

# Sir John and the Point of Maximum Pessimism



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**I**mmersed in a project over the last two weeks, I paid little attention to the markets. Naturally, I was saddened to learn of the death of Sir John Templeton, who was a prince of a man and a king among investors.



Sir John was famous for advising investors to sell at the moment of maximum optimism and buy at the point of maximum pessimism. That strategy created the fabulous long-term growth of the flagship Templeton Growth Fund, dubbed “the mountain chart” by financial advisors fond of selling that fund. Whether it turns out that Sir John died during a buying opportunity remains to be seen. Certainly the markets have been depressing to witness for anyone that’s “fully invested.” The well publicized problems with Fannie Mae and

Freddie Mac are nothing short of frightening, despite talks the Bush administration will move to prop up those government-sponsored but shareholder-owned mortgage groups.

Add that to the classic depositor panic over IndyMac Bankcorp Inc. and its takeover by the U.S. government last Friday and we certainly have the conditions for maximum pessimism. After regulators took control they said IndyMac was the largest regulated thrift to fail and the second largest financial institution to close in American history.

Most of the market commentary I’ve seen on these developments is suitably sober. Even veteran market-watcher Richard Russell observed in his Friday edition of Dow Theory Letters that “the problems now imbedded in the US (and the world) economies are so severe that it could take several years of a bottoming process before the next bull market can get started.”

Russell has been relatively upbeat as this bear market has deepened in recent months and observes that despite the anemic action of the Dow Jones Industrial Average, its lows have not yet been “confirmed” by the Dow Jones Transportation Average. He would be very worried if the Transports dropped below their July 2nd low of 4653 or the January 17th low of 4140.

As Tyler Mordy writes in the July edition of his ETFocus, “the bears are back and Goldilocks has left the building.” He notes that States Street’s U.S. financial sector ETF (XLF on the Amex) is down almost 50% since early 2007. Dividend-weighted ETFs with large financial positions have also taken large losses, something I see in

my own account in the depressed values of the iShares Dow Jones Select Dividend Index Fund (DVY).

If I had spare cash I might be tempted to add to it but critics would liken such a move to trying to catch a falling knife.

In her [Juggling Dynamite blog](#), investment counselor Danielle Park tells investor wondering if the worst is over and whether it’s time to buy that “we’re not there yet.” “I doubt we are through the worst of this bear market yet. Counting from the October 2007 peak, we are now into this bear about 9 months. And while the historical average duration of bear markets has been about 10 months, I suspect this bear will prove to be a bit longer than average. Reverting to the mean on various metrics this time will likely dictate a longer than average market contraction, perhaps of the 12 to 15 month variety.” She suggests remaining seated with cash.

In his Internet Wealth Builder, Gordon Pape suggests investors should “hope for the best, prepare for the worst.” Pape is not advocating abandoning the stock market altogether but suggests taking profits or dumping losers like Citigroup that are likely to fall further before they rally. He suggests building cash reserves to 20 to 25% and limiting new buys to very defensive stocks.

Personally, I continue to hold, confident that in the long run strategic asset allocation will be the best strategy. Not without anxiety, however. It may be darkest before the dawn but it’s possible dawn is still a few hours away.

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