

# Monterey Wealth Report

## April 13, 2009



### The Markets

Does August 12, 1982, mean anything to you?

On that day, the S&P 500 index closed at 102, which was about 9% lower than where it closed 10 years earlier, according to data from Yahoo! Finance. To repeat a popular phrase, it was a “lost decade.” However, 10 years later, on August 12, 1992, it was a completely different story. The S&P 500 index closed that day at 418 for a cumulative gain of more than 300%.

Could we be in a similar situation today?

As of last Thursday, the S&P 500 closed at 857, which is roughly 36% lower than where it stood 10 years earlier. That’s an even worse “lost decade” than the 10-year stretch from August 1972 to August 1982. Over the upcoming 10 years, if the S&P 500 repeats its August 12, 1982, to August 12, 1992, performance, we’d end up with the index at more than 3,400 on April 9, 2019.

Things looked bleak in August 1982 just like they look bleak now. Nonetheless, just when investors had metaphorically thrown in the towel back then, the market proceeded to do what it does best – it fooled just about everybody. It went on an 18-year expansion that was one of the most powerful secular bull markets in history.

While we’re not predicting a 300% gain over the next 10 years, we’re not ruling it out either. Just like few people predicted our “lost decades,” or the 1982–2000 bull market, the next 10 years will likely surprise us, too. Whether that’s a positive or negative surprise, nobody knows. What we do know is that we continue to keep our eyes and minds open to all possibilities and we will do all we can to help you profit from whatever ensues.

Data as of 4/9/09	1-Week	Y-T-D	1-Year	3-Year	5-Year	10-Year
Standard & Poor's 500 (Domestic Stocks)	1.7%	-5.2%	35.7%	12.9%	-5.6%	-4.4%
DJ Wilshire Global ex US (Foreign Stocks)	0.7	-4.1	-46.0	-14.0	-2.0	-0.9
10-year Treasury Note (Yield Only)	2.9	N/A	3.5	5.0	4.2	5.0
Gold (per ounce)	-2.7	1.2	-4.0	13.8	16.6	12.1
DJ/AIG Commodity Index	-0.5	-3.5	-46.4	-12.6	-5.7	3.5
DJ Equity All REIT TR Index	5.0	-17.1	-50.0	-18.6	-2.2	N/A

Notes: S&P 500, DJ Wilshire Global ex US, Gold, DJ/AIG Commodity Index returns exclude reinvested dividends (gold does not pay a dividend) and the three-, five-, and 10-year returns are annualized; the DJ Equity All REIT TR Index does include reinvested dividends and the three-, five-, and 10-year returns are annualized; and the 10-year Treasury Note is simply the yield at the close of the day on each of the historical time periods. Sources: Yahoo! Finance, Barron's, djindexes.com, London Bullion Market Association. Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested into directly. N/A means not available.

Securities and Insurance Products Offered Through LPL Financial. Member FINRA/SIPC.

Not FDIC Insured	No Bank Guarantee	May Lose Value
Not a Deposit	Not Insured by Any Government Agency	

The LPL Financial Registered Representatives associated with this site may only discuss and/or transact securities business with residents of the following states: Georgia, Florida, Virginia, and New Jersey

**A LITTLE KNOWN STOCK MARKET VALUATION MEASURE** called “Tobin’s Q ratio” may be signaling that the stock market is near historic valuation lows. According to Investopedia, the Q ratio results from dividing the market value of a company by the replacement value of its assets. Nobel Prize-winning economist James Tobin developed this analytical tool in 1969 and, although Tobin is now deceased, his former research assistant, John Mihaljevic, continues to update it.

Tobin thought that the market value of a stock should be roughly equal to the replacement cost of its assets. We can also apply this ratio to the stock market as a whole using data from the “Flow of Funds Accounts of the United States Z1,” which is published quarterly by the Federal Reserve.

Over the past 130 years, the Q ratio for the U.S. equity market has fluctuated between 0.29 and 2.90. In general, when the ratio is above 1.0, it indicates the market may be overvaluing company assets while a ratio below 1.0 may suggest shares are undervalued. The ratio peaked at 2.90 in 1999 and, of course, we know what happened to the markets over the next three years. The ratio reached its 0.29 low in 1921, 1932, 1949, and 1982, which, how conveniently, happen to be the same years that mark the beginning of four powerful secular bull markets, according to *Anatomy of the Bear* author Russell Napier.

So where is the Q ratio now? In Mihaljevic’s recently released report, he estimated that the ratio had declined to 0.43 as of March 15, 2009. He commented that the ratio had only been that low on six other occasions since 1900. In plain English, this suggests the stock market was near historic valuation lows as of mid-March, at least as measured by the Q ratio.

That’s helpful to know, but remember, when it comes to investing, no single number can tell you with certainty whether the market is undervalued or overvalued. And, even if you knew it was undervalued or overvalued, the market can stay in those conditions for a very long time and confound the best laid plans. However, by monitoring numbers such as the Q ratio, we may start to get a feel for trends that are developing and it may help us make better investment decisions on your behalf.

### **Weekly Focus – Think About It**

“If you will call your troubles experiences, and remember that every experience develops some latent force within you, you will grow vigorous and happy, however adverse your circumstances may seem to be.”

-- John Heywood

Best regards,

Jay W. Cohen, MPA, CPA, CFP®

Securities and Insurance Products Offered Through LPL Financial. Member FINRA/SIPC.

Not FDIC Insured	No Bank Guarantee	May Lose Value
Not a Deposit	Not Insured by Any Government Agency	

The LPL Financial Registered Representatives associated with this site may only discuss and/or transact securities business with residents of the following states: Georgia, Florida, Virginia, and New Jersey

P.S. Please feel free to forward this commentary to family, friends, or colleagues. If you would like us to add them to the list, please reply to this e-mail with their e-mail address and we will ask for their permission to be added.

Securities offered through LPL Financial, Member FINRA/SIPC.

\* The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general.

\* The Dow Jones Industrial Average is a price-weighted index of 30 actively traded blue-chip stocks.

\* The NASDAQ Composite Index is an unmanaged, market-weighted index of all over-the-counter common stocks traded on the National Association of Securities Dealers Automated Quotation System.

\*Yahoo! Finance is the source for any reference to the performance of an index between two specific periods.

\* Opinions expressed are subject to change without notice and are not intended as investment advice or to predict future performance.

\* Consult your financial professional before making any investment decision.

\* You cannot invest directly in an index.

\* Past performance does not guarantee future results.

Securities and Insurance Products Offered Through LPL Financial. Member FINRA/SIPC.

Not FDIC Insured	No Bank Guarantee	May Lose Value
Not a Deposit	Not Insured by Any Government Agency	

The LPL Financial Registered Representatives associated with this site may only discuss and/or transact securities business with residents of the following states: Georgia, Florida, Virginia, and New Jersey