

## Groundhog Day

Dow 10,000 – haven’t we been here before? In the 1993 movie *Groundhog Day*, Phil Connors, an obnoxious, egotistical weatherman (played by Bill Murray), is condemned to live the same day, Groundhog Day, repeatedly. As Phil comes to realize he knows, by “experience,” exactly what is going to happen during the ever-repeating day, he engages in selfish behavior – seducing women, stealing money, etc. He bores of this, though, and becomes self-destructive, despairing of experiencing the same things over and over in what may be eternity. Slowly, he matures and uses his foreknowledge to help people – and then the day stops repeating and he is free to go on with his life.

Phil would sympathize with investors from the mid-1960s to the early 1980s – they were stuck in a seeming eternity of sub-par investment returns. Like Phil, they were slow to comprehend their situation. Having experienced a huge bull market from the late 1940s until the mid-1960s, investors believed a buoyant market was normal. In February 1966, the Dow Jones Industrial Average touched the 1,000 mark for the first time, to much fanfare. From that date until late 1982, the U.S. stock market seesawed around that magic 1,000 level. Each time the market climbed above 1,000, investors believed the previous big bull market had continued, but each time, they were disappointed by a subsequent bear market. From that date in 1966, an investor in a money fund or its equivalent did better than an investor in the Dow Jones Industrial Average for the next 21 years, during which investors, one by one, gave up on their optimistic financial dreams and despaired. In August 1979, *Business Week* ran a cover story titled “The Death of Equities.” The final paragraph of the story began “Today, the old attitude of buying solid stocks as a cornerstone for one’s life savings and retirement has simply disappeared.” After more than a decade of sub-par returns, you can imagine why *Business Week* thought they could sell more copies of their magazine by talking about the death of equities than by trumpeting the advantages of “stocks for the long run.”

This depth of despair, though, occurred when investors should have been greedy. After bottoming in August 1982, at price levels approximating those of 20 years before, the market blasted off into one of the biggest, longest bull markets in U.S. history. Like Phil in the movie, it was not until investor sentiment bottomed out that the solution appeared. Stocks were inexpensive and prospective returns were rosy.

More than a decade and a half into the subsequent, huge bull market, we began bumping up against a new magic number for the Dow Jones Industrials, ten times the old mark – a number that should now be familiar to all investors. In March 1999, with party hats and champagne corks popping on CNBC, the Dow first closed above 10,000. As was the case more than 30 years before, the high point of celebration, the height of investor greed, occurred when investors should have been fearful. Stocks were very expensive, destroying the potential for subsequent returns. The Dow passed through the 10,000 level going downwards in 2001, broke back above the 10,000 level going upwards in late 2003, passed below the 10,000 level going downwards in October 2008, and broke back above the 10,000 level going upwards in late 2009. Depressingly, it's Groundhog Day all over again.

*Rita: "Do you ever have déjà vu?"*

*Phil: "Didn't you just ask me that?"*

*- Groundhog Day, screenplay by  
Danny Rubin and Harold Ramis*

A year ago, the returns from 3-month T-Bills had exceeded returns from the Dow Jones Industrials for more than twelve years. Even now after the furious rally in the stock market off the low, you still would have been better off investing in bonds than investing in stocks during that period. Investor sentiment is an imperfect guide to future market returns. In the previous long bear market, the index low was in 1974, but investor sentiment reached its

nadir in 1982 when the market was 35 percent higher. Several great investment managers established their reputations in the choppy markets of the late 1970s, nimbly racking up superior returns while the average investor was getting more and more depressed. We believe we are now in a similar period for investors.

If, from an investment standpoint, we are like Phil in Groundhog Day, what is our equivalent of Phil learning to live a virtuous life? What do we need to do to set the stage for another long, huge secular bull market? There are three conditions to look for: valuation, psychology and time. First, the bottoms of the long bear markets in the Great Depression and the 1970s saw stunningly low valuations of common stocks of less than 10 times earnings, compared to more than 20 times earnings now. Second, at the bottoms, investors were disinclined to chase the newest hot idea to come out of the Wall Street product factories – fear and disgust were the dominant emotions, not greed. Now, investors are still looking for quick fixes to salvage the destruction of portfolio values in the 2008-09 bear market. There may have to be more frustration in store for them to learn to seek true value rather than fast money. Finally, while it may feel like we already have endured a long winter of sub-par returns, we are “only” about a decade into the current bad phase. According to Ned Davis Research, Inc., the three previous secular bear markets since 1900 lasted roughly 20 years, 13 years and 16 years, respectively.

This does not mean disastrous returns are in store for the stock market – just that the current market will reward flexibility and nimble adjustments more than dogmatic adherence to a belief that the market can only go up. Like Phil Connors, we might have a ways to go.