

## This Time It's Different?

*Market Commentary by Randy McGill, Branch Manager/Owner – July 26<sup>th</sup>, 2002*

Back in 1999 and early 2000, I heard a lot of clients and advisers alike declaring “This time it’s different!” They were referring, of course, to the remarkable growth in both the economy and the stock market and to its likely continuance. They were responding to those of us who were somewhat skeptical about this growth and who insisted on keeping our clients’ portfolios allocated across different asset classes – when it seemed that only one asset class – growth stocks fueled by technology, was the place to be.

Now, once again, I am hearing people say “This time it’s different!” Only this time, they’re referring to reasons why the stock market will not go back up. I’m sure you’ve heard some of these reasons – they range from the fear of another terrorist attack to revelations of yet another corporate accounting scandal.

Well, in response to this type of thinking, I’d like to offer a little perspective. Many of you have often heard me say that “the truth usually lies somewhere in the middle.” In fact, I often say that when confronted with an “extreme” viewpoint. And so, let me say that just as “it wasn’t different” back in 1999, (as born out by the tremendous correction we’ve experienced the past two and one half years), my belief is that “it isn’t different this time” either. The fact is that stock prices will “regress to the mean”, i.e., they will rise from their lows, just as they have in the past. And over time, stocks will remain an attractive investment. Will stocks go down again? Yes. Will a terrorist attack disrupt the market again? Probably. Will corporate scandals continue to exist – yes, just as they always have. But will the economy and stocks march forward anyway? Yes. Why? Because, after all is said and done, and although past performance is no guarantee of future results, the stock market is the foremost standard bearer of our economic way of life – and it will not just survive, it will flourish – not necessarily in the short-term, but over time.

As far as the near term is concerned, I believe that evidence is accumulating that we are nearing the end of this bear market cycle. In fact, history tells us that the bottom of a bear market is almost always characterized by several things. They include: the rise of bearish sentiment, tremendous volatility, high trading volume, and even the best stocks dropping in value.

As far as bearish sentiment is concerned, all you have to do is answer the phones here in our office to get a feel for how people are feeling about investing in stocks these days. While the great majority of our clients remain calm and patient, (and some even view this as a buying opportunity), many have expressed their fear of falling account values. For a more scientific sampling of sentiment, we turn to *Investor’s Intelligence* for their weekly survey of bulls and bears. Two weeks ago, for the first time since September of last year, the percentage of bears exceeded bulls. From a “contrarian” viewpoint, this is good news. Believe it or not, it is important that people believe that stocks are no longer going to go up. That leads to selling which ultimately creates a “buying opportunity” for savvy investors.

As far as volatility is concerned, we need look no further than recent days in the market. Perhaps the best example of volatility would have been the trading activity of Monday, July 15, when the DJIA traded down 440 points only to close down 45. That’s down 440 and back up 395 - an 835-point, intra-day swing! More such days - including a couple of near-record days on the Dow - have followed.

You may also know that trading volume has been setting records lately. In fact, four of the highest volume days in the history of the market have occurred in the last two weeks! On Friday, July 19<sup>th</sup>, investors traded the highest volume of shares ever recorded on the New York Stock Exchange – a staggering 2.6 billion! Compare that to “The Crash” of October 19<sup>th</sup>, 1987 when the NYSE set records as approximately 600 million shares changed hands.

Finally, the last point from above – even the strong stocks dropping in value – will be born out on your July account statements. This month we have watched even our strongest funds and managed portfolios – the value funds/accounts – fall in value. As you review your accounts, the natural reaction will be disappointment and fear, and the temptation to “stop the bleeding” by bailing out will be strong. This is what creates the aforementioned “buying opportunity” for savvy investors. Again, I remind you, this is characteristic of a “bear market bottom.” As the celebrated value investor Warren Buffet once said, “Be fearful when others are greedy. Be greedy when others are fearful.”

So is the selling over? Again, on a short-term basis, I simply cannot know for sure, although for all the aforementioned reasons, I feel very strongly that we are getting close. On a longer-term basis, stock prices tend to be driven by one thing – *growing* as opposed to *shrinking* earnings. And we have a lot of evidence that suggests the economy and companies are turning things around.

For example, retail sales surged 1.1% in June, more than doubling analysts’ expectations while the number of new jobless claims dropped to their lowest levels in nearly a year and a half. On the interest rate front, thirty-year mortgage rates have dropped to their lowest level in 31 years. And on the earnings front, a number of companies – Kodak, McGraw-Hill, and Xerox among them - each posted higher-than-expected second-quarter earnings while Microsoft announced plans to add 5,000 employees and increase its research and development budget by nearly \$1 billion. All of this good news while inflation is nil and productivity remains high. Finally, the U.S. Congress recently passed a bill designed to reign in corporate wrongdoers and toughen oversight of the accounting industry by an overwhelming margin – a bill President Bush has promised to sign. What does all of this add up to? A pretty good environment for stocks.

In closing, I’d like to say that I know how frustrating times like these can be. Remember that like you, I too am an investor. My best advice, advice that I have followed myself, is to remain calm and patient. Do not lose faith in our economic system; and do not ignore the lessons of history. *This time is not different.* In fact, when all of the smoke clears, once again we will learn to rue extremist views. The truth, after all, lies somewhere in the middle.

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