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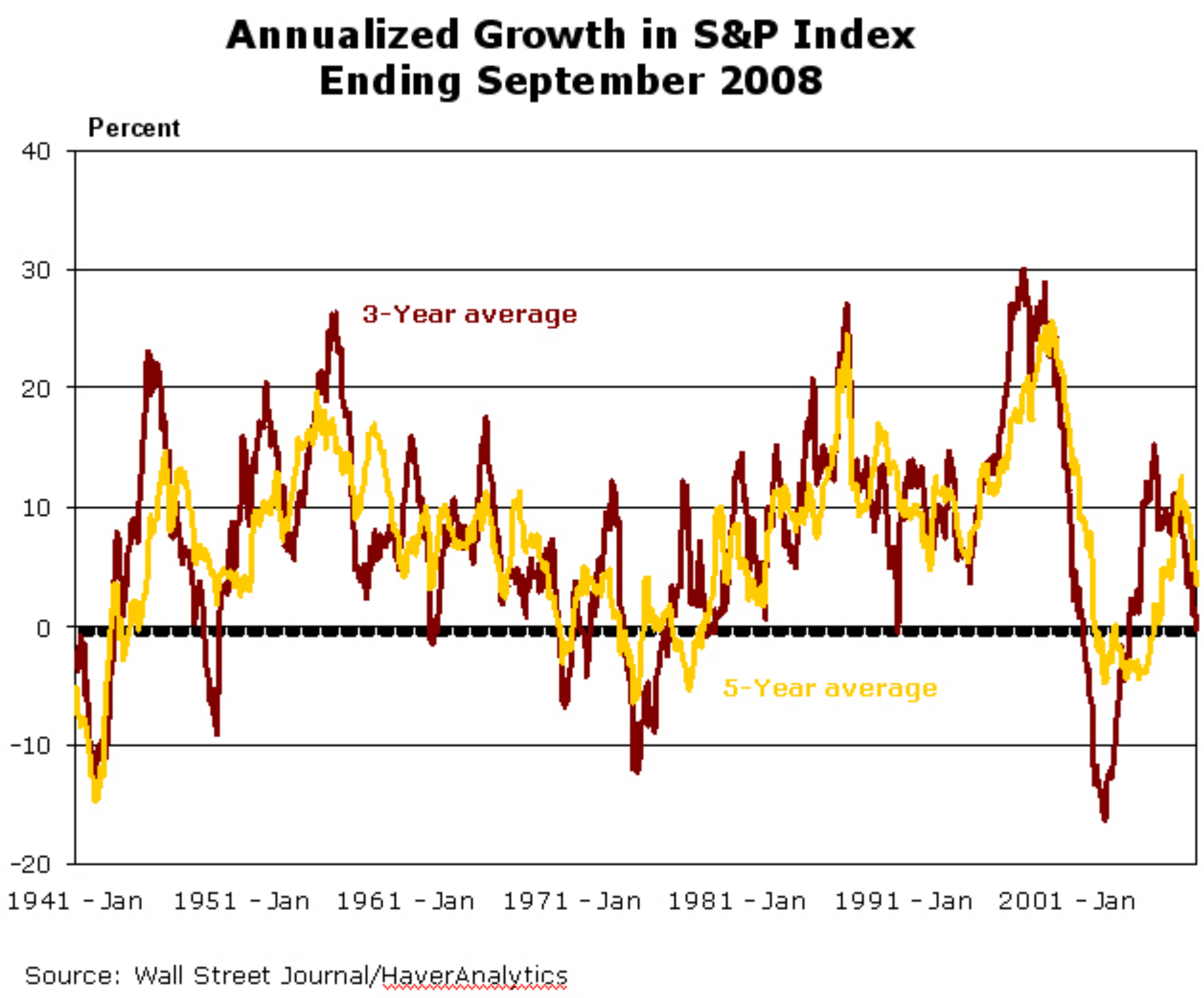
The end of buy and hold?

I trust you will not judge me guilty of overstatement if I say that good news from equity markets has been hard to come by of late. So rough has been the ride that at least one (quite) famous pundit-analyst has taken measure of the landscape and concluded that the time has come to abandon the venerable "buy and hold" investment advice generally offered ordinary savers:

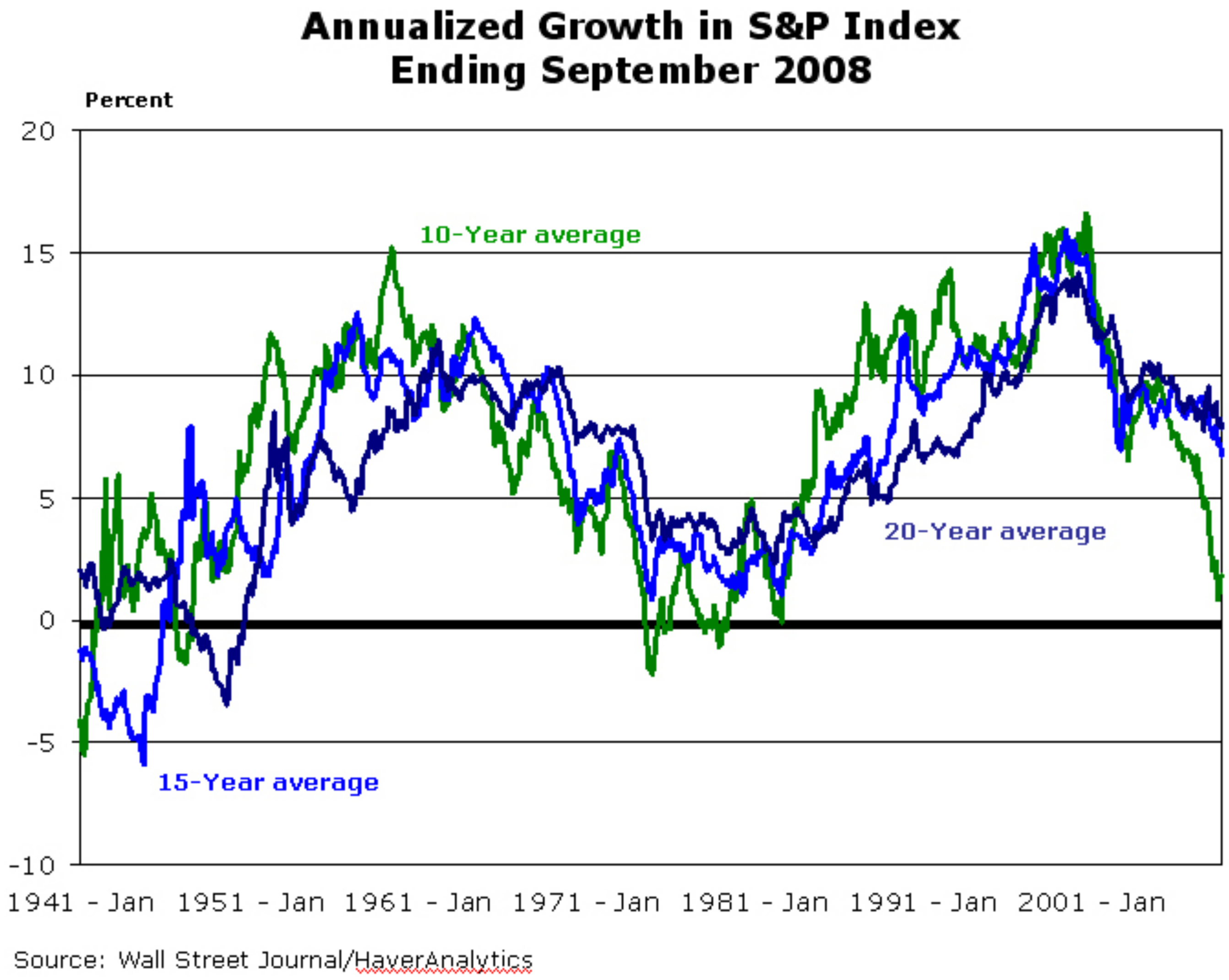
> "It's time to unlearn a common myth about investing," Jim Cramer told viewers on Monday. "The best way to invest is not to buy a bunch of stocks and just sit on them."

As is usual in such cases, it is useful to have a look at the record. Though it's not entirely clear what quantity constitutes "a bunch of stocks," one reasonable definition would be a broad stock index. With that in mind, here is a look at the annualized three- and five-year rates of change in the S&P 500 index going back to 1941.



This is not the *return* on an investment in the index, of course, as holding the portfolio of equities in the index would also generate dividends over the holding period. But it does give some sense of how the recent past compares with the more distant past. While it is true that things look bleak at the moment, this is hardly an unprecedented circumstance. If the buy-and-hold strategy had merit before, it really isn't that clear things had changed that much through this past September.

You might reasonably argue that buy-and-hold really applies to horizons that extend beyond five years. Here, then, is the same sort of chart as above with index growth for 10-, 15-, and 20-year holding periods.



True enough, the past 10 years have been a little ragged, though again not really unprecedented. And if you were lucky enough to be a long-term saver—that is, held the index for the past 15 to 20 years—good for you. (And note that returns over these horizons are, not surprisingly, substantially less volatile than over the shorter periods.)

Ok, I hear you. Why did I conveniently stop just short of the dramatic decline in the stock market since September. Sure enough, things look substantially worse when the stock market loses over a quarter of its value in a month. For the sake of argument, let's assume that the S&P average for October ends up at 900, or near the low so far this month. Redoing the three-, five-, 10-, 15-, and 20-year growth calculations would yield annualized rates of –8.9 percent, –2.8 percent, –1.4 percent, 4.5 percent, and 6.1 percent, respectively. Even with the major reversal of the last month, the implied returns on the 15- and 20-year holding periods look pretty good.

Of course, the "buy-and-hold is dead" idea relies on the presumption that the next 10 years are going to look a lot like the last 10 years. Only time will tell if the current growth rate on the three- to10-year holding periods is a trend, or just evidence that you won't do so well when you get out of the market at exactly the wrong time. I don't know what the answer is—and I don't offer investment advice—but the verdict of history is pretty clear.

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