

Maintaining the 40,000 Foot Perspective

Without a base knowledge of the proper, proven long-term fundamentals of investing, the constant news flow is like a virus attacking a person with no immune system.

A comment often shared by those who attend football games is that by sitting higher in the stadium they are able to see plays develop and more clearly identify trends in the game. This is supported by the fact that most coaching staffs place coaches in the press box to relay the aerial view down to the coaches on the sideline. The view from above provides a perspective that is difficult to obtain at field level where the speed and emotion of the game stand in the way of effective decision making.

A primary responsibility of our firm is to identify and monitor the top mutual fund managers in the industry, and after years of research and experience, the attributes that distinguish the top teams are unmistakable. These include discipline, experience, talent and resources. In addition, a team's ability to separate themselves from the daily bombardment of information to obtain a view of the economy and markets from above is a competitive advantage. Unfortunately, there is no physical location like a press box that provides the aerial perspective, so managers must consciously separate themselves from daily information on a regular basis to ensure that their decisions are based on solid long-term fundamentals. When commenting on the fundamental view of the economy and markets from above, many fund managers and economists refer to this as the view from 40,000 feet – a common cruising altitude for airplanes.

We hire mutual fund managers to perform rigorous research and tactfully allocate our clients' retirement assets in a manner that produces above average risk-adjusted results over the long-term. Instead of sitting in their offices nervously watching the countdown to the next jobs report, the top managers are able to put the current economic recovery into perspective, realizing that a problem that was built over twenty-five plus years is not going to resolve itself overnight. They also realize that the long-term fundamentals of investing have not been changed by this event or any other event. Instead, they are taking advantage of the opportunity to buy solid investments at the attractive prices created by short-term focused investors who cling and react to every piece of news.

Separating oneself from the emotion-causing daily information flow and maintaining a fundamental perspective is equally important for individual investors. However, this has become increasingly difficult in a world of 24-hour cable news, the internet, and other information sources. We have become information junkies and it is easy to be drawn in, even for those who have historically had little difficulty maintaining discipline. Investors who are caught in the trance of short-term news do not realize the damage this causes. Their fascination with news and the constant onslaught of information clouds the brain and distracts them from the fundamental view 40,000 feet above.

Recently, a retirement plan participant asked if we could come up with a reason to invest in large cap U.S. companies. His mind was clouded by the view from the ground where high U.S. unemployment, weaker domestic consumption, an ongoing currency debate with developing economies, and the attractiveness of growth in those same developing

economies made it seem obvious that he should shift his allocations toward foreign stocks. Our first of several responses from 40,000 feet was that he had just stated the reason to stay the course with U.S. large caps. If the picture seems so obvious, others are thinking and reacting to the same information, meaning these factors are priced into both U.S. large caps and foreign stocks. This results in lower valuations for U.S. large caps and higher valuations for foreign stocks. *Remember, lower valuations typically result in stronger results moving forward.*

Of course, there are a number of fundamental reasons to diversify internationally, and tactfully increasing one's international exposure is prudent for most investors given the degree of globalization that is occurring. However, reacting to news by making poorly timed asset allocation shifts is one of the primary factors that cause investors to fall short of their retirement goals. Regular readers of this newsletter have heard us make this point on several occasions due to the fact that the information flow is on the rise and many investors are not prepared to handle it.

There seems to be a thought among investors that by filling their heads with daily information they will become better investors and be able to more accurately maneuver their retirement accounts to avoid the next selloff - or take advantage of the next hot run. However, many investors are attempting to build a house of knowledge with no foundation. Without a base knowledge of the proven long-term fundamentals of investing, the constant barrage of financial news is like a virus attacking a person with no immune system. For this reason, it is critically important that investors focus their knowledge building efforts on the fundamentals that will help them put information into perspective prior to turning their televisions to the financial news channels.

Conclusion

We think it is important for you to ask yourself on a consistent basis where you are mentally as it relates to investing. Are you at 40,000 feet in the world of fundamentals, at 10,000 feet, or potentially worse, on the ground caught up in the emotion-causing daily information flow? It may seem that the world has changed and the right answer is to fight on the ground, focusing on and reacting to each piece of news, but our experience is that the path to prosperity is much easier at 40,000 feet.

Market Comments

After pricing in concerns of a double dip recession in the second quarter, stock and bond investors seemed to put a good portion of that fear behind them in the third quarter. The result was a strong quarter for stocks and increased risk-taking in the bond market. The Russell 3000 Index (a broad representation of the U.S. stock market) gained 11.5% during the quarter aided by one of the strongest Septembers on record and is back into positive territory for the year (+4.8% YTD).

Another contributor to third quarter results was the stabilization of global economies. Bank stress tests in Europe calmed financial market concerns and recent news from China has calmed fears of a significant Chinese economic slowdown. Moving forward, the U.S. economic recovery continues to battle the structural headwinds of increased savings rates, high unemployment, and continued deleveraging. However, the stock market appears to have priced in these concerns. The Federal Reserve seems poised to continue its efforts to spur the economy along by buying U.S. debt in an effort to keep interest rates low (a stimulative measure since many consumer rates are influenced by treasury rates).

The bond market has been helped by continued demand from investors and the weak nature of the recovery (kicking the likelihood of higher rates down the road a bit). The



appetite for bonds has been extremely high due to very low money market rates and lingering frustration with the stock market. However, bond investors should keep in mind that there is likely a demand component aiding bond returns, and given the low rate environment, more modest returns should be expected moving forward. The Barcap Aggregate Bond Index gained 2.5% in the quarter and is up 7.9% for the year to date.

Disclaimers: While Veratis Institutional Advisors, Inc. uses reasonable efforts to obtain information from reliable sources, Veratis makes no representations or warranties as to the accuracy, reliability or completeness of information obtained from third party sources presented herein. Any forward looking statements or forecasts are based on assumptions and actual results are expected to vary from any such statements or forecasts. No reliance should be placed on any such statements or forecasts when making any investment decision. The views expressed herein reflect information as of the publication date only and may change at any time without notice. The information provided is confidential and shall not be copied or distributed without the express written approval of Veratis Institutional Advisor, Inc. No guarantee of investment performance is being provided and no inference to the contrary shall be made. Copyright © 2010 Veratis Institutional Advisors, Inc. All rights reserved.

