OFG FINANCIAL FOCUS
Second Quarter, 2014

It's Always Something—And Then It's Nothing

On December 10,1987—just as the equity market was limping along the bottom of a bear market whose key feature had been the biggest one-day crash in stock prices of all time—the NASDAQ stock market suddenly ceased to function, and continued to be off the air for close to an hour and a half. It seems that a squirrel had chewed through a power line that ran to NASDAQ's computer center in Trumbull, Connecticut.

Among serious aficionados of oddball market outages (a cult of which your present correspondent is a charter member), this episode is designated Squirrel One, because on August 2, 1994, the exact same thing happened, although this time it took only 34 minutes to fix. Inevitably, we call this Squirrel Two, not least of all to make clear that the miscreants were two different squirrels—both of whom were electrocuted.

These and many other dramatic but ultimately meaningless market malfunctions were brought to mind by the three-hour shutdown of NASDAQ on August 22, which financial journalism covered in predictably apocalyptic terms. Even the normally rational Wall Street Journal, in its lead story the next morning, termed it "an unprecedented meltdown for a U.S. exchange that paralyzed a broad swath of markets and highlighted the fragility of the world's electronic backbone."

And if you blinked, you missed it.

That is, if you were at the beach with your grandchildren that lovely summer afternoon, came home too tired to turn on the television, and slept soundly until the following day, the first you heard of this "unprecedented meltdown" (which was, in point of actual fact, neither) was over your morning coffee. And when you thereupon checked your investments, if such is your wont, you discovered that ...nothing much had happened. The market had even managed to close a little higher on the day.

Permit me to suggest that there's a really good lesson in this for the long-term, goal-focused investor.

Indeed, it is for all intents and purposes the same lesson of such precedents as the May, 2010 "flash crisis," in which for largely technical reasons the Dow Jones Industrial Average went down 600 points in five minutes, and recovered all 600 points in the following 20 minutes. (Now that—however evanescent—was a meltdown.)

Spelled out as clearly as I know how, that lesson is temporary dysfunctions in mechanisms of stock trading—and the resultant gyrations, if any, in stock prices—do not, because they cannot, alter the intrinsic value of companies. The long-term, fundamental investor in companies is therefore unaffected by these glitches, nor indeed by any of the vicissitudes of trading—as distinctly opposed to investing in—common stocks.

The value of quality common stocks in the long run is essentially a function of the earnings, dividends and cash flows of the underlying companies, and is not lastingly distorted by computer malfunctions, human error...or squirrels. No one is more keenly focused on this incontrovertible fact than Warren E Buffett—America's most admired yet least imitated investor—who famously if somewhat hyperbolically said that it wouldn't affect what he does if the stock market were to close for three years. While you and I might not be able to wait three years in order to draw from (or add to) our long-term investment portfolio, we most probably can wait three hours, as on August 22. (or even a couple of days, as we had to do when markets remained closed after 9/11 and Superstorm Sandy.)

Chronically unable as I am to quit while I'm ahead: perhaps we might venture to press this point just a bit further—into the ominous nether world of "high frequency trading." Fear and loathing of equities have a hard time finding a place to hang their hat in these days of new all-time market highs. But one of the last bastions of pessimism seems to be the illusion that a dark horde of computer algorithms, trading furiously against each other to capture price differentials of pennies per share, can meaningfully distort equity values—and indeed somehow "rig" the market itself against the poor, defenseless small investor.

If you're following the logic set forth so far in this little essay, you will be inclined to suspect that this can't be true. Again, never knowing how to quit while I'm ahead, I would offer one man's opinion that it is in fact impossible. My blissfully unscientific guess is that in the long run, all that algorithmic stock trading probably ends up canceling itself out— with some computers winning a little as others lose a little on any given day—while good companies go about their fundamental businesses. (By the way, when instantaneous trading becomes such a mania that a major online discount broker starts advertising one-second trade executions to the retail investor on television, you know the gargoyles have taken over the cathedral.)

And as to whether anybody or anything can ever "rig" a fifteen trillion dollar global market: you'd have to explain to me how that might be done, speaking slowly and using very small words that you're sure I'll understand.

In the end, as with so many other issues in investing, the critical question is whether your personal view of the financial world is essentially focused on stock prices in the short term, or on the fundamentals of quality companies in the long term. Next time the market goes on the fritz—electronically, emotionally, or even both—you may want to consult your financial advisor, just to get your focus checked

And watch out for those squirrels.

WHAT DOGS KNOW

When 8-year-old George arrived home from school, his father took him for a long walk where they found the shade of a large oak tree to sit under. It was there that George's father began the complicated task of explaining why Banjo, the family's beloved cocker spaniel was no longer with them.

"I know it may not seem fair," George's father said as he placed a hand on his son's hand, "but the truth is dogs don't live as long as we do."

"I think it's fair," little George replied placing his hand on top of his father's while rubbing it gently.

"When people are born we have to learn how to be good and do the right thing and love everybody and always play nice," George said. "But dogs already know that so they get to go to heaven sooner."

Adapted from the Sunny Skyz website

Focus is a matter of deciding what things you're not going to do.

JOHN CARMACK

BREAK THOSE CHAINS

A man vacationing in Africa was stunned to encounter a herd of elephants walking down a road in an orderly procession being led by a trainer. The animals were attached by a thin chain linked around their front left leg.

"I don't understand," the man said to the trainer. "How can these powerful beasts be contained by such a weak line?"

"We use a similar chain to restrict their movements when they are young," the trainer replied. "They are 'taught' to believe that the chain will restrict them even though they are bigger, stronger, and could easily break free."

The man was left speachless. The elephants were imprisioned by cruelty and conditioning from knowing their own power.

Negativity, fear, discouragement, lack of self-confidence and support are just a few tactics we employ to "train" ourselves and others to embrace less than what we are capable of. But why should we live under such constraints? Wouldn't it be better to encourage the idea that our potential is limitless and affected only by our level of enthusiasm and persistance?

Adapted from the Inspirational Stories website

Why does getting ahead always have to involve getting up early?

ELIZABETH JANE HOWARD

John D & Kelli C. Webb
Eric Stewart
Jordan Webb
600 S Santa Fe, Ste. C
Salina, KS 67401
Local #820.8161 or 888.756.6670
webbandassocinc@ofgfinancial.com
www.webbandassociatesfinancial.com