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# Fret Not: The (Bond) Market Will Recover

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**April, 2009-** If we could have put a price on the value of the entire planet just eighteen months ago, we are now worth only one half of that value. Think about that. Clearly 50% of the world's wealth has simply vanished. But the population is the same. The same 6.4 billion people have to eat every day, and they still have to buy things, though maybe not as much. People are losing their jobs all around us; but not *everybody* can lose their job.

Companies are cutting back in many areas, the most significant being labor. Though this is painful now for all involved, it also makes the companies more profitable in the long run. The most understated variable in this whole scenario is oil prices. It can never be truly known exactly how much of a factor oil prices played in tipping the economy, but it was surely significant. The Fed under both Greenspan and Bernanke seems to have misunderstood the effect oil prices has on the market as, of course did the empty talking heads on TV.

Oil prices, as it turns out, have an effect similar to interest rates. When interest rates rise, more money is needed to pay for the use of money, and thus money is diverted away from other uses. Likewise, when oil prices rise, companies are forced to divert money—sometimes profits—to pay for higher energy costs. The net effect on the economy is really the same: brakes on growth. So with higher interest rates and sky-high oil prices, the brakes on the economy were doubly engaged, leading to a sharp reversal.

Now the situation is quite the opposite, with low interest rates and low oil prices. What can this mean for the future? It means surprise earnings. We were very nervous two years ago because we knew that the stock market was overvalued. Now that we've seen the Dow drop below the 7000 mark, the obvious question at hand is: "how low can we go?" Well, here's what we believe to be true:

1. The stock market won't go to zero. If it does, money won't matter; only guns.
2. The planet's population has not decreased, and base demand will continue.
3. Though the bond market is depressed, interest payments continue (for most).
4. The bond market will recover when banks restock their holdings of bonds.
5. Banks will restock their bond holdings when losses cease and profit returns.
6. Banks can't be profitable when people are walking out on their mortgages.
7. Obama knows this is a problem, but it has not yet been adequately addressed.
8. Congress is completely clueless (per usual) and party politics and self-promotion rule the day on Capitol Hill. This is our ultimate root problem.

9. Eventually, we are hopeful that Obama will push provisions through Congress to force a readjustment of mortgage terms for millions of Americans.
10. With or without the foregoing, the stock market will eventually recover, and those companies left standing will have an ever-larger market share.
11. Companies in the future will have less overhead, thus more earnings, and thus be in more demand, driving up their stock price.
12. The trillions held in treasuries will flow back out into the stock market, and treasuries and the dollar will decline. This decline will become sharper as treasuries are unloaded by the billions.
13. Stock markets worldwide will once again rally, and inflation will be the next problem. Oh, and a $15 trillion dollar national debt.

Right now you're thinking that I'm crazy to think that this economy will ever turn around. But be honest with yourself; if two years ago I had told you that we would be in this shape today, you would've thought I was crazy. Admittedly, it's worse than even I expected, but at least we will all remember this when I try to force those boring bonds on you again during the next bull market. And not just boring bonds, but the most boring of all the boring—treasuries.

So here's our game plan—it hasn't changed, and it will not change no matter how low the stock market goes. First, we've simply got to ride this out. The reason that our portfolios are broken down into stocks and bonds and cash is so that our immediate needs can be met with the cash if the longer-term money (stocks) happen to be depressed. Remember, we want to sell stocks when they're up—not when they're going for peanuts.

Secondly, remember that most of our money is not in the stock market but the bond market. These bonds continue to pay income and the average yield, both for munis and corporates, is around 4½%. Even though the price of the bonds has dropped on paper, they're still paying their interest, and eventually will recover. Experienced bond holders know that a bond matures at par (the price at which it was issued), and as long as you hold the bond until maturity, any losses (or gains) created by market forces like interest rates and credit worthiness (as now) are essentially negated.

We expect that small and mid cap value stocks will be the leaders out of this quagmire once bonds have fully recovered and have a sustainable secondary market. In our opinion, this won't happen until the mortgage issues are resolved.

It's times like these when we really earn our fee, because we have to convince you to do the opposite of what you feel you want to do and what everyone on TV is telling you to do. I completely understand the thinking of "let's just go to cash and wait for things to recover." But trust me on this: It never works. By the time you've had a chance to make sense of the economy; you've missed your opportunity and end up buying in too late, and at a high. This is what we expect the amateur Joe Public investor to do, and we can profit from his ignorance—*IF* we are smart, steadfast and self-heeding.

## About J. Kevin Meaders

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Kevin Meaders graduated from Oglethorpe University in Atlanta with a double B.A. in Philosophy and Political Science, and then obtained a law degree from Georgia State University College of Law, focusing on estate planning and trust law. He has earned the designations of Certified Financial Planner (CFP®), Chartered Financial Consultant (ChFC) and Chartered Life Underwriter (CLU). He holds a General Securities Principal and Registered Representative registration and Investment Advisor Representative registration through ING Financial Partners (member SIPC).

## About Magellan Planning Group

www.magellanplanning.com

Magellan Planning Group was established in 2000 to provide a service uniquely tailored to the needs of our affluent Atlanta community. We concentrate on *personalized* retirement planning through tri-disciplinary coordination:

- Financial planning with our Certified Financial Planner™ to prepare a retirement plan that takes into account your needs and expectations. We are a fee only asset management firm with a $500,000 minimum relationship.

- Estate planning with our in-house Attorney-at-Law to determine and prepare the documents needed to minimize family liability and maximize privacy. (www.magellanlegal.com)

- Tax planning through a relationship with our in-house CPA to manage tax obligations throughout the year and prepare a tax return that takes into account current tax laws. (www.magellantax.com)

Our relationship doesn't begin and end with the preparation of a plan and the appropriate documents. We establish close personal relationships with our clients and their families and maintain those relationships through regular 'check-ups', market commentaries and educational Lunch & Learns.

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