

# *The* INVESTMENT LETTER

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## I Heard of a Guy That Quit His Job and Got Rich Day Trading!

**B**uy low. Sell high. We can put that advice to work in many ways. With options come complexity. And risk. We are all willing to take on some risk; otherwise, we would just sock our money away in an FDIC-insured, low-interest savings account, or perhaps, in an old mattress. The stock market exists for those of us who want more. For investors, the stock market exists to pursue and realize gains. But, again, there are many ways to do this.

Which securities do you buy? What relative positions should each hold in your portfolio? How long should you hold securities?

There are probably as many different answers to these questions as there are investors. One way to frame a possible response is to divide the mass of investors who form the markets into two groups and differentiate them by the length of time each holds its investments. We would call these groups: day traders and buy-and-hold investors.

### **Day Trading**

Day trading has gained immensely in popularity with the advent of online stock brokers and low transactional fees. Day trading takes a lot of effort. With day trading, you follow, analyze and, yes, sometimes live the short-term price fluctuations of a portfolio of stocks. Buy low, sell high applies to day traders too. Many day traders set a pre-determined percentage increase they must realize before they sell or watch for a pre-determined decrease before they buy. Day traders look to roll the quick wins of daily gains into a windfall of funds that can pay off their mortgage or send them sailing into retirement.

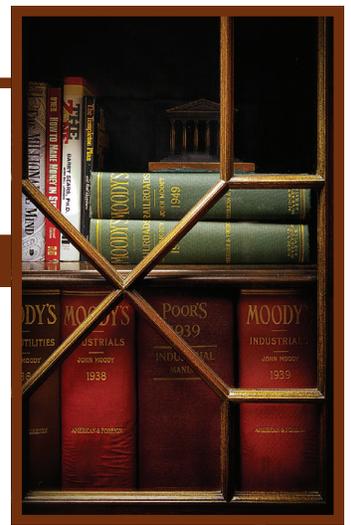
In day trading, the potential for rewards is immense. But, with those rewards come commensurate risk. Stock prices can be wildly volatile and subject not only to the expectations, press, and pressures facing the company, but also those facing the larger market, country, and world as well.

A stock's value may drop and not recover within the short timeframe the day trader needs. Also, a day trader's profits must cover the considerable brokerage fees that large amounts of transactions generate. And, there are tax considerations as well. For stocks held less than a year, gains are taxed at an investor's ordinary tax rate and not at the lower capital gains rate. Also, some day traders buy securities on borrowed money, which heightens risks and raises the stakes even more.

### **Buy-and-Hold Investing**

Another investments approach, vastly different than day trading, is called buy-and-hold. In a buy-and-hold strategy, investors keep their investments for a longer period, with the assumption that their value will increase with time. With a buy-and-hold strategy, transactional fees and tax rates are lower, but there is an increased need for patience. Buy-and-hold investors are buying in for the long-haul.

Experience shows that a stock's long-term movement is much more highly correlated with its respective company's business fundamentals and long-term performance than with external market and political happenings. Buy-and-hold investors need to follow the fortunes of the companies represented in their holdings. The price at which



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investors purchase their investments determines the profits they eventually take, no matter how far in the future they sell those investments. With that said, buy-and-hold investors do best when they purchase securities at competitive and not inflated prices. And, after the stock lands in a portfolio, it still makes sense to check regularly to ensure it is hitting its targets and maintaining its place within its industry. Unlike day trading, buy-and-hold investing allows investors to withstand a short-term, or even medium-term, slump in prices.

### Which approach performs better?

Many day trading stories that reach us paint a rosy, even exciting, picture of day traders reaping huge profits, living comfortable, posh lives, and even retiring early. Research shows otherwise. One recent study, carried out by the blog CuriousGnu, found that day traders have a nearly 80% chance of losing 'real money' during a 12-month period. CuriousGnu went on to divulge that those losses reached a median of 36.3% over a one-year period. The study was realized using the publically-available data of some 83,300 investors at eToro, a London-based social trading network. Other studies paint even more dire results for day traders. A 2010 study undertaken by UC-Davis found that, over a 14-year period, less than 2% of day traders were profitable, after paying fees. The same study found that more than 75% of day traders quit day trading within two years.

Contrast those dire numbers with the fact that, if you had invested in the S&P 500 two years ago, you would have enjoyed an annualized return of over 20% (assuming dividend reinvestment). And, if you had held tight to that S&P 500 Index Fund since 2008, you would have reaped an overall return exceeding 115%, with an annualized return over those ten years approximating 8% (again, assuming the reinvestment of dividends).

### Conclusion

The allure of day trading, and the legends of the successful few, seem to promise a panacea of fast money for those who, against all odds, accurately predict a stock's near-term movements. The

reality is that this is much more difficult than it seems. While precious few day traders earn enough to retire, or to even maintain their initial investment outlays, most buy-and-hold investors earn competitive returns in the long-term. For this reason, Investment Counsel, and most creditable financial advisors stand behind the buy-and-hold approach and encourage investments in well-diversified portfolios. Investment Counsel's buy-and-hold approach represents true investing, while day trading is, at best, just speculation, and more accurately gambling. ■

## INVESTMENT COUNSEL NEWS

### *Inside the Office*



*Should you or your tax preparer require any information on your 2017 returns, as always, please contact us and we will be pleased to forward the information.*

### *Outside the Office*



*Chris and his wife, Barbara, are excited about the engagement of their oldest daughter, Jessica, to Scott.*