

## Boenning Morning Comment

*This report is prepared for us by Tower Bridge Advisors*

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Stock prices are about where they were at the beginning of September. Bonds are essentially unchanged as well. With that as a backdrop, it is interesting to look at the pattern of equity investors. Historically, market analysts have hypothesized that the “small” investors always did the wrong thing. They bought at the top. They capitulated and sold right at the bottom. When they did buy, they bought whatever worked yesterday. At least that is the theory.

But if you look at mutual fund statistics issued by the Investment Company Institute every month, the small investor hasn't been so stupid of late. They were small net sellers of equity funds through late 2007 into mid-2008. In July they began to sell in earnest (they could have been a bit earlier) and they continued to be big net sellers through March. But they began to buy in April and continued to be buyers until September when they began to sell equity funds. Although they became net buyers in January, on balance by bailing out in September so far they haven't done themselves any harm.

Look at the debt side. They were heavy net sellers at the bottom of the stock market in the fall of 2008 but by January were consistent and large net buyers. If I need to joggle your memory, 2009 was a great year for both stocks and bonds.

That is all well and good. At least in the short term, their decisions have worked out well. But the historic record suggesting that the small investor does what worked yesterday continues to be valid.

Bonds have been in a quarter century bull market. As interest rates have fallen from double digit levels to almost non-existent rates, bond prices rose. As the economy improved and credit spreads went from record levels to normal, bonds rose further. The question today is whether there is still upside room.

For equity investors, looking backwards the opposite seems to be true. The first decade of the new century have seen stock prices fall, the first time they have fallen in any calendar decade since statistics were recorded. Combine that with the signs of greed on Wall Street and the apparent signals that the little guy has the cards stacked against them, and it is no wonder that small investors quickly became net sellers when upward momentum began to slow.

All this raises two questions. First, are the movements in funds by small investors seismic enough to move the market in either direction by themselves and second, are the small investors correct for a change? The answer to the first question is a pretty strong no. They sold a little over \$20 billion in equity fund shares since September, not a tiny number but one that barely exceeds one large bank TARP repayment offering. They were much bigger buyers of bond funds but in a market where the Treasury raises \$50+ billion dollars at a time (\$80+ billion this week), mutual fund debt purchases look like a drop in the bucket.

As for the second, one cannot give a factual answer. But signs suggest, at least to me, that the past may not be a good prognostication of the future and recent decisions to be tepid sellers of equities and huge buyers of bond funds may not be the right choices.

I don't know when the bull market for bonds will end, but it is hard to believe that 3-4% long term Treasury rates are high. If I am correct and fairly soon (within the next year or two) there is some reversion to the mean, bond prices will fall and total returns for bond holders will be anemic. Yes, bonds will continue to be safe from a credit standpoint, but not from a total return standpoint.

As for stocks, I think the current recovery will continue, Yes, I believe growth rates over the next several years will be subpar, but subpar isn't zero or below. U.S. growth may be subdued but most big U.S. companies have a significant international component that can increase at a moderately faster rate. Once economic equilibrium is restored, maybe growth will average low single digits rather than mid-high single digits. And maybe that gets reflected in a lower than normal P/E ratio. But in the end, growth will be rewarded and companies with good dividends will compete especially well against 10-year Treasury yields.

Today Arsenio Hall is 55. Judy Blume is 72. Joe Garigiola is 84.

The market is closed on Monday. There will be no letter. I will be away until March 1. Unless there is something extraordinary happening, there will be no letter until then.

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Additional information is available upon request.

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