# Market Recovery Do-It-Yourself Rule Of 72

# 13

GIBBS HILL LIGHTHOUSE.

Since 1846, casting a beacon of safety into safe harbours for sailors offshore Bermuda in treacherous, stormy seas

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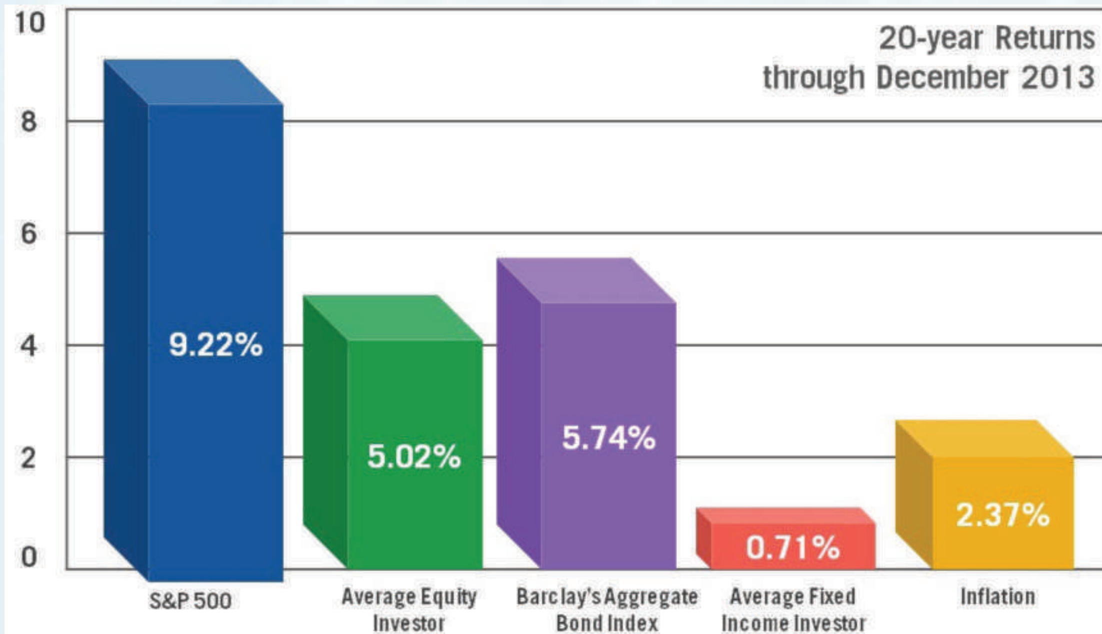
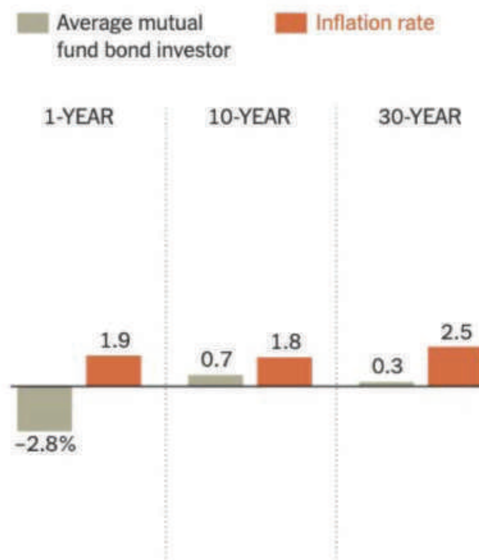
DALBAR QAIB (Quantitative Analysis of Investor Behaviour) 2013 & 2018




ANNUALIZED RETURNS




By The New York Times | Source: Dalbar 2018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# Step Thirteen - Rule of 72, Market Recovery, Do-It-Yourself Investing

Your review plan is almost finished - don't give up now.

What average returns should you be looking for in long-term appreciation of your pension and your personal investing?

The charts above demonstrate on a statistical basis the average return for stocks, bonds over thirty years through year end 2018. Source courtesy of Dalbar Inc.'s QAIB report (Quantitative Analysis of Investor Behaviour) and the New York Times. We see that the S&P index (made up of the weighted values of the 500 largest publicly traded US companies by market capitalisation) returned 9.22%, the Barclays Aggregate Bond Index (representing most US traded investment grade bonds) returned 5.74%.

These indexes are not adjusted for fees.

Yes, there is another set of numbers in that chart. We will discuss them later in the article. For now, take a guess what they represent.

Thus, using simple math assumptions for a pension balanced fund of 60% stocks and 40% bonds, the average return - without taking into consideration any fees for management, administration, sales commissions, custody fees, etc. - would be somewhere around an estimated 7%.

Using ordinary assumptions, then, a more conservative portfolio (more bonds than stocks) would generally have a lower return than the balanced fund, and a more aggressive fund weighted toward stocks will be closer the stock index. Keep in mind, that these are average returns - meaning that on the proverbial bell curve, some securities under-performed while others will reach higher than the average.

## Fee-adjusted rates of return.

Now comes the more difficult section because different pension firms, different portfolio managers may calculate fees in different ways.

What does this mean to you? Fees affect the growth of your pension portfolio (or any portfolio) over time. You want your pension portfolio to have competitive fees with the real fee-adjusted rate of return reported on your statement so that you know where you stand.

Mutual fund fact sheets, generally, disclose all fees as well as reporting the Total rate of return - NET of fees.

I was unable to determine – based upon website information currently available – what the total fees are charged by the local Bermuda pension administrators / managers by reviewing their websites. Fees may be disclosed to you individually, as a holder of a pension account - so, it is up to you when meeting with your pension advisor to obtain fee clarity.

Calculating an illustrative fee-adjusted rate of return. Let's assume that the total fees are estimated 2.%. Taking our assumed average rate of return for the illustrative balanced fund of 7. % minus all fees of 2. % = estimated real adjusted rate of return (RoR) of 5%.

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## How Am I Doing - Investment Wise?

A very simple calculator to track how your investments are accumulating is The Rule of 72. Take an illustrative accumulated pension example: Individual worked for ten years and accumulated 70,000 in a pension. Divide 72 by RoR 5% = 14.4. The answer means that the accumulation of $70,000 MAY double in 14.4 years without any additional pension contributions at all.

But, this is a big point, remember that investment returns will fluctuate. Your pension investments will not compound on a straight-line basis, because they are invested in capital market assets. However, over the longer term, the average return can possibly be around 5%-7% for a balanced portfolio.

## The Rule of 72

The Rule of 72 works fairly well for the range from six to 10. Outside that range, there are additional calculations needed; it can be more efficient to use an online calculator.

| Rate of Return (%) | Divide into | Approximate Number of Years to Double Investment |
|---|---|---|
| 6 | 72 | 12 years |
| 7 | 72 | 10.3 years |
| 8 | 72 | 9 years |
| 9 | 72 | 8 years |
| 10 | 72 | 7.2 years |

| US MARKET CRASH DATES | RECOVERY TIMES |
|---|---|
| 1987 | 456 trading days |
| 1997 | 46 trading days |
| 2000 | 1015 trading days, including the tech bubble blow up and the terrible tragedy of September 911 |
| 2008 | 230 trading days |
| 2011 | 116 trading days |
| 2015 | 30 trading days |

Critics will say this is not realistic, but the long-term appreciation bears this out. Imagine adding in additional contributions as well. Most important, this number also assumes that you do not move your pension in and out of various allocations, selling at the low values, and taking losses.

See complete article. "Thirty years of stock market crashes – and the signs they were coming," by Kyle Caldwell, The Telegraph, October 17, 2015. http://goo.gl/6UrslT


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## If Time is On Your Side, Think Long-Term

Do yourself a favour.

Think long-term, always with the exception of the close-to-retirement individuals.

Be willing to be a little more investment aggressive when you are younger, then, tapering off as you age, accumulate other savings and investments, your first home, an individual investment account.

Why? Because time is on your side.

Do not focus on short term investing results. Further, there have been numerous market volatility episodes as well as capital market crashes. Each and every time, markets have recovered from loss positions, and moved forward into positive territory.

The above chart that records only the major disruptions since 1987 demonstrate that truism. Even the great depression of 1929-1933 in the United States saw the US securities market recapture the loss valuations.

It is reassuring to understand that even though the entire global economy is in severe disruption due to COVID-19, eventually, capital markets will again (and have) returned to normal.

Postscript - and they did recover quickly!

## Should You Be A Do-It-Yourself Investor?

Can you translate understanding your pension investments to taking tentative steps as an individual investor? Consider do-it-yourself investing, or taking the passive investor approach with high quality, low cost mutual or ETF funds?

We, along with millions of individuals the world over, have been depleted emotionally, physically, mentally and financially during this tragic, catastrophic COVID-19 pandemic. Thousands of families have lost loved ones forever, had their work and home life disrupted, and have seen their financial security well into the future almost destroyed.

The social-distancing quarantine has been exhausting, as we have coped with the most daunting event of our lifetimes. Most of us would rather not, for a while at least, reflect on our roles or goals moving forward.

But we have to move forward.

Life will not stand still. We are all one-step closer to retirement, whether that day is next year, five, ten, or thirty years away.

We have much to achieve in the interim.

We, as people, are intuitive, incredibly smart survivalist-attitude individuals with highly developed reasoning processes.

We can, and must vote for survival back to normalcy, to begin to plan ahead again:

- to continue to take charge of our finances;
- to keep up disciplined savings and maintain less exuberant spending:
- to become more financially savvy with our goals to financial success

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**Pluses.** Should you think about just buying individual stocks or bonds, since you have more control, and can possibly save fees? The process requires much investment educational reading, opening an individual investing account here in Bermuda or online, keeping your emotions in check when markets are crazy and monitoring of your security positions.

**Minuses.** Don't feel you can be a successful DIY individual investor? There are valid reasons: Individuals cannot afford to buy sufficient securities to diversify investment risk; they react emotionally, making poor decisions during market downturns; having barely enough energy to focus on family, working and living, DIY just becomes another life stressor.

## Investment Mistakes.

## You will make them.

According various industry sources, the biggest errors that investors make are these:

- too aggressive a portfolio for your comfort level, especially at a close to retirement age
- young investors who are far too conservative based upon their own career longevity
- the worst of all, reactionary pension (and individual) portfolio moves in and out of aggressive to conservative allocations when markets crash, thereby locking in losses, reducing your portfolio capital, sometimes never to fully recover.

And, that is what the second set of numbers represent on the Dalbar charts, listed above, The average equity (stocks) and fixed income (bonds) by D I Y investors do not come close to index and inflation returns - one of the largest influencing factors is investor behaviour.

**You guessed it!**

Investors sell out at market low values and pile into investments when markets are at high prices.

Even, if after understanding what investing is about, you decide not to participate, you will have enhanced your investment knowledge and have a better comfort level relative to your personal finances, along with your future pension investment management.

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But, taking on this task means that you have to commit to understanding investments and what choices are right for you!

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## How should you start DIY?

- Basically, with one – to a few stocks of companies that are familiar
- Invest small amounts of cash
- Use the twelve research principles below and other research sites when researching a stock and the underlying company
- No investing until you have your emergency cash cushion fully funded
- Be comfortable and prepared to possibly lose the money you invest

The securities themselves – review the company balance sheet – you can quickly find this information in Yahoo Finance by typing the stock name or ticker into Google.


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The company balance sheet is an integral part of the company financial statements.

A. lots of free cash
B. low debt ratio
C. consistent dividends for at least ten years
D. low dividend pay-out ratio
E. decent profits year on year
F. company revenue increasing along with market share
G. little or no company share buybacks
H. more company insider buys than sells
I. stable-type industry, products or services that everyone needs on a consistent basis
J. monitor the industry for changes
K. set a profit margin at which to sell the stock
L. be very careful of young companies operating on venture capital and loans with no consistent revenue and profits

Refer to the Stock Criteria Selection Checklist featured in Step 10 for further help.

## Your discovery process needs to be two-fold:

- learning about securities and
- understanding how they work.

So, your work is cut out for you, but you will find it illuminating and so very interesting.

Beginner investment websites for three of our large North Atlantic neighbours that are easy to digest are listed below in References and are good places to start.

Bermuda is a cosmopolitan finance jurisdiction. Bermuda residents themselves often invest overseas, while work permit holders from other countries can utilise this starter information as well.

Once familiar with basic investment concepts, take your curiosity further to explore websites that are strictly fact-based and educational, rather than financial sites that ultimately want sell you something.

Research websites online trading services also listed below also allow you to practice simulated trading, giving you an almost real experience of how capital markets work.

But be forewarned, of the following:

## Watch your financial emotions and reactive investing decisions.

You should also know that overall, individual investors have not always fared well – investing on their own behalf. We individuals tend to react emotionally when dealing with issues of money. The educational term is researched under Behavioural Finance (and see the Dalbar Quantitative Analysis of Investor Behaviour) – the Internet is loaded with sites addressing this very topic that boils down to the following:

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The emotional herd mentality.

Buying securities at the high valuation and selling at the low, thereby setting yourself up for realised losses.

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I highly recommend that you, as a beginning DIY investor start the process with these basic thoughts:

Understand that you may develop an emotional attachment to stocks, bonds, etc., but remember stocks are not people, nor should you love them because they will not love you back.

Develop your own risk assessment and a trading plan to adhere to, so that you do not react emotionally to severe market volatility. The COVID-19 market crash is the absolute emotional test, possibly of this century. Ask yourself, would you be more than tempted, maybe even frantic, to sell everything when seeing a more than 30% drop in value of your investments **– on paper.**

## Know this as well.

Capital markets today are not the markets of old. Your small investor trade choices will be up against the rapid activity (micro-seconds) of thousands of remote computer-trading models, short-sellers, high-frequency traders, robo-advisory service firms, and extraordinarily nimble massive global financial institutions with immediate access to investment information that you won't have, along with the trading power to overwhelm the system.

CAVEAT: Bermuda residents may have difficulty opening trading accounts in other jurisdictions due to FATCA, AML/KYC and other international and domestic tax/anti-money laundering compliance.

Know What market conditions are on a current basis always understanding that those conditions can change without notice.

For instance, Capital market security valuations during the COVID-19, on average, fell incrementally well below the euphoric conditions for the prior several years and below the 2008 global market crashes.

There are more than 15 million websites for the do-it-yourself investor – some generic, some complicated, some cumbersome. Moneywise cannot recommend any specific website, but here are some common sense (and experience culled from many years of working with clients) does and don'ts to get you going. There are also some suggested websites to start your DIY in the reference section below.

You can track small investor trading patterns (like yourself) by utilising the TDAmeritrade monthly Investor Movement Index® (IMXSM).

The Investor Movement Index, or the IMX, is a proprietary, behaviour-based index created by TDAmeritrade designed to indicate the sentiment of individual investors' portfolios. It measures what investors are actually doing, and how they are actually positioned in the markets.

Sign up for their monthly email.

The IMX does this by using data including holdings/positions, trading activity, and other data from a sample of their 11 million funded client accounts. Type IMX TDAmeritrade into Google and sign up. It's free, monthly and very, very interesting.

Use Yahoo Finance or a like-kind website for easy access to current markets (and your stocks condition).
Yahoo Finance is featured in numerous country-specific websites, e.g. US, UK, Canada, Japan, Australia, Germany, and more.


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## The process

1. You will need to open an investment account at a brokerage and/or a mutual fund firm.

   Be careful about this process.

   You may be handed a lengthy contract - read it carefully. A basic brokerage account may also include a request to open a margin account where you can purchase investments on margin (leverage).

The use of margins or leverage to accelerate your profits – and your losses – is never a good idea for a beginning investor. Essentially, you are contracting for a loan with the brokerage firm; this loan is secured by the value of your underlying stock positions, for instance. If the stock value heads south, you will be subject to a margin call and will be expected to remit any difference in cash to the firm. If you are unable to equalise your position, the brokerage firm will move to sell your positions, and attach lien to other assets you own, if you cannot replenish your account.

2. Set a profit, loss and time limit on each position. Some investors decide on a timeline based upon the 200-day S&P moving average. For instance, if your security position is net after costs 20% above that recent line in three months –you can sell! After all, that is an annualised return of 80% per year.
3. Do not give in to greed by coveting huge gains. Just because one stock is doing well, this does not mean you should buy more of the same – suddenly you may find all your cash tied up in four stocks. **Now that's an emotional roller coaster.**
4. Do not start loving any stock, mutual, hedge, or any other security. If it rises in value and it's time to sell according to your formula, say a 25% gain in a year, sell it. If it drops in value, do not hold on, hoping and hoping. Sell it and move on.
5. Buy small positions, say $1,000 per. If one stock performs really well, and you do like it, sell off all the profit, back to your original position, invest in another gem.
6. Do enough research on each position to understand how it reacts in volatile markets. www.smartmoney.com has a great tool called Map of the Market, which shows hues from dark green to red, with bright red indicating more volatility and price swings in a stock. You can also use Yahoo finance and set up a five-year chart for any stock that will demonstrate quite vividly historical price swings.
7. Buy equities of companies you know and whose products you use consistently, Learn to Earn, as Peter Lynch says. Chasing unknown penny-stocks and other short-term plays is not for the timid, the beginner, or the budget minded.
8. Read Bloomberg every day. Research commentary you don't understand. You will down the road!
9. Do not be tempted by website and media ads to trade currency, options, and other 'get rich quick' enticements.
10. Do not be tempted by the super slick salespersons. They will promise anything to make a sell. Take your time reviewing and thinking about your buys. Research never hurt anyone.
11. Pay attention – at least once a week or more. Consider joining an alert type service (or uploading it yourself ) that will notify you if your positions are changing.

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11. Compute your real rate of return and watch your fees. Broker commissions, turnover costs, mutual fund fees, back end loads all take a chunk out of your actual profit. Do not delude yourself, do the maths and get the real net rate of return. If you live in a tax regime country be aware of the tax impact on your rate of return, e.g. capital gains, dividend tax, etc.
12. Beware of implementing trades during your workday – this type of activity is not condoned and is considered a redundancy offence in today's heavily-remotely monitored employment arena.
13. It is always wise to remember that investing is a Zero-sum game. For every gainer, someone is a loser. You won't win all the time, but you want to land on the winning side on a consistent basis.
14. Never believe your friends, or anyone else about how spectacularly successful they have been. No one wants to admit to a loss – and if they do, you know it was a zinger.

Now, after reading this, if you feel exhausted or that you'd rather garden or plan your next trip, you know that your homework has a different tilt.

Rather than researching good stocks to buy, consider a focus on establishing a relationship with an objective licensed experienced investment professional.

See STEP Seventeen: The Alphabet Soup of Financial Advisors

Not all of us can or want to do it ourselves.

I urge you to continue to learn about your investments. They are so important for your future financial security.

Time after time.

## Finally, A buyer-beware investment anecdote (true).

An individual met with a broker at an investment firm - requesting something that would return a good fifteen percent (15%), then plunking down $25,000 on shares of one single company hot stock.

What a great rate, 15%, but one always has to consider the risk and safety of the security as compared to the US risk-free rate of return, generally, the United States ten-year treasury note. At that time, the US T-Note was paying around 4% rate of interest.

The beginner investor's stock had almost 4 times the level of risk.

A few hours later, after a particularly volatile market day, the customer was over- heard - on the phone, yelling at the broker! "You told me this was a good investment! Look at what is happening, the value is dropping like a stone. This is all the savings that I have."

The customer was devastated - but there are two things that did not happen.

The customer never told the broker this was his entire savings.

And the broker never asked. Who was at fault?

**Both of them.**

True story.


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# References
# & Resources

Here is a sampling of a few websites for DIY, but there are hundreds more. Use your own discovery process to find investment educational websites that you are comfortable with.

Bermuda Stock Exchange. www.bsx.com Investing Tutorial

Importance of DALBAR QAIB (Quantitative Analysis of Investor Behaviour)

The best financial professionals double as behavioural finance coaches of their clients. When markets are down or even volatile, questions will arise from concerned clients and perspective will be needed. The QAIB report and materials give advisors the tools to tell a story, put things into perspective, and deliver the calming messages that are needed to mitigate return-destroying behaviour.
Such messages include:

- The prudence of a long-term, buy and hold approach
- The folly of measuring investment success against statistical benchmarks
- Awareness of common behavioural influences
- Lessons from past markets
- The importance of investing assets as early as possible

Investors Are Usually Wrong. I'm One of Them. By Jeff Sommer July 26, 2019,

The Investing Educator: Focused on improving your investment knowledge

https://investingeducator.com/

For Canadian investments and investors

StockChase.com- 7 Essential Tips and Tools to Succeed as a Canadian DIY Investor

Simon B. March 25, 2019

Investing Sites
Schwab Trading Services
StashInvest.com

Research

The Globe and Mail
Yahoo Finance Canada
Canadian Securities Institute

US Investments and Investors

TheBalance.com. Best Investment Apps of 2020.
Financial Samurai. Slicing Through Money's Mysteries
SoFI Investing 101 Center: Investment Education For Beginners

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- TD Ameritrade. New to Investing Research
- Investopedia. Investment Education and Stock Trading Simulator
  Yahoo Finance US
  Seeking Alpha – for the more sophisticated
  US Securities & Exchange Commission

- United Kingdom Investments and Investors
- MoneytotheMasses. Best Investing Apps in the UK for Smart phones Nutmeg, Plum

- Regular investing websites
- Vanguard – funds only The Share Center Research

- This Is Money UK DIY Investing
  Yahoo Finance UK
  UK FCA Financial Conduct Authority/ Consumers

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Market Recovery1

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