The MoniResearch Newsletter

Performance Rankings of Market Timers

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JACK BE NIMBLE, JACK BE QUICK...

This is the opening line of an old English nursery rhyme. It's relevance to the subject matter of this newsletter will become abundantly clear by the end if this article in which I introduce a newcomer. I'd like to introduce Safe Harbor Management Corporation. This is a significant addition to the group of market timers we track, and I think it will be worth your time to read this section carefully.

The portfolio manager for Safe Harbor is Richard M. Paul, and it is he who calls the signals. As you will shortly see, he has done an outstanding job.

We were contacted by Safe Harbor shortly after they saw our name in the Money Magazine article. Safe Harbor is a very small firm at the present time and I was unaware of their existence. They asked what would be required from them in order to appear in the MoniResearch Newsletter. I explained that the only requirement was that they be bona fide market timers. I also explained the difference between the 'A' and 'B' groups, and inquired about the particulars of Safe Harbor to see where they would fit.

It was clear that Safe Harbor belonged in the 'B' Group. The firm was incorporated in April 1986, and began managing client money in January of this year. Assets under management are under $1 million.

But now the interesting part of this story begins to unfold. Rich told me that he had been managing his IRA account since 1979, and that he had continuous statements from the mutual funds that showed all activity in this account. I asked him to send them to me. It is quite unusual for a 'B' group market timer to be able to provide continuous customer statements for an 8-year period, as you can confirm by reading the footnotes to the performance table.

When the statements arrived I was surprised at the bulk of the package. The reason soon became evident, and that brings us to the second unusual facet of Safe Harbor. On average, Rich switches 37.8 times per year. In other words, a switch is executed every 6.75 trading days! Again, if you glance at the performance table, you will see how different this is from average.

Of course, when I first removed the statements from the package in which they came, I did not yet know the exact value of these numbers -- I just knew that I had something quite different on my hands.

Beginning with August 1982, five years ago, I started tracking through the statements, checking for continuity, and recording the dates of the buy/sell signals. I found that Rich used a wide variety of mutual funds. Many market timers use a collection of mutual funds, and the methods we use reflect their performance reasonably well. We footnote the performance table to this effect by saying that by timing individual mutual funds, a market timer can be expected to have slightly better performance than we report.

However, there is a significant difference between that situation and what we have here. Most of the market timers who use a variety of mutual funds switch them all on the same day, or within several days of each other. (A rising tide, i.e. market, lifts all ships, albeit at somewhat different rates.) However, this doesn't apply to Safe Harbor because some of the funds they use do not correlate well with the U.S. equities market. For example, gold funds, bond funds, contra funds, and overseas funds.

My first reaction was to call Rich and tell him that there had been a misunderstanding, that we could not include Safe Harbor in our newsletter because they did not fit our mold. We have done that in the past with firms that were not really market timers in the classical sense. (Whether we ***should*** have a special mold to fit these kind of firms is another matter that I don't want to get into right now.) However, I was intrigued by the agility with which Safe Harbor moves money around and I wanted to see how good they were at it.

For a trial, I selected the one-year period from April 9, 1986 to April 9, 1987. This period corresponds exactly to the one-year period we used to rank the 'B' Group in the May/June issue of this newsletter. I computed Safe Harbor's performance for this same period using <u>the exact mutual funds</u> that they had used. No approximations. The result --- hold your hats --- 56.8% for this one year, after management fees!

So, what to do now. I felt it was important to bring this kind of performance to your attention. To call up Safe Harbor and tell them that I could not include them because they did not fit my mold would be incredibly obtuse.

On the other hand, I am not about to change the methodology we use to compute performance because there are valid reasons for preferring it for the great majority of market timers.

So, as with many things in life, a compromise was indicated. I have made the following approximations and assumptions regarding Safe Harbor. When a switch was made into a fund that was well correlated with the U.S. equities markets, I left it alone. When a switch was made into a fund that was clearly not so correlated, I assumed that the money had been moved into a money market fund instead. A really tough decision was how to handle switches into overseas funds; they are partially correlated with the U.S. market. There have been occasions when one was rising and the other was falling. My decision? I called them 'buy' signals.

And this is the basis for Safe Harbor's ranking in the performance table later in this issue. Clearly the performance figures shown for Safe Harbor are substantially less than reality. It is not a happy situation and does not sit well with me. However, my rationalization is as follows:

- Safe Harbor clearly shows up as one of the best overall performers, even though we are not giving them their full due. They are first in the 1-year and 3-year categories, and seventh in the 5-year category (where they were up against mostly hypothetical signals of the other market timers). Therefore the conclusion must come through to even a casual reader that they are worthy of attention. And all this with real signals.

- It would be unconscionable to leave them out.

- Having read the foregoing material, you are able to mentally compensate for the fact that Safe Harbor is a round peg in our admittedly square hole.

Before leaving Safe Harbor, there is an obvious question waiting in the wings -- how do they do it? A partial answer is contained in a 9-page writeup that Rich Paul sent me on this subject. Obviously, we cannot reproduce that entire document here, but here are the highlights.

Rich follows both fundamental and technical indicators. The fundamental indicators tell him which technical indicators to look at for making the actual buy/sell decisions. Or, to quote from the writeup, "In effect, the technical indicators comprise the 'tool box' from which the proper 'tools' for the appropriate time are drawn upon by the advisor for evaluation and making trading decisions."

The writeup mentions 30-40 different indicators, divided into the following categories: Momentum, Sentiment, Monetary and Other. According to Rich, "Momentum indicators are the key indicators used in generating. . .buy and sell signals. These are the only indicators that [can be used] independent of the other types of indicators to generate trading decisions." Some of the momentum indicators are confirmations or divergences of market trends, moving averages, rate of change, velocity, acceleration and relative strength.

Performance Ranking

Group being ranked : **Group B**

Issue : **Sept / Oct 1987**

Period ending : **August 14, 1987**

1, 3, and 5-Year Performance (Annualized Rates of Return)					
Timer (Alphabetically)	Last 5 Years	Last 3 Years	Last 1 Year	Avg switches/yr (for 5-yr period)	Notes
Allocation Advisors	24.2 %	24.9 %	26.6 %	2.2	1
Chicoine, Halliburton & Shannon	14.7	21.3	24.4	5.0	4
Clark Capital Mgmt. Group	27.8	22.6	14.1	8.0	5
Flexible Plan Inv. Ltd.	28.8	25.9	25.8	2.8	6
Forbes Portfolio Mgmt.	26.7	25.3	29.7	7.4	7
Hensley, Griffin & Co.	30.8*	26.2	14.0	4.6	15,19
Kensington Inv. Group	29.4	25.5	25.6	2.6	18
Paul A Merriman & Assoc	17.5	14.4	5.1	3.2	5,10
Money Mkt Buy/Hold Strategy	8.3	7.5	6.0	0	13
National Investment Advisors	29.8	25.3	31.9	0.8	9,17
PSM Investors	20.1	23.3	28.7	2.4	2
Provident Mut. Fund Mgmt.	28.9	27.9	37.3	0.8	2,11
S&P-500 Buy/Hold Strategy	31.5	31.6	40.1	0	13
Safe Harbor Mgmt. Corp.	26.9	29.1*	40.6*	37.8	16,17
Schield Mgmt Co	20.0	19.1	21.7	2.2	5
T-Bill Buy/Hold Strategy	8.0	7.3	5.7	0	13,14
Triad Fund Mgmt	22.7	15.8	10.8	2.0	12
Steve Ventimiglia	19.8	19.2	16.4	1.8	8,15

* Leader for this time period

Notes:

First, we will cover some notes that pertain to the table as a whole, and then we will list the footnotes that pertain to the individual market timers.

For 'buy' signals, the money is placed in the Standard & Poors 500 Index, which has been adjusted for dividends. During defensive periods, money is invested in a hypothetical money market fund. The rate paid by this fund is determined by taking the 91-day T-Bill rate and adding a quarter of a percentage point. For example, if the T-Bill rate is 5.0%, the money market rate would be 5.25%.

The column labeled "Annualized Pct Gain" is net of management fees, which are applied as follows. Almost all market timers have a sliding fee schedule based on the size of the account. The larger the account, the smaller the percentage taken. We assume a $50,000 account for this purpose, and use the percentage for each market timer associated with an account of this size. If the minimum account size is greater than $50,000, we use the percentage for that timer's minimum account.

The rate-of-return figures are calculated as follows. First, the total appreciation in the portfolio is calculated for the entire period under study, after deducting management fees on an annual basis. Then, an interest rate is computed, which when compounded annually, would result in the appreciation actually observed.

The number of "Switches per Year" is an average figure which is obtained by taking the total number of switches for the most recent 5-year period and dividing by 5.

Footnotes pertaining to individual market timers --

1. The principal of Allocation Advisors is Scott Smathers. Mr Smathers was formerly a principal of Smathers & Co, one of the participants in the 'A' group. However, Smathers & Co is out of business. Allocation Advisors uses the same model that was formerly used by Smathers & Co. Signals from that model have been fully substantiated from continuous customer statements. The reasons that Allocation Advisors are not in the 'A' group are: a) They have been in business only since 1985; b) They have less than $20 million under management.
2. No substantiation offered for signal dates.
4. Chicoine, Halliburton & Shannon submitted customer statements for 3 disjoint periods totaling 18 months. In-house buy/sell orders were submitted for 2 periods totaling an additional 12 months. The remainder of the 5-year period is unsubstantiated.
5. Signal dates are supported by a letter from a CPA firm, or an attorney, or an actuary, or similar.
6. For Flexible Plan, signals prior to 11/9/83 are hypothetical. Signals since this date are supported by continuous customer statements.
7. For Forbes, signals prior to 1/1/86 are hypothetical. Subsequent signals are supported by continuous customer statements.
8. Prior to 1986, Steve Ventimiglia was a principal with Investment Timing Consultants where he used his proprietary model. For that period of time, his signal dates were supported by customer confirms from a variety of accounts. There were no continuous customer statements to prove lack of activity during the intervening periods. In 1986, he joined

9. National Investment Advisors (NIA) was formed in February 1986. Prior to this, the principals of NIA worked under the auspices of AFC Advisory Services (one of the market timers in our 'A' group). The customer statements provided by NIA, which covered 5 years, represent customers who were originally AFC customers.

10. Merriman's signals prior to 7/31/83 are hypothetical.

11. Provident has been doing timing for clients since late 1984. Prior to that, one of the principals traded for his own account and for friends.

12. For Triad, signals prior to 1983 are hypothetical. Beginning with 1/1/84, Triad's signals are corroborated by continuous customer statements.

13. No management fee was imposed because no one *needs* to pay a management fee for this kind of strategy.

14. T-Bills are rolled over every 91 days at the prevailing interest rate (i.e., discount).

15. For these firms, the signals do not always represent 100% switches of the funds available. Often, only a portion of the money is switched between the money market fund and the aggressive fund.

16. For Potomac, continuous statements for the entire 5-year period were submitted for the account of the principal who does the timing.

17. These firms time individual mutual funds rather than the overall market. Their model is optimized to derive the maximum return from each particular mutual fund. Our ranking methodology, however, standardizes comparisons by eliminating all factors other than timing, and for this reason we use the S&P-500 Index as the aggressive vehicle. This places these firms at a disadvantage. Had they optimized their model for this index, their performance would most likely be higher than that shown in the table.

18. For Kensington, signals prior to 10/10/84 are hypothetical. Continuous customer statements were provided from 5/20/85 to present.

19. For Hensley Griffin, signals prior to 7/1/86 are hypothetical. Continuous customer statement were provided from this date forward.

20. The management fee for Ayres & Co is only a flat 0.5%. However, this firm invests primarily in load funds. Therefore, to make the performance figures comparable to the other firms, we have arbitrarily used a 2.0% fee.

21. Bond Timing Services began timing equities in January 1984. (As their name suggests, they have been timing bonds for over 5 years.) No figure is shown for the 5-year performance because BTS does not believe in the concept of hypothetical signals.

22. For SDS Investment advisors, signals prior to 8/19/86 are hypothetical. Signals since that date are supported by continuous customer statements.

23. Sentinel Asset Management was founded on 4/1/87. Signals prior to that date are claimed to be generated by the same model in use today, and that the model has been in actual operation since October 1974. However, no evidence was submitted for those earlier signals. Signals since 4/1/87 are supported by customer statements.

24. For Vari, all signals are supported by continuous customer statements.