that a change was needed. That event could be triggered because specific investment event or even as importantly, a change in long-term economic fundamentals that was not present at the time the investment was chosen. The past (prior to 2008) economic and investment landscape was such that this methodology would facilitate success and was supported by compelling long-term statistical data. So, it was not truly "buy-and-hold" but rather "buy-monitor-and-change as needed."

Warren Buffett, the champion of the "buy and hold" strategy, has built a hundred billion dollar company by following this type of investment strategy. However, both Mr. Buffet and the "buy and hold" followers have taken it on the chin in the past year. People who employed this style of investing have seen decades of gains get flushed down the toilet in just a few short months. As such, for the average investor who is short on patience but long on memory, the "buy and hold" investment philosophy is likely to be dead for a while until faith in the markets has been restored. Investors will need to get excited again about the long-term prospects of the markets, and in order for this to happen, a sustained bull market will need to take place. There will always be the short term speculators who see an opportunity in any environment but true buy-and-holders are now very wary of the markets and have become gun shy towards investment risk.

In summary, buy and hold, properly defined, is not a static, one-size fits all investment strategy -- it is a philosophy -- one that speaks to the virtues that embody successful financial behavior -- simplicity, moderation and patience -- the same virtues that define the one investor that may embody this buy and hold philosophy more than any other investor -- Warren Buffett.

Like the Great Depression, the current crisis has changed the United States and possibly the world forever. While the final outcome is uncertain, what can't be denied is that in the years to come, because of their inexorable link, the world economy, investing and financial planning will never be the same. As such, investors will not only


need to adapt to the current new investing paradigm created from the latest bursting bubble(s) but also be flexible and open to change because I expect to see dramatic changes going forward based upon structural shifts to the world's economic model which include. Some of these are in process and others will take a long time to unfold.

- Massive Governmental debt loads that could take decades to wind down
- Increased taxation or excessive inflation in an effort to reduce debt
- Ongoing consumer and corporate de-leveraging (which will be offset by that taken on by the government)
- Increased regulation and oversight muting the liquidity and freedom of unabated market movements
- Increased consumer savings
- Global economic power shift from a US-dominated sphere of influence to a multi-national one
- Debasement of the US Dollar
- Reduced appetite for investment risk
- Muted long-term US growth
- Focused growth opportunities in demographically favorable countries

While one could argue that some the above shifts have been on the radar for years, they had been overshadowed and virtually ignored by retail investors due to the continued historical upward momentum of stock prices. This euphoria was driven by massive expansion of US consumer debt fueled by the Fed's "cheap money" policies of the past decade and like all bubbles before it was doomed from the outset and was just a matter of time before it burst. Our past indulgences have come back to roost and will take years to unwind. As investors, never in the past have we faced so many obstacles with so many interchangeable moving parts that will affect our investment success. Considering the headwinds investors face, now is not the time to close your eyes, let your attention drift off to other things and hope that the previously successful "buy and ignore" strategy will thrive. Success will find those who have built a "buy and monitor" portfolio ready to not only weather but capitalize on the coming shifts. Additionally, each investor will need to remain actively involved because even in a poor economic climate opportunities will present themselves but until they do capital preservation and financial staying power is paramount.

Financial Perspectives was founded in 2000 by Charles "Chuck" Gibson—a CERTIFIED FINANCIAL PLANNER™ certificant, Accredited Asset Management Specialist, and Chartered Retirement Plans Specialist—who has worked in the financial advisory industry since 1994. With more than \$40 million in assets currently under management*, Chuck and his staff have advised hundreds of individuals, businesses, and other organizations, helping them establish sound investment strategies by providing informed, objective financial planning and asset management advice.

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