# The Krygier Report: SPECIAL EDITION

An exclusive newsletter from Mark J. Krygier, Vice President & Portfolio Manager | March 2020 www.krygierwealthmanagement.ca


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# Pandemic of Panic

**For the second month in a row**, I am writing a "Special Edition" mid-month newsletter, due to the continued extreme volatility in the markets. In doing so, what I do NOT want to do is to simply rehash the financial industry's mantra of "hold for the long-term." Nor do I wish to try and dissuade anyone who ought not to be invested from pulling themselves out of their investments, if that is their "comfort zone", albeit at what appears to be "fire-sale" prices. What I do want to do, in writing this special edition commentary, is to add a bit of perspective based on my experience.

**I started my career as an investment advisor** in late 1996 with RBC Dominion Securities, having left the practice of law after my articling year with a Bay Street law firm. In doing so, I joined the securities industry at the tail-end of the technology boom. That boom was accented by several crises, which, being in my "formative" years, made a tremendous impact on my investing philosophy that has lasted until today. The first few crises I recall from that time period were the Asian Currency Crisis, followed by the Russian currency crises. The latter was even more impactful, as it was the proverbial straw that broke the camel's back of what was then the world's largest hedge-fund, "Long Term Capital" ("LTC"). The people who owned and operated LTC were literally "THE" gurus in the investment industry - the people who wrote the books behind Modern Portfolio Theory and essentially the rules of the game. Their genius approach to investing saw LTC perform almost miraculous-like returns, if I recall 30%+ returns for well over 5 years, perhaps as many as 10 years. Unfortunately, one big bet against the Russian Currency, with the odds of losing being lower than getting struck by lightning or winning a lottery, didn't work out, with the result that LTC collapsed 60% in a matter of months and was shut down completely a short-while later. The LTC collapse was so impactful, that if not for the "behind the scenes" intervention from the government, pushing the big banks to provide liquidity to the markets, the financial sector was in danger of collapsing.

**The next major event was the tech boom** itself, of which I have written about many times. Essentially, the philosophy of "all things new are better" was manifested in the stock markets, as investors jumped on the bandwagon of high-tech – companies that would provide us all with a "better tomorrow." The problem for investors, is that while many technological innovations would indeed help improve the quality of life for many, in particular improved means of communication, it also took advantage of greed. The possibility of quick riches, an age-old problem, pushed valuations of companies well beyond the revenues they could ever dream of earning. I will never forget walking out of a research meeting in which the "top-ranked" investment analyst for the telecommunication sector in Canada spent an hour extolling the virtues of Nortel, the Canadian darling that in his opinion would line the pockets of all those who invested in it. Indeed, in 1999 the company's stock price was up well over 100%, quite a feat for a "large-cap" stock. As I left that meeting, I overheard a senior Portfolio Manager muttering to no one in particular, "that young fellow has never seen a bear market." This was an investor who

held stocks for himself and for his clients in companies that made “real” things – goods and services which people relied upon for their daily living or business needs, whether in strong or weak economies. The success of the high-tech market had brought with it what I would in hindsight call “panic buying.” Clients who were professionals or business people and very bright and successful people, but not necessarily experienced in the world of investing, were getting swayed by media headlines and from the “water cooler” chatting of those around them – relatives, neighbours, friends, even the local barber, about the next, greatest “sure thing” to buy. I distinctly remember a client calling me in January 2000, shortly before what would be the peak of that technology boom. He was almost desperate to buy some stock in the latest technology “IPO” which a relative had recommended to him that he buy. We couldn’t even get our hands on the IPO because it was so “hot”, which was a saving grace, as a year-later the company was almost out of business together with the downturn of the whole technology sector. It would take 16 years for tech markets to recover back to the unrealistic heights achieved in that time period – giving a new definition to the term “holding for the long-term.”

**Fast forward to the spring of 2008**, oil was nearing its all-time peak price of just over $140/bb, when a well-known bank economist projected that oil would climb to as high as $200/bb by year-end. Again came the calls from investors to add money to the stocks of oil companies, with the lure of quick riches within reach. What followed was the quickest drop of which I am aware, in the price of any major commodity, as oil prices plummeted by almost 2/3 in a matter of months. Panic buying once again led to panic selling.

**In addition, I would be remiss** not to mention the true human tragedy, the “JFK” moment of our generation, when the twin towers in downtown Manhattan were attacked on “9/11”, or the financial catastrophe of the 2008-09 subprime mortgage market which impacted a much broader base of investors than did the tech–boom collapse of the early 2000s. I also recall disease-driven panic impacting the markets, as my own brother was working as a respiratory therapist in a Toronto hospital during the “SARS” crisis, with a picture of him working in a “space suit” being published in a local paper. Having experienced each of these events personally, side-by-side with those that entrust us with their hard-earned capital, my team and I manage our investments according to several principles.

**My observations**, which have helped me formulate those investing principles, are as follows:

1. The human psyche will vacillate between periods of greed and fear. It has always been so and it will continue to be so in the future. The promise of “market-neutral” or “low-volatility” is a textbook example of a vacuum outside of real-life. In a panic (of buying or selling) most investments, and markets as a whole, will move in the short-term according to the latest “wave”.
2. Growing capital “over time” has been a mathematical reality of the stock markets, and in every mathematical “average” there are by necessity numbers which are above and below the “mean average.”
3. There is no such thing as a “get rich quick” scheme that is both legal and enduring.
4. Commodity prices like oil, copper, etc. go through cycles based on supply and demand.
5. There is an idiom that there is no such thing as a “sure-thing” other than death and taxes. As one cannot avoid either, we need to be sure that the extent to which we spend our time and energy trying to avoid one or the either is not surpassing the time and energy we spend enjoying what we have.
6. Lotteries are bad. Governments make a lot of money from them or they wouldn’t be legal or popular. The chance of winning a lottery is extremely low. People who treat investments like lotteries don’t really expect to “win”. They hope they will, but in their inner gut they don’t really believe they will be successful. When they “lose” it confirms their underlying belief that investing in stocks is gambling. When they “win” it is merely a “lucky roll of the dice”.
7. Clients who frequently look the fluctuating value of their investments are more likely to experience temporary euphoria or hysteria than those who look at the values much less frequently. See point #13 below.
8. There really is a difference between “good quality” and “poor quality” investments. However, during short-periods of time, the latter may in fact outperform the former.
9. Valuation really matters. Even the best quality of investments can become “over-valued” or “under-valued.” The trick is not to let the success <u>or</u> the failure in the short-term lead to poor decisions for buying or selling.
10. In “bad times” one needs to distinguish between “good quality” and “poor quality”. When a garden is full of weeds, one doesn’t rip out what remains of the living plants. Instead, one should remove as many weeds as possible, prune the healthy plants, add some fertilizer to promote healthy growth, and then have patience for nature to take its course.
11. In “good times” one also needs to distinguish between “good quality” and “poor quality”. Many a “weed tree” has flourished and provided foliage in a back yard but which, when ripped out, reveal that the “good quality” cedars have been suffocated and have died.

12. The media is very, very good at promoting one thing in particular and that is panic – either greed-driven or fear-driven. Behavioural finance studies have looked into the phenomenon of media headlines marking the "peaks" and "troughs" of investment cycles. Unfortunately for investors, the media-marked "peak" of greed is typically promoted as the next "sure thing", while the "peak" of fear is typically promoted as "Armageddon" and the destruction of all things good. Neither are true.
13. Finally, I have observed that rarely are good decisions made out of panic – neither decisions to buy nor decisions to sell.

**KRYGIER WEALTH MANAGEMENT INVESTMENT PRINCIPLES**, by which we manage our own and our clients' investments (as the method for managing them as well as the actual contents for each are identical), are as follows:

A. Only invest money that is intended to be held long-term.
B. Only buy good quality investments. That means good quality debt and equity in good quality companies that are profitable, have reasonable debt levels and whose profits are rising and not dependent on outside factors such as commodity prices which are beyond control of management.
C. Seek out many different sources of information to confirm the quality of one's investment decisions.
D. Diversify amongst one's investments to avoid concentration and ensure exposure to any one particular stock, bond, sector or geography is limited, as decisions made on even the "best" information is rarely perfect.
E. Buy investments which are rising in value – both the intrinsic value and share price as indicative of the former. Conversely, avoid buying investments which are dropping in value – sometimes there is a good reason why prices are dropping.
F. As valuation really matters, trim capital gains when securities are "over-bought" (i.e. "over-valued"), even if the underlying business is stable and growing.
G. In a "normal" market, have parameters for selling losing positions before they become big losers. I like to use "moving average" prices to judge the "range" which defines "normal" for a given investment, as "nothing goes up in a straight line".
H. Avoid acting rashly in the midst of either extreme greed or fear. My biggest regrets over my investment career were not from my decisions to buy, but rather were from my decisions to sell good quality investments at the worst possible time.
I. Recognize that media hype is hyperbole which is almost entirely useless as a guide to investing.
J. Remember that the same human ingenuity which has provided and continues to provide us with an increasingly higher standard of living, with incredible advances in medicine and technology that was unimaginable only a few short decades ago, is the same human ingenuity into which we are invested, which has provided our generation with an increased level of wealth unimaginable only a few short decades ago.

**Bottomline** – we have seen volatility in the markets before, even extreme volatility such as we are now experiencing, and we continue to adhere to these same principles of investing.

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