What's Better Than Buy And Hold? NEW!

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Is it time to look for an alternative to buy-and-hold?

I write a regular column for Financial Advisor (FA) magazine. In my last column, I interviewed a handful of financial advisors who have targeted 401 (k) plan participants as their business niche.

I grew interested in advisors specializing in 401 (k) participants because of the recent flap over the Department of Labor rules on who can offer advice to plan participants under the scope of the Pension Protection Act of 2006.

But while I was reporting on the 401 (k) plans, I stumbled on something entirely different and quite interesting.

Three of the four advisors I interviewed use technical analysis to manage the 401 (k) investments. All three use the data from Dorsey Wright & Associates in Richmond, Va.

I was surprised by the amount of mail I received from FA readers on this column. Nobody argued that these advisors were crazy to desert the tried-and-true buy-and-hold method.

Indeed, several readers claimed that Dorsey Wright changed their lives and their practices when they began to use it. Two criticized Dorsey Wright but said they use a different type of technical analysis. And two said that it’s about time I tell my readers to look for an alternative to buy and hold after watching the volatile and scary markets over the last two years.

I had never heard of Dorsey Wright and became so curious that I called the company and spent over an hour on the phone with Tom Dorsey, one of the founders. That is the subject of my next column, which will appear in the July issue of FA magazine.

Meanwhile, I’d like to bring up the issue here on a4a. I’ve sometimes had a good response to questions to readers, at least good enough to try it again.

Are you searching – or have you already found – an alternative to buy and hold? Let me know!

Comments (4)

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I cannot speak to the benefits of Dorsey Wright, except what I have seen is reasonable in performance, if not a game changer.

However, advisors have a tendency to look for a "method" that works, a packaged approach that can easily be plugged into a financial planning program, takes minimal work to manage, etc. Much like MPT and Strategic Asset Allocation. That is probably best, since most advisors are generalists, not true asset managers. Hence your question, "What have you found?"

We have an absolute returns bias, with a particular hatred of large draw downs, but an expectation of equity like returns. That cannot be done by sitting in bonds and cash because you wish to avoid losses. Our approach does use a bit of technical analysis, plus economic analysis and valuation analysis (the most important), but most of all the careful construction of risk exposures, both idiosyncratic and systematic. That means different strategies, not just different assets.

Fundamentally that allows us to expose portfolios to a diverse set of risk and return opportunities, but without holding assets with little likelihood of adequate long term returns. We can hold only assets and strategies with a reasonable expectation of profitability over the long term, yet still be very diversified and participate on the upside. It has been extremely successful, including in the period from Oct 2007 to March 2009.

To construct such a portfolio does not generally require lots of trading, though we do actively hedge when it is most likely to be useful. A variety of securities can be used in combination. Individual equities, etf's, mutual funds (both active and passive; traditional long only or alternative) hedge funds and managed futures.

While such an approach is not dependent on lots of trading. Most themes we try to profit from are on a 12-36 month time horizon, unless the market makes very large moves that change the risk reward ratio significantly. It does require a firm and well thought out view of what exposures are likely to be profitable. Or, to quote Ken Solow, "you have to do the work." You cannot fully outsource it to any large providers that I see, nor is there a simple piece of software to plug a client into and spit out an allocation.

My suggestion is to find someone who has successfully implemented such a relatively low maintenance, if high in intellectual capital, approach and partner with them. Sit in on their investment discussions and learn. Negotiate a reasonable fee and use areas where you are stronger to barter and possibly eliminate any direct expense. People like us are out there, and not all are afraid to share with fellow professionals.

Lance , June 06, 2010

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We view volatility as an asset class unto itself that's negatively correlated with equity indexes. We believe markets are efficient, but traditional asset-class and buy hold investing is inefficient. We're investing with the goal of achieving high absolute returns independent of the market's direction.Our returns are structured and targeted and we acheive this through the use of a global basket of indexes and option strategies. Here is a link to an article that was published in Index Universe.
http://seekingalpha.com/articl...portfolios

KRH , June 07, 2010

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KRH,

I agree on volatility, and that is certainly one way of taking advantage of being long/short volatility. Some managed strategies are structurally correlated with volatility as well.

The point you make about the return relative to risk is very accurate. While advisors in general should not trade like one, thinking like a global macro fund, with the emphasis on risk management and risk budgeting, as opposed to return, will be much more productive for clients over the long term.

Lance , June 07, 2010

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I am impressed with both of you. But how many advisors are qualifed and confident

enough to do this? Lance, what do you mean by partnering with someone? Do you mean another advisor? How do you do that? KRH, thanks for the link to Seeking Alpha.
Mary

mrowland , June 08, 2010

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