

## Just How Many Years Are Required to Make an Investment Long Term?

People like Warren Buffett have made substantial profits from smart long term investing. Just how many years are required to make an investment long term? We can get a hint from the so-called Oracle of Omaha who says that he cannot outguess the market in the short term but has a pretty good idea of what will sell well ten years hence. Thus we should not be surprised when *Market Watch* says **long run for investing is longer than you think.**

*There are certain truths that are etched into the brains of investors. They know that in the long-run, their portfolio returns will be close to the historic average of the stock market. In the short-run, they know that returns will fluctuate wildly. However, many investors have an unrealistic idea of when the short-run ends and the long-run begins. My clients are often stunned when I tell them that in the stock market, five years is a short-term time horizon.*

*From Feb. 1, 1988 to Jan. 31, 2017, the S&P 500 generated an average five-year compound rate of return of 9.83%. However, during the worst five-year period from March 1, 2004 to Feb. 28, 2009, the S&P 500 compounded at a rate of minus 6.63%. At the other extreme, the S&P 500 compounded at 28.56% from Jan. 1, 1995 to Dec. 31, 1999, according to S&P Dow Jones Indices.*

*Unfortunately, this wide-dispersion of returns causes investors to make big mistakes regarding their investment strategy or their investment professionals.*

So, you need to stay in the market for longer than 5 years and perhaps even longer than 10 years to see the benefits of long term investing. But, what stocks do you buy. And when should you sell before waiting 5 or 10 years or longer?

### How Does a Company Make Money?

For decades Eastman Kodak had a fantastic business model making film for cameras. Then digital came along and Kodak's business model did not work anymore. On the other hand people still drink Coca Cola, eat M&Ms and use laundry soap. An investor could do a lot worse than follow Buffett's thinking and pick stocks of companies that have been selling everyday items for years and will likely continue to do so for decades to come. Is there a good guide for when to buy and when to sell even though we are thinking in terms of a decade or more?

## **Intrinsic Stock Value**

What is a stock selling for and what is it really worth? Many say that the market today is overvalued. That means that at current prices you are buying stocks that may well correct downward in the near future. A useful concept is **intrinsic stock value**.

*In the aftermath of the stock market crash of 1929 in the early days of the Great Depression Benjamin Graham introduced the concept of value investing. No longer would those buying and selling stocks need to act like they were at the casino. With the concepts of intrinsic value and margin of safety Graham taught investors a rational means of investing in stocks.*

*The dictionary definition of intrinsic stock value is its fundamental value. It is obtained by adding up predicted future income of a stock and subtracting current price. It can also be seen as actual value of an equity versus its book value or market value.*

Calculating intrinsic stock value takes into account the long term. If you see a Kodak-like situation emerging with a stock you will likely see that its intrinsic value is substantially below its market value. That is a stock to sell. Likewise if a company shows long term promise its intrinsic value may well exceed its market value and it is a stock to buy and hold. Then, to take advantage of the market you need to hold the stock for a decade or more in order to see the long term benefits of buy and hold investing.

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