Tom: In this episode, we're going to talk about something really important, the math behind losing money.

Welcome to the Mullooly Asset Show. I'm your host Tom Mullooly. This is episode 12, an even dozen. This is the John Sterns episode. John Sterns was a really good catcher, came up through the Mets system. He actually made it to the All-Star game once. He wore number 12. He came back later on as a coach and wore number 12 for a while. Trivia question, Casey. When John Sterns stopped playing for the Mets, he gave up number 12. Who took number 12 after that? Bet you don't know.

Casey: No idea.

Tom: Ron Darling. One of our favorite announcers. There's been a couple of other 12s out there too.

Casey: Roberto Alomar.

Tom: Roberto Alomar. I'm not spitting on you.

Casey: Juan Lagares.

Tom: Juan Lagares, gold glover. That's right.

Anybody else?

Casey: Willie Randolph

Tom: Willie Randolph twice, wore it as a player and as a manager. That champagne's going to taste only sweeter when they win the big game with him, right?

What we talk about on these videos are topics that you're talking about because we get our topics from conversations that we're having in the office or on the phone with clients or in emails. Sometimes we're just talking about this in the office amongst ourselves because we know that clients are calling and talking about it. The way these typically work, Casey reads the questions and I'll answer them. We only have one question today, Casey. Why don't you lay it on us.

Casey: The stock market's been pretty messy to start 2016. I'm getting pretty worried. What do you think I should do?

Tom: That's a big question, and we have been getting a lot of calls from folks that are wondering should they be getting out of this market. RBS, Royal Bank of Scotland, grabbed the headlines a couple of days ago. One of their analysts came out and said, "This looks like 2008, you should sell everything." Funny thing is, they were pretty bullish in 2008, so I don't know what they're looking at today.

That feeling that you have is a real feeling. We don't want to simply just disregard it. What I'm trying to stress with folks that are talking about ripping up their script is that a loss when the market's going down, it's really just a loss on paper, it's not real. Once you decide to sell, that loss is, it's real. That money is gone. It's for reals, and it ain't coming back.

Let me give you a simple math example. If you've got $200,000 and you lose 10%, the account goes down by $20,000. Now, instead of having $200,000, you've got $180,000. Then people say that they want to start becoming conservative with their investments. Just think about this. Mentally, the first thing that an investor wants is they want to get back to even, so we want to get from $180,000 to $200,000. We're not trying to earn 10% back. We actually have to earn a little more than 11% to get it back. But wait, you said you wanted to be conservative, so now we have to try and make money with slower moving investments. It's hard to do. Retail investors, individual investors tie one hand behind their back when they become conservative at the wrong time. I think trying to time the market, I hate to sound like everybody else out there, but trying to time the market is just a real not smart thing to do.

You have to really be careful about this, but you also have to realize that the numbers, the math, is working against you. The losses that you might see on your account if you look online or if you look at your statement when you get it in the mail, those numbers are not real until you decide I'm going to close out this position and recognize that loss. Recognize the loss, okay? That means that money is gone. You really have lost $20,000 and it's not going to come back. I think a lot of people overlook that because now what you're trying to do is you're trying to get back to even but you have less to work with. If you want to be conservative, now you're changing your whole strategy and you're trying to get back to even with less money and with a slower strategy. It's not something that really works that well.

It's amazing that 30 years in the business there's a lot of people out there that I've met that say, "Well, I want to be aggressive when the market's going up, but when the market's going down I just don't want to loose money, I want to be really conservative." You can't flip a switch like that. It doesn't work that way. In fact, I'd say it's impossible to be aggressive on the way up and conservative on the way down. It just doesn't work that way.

One of the things that's become a real big theme in the last couple of years is this term robo-advisor. That's where people, they don't even work with an advisor. They just go to a website and they plug in what they think their risk parameters are and the website spits out a formula, says "Okay, do it this way." The problem that people are starting to discover is that when markets start to change, like what we're going through lately in the market, people log into the website and they change their risk parameters, now they're changing from, "Hey, I want to be aggressive," or "I want to be long-term growth," and "Now, I want to be conservative," and the model changes. Now, instead of working with an advisor who may stop investors from making a bad mistake in their investment, now they're just confirming what they have been doing all along.

Look, we understand that there's a lot of panic right now in the market, especially these first two weeks in January. Panic is a real emotion, it's a real feeling, so you can't just disregard this. It's an emotion, and making investment decisions by emotion is a really bad plan. It's one of the reasons why in the 90s I pretty much started diminishing my reliance on fundamental analysis and looking more at the technicals. The great thing when you look at a chart is that there's nowhere on the chart where they have a little asterisk and they say, "Oh, here's where the economy went into a recession," or "Here's where the CEO of the company came out with a terrible decision," or "Here's where they lost all the money or they had a bad quarter," or anything like that. It just shows you patterns of the stock price moving up or moving down based on supply and demand. That's really it.

We can go on and on talking about the charts, but right now I know that the concern for people out there is they flip on CNBC or they look online at their accounts and they're freaking out. I totally understand that. The thing you need to keep in mind is this. Couple of things I've learned over the years, and I've learned this from my friends at Dorsey Wright, a 5% pullback can happen in the market at any time for any reason or for no reason at all. The other thing you need to know going all the way back to the 1920s, now almost 100 years, is that a 10% pullback can happen on average, it does happen on average, once per year. It's happened 86 times in the last 92 years. That's almost once per year we get a 10% pullback.

What's unfortunate is that we had a 10% pullback just a few months ago near the tail end of 2015 and we're not off to such a hot start in 2016. This is why it's really important to not let emotions guide your decisions, not to panic, but to just trust in the indicators that we use and to make sure that your risk profile is pretty accurate.

We've had conversations with clients over the last couple of days where they've said they'd like to be a little more conservative, and that's okay. We're on board with that, if they want to change their risk profile. What we want to avoid though is we want to avoid selling at what may be a really big down day or maybe the low point in a pullback in the market. When the market does recover, we're probably going to implement changes for clients who want to reevaluate their risk profile. If you want to reevaluate your risk profile, get in touch with us, okay? You can find us on Twitter, you can find us online, email us, phone, whatever, but do get in touch with us.

These questions that we cover in these videos come from topics that you're talking about. First of all, this is how we get the topics. If you're thinking of something, let us know because if you're thinking about it other people are probably thinking about it too, and we'd be happy to answer your questions. In the meantime, if you're watching on YouTube, there's a red subscribe button right here. Don't forget to hit subscribe. This is episode 12. I appreciate you watching. The next one will be episode 13. Let's see, a famous Met who wore number 13. Who would that be?

Casey: Edgardo Alfonzo.

Tom: Fonzie. The Fonzie episode is next. We'll see you on that.