

Eads & Heald Investment Counsel

Established 1987

Atlanta, Georgia

Professional Portfolio Management With Experience And Integrity
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Equity Investing

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Chapter 7: Short-Term vs. Long-Term Investing

Simply stated, common stocks are not suited for a short-term approach. I would compare short-term investing to a fool's game. Using inside information is illegal and one is competing against other bright, well informed and greedy people. They could possibly be brighter, better informed and greedier than you.

There are a large number of professional investors vying to manage large investment funds and they are all attempting to perform well over a period as short as two to three to five years in order to keep the funds they have and to gain new funds. This is in spite of the fact that a given investment style might well be out of favor for a time period much longer than five years. The point is that you have stiff competition. However, you have one excellent advantage as an individual. You do not get fired from overseeing your own funds if you do not perform well over, say, three years. Thus, you have the possible luxury (depending on your age) to invest looking out five to ten to twenty years or more. More times than not, this is not the focus of the big outfits. Many of them work under a "perform or die" rule.

So, how does a long-term approach help you? In this series of chapters it will be shown that there are long-term trends at work and certain factors appear to be directly dependent on other factors. These insights will be based on empirical history and not on some arcane "wave theory" or such. Our work comes under the heading that history has a lot to teach us if we will observe and learn. Further than just blindly using historical relationships we want to be able to explain why the relationships make sense.

Unfortunately, much of the year-by-year data relevant to equity investing is full of "noise". That is, while there may well be an underlying trend at work in a data series the year-by-year data may mask the trend by bouncing around and fooling both the eye and the brain. As you will later see, we overcome this "noise" factor by using moving averages of data. Out of apparent chaos can appear a logical trend. This gets back to our endorsement of longer-term trend investing.

There is another very real bonus to longer-term investing. The amount of portfolio trading (turnover) tends to go way down. This saves the investor money on trading costs. Also, much of the research time spent on examining short-term jiggles in stock fundamentals can more productively be spent on studying long-term trend fundamentals.