

# Client Bulletin

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## PANIC, PRICES, AND PERSPECTIVE

A panic selloff has occurred in U.S. and global stock markets. To the extent that money was invested long in stocks, there was essentially no place to hide. The S&P500 crashed more than 28% in the first ten days of October. That was a continuation of a 9.2% crash in September. This was a historic, classic panic selloff. A good thumb rule is that it is usually unwise to sell into a panic. If anything, panic conditions often present a buying opportunity; however, they are not a good reason to sell and lock in losses at or near a bottom. Depending on the extent caught in it, it's usually prudent to ride out a panic.



There are exceptions to the above thumb rule. For example, in taxable accounts, a panic selloff may present the opportunity to sell stocks to realize tax losses, and simultaneously buy other equally-, or higher-quality securities that also have been driven down in price. In other words, sell where you can appropriately incur tax losses. At the same time, buy high quality, good-valuation stocks that have sunk in price along with everything else.

Another exception relates to a person's level of investment being in line with their ability to sleep at night. If sleep is lost because of an investment portfolio, that's a serious issue that needs to be resolved. Along these lines, it is worth remembering that investment money is a longer-term proposition, not money intended to pay monthly or short-term bills. Short-term liquidity requirements require liquid assets.

Given that equity prices have fallen to Bear Market levels, down more than 20%, let's put current conditions in some perspective. (Note: After the October 13<sup>th</sup> historic upspike in prices, the S&P500 and other major indices still remained down more than 35% from their October 2007 highs.)

The panic sell-off in September and October created stock price valuations that are the best they have been in many years. That is good news. My guess is that these low stock valuations have already figured in most of the bad news including the collapse of the global housing bubble, the credit crisis, and the current global recession. That's a guess not a guarantee. A recession is not even for sure until it is over and declared a recession by the National Bureau of Economic Research. In any case, stock valuations at these levels suggest that selective, careful buying is a more prudent action than blanket selling.

Investor expectations are running above 60% that the stock market won't be a good investment over the next six months. This bearish sentiment is near historically high levels and it is a contraindicator. Therefore, odds are, no guarantee, but odds are, that those bearish sentiments will be wrong. As I said in the last Bulletin, the stock market looks ahead and is usually higher at the end of a recession than it is during the recession. *(continued on next page)*

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Our primary supply-and-demand risk indicators have reversed up from extremely low levels to put us back into an offensive, wealth accumulation position. Unexpected fundamental events could rise up and throw a new curveball at us. However, we're optimistic about the results of gradually and carefully adjusting and increasing the equity exposure in our portfolios.

What we would like to see happen in the markets now is an orderly base-building period. That means that stock prices would periodically rise and fall (breathe in and breathe out) between levels of resistance (ceiling) and levels of support (floor). The next step, assuming a positive macro-economic outlook, would be for prices to eventually break out to the upside as the stock market and individual securities regain strength. Then a progressive series of higher tops and bottoms would be desired as the markets ratchet up. This would be the ideal situation. On the other hand, a V-shaped recovery pattern is not desired because it historically is like a flash in the pan and would not likely be a prelude to sustainable price growth.

To sum up, there is never any guarantee of the future but we have seen significant policy actions taken and, with the crash, now see good stock valuations. We also see signs of demand regaining traction in the markets. We'll continue our daily due diligence and adjust with conditions as we see how it plays out from here. With some of the best research tools available to continue to protect and grow our client portfolios we are very optimistic going forward. And, we remain committed and diligent in our continual goal and efforts to be at the top of our industry in terms of performance, advice, and service.