
THE WALL STREET TRANSCRIPT

Questioning Market Leaders For Long Term Investors

Investing in Large Cap Stocks



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Options, and served as Director of Research for HOLT Value Associates. He graduated Phi Beta Kappa from The University of California, Berkeley, with a Bachelor of Science degree in Finance and Economic Analysis, and obtained his MBA degree from the University of Chicago.

TWST: Would you start with an overview of Toreador and your investment philosophy there?

Mr. Resendes: The first concept that drives our thinking is that we are a sector-neutral fund; we're not looking to make sector bets and so we stay invested in proportion to each major sector's weight in the S&P 500. We are a large cap fund, so we purchase predominantly stocks that are in the S&P 500 or Russell 1000. We will drop down to stocks with market caps as low as \$5 billion sometimes, if there are some large stocks that are falling that we believe are attractive, but predominantly, we are in the upper mega-cap range with our stock selection process. Therefore what we believe sets us apart from other fund managers is our stock selection process.

We really try to focus on four major drivers behind any stock that we look at. The first is understanding a firm's earnings quality; in other words, GAAP accounting metrics and procedures result in a fair amount of latitude in the way companies can report their earnings and prepare their books, and we want to understand the quality of those earnings before we buy them. For example, compa-

nies may push their product out to their end customers and "book" a sale, without collecting any cash from the transaction. If this happens enough, we will see accounts receivables rise faster than collected cash, and indicate a potential problem in the future. Therefore, we rank all the companies we follow on a metric we created that determines the quality of a company's reported earnings. We do not consider firms with low earnings quality unless we understand the reason and believe it is short term in nature.

The second factor we evaluate is a firm's economic earnings, rather than its GAAP accounting earnings. There are a number of issues that prevent reported earnings from being a true proxy for a firm's economic performance, so we take the time to fix those issues and put all firms on a level playing field to evaluate their performance. There are examples, such as the use of R&D for instance — in the technology sector, technology companies according to GAAP must immediately expense their R&D investments. These investments tend to be strategic expenditures that have relatively long-term impacts. It's much like a company buying a new piece of

equipment. We don't expect manufacturing firms to recoup the cost of a new machine in the year they make the purchase, and companies investing in R&D do not expect to recoup the entire investment the year they make the expenditure. Therefore the R&D expenditure needs to be reversed from the income statement, capitalized on the balance sheet, and depreciated over time — similar to physical piece of equipment. As the knowledge economy continues to grow such adjustments become more and more important. We make this adjustment for every firm in our investable universe.

Another adjustment we make is looking at off balance sheet assets and liabilities, such as the use of operating leases, which is particularly important when analyzing retail companies. For these firms, 30% to 50% of their assets never make it to the balance sheet because they are tied up through operating leases, which as a result of GAAP never have to be booked on the balance sheets. We go back and we make a number of adjustments to move from an accounting balance sheet to an economic balance sheet and an accounting statement of income to a economic statement of income, resulting in a calculation we call an Economic Margin, which ultimately looks at the return the company generates on all of its assets relative to the risk of the company or its cost to capital. We then begin to evaluate all companies on the basis of their economic, not accounting earnings.

Once we understand the company's true economic performance, we then evaluate how well management is running the business. We do this by looking for the companies that are able to earn more than their cost of capital and grow their business. When we find opportunities in those types of firms, those have tended to be very good, long-term investment opportunities. Conversely we try to avoid firms that are growing at the expense of creating shareholder value; in other words, they can't generate an adequate rate of return on their assets and yet they try to continue growing their way out of problems. In simple finance terms this means that as investors we provide the company \$1 of capital today, and they return less than that \$1 in present value terms. Those are companies that we call wealth destroying management teams and we go out of our way to try to avoid investing in those types of firms. Firms such as Enron, MCI and Adelphia all had one thing in common — aside from problems with their management teams' honesty — the business model was fundamentally flawed; they failed to earn their cost of capital after properly measuring their corporate performance from an economic perspective. Using this management quality screen that we created helps us avoid those types of torpedoes.

The fourth piece of the puzzle is understanding what we're paying for at a given stock price. The Applied Finance Group (AFG), our sister company, has pioneered the use of the Economic Margin model and analyst research to understand the expectations embedded in stock prices. We apply this comprehensive valuation process to every company in order to understand what are the sales growth, EBITDA margin, and asset efficiency expectations embedded in today's stock price and how that compares against the company's

likely ability to deliver on those expectations in the future. We take every company we own, we walk it through those three parameters on a systematic basis and then we give that to a team of analysts who overlay their understanding of the company and more recent current events that mainly show up in a quantitative process, because the data just hasn't hit the company's financial statements yet, whether it's lawsuits, whether it's the potential for a new acquisition, a divestiture or changes in market conditions.

What we do is really assimilate what we think are the best of both worlds, a very thorough systematic process combined with an ongoing analyst team who are experts in the companies they follow. We combine these two processes to come up with a portfolio of roughly 65 to 80 names dispersed across the entire base of economic sectors and invested in a sector-neutral fashion relative to the S&P 500. Over the long run, the goal is, through superior stock picking, to add alpha to the S&P's returns with similar risk.

1-Year Daily Chart of CVS Caremark



Chart provided by www.BigCharts.com

TWST: How has that process been able to withstand the turmoil in the market over the last several months?

Mr. Resendes: I think one of the things that happens when you start to have a lot of dislocations in the marketplace is that fundamental factors oftentimes tend to go out the window and you end up with, in many cases, a flight to size. In other words, some of the largest mega-caps within the S&P have been outperforming on a relative basis; they have been relatively strong. From our perspective, I believe our numbers have held up pretty well. Year to date we're still outperforming the S&P, I think, by maybe 200 basis points or something like that, after fees, so we've held up pretty well. A research study by AFG shows that often entering into dramatic sell-offs, value stocks tend to underperform growth stocks. However, exiting the trough, value stocks tend to perform much better. That said, our performance feels all the better.

What I look forward to is a bit more of a calm market, where people start to pay more attention to the fundamentals and less attention to immediate momentum type of trends in terms of driving stock prices inordinately up or down. Making this recent selloff more

complicated to understand has been the selling by hedge funds. Many hedge funds have been liquidating and oftentimes they have been liquidating some of their better holdings, because those are the ones that are easiest to get out of and so some of the better companies have been punished inordinately over the last month, which will likely position us really well as the market gets back to normal.

more toward a cost-driven medical structure, the ability of a firm that has scalability and can offer cost savings and efficiencies will be more in demand going forward. That's been our most recent change.

In general, we don't tend to trade our stocks very often, we tend to buy them and we're buying them with a long-term perspective. We don't really go in there looking to make a lot of trades.

“We added to our position in JPMorgan, because we thought the ability of this firm to capitalize on the weakness in the sector by acquiring some marquee assets over time would play out pretty well. JPM holds really attractive long-term opportunities within the sector, given some of the assets it's been acquiring and the way it has structured itself to move forward.”

TWST: How would you describe your investment style? Are you looking more at growth or at value or is it a mix?

Mr. Resendes: In terms of the traditional definition, I guess it would be a mix. From our perspective, the notion of growth versus value is kind of a misnomer, in the sense that you can have a very expensive company that's cheap, because the expectations of the company's future cash flows relative to its price are very reasonable, and you can have a stock like **General Motors**, that's very cheap in theory according to most metrics but may have very poor prospects about its future, making it not only very expensive, but very costly to own.

At the end of the day, we never really look at a traditional definition of growth or value, we let the portfolio kind of settle into its own niche, while staying true to our guiding principle of sector neutrality. That said, our stocks are companies where the current traded price relative to the expectation of the company's ability to generate future cash appear very reasonable and so we end up with stocks as diverse as **Google** (GOOG) and **Valero** (VLO), which according to traditional definitions would be considered a hyper-growth stock and a deep value stock. We just see them as companies that are cheap relative to their future ability to create shareholder value and generate cash flow. So we really aren't looking for a standard definition, we really don't pay attention to the traditional box definition of growth or value and at different points in time, we tend to tilt toward one end or the other, depending on what the market gives us in terms of discounts on the expectations of future cash flows for well-run companies.

TWST: Have you made any changes relative to the market downturn? Are you more defensive in nature, for example?

Mr. Resendes: Nothing really dramatic. However, one change that we made recently, with the results of the election and thinking through that the healthcare industry might transform itself a bit, was to move out of traditional health insurers. We bought **CVS Caremark** (CVS), and the thought process behind the move was, if we start to move

1-Year Daily Chart of JPMorgan



Chart provided by www.BigCharts.com

TWST: What about your financial services stocks? Did you change some of those according to the different fortunes of the financials?

Mr. Resendes: It hasn't been anything we've done recently, but we started this back in, I would say, mid- to late summer and that was consolidating some of our positions in the financial space and moving more into the bigger players that we've thought had superior staying power. For example we added to our position in **JPMorgan** (JPM), because we thought the ability of this firm to capitalize on the weakness in the sector by acquiring some marquee assets over time would play out pretty well. Again, the financial services sector is not by any means a safe place to be in right now, but our charter is to be sector-neutral. After all, during the summer, everyone thought energy was the hot place to put money and now look at the sector. We believe forecasting oil to go from \$150 to under \$50 a barrel in four months is much harder than identifying and buying firms likely to outperform across sectors. A firm like **JPM**, we believe, holds really attractive long-term opportunities

within the sector, given some of the assets it's been acquiring and the way it has structured itself to move forward.

TWST: What are some of the companies that you have purchased over the last several months or so that are representative of your investments approach?

Mr. Resendes: Let me tell you, we recently did a study and I think this study is interesting, because it highlights the way that we think about some of the acquisitions that we made. We titled the study "Then and Now" and the point of it was to compare and contrast the emotional versus the financial pain of investing. The thesis there was, if you go back to March 2000, the economy was doing great, GDP was growing every quarter, unemployment was falling every quarter, the

Now let's fast-forward to today. We did the same study here at the end of October and what we found is that for the industrial group of firms in the S&P 500, the market was making you expect that these firms would deliver negative 5% a year of sales growth for the next five years. In other words five years from now these firms would be about a quarter smaller than they are today. Now from our perspective, we believe nobody can accurately forecast the future. But what we like to think, in terms of our different distributions of events or probability distributions and the prospect of buying some of these fantastic brands that are on sale at these huge discounts, is that it's emotionally a very tough time to buy stocks, but financially there are some really great opportunities.

"Coach is a stock that has great long-term growth implications as the economies around the world start to straighten out. Right now, however, if you were to go in and figure out what you'd pay for Coach today, the market basically has discounted the stock so that you are paying negative 10% a year sales growth. What the market is saying at today's prices is that five years from now, this company's top line will be over 50% smaller. We just think that creates a great opportunity to buy a fantastic brand that's profitable at a significant discount."

market had been going up for years and, in general, the emotional cost to getting into the market was quite low. If you think about the typical investor out there, it was relatively easy for him or her to go out and purchase the latest growth stock fund or buy the latest Internet offering that had just IPO'd and gone up or doubled or tripled over the last few weeks. Emotionally it was relatively easy for them to do that.

Financially, however, it was very expensive in the following sense: We took the S&P 500 and combined all of the companies' income statements and balance sheets and formed one giant company, call it Corporate America, Inc., one firm representing all the industrial firms in the S&P 500. Then we sat down and said, in order to justify the market valuation of this entity, what kind of fundamental performance does this new company have to generate in terms of sales growth, EBITDA margins, asset efficiency and so on. What we found is, back in March 2000, in order to justify the price that the market had assigned to these companies, this group of firms would have to grow their top line sales 22%, while achieving near historical rates of return on those sales. That was a steep challenge, given that on average they had only grown about 8% a year in the prior five years when times were relatively good. It wasn't really that surprising, when you look at it, that the market started to sell off from that point. In fact, from March 2000 through 2003 was a terrible time to be in stocks.

1-Year Daily Chart of Coach



Chart provided by www.BigCharts.com

A recent stock that we purchased was **Coach (COH)**. Now, **Coach** is sort of the ultimate consumer discretionary stock. Nobody really needs an expensive Coach bag or a Coach wallet, but here is a company whose management team, since they were spun out from **Sara Lee**, has consistently beaten its cost of capital. When I say beaten, I mean 9% to 10% returns in excess of its cost of capital, as measured through this Economic Margin calculation we use, and it consistently expanded its asset base in conjunction with delivering those high rates of return, and now the

management is saying, where can we go from here. They have about 300 stores in North America. They project the overall market for North America to be about 500 stores. That gives them roughly 40% growth domestically, with enticing opportunities in Asia.

Here is a stock that has great long-term growth implications as the economies around the world start to straighten out and when I say straighten out, I'm looking at a two- to three-year horizon. Right now, however, if you were to go in and figure out what you'd pay for **Coach** today, the market basically has discounted the stock so that you are paying negative 10% a year sales growth. What the market is saying at today's prices is that five years from now, this company's top line will be over 50% smaller. We just think that creates a great opportunity to buy a fantastic brand that's profitable at a significant discount.

"AutoZone is a stock that, as consumers are buying fewer new cars, the need to maintain their existing automobiles becomes greater and greater and what's interesting about AutoZone is that in spite of the high oil prices that we had previous to this fall, which basically drove driving habits down, as consumers were driving less and less each quarter, AutoZone continued to generate positive same-store sales. Now we view that as a big plus."

1-Year Daily Chart of Wal-Mart



Chart provided by www.BigCharts.com

Now I'll contrast that with an opportunity that we had been looking at but it's still hasn't met our criteria and that's **Starbucks** (SBUX). **Starbucks** is also a great brand. Even though it is at \$10 a share, the market hasn't penalized **Starbucks** enough for us to think that it still creates as attractive an opportunity as what we saw with **Coach**. That process is something we call Value Expectations and that tends to drive the way we like to think about investment opportunities, because at the end of the day it's not just buying a great company, it's buying a great company that also makes a great investment and that was some-

thing that earlier in the year drove us toward **Wal-Mart** (WMT). We saw **Wal-Mart** was getting cheap relative to its abilities to support its business and relative to what management was doing. Management quietly changed its direction in the sense that instead of aggressively building new stores, management focused on fixing up its existing businesses and making those businesses more valuable. What we saw there was as, it did better, its ability to generate cash flow of the existing asset base it had in place was being misjudged by the marketplace and the stock had become inordinately cheap. Then we laid on top of that the macroeconomic conditions that had been unfolding throughout the year and **Wal-Mart** is really well positioned to take advantage of what's going on here. One other thing that adds to the **Wal-Mart** story is that because it is a net importer of goods that it sells, as the dollar strengthened, its input costs

have basically declined, because it's able to source its merchandise cheaper around the world thus increasing its margin even more, and that is another factor that we think makes **Wal-Mart** even more attractive, given where we are in the economic cycle right now.

Another similar type of story to **Wal-Mart** is **AutoZone** (AZO). It's a stock that, as consumers are buying fewer new cars, the need to maintain their existing automobiles becomes greater and greater and what's interesting about **AutoZone** is that in spite of the high oil prices that we had previous to this fall, which basically drove driving habits down, as consumers were driving less and less each quarter, **AutoZone** continued to generate positive same-store sales. Now we view that as a big plus. In a business like that, when you have consumers demanding less and less and less of a product, yet the store is able to continue increasing its share of the pie, we really like that. In essence, **AutoZone** will be grabbing market share from its competitors, while at the same time, continuing to deliver its high rates of return on its assets. What's also interesting about the **AutoZone** story is how it changed its behavior relative to what the company had been doing.

Before the company had been pursuing kind of a growth-at-any-cost strategy and as a result of that, it was really driving down the returns that it generated on its assets and its Economic Margin was consistently declining. Starting roughly in 2000, 2001, the company again changed directions and said, look we need to increase the yield from our

existing businesses and our existing investments, and since then, it has slowed down its rate of expanding new stores and instead focused on making its existing stores that much more profitable, and that's turned out to be a really nice pick for us over time.

1-Year Daily Chart of Auto Zone



Chart provided by www.BigCharts.com

1-Year Daily Chart of Cisco Systems



Chart provided by www.BigCharts.com

TWST: Those all have been consumer-oriented to some degree. What about other areas?

Mr. Resendes: It's kind of the same story that tends to apply in technology. **Cisco** (CSCO) is a great example. If you looked at **Cisco** in 2000 and you actually looked at what sales growth was priced into the stock, you were looking at a stock that had roughly 65% a year sales growth built into its stock price in order to support that market cap valuation. The company had to grow at 65% a year; for a small company that may be achievable, but for a company that had become as large as **Cisco**, just seemed unreasonable. In fact, if you looked at what sales growth **Cisco** deliver the next year, it was closer to 20%, still very good, but so far below the market's expectations, it's not surprising that **Cisco** underperformed the S&P by about 60% from 2000 through 2001. When you look at **Cisco** today, you have a very different situation. We were able to recently add to our position in **Cisco** with the expectation that **Cisco** is going to shrink its top line by 5% a year over the next five years. Again, as I said earlier, you never know how the future is going to turn out and

you can't forecast the future, but it's very similar to a casino underwriting 50 tables of blackjack. You never know how one hand is going to turn out, but if you can fill the tables with players playing blackjack, over time statistics will work in your favor, and as a casino owner you will make money. This is the way we like to look at companies. We never know with any one company how its future is going to turn out, but when we identify opportunities that we believe are mispriced such that the odds are in our favor over a three- to five-year horizon that the company will execute its business plan and we can buy that business plan at a discount, we feel really good about putting on these types of positions and we can see this happening at **Cisco**.

1-Year Daily Chart of Google



Chart provided by www.BigCharts.com

We recently purchased **Google**, with roughly the same idea. In other words we didn't like **Google** when it was trading up about \$720, but when it's in the \$350 range it looks much more attractive. We are basically able to buy **Google** for about 5% a year sales growth. Again, we don't know how things are going to turn out, but we think the moves they are making with the Android cell phone platform make a lot of sense. As the 3G networks get built up throughout the US (and they are already in existence elsewhere), cell phones will surf the Web better and people will use them more for search. We think **Google** has made a really strong play to establish a nice foothold there. Again, the concept underneath what we're trying to do is to identify companies that are able to create economic value, identify the management teams that know how to build value and grow their businesses to create value and then lastly, with the valuation framework that we've been using at The Applied Finance Group for the last 13 years, identify companies where the expectations on the table seem very reasonable relative to their ability to meet or exceed those expectations. So that we try to limit our downside and set ourselves up nicely for upside surprises.

TWST: What you do for your sell discipline and do you set sell targets in your stocks?

Mr. Resendes: We do. Our sell discipline — again, it looks at the factors that we started with. All of a sudden we do the reverse checklist that started our buy process. Once a firm fails to meet our valuation attractiveness, or its management team adopts a strategy

that is not consistent with creating value, or its earnings quality deteriorates, we look to sell. We're constantly evaluating our holdings against other opportunities with any sector. That's another area where the analyst's importance comes into play because they are constantly monitoring the relative valuations of every holding we have against all the other investment opportunities available to us within each sector and within the market cap constraints that we work with. The sell discipline is basically the inverse of the buy discipline.

“Our ability to link up a systematic process with an analyst review is something that most firms don't tend to do. They tend to have fundamental, analyst-driven approaches or more systematic, quantitative approaches, and we are one of the few firms that have 13-years of experience combining those processes together, linking a systematic fundamental process with ongoing data of the circumstances of the company.”

TWST: What about risk control? What are the risk management techniques that you incorporate within your investment process at the portfolio level and at the individual security level?

Mr. Resendes: Let's start at the individual security level first. There was actually an article recently in *Investment News* by David Hoffman and the title was “Fund Managers Shift Focus to Risk,” and the upshot of the article was that historically, portfolio managers viewed risk in terms of volatility. We've never taken that perspective. We've never really viewed company risk defined by the volatility of its price action. In fact, we view volatility as something that creates opportunity, because that's ultimately where we are able to trade our longer-term horizon against people with a very short-term horizon. That's what creates a lot of dislocations in the market. That gives rise to very interesting and attractive long-term opportunities. What the article talked about was how fund managers and analysts are now shifting toward understanding a company's balance sheet more, understanding its leverage and understanding its return on investment. The interesting thing about that is, that's something we've been doing with the Applied Finance Group and we've been providing that type of research to investors for the last 13 years.

In particular, whenever we evaluate a stock in order to understand whether the company is creating value or not, we review the company on a risk-adjusted rate of return basis. We specifically account for a) leverage, with more levered companies expected to generate a much higher rate of return to compensate us for their risk, and b) size, the bigger the company the more stable it tends to be and the more likely they will be able to access funds as capital dries up. We view those companies as a little safer than smaller funds. If you think of risk at a firm level, a small, highly leveraged firm tends to carry a much greater risk

differential, in our view of the world, in terms of the types of returns management must generate, than a very large, unlevered stock. In addition, what we've been looking at lately has been its capital structure, not just whether it's levered or not, but in particular, whether the leverage is of a long-term nature or short-term nature, in the sense that companies that are required to refinance their debts or access capital markets have just been getting slaughtered. One of those things that we have been looking to do is to try to avoid or minimize our exposure to firms that

have significant short-term capital funding requirements. Those are the individual stock level things that we review in assigning company risk.

At the portfolio level, again, because we tend to have relatively smaller positions in stocks (our portfolio is 65 to 80 names, so the typical stock tends to have less than 2% at any point in time), we diversify across names and secondly, we're diversified across all sectors. Almost by definition we've built a very cohesive step of risk management principles into the underlying structure of the Fund from the get-go.

TWST: What do you think gives Toreador its edge? What is distinctive about your approach to investing that differentiates you from other large cap investors?

Mr. Resendes: Number one would be the ability to pick stocks, because so many firms tend to rely on things such as p/e multiples to evaluate whether the stock is cheap or expensive. I believe that's a very naive way to think about value because for the typical stock, earnings tends to represent about 40% of cash flow. If you believe ultimately that cash flow determines value, when you look at a p/e ratio, you're missing, for the typical company, 60% of what drives the firm's value. It's a very convenient metric, but it's not a very insightful metric. The other thing about relying on something like a ratio, and this is another area that we've sort of pioneered over the last decade and a half, is the concept of applying competition to valuation. What I mean by that is, over time — and we made a study on this a number of years ago at a client conference that we hold annually — if you looked at the best performing companies in terms of return on investment and the worst performing companies in terms of return on investment and then you subtracted out the risk of those firms or their cost of capital, so again, you deal with just that excess return or the Economic Margin these companies generate, and then you go back and

review these firms 10 years later, what you'd find is that the top group had lost roughly 75% of its excess returns and the bottom group had made up about 75% of its excess negative returns.

In other words, competition is always at work driving companies' returns to where they should be, which is basically their cost of capital. A lot of analysts that perform discounted cash flow valuations never incorporate that concept into their work. They tend to use a traditional five-year projection period and then capitalize those earnings at the end. I know this first hand, as for the past four years I have trained analysts on five continents on behalf of a program sponsored by the CFA Institute. So I would say the first thing that differentiates us from most fund managers and firms is the passion at Toredor toward valuation technology. I think very few firms invest as much as we do to continually understand how valuation works and how securities are priced and linking corporate performance, or how well the company is doing in terms of its performance, to what the company's worth in terms of its value. So that's number one.

I think the second thing that differentiates us is our structure. Our ability to link up a systematic process with an analyst review is something that most firms don't tend to do. They tend to fall into one camp or the other. They tend to have fundamental, analyst-driven approaches or more systematic, quantitative approaches, and we are one of the few firms that have 13-years of experience combining those processes together, linking a systematic fundamental process with ongoing data of the circumstances of the company.

Then the last piece that differentiates us is our experience in applying these concepts to a portfolio and again, because we've been in the business providing research over the last 13 years through The Applied Finance Group, this is something that we're very comfortable and very familiar with.

TWST: Who are your typical clients?

Mr. Resendes: The typical Toredor clients are registered investment advisers, folks that basically tend to have two parts of their business — they tend to work with individuals and build distinct portfolios for them and then they also have clients where our mutual fund is more appropriate. They've probably heard about The Applied Finance Group's research process, they like it, they want to have that same process applied on a mutual fund basis, so they move forward and select Toredor as the vehicle for the funds they put into the large cap space.

TWST: What challenges ahead do you foresee that investors should be wary of now, particularly concerning your large cap stock arena?

Mr. Resendes: There are a number of challenges, but I think the biggest challenge investors have to be aware of is coming to grips with the emotional cost of investing right now. What I mean by that is, if you look back historically, it's very difficult to really time the bottom of the market, and if you try to move your assets around back and forth and jump in and

out of the market, I am sorry but you're probably going to miss out when the market really starts to run. Then you go through different levels of regret. In other words, let's say you take your money out now, because things look so bad. Well, things do look "so bad" now, but they tend to be priced in, so this is where you get your better, longer-term opportunities to be in the market. Let's say you take your money out now, and then next month the market goes up 10%, and you look at that you go, "Oh jeez, I missed that 10% and that's too bad. But let me just buy when it dips again." Then the market stays flat for a while and then it jumps another 7% or 8% and you say to yourself, "Damn, I missed that one, but when it dips again, I am going to step up and I am going to buy it." Then maybe the market dips a little bit and you start looking at all the news around you and you realize, "God, things don't look so good. Let me just wait a little bit longer." You wait a little bit longer and boom, the market jumps up again.

There are numerous studies that look at type of behavior and conclude that basically investors often end up chasing returns. While the market may be up big over a longer period of time, investors that are moving from one fad to the next and then to the next constantly miss out on superior longer-term returns. I think emotionally or from a behavior of finance perspective, that's one of the biggest challenges investors have to basically steel themselves for. They should say, "Look, I am not investing for next week, I am not investing for next month. This is something I am looking to do over the long run." You find that you create an intelligent investment strategy and appropriate investment allocation and then you should try to purchase into that allocation consistently over time. I think what we are seeing now is stocks are priced such that over the next three to five years, people are going to make a pretty handsome penny from today's prices. This is a longwinded explanation, so I will get to the final punch line. I would say, people shouldn't focus on finding the market bottom, they should identify points in the market from which they can make money, and I think at today's prices, we certainly are at such a level. This may not be the absolute bottom, but if you have patience and a reasonable time horizon, you can make money from these levels.

TWST: Thank you.

Note: Opinions and recommendations are as of 12/2/08.

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