April 2017 – Market Timing and its Follies

"Far more money has been lost by investors preparing for corrections, or trying to anticipate corrections, than has been lost in corrections themselves."
- Peter Lynch

Marty Bannon and the Relevance of a Financial Advisor

Most readers of our quarterly newsletter have not heard the name of Marty Bannon. He is the father of the current White House counselor and chief strategist Steve Bannon. *The Wall Street Journal* recently profiled the 95 year old Mr. Bannon in an article on his son. In short, Marty Bannon had a 50-year career with AT&T and had his entire nest egg in the company's stock. According to the article he often joked that he would rather quit the Catholic Church than sell his AT&T stock. The stock holding reflected his deep trust in the company and he was hoping to leave the money for his kids. Then came the 2008 crisis and what did Mr. Bannon do? He panicked and sold all his shares in AT&T. At the time, many cast the blame on Wall Street, Silicon Valley, banks, overleveraged companies etc. But let's take a minute and reflect what Mr. Bannon did wrong:

- At the age of 86, all his investments were held in one stock of a single company.

- The sell decision was not made after consulting a financial advisor, nor did he have a relationship with one to consult. He also did not consult any family prior to the trade.

- Gloom and doom were everywhere. Lehman was going bankrupt, AIG was failing, banks were forced to raise capital and there were widespread layoffs. Everything was on live television. As Marty says, he made his decision to sell all his AT&T once he heard Jim Cramer (CNBC host of Mad Money) advising individuals to sell if they needed cash during the next five years.

- Mr. Bannon immediately went from being fully invested to being all in cash, and further, never got back into the market.

As you can see, Mr. Bannon made several mistakes that cost him. The two biggest mistakes were his attempt to time the market and to put his entire net worth in just one stock. There were many investors like Marty Bannon who made the same mistakes. In fact individual investors generally tend to buy and sell at the wrong time. With markets at record highs we are often asked if it is time to sell or for those newly venturing into the markets, should we buy at all? We have answered such questions in the past by addressing the futility of market timing.

According to the financial market research firm DALBAR, Inc., equity investors underperformed the S&P 500 to the greatest extent in October 2008—the same month Mr. Bannon sold his shares in AT&T. In this month, investors lost 24.21% compared to an S&P loss of 16.80% for a net underperformance of 7.41%. The next greatest underperformance occurred in March 2000, when the S&P surged 9.78% but investors took home only 3.72% for an underperformance of 6.06%. This underperformance was a result of bad investor decisions at critical points, the first in the face of severe market declines and the second when equity markets surged. According to another study by Mercer Advisors, these bad decisions add up over time, resulting in a “bad behavior penalty” of approximately 6% per year between what the market averages and what the average investor actually earns!

Legendary investor Warren Buffett has said that he has yet to meet someone who can time the markets correctly and consistently for an extended period of time. This is where a firm like ours plays an important role. This was another mistake Mr. Bannon made; not seeking an investment advisor’s counsel. We are not market timers and, we don’t believe we can do that successfully nor can anybody else. But what we do know is that investing in a diversified portfolio of stocks across sectors in companies that have a strong history of performance and rewarding shareholders will always stand the test of time.

Having all your eggs in one basket has been a dangerous proposition. History is littered with investors who had concentrated positions in companies like Enron and MCI WorldCom. It would have been wise counsel had someone advised Mr. Bannon about diversifying away from a single stock.

AT&T’s stock has recovered nicely from the lows of 2008. There may have been plenty of blame to go around but he should not have been making such decisions at the age of 86 and relying on CNBC for guidance. Mr. Bannon simply did not have the expertise and should have sought help from a knowledgeable advisor.

One should conclude from the above that market timing is next to impossible and holding concentrated positions in a few stocks carries hazardous risk. Also seeking an investment professional’s help goes a long way rather than a do-it-yourself approach. A combination of patience, fortitude and professional help can achieve the desired results over the long run.

As always we are grateful for the opportunity to help you with your investments.

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