

Commentary

The Death of Buy and Hold

The events over the last 6 weeks have changed the markets forever. The events unfolding today and the events yet to come will someday be compared to The Great Depression. The emergency actions taken by the US government in the last month can only be compared to actions taken by Franklin Roosevelt during that dark time. They are unprecedented in this modern economic age. The nationalization of the Global financial system will be considered a watershed event. We are in a full blown financial storm. It is the real thing.

The markets have changed as well. The old models of asset allocation used by professional money managers and financial planners are now the equivalent of your old VCR recorder. A while ago, they were cutting edge new tech and today they are garbage. The time proven adage of being fully invested at all times and simply buying and holding stocks and bonds for the long term is being crushed on a daily basis. And who invented that rule anyway? I suspect it was an idea born in a marketing meeting at a major Wall Street brokerage firm as company executives were trying to figure out an original way to retain client assets without looking greedy. And the occasional bull market would reinforce this golden rule and lead investors to the bad habit of ignoring their investments and the people managing them.

Making money on Wall Street is not about picking stocks or mutual funds that go up. Any one can do that. During bull markets you can throw darts at the stock tables and pick winners. Making money on Wall Street is all about money management and risk. You must identify your risk before you invest and then manage your money accordingly. As soon as you lose site of your risk, you lose all your money.

Unfortunately, many investors over the last few years lost site of their risk, and are now losing lots of money. Even the smartest people in the world with the best educations and a pile of advanced degrees to show the world how smart they really are, are broke. Some may end up going to jail. Most are not really that smart. But they thought they were and became the "Masters of the Universe". Even when the smartest lose site of their risk, they lose everything including their companies.

I am a firm believer in the economic theory of Creative Destruction. Championed by Joseph A Schumpeter, it simply states that the real function of capitalism is to facilitate innovation. Capitalism simply chooses winners and losers and because of this efficiency when something is no longer creating value, it is inevitably replaced by a new, more productive form. There are always vast opportunities created when this destruction occurs. The creativity of individuals within the marketplace will replace the old inefficient model or company with the new dynamic efficient one. And the opportunities are just around the corner.

This historic crisis will test this Creative Destruction theory and I believe uncover great opportunities for those investors willing to throw out their old ways of thinking and be open to exploring new ones. As Jim Bianco of Bianco Research recently put it in a report to his research clients:

"An asteroid hit in early July and all the dinosaurs are dying. After the asteroid hit, the only food left are those financial institutions that are light on mortgage holdings and get their funding from a retail base. Either get with the food source or die."

I believe the same analogy is relevant to the buy and hold strategy of investing. The only food left are those investors who know how to trade stocks, and that understand and can identify their risk and know how to manage that risk in the market. Either learn how to do this or die. .

Microsoft is trading at \$21 as I write this column down from a recent high of \$37. The first time Microsoft traded at this price was April of 1998, over 10 years ago. If you bought Microsoft then and still hold it today, you have made no money. Over this same period of time you would have been better off holding T-Bills which gave you an annualized 4.77 percent rate of return. In today's new world, portfolio values that took ten years to grow can be destroyed in

months. This is not your Dad's stock market. That has been destroyed. But in its place, creative new ideas and strategies will be born. It is up to you to open your mind and to embrace this new thinking. Economic adulthood is upon us. Don't fight it, embrace it.

The asteroid has hit and the dinosaurs are dying. If you are going to survive, you need to adapt. If you want to invest in stocks you must learn to trade. You must learn to identify your risk. You must learn to manage your money.

And most importantly, don't be a dinosaur.

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