THE BEST OF THE VALIDEA HOT LIST – 2008

HIGHLIGHTS OF THE TOP INVESTING COMMENTARY THROUGHOUT THE YEAR

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Staying The Course Paying Off

Excerpted from the May 30th, 2008 Validea Hot List

This week's news helped the market recapture some of the losses it had posted last week, and the major indices ended up in the red, but not far from where they had started the fortnight. The Hot List fared a bit better, finishing closer to even. The portfolio has now beaten the S&P 500 in seven of the past nine newsletter periods, and is ahead of the index by 9.5 percentage points this year.

In fact, since February, the Hot List has shown the form that it exhibited in its first four years (including the partial year of 2003, since it was introduced in July of that year), when it posted returns that at least doubled the S&P 500 each year. The value-focused portfolio has bounced back strongly from last year's underperformance, which was caused by a rare prolonged momentum-driven market. The Hot List has now gained about four times as much as the S&P since its inception (159.1 percent to 39.8 percent).

While those numbers are nice, one question you might be asking is why we didn't use a different strategy during last year's momentum-driven market. It would seem simple in retrospect: Once we realized what the market condition was, why not just switch to a momentum-type strategy, like our William O'Neil model? And then, once the momentum run ended, switch back to the Hot List approach?

It sounds great in theory -- but in reality, it's a plan that is fraught with holes. Looking back at the pattern of the past year or so, the momentum push started sometime last February or March. But while a general trend like that becomes apparent after the fact, it's much less clear-cut when you're in the middle of it -- and, on a week-to-week or month-to-month basis, there might not even be an observable trend. While momentum significantly outpaced value last year, there were certainly days, weeks, or perhaps even month-long periods where it didn't. So, do you make the switch to a different strategy after it has outperformed your original strategy for one month? Two months? Six months? And when do you switch back to your first strategy? After it has re-taken the lead for a single month? Three straight months? Six months?

Unfortunately, more often than not investors who try to switch strategies based on recent performance end up buying high and selling low. If you'd jumped on the momentum train after it had established itself last year, you might have caught some of the tail end of the run-up. But then you'd have crashed this year with little, if any, warning, as deep value approaches like my Benjamin Graham and Warren Buffett models quickly re-established themselves and momentum stocks took a nosedive.

Someone who knows a good deal about strategy jumping is Joel Greenblatt, the hedge fund manager and author who laid out a simple two-step way to beat the market over the long term. By focusing solely on earnings yield (similar to the inverse of the P/E ratio) and return on capital, Greenblatt produced a strategy that would have gained two-and-a-half times as much as the S&P over a 17-year period. He was even kind enough to disclose the strategy in a book that was published in 2006. Follow the two-step strategy, and you can more than double the market over the long haul -- if you're willing to stick to it. Seems like a pretty good deal, right?

Well, while Greenblatt's strategy is about as simple as it gets, there's a problem: Many people won't follow it. In an article in Kiplinger's magazine in March, Fred W. Frailey writes that evidence in blogs, Web discussion, and e-mails from readers shows that many people who began using Greenblatt's "Magic Formula" have already lost faith, because the formula's results weren't the greatest recently. This, despite the fact that Greenblatt stated repeatedly in his book that the strategy will underperform the market about one of every four years, and that, to reap its rewards, you'd have to stick with it for a minimum of three to five years. Greenblatt warned people ahead of time that they'd be tempted to jump ship when the going got tough, and made a convincing case for why they should stay the course. But even with that warning, it seems people have started using the strategy, and then done exactly what Greenblatt said not

to do when they ran into short-term underperformance.

The reason for this is, simply, that we are human. When we see our portfolio dropping in value, we get fearful -- fearful that we'll lose more money than we'd like, or even that we'll lose everything. So many people give in to those fears, jumping on to a new "hot" strategy, only to find that they've sold low and bought high. That's why staying disciplined and sticking to a proven strategy is one of the most critical things you can do as an investor. While the Hot List has performed remarkably well over the long term, I have no doubt that it will have bad months, and even bad years, sometime in the future. But because the strategy is a proven winner that targets solid companies whose stocks are selling at good prices, I'm also confident that the "up" months and years will be much more frequent than the "down" months and years. No strategy can beat the market every month or every year -- even Warren Buffett, Peter Lynch, and all of the other gurus we follow have had down periods. But by sticking to a proven strategy, you tilt the odds nicely in your favor. And, just as we've seen over the past five years with the Hot List, that will result in some very nice gains over the long haul -- the type of gains you likely won't see if you're playing the strategy-jumping game.

Fear Factors

Excerpted from the June 27th, 2008 Validea Hot List

Two of the big factors leading to the market's recent stumbles have been inflation concerns, and analyst downgrades that hit financials hard. But while these issues have been spooking a lot of investors, they are much less of an issue for long-term investors than many think. Here's why.

Analyst Downgrades
First, let's take the downgrades. In addition to predicting some more big writedowns from Citigroup and Merrill Lynch, an analyst at Goldman Sachs cut his rating for U.S. brokerage companies from attractive to neutral this week, saying that a financial recovery may well take longer than previously thought, MarketWatch reported.

Downgrades have a scary ring to them, so, not surprisingly, Citi, Merrill, and a host of other financial stocks tumbled Thursday after news of the Goldman rating change. After all, analysts are supposed to be the experts; they have far more time to research firms and far more access to companies' higher-ups, so in theory they should have the best idea of where stocks are headed. The problem, however, is that while analysts may be nice, intelligent, well-meaning people, they're also human. And as humans, they're subject to all of the same emotional failings that confront average investors.

James O'Shaughnessy, one of the gurus upon whom I base my strategies, wrote extensively about how humans are prone to misjudgments. People prefer good stories to cold, hard, data, O'Shaughnessy noted, and analysts are no different. "A market analyst who has visited a company and knows the president may ignore the statistical information that tells him a company is a poor investment," O'Shaughnessy wrote in his book *What Works On Wall Street*. Presumably, the reverse can also be true.

David Dreman, another of our gurus, also was skeptical of analysts' findings. In fact, Dreman stated in his book *Contrarian Investment Strategies* that "there is only a 1 in 130 chance that the analyst's consensus forecast [of a firm's earnings] will be within 5 percent for any four consecutive quarters. . . . To put this in perspective, your odds are ten times greater of being the big winner of the New York State Lottery than of pinpointing earnings five years ahead.

The great Benjamin Graham also raised questions about analysts predictive powers. In his book *The Intelligent Investor*, Graham said analysts hired by brokerage houses "are greatly handicapped" by the fact that they are really expected to not only be company analysts, but also stock market analysts. "When they are asked whether a given common stock is 'sound', the question often means, 'Is this stock likely to advance during the next few months?'" Graham wrote. "As a result many of them are compelled to analyze with one eye on the stock ticker -- a pose not conducive to sound thinking or worthwhile conclusions."

In the end, the Goldman analyst who downgraded brokerage firms could prove to be right in this particular instance, or he could end up being wrong. But that is, in a sense, beside the point. The key here is that over the long term, analysts quite often miss the mark. Basing your investment decisions on their recommendations instead of cold, hard fundamentals may work for you today, tomorrow, or next week, but over the long term it doesn't significantly put the odds in your favor. In the end, it's probably no more of a sure thing than relying on your own instincts -- and neither is a good way to pick stocks.

Inflation
Now, on to those pesky rising prices. Unfortunately here, some of the fear in the marketplace is on the

money: Rising gas, food, and commodity prices can indeed be a problem, cutting into disposable income for consumers -- and profits for investors. And that's exactly why it's so important to stick with stocks.

Stick with stocks? But doesn't inflation mean that profits for companies will decline, which will lead to their stock prices declining? In the short term, that's a possibility (though by no means a certainty). But over the long term, stocks have actually proven to be inflation fighters.

A great source of information on this is Dreman. He wrote that inflation-adjusted returns for stocks have consistently outpaced those of bonds and T-bills since the start of the 1800's. The gap has widened since the mid-1920's, when inflation began to have a more significant impact.

From 1946-1996, according to Dreman, compound returns after inflation for stocks were better than those of bonds 84 percent of the time if your holding period was five years; stocks outperformed T-bills in 82 percent of those five-year periods. Using 10-year periods, stocks beat bonds 94 percent of the time and T-bills 86 percent of the time. When you look at 20-year holding periods, stocks beat both bonds and T-bills 100 percent of the time. A big reason: Stocks, unlike bonds or T-bills, have the ability to produce increasing earnings streams, which has made them safer from inflation than fixed investments over the long haul.

All of this isn't to say that inflation can't have an impact on a company's profits, or that fear of inflation can't hurt stock prices in the short term. In fact, given all the hype surrounding oil prices and inflation, it might seem like a good idea to jump out of the market for a bit, and wait until inflation decelerates. There's a problem with that tact, however: Research shows that you may well end up missing out on some very good opportunities.

According to the National Bureau of Economic Research (the group whose duties include officially declaring when recessions occur in the U.S.), multiple studies indicate that investors may fall prey to what is called "The Inflation Illusion". Essentially, the inflation illusion occurs because people make projections of earnings growth rates by extrapolating historical growth rates, even if those historical growth figures came during times when inflation was very much different.

If you've just come out of a period of high inflation, for example, and you use nominal historical growth rates to predict future growth, there's a good chance you'll expect higher growth rates than you actually get, because inflation is now lower. Conversely, if you're using historical growth figures from a period of low inflation to predict growth for future years, you may well underestimate the nominal growth rate if those future years feature higher inflation, which should increase nominal profits.

What this could mean, according to NBER, is that "stock prices are undervalued when inflation is high, and can become overvalued when inflation falls." So, while investors often get fearful when inflation increases, it can actually be a good time to bargain shop.

Whether you're dealing with inflation, analyst rating changes, or any other stock market issues, there's another key point to keep in mind, and it's one I've referenced many times before: We are dealing with a market of individual stocks, not a single, monolithic stock market. Even if an analyst is generally correct in downgrading an entire industry, that certainly doesn't mean that every stock in the industry is a bad one. And while high inflation can negatively impact some companies, it by no means will slam every stock. There will always be good buys out there -- often in places that are most beaten up. By sticking to the numbers -- a stock's fundamentals -- you give yourself the best chance of finding them.

Three Cheers For "The Death of Value Investing"

Excerpted from the August 22nd, 2008 Validea Hot List

While the Hot List's performance so far this year has been strong, there is some evidence to suggest that it might be headed for even better times. One big reason has to do with the fact that my models collectively have a value bias. Of the 12 guru-based strategies tracked on this site (that counts James O'Shaughnessy's growth-value hybrid as two strategies), six are fairly deep value approaches. In addition, most of the strategies that focus on fast-growing stocks also incorporate critical value elements -- the Peter Lynch model's P/E/Growth ratio and the O'Shaughnessy growth model's price/sales ratio come to mind.

Because of that, my models are designed to perform best when value stocks are being rewarded. And, while the models have been performing well this year, we still haven't hit the kind of value-driven climate in which they should really excel. In fact, as of Aug. 11, growth stocks were 15.5 percentage points ahead of value stocks in the market this year, Bloomberg's Michael Patterson and Eric Martin wrote recently -- the largest such spread since 1980. That puts growth stocks on track to beating value stocks for the second year in a row, something that has only happened five times in the past 56 years, Patterson and Martin stated (citing data from Societe Generale).

For some, that's reason to panic. The prolonged run for growth/momentum stocks has even led to some pundits to question whether value investing is as good as gone. In the past few weeks, for example, I've seen such headlines as "The Death of Value Investing", and "Is Value Passe?"

To me, however, headlines such as those aren't a reason to panic; instead, they're a great sign. Whenever something swings far, far to one side of the Wall Street pendulum -- whether it be it a prolonged shift from small-cap to large-cap, international to domestic, or value to growth -- it isn't long before the pendulum swings back. And, like a pendulum, the more extreme things get, the more extreme the bounce in the other direction will be. In other words, when newspapers and magazines start talking about the "death" of value investing, it's probably a good time to be a value investor, because the pendulum is way toward the growth side and getting ready to swing back sharply. As David Dreman, the great contrarian guru I follow, told Bloomberg's Patterson and Martin, "The more [value] underperforms, the more it normally snaps back. The probabilities are very strong we'll have a major upswing."

The data backs up this notion. According to Patterson and Martin, in the five cases in which growth beat value two years in a row since 1952, value vaulted back into the leadership position shortly thereafter, outpacing growth stocks by an average of 17 percentage points per year for the next seven years.

Still, no matter how much long-term data is out there, the majority of investors will always succumb to the fear of short-term events, and the idea that a hundred years of history can be thrown out the window because things are now "different". In the late 90's, we heard how the Internet had fundamentally changed the way the stock market worked; things were "different" now, and the Web had opened a world of infinite profits. Early last year, we heard how developing nations like China and India had so much more room for growth that the profit stream was near-infinite; things were "different" now, and stocks from these emerging markets could keep going up, and up, and up. How did those two "different" situations work out? Well, we all know how the Internet boom came to a crashing end. And as for the unstoppable emerging market stocks, it turns out a lot of them were, well, stoppable.

So why, with all of the historical evidence that value investing beats growth over the long haul, and that value investing tends to bounce back very strong after periods of underperformance, are many investors and pundits still shying away from value -- and even questioning whether the approach will have any relevance in the future investing world?

James O'Shaughnessy offers quite a bit of insight into this sort of phenomenon. In his book What Works On Wall Street (which I use as the basis for my O'Shaughnessy models), O'Shaughnessy writes that humans tend to rely on their own personal experiences rather than historical statistics. One example he cites is the tech boom and bust of the late 1990s. "Every bit of evidence that [investors] had personally experienced suggested that it was different this time, that a new era had dawned, and that only those who implicitly rejected history would do well going forward," he wrote. "Only after two and a half years of "new personal experience" did the hapless intuitive investor learn that alas, it wasn't different this time."

In the current stock market, things aren't really that different either. Sure, the specifics have changed; they always will. But the broad concepts and cycles underlying the stock market remain the same. The notion that the decades and decades and decades of alternating value and growth cycles has suddenly reached an endpoint where growth is king is short-sighted, if not foolish. Why would value investing cease to be relevant? What has changed so dramatically that would precipitate such a change? The answer is, quite simply, nothing.

The bottom line is that growth is taking a normal -- albeit elongated -- turn in the growth-value cycle. It won't last forever; in fact, as we've seen, there's evidence that shows it will only lead to an equally dramatic shift back toward value investing. That's because the longer the growth push goes on, the further value stocks will fall. And the farther they fall, the more room they'll have to grow once the market realizes how undervalued they've become.

Two Centuries of Resilience

Excerpted from the October 17th, 2008 Validea Hot List

The fear spreading through the market has meant a very difficult week for both the Hot List and the broader market. Since our last newsletter, the Hot List is down 19 percent, while the S&P 500 has fallen 15.1 percent. For the year, the portfolio has lost 32.6 percent, while the S&P is down a bit more, having fallen 35.5 percent.

While the problems that the economy is facing are substantial -- and the fear permeating the market widespread -- I still remain confident that we are not headed for some sort of great calamity that will destroy the economy and stock market as we know it. One reason is that, throughout history, the economy and market have continually and repeatedly faced challenges that were deemed "unprecedented", and each time they have recovered and pushed ahead.

Jeremy Siegel, the well-known investment author and commentator who teaches finance at the University of Pennsylvania's Wharton School, is a great source of information on this notion. In his book Stocks for The Long Run, Siegel examines stock returns over a variety of different periods from 1802 through 2006. His findings show that the U.S. stock market produced real returns (that is, after-inflation returns) of 7.0 percent from 1802-1870; 6.6 percent from 1871-1925; and 6.8 percent from 1926-2006. "Even since World War II, during which all the inflation that the United States has experienced over the past 200 years occurred, the average real rate of return on stocks has been 6.9 percent per year," Siegel writes. "This is virtually identical to the previous 125 years, which saw no overall inflation." The returns were similar over many other subperiods, Siegel notes, adding that periods that veered significantly from that 7 percent real return (such as 1965-1981, when real returns were -0.4 percent) have been followed by swings in the other direction that brought the average back to around 7 percent (following that 1965-1981 trough, stocks rebounded to average a 13.6 percent real return over the next 18 years). This phenomenon is known as the "mean reversion of equity returns", writes Siegel.

Think about that for a moment. Over the past two centuries, the U.S. has gone from horse travel to simple Model T cars to high-tech SUVs and commercial jetliners; it has gone from crude medical practices to laser surgeries; its communications abilities have gone from the days of the Pony Express to the immediacy of the Internet. And through it all, the stock market has always come back to a real, after-inflation returns of about 7 percent.

And the changes the country and the world have gone through don't just involve social or practical issues. As Siegel notes, the very essence of the U.S. economy has gone through a variety of huge metamorphoses. "The U.S. evolved from an agricultural to an industrial economy and then to the postindustrial, service- and technology-oriented economy it is today," he writes. "The world shifted from a gold-based standard to a paper money standard. And information, which once took weeks to cross the country, can now be instantaneously transmitted and simultaneously broadcast around the world. Yet despite mammoth changes in the basic factors generating wealth for shareholders, equity returns have shown an astounding stability."

Good Times Ahead?

Great, you may be thinking. Siegel's data shows that over the long, long haul, there's a good chance real stock returns will continue to be in that 7 percent range. But what about those interim periods when the market gets hit hard? After all, during that 1966-1981 period I referenced earlier, nominal returns

averaged 6.6 percent per year, and high inflation caused real returns to be about break-even. What if we're in the middle of a long-term trough like that?

Well, in fact, we are in the middle of such a trough. From Oct. 15, 1997 through Oct. 15 of this year, the S&P 500 (adjusted for splits and dividends) was *down* 6 percent,*before inflation*. That means that over the past 11 years, the S&P is actually *well in the red*. It seems hard to believe, given the incredible bull run we saw from 2002-2007, but it's true. In fact, over the past 20 years, returns have been just over +6 percent -- and that's before inflation, which has run at about 3 percent per year.

While that's certainly been bad news for investors over the past decade or two, there's a silver lining: If history is any judge, such poor returns over such a long time are a sign that we may be close to a big turnaround, one that could be quite lengthy.

One reason to think that this could indeed be the case is that, historically speaking, stocks are cheap -- very cheap. In Forbes this week, Kenneth Fisher (whose book Super Stocks forms the basis for my best-performing Guru Strategy) writes, "Unless you are in your late 80s and were an adult as World War II ended, stocks are cheaper, adjusted for tax rates and interest rates, than they've been at any time in your adult life. That's a simply stunning statement looking forward." Fisher's advice: "Buy great franchises at cheap prices now and be patient."

Similarly, The Wall Street Journal's Jason Zweig recently wrote that "Regardless of how much further it might (or might not) drop, the stock market now abounds with so many bargains it's hard to avoid stepping on them."

Zweig noted that the current situation on Wall Street appears to be quite similar to the situation Benjamin Graham -- another of the gurus I base a strategy on -- described just eight days before the market bottomed and turned upward in the Great Depression era. At that time, Zweig writes, Graham pointed out that many companies "were now worth more dead than alive"; that is, they were selling for less than the value of their cash and marketable securities. Banks had stopped lending to big firms, "but operating companies were still flush with cash -- many of them so flush that a wealthy investor could theoretically take over, empty out the cash registers and the bank accounts, and own the remaining business for free," Zweig states.

At that time, Graham had said that about 1 in 12 companies on the New York Stock Exchange were in such a position. Today, nearly 1 in 10 stocks, trade below the value of their per-share holdings of cash, Zweig says, adding that close to 40 percent of stocks tracked by Standard & Poor's Compustat service are trading at less than eight times their earnings. Zweig's conclusion is similar to Fisher's: "Investors who have, as Graham put it, either the enterprise or the money to invest now, somewhere near the bottom, are likely to prevail over those who wait for the bottom and miss it."

So, are we near the bottom? As you know, I believe market timing is a dangerous game, and don't practice it. That being said, there are some good signs. Over the past 50 or so years, average bear markets have lasted about 15 months, during which time the market has dropped an average of about 33 percent. As of the close of market Wednesday, the S&P 500 was down about 42 percent from its most recent new high, which occurred just over 12 months ago.

But what about the recession? As you're also well aware, I don't spend a lot of time worrying whether we're technically in one or out of one; recessions are called retroactively, and often you don't know you've been officially in one until you're coming out of it. If you're particularly worried about the "R" word, however, you should keep this in mind: The 10 post-World War II U.S. recessions have lasted an average

of about 11 months in duration, Joseph Feeney, Jr. recently wrote in Advisor Perspectives. And a year after those market troughs, the S&P 500 has been up, on average, 37 percent, Feeney's piece added.

In the end, however, I don't know for sure how close we are to this current market's bottom -- and anyone who tells you they do know for sure is at best making an educated guess, and at worst being foolish. You can read every piece of news, know every bit of stock market history, and study human psychology as much as you want, but you'll never be able to call all the tops and bottoms with any degree of certainty. As I've noted many times before, there are simply too many factors at play in determining the market's short-term movements, be they economic, psychological, or otherwise.

What you can do, however, is find financially stable companies with long track records of success, and try to buy them at prices that are cheap compared to their fundamentals. That's how investors like Ben Graham, Warren Buffett, Peter Lynch, and the other gurus I follow made their fortunes, and it's how the Hot List has made huge gains while the S&P 500 has been in the red over the past five-plus years. And, while the current market situation has been filled with pain and fear, it is also filled with as much opportunity to find those solid, undervalued stocks as we've seen in decades. If you take advantage of those opportunities now, you should be quite satisfied in the long run.

President Obama Doesn't Mean Market Drama

Excerpted from the November 14th, 2008 Validea Hot List

Of course, since our last newsletter we've also had another big change: the election of a new president. Barack Obama will be inheriting a whole slew of problems when he takes office in January, and some fear that having a Democrat in the White House -- one who's calling for some serious government plans, no less -- could mean more trouble for the stock market. After all, aren't smaller-government, trickle-down Republicans better for the market than big-spending, tax-the-wealthy Democrats?

Not necessarily. In fact, over the past 60 years, the stock market has performed far better under Democratic presidents than it has under Republican presidents, gaining an average of 15.26 percent per year under Dems and 9.01 percent per year with a Republican in the White House, according to columnist and author Jeremy Siegel. Even during the administration of the biggest of the big-government Democrats -- Franklin D. Roosevelt -- stocks' real annualized returns were about 2.5 percent greater than the market's historical average.

Even the Democratic double-dose that we'll soon be getting, with Dems controlling the White House and Congress, isn't reason to panic. Siegel's research shows that such a combination has generated annualized returns of nearly 14 percent since 1948 -- more than 4 percentage points better than under a GOP president/GOP Congress, and more than 3 percentage points better than under a GOP president/Democrat-controlled Congress.

All of this isn't to say that Democrats are better for stocks than Republicans, either. Regardless of who is in power, there are a myriad of factors outside of the president's purview that affect how the stock market acts. Stocks soared under Democrat Bill Clinton's administration, but a key factor was the tech bubble of the late 1990s. The bubble burst during George W. Bush's first term, part of the reason returns during his tenure have been so poor. Surely, however, the speculative bubble would have also burst under a Democrat (and even under Clinton himself, had he been allowed to run for a third term).

What history does show, however, is that the president's economic plan is only one of a multitude of factors that drive the nation's economy and stock market. And given the fact that he's taking over at such a trying time with the market being so battered, it actually is likely that stocks will be significantly higher when Obama leaves office than they are today -- regardless of what the pundits or the headlines say.

The More Things Change

Speaking of the headlines, take a look at these major newspaper headlines and try to guess what they have in common:

"Fed Chief Expresses Guarded Optimism: Greed Poisoned Businesses"

"S&P 500 Hits Another Bear-Market Low"

"Companies Take Action to Regain Investor Trust"

"Bear Drags Stocks Deeply into Den: End of Third Quarter Finds Markets Badly Mauled"

"Have Stocks Finally Hit Bottom?"

"Throwing in The Towel? Some Investors Head for The Sidelines to Escape Bear Market"

"Despair Grows as Markets Plunge: Investors Stampede out of Stock Funds"

"Stocks get smacked down again: Dow Below 8000 as Search for Market Bottom Drags On"

So, is the answer that all of these were made possible by the credit meltdown? No. That all of them have been scaring the heck out of investors for the past couple months? Nope. That they've caused many an investor to rethink whether they should stay in stocks, given the current economic woes? Wrong again.

The answer is this: All of these headlines were written more than six years ago.

That's right, while you could just as well find any of these on the cover of a paper from the last week, all were in fact written between July and October of 2002, when the economy was in the tank and the stock market was in the throes of a tough bear market. It was bleak back then; maybe not quite as bleak as things are now, given the severity of the credit crisis, but quite bleak nonetheless, as the headlines show. But by October 2002 -- just a week after some of those headlines were written, a bull market had taken off, one that would run for the next five years and see the Dow gain close to 90 percent.

This isn't to say that within a week we'll be seeing the start of a new bull market. The challenges we face now are certainly different than the challenges we faced in 2002, and as I said, in some ways they are obviously more severe. But the point is this: We've been through crises before, crises that have shaken our resolve and led to fear and negativity that made people wonder whether stocks and the economy were ever going to bounce back. And each time, the market has done more than bounce back -- it's gone on to new heights.

The other point is that stocks can experience those bounce-backs when you least expect it. And when the turnarounds come, they come quickly: In the first 40 days of a new bull market, stocks usually regain a third of what they lose during the previous bear market, Money magazine stated in a recent article.

The coming period will thus be a dangerous one for many investors -- but not because the economy or market are going to disintegrate and leave us in another Great Depression. The danger, rather, is that every day the bear market continues, those investors who have stayed the course through the bear will be more and more tempted to bail, having had their emotions so battered over the past year. If they do bail and wait to re-enter the market until they're sure the bulls are running, it's likely they'll miss out on a major portion of the rebound -- history has proven that. That's why, as hard as the past weeks and months have been, we'll keep sticking our guru-based strategies and our disciplined approach. And in the end, I believe we'll reap the rewards for our patience.