Individual Investors Reveal the Advantages They Have Over Professional Money Managers

As investors, it's hard to ignore the run the stock market has been on since November. Last week the Dow Jones industrial average pushed through the 21,000 mark only 24 trading days after clearing 20,000, tying the record for the quickest 1,000-point move from one millennium round number to the next. The 24 trading sessions between January 25 and March 1 matched the time it took for the index to climb from 10,000 to 11,000 in 1999, according to The Wall Street Journal. The Dow also fell one day short of setting achieving a first in its 120-year history. If the index had closed with a gain last Tuesday, it would have set a new record close on 13 consecutive trading days. Instead, it had to settle for 12. In addition, the S&P 500 has gone 98 trading days without a loss of more than 1%, the longest stretch since 1995, per The Wall Street Journal.

According to Schaeffer's Investment Research, when the S&P 500 starts a year with gains in January and February, the index has gained an average of 12% the rest of the year and was positive 92% of the time. In all other years, the index has gained an average of 5% from the start of March through the end of December and is positive 61% of the time. Of course, past history is no guarantee of future performance.

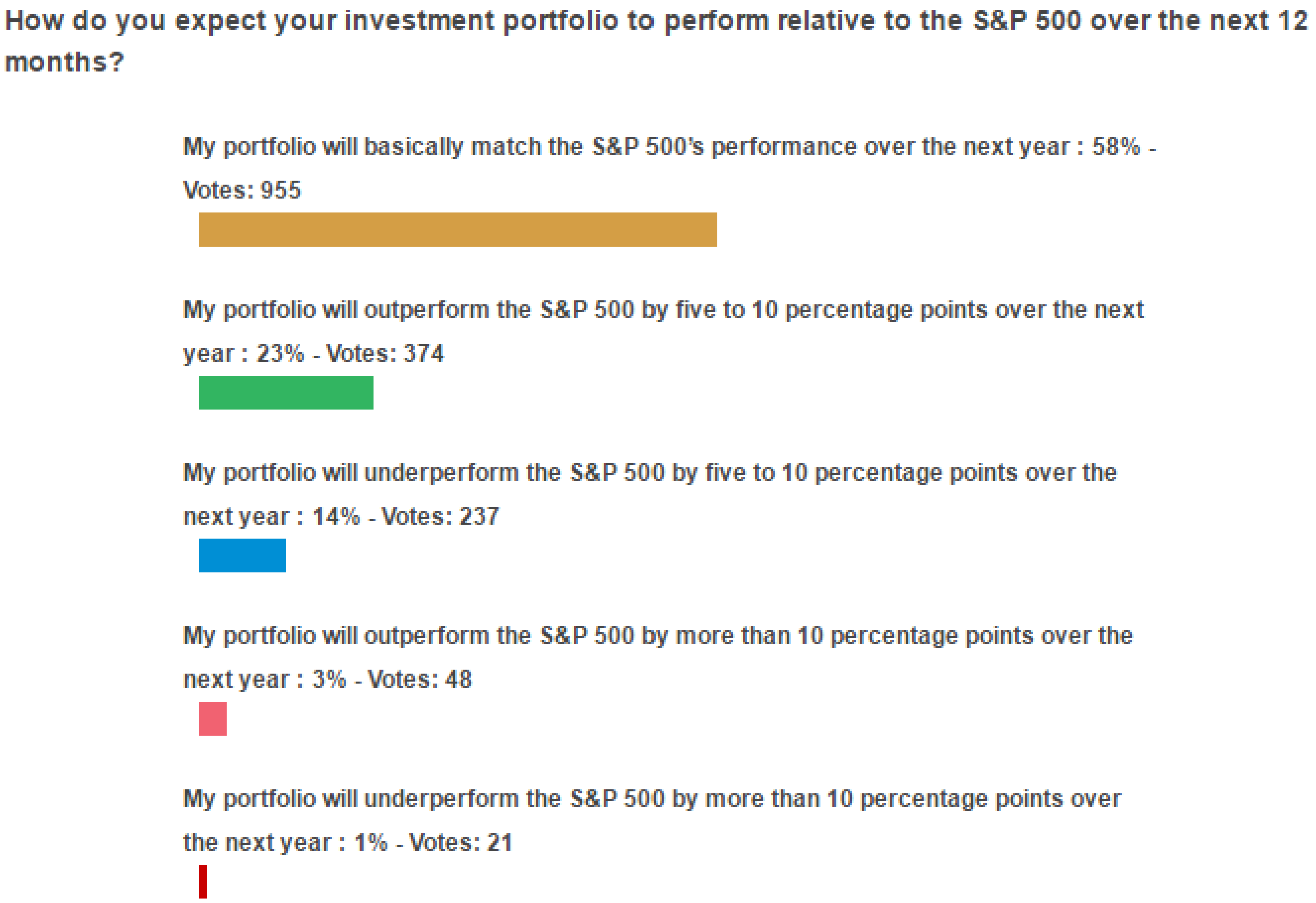
While history is on our side when it comes to the market's expected results for the rest of this year, as a contrarian investor I am certainly keeping an eye on the market's lofty levels.

AAII Weekly Survey Question

Given the returns the market has generated over the last several months, I was curious to know how our readers expect their own portfolios to do relative to the market over the next year. So I posed the following question to our readers:

How do you expect your investment portfolio to perform relative to the S&P 500 over the next 12 months?

Here are the results:



In all, 1,635 readers responded through 6 a.m. (Central) on Sunday, March 5. Of those, the majority (58%) believe their portfolio will basically match the performance of the S&P 500 over the next 12 months.

Roughly one-quarter (26%) think they will be able to outperform the S&P 500 over the next year, with 88% of that group believing they can beat the S&P by five to 10 percentage points, while the other 12% think they can do more than 10 percentage points better than the S&P 500.

Only 15% think their portfolio will underperform the S&P 500 over the next year. Of those, however, 70% think they will underperform the S&P by more than 10 percentage points and the other 30% think their underperformance will range from five to 10 percentage points.

Weekly Special Question

Here at AAII, our mission it to help individual investors become more effective managers of their own assets. We feel that individual investors are in a unique situation whereby, with patience, discipline and knowledge, they are able to do better than professional investors.

However, many individual investors feel the deck is stacked against them, and professional money managers and high-frequency traders have an unfair advantage. To see what advantages our readers think they have over professional investors, last week's special question asked:

What advantages, if any, do individual investors have over professional money managers?

Luckily, out of the 140 readers that responded, the overwhelming majority think individual investors hold some advantage over the pros. In fact, only 6.4% of respondents said that individual investors have no advantages over professional money managers.

I was a bit surprised, though, by the number of readers who said that individual investors are at an advantage since they are not paying management fees. However, it is important to remember that even if you are making you are managing your own investment portfolios, you are still paying "fees" in the form of commissions, bid-ask spreads, etc. Investors who do not pay attention to these costs could end up paying much more than they would to have a professional oversee their assets.

The most widely cited (19.2%) advantage our readers see individual investors having over professional money managers is a longer time horizon. This means individual investors don't have to worry about quarterly performance reviews; can hold onto weak price performers they believe are fundamentally strong; and don't have to sell at the wrong time to satisfy redemptions.

Another 14.2% of readers said that individual investors are at an advantage in that they have a broader investment universe from which to choose, including **micro-cap stocks** and illiquid investments.

Flexibility was cited as an advantage individual investors have over professional money managers by 10% of respondents.

Here is a sampling of the responses:

- "[Individuals] can use a longer time horizon and be less focused on tracking a benchmark within shorter time frames [and] can invest in smaller cap names without impacting bid/ask [spreads]."
- "Flexibility to invest in anything desired [and the] ability to react quickly when warranted."
- "Individual investors generally have no pressure for short-term gains [and] can more easily ride out a downturn without having to "do something."
- "Not tied to orthodox approaches: e.g., 60/40 stock/bond split [and] can invest in areas where large institutional investors can't."
- "An individual can invest long term instead of quarter by quarter."

- “Do not have be concerned with peer performance.”
- “You may know more about your individual risk tolerance. You may better understand your time horizon.”
- “It is our skin in the game. True, we may lack some market knowledge, but do not have the pressures to perform in the short term.”
- “[Individuals] do not have to worry about redemptions.”
- “Not many. When you need to do something that you are not skilled in you hire a professional and that goes for money managers. Unless you are very skilled in that field and have the time they do to do research, etc. you should turn it over to someone who has the knowledge, contacts and time. It is a no brainer. You hire and pay for a specialist. Naturally, you monitor their work and success and if they are good you stay with them and use your free time to do other things.”

Everybody has an opinion! Why not give us yours? Participate in our weekly member poll, updated every Monday, and see the results online at http://www.aaii.com/memberquestion.