Philequity Corner
By Joseph Liao Ong

PAINFUL BANKING

We got exciting calls when our September 14 article touched on 'Lessons from Lehman'. To add to the excitement, here are more lessons on banking and investing. Most investors have seen their portfolios melt while being frozen into inaction. The adage 'no pain, no gain' applies to investments too.

The crux of the matter is when does an investor listen and when does he not follow the advice of bankers and brokers. Most of us are not full time investors. Most secure their principal money through business, career, inheritance etc. and then hand over the funds to banks for investments. Many are busy and rely on bankers for financial advice and guidance. When the advice goes wrong, that is when the pain starts.

KNOWLEDGE IS POWER

In the 1960's, a small bookstore in CM Recto called Webster used to give out free book covers to customers. In big letters, it says "Knowledge Is Power". How very true till today and more relevant when it comes to investments. Peter Lynch, the legendary Fidelity Investment fund manager, said 'buy only what you know'. Warren Buffet was not hurt in the 2000 dotcom bust, since he claimed he did not understand and therefore did not invest in the dotcom tech companies. People tend to buy what they hear. Or they follow the herd. The wealthier ones tend to rely on private bankers and financial experts. They nod their heads to the presentations and promotions of so-called experts, usually understanding only half of what is being presented. Then after a sumptuous meal, they buy in. Be careful when you buy with a big burp. Buy with your brains not your tummies.

Some financial advisors spin good stories relying on past financial results and reports. Others pride themselves in doing the legwork and visiting the companies. One banker even proudly proclaimed he personally visited the Kazakhstan banks while others do not. Little did he know he was talking to crooks, as malfeasance and fraud were being committed right in front of his eyes. Does your banker fully know who and what he is promoting? How good is his due diligence?

Do you know your banker?

PAST NOT EQUAL TO FUTURE PERFORMANCE

Fund managers can promote financial products using past models with projected future profits. Somehow, the prices drop once investors buy in or the subsequent gains are below forecast. Another way bankers stimulate investors' penny envy is to say how other clients earned on their previous advice. Yet the investors seldom hear about clients who are stuck with losses due to their bad advice.

During initial public offerings, rosy financials are presented. They may not necessarily be misrepresentations but do not depend on the banker to monitor future corporate performances. The due diligence applies only to the past and present. After pocketing banking fees and commissions, the banker leaves the investors on their own.

WHEN IN DOUBT, DON'T

Once, a designer shared a simple rule of fashion - when in doubt, better not. Does this fashionable yellow shirt match these latest red style pants? Apply this simple rule to investment to stem the red ink. If you are a Philequity Corner reader, chances are you have acquired enough knowledge and experience to form intelligent hunches. When in doubt, stay with your hunches. Better still, stick to what you know.

Some investments and banks are so private, the bankers themselves do not know what they are. If it is very private, the financial mystique and glamour are so tempting. The more esoteric and elite, the more dangerous they become. Bernard Madoff was able to entice many sophisticated clients because he was very elite. His institution was private and selective. It was like by appointment and invitation only. One has to fall in line for what turned out to be a guarantee to lose all money!

When the returns are unusual and the yields are too attractive, please doubt. When you cannot erase the doubts, please don't. Financial history is full of high-yield robberies. Doubting Thomases in investments become believers then become martyrs.

BALANCE AND REVIEW YOUR PORTFOLIO

Some investors said a diversified portfolio did not work during this crisis. All asset classes crumbled. It is partly correct. Some assets fell more than others. Subsequently, some assets recovered faster than others. If one invested all in emerging market bonds plus leverage for boosted yield, the investor ends up holding a bag of defaulted or restructured bonds, suspended coupon payments, and only a handful of recoverable notes. If one invested all in a supposedly safe and steady Fairfield Greenwich Fund, one's portfolio value is now zero. The Fund simply re-invested with Madoff.

An investment portfolio should be balanced according to one's present and future financials needs, risk profile, risk tolerance etc. and contain different asset classes. And like any other skills, constant practice and review are a must. Even for buy-and-hold investors, continuous study and review of holdings is prudent. Some gold may have turned to garbage. Some profits have to be realized to make real money.

BE PRUDENT AND AVOID LEVERAGE

Remember bankers are fair weather friends. They extend loans and allow margins when the weather is good. Once the storm comes, they take away your umbrellas. The worst is when margins are called, a leveraged investor is forced to sell the better assets and keep the bad ones. During periods of panic, the fundamentally sound stocks and bonds are more liquid and command better prices, whereas the junks exhibit battered prices and become illiquid. Ironically, the leveraged investor has to give up his good eggs and keep the bad eggs, which eventually rot.

PLAY THE MARKET CYCLES

Markets move in cycles. There is a bull and a bear cycle. Be aggressive at the start of a bull and be careful when there is euphoria and frenzy. It is hard to consistently predict the start of the bull and the arrival of the bear. As quite often, the bear starts with a Black Swan event. (*See Black Swans & Minsky Moments article last 29 September 2008*). Be greedy when the crowd is fearful; be fearful when the crowd is greedy.

The big picture of market cycles has an equity bull phase, alongside or followed by a commodities bull, then a cash-is-king phase when equity and commodities go bust, and a fixed income or bond bull coinciding with decreasing interest rates.

LAUGH ALL THE WAY TO THE BANK

Humor is the best antidote to pain.

A friend refuses to bank with Goldman Sucks. He says it's smelly. He prefers Gold Toe.

Another friend parks his standby funds with a bank, only to realize it is "More Gone Standby".

Some people pronounce letter "c" as "sh". A friend hesitates to bank with Citibank.

One friend saw his initial $100 become $5. He threatened to sue his banker. The banker retorted "**I**'m **N**ot **G**uilty"! and followed by "**I**kaw **N**o **G**ood!"

The world's local bank may turn out to be '**H**ighly **S**ophisticated **B**anking **C**rooks".

A friend received a text from his banker, "**U** **B** **S**afe". Later, he realized his funds are stuck and locked up with 3 keys.

One old diabetic friend found out his credit can now only buy a few "**C**hocolate **S**weets".

Another friend confided that a portfolio with J Bull is better than with J Baer.

One naughty friend lamented giving his money to Lehman. He might as well have given it to a Woman. The company is better.

Instead of buying Kazakhstan, Urbekistan, Turkmenistan, it is safer to bet on Andrew Tan and Lucio Tan.

Happy Painless Banking!