Memo to: Oaktree Clients

From: Howard Marks

Re: Hindsight First, Please (or, What Were They Thinking?)

> "The farther backward you can look, the farther forward you can see."
> – Winston Churchill

I often cite John Kenneth Galbraith's observation that one of the outstanding hallmarks of the financial world is "the extreme brevity of the financial memory." Investors lose money over and over because they simply forget that cycles are inevitable and there's no such thing as a free lunch. Now I've found a great quotation from Churchill, also reminding us that foresight comes largely from awareness of history.

Along similar lines, I'm struck by the extent to which a related factor, inadequate skepticism, also contributes to investment losses. Getting the most out of a book, play or movie usually requires "willing suspension of disbelief." We're glad to overlook the occasional plot glitch, historical inaccuracy or physical impossibility because it increases our enjoyment. When we watch Peter Pan, we don't want to hear the person sitting next to us say, "I can see the wires" (even though we know they're there). While we know boys can't fly, we don't care; we're just there for fun.

But our purpose in investing is serious, not fun, and we must constantly be on the lookout for things that can't work in real life. In short, the process of investing requires a strong dose of disbelief. **Time and time again, the post mortems of financial debacles include two classic phrases: "It was too good to be true" and "What were they thinking?" I'm writing to explore why these observations are so often invoked in the past tense.**

The combination of greed and optimism repeatedly leads people to pursue strategies they hope will produce high returns without high risk; pay elevated prices for securities that are in vogue; and hold things after they have become highly priced in the hope there's still some appreciation left. Afterwards, hindsight shows everyone what went wrong: that expectations were unrealistic and risks were ignored.

It is my point that:

- **Investors mustn't dwell excessively on recent experience.**
- **Instead, they must look to the future.**
- **They must consider today's developments critically.**
- **That assessment must take place in the light of history's lessons.**

All too often, investors' interest in the past is limited to the last few months or perhaps a year or two. They look unskeptically, are dazzled by the high returns they see, and jump aboard for more of the same. But they usually fail to consider longer-term history, which would show that "free lunches" never last forever. When the check ultimately comes in the form of losses, there's surprise and disappointment that could have been avoided.

Time after time when I read about trends being taken to excess – and later, when the painful consequences become clear – I find myself asking what they could have been thinking. **The alpha that's so much in demand today is really the ability to see ahead to things others will see only afterwards, in the rearview mirror.** The people of Oaktree spend a lot of their time figuring out what might be the next mistake and preparing for it. In other words, we try to anticipate – and avoid – pitfalls that others will rue after the fact.

Caveat Emptor

Today's financial *cause célèbre* is the Bayou group of hedge funds. Results were falsified and a lot of money has disappeared. It's easy to make a list of those who deserve blame in this affair, but few of the articles I see focus on the people I think should head the list: the funds' investors.

We live in an age when fingers are pointed at others all the time. Losers feel aggrieved and sue. That's what Bayou's investors will do, and certainly they were defrauded. But what was their part in the process? Where was their disbelief when they swallowed the following:

- They put their trust in a manager who claimed to have been a senior trader at Leon Cooperman's Omega Fund. But Leon – who denies that claim – says he got only one call over the years to verify it, while investors poured hundreds of millions into the fund.

- They invested in funds that executed trades through a brokerage firm owned by the funds' manager. Didn't they worry about the conflict that arises when a manager makes more money when his fund trades more often?

- They invested with managers who were the subject of complaints and lawsuits alleging improper conduct; these things can be checked out but apparently weren't. It seems investors took comfort from the fact that the brokerage affiliate was licensed by the NASD. What they missed, however, was the fact that the NASD would police the conduct of the brokerage arm but not the fund or its management.

- They went into funds whose auditors they'd never heard of. They couldn't have heard of them, because they'd never audited anyone. And if they had asked, they would've learned that the accounting firm's registered principal was the hedge fund's CFO.

- Some invested on the recommendation of people claiming to be hedge fund consultants. But in many cases these "advisers" disclosed that they were being paid by the funds they recommended. How could investors have relied on what so obviously could be biased advice?

In the case of Bayou – as in other scams before and others to come – it's clear that a drawerful of cash provides a strong incentive to steal. But if that's so obvious today, shouldn't it have been obvious to people before they became investors? Shouldn't that have encouraged caution? As The Wall Street Journal wrote on September 30 regarding Bayou's founders, "Such tidbits from the duo's business backgrounds were easy to find via Internet research and other inquiries." **Thus the bottom line is a simple one, and instructive. Which of Bayou's limited partners would have invested if they had known the above facts? And why didn't they know them?**

Stocks for the Long Run

Going from the micro to the macro, another subject that suddenly looks a lot different in retrospect is the likely return on U.S. stocks. When I was in graduate school at the University of Chicago in 1967-69, I learned that its Center for Research in Security Prices had input the closing price for every stock every day since 1929 and computed that the average yearly return on U.S. equities had been a shade over 9%.

Later, a few more years of good returns had raised the historic figure – and thus expectations for future returns – to the range of 10-11%. **And from the late 1960s through the late 1990s, nothing – and I mean nothing – was more universal than the belief that stocks could be relied on for 9-11% per year. I don't think I've ever seen an assumption that was less questioned than this one.**

The next step in cementing this expectation was the publication of "Stocks For the Long Run" by Wharton's Jeremy Siegel, one of the nation's highest-rated professors. Siegel's message had the effect of minimizing worry about the variability of equity returns. He demonstrated with past data that stocks could be depended on to beat cash, bonds and inflation over the long term. In the popular perception, this morphed into an expectation that stocks could be depended on to beat cash, bonds and inflation . . . period.

Along with the boom in tech/media/telecom stocks and the first-day gains of IPOs, Siegel's data contributed to one of the greatest equity manias of all times. Of course, it evaporated after the TMT stocks collapsed in 2000 and was buried as the major stock averages did the unthinkable, declining for three straight years for the first time since the Great Crash.

So what do people expect from stocks today? Equity investors now realize that p/e ratios are too high for multiple expansion to be counted on, and that dividend yields have declined from 4-7% in 1925-55 and 3-4% in 1955-95 to 1-2% in the last ten years. Thus, they conclude they may have to look just to profits growth for their returns, and that's likely to be in the mid-single digits as usual. As a result, in my view, everyone's thinking 6-7%. No one's talking about 9-11% anymore.

What changed? There's nothing new about the argument contained in the paragraph just above. The cautious were making it in the 1990s. When stocks were rolling along, however, it had little persuasive power. **With stocks high, expectations regarding future returns were high.** The S&P 500 is 20% lower today than it was in 2000, on higher earnings, so it's demonstrably cheaper in p/e ratio terms (even if not necessarily cheap). **And with stocks lower, expectations regarding future returns are lower.**

Can there be a more clear-cut case of hindsight prevailing? I don't think so. And by the way, in the late '90s, people were sure stocks held the key to investment performance, and were pushing up their allocations. Some got to 80% just in time for the crash. I may not travel in the right circles, but it's been years since I last heard of an institutional investor that wants to increase its allocation to domestic equities. **If they're correct now, what were they thinking in the late '90s?**

If Not Stocks, Then What?

Since no one wants to increase allocations to U.S. stocks (or high grade bonds, for that matter), where's the money going? The answer is, just about anyplace else. Everyone knows there's too much money looking for a home in buyouts, venture capital, distressed debt, hedge funds, real estate, and on and on. But that isn't keeping more from flowing there.

I love that terrific Yogi-ism: No one goes there anymore; it's too crowded. **But the corollary is appropriate for the alternative investing world of today: Because it's so crowded, everyone wants to go there.**

Buyouts represent a great case in point today. It's a simple business (execution aside). You buy a company with a little equity and a lot of debt. If you buy it right, if you can make it a better company, and if you run into an environment characterized by a strong economy, freely available capital and rising asset prices, you'll be able to sell it for more than you paid for it, pay off the debt and enjoy a leveraged return. The theory is clear, but (like everything else in the investment world) it doesn't always work.

It worked very well from its inception around 1973 to roughly 1985, a period in which it was cheaper to buy a company through the stock market than start it and no one had ever heard of Henry Kravis. Then LBOs became enormously popular in the late 1980s, and companies were bought at ever-higher prices and ever-higher leverage ratios. Many of those went bankrupt in 1990 (causing a boom for distressed debt investors, but that's another story).   That's what we call a full cycle.

Then a new cycle began, as it always will. Because the market was depressed in the early 1990s, as were investors, companies could be bought cheap again. And with both borrowers and lenders chastened, no one had to worry about deals becoming over-leveraged. When a lengthy economic recovery ensued, those deals did well. (Even in the next heyday for distressed debt investors – 2002 – very few buyouts went bad.)

But every trend eventually is carried to excess, and it's absolutely inevitable that "what the wise man does in the beginning, the fool does in the end." So now everyone thinks buyouts hold the answer again. Everyone's emboldened rather than chastened. And everyone's enticed by the recent returns, which in many cases have been eye-popping.

What's been happening? Simply put, the stars have been perfectly aligned for buyout success. In the recession, the scandals and the stock market malaise of the early 2000s, companies could again be bought reasonably. Lenders became motivated to put out capital, so higher leverage could be piled on at low interest rates. The economy turned strong, and business recovered. As increased capital flowed to buyout funds, the competition to buy companies – even from other buyout funds – drove up prices. And most crazily, lenders became willing to extend debt capital so that equity sponsors could take out their investment in short order. Nothing could be better for buyout returns than the ability to minimize your equity investment, increasing the extent to which returns are geared up. Thus the deals made in the last year or two have produced great returns.

But that doesn't mean the returns on deals made today and tomorrow will be similarly high. Will the favorable trends continue, or will they reverse? Will companies be costlier? Will interest rates rise? Will the economic environment continue to be salutary? Will leverage have the effect of magnifying gains or losses? Will the mega-fund managers do as well with $10 billion funds in the environment of tomorrow as they did with $3-6 billion in the past, with the stars aligned beautifully? **No one knows the answers, but investors should be asking these questions.**

I recently had a visit from the head of one of America's largest pension funds. He agreed with me that money is flowing to buyouts (and other forms of alternative investment) mainly because no one wants more mainstream stocks and bonds. He also pointed out that people are making these investments to capture the "illiquidity premium." The illiquidity premium and its cousin, the risk premium, are return increments that illiquid and risky investments should deliver to compensate for their illiquidity and riskiness. If return premiums couldn't be expected, investors wouldn't make those investments. **But the fact that something's illiquid or risky absolutely does not mean that a return premium can be depended on to materialize – and certainly not in short-run periods as brief as 5 or 10 years**.

It seems like a long time ago that people talked about the equity risk premium: the amount of return in excess of bond returns that stocks would deliver to compensate for their riskiness. But, again, the fact that it should have been there doesn't mean it was. In 2000-02, it certainly did not show up.

Investors should demand return premiums, but they shouldn't count on them. They should try to figure out whether they're in prospect – and as "prospect" implies, that's done by looking forward, not backward. The fact that return was there in the past doesn't mean it'll be there in the future. And, in fact, if too much return was earned in the past, that implies not much may be left for the future.

The Impact of Oil Prices

I'll try to be brief here. If I told you the government had just enacted a $125 billion annual tax increase, you might think consumer purchasing would be crushed, business strangled and stocks beaten down.

Thus I'm incredulous that, with the price of oil (of which we import 12 million barrels a day) having risen from $33/barrel in January 2004 to $62 today, the stock market is still up (albeit not much). What is a price increase on imported oil other than an enormous tax increase, with the proceeds going abroad rather than to Washington?

Maybe I'm just looking for the next thing to worry about (as usual). But if the economy slows in 2006 or 2007 and security prices decline, and people explain it all by citing the increased cost of oil, I hope you'll remember to ask people what they were thinking in 2005.

By the way, I don't include this section because I want to discuss oil prices, but because the recent developments exemplify typical investor behavior. **When investors as a group are feeling upbeat, the market is able to shrug off negatives as isolated and insignificant. When they're depressed, investors generalize individual complications into an insurmountable web of negatives.** I feel it's very important that we be aware of whether the market is giving events their proper weight, versus overlooking or overrating them. When things develop that should be considered, it's a matter of "Pay me now or pay me later."

We're from the Government and We're Here to Help

In 2002, at the height of the Enron/WorldCom corporate scandals, the federal government gazed unerringly into its own rearview mirror and demonstrated its ability to solve the last problem . . . and cause the next one. I've been looking for an opportunity to pop off on the subject of Sarbanes-Oxley, and here it is.

There was little discussion or dissent before Congress passed – and the president signed – this piece of legislation designed to root out corporate corruption and hold executives responsible for future infractions. The vote should tell you something: 423 to 3 in the House and 99 to 0 in the Senate! Any time the Great Deliberators on both sides of the aisle agree on something so overwhelmingly, it's probably being done in the heat of the moment and in response to rampant popular sentiment – and it's probably a mistake.

Let's look at the law's operation and effects. First, it required enormous one-time expenditures for the scrubbing of corporate books and the creation and assessment of control structures designed to avoid misdeeds. Second, it called for significant incremental ongoing expenditures along these lines.

At a conference I attended recently, a venture capitalist estimated that the average company with revenues of $50-60 million faces increased costs of $1-1½ million per year associated with being public. Larger companies are spending far more. I view this as an enormous tax on American business in perpetuity, and the benefits as far smaller than the cost.

When the hue and cry was at its apex and this law was enacted, a widespread epidemic of corruption was suspected. It turned out that the early reports were the worst, and few additional cases were detected in the mandated examinations that followed. So as a result of about $10 billion in scandals – at Enron, WorldCom, Adelphia, Tyco and a few others – we've ended up with a law that will require the largely unproductive expenditure of many billions every year forever (or until rectified).

And it's not as if we had no laws on fraud before Sarb-Ox. They were there, and they were enforced. It's just that in 2002, citizens, and thus politicians, became frustrated with the fact that the old laws didn't prevent all fraud or keep CEOs from saying, "I had no idea that was going on." Thus the government moved precipitously to enact new laws. It's worth noting in this connection that the executives of Tyco, Adelphia and WorldCom all were successfully prosecuted under the preexisting laws, while the major alleged malefactor targeted under Sarb-Ox – Richard Scrushy of HealthSouth – escaped punishment altogether.

So has Sarb-Ox solved the problem? Mistakes made by generally honest managements will be identified in some cases, as they may have in the past, and some inept fraudsters will be caught. But I doubt the serious crooks will be prevented from taking a crack at robbing the cookie jar. And there is genuine risk that Sarb-Ox's single-minded emphasis on driving out fraud will have negative implications for corporate decision making.

What will be the effect of all of the above on companies' future development, and on the free enterprise system that has done so much for America heretofore? That's what our government should be emphasizing – not an overblown reaction to the scandals of the past. If the shortcomings of regulation can be reduced to one, I think it's the inability to anticipate second-order consequences. My advice to Washington (not that anyone's asking): don't look back at the problems of yesterday, but ahead to the impact of your "solutions."

<u>Saving for Old Age</u>

Henny Youngman used to tell about being stuck up at gunpoint. When asked for "Your money or your life," he answered, "Take my life; I'm saving my money for my old age."

Well, we rarely hear anymore about saving for old age. That's part of the financial prudence that has become hopelessly passé. After all, saving for later means consuming less today and delaying gratification, and those things are entirely out of style.

But then how do people expect to live in their old age? People seem to be retiring earlier, and certainly they're living longer. Medical advances are prolonging life but not getting any cheaper. With retirement lasting longer and entailing greater costs, how will people pay their bills?

Heretofore, the solution has been a stool with three legs: Social Security, private pensions and personal savings. How solidly constructed is the stool of today?

We've heard a lot about Social Security's woes. The number of active workers supporting each retiree is declining, threatening the system with insolvency a few decades out. After reading (and reviewing for the L.A. Times) Pete Peterson's excellent book "Running on Empty," I'm convinced we'll need some combination of higher taxes, delayed retirement or reduced benefits . . . but equally convinced that few politicians are going to commit career suicide by advocating tough medicine to solve a problem that's decades away. Not having to worry about reelection, President Bush came out of his 2004 victory willing to spend some political capital on his solution: the private retirement account. But no groundswell formed behind it, and other issues have taken center stage, and we haven't heard anything on this subject for months. One way or the other, I think retirees in the future will receive less from Social Security than the system promises today.

So what about private pensions? Defined Benefit plans are declining in popularity among employers, and a not-insignificant number are headed for insolvency. Defined Contribution plans are taking their place in many cases, but some of the bloom is off the rose now that "401-k" and "Acapulco" have ceased to be synonymous. Certainly their benefits are expected to be less lavish and less dependable now than was thought to be the case while the equity bubble of 1998-99 was in full flower.

And that leaves personal savings . . . which as a percent of income just went negative in July. I am amazed when I read about the people who spend all of their income and more on lifestyle. **Maybe they think old age won't come, but that's not a solution I'd be eager to rely on.** What about the millions – with no savings – who each year spend thousands of dollars more on their credit cards than they earn. How do they think this movie will end?

Anyway, early Baby Boomers like myself are probably well taken care of, because we partook of the post-war economic miracle before it had to be shared broadly and heeded the lessons of thrift taught by our Depression-era parents. But I worry deeply that those who retire in the 2020s and thereafter will find themselves without the resources they need. I also worry that the government will write checks to cover the shortfall. Compassion is a good thing, but swollen deficits, higher taxes and the implications of teaching people they don't have to save are all very bad.

When 2030 rolls around, with the centennial of the Depression, there's likely to be widespread wonder about what the non-savers of 2005 were thinking. I'd rather people started asking the relevant questions today.

You Can Always Live in It

Of course, the solution *du jour* for the question of wealth building is real estate. People are lining up to buy residences – especially condos – that they don't need, don't intend to occupy and can't rent out at prices providing a reasonable return on their investment, all in the expectation that they'll be able to sell them at a profit. That prompts me to coin a Yogi-ism of my own: My condo produces negative cash flow every month, but somebody else will pay me more for it than I paid.

My May memo "There They Go Again" discussed the residential real estate boom in depth, and I'm not going to repeat its message. Suffice it to say that "It can only go up," "It's been rising for months, but it's sure to keep going" and "If it starts to go down, I'll just get out" are routinely scoffed at after the fact.

What I want to review here is the extent to which people are buying highly appreciated properties that they couldn't afford if they had to pay full debt service on them on a current basis. This is entirely analogous to the highly leveraged buyouts of the 1980s that depended on zero-coupon borrowing. This debt was a big red flag: "I'm buying something I can't afford, with debt I can't service on a current basis, hoping positive developments will bail me out." Most of them went bankrupt in 1990 when the economy softened and debt couldn't be refinanced.

Now people are assuming increased financial risk to buy homes, often taking out interest-only loans at artificially low teaser rates. The September 2005 issue of The Gloom, Boom & Doom Report quoted Grant's Interest Rate Observer quoting David Rosenberg of Merrill Lynch:

- An estimated 42% of first-time buyers made no down payment on their home purchase in 2004.
- In the hottest price areas in the U.S.A., ARMs [adjustable rate mortgages] now account for over 50% of new mortgage originations.
- Over 60% of new mortgage loans in California this year have been interest-only loans or option ARMs.

People are stretching to buy the most house they can with the biggest mortgage payment they can afford. But if they can barely cover today's artificially reduced payments, what will they do when interest kicks in and/or rates rise? And what if their incomes fall? Where's the margin for error? When I was young, the rule of thumb was that no more than one-quarter of your paycheck should go for shelter. Today lots of people are paying more than half.

"Everyone knows" it's better to make tax-deductible mortgage payments than to pay rent. But the beauty of financial puzzles is that there's no answer that's always correct regardless of the circumstances. I'd rather pay a low rent I'll be able to afford even if things get a little worse than a high and possibly rising mortgage payment, on the continuation of which my home ownership is riding.

The old goal was to have the house paid off by retirement, so you could live in it when your paycheck stopped. Now, thanks to the magic of minimal down payments, minimal amortization and adjustable interest rates (starting from historically low levels), payments may well be higher in retirement than during the owners' working years. How will people – possibly with little or no savings – hold onto their properties when their paychecks stop?

We never hear anymore about people "saving for a rainy day" or "saving for their old age." If you do those things, it may be harder to get the house of your dreams . . . but you'll never go broke. I wonder how many of today's home buyers will learn this lesson through painful experience.

Selling Money

If a seller wants to move more of his product, what does he do? Well, that depends on whether the product is capable of being differentiated from its competitors. If it is, he can try making it better, advertising it more or improving distribution. But if it's not differentiable, those things won't work. Can you imagine the success that's likely to come from an ad slogan like "Burn our natural gas; it's better"? Goods that can't be differentiated from their competitors are called commodities. If a seller of a commodity wants to increase market share and thereby sell more of his product, he has only one way to go: price it below the competition.

For the last two years, financial institutions have been able to make money by borrowing at short-term rates held down for stimulative purposes and lending at higher, longer-term rates. Thus, the institutions have battled to increase market share. But how could they do that, given that everyone's money is green (and leaving aside the fact that it makes no sense for all participants to expect to increase market share at once)? The answer's the same as for any other commodity: price it below the competition. In the case of financing, that means offering more of it for a given use, at lower interest rates, with looser terms and covenants.

As The Wall Street Journal of October 7 reported,

> UAL had been shopping for $2.5 billion of financing to fund its exit [from bankruptcy] **before competition among four financial institutions resulted in the larger [$3 billion] loan package on "very competitive" terms**, the company said. . . . This is a very competitive rate in this

> industry, [J.P. Morgan Vice President James] Lee said, noting that some recent airline financings have carried much higher rates. (Emphasis added)

When suppliers of capital are trying to pump out more money at lower rates, usually they also apply looser credit standards and offer easier terms. When that's the case, it's time to be a taker of capital, not a supplier. Our best investments have been made when suppliers of capital were shrinking from the market, refusing to lend or invest at any price. That means it's important, as in so many things, to look at the behavior occurring around you and ask one simple question: **"What kinds of times are these?"** The answer is usually clear, and thus so are the implications for the future.

<u>But Does It Make Sense?</u>

Ultimately, that's all you have to ask. The same October 7 issue of the Journal carried a story describing the efforts of mutual fund companies to offer "absolute-return" funds.

> The bear market was "a wake-up call" for investors who previously were fixated on trying to earn as much or more as the surging stock market . . . Now, while investors may not recognize the terminology of absolute versus relative investing, "they just know they don't want to lose money."

When the stock market was doing well, investors were pursuing high returns. Now, after some serious losses, they're pursuing safe, dependable returns. Even the Journal, not particularly known for cynicism, points out that, "the recent enthusiasm for absolute-return funds will fall by the wayside whenever the stock market takes off and market benchmarks rise far more than the gains at hedge-like funds." **In other words, investors pursue safety when past results have been poor, but they lose interest in safety when past results have been good for a while. Not exactly contrarian, but the way it's always been. Investors have to learn that last year's return is not an indicator of next year's return, and thus of the appropriate strategy.**

And while I'm asking investors for more insight, I see the Journal goes so far as to point out that "it's also possible that the absolute-return vehicles won't achieve their stated objectives." There's nothing new about investment managers falling short of their goals. Further, managing a portfolio of diverse asset classes and both long and short positions to produce steady returns regardless of the market environment is a particularly challenging task. Few people are able to do it successfully, and someone who can is more apt to work at a hedge fund charging "2-plus-20" than a mutual fund charging 1%.

In other words, I think most investors in these "absolute-return" mutual funds will find a few years from now that they didn't get what they wanted – that their returns were disappointingly low or disappointingly volatile (or both). **It would be great, instead, if they could ask <u>today</u> whether it's reasonable to expect consistent returns in the high**

single digits after significant fees. Otherwise they're likely to end up asking themselves – once again – "What was I thinking?"

*   *   *

The philosopher George Santayana is famous for having said, "Those who cannot remember the past are condemned to repeat it." (Most apropos of this memo, but less famously, he also said, "Skepticism is the chastity of the intellect, and it is shameful to surrender it too soon or to the first comer.")

The value of hindsight lies in the fact that lessons learned in the past by others can enable subsequent generations to avoid having to learn them anew. And yet, it seems investors must learn those lessons over and over – and often the hard way. The exact circumstances may not repeat, and the mistakes may not surround the same asset classes, but the general lessons of investing go on having to be learned. To avoid this, we have to improve on the brevity of memory that Galbraith complains about; refuse to surrender our skepticism; and learn to assess market behavior around us and extract the proper inferences for application to our own behavior.

Readers of my memos know I feel awareness and understanding of cycles is an essential tool for investment survival. I always say about cycles, "We may never know where we're going, but we'd better have a good idea where we are." Hindsight is helpful in this regard, not because the future will be exactly like the past, but because by learning the time-honored lessons of the past we can better cope with the uncertain future. Recognizing past patterns permits us to increase our preparedness, the payoff from which can be considerable.

Recent trends must not be counted on to continue unabated; that's one of the main lessons of the long-term history that matters. A better understanding of that history tells us that every day of the recent past – and of current experience – is just another step toward the inevitable next cycle. **A critical analysis of the future will prove far more profitable than will unthinking adherence to the latest trend. But it's the latter that always has dominated market movements, and that we have to watch out for.**

So every day when you read the newspaper, watch your Bloomberg or witness investor behavior, I encourage you to divine what those things say about what's going on. That's one way you can change your investing future for the better.

October 17, 2005