

While one can certainly argue for having 100% of your portfolio in stocks in the depths of a recession when prices are depressed, (and looking back, I wish I had been that brave), after a long recovery, when prices are at their peaks, there's an equally persuasive argument for owning no stocks at all. I don't follow either of those precepts in practice however because predicting the exact timing of these turns is problematic at best, impossible is more like it. I lost more accounts and had more unhappy clients in 1999 than anytime since because I sold too early, never believing that the market could continue to go up. And if you look back at the 2009 editions of this market commentary, I had plenty of sound (but, as it turned out invalid) reasons to wait before going back into the market. Fortunately, you – my clients- are pretty understanding as well as sharing my aversion to losses. So, in practice I like to have enough in stocks to enhance the steady bond returns, but not so much that the inevitable drops on the market will hurt. We have been in a great bull market for stocks since 1981. But in spite of the fact that we are valuing the stock market at close to the highest level in fifty years – see the black line on the chart immediately below - and in spite of the fact that corporate profits' share of the economy are also at a fifty year high (the red line), buying at a premium valuation at the top of an economic cycle has still been a losing proposition. In the chart at the bottom, there's a total return history of three different investment portfolios going back to about a year before the market top in 2000. This is arguably about equivalent to where we are now, within a year of the top of this economic and market cycle and with valuations at highs. While those 100% invested in an S&P index fund had a lower return (equivalent to 6.25%/year) than those on the Conservative portfolio (7%/year), they suffered through some pretty heart-wrenching declines. If we begin a political cycle less friendly to profits, the next twenty years will be much worse.

