March 13, 2020

Re: Market Meltdown

Dear client,

There was a good market rally today in which I suspect the losses from yesterday were largely made up. This is an encouraging sign because the market is trying to find an equilibrium. Yesterday, the market was in no mood to discriminate and sold off stocks, gold, and bonds to meet margin calls. There may be another leg down and more up-down days. There were several major factors driving the swings of the stock market this past week.

One culprit is programmed computer trading. When the computers see that a stock price level has been breached, it automatically sells. When in reverse, and the market rises, programmed computers buy and accentuate any upside. This week, the program trades had a lot to do with the steep selloffs.

Over the past 10 years, many unsophisticated investors have put their money in index and exchange traded funds without fully understanding them. It is usually the unsophisticated small investor who sells when he or she shouldn't and buys when stocks are overvalued. With a push of a button, stocks in the index are immediately sold and that also accentuates any market slide or melt up. I have talked about the dangers of index investing many times in the past and why we usually don't recommend it, except for small savers. A large part of the extreme downdrafts is because of index and exchange traded accounts in which a basket of stocks can be sold with a click of a button.

Other investors sold in a panic because they got margin calls. A margin call is where an investor leverages his or her account with borrowed money. Using margin allows an investor to compound his investments at a faster rate when the market is going up and gets wiped out if the market goes down enough. This happened last week when heavily margined borrowers were wiped out as brokerage firms liquidated holdings to pay off the loans.

Benjamin Graham avoided the stock market crash of 1929, but he got wiped out in 1934. Learning from his experiences, Graham wrote the book "Security Analysis." The book is considered the bible of value investing and its most famous pupil, Warren Buffet, adheres to Graham's investment philosophy. We also follow Graham's investing philosophy and have been doing so ever since 1974. We have kept the stock allocation to a manageable level in order to control risk.

We anticipate holding our current stock, gold, and bond positions unless dire circumstances warrant otherwise. When the rate of NEW infections of the coronavirus starts to level off and decline in the United States, then we anticipate buying bargain basement quality stocks for a once-in-a generation opportunity. We may miss that chance if the market goes back up as fast as it did go down, but I am wiling to take that chance. However, I think we will have our opportunities to buy quality stocks in the next few months.

We are postponing our Coffee with Dr. Steve segment today because Katie is off, and we will be back next week. However, if you need to talk to me this weekend, please don't hesitate to call me on my cell phone: 310-270-5256.

All the best,

Steven Yamshon
Managing Principal

Disclosure:

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