Vol. 9, Issue 25
August 21, 2015

Something to Think About

OAKWORTH CAPITAL BANK

COMMON CENTS

I started and stopped this newsletter several times today, as I would write a full paragraph; read it, and then delete it for being, I don't know, redundant. There is/was no shortage of other similar commentary available on the Internet, so why reinvent the wheel? After each deletion, I would go back to the stock ticker, and get a sick feeling in my stomach. Sure, this job can be fun when the markets are making money; however, it is an absolute nightmare when they aren't.

With that said, everyone knows the old saws the industry throws about. You know, about the importance of being a long-term investor, and not freaking out when the market freaks out. After all, history suggests a well-diversified portfolio will ultimately recoup any losses you don't realize. Of course, I have to say something like "past performance is not indicative of future results," even if the odds say it normally is, at least to a degree.

But I have also found being a long-term investor doesn't mean beating your head against a locked door hoping it will open. Sure, it eventually might, but at what cost? As such, being a long-term investor means having a road map, if you will, that has a known end destination. However, we all know you sometimes have to get off the highway, for what ever reason.

With this in mind, we have raised more cash in client accounts over the last two days than at any time since we opened the doors. No, we are not of the opinion we are facing another 2008 or 2002 square in the face. However, the markets have far more headwinds than they do tailwinds right now, and the tailwinds they do have aren't exactly gale force. We recognize that, have done what we believe is the prudent thing, and have saved literally hundreds of thousands of dollars in the process.

Could we have done more? On Friday afternoon after the Dow Industrials just closed 531 points down, the answer is obvious. However, should we have? Therein lies the rub.

Some years ago, while at a previous employer, I got a phone call from an irate client of the bank's in another city. I had no personal dealings with this person, didn't know them from the man in the moon, but due to the nature of my position and title, I sometimes got the angry people when others didn't want to deal with them.

I will cut to the quick and tell you: there is no worse thing than presenting a client with a large capital gains tax bill when the overall account has done next to nothing, at best. I mean this person was hot, and, frankly, I didn't blame them. The portfolio manager in, let's say, Neverland had loaded them up with a bunch of mutual funds the week before they distributed a large amount of capital gains. In essence, they got none of the return that produced those gains and all of the taxable consequence. This as their portfolio actually fell in value even before the taxman cometh.

Unfortunately, there was precious little I could really do for them, but I had learned a valuable lesson. Investors hate paying taxes when their portfolio doesn't perform well. So, avoid sticking your client with a big bill unless you are absolutely certain it is in their best interests to do so.

With that said….

Even with all the unpleasantness, our fundamental forecast for the US hasn't changed dramatically. With mediocre economic and earnings growth, we should end 2015 with mediocre returns. I have

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told our clients we will go through the proverbial ringer this year, just to get to December 31 in order to say "meh." No, I don't think Apple is overpriced at now, what, 11.57 times forward earnings and a PEG ratio of 0.68. I would say the same thing about Skyworks Solutions at 14.98x and 0.71, and JP Morgan at 10.8x and 1.62. The list goes on and on. There are names and sectors that weren't overbought, in our opinion, and sometimes the baby gets thrown out with the bathwater when the markets freak out (again with that phrase...it has been a long day). Such as it is here, and if we have another day or two like today (and yesterday) we will deploy some of the funds we raised right into them.

However, there are names and sectors for which the future is decidedly more cloudy, with imbedded losses in client accounts. So, what is the first to go if you have to get off the proverbial highway? That's right, you sell the stuff for which you have less or little conviction, the low hanging fruit….which is what we have done, and will continue to do should conditions warrant. If you would like to know what those sectors are, please call an Oakworth associate about opening up an account.

With that said, until it becomes obvious the wheels have come completely off the tracks; until it becomes readily apparent valuations are far too high without resorting to the second derivative of some obscure equation, the odds are we are probably repeating 2011. Remember that year? Wasn't that awful, as the S&P 500 topped out on April 29 at 1,363.61 only to fall to 1,099.23 by October 3? That stunk, but guess what? It rebounded to close the year at 1,257.60, only 0.04 points below where it started 2011. Throw in the dividend, and, voila, stocks took us for a wild ride and we still ended up slightly positive. Truly, it was akin to a roller coaster, and 2008 was all the more fresh in our memory.

In the end, and this is a short newsletter this today, markets correct due to the overused term 'uncertainty.' However, markets tend to collapse on certainty. Right now, the markets are uncertain, so it would be wise to treat the recent unpleasantness as a correction, as opposed to the prelude for a collapse. Of course, things can and might change, but until they do, the most efficient thing to do is to realize some losses in sectors for which the 'uncertainty' is greatest. In this way, you have dry powder when the markets stabilize OR you have some room to realize gains should a less than desirable certainly become apparent.

Have a great weekend, or at least better than yesterday and today. That shouldn't be too hard, should it?

Disclosure