



Mark Hulbert

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## Great Rotation equals sloppy thinking

Commentary: Can the rotation chatter withstand critical scrutiny?

By **Mark Hulbert**, MarketWatch

CHAPEL HILL, N.C. (MarketWatch) — Have you been gullible enough to believe all the recent talk about a Great Rotation? If so, I have a bridge I want to sell you.

### THE 'GREAT ROTATION' DEBATE

- [Is 'Great Rotation' the real deal? \(\\$\)](#)
- [Pimco's Gross a rotation-skeptic on Twitter](#)
- ['Great Rotation' equals sloppy thinking](#)
- [Now playing: 'The Great Rotation'](#)
- [Bond links: The 'Great Rotation' debate](#)

definition — no under- or overownership.

To forecast an asset allocation shift by one group of investors, therefore, you logically must also be forecasting an equal and opposite shift on the part of all other investors.

But who might those other investors be who are going to be so willing to increase their bond holdings and decrease their equity holdings?

Indeed, a cynic might wonder if the whole notion of a Great Rotation has been concocted to assist those other investors in unloading their equities at higher prices.

John Hussman, chief investment strategist for Hussman Funds, is one such cynic. He suspects that one motive for the notion is “a desire to distribute overvalued institutional holdings onto the unwashed muppets.”

In any case, even if we focus only on the individual investors who the Great Rotation adherents think are “overinvested” in bonds and “underinvested” in equities, it’s worthwhile to ask what this really means — “over” and “under,” relative to what standard?

### Apple vs. Einhorn: An analyst's take

Investor David Einhorn has come out against an Apple proposal to eliminate preferred stock. What's the analyst take on it?

Might that standard be the average equity-versus-fixed-income allocation that individuals have had at different points in the past? Well, what past period should be chosen? What should be considered normal?

Claude Erb, a former commodities and fixed-income portfolio manager for Trust Co. of the West, argued in an interview that it's possible that the average individual's allocation shift in recent years away from equities into fixed income was entirely rational. In that case, of course, there is no reason to expect any shift in coming months.



Treasury Direct.gov

Image of a vintage U.S. Treasury H bond.

I was prompted to interview Erb after reading a recent study he co-authored with Campbell Harvey, a finance professor at Duke University. Their study, published by the National Bureau of Economic Research in Cambridge, Mass., focused on, among other topics, the related notion of whether gold is underowned. [Read their study at SSRN.com.](#)

In my interview with Erb, he reasoned that the Baby Boomer generation — which has exercised an outsized impact on the behavior of the average individual investor — has in recent years been getting close to, or reaching, retirement age. A reduction in portfolio risk was an appropriate response.

To support the Great Rotation thesis, Erb continued, you have to argue that the Baby Boomer generation overshot its target while reducing portfolio risk over the last decade. If so, of course, equities will benefit if and when the Baby Boomers decide to correct their mistake.

It's difficult, if not impossible, to know which of these explanations, or others, is true, Erb continued: "We have only one data point with multiple explanations."

Another reason to question the Great Rotation argument is that it could have been advanced before. What makes today any different than those other times, other than that this time around the forecast comes packaged with a fancy title?

At any point since this bull market began in March 2009, for example, bond-heavy individual investors could have decided it was time to shift some of their fixed-income allocation into their supposedly undersized equity allocation.

And don't kid yourself that this time is different because interest rates have finally started to climb back up. There have been other periods in the past couple of years when rates have increased by as much as, or more than, they have recently.

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When I asked Erb whether he thought there was any good reason why the Great Rotation hypothesis should only be advanced now rather than at those other points in recent years, he said no. "There is absolutely no reason in the world," he said.

So the next time you hear someone pontificating about the Great Rotation, ask them why they weren't making similar pronouncements on those functionally equivalent occasions of the last four years.

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