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Glenn Woody
Certified Financial Planner

Secular Bear

While it is historically true that the market goes more up than down over the long haul, there have been lengthy periods of time in which that was not true.

The long-term chart of the U. S. stock market clearly shows periods in which the trend was clearly up and periods in which the trend was clearly flat. The Rydex mutual fund people have produced such a chart of the Dow Jones Industrial Average, from 1896 through 2008, which clearly shows these periods.

The up-trending periods are often called "secular bull markets", while the flat trending are called "secular bear markets". (Secular here is not used in the religious sense, but to mean long-term or strategic.)

On this chart, there are four secular bull markets and four secular bear markets.

It is obvious that we have been in a secular bear market since early 2000, and while we are not out of that trend, it is used as the fourth secular bear market on their chart.

The shortest secular bull market is 5 years in length, the longest is 17 years long and the average length is 10.5 years. The average cumulative return in these bull periods was 400.26%.

Excluding the current bear period we have now been in for 10 years, the shortest secular bear period was 17 years, the longest was 25 years, while the average was 20 years. The average cumulative return in those three bear periods was -.59%.

The bear periods, including the one we are in now, are marked with a great deal of volatility, but a relatively flat return over the period.

In the bull periods, the so-called buy-and-hold strategy works well. While there are certainly periods of downside volatility included, they always recover to a new high.

However, in the bear periods, buy-and-hold simply produces a wild roller-coaster ride that ends about where it started. So what does an investor do in such bear periods?

Even in such volatile, flat, or even down-ward trending periods, there are asset classes or sectors that are advancing. But, one cannot benefit from these advancing "slivers" by buying large sectors of the market. If one buys the S&P 500, or even large value, large growth, small value or small growth, the advancing sliver embedded in there gets overwhelmed by the rest of that sector.

The somewhat traditional style-box

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Secular Bear (Cont'd)

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diversification strategy, which served us so well during the 17 years of the prior secular bull market, 1982 through 1999, does not work well in a secular bear market, as it is a form of the buy-and-hold strategy.

In a secular bear market, one has to develop a method of seeking out the narrow asset classes and sectors that show promise. That suggests one's need to be more nimble in approach, making changes between asset classes, industries, market-caps, sectors and even geographical regions as economic conditions and market valuations seem to dictate.

In 2002, it began to be apparent to us that the secular nature of the market was changing from bull to bear and we began a study of historical bear markets to see what strategy worked to produce some return in an otherwise flat period.

That study led us to abandon the style-box diversification approach and seek out managers with a history of success in being unconstrained and going "anywhere" to find value.

Some would suggest that we, as your portfolio

manager, could pursue this unconstrained strategy by researching dozens of sectors, asset classes, industries and world-wide regions, selecting the attractive ones and then buying into a no-load mutual fund or Exchange Traded Fund to take an appropriate position. We opted to seek out managers of mutual funds who are professionals at that approach. Such professionals pursue their strategy fulltime assisted by armies of economists, and research analysts around the world. Such managers are variously called "go anywhere", "whole market" or "all-cap, all-style".

We carried that same general philosophy into our non-U. S. exposure. We have always had some allocation to international equity funds, but have turned to using global funds. While an international fund invests outside the U. S., a global manager can "go anywhere" including investing in the U. S., if he or she judges that to be the place to be. We added that same global strategy to some of our fixed income allocation.

In the recent decline in the market, we kept our "go anywhere" strategy but moved into equity funds that had some degree of defensiveness in their strategy, to soften the downside participation.

With regard to the need to be more nimble, we are adding a category to our asset allocation table that we are calling "opportunistic". In it, we will allocate to investment strategies that we do not expect to hold forever, but rather that we believe might produce some benefit over the next one to two years.

In that Opportunistic area we have put international real estate and emerging market equity funds. We will add other strategies that may not be closely correlated to the U. S. equity markets.

Thus is our approach to the secular bear market in which we find ourselves.

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# Market Highlights

## November 2009

### Positive:

- Real gross domestic product gained 3.5% in Q3 2009, from a 0.7% decrease in Q2.
- Privately-owned housing starts increased 0.5% in September over August, but were 28.2% below September 2008.
- Sales of existing homes jumped 9.4% in September and were 9.2% higher than in September 2008.
- New orders for manufactured durable goods in September increased 1.0%, following a 2.6% decrease in August.
- Industrial production rose 0.7% in September after a gain of 1.2% in August.
- Construction spending in August was 0.8% above July, but 11.6% below August 2008.
- Economic activity in the manufacturing sector expanded in September for the second consecutive month, and the overall economy grew for the fifth consecutive month, say the nation's supply executives in the latest Manufacturing ISM Report On Business®.
- The balance of international trade was at a deficit of \$30.7 billion in August, down from a \$31.9 billion in July.
- U. S. retail e-commerce sales for Q2 2009 increased 2.2% from Q1.
- Manufacturers' and trade inventories in August were down 1.5% from July 2009 and down 13.3% from August 2008.

### Mixed/Cautious:

- Sales of new one-family houses in September were 3.6% below the August rate and 7.8% below the rate in September 2008.
- Nonfarm payroll employment continued to decline in September and the unemployment rate, at 9.8%, continued to trend upward.
- The advance estimates of U. S. retail and food services sales for September decreased 1.5% from the previous month and were 5.7% below those of September 2008.
- Personal income decreased 0.1% in September.

### Informational:

- In the month of October, large-cap was slightly positive, small-cap was negative, domestic outpaced international and growth vs. value were mixed.

## FYI: Short-Term Observations

*These comments are offered for your information and thought. They are short-term and tactical in nature. We invest for the long-term, three to five years plus. Don't confuse these short-term observations with what may be the best decisions for the long-run. Some even believe it is confusing, at best, and distracting, at worst, to involve short-term issues in long-term investing.*

### Continued Uncertainty

**W**hile there continue to be a number of pieces of economic data that compare favorably with the recent past, there is also more chatter in the economic/investment community about the items of concern. We listed a number of them in last month's newsletter.

This has cast a bit of a pall on the strong stock market rally we have experienced since last March 9. The popular U. S. stock market averages in October were either flat or down. That was the first negative month we have seen since February, except for the S&P which was off a bit in June.

There is some talk of the Fed's raising interest rates sooner rather than later, producing a heightened level of interest in the outcome of their meeting on November 3. While they may not actually raise rates, there could be some significance attached to their verbal pronouncement, sending a signal as to their future intentions.

Virtually everyone feels there will be increased interest and inflation rates in our future due to the dramatically increased spending on the part of the government, but, most have predicted we will not see either for a year or more, and at least not until the economy is clearly healthier.

The Gross Domestic Product came in for the third quarter at 3.5%, a favorable surprise from the expectation. That produced a strong 200 point gain in the Dow Jones Industrial Average on that day. But, it gave back all of that and more the very next day with concern about the unemployment and anemic consumer spending.

The one certainty is the aspect of high volatility.

### Is The Rally Faltering?

**T**he month of October produced flat to negative results in the major U. S. stock averages for the first month in several.

We have been advising that this rally could not possibly continue at the same pace it has enjoyed.

Here are the results:

#### Dow Jones 30 Industrials

|                |           |
|----------------|-----------|
| October        | + 0.00 %  |
| Last 3 months  | + 5.90 %  |
| Year to Date   | + 10.68 % |
| Last 12 Months | + 4.16 %  |

#### Standard & Poor's 500 Index

|                |           |
|----------------|-----------|
| October        | - 2.00 %  |
| Last 3 months  | + 4.96 %  |
| Year to Date   | + 14.73 % |
| Last 12 Months | + 8.60 %  |

#### NASDAQ Composite

|                |           |
|----------------|-----------|
| October        | -3.63 %   |
| Last 3 months  | + 3.39 %  |
| Year to Date   | + 29.68 % |
| Last 12 Months | + 18.83 % |

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