THE NEWS TRIBUNE

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Views differ on direction of markets through 2010

When managing your investments, you've probably experienced times when you reviewed information, made a decision and been uncertain if it was the right decision at the right time.

Today, even veteran money managers who have been through bear markets, bull markets and everything in between can't agree on whether the stock or bond markets represent opportunity or pitfall.

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For example, Jeremy Grantham is a partner at asset management firm GMO. He is known for his pessimistic views and the accuracy of gloomy predictions during the past decade. Grantham thinks the fair value of the S&P 500 Index, measuring mostly large U.S. companies, is 850. It would take roughly a 20 percent drop from where we ended January to fall to 850.

But Bill Miller, a mutual fund manager for Legg Mason who became famous for outperforming the S&P 500 for 15 consecutive years, ending in 2006, sees plenty of room for growth in 2010. In his January outlook, he expressed shock that, despite growing company earnings and a growing economy, U.S. stocks are still at levels below where they were after Lehman Brothers failed in September 2008 and the financial world was at the edge of destruction. He wouldn't be startled by a 20 percent rise in U.S. stocks from where we are.

The only certainty is that, regardless of present or future conditions, you have to make decisions based on informed, but incomplete, information.

Since you can't count on having the right timing or being consistently lucky, why should you place faith in something that is imperfect?

Because through peaks and valleys, the compound growth of an intelligently invested dollar is the best way to fund a multi-decade retirement.

You can't keep up with inflation and build a retirement fund with cash or home equity.

Some people have terrific entrepreneurial opportunities and skills that offer a path to financial security. But it is a path at least as risky as the stock market due to the concentrated risk.

'LOST DECADE?' NOT FOR ALL

You may perceive that there is too much risk in investing because headlines have told you about the "lost decade" of the 2000s. It could only truly be lost, however, if you stopped contributing to retirement accounts and moved your money to cash at market bottoms.

Sure, the S&P 500 turned in an average annual return of -1.0 percent in the 2000s. But it was the only primary global market segment that was negative over the full decade.

A balanced portfolio that I track consisting of 60 percent stocks (both U.S. and foreign) and 40 percent bonds had an average annual return of 4.73 percent in the 2000s. That's not great but it's far from a lost decade.

Now stretch the view out to a full working lifetime. Imagine a 25-year-old in 1973 beginning to invest for retirement.

A significant bear market in 1973-74 may have been discouraging at the start and declines for much of the 2000s would have challenged retirement expectations.

But that 25-year-old in 1973 would be 62 entering 2010 and able to retire because of the 10.42 percent average annual return that carried the 60/40 portfolio to an acceptable level.

DIVERSIFY AS A HEDGE

Along with having global balance of stocks and bonds, if you include "specialty diversifiers" in your portfolio, the likelihood of a lost decade is even more remote.

Consider the average annual returns of these diversifiers in the 2000s.

The FTSE NAREIT Real Estate Investment Trust Index averaged 10.2 percent for the decade. The MSCI Emerging Markets Index returned 10.1 percent per year.

Treasury inflation-protected securities added 7.7 percent annually. The Dow Jones UBS Commodity Index averaged a 7.1 percent return. By including 3 to 5 percent exposure to each of these markets in a balanced investment strategy, you might not only increase returns but reduce risk at the same time.

It's this broad diversification that allows you to be generally right rather than precisely wrong by trying to pick the portion of the market that will be most favored in the near term.

Gary Brooks is the president of Brooks, Hughes & Jones, a Tacoma registered investment adviser. Read more investing insights from Brooks and his partners at their blog, www.themoneyarchitects.com.