070910 Observations and Conclusions
By Gary Case

As I write this on July 1st, the Quarterly Markets Review in today's edition of the Wall Street Journal contains headlines alluding to the "Flash Crash", Greek Worry, warnings of technical indicators eroding investor sentiment, China (Shanghai) stocks falling twice as far as those in the USA, and increased risk in corporate bonds, record gold prices, and the strength of US Treasury prices.

During the past week I have purposely spent time reviewing economic forecasts and commentary from a folks with a variety of agendas, from those predicting the stock market closing in mid 2011 below the March 2009 lows with others predicting new stimulus packages which will allow us to spend ourselves into economic expansion.

Rather than try to stake out a position in this tumult of economic noise, it occurred to me to simply try to see what is actually happening now without trying to judge what may occur later because of what is happening now. I have found in the past that trying to predict the future is usually futile, while logically following what is happening has helped protect the assets, limiting downside capture and allowing for some (but not all) upside capture of market movements across asset classes and investment strategies.

What I see occurring in tactically managed portfolios is massive hedging against widening credit spreads and volatile stock prices. Typically tactically portfolios attempt to exploit specific opportunities to either produce gains or limit losses, often in response to a proprietary set of criteria developed by the manager.

Others manage fundamentally researched, strategic portfolios by seeking to find specific securities or asset classes that appear to be undervalued and make long-term buy-and-hold purchases, generally selling only when the security has reached a fundamentally fully valued point. Finally, index, or passive investors simply purchase an investment that represents broad market indices, with the theory that broad market returns over time will outpace any sort of active management.

For my clients in any of the above categories, I recommended they consider using a technique designed to mitigate current volatility: hedging their "long" portfolio positions. Theoretically, this means that I recommend purchasing an investment that price-wise tends to move in the opposite direction of broad markets. There are a variety of vehicles suited to this objective, including options contracts, mutual funds, and exchange traded funds. The potential "smoothing" of portfolio values can often help an investor maintain their course of action, regardless of their overall philosophy.

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