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MONEY MATTERS

TIME, NOT TIMING, IS WHAT MATTERS

A ten-year bet made by legendary investor and one of the richest men in the world, Warren Buffet, comes to a conclusion at the end of this year. The wager has been hosted by Longbets, an organisation set up as 'a way to foster better long-term thinking'. The bet was that an investment in the S&P 500 index would outperform any portfolio of hedge funds over the ten-year period ending 31 December 2017. The size of the bet was one million dollars. But the winner will not keep the money; it is to be donated to a charity of the winner's choice.

There were very few bold enough to take on the bet despite the strong performance of hedge funds in the past, but one taker, Protege Partners, took up the challenge.

The hare and the tortoise

For Warren Buffet it looked like game over in a very short time as the Global Financial Crisis in 2008 brought down the S&P 500 index by 37% while many hedge funds revelled in the misery (through their 'short' and other contrarian strategies) by producing strong returns for investors. The timing for Buffet was disastrous. The S&P index took five years to catch up with the hedge fund portfolio but since then it has shot ahead and at the time of writing is showing a gain of 85% as opposed to just 22% for the hedge fund portfolio.

We haven't seen the end of the story yet as there are still a few months left in 2017 but unless there is a cataclysmic event that rocks the stock markets and hedge funds are able to capitalise on it (assuming they too have not been wiped out) then it seems extremely likely that the S&P index will win by a huge margin, and Warren Buffet's chosen charity will be the lucky beneficiary.

What does this tell us?

This tells us that staying the course, irrespective of temptations to keep buying, selling or switching from time to time, is likely to produce the best long term results.

You could substitute other indexes or asset classes and also see good returns over a ten year period. But many who have tried to actively 'play the markets' have ended up with losses. Trying to guess the best time to put money into or take money out of the markets is a fool's game, because markets can be very unpredictable. To quote Great Depression era economist John Maynard Keynes: 'Markets can remain irrational far longer than you can stay solvent'.

I have frequently heard the reason for not investing being "there are too many uncertainties; I prefer to wait a while." Often the nervous investor will wait until others have pushed up prices and will then wade in, missing most of the uptake and if too late, suffer losses when a bubble bursts. Many have been burned like this, not just with stocks but also with gold and property.

Selling at the wrong time can also be a mistake. Some fund managers in the past have got into trouble for trying to be heroes by moving into cash to preserve profits only to be left behind and watch other funds flourishing as markets continued to rise.

There is however one situation where you should stay out or get out of the markets and that is when you forsee a need for cash in the short to medium term. Stock markets, like property, are strictly for the long term (at least 10 years) unless you are prepared to take on the risks of short term speculation.

When is the best time to start a long term savings or pension plan?

The simple answer at all times is NOW! That is, provided you fully understand how they work and you are confident you can stay the course. If you have a steady job or business and – importantly – ample cash reserves, you can ignore the clouds on the horizon. Yes, I have known times when markets have fallen sharply just after clients have started a plan and have seen early losses. But it can actually be good news as there is then effectively a discount on the new money going in.

All such plans will see ups and downs as markets go through sometimes long cycles. But if the plan is invested in a diversity of assets with an emphasis on major markets it will invariably come out on top at the end of the day. I know because I have seen plans mature after 10, 15 and 20 years, including many held by expatriates in Bali. Admittedly, the end results have not matched projections supplied in the distant past, as 20 years ago interest rates and market returns were much higher than today. But they have invariably outperformed cash and perhaps, more importantly, provided a vehicle for accumulating savings in a disciplined manner that would probably not have occurred any other way.

What matters is not when you start, or where you are after one year or even half way through; what counts is the finishing line!

Why so many lose their way

Apart from seeing plans reach maturity and attain their objectives (nice to receive a lump sum of $100,000 or maybe a quarter of a million dollars shortly before retirement) I have also seen cases where others have lost their way and given up, often due to abandonment by their advisers and disinterest from the product provider. The rationale for throwing in the towel is usually that the value of the plan is far less than the money invested and therefore “I don’t want to throw any more good money after bad.” Unfortunately this reflects a lack of understanding as to how the plans work. The fact is they usually offer a ‘bonus incentive’ during the first 18 months to two years. This results in positive valuations initially and encourages investors to maintain contributions while the company recoups the bulk of its marketing costs. There then follows a period of higher charging which may depress valuations for a few years unless there are strong compensating returns in the selected funds. This period can last a few years and is when many investors will lose heart and drop out. The plans really come into their own in the later years when the impact of charges becomes much lower.

There must be thousands of such ‘paid-up orphan plans’ in existence throughout the offshore world. The life companies are not bothered as they still collect fees from the plans or take a whopping surrender charge should anyone cash in. Some investors are persuaded to take out new and ‘better’ plans but that is a big mistake as they will follow the same process. The best value for continued saving would be to review the fund composition of the ‘dead’ plan and revive it (if permitted) with new contributions. All things being equal, the performance would be better than before as the bulk of the charges have already been paid.

Conclusion

Good timing can sometimes bring good results but it is usually more by luck than good judgement. Where long term investing is concerned, time is far more important than timing. If you are not convinced then feel free to take up Warren Buffet on his next challenge, but be prepared to pay out a million dollars to a charity of his choice!

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