

# The Colorado Springs BUSINESS JOURNAL

www.csbj.com

WE MEAN BUSINESS

June 05, 2009

DARE TO BE DULL

## Active investing strategies I use

I recently taught an investments class to some talented students at Colorado College. I was a bit concerned that I might go overboard in suggesting passive investing but, surprisingly, the students pointed out just the opposite.

Here are the four ways they claim I'm an active investor.

■ **Rebalancing** — Passive investing implies “buy and hold.” While I happen to think that buy and hold is far superior to following the herd, I'm a believer in being a true contrarian. That means rebalancing by setting a target equity allocation and sticking to it. It also means you have to sell stock when the market goes up and buy when it's down.

That's why when the market was crashing during March, and a local radio guru was on the air talking about the next Great Depression and getting his mother out of the market, I was writing about buying stocks. In fact, during the “lost decade” ending in 2008, a 60 percent equity and 40 percent fixed-income portfolio earned 36 percent, while the stock market tanked. Rebalancing meant selling stocks during 2000 and 2007, and buying after 2002 and 2008.

Simple, yes, but rebalancing is far from easy. Buying in March was like running with the bulls in Spain and being a slow runner, and then asking for more.

■ **Better than bonds** — I've virtually given up indexing when it comes to bonds. The market inefficiency our federal government has created with FDIC and NUCA (credit unions) allows us small guys to invest \$250,000 per account holder through 2013. That's a sweet advantage we have over the billion dollar institutions that need risk free money, since they could only invest in a one year Treasury Bill earning 0.49 percent,



R O T H

while you and I can get 3.03 percent at Melrose Credit Union. That translates to an extra 2.54 percent annually.

For those who might be thinking these rates are low, I'm going to argue that they are actually quite high. Last year we could earn 4.5 percent which, after taxes, left about a 3 percent gain. With inflation at 3.5 percent, we came out behind in real terms. This year, our 3.03 percent comes out to be about 2.02 percent, which, after taxes and with no inflation, leaves us

with a real 2.02 percent return. The best single place to find the best rates is [www.BankDeals.Blogspot.com](http://www.BankDeals.Blogspot.com). [Bankrate.com](http://Bankrate.com) only has those institutions that pay to be listed. Rule of thumb — the more the bank pays for marketing, the less it can pay you.

■ **Getting real with TIPS** — TIPS are Treasury Inflation Protected Securities that are issued by the federal government and pay a fixed amount plus inflation, as defined by the Consumers' Price Index. They were smokin' hot early last summer when gas was \$4 per gallon and the gurus were predicting an increase to \$10 by the end of 2008. The demand for TIPS drove the real yield down to less than 0.50 percent annually.

By October, guru talk turned to predicting deflation. Investors left TIPS, driving their real yields up to more than 3.5 percent, because people expected the amounts paid by these instruments to decline significantly. They have now moderated, and the yields are somewhere just below 2 percent annually.

I might be guilty of committing the ultimate investing sin by thinking I'm smarter than Mr. Market on this one, but I believe investors tend to think in nominal terms rather than in real, inflation adjusted returns.

Much like CDs, I'd rather get a 2 percent total return with no inflation than a 12 percent return with 10 percent inflation. That's because the government taxes us in nominal dollars so, if we earn 12 percent, we are likely to underperform the 10 percent inflation after paying those taxes.

Buying TIPS when the real yields are high (and prices are low) and selling some when real yields plummet (and prices are high) meets every definition of active investing via market timing.

■ **My gambling portfolio** — I've previously “shared” that daring to be dull in my investing doesn't immunize me from the occasional bout of gambling fever and having my own gambling portfolio. A recent Citigroup purchase clearly demonstrates I am capable of some risky business. It's not that I'm proud of my gambling habit, but it is satisfying to that thrill-seeking part of my brain that wants to see my money double or triple in just a few weeks. You know, the delusional part.

So these are the strategies that have defined me as an active investor by my students. I'm OK with that.

Investing isn't a religion, after all. Investors don't need to blindly pledge an active or passive oath.

Some of these strategies might work for you. Just be sure to implement the first three with focus and discipline, and the fourth one only with fun money.

*Allan Roth, a CPA and Certified Financial Planner, is the founder of Wealth Logic LLC, an hourly based financial planning and licensed investment advisory firm. He also is the author of “How a Second Grader Beats Wall Street.” He can be reached at 955-1001 or at [ar@DareToBeDull.com](mailto:ar@DareToBeDull.com).*