

**FIM GROUP INVITES YOU TO**
**InvestNews – Question & Answer**

**Q: If market volatility creates wealth transfer, how does that wealth transfer to our personal accounts instead of those accounts fluctuating correspondingly to the ups and downs of the market?**

A: The idea of wealth transfer is a concept that stretches over full market cycles, not so much to month-to-month, short-term movements. During periods of extreme volatility, such as the Great Depression of 1929-1933, the crash of 1973-74, the crash of 1987, the bear markets of 2000-2002 and 2007-2009, including the ensuing recoveries that typically last two to five years, wealth frequently transfers from those who (often first get caught up in the bubble speculation near the top and then) give in to panic during downside volatility and sell out, to those who look past the emotion and see the economic reality that is the fabric of society and commerce. During those crashes the prices of many companies fall to levels far below their intrinsic values as investors gripped with fear, or those trying to time the market, just “sell everything” and move to cash. Investors who can look out several years past the panic hold onto or buy investments from those selling them and are generally rewarded in the ensuing upside volatility within a few years.

**Q: Why don't you use hedging positions or options to reduce portfolio volatility?**

A: When people think of hedging, they usually think of futures, options or some form of derivative. Diversification is a “hedging tool” that we use liberally. Hedging using options, derivatives or futures tends to be very expensive. They don't just move in the opposite direction of the underlying asset, and they also contain a continuously eroding “time value.” During periods when the underlying investments are moving in the positive direction, hedges cause a drag on the portfolio. Combined with their eroding time value, the costs of holding them are very high. So it is critical if you are going to employ such tools that you: First, apply them appropriately; second, get the timing right – because they are very expensive if held over the longer term and can cost more than the benefit; and third, accept that hedges will very likely negatively impact long-term performance. Our goal is to maximize long-term performance, so rather than employ costly direct hedges, we use informal hedging techniques, including diversification across companies, industries, geographical regions, currencies, etc.

**Q: Recent data indicate the nascent economic recovery, if you can even call it a recovery at all, which began in 2009, is already stalling. How does this affect how FIM Group invests?**

A: FIM Group has been steadfast in our opinion that the economy is stuck in a very low gear and will remain so for a long time. Whether the economy is growing at 2% or 1%, or not growing or even falling at 1%, is really pretty much the same. Yes, -1/2% is technically a recession and +1/2% is expansion, but in our mind that is splitting hairs. The fact is that regardless of these numbers, people will still eat, consume energy, communicate with each other, need medical care, etc. Businesses of all sizes will continue to invest where they have the greatest opportunity and focus on the areas where they are or can be the most profitable. But the days of high-leverage borrowing and loose spending, both at the personal and business levels, are gone for the foreseeable future. We are patiently investing with these trends in mind, focusing on companies in the industries mentioned, favoring those with low debt, strong balance sheets, good cash flow, who pay significant dividends to shareholders and are priced below what their businesses are worth. Such investments should increase in value over the long term regardless of what the economy or the markets do in the short term.

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**LEARNING LESSONS**

By Jeff Lokken, CFP®, ChFC®

To my Dad the Depression was always yesterday, and I am sure he really wanted me to understand his Managing Manias experience of growing up during those times. But the years passed, I began to realize that his seeming obsession with this time period was an even more important lesson of gratitude and...

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