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***"Quick decisions are unsafe decisions"**—Sophocles*

To our clients and friends:

In investing—unlike football, hockey or other "fast" sports—the turtle usually wins the race against the hare. We all know of the quarterback who garners the most accolades for "quick decision-making". We've all heard the Wayne Gretzky quote of "skating to where the puck is *going* to be, not where it is now".

However, investing is quite the opposite. As many of you know, the core philosophy of our firm is that there is never a reason to rush into buying or selling any investment.

Instead, we recommend a different approach: 1) plan ahead; 2) employ a strategy; and 3) remain flexible in your analysis and portfolio positioning. These three keys are critical to building wealth and achieving one's objective.

We all recognize that Sophocles was correct—it's best to "stick with the plan" and never let panic or fear, greed or euphoria drive your investment strategy. But sometimes a lack of discipline throws us off course, and we make the wrong decision.

"Big Picture" Thinking on Markets

I'm often asked at any given point during the year, "So what do you think the market is going to do going forward?" I always need to pause when I hear that question. Not because I don't understand the question, but because I have to remember that I have no crystal ball readily available.

My answer is sometimes rambling, other times more succinct. But as a rule, I do not try to predict what the market might do this year, next year or in the next five years. In fact, the further out the time horizon, the less likely any prediction will be accurate. I suspect you would agree that my logic on this is common sense, and is not rocket science.

Many smart commentators have been known to say: *"The market will do what the market will do".* I've repeated these words of wisdom to clients over the years. And the words are true. Observing and studying the market averages and key indicators are what guides a successful strategy, not making predictions or guesses. It is *data* which drives intelligent decision-making, not emotions.

Contrarian Thinking Makes for Contrarian Investing

We all know someone who is a full-fledged non-conformist, and marches to the beat of their own (usually a very different) drummer. As investors, we are best served by taking a cue from our non-conformist friends. "Follow the leader" is a losing proposition when it comes to investing.

The stock and bond markets are overreaction machines. Absent specific news about a company (earnings, big contract, lawsuit), most of a stock's daily price movement is just pure noise. I've addressed the danger of market "noise" to many of you in the past.

The financial media, particularly on television, offer so-called "investment advice". This includes what industry pundits have described as a "screaming madman"(Jim Cramer) and other professional money managers in suits who regularly predict the future but then are never held accountable when they're proven wrong. Just because these people are on television does not mean you should be listening to them!

"Beating the S & P 500"

When I discuss portfolio performance and investment returns with clients, I remind them that we are NOT equity-only, full "risk-on" investors. In other words, no individual client of our firm is invested 100% in stocks. Therefore, listening to the pundits talk about "the market" has diminished relevance to our client portfolios.

Instead of trying to beat "the market", we focus on two things: (a) absolute return and (b) the management of risk. One way to accomplish this is to be invested in bonds and fixed income when stocks unexpectedly fall. This can only be accomplished by proper asset allocation three hundred sixty-five days a year. The obsession some people have with beating the S&P 500 more often than not results in extremely poor results because it ignores risks taken to do that.

During 2013, many actively managed mutual funds underperformed the S&P 500. Does that mean those funds are terrible? Absolutely not! Why? The simple answer is that not every mutual fund is a domestic U.S. equity or stock fund. Making the right comparisons is crucial to understanding how to grow wealth over time, and to prevent wrong thinking and wrong decisions.

An investor doesn't need to be 100% in stocks and expose themselves to constant volatility and risk in order to have strong returns over time. Instead, it's important to minimize downside risks (and thus limit potential losses) by monitoring risk levels, studying volatility readings and measuring various other technical indicators.

The Origins of "This time is different"

Charles H. Dow, in 1900, said this about predicting future market levels:

> *"There is always a disposition in people's minds to think that existing conditions will be permanent. When the market is down and dull, it is hard to make people believe that this is the prelude to a period of activity and advance. When the prices are up and the country is prosperous, it is always said that while **preceding** booms have not lasted, there are circumstances connected with **this one** which make it unlike its predecessors and give assurance of permanency. The one fact pertaining to all conditions is that they will change."(bolding/underlining is mine)*

In so many words, Charles Dow was stating the contrarian case. And in his words there is a saying that we've all heard many times. That saying is: *"This time is different"*. It was undoubtedly borne out of the comments made in this quotation by Charles Dow.

Another well-known market guru and author, William O'Neil, said: *"It is one of the great paradoxes of the stock market that what seems too high usually goes higher and what seems too low usually goes lower."* We can all relate to the highs leading up to the peak of 2000 and the lows leading to the bottom in 2009 as a testament to this quote.

That same paradox highlighted by O'Neil can also be likened to today's market conditions. It has been said that the longer a bull market lasts—and the longer it goes without a 10% correction—the greater the odds are that this same pattern will continue.

Major trends such as the one we are now in invariably display incredible staying power. The longer a trend persists, the greater the chances are that it will continue to persist. It has now been well over two years since the stock market has corrected at least 10%. This is what has frightened the naysayers most of all. But this trend could continue.

Timing the (Bond) Market

Most of you may recognize the man in the photo above—no, it is not Clint Eastwood! However, it may be someone just as famous—the "Bond King", Bill Gross of Pimco. Gross has been in the financial news for the past several weeks, having left Pimco to join the Janus mutual fund family. He is a financial media celebrity in his own right.

Gross has for several years been the bond market's central character, caught up in the hype regarding rising interest rates. But those who made risky timing bets on bonds and decided to sell over the past few years have been unpleasantly surprised.

The so-called "experts" have predicted that interest rates would rise and therefore, yields would also rise. In fact, Treasury ***yields*** have continued to go lower, not higher, over the past few years. Lower yields mean higher principal value for bonds (i.e., the investor makes money as their principal grows). The reality has turned out nothing like the warning. These predictions are now recognized for what they were—a lot of hype.

It's true that—eventually—the principal value of Treasury bonds will decline in value—this often happens when interest rates rise. And it is agreed that "it's not a matter of ***if,*** but ***when***." However, no one knows when that will be. Obviously economists and other so-called "experts" don't know either. The experts who have been forecasting that Treasuries yields will rise (and bond prices will fall) will eventually be right, but not yet.

And as is the case with stocks, there is a cost and a risk of trying to time the bond market. This is something Bill Gross has experienced in recent years. He has been wrong on more than one occasion—not just about bonds—but also about the direction of stocks.

Market timing in bonds—just as in stocks—is risky. Lengthening or shortening Treasury maturities in bonds—just as over or underweighting stocks—subjects you to the risk of underperformance, increases uncertainty and expands the range of potential outcomes. These are risks you can eliminate by avoiding such market timing bets.

Predicting Interest Rates: A Loser's Game

Many people who have made a bet on the longer-term direction of interest rates over the past few years have been terribly wrong. As with stocks, bonds will also "do what they are going to do". No one has any control over the bond market or interest rates.

It always puzzles me when a pundit proclaims that "interest rates are going to rise, so you should lock in your mortgage rate now". I regularly decline to make predictions on the direction of interest rates because they cannot be accurately forecast by anyone.

Conclusion

In my next market newsletter—to be published in January 2015—I plan to address two related topics in more detail: 1) reducing volatility by more thoughtful asset allocation techniques; and 2) preparing for and addressing future bear markets.

Until then, thank you for your interest in this newsletter and for your continued loyalty.

Sincerely,

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Principal, Fama Fiduciary Wealth LLC, Registered Investment Advisor

Past performance is no guarantee of future results
****Nothing contained in this quarterly newsletter should be construed as investment advice****