

The following constitutes the general views of the author and should not be regarded as personalized investment advice or a reflection of the performance of Fisher Investments or its clients. Nothing herein is intended to be a recommendation or a forecast of market conditions. Rather it is intended to illustrate a point. Current and future markets may differ significantly from those illustrated here. Not all past forecasts were, nor future forecasts may be, as accurate as those predicted herein. Investing in the stock markets involves a risk of loss. Investing in foreign stock markets involves additional risks, such as the risk of currency fluctuations. Past performance is never a guarantee of future returns. This article is from the year 2010 and statements made as of this date may no longer be applicable.

Article

Outside the Box with Ken Fisher

The wise man of Woodside talks about his new book on detecting financial fraud and offers his always unique perspective on the current market.

BY [JANE WOLLMAN RUSOFF](#)

Published in the [3/1/2010](#) Issue of Research Magazine.

[Return to Article](#)

Redwood-rich Woodside, Calif., is geographically and aesthetically about as far away from Wall Street as you can get within the U.S. Yet this small town on the San Francisco Peninsula is headquarters of one of the investment world's foremost experts.

Money manager Ken Fisher, 59, a champion of value investing, is developer of the price/sales ratio and famed for ground-breaking investment-cycles research. In the autumn of 1990, he notably called the start of the decade's roaring bull market. He has written Forbes' "Portfolio Strategy" column for 25 years.

Fisher, son of legendary investor Philip A. Fisher, is founder, chairman and CEO of Fisher Investments, managing \$38 billion in assets of prominent institutions and affluent individuals. Founded in 1979, it has a London subsidiary as well as a joint-venture affiliate in Germany.

In his latest book, *How to Smell a Rat: the Five Signs of Financial Fraud*, written with Lara Hoffmans (Wiley 2009), The New York Times bestselling author tells consumers how to spot a swindling advisor to prevent falling victim to his scheme.

Research chatted with the native San Franciscan about how his book can help financial advisors, as well as a broad range of economic, political and market trends.

Your book alerts consumers to red flags that might signal embezzling FAs. But what's the lesson to advisors?

To set themselves up to do the reverse of those things — and not just for the sake of marketing or even client service. For instance, separating custody from decision-making protects you from yourself. Many Ponzi-scheme artists didn't set out to intentionally cheat clients; some took custody and then, at a moment of weakness, dipped into the till and never got out.

Why should investors seek advisors that make it easy to conduct due diligence on them?

The easier you make it for clients, the more likely they'll do it — and the more likely they'll be comfortable with the advisor. Be as transparent as possible. The Ponzi-scheme guys invariably make it as hard as possible because they don't want to get caught.

You advise against the popular strategy of putting assets in disparate pockets but, instead, to think holistically. Please explain.

That's the basis of Modern Portfolio Theory. It's such a basic concept, but so hard for people to "get": You want the simplest portfolio that maximizes expected return relative to expected risk. Anything

beyond that is excess diversification and a negative; anything less isn't enough diversification.

Be wary of advisors who make a big deal about their hobbies, you write. Why?

I'm not trying to suggest that no one should have a hobby or that golf should be banned. But bragging about your hobby leads to the notion: Is the customer hiring you because you're an advisor or because, say, you play in a rock 'n roll band? If it's because you play in a rock 'n roll band, that's a bad reason.

You warn readers about feeder funds, or funds of funds. What's wrong with those?

They're ludicrous. It's fees on top of fees on top of fees. It's ever-more complexity in a world where less complexity is better for the customer. Myriad managers co-mingled creates excess diversification and lack of control — both are negatives. It creates complexity so that neither the customer nor the advisor really knows what they're getting.

You recommend that investors ask advisors, for example, how they decide which countries to invest in. Do clients really have to know that process?

The advisor needs to be able to explain basically what they do. That doesn't mean the customer could do it or that they necessarily understand all the nuances. But if advisors believe that it's not any of the customer's business to understand how they do what they do, it puts them in the realm of the Ponzi-scheme artist: "You can't figure out this stuff, so don't ask." Whereupon, they take it out the back door — because "You don't know what I'm doing anyway."

Zeroing in on 2010, what can we expect from the market the rest of this year?

Going back more than 100 years, in the United States a big market drop followed by a positive year — which is what we had 2008-2009 — has been positive for the next year all but one time. And that was only a negative four-tenths of one percent in 1933. A huge drop (a bear market) and then a positive year (the big rally of 2009) is a very bullish sign for the period ahead. So this combination portends a positive 2010.

But that's going only by history. What if some terrible event occurs? Couldn't that throw it off?

Sure, we could have a nuclear war or an actual [viral] epidemic. But you can't find one example showing the second year to be markedly negative after a big drop that was followed by a big year. Whenever you're [expecting] something that history hasn't had happen before, it's a really tall order. History isn't a perfect guide; but when you want to buck it, you're asking for something big. It's a hard thing to bet on.

What does the term you've coined, "the Pessimism of Disbelief," mean — and what's important about it?

Investors are focusing on negatives. That stocks aren't higher and people aren't wealthier have them pessimistic. Anything that's bad is, of course, bad. But anything that might be characterized as a positive is disbelieved and turned into something bad, a negative.

Something that might be good would be, for instance, the stimulus effort. But that's seen as too much government spending, likely to cause inflation, socialistic in nature. So, the thinking goes, it's probably bad. It won't work, and it will lead to problems, whatever it is.

How widespread is this attitude?

It extends all over the world. Pessimism and not believing in good things has become faddish. Believing that America's best days are over has become the norm. Being optimistic is seen as a fool's game. In that regard, it's an extreme hyperextension of pessimism on top of a lack of optimism: The bear market we had [2008-09] was the first I've ever seen that was not preceded by a period of tremendous optimism about stocks.

What does all this gloom mean to the market?

It's positive. The Pessimism of Disbelief is actually the archetypical example of what otherwise is thought of as the wall of worry a bull market wants to climb. That is, if there's that much pessimism, we're going to get less pessimism as we go forward. That buoys stocks. A sign of excess pessimism is already priced into the market.

What do you make of America's leftward political trend?

Americans have largely become frightened by Mr. Obama: Hard-core Republicans always hated him; and with the more moderate and independent people, his polling numbers have fallen steadily. (Hard-core Democrats liked him and still do.)

[Many] Americans are paranoid about the shift to the left in politics. But they don't think about the fact that, on balance, the other three-quarters of the world — though not all places — is shifting to the right. Most Americans don't think about the fact that for most non-U.S. developed nations, the trend has been moving the other way.

What effect does that trend have on the market?

More stability. People who are frightened because of the leftward movement and how that might impact U.S. markets don't stop to appreciate that the rest of the world is going in the other direction. And in whatever direction the world goes, the U.S. is going also. The non-U.S. market has been leading the U.S. market for a long time. If people are [still] U.S.-centric, they're probably missing the forest for the trees.

What are your thoughts about the fad-like enthusiasm for gold?

Historically, most gold bugs have believed the real value of gold is that it's going to provide you with a return that's either negatively correlated or non-correlated to the rest of what you own. Actually, over time, the correlation between gold and other things has varied widely. During the last couple of years, gold has been amazingly positively correlated; e.g., with the S&P 500.

The question should not be, "Is gold good or bad this year?" but "How good a timer are you?" Because since Bretton Woods [the international monetary management system] broke down [in 1971], 85 percent of the time, on a monthly basis, gold actually lost money; only 15 percent of the time did it make money.

What's the bottom line here?

You've got to be a really good timer to make money in gold. If you're not able to do oil very well, you're probably not able to do gold very well. If you didn't figure out to do emerging markets last year, you shouldn't be thinking about gold.

Many consider gold to be a long-term holding. But you say that's wrong, right?

Too many people end up buying into gold because they think that. Again, gold has made all of its return and more in 15 percent of the months. The rest of the return is a negative 6.3 percent. So if you didn't get those 15 percent of the months, the other 85 percent is a negative return. That's a point most people don't think through.

Speaking of emerging markets, what is their role now and up ahead?

Emerging-markets stocks remain cheap. Thirty-five percent of global GDP is emerging markets. That's markedly bigger than America. [People] keep looking for America to lead the world. But they don't realize that the emerging markets world, which is half-again as big as the U.S. in terms of total GDP, is actually leading.

Americans tend to [still] have the view that, as goes America, so goes the world; America catches a cold, the world gets pneumonia. But today it's the other way around. The other portion of the world is where the growth is. That economy started improving well before ours did.

Which specific regions are stand-outs?

The entire emerging-markets world is leading, whether it's Hispanic America, Eastern Europe, India. Mind you, you can find problems in any of these places. But it's emerging markets first, portions of the developed world second and America third, lagged by other portions of the developed world. Today, emerging markets are leading the world.