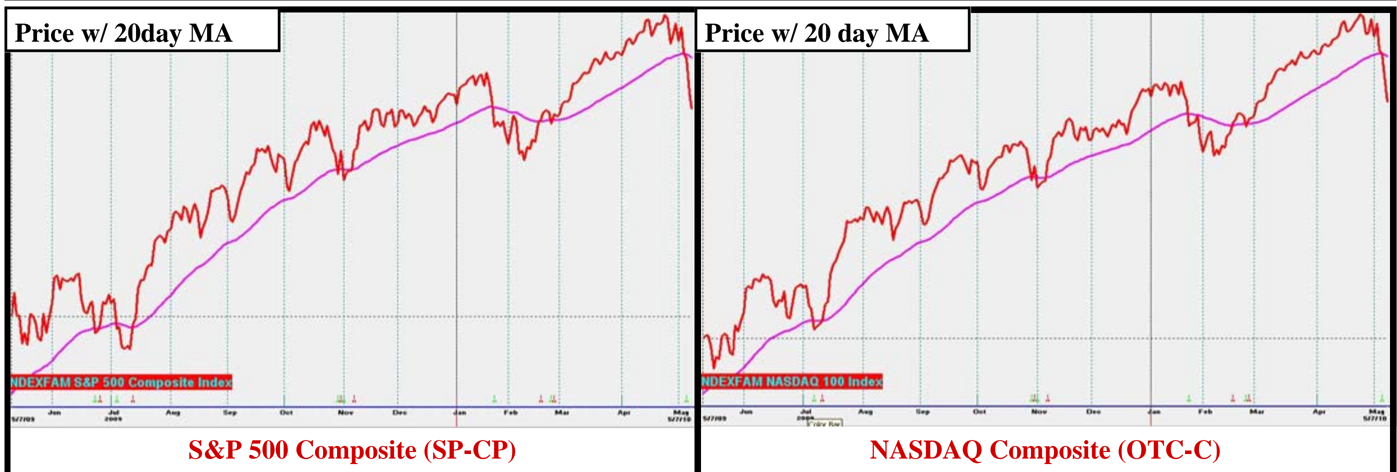
COASTAL
WEALTH MANAGEMENT

# MARKET COMMENTARY

In the wake of the market chaos that persisted last week, it is important to step back and take a look at the big picture. The media has focused almost entirely on the events of Thursdays apparent melt down, when in fact the turn down in the market began the previous week. Since April 23rd, the major indexes are down as follows: Dow Jones Industrial Average (-7.36%), the S&P500 (–8.74%), Nasdaq 100 (–10.02%), and the Russell 2000 (-11.99). Below are charts for the S&P 500 and the Nasdaq Indexes. Most of the carnage was blamed on the events in Greece and a wildly speculative comment that an erroneous trade entry led to short lived drop of over 1000 points on the Dow during trading late Thursday. The fact is that what caused the change in the market is not nearly as important as recognizing that conditions have changed and taking appropriate action.

While I dislike any drawdown in accounts please keep in mind that we can not eliminate risk. Instead what we do is strive to identify and control risk. To that end, in the time period from April 23rd, our average account suffered relatively minor drawdowns of between –1.07% and –1.98%. We liquidated the funds with equity holdings which hit their stops on Thursday and Friday and were responsible for most of this movement. If the market conditions continue to deteriorate, even our holdings in the low volatility bond/debt/income funds will hit their stops. If however, the market begins to stabilize at this level, we may find ourselves in a very good position.

As I stated above, we cannot eliminate risk. In fact trying to hedge away all risk can be counter productive as evidenced by today's 4% rebound. All investing involves some risk and while we strive to control it we will never get out at the exact top of the market. By using predetermined stops though we can control the amount of damage during market corrections and be better positioned to take advantage of opportunities when they develop. Rest assured that no matter what direction the market takes, we will take action to provide the best risk adjusted returns possible.




S&P 500 Composite (SP-CP) | NASDAQ Composite (OTC-C)

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# WINNING BY NOT LOSING

In the economic climate that we are currently living in, we find ourselves dealing with greater volatility and external factors which influence the marketplace. As investors we are constantly faced with the decision of when to participate in the market. The mutual fund industry media has bombarded us with the message that we must invest for the long term picture; that buy and hold will always benefit you most; or that the market always comes back.

As active investment advisors, we don't subscribe to the buy and hold philosophy. In fact, in theory, we would choose to participate only on the up days and sit out the down days. The practical side of this is how do you execute such a strategy. It is easy looking back to say which days you should have been out, but choosing the correct days in advance is a bit tougher.

It is fairly easy to identify trends in the market as well as within individual sectors or mutual funds. But trend reversals leave us exposed to either significant losses when the market turns down or missing a significant up-leg when the market turns up. Many times we find ourselves sitting on the sidelines when the market reverses direction and makes a huge move up.

Given the choice of (1) participating in the best days of the market or (2) missing them altogether along with the worst days of the market, which would you choose?

A recent study by Hepburn Capital Management which looked at over 25 years of the S&P500 index history found a surprisingly consistent answer. Investors don't need to participate in the best days of the market if they can miss the worst days. Missing both the best and worst 10, 20, 30 or 40 days of the S&P500 returns outperforms the index by more than 1% annually. Over the 25-year period of the study, that 1% difference turns an investment of $100,000 into $846,624 versus $673,836 – a $172,788 difference or a 25% increase in value.

S&P 500-25 Years Ending Dec. 31, 2009
Average Annual Return 7.93%

| | **Miss the Best** | **Miss the Worst** | **Miss Both Best and Worst** |
|---|---|---|---|
| **10 days** | **4.83%** | **12.14%** | **8.92%** |
| **20 days** | **2.79%** | **14.74%** | **9.28%** |
| **30 days** | **1.12%** | **16.93%** | **9.56%** |
| **40days** | **(0.46%)** | **18.86%** | **9.67%** |

*Source: Hepburn Capital Management 2009*

While the study is purely hypothetical and has no way of taking into account management or trading fees that might be incurred in implementing such a strategy, it does demonstrate how important losing can be to the performance for and investor. Warren Buffet is often quoted as saying that "the number one rule of investing is don't lose money."

2008 -2009 provided us with a perfect example. The average mutual fund was up 34.9% in 2009 according to Morningstar. Unfortunately, Morningstar also reported the average loss in 2008 was -40.5%. While at first glance one might feel they were almost back to even, at the end of 2009, despite one of the best years for the S&P500, the average mutual fund was still down -19.7% from where it started in 2008. Because you are starting from a lower point in 2009, a previous year loss of 40.5% requires a gain of 68% to make it back to breakeven.

The loud and often obnoxious TV commentator Jim Cramer has a book out called "Getting Back to Even". I would submit to you that if you had not lost in the 2008 market meltdown, you would not need to simply "get back to even". Instead you would be growing your retirement capital from a much higher plateau.

If nothing else, the above should emphasize that it is much more important to know when to exit losing investments than being fully invested every day. Proper selection of mutual funds along with daily management continues to prove itself to be much more effective than buy and hold of any investment. If you are interested in learning more, please visit our website at www.Coastal-Wealth.com or call us at 713-621-9898.