INVESTING WITH 20/20 VISION

Scott M. Yates, *CIM*
Portfolio Manager

Raymond James Ltd.
Suite 4100, 525 – 8th Avenue S.W.
Calgary, AB T2P 1G1

T: **403-221-0359**
TF: **1-844-459-0359**

scott.yates@raymondjames.ca

www.raymondjames.ca/scottyates

Here is an outline for this, my first quarterly client letter for 2020:

- Market predictions and economic forecasts don't work.
- In fact they often do more harm than good.
- The 'experts' are prone to greed and fear, just like the novice investor.
- Besides ***"What will the stock market/economy do this year?"*** is the wrong question anyway.
- What IS the right question for investors in 2020?
- Given that the future is unknowable, how can we invest with "20/20" vision?

Market predictions and economic forecasts don't work

> ***"The year came and went. Stocks went down and then up more than they went down. As is the way, predictions were made (almost all wrong) and then once the future showed up, quick explanations were made as to what happened and why. This was followed by a whole new slew of predictions. In short, it was business as usual for the market."*** - *Matt Wood*

At the start of every year we're inundated with market "outlooks" and "forecasts". And while many *novice* investors seem to want to hang off of every word, the *'intelligent investor'* will recognize these for what they really are - *nothing more than a guess*. According to Warren Buffett, the world's greatest investor: ***"We've long felt that the only value of stock forecasters is to make fortune tellers look good."***

As such, one of the worst things we can do is base our current investment strategy on *anyone's* near-term outlook for the stock market or the economy. We simply refuse to play any sort of a guessing game with your investments and your financial success!

In fact, they often do more harm than good

Peter Lynch, a wildly successful portfolio manager, considered it futile to predict the economy. Here is one of his most famous quotes: ***"If you spend more than 13 minutes analyzing economic and market forecasts, you've wasted 10 minutes."***

Not only are market forecasts and economic commentary largely a waste of time, they can also do more harm than good to your portfolio. Many 'newbie' investors find comfort in *following* 'the herd'.

Given that the consensus is often proven wrong in due course, this tends to leave the novice investor *'wrong footed'* year after year; defensively positioned when they should be more aggressive, and aggressive when they should be exercising caution.

On the other hand, the *successful investor recognizes that the consensus view should be regarded as nothing more than a good contrarian indicator*. Here's what the data shows, according to Richard Bernstein Advisors LLC:

> ***"For nearly 30 years, we have surveyed Wall Street strategists for their recommended equity allocation. Through time this survey has shown to be a very reliable long-term sentiment indicator. In other words, it has historically been bullish when Wall Street suggested underweighting equities and bearish when they suggested over-weighted positions."***

When the experts were bullish, stocks proceeded to go down, and when the consensus was bearish stocks actually went up! (This is also known as the 'bull/bear sentiment indicator'; again, a *contrarian* indicator). As the above survey shows, investors would have been better off *doing the opposite* of what the "expert consensus" recommended. Let's give Buffett the final word on this particular subject; ***"Forecasts may tell you a great deal about the forecaster; they tell you nothing about the future."***

The 'experts' are prone to greed and fear, just like the novice

The forecasters themselves are, of course, human (…in most cases!). As such, they too are influenced by human emotions like greed and fear. As evidence, let's do a quick review of the 'expert' sentiment over the past couple of years.

Going into 2018 the mood was generally optimistic and the overall market sentiment was bullish. According to the 'experts' – investors should overweight stocks. In turn, the stock market (as per the S&P/TSX index) *dropped* by ~11% in 2018. And then, looking *backward* at the dismal results of 2018 (and after stocks had just gone '*on sale*'), market sentiment turned distinctly negative going into 2019. What did the stock market do in 2019? As we all know now, it flourished - *during a year when the expert consensus was decidedly negative?*

As for today, with eyes firmly focused once again on the ***rearview*** mirror, the sentiment has now turned bullish - yet again. Indeed, the experts are singing the market's praises for 2020. We'll consider this enthusiasm as somewhat of a warning sign. In typical fashion, the euphoria comes *after* the stock market just got significantly more *expensive*, AND some might say – more risky!?

These examples explain how, due to human behaviour, even an *educated* guess can end up having *less* odds of success than a coin flip. Even the so-called experts are influenced by their emotions. They too, can't help but become pessimistic *after* a market drop (again, *when stocks are cheap*), and then in turn become optimistic *after* a large advance. While this is human nature, it is obvious to us that any *backward* looking, emotions-driven investment approach clearly does not work. Rather, we adhere to the wisdom of Buffett's mentor, Benjamin Graham; ***"The intelligent investor is a realist who sells to optimists and buys from pessimists."***

What will the market or the economy do in 2020?

An annual market outlook attempts to 'forecast' what will happen over the next 12 months. ***That's the wrong question.*** In the world of investing, when everyone is asking the same question, it's typically the wrong question.

According to Tom Bradley (founder and portfolio manager at Steadyhand), ***"…talking about where the market is going is investing's lowest common denominator. It's like talking about the weather, except it has less chance of being right."***

To the serious investor, the near term gyrations of the market or the economy is of little concern (…other than perhaps, to take advantage of large moves one way or the other! More on that in a minute). We recognize that attempting to somehow predict the unpredictable - the short-term ebbs and flows of the market - is not only a loser's game; it's also not even remotely necessary in order to be successful. Buffett: ***"I can't predict short-term movements of the stock market. I haven't the faintest idea as to whether stocks will be higher or lower a month – or a year – from now."*** If Warren Buffett, the world's most successful investor, can't do it – how is it that anyone else can?

If what the market does in any near term period really matters to you, you shouldn't be in the market. And if you are, clearly you are a speculator – not an investor. A true *investor* would never succumb their serious money to the short-term, *entirely unpredictable*, vagaries of the stock market. After all, who could have possibly predicted things like the current *doom du jour*; the coronavirus?

Referring back to the novice investor, they might view the unpredictability of the markets/economy in the near term as the bad news. To the 'trained eye', this is actually the good news. Let's briefly walk through some examples.

But before we do so, allow me to premise this for you, my client. ***"I'm a serious investor with a serious amount of money*** (…I must add, any dollar amount – regardless of the number of zeroes – is "serious" to you AND me, if it encompasses the entirety of your life savings!). ***I understand that while making money is one thing; managing it – on a full-time basis – is a whole other matter. As such, I have a portfolio that is managed by a professional portfolio manager. My asset mix is appropriately allocated based on my investment time horizon – NOT a market call. My portfolio manager has as much of my money in stocks as I can stomach, and no more. Never enough to make a killing AND never enough to get killed!"***

On that basis, let's say stocks drop ***a lot*** in 2020. Not a prediction, but it could happen. As a client of mine, ***we don't react, we act.*** (*Reacting*, by the way, is the investing equivalent of what we call "*the big mistake*"; buying at or near market tops, and then panic-selling at market lows). We've *already* positioned your portfolio, *in anticipation of the next big market drop*. Not because we knew *when* it would occur but simply because we knew that it *would* occur.

As such, we're not immune from market downturns, but we relish them when they do occur. ***Our mantra during a market downturn: bear markets and recessions are where the real money is made, not lost!*** (Thanks again, Warren). No panic - no sell. No sell - no lose. Not only do we refrain from panic when stocks are temporarily on sale, we go shopping!

On the other hand, let's say stocks continue to go up, ***a lot***, in 2020. As equity investors, by having as much exposure to the stock market as your long-term plan will allow, we're "in the market" – and as such we'll benefit from an ongoing bull market. ***But here's the difference***. We understand that, as share prices go higher and higher, it's time for caution – not euphoria. Referring back to Ben Graham, ***"A large advance in the stock market is basically a sign for caution and not a reason for confidence."***

Counter to the herd, simply by sticking to your long term plan, we'll be net *sellers* of equities when they're expensive (and of course, net *buyers* when stocks are temporarily *undervalued*). To the uninformed, I might ask, *"Who would you rather be when share prices have already appreciated significantly, and stocks are expensive; the buyer or the seller?"*, or *"When house prices are already high, is it a buyer's market or a seller's market?"* Why should the *stock market* be any different?

On a related note, here's a pop quiz from Jason Zweig, who writes *"The Intelligent Investor"* piece every Saturday for The Wall Street Journal: ***"Name the giant store where customers scoff at whatever goes on sale, but flock to buy whatever costs the most? It isn't a supermarket. It's the stock market."***

What IS the right question for investors in 2020?

It's the same as it is each and every year: ***"How can I best position your portfolio to meet your long-term goals and objectives?"*** That's what I'm here for, and that's ALL I do – manage money for folks like you (…and perhaps a little poetry in my spare time).

If your long-term goals and objectives don't change on a day-to-day basis, neither should your portfolio. This, despite the daily "news", and the constant 'zigging and zagging' of stock prices. This approach differs greatly from what I most often hear;

- ***"I'm nervous so I'm going to cash."*** (Translation: Sell low!)
- ***"I feel good; let's overweight equities."*** (Buy high!)
- ***"I hear canola futures/crypto currencies/cannabis*** (fill in the blank with whatever's next) ***is really HOT right now; let's back up the truck!*** (I'm really a gambler, not an investor… AND I like to 'buy high')
- ***"I'm worried about the Fed's policy on interest rates and the impact it'll have on inflation. Shouldn't we be in gold?"*** (I have a crystal ball that allows me to see what no-one else can; the future. In that sense, I guess I'm smarter than Warren Buffett?). And finally;
- ***"My taxidermist says now is the time to be buying real estate."*** (Translation: I really don't have a clue, but I'm open to suggestions, from anyone!)

To reiterate, the "right" question, now, and always: ***"How can I best position your portfolio to meet your long-term goals and objectives?"*** This is do-able. Forecasting the economy and timing the market clearly is not.

Investing with 20/20 vision

What this comes down to is basing our decisions today, on what is far more knowable vs that which is entirely unknowable. Not only is this just plain common sense; it allows us to see clearly amidst a future that is otherwise so very unclear. By focusing on what we know, only then can we formulate a plan for you. *Your plan*, designed toward the achievement of your own unique goals and objectives.

When it comes to achieving investment success, Benjamin Graham had this to say:
"To invest successfully over a lifetime does not require a stratospheric IQ, unusual business insights, or inside information. What's needed is a sound intellectual framework for making decisions and the ability to keep emotions from corroding that framework."

Note the distinct absence of the need for a market outlook or an economic forecast (*and keep in mind, this is from Warren Buffett's mentor!*).

It's my job to provide you with the *"sound intellectual framework for making decisions"* part. I'm relying on you to keep your emotions from corroding that framework. By doing so, we can invest with "20/20" vision, both in 2020 – and beyond.

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