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October 2008 stock returns will go down in history as one of the most difficult months for market returns in the last century. The table below illustrates what you have been hearing in the media:

The Five Worst Stock Market Months (Returns including dividends)

Canadian Equity 1956-2008 (S&P/TSX Composite Index)		U.S. Equity 1926-2008 (S&P500 Index)		International Equity 1970-2008 (MSCI EAFE Index)	
October 1987	-22.52 %	September 1931	-29.73 %	October 2008	-23.50%
August 1998	-20.11 %	March 1938	-24.87 %	October 1987	-18.38 %
October 2008	-18.75 %	May 1940	-22.89 %	September 1990	-15.57 %
March 1980	-17.64 %	May 1932	-21.96 %	August 1998	-13.48 %
September 2008	-14.45 %	October 2008	-18.50 %	September 2008	-12.10 %

Sources: Ibbotson Associates, Bloomberg

As this table indicates, October 2008 stock returns were significantly negative, but not without precedent. It is important to recall that the PWL broadly diversified portfolios include a further 10-12 asset classes.

Recently, the turmoil in the interbank lending market has started to settle down and banks have started lending to each other again. This improvement is largely due to governments guaranteeing these loans, over and above their generous injections of capital to shore up many major international banks. In spite of this, market nervousness and volatility persist due to major declines in the currencies of several emerging countries. This is to be expected.

What does this mean for you?

More than ever, these events highlight two schools of thought about the investing in the stock market. The first is focused on the “zigzags” of the market, purporting to generate profits by buying and selling at “the right time” i.e. timing the market. The second school of thought, to which we belong, believes that short-term market movements are unpredictable and only serve to distract investors. This investment philosophy focuses on the risk premium where the riskier the asset class, the higher the expected return.

Consider the following facts, reprinted from one of our recent publications, which demonstrate the risk/reward equation or the “risk premium” of the riskier asset classes:

U.S. Asset Class Returns 1927-2008

Inflation	3.16%
Treasury Bills	3.73%
Long-term Government Bonds	5.39%
Long-term Corporate Bonds	5.73%
Large Cap Equity	10.12%
Value Equity	11.53%
Small Cap Equity	12.29%

Source: Ibbotson Associates

While this data is based on U.S. historical returns, the same relative risk/reward equation plays out in Canada and other countries.

There are two key points that we conclude from this:

1. As difficult as it may be, the only way to obtain decent returns is to invest in the economy via the stock market and hold stocks for the long term. Successful investors accept the risk of the equity asset classes as the key to generating superior returns.
2. Timing the market – i.e. trying to move in and out of the market at “the right time” - will inevitably lead investors to sell low (after the market has tanked) and buy high (after the market has soared).

We firmly believe that the successful investors of the years to come will be those who ignore the sensational media reports and who adopt a rational, disciplined approach to investing in the markets.

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