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Don't Lose The Client's Money!

Eugene Bolter, an investment advisor with more than 45 years investment experience, began moving his clients out of the stock market towards the end of 2007. What's the secret of his crystal ball? Years of experience and a conservative approach that develops from his first rule: "Don't lose the client's money." Bolter, founder of Bolter & Company, in Garden City, New York, has a unique perspective on today's financial market and how to make it through this difficult period.

You say your first rule of business is to not lose the client's money. Shouldn't every advisor have the same rule?

One would like to think so! But we also have a second rule: "Don't forget the first rule." This means you need to weigh the risks, even in good markets. In essence, if you don't lose money, over time, you will make money. These rules are particularly true today in what is the deepest and most synchronized world recession.

In the summer of 2007, signs of strain began appearing in credit markets. Complacency was high. As a result we began moving our investments away from stocks and into Treasury notes and money market instruments. Today, our equity percentage is

slowly approaching 50%. Last year, when many portfolios were down 40 percent or more, our client losses approximated 17 percent. No one likes any loss, but our clients know we were in there fighting for them.

What makes the difference?

It goes to the difference between investing through a large, impersonal institution that invests through mutual or comingled funds; or a smaller, personal advisory firm similar to ourselves. We manage our portfolios directly within the guidelines and objectives that are established with each client. This attention to each client enables us to follow through with a conservative strategy designed to achieve above average real returns with below average levels of risk. And, as a small firm, we have the flexibility and freedom to change our asset mix or industry allocations at will. In good markets, our portfolios will be heavily invested in equities and less in fixed income. In bad markets, we do the reverse.

But, when you invest in mutual funds, you don't have access to the fund manager and the relationship is impersonal. Further, you may not realize that the funds have guidelines which limit the percentages of cash they can hold, even if they want to be defensive.

Many people say you can't time the market. Maybe so, but it's our responsibility to protect our clients. We have been reasonably successful in doing so during the market decline in 2000-2002, and again this past year. In the period 2000-2002, the S&P 500 Index lost 38% in value, where our strategy resulted in a consolidated decline of only 3% for our client portfolios.

As an example of changing market weightings, three years ago we correctly identified the beginnings of a worldwide imbalance between an increasing demand for oil and the coming inability to expand the supply. We increased our energy holdings and our portfolios benefited accordingly. Then, in the summer of 2008, we saw a slowing in world oil demand and we started to move away from our energy investments. Nobody can be perfect doing this, and errors will be made, but we try. We believe success comes from being totally involved and responsive to market and economic conditions and having the common sense to shift tactics before it's too late. Today's market environment is no longer conducive to just buying and holding stocks.

What caused today's economic crisis?

Over the last 20 years or so our country's extraordinary growth was, in large part, based on a financially driven addiction to assets, with zero savings, and a large and unsustainable debt burden. In effect, assets became our savings. We lived in a multiplicity of bubbles in asset markets (equity, property and credit) and those bubbles have burst – leaving behind an over-extended, indebted and saving-short consumer and a broken and bankrupt financial system. Unprecedented monetary interventions and government stimulus promise a fairly quick and superficial recovery but it will still take considerable time to repair the period's many excesses and complete the debt restructurings, global de-leveragings and asset liquidations that are necessary before one can see a sustainable upturn.

What would you tell the average investor?

We believe that investors, in seeking out future capital gains, should also focus on accumulating cash flows. With interest rates close to zero, one should look to securities that provide a reliable stream of income as well as growth.

Look to invest in high quality corporate and municipal bonds, and quality stocks with high and secure dividends. Also, if you have some liquidity, you are able to take advantage of market opportunities when they develop.

How do you pick the stocks you do invest in?

Generally, we work off the S&P's 100 Index of the largest companies, discarding about half and focusing our attention on the remaining companies. Any prospective company must have strong industry prospects, be a market leader with a demonstrated long-term record of success, and hopefully have a good cash dividend policy. In addition to fundamental research, we find technical analysis helpful in identifying new ideas as well as observing changes in the market makeup.

What about other investment opportunities?

We have a small position in the gold market.

You have more than 40 years in the investment markets; what does that experience tell you about where our economy is going?

If you look back, since World War II, there have been a half dozen recessions and stock market declines that were brought about by rising inflation. To counter inflation, the Federal Reserve would raise interest rates and later ease rates when inflation declined.

The economy and the stock market followed along. In each of these episodes, the net worth of the average household declined on the order of 5%. The repetitive pattern of these market swings served to create a belief that when stocks go down, they automatically bounce back. To some degree, this is true. However, in this current punishing recession, household wealth which began to decline in mid 2007, lost a staggering 20% in 2008 and is continuing down further this year. It becomes a different world, psychologically and financially, when you're facing the destruction of one's previously assumed wealth by 25% or probably much more. How this affects future confidence and behavior is hard to guess.

Together with sharply rising unemployment, this loss of wealth has frightened consumers into a multi-year shift towards thrift and debt repayment and away from discretionary spending. After the recession hits bottom, it's not clear from where the new demand will emerge to permit a meaningful and sustainable long term recovery that creates new jobs. A structural budget deficit approaching two trillion dollars will constrain future expansionary policies from continuing to put a prop under the economy. Growth in the U.S. may remain subpar or lethargic for some time. Unemployment will remain high for many years, especially for young people.

What do you think about the Ponzi schemes? How does one protect oneself?

The investment advisory industry has been battered by financial fraud and scandals lately. Trust has become a significant issue. The safeguards that we have in place for our own clients may be helpful as an example of what protection one should look for in an investment advisor relationship.

We handle all investments for our clients directly, and we do not invest with or through other money managers. Our clients' funds are held in their own names at Fidelity Investments. Fidelity is a large mutual fund manager, broker and custody agent that as a private firm has not been involved in Wall Street's problems. This gives our clients the security of knowing their funds are safeguarded. We have a limited power of attorney to invest and trade securities on their behalf, but we have no access to those securities or to our customers' free cash balances. In addition, we interface with Fidelity daily and have the ability to reconcile our positions with theirs on a moments notice.

Also, we are registered with the Securities and Exchange Commission and are subject to the same reporting and compliance requirements as the major financial institutions. We provide quarterly performance and capital gain reports; in fact, clients can call at any time for real-time results. Clients also receive trade confirmations and monthly statements directly from Fidelity.

Anything else you'd like to add?

For us, it's always been more about the relationships and trust that we've earned with our clients. Most of our clients have been with us for years because of our results, having a trusted personal relationship, and knowing our business is based on the satisfaction we get from helping them.

Disclaimer: The views expressed are the views of Eugene Bolter and are subject to change at any time based on market and other conditions. Past performance is no guarantee of future results.