

Dear Client,

Only eight weeks have passed since our last communique, a mid-quarter letter which we felt was timely because of the extreme volatility of the stock market. The third quarter of 2015 proved to be a real test of investors' fortitude. The Dow Jones Industrial Average, the S&P 500, and the Russell 2000 index all lost ground, with negative returns of 8%, 7% and 11.86% respectively. It was the worst quarterly performance since 2011. Statistically, as seasoned investors well know, September and October are the two worst performing months. A considerable amount of research has shown that the November to May time period vastly outperforms the opposite stretch from May to November. There are many theories as to why this happens, one of the oldest being it was a result of banks pulling money out of the stock market in order to finance the harvest of the crop. For whatever reason, bad stuff seems to fall into the ninth and tenth month of the calendar.

Fortunately, not every autumn swoon in the stock market presages an economic calamity. There is an old adage that the stock market has predicted five of the last two recessions. Very often these seasonal patterns are just a normal ebb and flow of the market. So how do we differentiate this pullback from the beginning of more serious decline, or a bear market?

At GBR Wealth Management, we use a combination of fundamental analysis, researching individual companies, and technical analysis, studying overall trends and investor sentiment. The latter is particularly useful in times of market stress like we are experiencing right now. Mark Twain famously once said "History does not repeat itself, but it rhymes". Many of the sentiment indicators which we follow are showing levels of extreme pessimism on the part of investors. Here is a sample of the headlines we are focusing on:

1. "Irrational Pessimism Takes Hold Of Surveys", 10/02/2015*
2. "Hedge Funds Peel Back Their Stock Exposure", 10/01/2015*
3. "Investors Fled Equity Funds This Quarter", 9/30/15*
4. "Closed-End Bond Funds Suffer Huge Discounts", 9/24/15*
5. "Penny Stock Traders Have Given Up", 09/15/15*
6. "Selling Climaxes Reach Three-Year High, 8/28/15*

Now after reading this you may be thinking, "Get me out, the world is about to end!" But in the upside down real world of making real decisions with real money, this is precisely the kind of capitulation we are looking for. We believe down markets do not stop going down until the last weak-kneed investor has thrown in the towel. Only when, at the margin, stock goes from "weak" hands (those looking for a quick buck) to "strong hands" (long term holders) do markets reverse course. We think there is a ton of evidence that this is the case right now.

Technical Analysis requires a completely unemotional outlook towards the market. It also requires that theory be backed up with historical evidence. Since history never exactly repeats itself, we study analogies of what has happened in the past and compare them to what is going on right now. With statistics, we can quantify how many times in the past the analogy led to a positive outcome at various intervals into the future. We try to look for patterns which “rhyme”.

The details of the analogies are too complex to explore here, but suffice it to say that in a vast majority of the instances, the patterns we are seeing now have resulted in positive outcomes three, six and twelve months after they manifested themselves in the past. Of course, past experiences are no guarantee of future results, which is why we say “most” and not “all”.

Investing is part art, part science. We believe that if we stick to our convictions, don’t waver at every passing crisis or fad, own quality companies and focus on the long term, our odds of success increase dramatically.

The final quarter of the year is when we usually take steps to minimize the inevitable bill to Uncle Sam due next April. We will be harvesting losses and taking other steps to eliminate or defer taxes. If you have a tax-loss carryforward or a gain we are unaware of, please let us know so we can take it into account. Also, please let us know about any year end gifting plans. We look forward to serving you in the future.

Regards,

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