THE

JENTNER REPORT

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Wealth Management Strategies from Jentner Wealth Management

INSIDE THIS ISSUE

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How Will the Presidential Election Impact the Market?

Spoiler alert: You are about to hear how this year's Presidential election may affect the U.S. stock market six months down the road.

Are you ready? The answer is – not much. That's right: a hotly contested election with competing economic policies in a time of world financial crisis probably will make little difference to your portfolio. Many academic studies have shown that political events usually don't have lasting effects on stock prices. In the long run market prices are determined by investors' perceptions of corporate earnings.

Consider some of the major political events of the post-World War II period:

In September 2001 a horrifying terrorist attack virtually shut down the United States for several days. The market was down 4% a month later, up 11% six months later, and down 9% a year later. Five years later it was up 84%.

In 1990 Iraq invaded Kuwait, precipitating the first Gulf War. Six months later the market was down by 5%, but within a year it was up 5%.

Last year's battle over the debt ceiling and the downgrade of U.S. debt? A year later the market is up.

Presidential Cycle Myths

A popular belief says that an election year should be one of the best for investors. Indeed, the S&P 500 Index has risen in 12 of the 16 election years since World War II, but that's about the same percentage that the market has risen in all years in the same period, says T. Rowe Price.

Forbes.com noted in March that the stock market fell by 34% during the 2008 election year. Said Forbes, "Market behavior is difficult to predict and sometimes the likelihood of future outcomes are already priced into equity and fixed income markets."

Former Secretary of the Treasury Lawrence Summers conducted research at Harvard 20 years ago and found that big world events had "a surprisingly small effect" on stock prices. Also, Ned Davis Research looked at 28 events prior to 2001. In 19 of the 28 cases, the Dow Jones Industrial Average was up six months after the crisis hit. Such studies suggest that investors should not adjust portfolios in reaction to headlines, no matter how major. The outcome of those events is unpredictable and in most cases will not have a lasting effect on stock prices.

The High Cost of Avoiding Volatility

Some investors do what worried investors always do in times of stress – try to avoid "risk" by buying the "safest" assets. Many buy government bonds from the U.S., Germany, Australia and other countries considered safe havens. Panic buying has pushed some yields to negative levels.
Is this rational? Probably not. Investors may just guarantee themselves a negative real return after inflation. The only way to make money on such an investment would be to live through a depression with accompanying massive deflation.

Investors also ignore the market's mechanisms for dealing with risk.

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The President's Word

Investors Don't Have 'Fun' Anymore. They Miss the Point

A recent survey by Spectrem Group found that well-to-do investors say investing isn't as fun as used to be. (In a survey a few years ago about two-thirds of wealthy investors said they enjoyed investing.) Only a third of investors with $1 million or less to invest said they enjoy investing these days. About 43% with $1 million to $5 million say investing is enjoyable, while 52% with $5 million to $25 million are having fun.

Fatigue Factor

Spectrem's director of business development said "investor fatigue" from volatile markets plus concerns about personal finances may cause the bad feelings. "Investors have almost become tired of the constant worry that comes from being so involved, and many just can't seem to find strategies that they're happy with," said Randy Wostratzky.

It's undeniable that markets have been volatile, but are investors missing the point? Is investing supposed to be "fun?" Some of these investors confuse investing with speculation. It can be fun to buy a hot stock and reap a quick profit, just as it is fun to hit a slot machine for a big payoff.

That is not investing. It is short-term speculation, and it is as easy to lose money as to win it. Certainly many speculators have lost money in recent years as they were whipsawed by up-and-down markets that ravaged individual stocks and market sectors.

Get Used to Boring

Investing is a long-term process of continually adding to a portfolio and leaving it alone to grow when markets move ahead. It may take many years of losses before a portfolio even shows a profit.

But an investor who is patient, maintains a diversified exposure to markets, and keeps adding to the portfolio usually comes out ahead. "Investing should be more like watching paint dry or watching grass grow," said Nobel-prize-winning economist Paul Samuelson. "If you want excitement, take $800 and go to Las Vegas."

Bruce A. Jentner, President
Jentner Wealth Management

"presidential election"

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Worrisome risks such as financial troubles in Europe or slowing economies in the U.S. and China are already priced into the market. Investors have pushed down prices of volatile investments such as stocks and commodities and at the same time pushed down yields on less-volatile government bonds.

If the market's risk appetite revives in the future, owners of risky assets will be paid "a very substantial return," Davis writes. "The takeaway is that sheltering in what are perceived as the safest government bonds may provide certainty for a time, but also comes at the cost of foregoing the significant increase in risk premiums that may be available."

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Perma-Bears Make Scarily Bad Predictions

Volatile stock markets create an odd type of celebrity known as the "perma-bear," a very negative forecaster who gets credited with calling a bear market before it starts. What you usually aren't told is that he or she has been calling for a bear market for years without success. When the big chance finally comes, perma-bears go for all they can get, selling books, newsletters, TV appearances and speaking tours.

Roubini's Warnings

The latest famous soothsayer is Nouriel Roubini, who teaches at New York University and operates Roubini Global Economics. He began calling for a collapse of the housing market and subsequent recession in 2005; three years later he was vindicated by the 2008 financial crisis and bear market. Roubini, now sought out by governments and investors worldwide, stays bearish, earning the nickname Dr. Doom. Yet the problem with being a perma-bear is that you will only be right about a third of the time: stock markets and the world economy typically expand during the other two-thirds.

Ruff Times

One of Roubini's predecessors as perma-bear was Howard Ruff, a famous financial advisor and hard-money advocate in the 1970s. He wrote a bestseller, "How to Prosper During the Coming Bad Years," just a few years before the greatest bull stock market of the century began. Ruff was a critic of stocks and advocated owning precious metals, art and coins. He lost favor after gold peaked in a 1980 speculative bubble. In February 2009 he was at it again, predicting stocks would crash just as a new cyclical bull market began that would lead to a doubling of stock prices.

Joe Granville

Granville achieved huge popularity in the 1980s by claiming to use his own form of technical analysis, "on balance volume," to predict future stock prices. For one investment seminar, Granville dressed as Moses, carrying stone tablets and wearing a crown. His market call to "sell everything" dropped the Dow Jones Industrial Average by 4% on April 22, 1980. He continued to proclaim the market was headed for imminent collapse after the last secular bull market began in 1982. His popularity declined and he later wrote a book about winning at bingo. His latest call at age 88 in January was for a 50% market plunge this year.

Political Ambition Also Loses

Another forecaster failed to become governor of New York in one of the worst losses on record in the state. Wall Street financier Pierre Rinfret, advisor to Presidents Kennedy, Johnson and Nixon, was a noted bear in the early 1980s. On the day the 1982-1999 bull market began, he said economic and stock market conditions were dismal and held no promise for recovery. Rinfret was beaten so soundly by Democrat Mario Cuomo for governor of New York in 1990 that he almost dropped the Republican line to third on state ballots.

Investors who seek guidance when times are hard and markets are falling should recall that, as Yogi Berra said, it is hard to make predictions, especially about the future.

Some Hedge Funds Have Trouble, Bail on Investors

With stock and bond markets shaken by the 2008 mortgage crisis, the 2011 U.S. debt crisis, and now the European debt crisis, hedge funds have been touted as an alternative for investors seeking shelter and profit during volatile times. Hedge funds are lightly regulated investment pools for qualified investors whose asset levels and investment experience indicate they can take more risk than the average person. Hedge-fund promoters cite their ability to go anywhere and do anything, such as shorting foreign currencies and specific stocks, buying and selling options and futures, and moving into and out of entire asset classes on a moment's notice.

Hedge funds are no panacea, however, and they earn the description of "risky." Hedge funds can close their doors at any time, giving investors no chance to make back their losses. In recent months a number of well-known hedge funds have thrown in the towel due to bad bets on the European debt crisis:

- Expo Capital Management, a $458-million fund in Los Angeles, folded this year after two years of losses in its health care stock portfolio.
- The Fortress Investment Group in New York City liquidated its $500 million commodities fund in May after losing 13% in the first four months of the year.

Others have followed suit. Hedge Fund Research of Chicago said 775 hedge funds went out of business in 2011, the highest number in several years.

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Public Pension Funds Courting Risk Fare Poorly

Some state and local public pension funds have sought higher-risk investments in order to boost returns and make up for funding shortfalls. Others have stuck to a traditional diversified stock and bond mix. Guess who has done better? (Hint: it wasn't the high risk-taking plans).

Falling tax revenues and rising retirement costs have put some public pension plans on the defensive. In an attempt to make up for shortfalls they have put some of their assets into alternative investments such as hedge funds, direct real estate investments and private equity arrangements. (Hedge funds are investment pools with no constraints on their strategies: they can short stocks, speculate in currencies, and engage in other risky pursuits. Private equity funds allow large investors to take direct ownership stakes in private businesses, rather than buying publicly traded stock.)

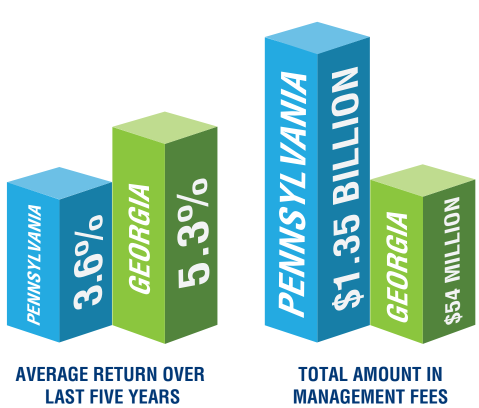
The New York Times recently reported that the Pennsylvania State Employees' Retirement System has put almost half of its assets into private equity, real estate, and other riskier alternative investments. The pension fund had average returns of only 3.6% over the past five years, and it paid $1.35 billion in management fees.

Meanwhile, the Georgia municipal retirement system is prohibited by law from using such investments. It invested in a standard diversified mix of stocks and bonds and earned a 5.3% annualized return over the same period, while paying about $54 million in management fees.

London-based research firm Preqin recently said that Pennsylvania was among a group of pension systems taking the highest risks, while Georgia's system was in the group taking the lowest risks. Preqin's study showed that those pension funds that had over one-third of their money in riskier alternative investments earned an average of one percentage point less than pension funds that avoided such investments. Meanwhile the riskier pension funds paid an average of four times more in fees.

The results seem to indicate that returns on alternative investments do not justify their higher fees.

Compare State Employees' Retirement Systems



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"Strategic financial planning helps you achieve personal and objective goals by asking smarter questions, listening more carefully and applying sound financial and investment strategies. It is not something different or new; it's simply planning the right way."