



Portfolio strategy: Ken Fisher

Forbe's Magazine's Portfolio Strategy columnist and Fisher Investments chief executive **KEN FISHER** argues that maintaining a defensive portfolio is the best strategy since a widely expected bull market has not materialised

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A yet rougher ride is in store for fatigued bulls

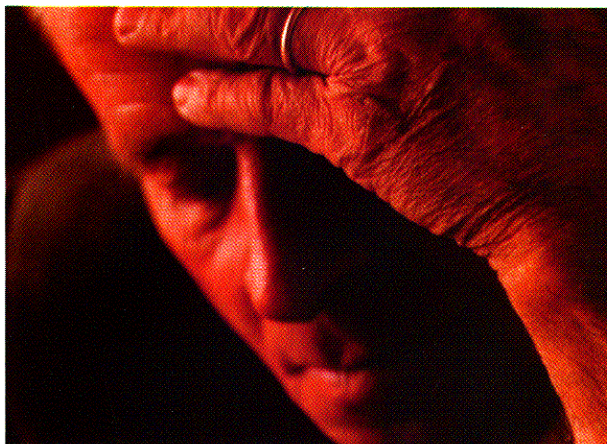
The stockmarket is no higher than in November or September. Many investors think a new bull market began in September but there is little carry-through from supposed recovery. The momentum has gone. The market looks fatigued. Can an upturn be real if its initial thrust isn't sustained? I think not.

Although Americans overwhelmingly believe it's a new bull market, continental Europeans and Japanese are still praying for robust US expansion to hoist them up. They hold no hope of being able to build their own recovery. The UK economy is stronger than most others and the normal Brit doesn't sense the global risk.

In the long term, financial markets even out competing costs of capital. Stocks versus bonds. Domestic versus foreign. Big versus small. All are competing for capital. In the short term, though, the stockmarket is a fatigue-ometer, measuring whose sentiment is wearying fastest. Right now it's the bulls. Why?

There is no US recovery nearly strong enough to pull up other economies. Indeed, deterioration in Europe and Japan impinges on the US. Few Americans fear this, though, because the positive outcomes of the crises of 1997 and 1998 trained them to be sanguine about foreign risk.

The autumn rally caused too many investors to become over-optimistic about 2002. The same thing happened in the spring. But the length of time for which the market has noodled nowhere indicates that optimism was misplaced. There's more fatigue to come for bulls.



As the new year fizzled into a non-January effect, those who had bought expecting a rally were overcome with fatigue

By December, a measurable consensus had grown that 2002 would be positive – and even that we would have a traditional “January effect” buoying up stocks. But if you expected a January rally, when would you buy? December, right? So December was strong. But as the first few days of the new year fizzled into a non-January effect, those who bought with that expectation were overcome with fatigue. The longer that stocks are down year to date, the more investors expect continuing stagnation. All this increases net selling pressure.

Note the January news that the US had a minor positive growth in GDP in the fourth quarter. With that the stockmarket fell. Only a fool would believe the US economy didn't actually contract in the quarter. Perhaps it was becoming clear to investors that it wasn't just Enron and a few fraudulent firms with funny accounting. As I said in *Forbes* five and 10 years ago, the US accounting system is

seriously broken and should never be believed. Yet when folks notice its erroneous ways they still panic. There will be more fatigue from this as GDP growth is steadily revised downward in 2002.

Further on this year is a US election. I'll say flat out that it is highly likely that the Democrats will take control of the House and increase their control of the Senate. If I'm wrong you'll see it via a sweep of six hair-trigger-close Senate races. These will be Minnesota, Missouri and South Dakota – where Democrats are vulnerable – and Arkansas, Colorado and New Hampshire – where Republicans are vulnerable. Each party should win three. If either sweeps the board that would take the Senate. This should become a clear and present fear by late spring. With investors much more Republican than Democrat, this too will induce fatigue.

In the US the market is about at its lows from last spring. But, elsewhere, markets can't begin to get back that high. The rally hasn't had the strength it had in the US and flattened and rolled over sooner. As it has declined, the continental Europeans and the Japanese have felt more fatigue than Americans. But fatigue is contagious, as are all market emotions. Without strength in Europe and Japan, the market will continue to fatigue Americans and stocks everywhere will drift lower into mid-2002.

If you don't want to be further fatigued, keep your portfolios as defensive as possible. Remember, at its end a bear market is most brutal. The ride gets rougher ahead.