

Market Outlook:

Fortifying...

A decade has passed since the Great Recession of 2008-2009. In that span the financial markets have recovered, and people have been feeling pretty good about the results they have achieved in their investments. And yet, a subliminal fearfulness underlies almost all of the success the recovery has yielded. The "next downturn" is something I have to address in my conversations with clients and the media more frequently than our current annual returns. Indeed, last week's extreme stock market volatility did little to postpone the discussion.

When, or if, the next market capitulation does occur, it is far less likely to impact the economy as severely as the last one, but no one seems to believe that.

Individuals and corporations continue to have 2008 on their minds. And yet, to their credit, portfolios and balance sheets are not nearly as reckless as they had been in the run-up to the last recession. So who's right?

Economic data such as unemployment, wages, and productivity have caught up with or exceeded their levels of a decade ago, offset today somewhat by current end-of-cycle slowdowns in earnings acceleration patterns, regional trade disputes, and international conflicts. Even so, the fear of a snowball running downhill should be somewhat muted. Yes, recessions and market pullbacks are costly and painful. No one denies the herculean task it has been to dig out from the wreckage wrought upon the global economic landscape. But recovery times should be much quicker this next time around because of precautions having been taken to avert such a catastrophe.

There are no easy fixes that limit the effects of excess and greed. The best way I know of to avoid portfolio demolition is by sector, asset class, and geographic diversification. Irrespective of one's tolerance for danger, the best guardian against multiple risk factors is *asset allocation*.

Consider, our portfolios were at or near record levels of cash right before the 2008 collapse, in response to the earlier half-decade in which our accounts were generating competitive capital gains. It was a time to pare down the risk-taking, bank our profits, and recalibrate the financial backdrop. We did not avoid the market pullback altogether, but our clients were spared calamity not only on a relative basis but on an absolute one as well. Foresight and planning ahead using quantitative metrics allowed us to scan the probability of capital gains from an already engorged stock market and make the decision to back off from full investment. Did we have too much cash as a result? Perhaps. But consider any other client who was 100% invested in equities and bonds and the cliff from which they fell.

...one brick at a time

Let's face it, investing does not have to mean *embracing* risk...it means *managing* risk. The elusive goal of un-correlating one's wealth-building from the day-to-day exigencies of economic, political, and anecdotal statistics is difficult, but not impossible.

As my investment processes demonstrate, structuring initially from a solid foundation (fixed income/cash reserves) is the most important component to creating risk-averse portfolios. Imagine the base of a triangle and build upwards from there. But secure reserves are not simply enough. There are few "growth" opportunities in cash. One must also construct supplemental franchises upon the base, which means biting the bullet and accepting growth as a component to the ultimate structure. One cannot "time" the markets; one must acknowledge that cycles are a part of the portfolio paradigm. I will also remind my readers that secular (generational) themes such as energy, food, infrastructure, healthcare have staying power and capital gains potential despite their unique short-term cyclical topographies.

A good money manager also recognizes that clients sometimes cannot fully articulate their inner thoughts, speaking in "code" about how they feel about their goals or their tolerances for volatility. It is the manager's job to construct appropriate lanes to help the client fully actualize his objectives and to sleep well at night.

There is no such thing as a perfect strategy, investment, or portfolio. There only is the perfect preparation for any contingency that might arise.

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