

Investment Advice From a Wise Man

By Roger Balsler

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As the bartender delivered our appetizer dish, my friend Steve glanced up from his recently opened retirement statement and quipped, “Roger, where did you learn all of this stuff about investment strategies? I’ve known you since your college football days, and I know you’re not smart enough to make this stuff up on your own.”

Steve was right. (Even about the intelligence part.) In the 30 years that I’ve been in this crazy, erratic business, I’ve been fortunate enough to learn a trick or two about investing. But his question took me back to my early apprentice days working as a stockbroker for the venerable Smith Barney.

It was 1999 and I was roaming the office hallways when I meandered past the glass-walled corner office that was occupied by Will, a 70-year-old salty dog who had clawed his way to the top of our organization and had been rewarded with an office sporting one of the most impressive views of Lake Erie that I had ever seen.

Will, a guy who only spoke when the need for insightful wisdom arose, must have heard me walk by because he suddenly spun his Herman Miller around and called my name.

“Roger, do you have a minute to talk?” he asked. Shocked that this guy even knew my name, I stumbled into

his office while he motioned for me to take a seat on one of the two Italian leather sofas positioned across from his desk.

“Roger, for the past couple of months, I’ve watched you walk by my office with this dour look on your face,” he said. “It seems as if you’re angry and frustrated. Is there anything I can do for you?”

“Thanks Will, but there’s nothing you can do for me,” I answered sheepishly. “Unless you can tell me how to buy stocks for my clients that go UP instead of down.”

Will looked at me and massaged his chin for a moment. “Not too sure I can do that,” he said. “But tell me how you select the stocks you’re working with. Tell me your process.”

My process? What process? At the time, my only process was lingering in bed until the last possible minute so that I would time my commute to arrive at the office by nine o’clock on the dot. That was the only “process” I owned (and it worked quite well, I’m proud to say).

But Will was waiting for an answer, so I said, “Well, I read all of the weekly and daily research put out by the firm. I look at what the firm’s analysts are pushing. I’ll follow those leads and wait for the right time to buy. Usually, the stock starts to go up, and the firm continues to talk about it. So I’ll finally buy in. Then soon after I do, the stock crashes and burns. I’m so lost and confused. I don’t know what to do.”

“Clear your schedule for lunch today,” said Will. “My treat. And I’m going to share the secret that saved my career.”

How could I pass up an offer like that? So at noon we walked down to the deli in our building and took a seat at a small table in the corner.

Will didn’t mince words. “What do you know about the markets?” he asked. I really wanted to shoot back with an answer that would blow his socks off, but the truth was that I knew absolutely nothing about the markets. As the new guy in my firm, I did what I was told, when I was told and how I was told. The only recommendations I made to my clients were the ones that the analysts from Smith Barney told us new guys to make.

“So you’re just buying the stock of the day,” said Will. I nodded yes.

“That’s your problem, Roger,” he replied. “You don’t have an operating system. You need an operating system.”

Benefits of an Operating System

Will explained that successful investing requires an operating system, similar to those which drive the workings of a computer. The operating system on a computer enables it to effectively read and run all the software. Without the operating system the computer is pretty useless.

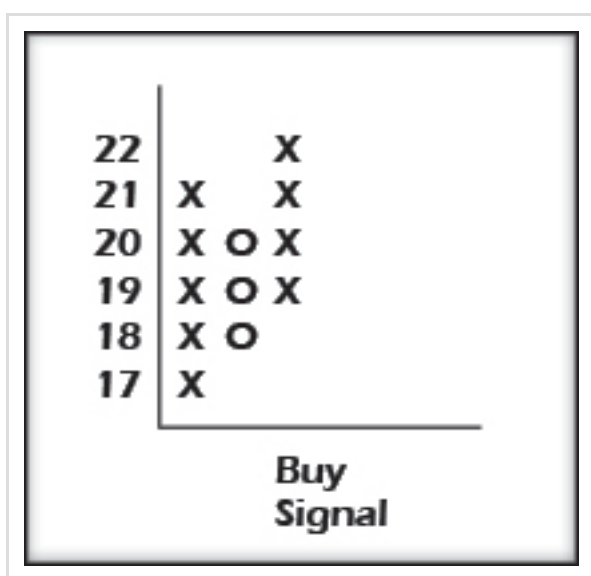
“In the investing world, you must have an operating system that you understand and work with to become a successful investor,” he said.

This operating system, according to Will, was based on the irrefutable laws of supply and demand. If there are more buyers than sellers then the price must rise. If there are more sellers than buyers then the price must decline. And if buying and selling are equal the price should remain the same. That was it. There is nothing else to know.

I looked at him in disbelief. It couldn't possibly be that simple. But this was Will talking, and he was always making money for his clients.

“Roger, it's just like shopping for produce at the grocery,” Will said. “Produce rotates in and out based on the season. Stocks in the markets rotate in and out of season the same way. There are companies that you should buy when the economy is humming and there are companies that you should buy when it's slowing down. “

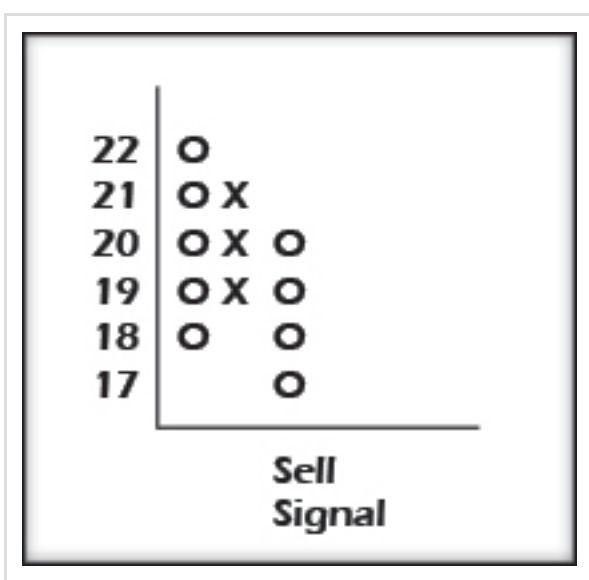
Suddenly the synapses started firing in my brain and the world was becoming clearer. And it was getting scary. I was starting to understand.



Will told me that this investment “operating system” was developed in the late 1800s by Charles Dow, the first editor of the *Wall Street Journal*, and it hadn't changed since. Then he handed me a napkin and told me to draw a chart with an 'X' axis and a 'Y' axis, and add a whole bunch of other stuff until the napkin looked like this when I was done.

I looked at my scribble and asked, “What is this?” Will replied, “Roger you've just drawn your first chart. It's an example of a buy signal. The X's mean demand is in control or the stock is in season and it may be a good time to buy.”

Will handed me another napkin and told me to draw what ended up looking like this:



“That’s a sell signal,” he said.

“Roger, there are two key questions you need to answer before making an investment,” Will said. “First, what should you buy? The firm’s research can help here. And the second question is when should you buy it? You’ve just learned how to answer the ‘when’ question.”

Focusing Investments

Will grabbed the last napkin on the table and said, “All right, listen closely. You’re going to learn how I determine where to focus my investments for myself and my clients. It’s called the ‘Silver Bullet of Relative Strength’.”

What he showed me was basically third-grade math. You simply take the price of one thing and divide it by another. “Multiply by 100 to get a number big enough to plot on a point and figure chart just as you did earlier,” he said. “The X’s mean the numerator is the one you should buy. And O’s mean you should buy the denominator.”

“Tonight, your homework is to compare every stock in your clients’ portfolios to the Standard and Poor’s 500,” Will instructed. “If the stock is underperforming then sell it. If it’s outperforming then keep it and review it daily. And the next time you think about buying a stock, do a Relative Strength chart to see if it’s time to buy. It’ll save you a lot of money and a ton of frustration down the road.”

$$\frac{\text{Stock Index}}{\text{Index}} \times 100 = \text{Relative Strength}$$

I've been doing my "homework" every day since my fortuitous lunch with Will that day. And through good times and bad times (and even through calamitous downturns in 2000 and 2008), I can honestly say that the Silver Bullet of Relative Strength has performed well for my clients and has been a boost to my career.



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