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What keeps you up at night?

After over twenty years of advising in the investment industry, I have observed a reoccurring theme which is the battle of human emotions between greed and fear. I call it a 'battle' as from a psychological point of view each human being has their own emotions they need to 'fight' against in order to function on a daily basis. Nowhere is this more apparent than in how people approach their money. There is an old Talmudic saying that the way to judge a person is how he behaves when he drinks alcohol, about what he gets angry, and how he spends his money. The human emotion with money is very powerful and has always been so, fluctuating between greed, in always wanting more (as if having more were the secret to life fulfillment), and fear about losing one's money. Behavioural finance studies reveal that these emotions drive our approach to investing and are the emotions we need to 'conquer' if we are to succeed in meeting our financial goals. In an investment newsletter to which I subscribe, author Jared Dillian recently suggested that "greed…is just another form of fear, it is fear of missing out [FOMO]…every single person trading is motivated by fear – every single kind of fear imaginable." Dillian concludes, "Instead of being dominated by fear, why not use it to your advantage." In my last newsletter for June 2018 I delved into the emotion of greed, so I thought it was only apropos in this month's edition to discuss the emotion of fear and how it relates to investing.

The one thing we can all agree about, regarding President Trump, is that he is really great for the media, as every form of it, whether in print, radio, television or on the internet, all spend a lot of time talking about him, his family, his views, his tweets, and I am sure the extreme polarizing opinions are likely driving a lot of profits for media companies. We can also agree that he has no problem taking a stand no matter how unpopular it may be. Unfortunately, even for those who tend to be small "c" conservatives, not all of the Trump administration's policies fall into the conservative mindset. Pro-fiscal conservatives mostly appear to be in favour of the administration's corporate tax cuts and reductions in regulations, which create unnecessary expenses and slow down small businesses which ultimately drive economic growth. However, few outside of the tight Trump circle appear to be in favour of trade barriers he has threatened, in the way of tariffs and additional taxes, whether they be fiscal conservatives or liberals. Historically, trade barriers have slowed the flow of trade, increased inflation by passing on higher costs to the end consumer, and propped up financially unsound industries which should have been allowed to close and allow other more financially sound operators to provide the service or product at a lower cost to end consumers and more efficiently. The increasing threats of a global trade war is one that should have everyone afraid, as there is no such thing as a zero sum game with trade – everyone loses out if a real trade war breaks-out.

Despite the success of famous investors such as Warren Buffett and Peter Lynch, many lay-people continue to view the stock markets as a form of gambling and something to be avoided by all but high risk-takers. Granted, the vagaries of the day-to-day movement in the markets are undoubtedly bizarre at times and there are definitely periods which make no sense at all. I recall both the euphoria and the terror created by the high-tech "bubble market" of 1999-2001 as an example of these extremes in emotions. Initially, the high-tech market became the source of "easy money", and companies with no profitability and no hopes for becoming profitable ran up in value as "investors" chased a dream. Eventually "when the chickens came home to roost", those companies with no profitability - the so-called "dot-coms", did what historically eventually happens to all companies not making money – they went out of business. Companies whose stock were valued as if their earnings were growing at over 100 times a year or more – an impossible task for any but the most micro-sized businesses, or who showed no net profits at all, collapsed, together with the investors' money who had bought those stocks. Back in the early '70s, there was a small number of stocks called the "Nifty-fifty" which pundits at the time wrote about as the "sure fire" way to make money – fifty great, profitable companies such as IBM, on whose coattails an investor could ride all the way to a successful retirement. Unfortunately, even great companies can get really overvalued, like any other investment class (think real estate!!!), and when the high valuations collapsed so too did the investment gains for those that held on too long. Today – investors need to be very wary as high valuations (like *Amazon* which currently trades at over 200 times earnings), no profitability (like *Tesla* which posts negative earnings), and a small number of stocks (like the "FANG" stocks) are driving the majority of market returns. *Caveat emptor* is as applicable today as it was in 1973 and in 2000.

Bottom line

The world of investing like any other area of human psychology can often be boiled down to the raw emotions of fear and greed. There are always reasons not to invest, crazy politicians, wars, geological disasters, terrorism, high inflation, and low inflation, and yet few places are better for investors to make money over the long-term than in these same capital markets. Jeremy Siegel, Wharton School professor and famed author of "Stocks for the Long Run", posits that "The focus of every long-term investor should be the growth of purchasing power…monetary wealth adjusted for the effect of inflation." The ultimate mantra to ward off whatever fear dominates an investors' thoughts is Professor Siegel's conclusion that "The growth of purchasing power in equities [stocks] not only dominates all other assets but also shows remarkable long-term stability." Enough said, sleep well.

Global benchmarks

As at June 30, 2018 (Canadian $ Returns)

Asset class	1 year	3 years	5 years
S&P/TSX Composite T/R (Canada)	10.4%	7.0%	9.2%
S&P 500 TR - US$	14.4%	11.9%	13.4%
NASDAQ Composite - US$	22.3%	14.6%	17.2%
MSCI Europe Index Price Return	3.7%	3.0%	8.0%
MSCI Emerging Markets	7.2%	5.0%	7.3%
China S.E Shanghai A Price Return	-7.5%	-13.1%	10.7%
MSCI World Index Price Return	10.4%	8.2%	12.7%

Asset class	1 year	3 years	5 years
30-year U.S. T-Bond - US$	-0.3%	3.6%	4.8%
10-year U.S. T-Bond - US$	-2.4%	0.7%	1.6%
Long GOC Bond (2048)	1.0%	2.5%	5.1%
10-year GOC Bond	-1.7%	0.7%	3.1%
5-year GOC Bond	-0.8%	0.0%	1.8%
3-month CDN T-bill	0.9%	0.6%	0.7%
US$/CDN$ (1.3130)	1.3%	1.7%	4.5%

Source: RBC Capital Markets Quantitative Research

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Wealth Management
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