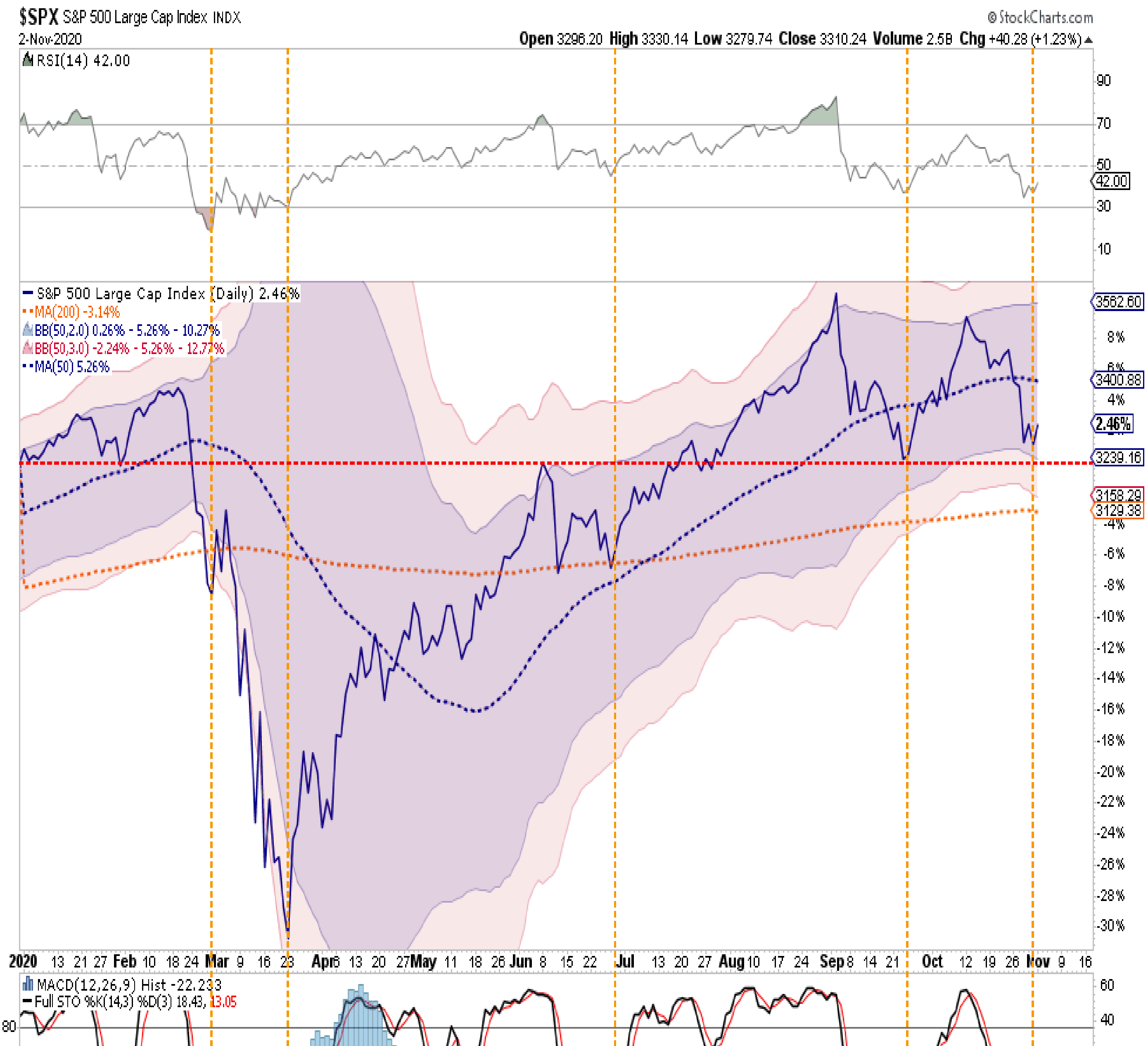
In ***"Policies Over Politics,"*** we discussed the markets' historical trends during the presidential election years. That data mostly assumes the election process goes smoothly, and a President is declared quickly. However, in 2020, a very different outcome is likely as the surge in *"mail-in ballots,"* not to mention potential lawsuits, will delay the outcome. For this reason, investors need a clear set of rules to navigate a contentious election.

Oversold Bounce

In this ***past weekend's newsletter,*** we discussed the short-term oversold condition of the market.

> *"All of our 'sell signals' have been intact for the last few weeks suggesting more downside risk near term.* ***Those signals have now reversed to the point where we are likely to see a decent reflex rally starting as early as Monday.*** *As noted in the year-to-date performance chart below, the market is 2-standard deviations below its 50-dma and is close to the September low support. Performance is positive year-to-date at 2.46%."*



On Monday, the markets did indeed bounce at the open, rising more than 1% from Friday's close. However, that opening momentum was unable to hold as investors used the rally to sell. Such is not surprising as we head into what will undoubtedly be a volatile next two weeks.

Increasing Hedges For An Unexpected Outcome

As we have repeatedly discussed, we have been gradually raising cash and rebalancing portfolio risks as we head into the election. We raised cash levels, reduced our bond portfolio duration, and rebalanced portfolio risk to lower volatility. On Monday, we added a short-S&P 500 index position to increase our downside hedge. **If on election night, we have a repeat of the 2016 election, and markets surge as results come in, we will remove our hedge and let our equity exposure run unfettered.** Given the more oversold condition of the market currently, there is a reasonable possibility we could see a rally if there is a *"concession"* by one of the candidates.

However, as noted, with the massive number of *"mail-in"* ballots, it is highly unlikely to see a *"concession"* from either candidate for up to 10-days post-election as the counting of ballots concludes and votes certified. Then comes the *"electoral college"* which is another issue entirely. We believe our current positioning is correct. We currently carry less than 1/2 of the market?s volatility and have plenty of cash to adjust risk accordingly. Once we have a more apparent outcome of the election, we will begin to make our next decisions. The following rules, really more guidelines, may be useful in helping you navigate the markets over the next several months.

Investing Rules To Follow

Investing, particularly in highly uncertain environments, requires focusing not only on increasing current capital allocations but also on preserving that capital. As any *"professional gambler"* knows, if you lose your *"stake,"* you are *"out of the game."* **The following are some guidelines that have served investors well over the years. They are not new or innovative, but they are time-tested and battle-hardened.**

1. Buy low, sell high.

> *As obvious as this seems it is the one thing that most investors do exactly the opposite of. Your ability to consistently buy low and sell high, will determine the success, or failure, of your investments. The simple reality is that 100% of your rate of return is determined by when you enter, or leave, the stock market.*

2. The price of the stock market is always right.

> *The only thing that truly matters in investing is the price. If prices are rising - then you are long the market. If they are falling; you are in cash or short. **What you 'think' the market should be doing at any given time is irrelevant.** With all things being equal, the longer you stay on the right side of the stock market, the more money you will make. The longer you stay on the wrong side, the more money you will lose.*

3. Every market or stock that goes up will go down and vice versa.

> *The more extreme the move up or down, the more extreme the movement in the opposite direction once the trend changes. This is also known as **the "trend always changes" rule.***

Rules To Wealth Building

4. Your career provides your wealth.

> *You most likely will make far more money from your business or profession than from your investments. Only very rarely does someone make a large fortune from investments, and it is generally those that have a business investing wealth for others for a fee or participation. (This even includes Warren Buffett.)*

5. Don't assume you can replace your wealth.

> ***The fact that you earned what you have doesn't mean that you could earn it again if you lost it.*** *Treat what you have as though you could never earn it again.* ***Never****, take chances with your wealth on the assumption that you could get it back.*

Trading Rules

6. The trend is your friend.

> *Since the trend is the basis of all profit; understanding both the long and short-term market trends are useful in understanding the risks versus the reward in putting capital at risk.* ***Contrary to the short-term perspective of most investors today, all the big money is made by catching large market moves - not by day trading or short term stock investing.***

7. You must let your profits run and cut your losses quickly.

> *This is the key to investing success. Trading discipline is a necessary condition of investment success. If you do* ***NOT*** *have a highly disciplined approach to trading - you will not make money over the long term.*

8. Traditional technical and fundamental analysis alone may NOT enable you to make money in the markets consistently.

> ***Successful market timing is possible but not with the tools and analysis most people employ****. The problem with most analysis is it is biased to sell product and, therefore, is optimized, employs data mining, subjectivism, or other such statistical tricks to promote a specific perspective, opinion or objective.* ***Focus on what the data is telling you rather that what you want it to be.***

9. The worst thing an investor can do is take a massive loss on their position or portfolio.

> *You can avoid making that huge mistake by avoiding buying things when they are high.* ***It should be obvious that your starting point is critical in determining your total return****, if you buy low, your long-term investment results are irrefutably better than someone who bought high.*

The Psychological Side

10. The most successful investing methods require changes at the margin.

> *A strong investment discipline requires patience, discipline, and work. However, once a portfolio is built and operational maintenance is a function of changes at the margin.*

> ***Investing is a long-term process with a view towards changes of trend. Such a portfolio requires very few changes between major trend changes****. If you are trading regularly - you are speculating and will eventually wind up losing more money than you made.*

11. Don't use leverage.

> ***When someone goes completely broke, it's almost always because they used borrowed money.*** *Using margin accounts, or mortgages (for other than your home), puts you at risk of being wiped out during a forced liquidation. If you handle all your investments on a cash basis, it's virtually impossible to lose everything?no matter what might happen in the world?especially if you follow the other rules given here.*

12. Whenever you're in doubt, it is always better to err on the side of safety.

> *If you pass up an opportunity to increase your fortune, another one will be along soon enough. But if you lose your life savings just once, you might never get a chance to replace it.* ***Always err on the side of caution. Always ask the question of what CAN go "wrong" rather than focusing on what you "HOPE" will go right.***

Beware Of The Media

It is extremely easy to get sucked into the media headlines and narratives. Such is why I turn off the media during the trading day and focus on what the markets are telling me. Such is also why I saved the best rule for last.

13. Create a bulletproof portfolio for protection.

> ***A portfolio of low-risk investments, fixed income and a healthy level of cash will ensure that no matter what happens in the markets, or in your life, you will be in a financially sound position to handle it.*** *A portfolio should be able to survive any uncertainty that arises and in today's world, there are plenty of uncertainties to choose from. It isn't difficult, or complicated,* ***to build a portfolio that can deliver lower volatility, income, and capital preservation.***

Yes, taking some defensive action before the election may lead to missing a short-term bottom if we get a repeat of the 2016 election night bounce. **That?s okay; you can put the cash to work the next day.** However, if a negative outcome occurs, you will have an opportunity to *?buy?* quality investments at a lower price from those panicking to sell. The financial markets will do one of two things to your future financial security:

1. *If you treat the financial markets as a tool to adjust your current savings for inflation over time,* ***the markets will KEEP you wealthy.***
2. *However, if you try and use the markets to* ***MAKE you wealthy, your capital will shift to those in the first category.***

Ample warning signs suggest the risks of having excessive equity exposure to the market outweighs the potential for reward. At least for now.