

# **Is BUY and HOLD Dead or Alive?**

*By John Atkinson*

Theoretically, in a solidly rising trend, there may be advantages to be gained in 'Buy and Hold' as trade management appears simple, capital gains are made and dividends are received.

Where this comes unstuck is what do 'buy and hold' investors do when markets fall?

Do they adopt the BHP mantra, i.e. Buy, Hope and Pray - hold and "wear the pain" in the hope that prices will come back? If they are fortunate, maybe prices will return, BUT what happens if they do not?

In fact, when faced with reality, often many investors are not able to actually "wear the pain" as they watch their portfolio values plummet. Some may have gut wrenching sleepless nights and reduced physical abilities by day as a result.....many such investors, having bought high, end up finally selling low when the mental pressure becomes too much.

During the GFC, many markets, shares and funds fell in the order of 50%. The cruelty of the market is that a fall of 50% requires not 50%, but 100% to recover to previous levels.

This very important point applies to not only individual shares and the market Indices...it also applies to your portfolio overall. I.e. If you lost 50% of your portfolio, you would need to recover 100% to get back to where you were beforehand.....Even worse, once losses exceed 50%, the recovery amounts needed blow out exponentially, as shown below.

The Cruelty of the Market:

<b>% Fall</b>	<b>Gain Needed to Recover</b>
<b>10</b>	<b>11%</b>
<b>20</b>	<b>25%</b>
<b>30</b>	<b>43%</b>
<b>40</b>	<b>67%</b>
<b>50</b>	<b>100%</b>
<b>60</b>	<b>150%</b>
<b>70</b>	<b>233%</b>
<b>80</b>	<b>400%</b>
<b>90</b>	<b>900%</b>

This is why capital protection is such a strong part of Jim Berg's approach.

Several 'Buy and Hold' investors who held on to their shares during the GFC while markets plummeted found that in reality they could not wear the pain so they sold out far too late and gave up on the market

Many others held all the way down and have not managed to rebuild their portfolios back to where they were in late 2007.

For instance, the ASX200 (XJO) on 1 November 2007 had a High of 6851.50. 16 months later, by 10 March 2009 the XJO had fallen 54.5% to a Low of 3120.80. This required not 54.5%, but actually 119.5% to recover at that time.



At the time of writing, 16th October 2015, the ASX200 (XJO) had closed at 5,268.20, i.e. so far it has regained only 68.8% of the 119.5% needed to recover to its 2007 High.

I.e. the XJO is now only just over half way back from its March 2009 Low to its former High of 2007 - of 8 years ago.

Similarly, let's look at this week's current example, Telstra (TLS) over the long term:



In its heyday of February 1999, Telstra reached an all-time High of \$9.20.

Soon afterwards, 'mum and dad investors' were encouraged to buy Telstra instalments and many were advised to 'Buy and Hold for the long term', while prices fell.

Those who held have received dividends meanwhile, but at what cost emotionally and financially 'on paper'?

Nearly 12 years later, by November 2010, Telstra had fallen 72.3% to a Low of \$2.55 requiring, not 72.3%, but 260.8% to recover at that time...

By 16th October 2015, Telstra (TLS) had closed at \$5.44, i.e. so far it has regained only 113.3% of the 260.8% needed to recover to its 1999 High, i.e. TLS is now LESS than half way back to its former High of 1999 of nearly 17 years ago...

Some 'buy and hold' investors are advised by their brokers to 'average down', i.e. to buy more shares after prices have fallen .....then to buy more shares later after prices have fallen further again, as they are seen to have become even 'better value'.

In theory, IF and when markets rebound, such investors would have more shares at a 'lower average price' to take advantage of the rise back, with the aim of offsetting the 'paper losses' of all the shares bought at a higher price.

This 'Dollar Cost Averaging' approach may appear to work in principle, but in practice Jim says it is more akin to 'Revenge Trading' – of trading a losing stock over and over trying to get their money back. In addition:

- 1) Money and risk management principles may be thrown out of the window
- 2) If the share price continues to fall without rebounding, then such an 'investor' has more shares to drag him/her down

When you read in the media that the suburb you live or invest in has risen 7% for the year, it is reasonable to assume that most houses in that suburb have risen about 7% on average, e.g. you do not expect that any houses have fallen 98.9%.

This is not so with the stock market.

For instance, let's now look at Lynas (LYC), which was previously a member of the ASX100:



In April 2011, Lynas (LYC) reached an all-time High of \$2.70.

Four years later, by 25 June 2015, LYC had fallen 98.9% to a Low of only 3 cents.

The cruelty of the markets is such that this required not 98.9%, but actually 8,900% to recover at that time!

As at 16th October 2015, LYNC closed at 4.3 cents, i.e. so far it has regained only 43.3% of the 8,900% needed to recover to its 2011 Highs. Percentage wise, this equates to only 0.5% of the recovery needed.

Some investors hold on to their falling shares in the belief that the market has never failed to recover and make a new high, so they wait patiently..... What many investors fail to realise is that the Index is contrived, so that while the market as a whole may go back and make those New Highs, it may do so without the shares they own.....

For instance, as mentioned above, Lynas (LYC) was previously part of the ASX100. This is no longer the case. As part of the 'rebalancing' of Indices, non-performers such as LYC are progressively dropped and replaced by better performing shares in Standard & Poors' Indices, in what is known as 'quarterly rebalancing'.

Therefore, those 'Buy and Hold' investors who held LYC for the long term, believing that the ASX100 will recover to its former Highs and so will their LYC shares too, now find that:

1. LYC is no longer part of the ASX100 Index and
2. Currently, these 'long term investors' still have 8,877% left to go to for their LYC shares to get back to their previous High.
3. Even worse, any investors who listened to their broker's advice and bought extra shares on the way down as they became better and better 'value' (see 'dollar cost averaging' see above) now find they have custom fitted a set of concrete boots to their portfolio.

Now imagine how much better off those LYC investors would have been if they had been given an EXIT signal after the Highs of 2011 and either:

- A. Switched to cash and protected their funds, or
- B. Switched from a share that was going down.....to a share that was going up in a rising trend....?

What is needed is a big picture approach. We look at this next week.