

Portfolio Management Disciplines, Rules, and Procedures

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Portfolio management disciplines, rules, and procedures that will govern the dynamics of change; *the ongoing investment decision making, action taking investment selection and portfolio management processes.*

Investment Portfolio Design, Management, and Performance Disciplines, Rules, and Procedures

Whatever the endeavor, discipline, rules, and procedures can only improve performance.

General (all investors, all portfolios, all of the time)

- **Investment Sectors**—Match investment philosophy and style and ‘what is working’ in the financial markets in general (such as categorized by broad investment classes; bonds, equities, mutual funds, money managers, and user defined or by different economic or business investment sectors) with an investor’s investment profile; risk tolerances, income/capital growth objectives, and investment time horizon.
- **Investment Categories**—As a subheading to Investment Sectors, match investment philosophy and style and what is working’ in specific types of bonds, equities, mutual funds, money managers, and user defined investments and/or in specific economic/business sectors with an investor’s investment profile.
- **Investment Quality**—Match to investor's investment risk profile.
- **Investment Database**—Potential and recommended investments.
- **Asset Allocation Matrixes**—A central investment theme and variations on that investment theme to generate different asset allocations for different types of investors.
- **Asset Allocation**—Match investor investment objectives with the appropriate types and numbers of weighted investment sectors and weighted underlying investments by investment categories.
- **Investment Diversification**—Match investor investing comfort zones and time horizons with the appropriate types, numbers, and weightings of investment sectors and underlying investments by investment categories.
- **Model Portfolios**—Suitable, hopefully timely, investment sectors and investments by investment categories for different investment strategies.
- **Cash Investment Portfolios**—Create unique investment portfolios that match different investors with the correct investments.
- **Blended Investment Portfolios**—Blend an investor's existing investments with a model portfolio to the extent and when needed, desired, or appropriate to bring new investors under one investment umbrella.
 - Update existing client's portfolios with current recommended investments as opposed to having too many different investment portfolios and too many different investments in different investment portfolios that were intended for the same or now outdated objective.
- **Rebalance Portfolios**—Reset investment portfolios to original investment sector and investment weightings to maintain the initial structural integrity of investment portfolios.

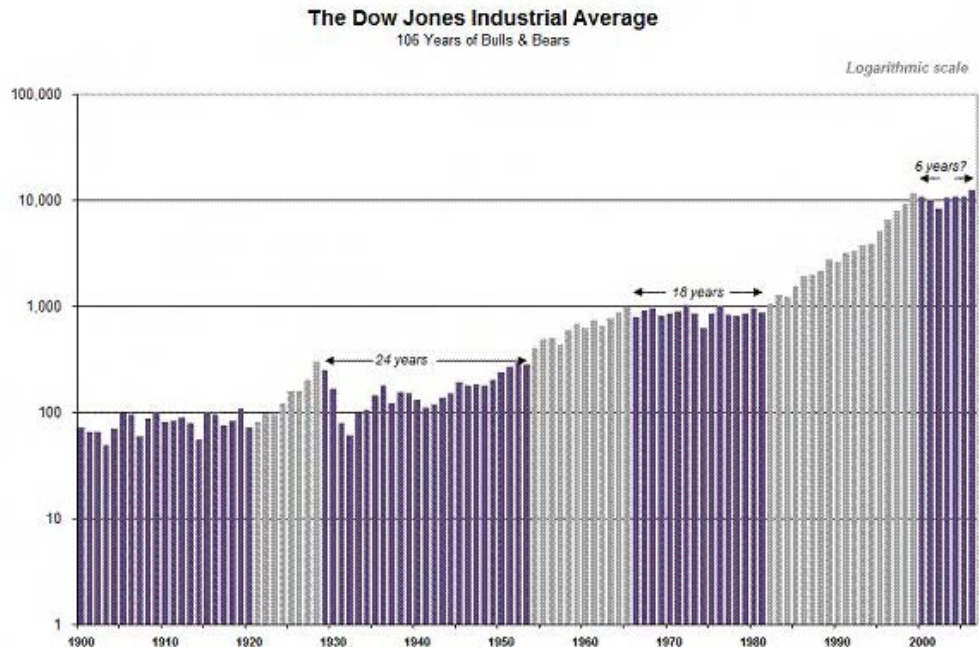
- For example, Rebalance Portfolios—two types, *'Basic'* and *'Price/Position'*— are powerful investing performance tools:
 - Basic portfolio rebalancing maintains the original match between investors' investment profiles (risk and income/capital growth objectives) and asset class/investment sector weightings and underlying investments.
 - Also, as equities do not go straight up or straight down, relative price performance valuations change constantly.



- Price/Position Rebalancing—resetting investments to their original/previous weightings—helps take advantage of short-term relative price performance discrepancies by distributing/selling portions of investments that are outperforming for the moment and accumulating/buying more of investments that are underperforming for the moment.
 - In effect, Price/Position rebalancing is the continuous process of disciplined *'buying low and selling high'* while accumulating investments that are intended to be held for the long term at the best/lowest possible price.
 - Clearly, a change in fundamentals or a price alert(s) set off by an unacceptable variance between current price and cost basis could result in a position(s) being closed.
- If you like, increase the weighting of an equity that is performing exceptionally well, that is *'going straight up'* and offset the increased weighting by reducing the weightings of other same asset class or same investment sector

investments before rebalancing to reduce its impact on or eliminate it from the rebalancing process.

- Many advise annual rebalancing.
 - Need and/or benefit rather than time are better ways to determine when portfolio rebalancing should be done.
 - Basic: When weightings do not match investors' investment profiles.
 - Price/Position: When there are significant relative short-term investment price variances.
- **Reallocate Portfolios**—Set investment portfolios to new selections, combinations, and weightings of investment sectors and investments to keep investment portfolios competitive as market conditions change.
 - Redistribute current investment capital to modified and or new numbers, selections, combinations, and weightings, of investment sectors and investments for individual, selected, or global investment portfolios.



- Holding asset classes, investment sectors, investment categories, and investments after a cyclical trend change has occurred has not been profitable for investors in the past.

Though trends change within asset classes, investment sectors, investment categories, and investments a summary review of broad DJIA cyclical trend changes illustrate the cost of 'buy, hold, and forget.'

Assuming the 25-year portfolio-building time-frame, an investor aged 50 during the stock market boom that ended with the crash of 1929 waited until 1954 just to break even. In real terms, using the Consumer Price Index (CPI) to measure inflation, that investor did not break even until 1958, at 80 years of age.

During the immediately preceding bear market cycle in equities that started in 1968, the Dow exhibited significant volatility but nevertheless ended at 985 in 1982; the same level it attained in 1968. Because this was a high-inflation period, it would have taken until 1995 to break even if the Dow's performance was CPI-adjusted.

Similar cycles can be seen in other asset classes and markets. After a 20-year bull market, the Japanese NIKKEI Index peaked at 38,900 in 1989. Seventeen years later, it is still 56% below that high.

- **Trading Portfolios**—Suitable, hopefully timely equities for different trading strategies.
 - Ruthless cutting of losses.
 - Doing so protects capital and helps force diligent care and patience in timing a Buy
 - A careless or impatient Buy, just *'to be in the market'* may force a preventable Sell if trade goes against you.
- **Transaction Management**—Accumulate/Buy, Distribute/Sell, Dollar-Cost Average, Scale.
- **Price Management**—Set investment price and investment sector alerts to build and to protect profit.
 - Price Alerts
 - Price and value are seldom aligned, but price will reflect value at some point in time; however, no one knows when, for how long, and by how much.
 - Therefore, it is imperative, **absolutely no exceptions** that investment price alerts be set to build and to protect profit.
 - **The most important decision one makes** after the decision to 'Buy' (including after accumulation and after dollar-cost averaging and the average investment cost is known) is to set the price at which one will 'Sell' if the investment goes down.
 - A loss of 50%, realized or not, requires a gain of 100% just to break even; a daunting task and an unnecessary, undisciplined, and unpardonable investment performance error.
 - The reasons for a stock's decline will only become apparent well after its decline.

- Take advantage of the greatest perks of the financial markets; liquidity, price alerts, and stop orders.
 - When a price alert is hit (5%, 10%, 15%, all manageable), let the market decide for you what to do and do what the market is telling you to do.
 - Sell at the market.
 - Stop-sell orders, no limits, and never, *'I'll place the order when the sell price is reached.'*
 - Stops remove emotion and guarantee action.
 - For investments that are appreciating, after a position has been established and the average cost is known, it is equally important to set trailing (below the current price) stop-sell orders to close a portion of or all of a position should the appreciated price begin to fall.
 - As an investment's price appreciates, the % variance between the current price and the stop-loss price may be increased to allow for normal price oscillations with the hope of holding an investment for the long term.
- Investment Sector Alerts
 - Investment sector management; set investment sector weighting alerts to maintain initial asset allocation.
 - Rebalance when required.
- **Replace Investments**—Take advantage of change rather than be the victim of change.
 - Deteriorating fundamentals with improving fundamentals, overvalued with undervalued, apparently poorly timed with seemingly better timed, underperforming with outperforming, weak with the strong.

Specific (personal)

- The Investment Past—Other than in passing, other than a reference point is irrelevant.
- Protect Capital—Regardless of the market conditions, always be in the investment present, on the investment defensive, and never excuse present portfolio cash value with future value hopes, explanations, and expectations.
- Primary Investments—Cash, bonds, equities, and real estate - Packaged products are never better than the investment integrity of the underlying investments.
- Interest Income & Dividends—All portfolios.
- Trading—Never, unless the client knows at least as much as I do.

- Alternative Asset Class Investments—Hedge Funds, Private Equity, and Limited Partnerships often have lock-up provisions and other limitations on liquidity, difficult to value/price.
 - No investment is so good that it is worth losing liquidity.
- Liquidity—Must be a daily market.
 - Never sacrifice for apparent investment opportunity.
- Commodities—At no time to speculate, OK to hedge, and never unless the client knows more than I do.
- Money Managers & Mutual Funds—Second choice.
 - Why have them do what I am supposed to be able to do.
- Bond Mutual Funds—Never.
 - There is always a better, smarter way.
- Investment Firms' IPOs—In most cases, if you can get it, you do not want it.
- Modern Portfolio Theory—Investment diversion amusement.
 - While confusing, comparing, and applying the concepts of order, causes, connections, effects, and rules (*Newton's three Laws of Motion, for example*) as found in the sciences and systems of the universe and as explained with mathematics to the chaos, incidences, coincidences, chances, correlations (none of which are causal; but, assumed in order to make the math of mpt work) and no rules as found in the artistry and complexity of investing and managing capital in the financial markets in an effort to predict investment outcomes, Modern Portfolio Theory, the Olestra™ of investing, using yesterday's news as an investment crutch, is just another way to record and illustrate investment history without valid analytical, interpretive, deductive, predictive, or directional investment value because it assumes and suggests, incorrectly, that the financial markets' cycles of the past and the valuations of underlying investments in the past, because they are somehow mysteriously connected as part of an orderly, sequential financial system, will repeat themselves similarly or exactly in the future as they did in the past in much the same order and with the same frequencies, durations, levels, relative valuations, and volatilities; *absurd, as anyone who has spent a nanosecond in the financial markets would, should know.*
- Monte Carlo Analysis—The probability of achieving an investment objective will be determined by the investing skills of the investment advisor or investor; not by past investment performance and market cycles.
- Efficient Frontier Analysis—Nothing more than a case, a very bad one, for justifying changing investments.
 - 'Updated Efficient Frontier Analysis historical investment performance data indicates that we might do better if you were to move your current investments that were selected based on an earlier Efficient Frontier Analysis and that did well in the distant past

prior to your investing in them, but have not done well since you owned them, into the latest investments that have done the best in the most recent past based on my current Efficient Frontier Analysis.'

- Optimizers—Investment hindsight is neither investment insight nor investment foresight.
- Companies—Quality, products, management, competitive, balance sheet, accounting, earnings, growth, research and development, entry, and use of debt.
- Earnings —Realistic, maintainable, accurate, honest, and increasing.
- **Margin***—Never leverage capital to buy more investments unless borrowed capital will be used only as a short-term source for cash needs outside the investment portfolio and where there is a clear and specific source of funds to eliminate margin in the short term.
- **Sell Short*** —If Warren Buffett can survive without shorting stocks, so can I; odds are bad going against the upward bias of the market, loss potential infinite.
- **Options***—Never buy, never write covered, and never, ever naked. Well, OK, maybe "buy" every once-in-a-while!