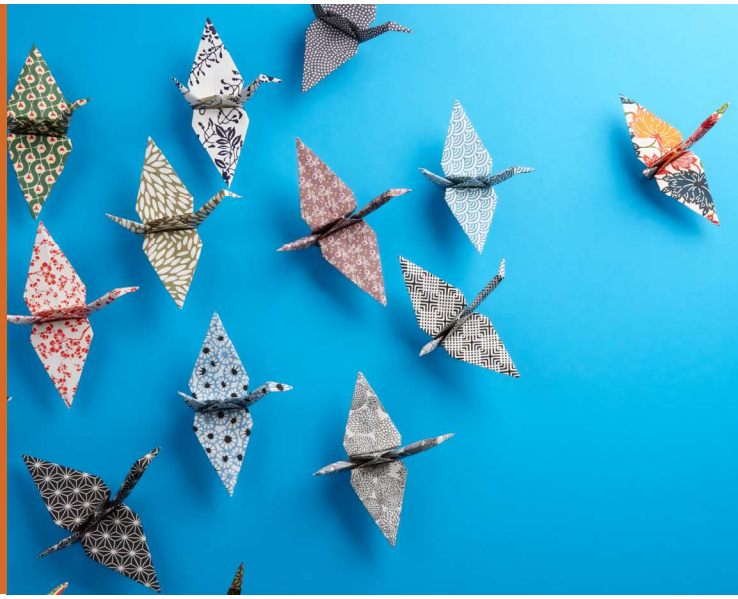
StrategicInsights
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# Investing Insights from Mr. Miyagi

> "The answer is only important if you ask the right question."
> —Mr. Miyagi, The Karate Kid



Last week two clients independently asked "Adrianne, when do you think the markets will stop going down?" Fair question, which others may also be pondering. My thoughts:

First, it is of course normal to wonder "When will markets stop going down?" But that might be the wrong question. A couple of reasons:

1. **There is no accurate answer.** You could analyze every shred of financial data ad nauseum, but you (and I, and anyone else) will never predict short-term market prices. We know this. It doesn't stop us from craving an answer or feeling uncomfortable. But we know this. In the short-term, markets are random. Over time, investment prices are led by earnings.[1] But in periods of weeks and months they are moved (and amplified) by factors like emotions, speculations & perceptions.

2. **If you're following a financial plan, #1 doesn't matter.** To be a successful investor, you don't have to forecast short-term market movements! We control many other elements – broad class allocation, size and style diversification, tax minimization and asset placement (e.g., Trad IRA vs Roth IRA vs Taxable). Why does financial planning work? Because we've identified your spending/burn rate and when you will likely need your funds, net of tax. We build in flexibility to account for your life's variations and uncertainties. And we map your portfolio to you, as it should be, and not the other way around.

## Camp A or B

If you are my client, you are in Camp A or B (or at times a blend of both):

A. **You are *withdrawing* from savings.** Whether you are living off your portfolio or need funds for a planned purchase such as vacation home, the appropriate allocation for these assets is likely not stocks. If you are retired, we have planned ahead and kept 5 to 10 years of savings in non-stock holdings. (As point of reference, the average period *between* S&P bear market cycles is 3.6 years, and average *length* of a bear market is 9.6 months.)[2] Pre-planned allocation removes the fool's errand of timing markets.

Each asset class has its own job. Cash provides value consistency. Bonds provide nearer-term liquidity with less volatility than stocks or real estate and allow us to ride out inevitable declines. For the part of your portfolio you need soon, we stay out of stocks. No timing needed. Just don't put yourself in a precarious position to begin with. To paraphrase Mr. Miyagi, "Best defense in fight: no be there."

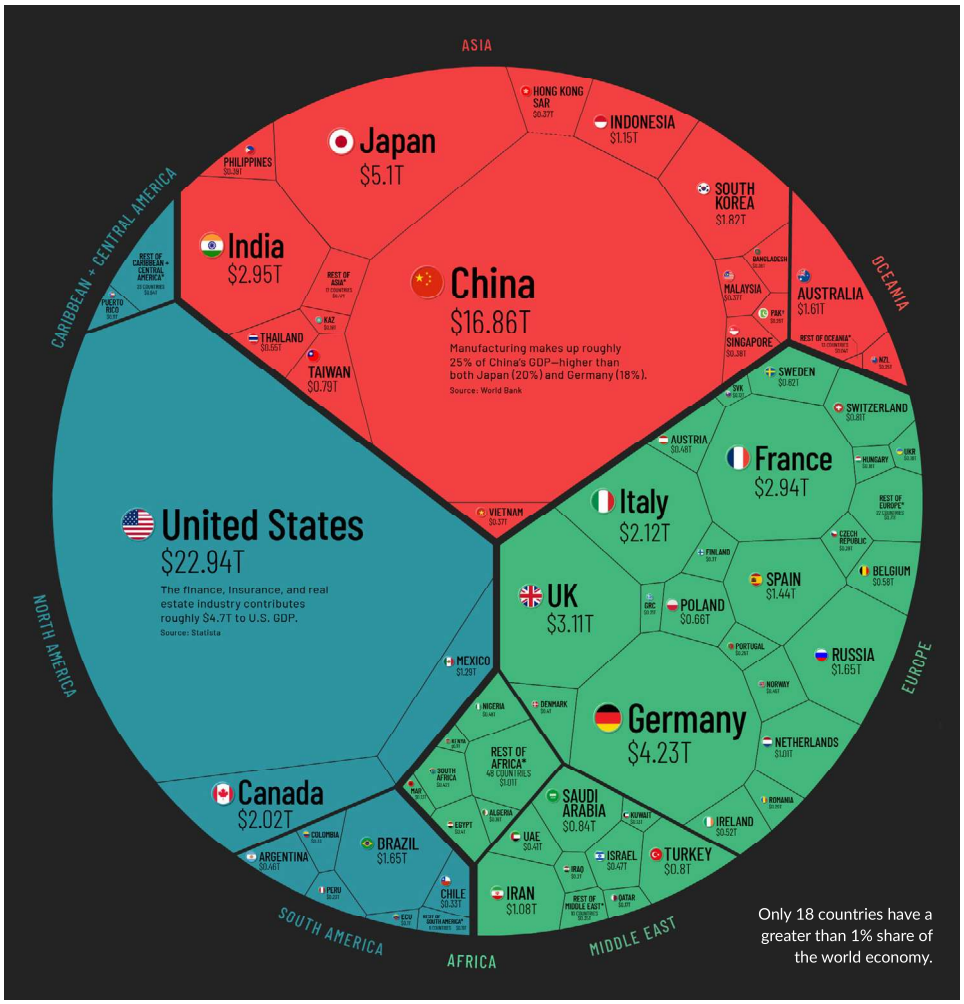
"You shouldn't own common stocks if a 50% decrease in their value in a short period of time would cause you acute distress." -Buffet

But because we still need long-term growth (to outpace inflation and preserve purchasing power), we retain longer-term assets in classes of higher growth, higher volatility instruments (stocks, real estate, alternatives), and the reward for stomaching declines is long-term appreciation.

B. **You are *contributing* to savings.** Market declines work in your favor. You are acquiring shares and building wealth. It feels counterintuitive but is not. When you accumulate assets, what you pay for them is incorporated into your total return. Lower purchasing costs boost ultimate return. I appreciate that it's uncomfortable to see one's net worth decrease. It may help to view it for what it is – as temporary decline which you use to your advantage to build long-term wealth.

## Market recoveries, like declines, can't be timed.

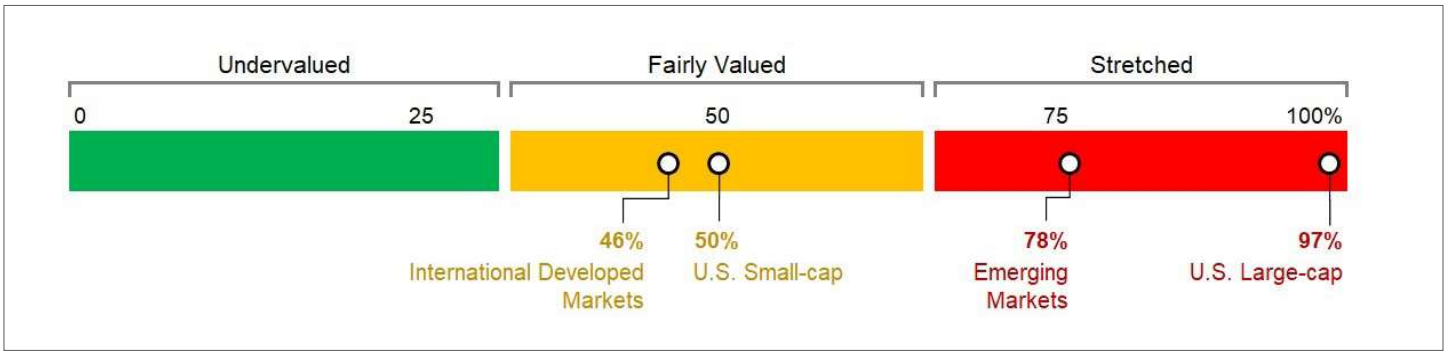
You give away your main advantage in equity investing when you are out of the market. For example, if you had stayed invested in the S&P the last twenty years, your annual return would have been 7.5%. But had you missed the 30 best days (out of 7303 – less than 1% of the time), your annual return **would have been a *negative* 1.49%.**[3]




"Visualizing the $94 Trillion World Economy," Visual Capital, 12/21/21.Graphics Sabrina Fortin & Harrison Schell.

## What in the World?

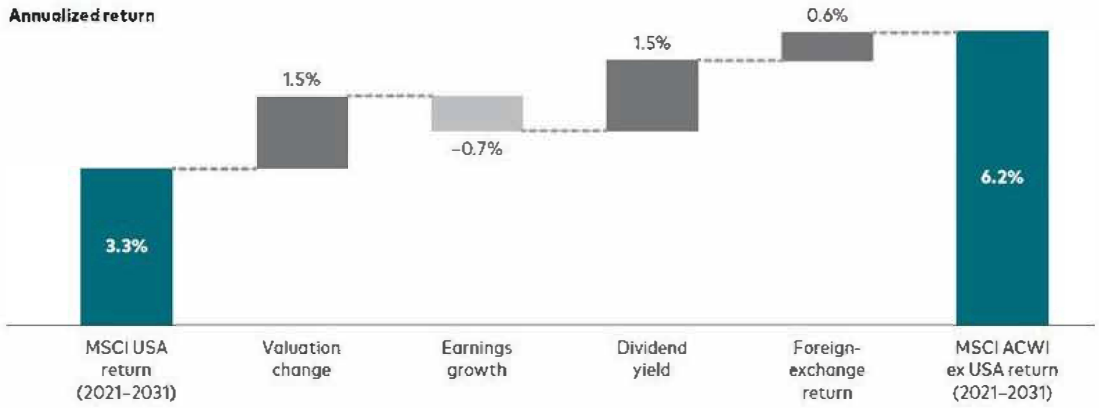
A specific note on international stocks, which have been more volatile than domestic. My belief is steadfast that over the next decade, non-U.S. equity markets will outperform large-cap U.S. equities. Substantial demographic trends, currency exchange, and elevated US equity valuations have widened the long-term appreciation expectations between large-cap domestic equities.




Vanguard Economic outlook: 2022, based on Robert Shiller's website, at aida.wss.yale.edu/~shiller/data.htm, the U.S. Bureau of Labor Statistics, the Federal Reserve Board, and Refinitiv, as of 9/30/21.

[3] Source: JP Morgan Asset Management, Bloomberg.

## Valuation contraction in the U.S. is expected to drive excess returns internationally over the next 10 years




| | Valuation change | Earnings growth | Dividend yield | Foreign-exchange return | Total return |
|---|---|---|---|---|---|
| **MSCI USA Index** | –3.2% | 5.0% | 1.5% | — | 3.3% |
| **MSCI ACWI ex USA Index** | –1.7% | 4.3% | 3.0% | 0.6% | 6.2% |

Vanguard economic and market outlook: 2022, based on Robert Shiller's website, at aida.wss.yale.edu/~shiller/data.htm, the U.S. Bureau of Labor Statistics, the Federal Reserve Board, and Refinitiv, as of 9/30/21.

***"Never put passion in front of principle. Even if you win, you lose."*** [7]

Vanguard economists provide a 10-year annualized estimate that the MSCI US index will produce a return of 3.3%, and MSCI ACWI ex US international index a return of 6.2%.

In the diversified investor's favor is also the fact that most Americans' portfolios are significantly underweight the asset class, which creates pent-up demand for earnings which can be purchased at fair value[6]. When recoveries occur, investors who owned the class from the beginning tend to be best positioned.

Lastly, international equities also offer investors a hedge against US inflation.

None of this info may assuage your market volatility discomfort; my aim is to provide insight into why we do what we do and the factors we weigh.

If you would like to speak in detail about any of this, I am here.

.[6] Source: JP Morgan "Is the case for international equities just about discounted valuations and currencies?" 1/2022.
[7] Morita, Pat, perf. "The Karate Kid", film, Columbia Pictures Tristar Pictures, 12/19/1984.

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