GSI Market View

4th Quarter 1998

FUDD. This term, developed by Goldman Sacks's Abbey Joseph Cohen, cannot be found anywhere in Mr. Webster's publications. Yet it is what seems to one of the key drivers to the constant gyration found in the market today. OK, so it is an acronym. It is however, pertinent. *Specifically translated, this means **F**ear, **U**ncertainty, **D**oubt and **D**espair (FUDD).* Turbulent global market and political conditions exacerbated by the media and a number of highly leveraged hedge funds, have left many experiencing a high degree of FUDD. Even Federal Reserve Chairman, Alan Greenspan, said recently, "if you read the newspapers in the morning, one gets the impression that the economy has collapsed, and we might as well go home and go fishing." Are things truly this bad or do we all suffer from a mild case of FUDD? This newsletter looks to answer this question and seeks a remedy in the case of contracting FUDD.

Are *YOU* currently afflicted with FUDD? The answer to this may be found by asking a few key questions. Do you believe that we are on the brink of a global market recession or collapse, one that may leave no room for developing countries to expand in terms of basic infrastructure? Do you find yourself truly concerned about how your investment portfolio did last week? Last quarter? The last six months? Have you recently changed your asset allocation in dramatic fashion (the split between stocks and bonds)? If you have, will you change it again? When might you do it and what will be your signal to do so*? If you have answered yes to any of these questions, it is safe to assume that you have FUDD.*

In all seriousness, Glenn and I know that there is turbulence in the market today. We also understand that many investors are, at least, concerned about what is happening to their respective investment portfolios. We are constantly being asked questions like, have we witnessed the full impact of the Asian Flu? How will Russia's instability affect the US and the rest of the world? Are corporate earnings in real jeopardy, both for the remainder of calendar 98 and 1999? Are there true deflationary signs to be found in the global economy? If so, what are the ramifications?

Contrary to the expectations of some, we truly don't have all of the answers. We can suggest however, caution in one's response to the tremendous overreaction witnessed in the market today. As of June 30, 1998, the S&P 500 was up an astounding 17.25% for the year. Two months later the average sat at -.38%. Was the market overvalued through the first part of the year? Many would have argued yes. Is the market now undervalued? We would argue that it might be. *Unemployment remains low, roughly 4.6%. Economic growth remains unspectacular, but solid, at roughly 2%. Interest rates and inflation remain in check, with no hints of acceleration on the horizon. These are not the signs of an economy that is nearing collapse*, yet, in the words of a Business Week contributor, "investors have been fleeing to the mattress-like safety of Treasury Bonds as if anticipating a 1930s-style depression." He goes on to say that if we are not careful "they (the pundits) might turn a mere slowdown (economic) into a recession."

Back to FUDD. As investors, we are constantly being conditioned by the endless streams of media, either electronic or written. *We are conditioned to believe that the sky is falling one day and that we are experiencing investment utopia the next. What we have learned over time is two-fold. First, neither is probably true. Second, if one sticks to the fundamentals in terms of evaluating his/her core holdings, viewing the media barrage as noise, the long-term outlook is positive.*

A famous investor by the name of Peter Lynch once said that if a company continues to grow its earnings over time, it will appreciate in price. *Almost certainly implied in his contention is that the primary killer for long-term investment performance is* ***impatience****.* In a recent Investors Business Daily article, the writer contends, "A lesson of long-term investing is that it's one thing to get out of the market while the indicators are crashing. It's much harder to get back in before losing out on growth during the inevitable recovery." ***Put simply, market timing has never been proven to be a successful long-term investment approach****. Glenn and I feel that our clients are best served by "staying the course" and remaining fully invested.*

So, are we making any changes to our core portfolio? *Yes, but only in accordance with changing fundamentals (either industry or company specific) or to remain compliant with our investment discipline.* During this turbulent time, we have focused on three things. *First, we have searched for companies who, despite potential short-term market conditions, are best positioned over time, for long-term growth.* Instead of asking what effect the turbulence of the current market may have on these companies over the next quarter or two, we find ourselves asking questions like, what is the outlook for the expansion of global communications (both voice and data) and internet traffic over the next five to ten years? How will the aging population (primarily baby-boomers) be dealt with over time, primarily as it pertains to health care? As the baby–boomers age, spend and save, what effect will they have on companies both here and abroad? Who stands to benefit? Finally, how do we position our clients to benefit?

Second, we have focused on another of our core disciplines. Specifically, we have tried to reexamine each of our holdings from a diversification standpoint. *In other words, we have not been afraid to "take some money off the table."* There are many companies that have been good to us over time. Consequently many have grown quite large as a percentage of our core portfolio. *We must never forget that greed can kill.*

Finally, we have tried to reposition our taxable accounts in an effort to balance the gains taken with any losses incurred (no, we don't get them all right). *Glenn and I remain committed to after-tax returns, not pre-tax returns.*

The long and the short of it, we need to stay the course and focus on the fundamentals. This is our best medicine in the fight against FUDD.

Referrals. They are the life-blood for this and any other service-oriented business. Please keep us in mind when uncovering potential investment management opportunities. Our experience, flexibility and strong performance record could be a benefit to those who wish to work with us. Thank you.

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