

Perspectives

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What We Know Makes Us Wise

Tony Batman, Chairman and CEO, 1st Global

In September 2008, our industry weathered “Lehman Weekend,” which began one of the most difficult tests investors would face. Just three years later, we are all victorious over that test and we are all wiser for it.

Since July 25th of this year, despite some recent rallies, the market has declined precipitously. We also are all aware of the stubborn 9.1 percent unemployment rate. One in seven Americans are on food stamps and the Gross Domestic Product (GDP) is ambling along at an anemic one percent. These events would lead any normal investor to fear the test of 2008 is happening all over again.

But it is vitally important we remember what is old is new again. A student of history knows this current turmoil will cycle through. To illustrate, see the following excerpt from *Time Magazine*.

If America's economic landscape seems suddenly alien and hostile to many clients, there is good reason. They have never seen anything like it. Nothing in memory has prepared consumers for such turbulent, epical change. This sort of upheaval happens once in every 50 years. Even the economists do not have a name for the present condition, but one has described it as suspended animation and never never land.

The outward sign of the change is an economy that stubbornly refuses to recover from recession. The current slump already ranks as the longest period of sustained weakness since the great depression. That was the last time the economy staggered under as many structural burdens as opposed to the familiar cyclical problems that create temporary recessions once or twice a decade.

The structural faults represent once in a lifetime dislocations that will take years to work out. Among them, the job drought, the debt hangover, the banking crisis, the real estate depression, the health care cost explosion and the runaway federal deficit. "This is a sick economy that won't respond to traditional remedies," said Bank of New York Mellon economist, Norman Robertson. "There is going to be a lot of trauma before it's over."

This article appeared, not a few weeks ago, but on September 28, 1992. The year 1st Global was founded.

It is important to remember to stay on course. Not too long ago, 1st Global's advisor, Dr. Harry Markowitz, was asked by *Research Magazine* to defend Modern Portfolio Theory (MPT). Developed in 1952, MPT seeks to minimize risk for a given level of expected return, by carefully choosing the proportions of various assets. He responded by quoting the following ancient proverb:

He who knows not, and knows not that he knows not, is a fool. Shun him.

He who knows not, and knows that he knows not is simple. Teach him.

He who knows, and knows not he knows, is asleep. Wake him.

He who knows, and knows he knows is wise. Follow him.

I would submit we are certainly not fools. But perhaps some of us may need a bit of a wakeup call. We need to remember that we know, and know we know and are wise.

Remember What You Know...

In the world of behavioral finance, the analysis of anxiety and fear is an interesting academic study.

Humans desire certainty, including investors who invest for their future in ambiguity. In absence of certainty, people become anxious. Anxiety is worse than fear. Anxiety expresses itself in a loss of direction, lack of action, inadequacy or overreaction.

Human nature transfers anxiety to fear. To cope, we need to dedicate our emotions to the source of either our anxiety or fear. When we cannot identify the source of the anxiety, the anxiety becomes the threat instead of the actual source of anxiety.

We must stay focused on reality and not on anxiety. History tells investors the turmoil in our economy is cyclical. This is what **we know**. We must stay engaged with our financial advisors who are constantly working on being the best at their craft. They will work with you to ensure your current plan is on track. **Then we know, we know**. So therefore, when it comes to investing, **we are wise**.

Strong Convictions Precede Great Actions

David Knoch, President and Chief Operating Officer, 1st Global

Since the last week of July, the stock market has been tumultuous, reminiscent of the disastrous market activity of 2008 and 2009. Just as many of us saw our investment accounts, 401(k) balances and other wealth recover, we see it slipping back again and wonder if the same kind of losses are ahead of us. The unfortunate reality is none of us can truly know. What we want, is a moment of clarity, a moment of *certainty*. . .

By definition, the future is uncertain. None of us can predict what will happen in the next decade, next year, next month, next week, tomorrow or even a minute from now. Nevertheless, we still feel a sense of responsibility for the future of our family, our friends, our places of worship and the other institutions we belong to. This creates a tremendous amount of anxiety. To manage, we do everything in our power to take action to bring order and clarity to a future beyond our control.

To create certainty where uncertainty exists, we consciously or unconsciously, verbalized or internalized, make promises. We promise to live deep into our retirement and never become a burden to our loved ones. We promise to give back charitably to our communities. We promise to save the down payment for our first house. We promise to send our children to the school of their dreams. These promises are intensely personal to each of us and they serve as a bond of honor. Our commitment to their reality stands firm in the face of uncertainty.

Although certainty is beyond our grasp, we are not powerless in these tumultuous times. Rather than fruitlessly pursue certainty, instead we can seek understanding and use it to develop a set of beliefs, based on fact, logic, history and faith. Your advisor and 1st Global strive to persevere through all markets, whether exuberant, cautious or fearful. These beliefs guide our actions over the short, medium and long term, and help our partner firms build portfolios, develop financial plans, or provide guidance to clients.

Since shared beliefs can deliver greater results, they transform into a “philosophy” as we continue to further our understanding, rationally, of the truths and principles behind investing. Investing is both a science and an art and has a rich history of brilliant minds that have shaped the past and influenced the future. We have the honor to work with two of these experts, on your behalf, on almost a daily basis (Nobel Laureate, Dr. Harry Markowitz and Father of Supply Side Economics, Dr. Art Laffer). We know there is much yet to be learned, and we are committed to the journey.

Here is what we at 1st Global believe:

1. Intellectual rigor, discipline, patience and a faith in the future matter.
2. Emotions influence actions.
3. Diversification, asset allocation and efficiency are separate and distinct concepts.
4. Asset allocation matters more than product selection.
5. Disciplined and automated rebalancing improves results.
6. Avoiding or minimizing losses improves the compounding power of wealth.
7. Annual equity market returns are normally distributed.
8. Mean reversion happens.
9. No one can predict the future; anyone who claims to, is lying.
10. Market timing does not work over the long term and those who extol its virtues suffer from a fallacy of composition.
11. Anyone can find confirming evidence, especially over the short term.
12. Investment skill can only be measured over long time periods.
13. Skillful managers can be identified.
14. Listening and advice are the most critical factors in developing and executing a plan to honor promises.

When faced with the prospect of losing the choices you have planned for so carefully, it's natural, proper, and justified to be anxious, scared and even angry. But these cycles in the market will repeat themselves and these emotions will become familiar over time. Working with an advisor who can help you develop *understanding* and share a set of beliefs designed to guide you on your way is critical to honoring your promises. Armed with a set of beliefs coupled with a clear understanding of why you hold them, you can easily equip yourself with fact, logic, history and faith; the tools you need to defeat fear in challenging times and stave off greed in exuberant times.

The American novelist, Louisa May Alcott, said it so clearly, “He who believes is strong; he who doubts is weak. Strong convictions precede great actions.” With an advisor you trust by your side you will have the strength to persevere in these challenging times and look back across the years to see how *your* strong convictions preceded *your* great actions.



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