

November 30, 2000

Dear Friends,

I received a call from a customer this morning concerned about the effect of the market decline on her investment portfolio. Since she was calling from overseas, her call suggested that my other customers and friends might be equally apprehensive and that I should share the advice that I gave her.

The question was whether she should move to cash. This is a difficult decision because getting out of the market implies that you are confident that you will know when it is time to move back in. If the market bounces back in mid December when the US presidential result is clarified, and you are in cash, you will lose out of that gain.

My advice is to design your portfolio so that near term gains and losses are unsettling but not important over the long run. This means having enough money in CDs or bonds so that you can weather an extended market downturn without being forced to sell stocks. By enough money, I mean three, five or even ten years worth. The more cautious you are, the more money you should have in stable investments.

If you don't have a "rainy decade fund" you probably should create one, even though this means selling stock when the market is down. But do it gradually, perhaps by doubling your current withdrawals and putting the extra money in stable investments.

If you have a "rainy decade fund", you should probably take withdrawals from your stable investments until the market recovers. Let us hope that the present decline is only a memory six months from now but the more likely scenario is that the recovery will take several years.

Investing is not just about making money, it is also about taking no more risk than you are comfortable with. If you are frightened by the current market, we need to make some gradual changes. If you have adequate resources, we should reduce your stock market exposure. If your portfolio is worth 25 or fifty times your annual withdrawals, you could get out of the stock market entirely and invest in inflation protected US securities. If you need a 10% return, you cannot afford either of these alternatives and you will have to reduce expenditures or find additional sources of income (part time employment, a reverse mortgage.)

Market fluctuations are less important if you are working since you do not yet need your investments. But this is probably not a good time to anger your employer!

These ideas are further explored on my website. Check out the topical bibliography at <http://lingane.com/tax/biblio.htm> or my discussion of inflation protected US securities at <http://lingane.com/tax/tips.pdf>.

Sometimes, we become less apprehensive the more we learn more about a subject. It might help to read Jonathan Clement's book or one of the books by John Bogle.

Please give me a call if I can be of assistance.

Regards,

Peter