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Painful Fund Statement? Think Positive: There Are Ways to Survive Despite the Lousy Market

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Soon it will be time for another installment of "Read It and Weep," as stock investors open their latest quarterly mutual-fund statements. Even after yesterday's market gains, there is little certainty that what has become a long-running soap opera soon can produce a happy ending.

Indeed, few fund managers attending an investing conference this week in New York showed confidence that an upturn in the stock markets is near. Columbia University Business School Prof. Bruce Greenwald asked attendees, "How many here think we're finished with this market crash?" Fewer than a dozen hands went up, out of about 250 people in the room. If that is how professionals feel about the current environment -- and those at the conference were of the bargain-hunting "value" investing stripe who have fared much better than their growth-stock counterparts lately -- how are less-seasoned amateurs supposed to feel about the market?

One answer is that it is a mistake to assume that a lousy market is always a lousy time to hold, or to buy, stocks. For those investing for the long term, meaning at least five years but preferably more, many investment professionals are saying this may be the time to get in, not out. After all, one hand that went up at the conference belonged to Charles Royce, of Royce Funds, a well-known value investor.

Howard Alter, of Alter Asset Management Inc., in Princeton, N.J., is one financial adviser telling his clients to buy, even though the timing might not feel right. "It's difficult to buy while the market is declining, while the headlines are talking about erosion in share prices and uncertainty of when it will end," he says.

That uncertainty was evident this week in the first-quarter fund-return data, which showed that the average domestic stock fund fell 13%, while only 8% of stock funds avoided negative returns. Noting that markets historically turn up when pessimism is rampant, Mr. Alter adds, "I would encourage investors who got out to use this as an opportunity to start getting their money back into the market."

Here are several strategies that fund managers, financial advisers and other professionals suggest for dealing with a market like this.

Dollar-Cost Averaging

This time-honored technique involves gradually investing a fixed amount of money at regular intervals, an ideal way to tiptoe back into the market for risk-averse investors with long-term investment horizons.

Stewart Welch III, a financial adviser in Birmingham, Ala., is using his own version of dollar-cost averaging to put clients with spare cash into funds that he says have the potential for a big bounce. Instead of investing at regular intervals, his firm buys selectively when the market dips. "I wait for

a day where there's a lot of carnage," Mr. Welch says. Of late, "There are more days like that than the other days."

Among the instruments he suggests are value funds, which typically invest in stocks with low prices relative to the company's earnings. One such fund is Clipper Fund, which is nearly flat for the first quarter but had a 37% return last year. Also on his list are two other value funds, Oakmark Fund and Oakmark Select Fund; they were up 12% and 26%, respectively, last year, and both are firmly in positive territory this year.

Many fund companies offer to help with dollar-cost-averaging arrangements. Investors with mutual-fund giant Vanguard Group, for example, can set up automatic transfers from their bank account, or from one Vanguard account into another.

A Vanguard spokesman says there is never a bad time to start dollar-cost averaging. "Any market -- up, down, sideways -- is appropriate for the strategy," he says. "The investor, however, must maintain the mettle and discipline to carry through in declining markets."

Don't Try to Call the Bottom

"If you have a large chunk of money to invest, it's easy to get paralyzed by a desire to get the timing exactly perfect," says Mark Riepe, senior vice president of Schwab Center for Investment Research, a unit of San Francisco discount brokerage Charles Schwab Corp.

So don't try. Adviser Malcolm Makin of Providence, R.I., thought the bottom had come in November, then in December. Still, he tells his clients that if they are invested in good stocks and good funds, "if you have the courage to hang on, keep hanging on," he says.

He says that if someone has money to invest for the long term, the opportunity is there, even if gains may take more time to materialize. "Is this a good time to buy?" he asks. "I sure think so. But I don't know when we start moving back up again."

Time for a Reality Check

For those not ready to jump all the way back in, there are different approaches. Adviser Iris Dayoub of Dayoub Financial Designs in Savannah, Ga., has been re-interviewing her clients, and discovering that while they thought they could withstand the market's ups and downs, they could handle only the ups. "Many of them thought they were more aggressive than they really were," she says. "This is back-to-reality time."

About 60% of her clients have started to change their asset allocation. They are venturing away from growth stocks, which are expected to show high levels of profit growth, and into bond or value funds. Her firm's investment committee is looking at such funds as Berger Mid Cap Value Fund and Select Funds' Selected American Fund, both of which held up even in value investing's dark days in the late 1990s but are down this year.

On the international side, where many fund portfolios also had a miserable first quarter, some clients are shifting their accounts into Harbor

International, which is more value-oriented, and away from Artisan International and Janus Overseas. "We're reallocating, so the portfolios aren't overly allocated towards growth," Ms. Dayoub says.

Going Bonzo for Bonds

The investors still too scared to get into stocks at all can join the growing ranks of those rediscovering the joys of bonds. Investors withdrew money from bond funds throughout most of last year, but they are pouring new money in now, according to Investment Company Institute, the mutual-fund industry trade group.

One easy way to pick bond funds is to key in on fees. Keep them low, with 0.15% to 0.40% of assets as a good goal, says Jim Peterson, a Schwab Center vice president.

Among the funds with low expenses, consider New York teacher's investment group TIAA-CREF's Bond Plus Fund, a bond index fund with expenses of 0.30%, and Vanguard Group's bond index funds, whose expenses are lower still. Those with good records include Hartford Bond Income Strategy, which had an 11% return last year and is up about 3% this year, but has fees of 1.24%.

In addition to expenses, Mr. Peterson says the two other most important factors in selecting a bond fund are its risk level and past investment performance. Investors can check risk by looking at a fund's prospectus or a fund data Web site, which will include a bond fund's average credit quality. Anything below triple B is considered below investment grade, and thus a riskier proposition.

While a shining track record is no guarantee, Mr. Peterson said his study, which examined bond-fund performance from 1992 to 1999, found that "bond funds that did well in the past also did well in the future," he says.