Market Insights

THE DAYS ARE LONG BUT THE YEARS ARE SHORT

When you first have kids, other battle-hardened parents are always willing to pass on sage advice. One tidbit that was oft-repeated to me in the early days of being responsible for another human life was that “the days are long, but the years are short”.

When you are in the throes of a midnight meltdown with your irrational newborn baby, the minutes drag on for hours until the sun eventually comes up and another sleepless day begins anew. These days and nights blend together into a seemingly never-ending blur. Even though you are often told to “cherish these days, they’ll be gone before you know it”, the thought of just bypassing having to endure this period of your child’s life does not exactly seem unappealing.

The days do ultimately pass, though. Those all-consuming stresses and the wakefulness of that phase of life end up representing just a small brick in the foundation of building a functional person. You do not have the joyful soon to be 7-year old bouncing around your living room without having made it through those nights — and in hindsight, those nights have become just a minor blip of a memory.

In much the same way, and as we have seen play out in the last couple of weeks — and today in particular — financial markets can be prone to throwing tantrums. And while it may be the case in recent history that investors have largely been able to enjoy the gains from market exposure hassle-free, no reward comes without an attendant degree of risk that must be endured.

Now, obviously not all tantrums are without merit. Sometimes a baby is fussy and unsettled because it is feeling ill. The current bout of panic in the market is driven by a significant amount of uncertainty surrounding the global economic outlook, first due to the unknown magnitude of the impact of Covid-19 and its spread, and now the nascent price war in crude oil markets compounding issues.

The question is how much of the sharp selloff in risk assets is actually warranted. Indeed, it is undeniable that the outlook is not as bright now as it was even two weeks ago, but as of yet there is no fundamental indication that we are veering uncontrollably into a substantial recession that would cause global stock markets to further crater by half.

For starters, while undeniably backward looking to those halcyon days before “coronavirus” was in the public’s vernacular, the dataflow indicated that economic conditions globally were improving. In particular, there were signs that the underlying fundamentals of North American economies, especially the more globally-important US, were actually in pretty good shape.

This positive momentum is obviously likely to slow as the broadening spread of Covid-19 stifles economic activity — just look at the number of concerts and festivals that have already been shelved over the last week with more likely to follow suit in the coming days and weeks. But the fact that this shock hit the economy at a position of strength would suggest that there is a solid foundation for business to rapidly return to normal, with extremely easy credit conditions resulting from aggressive rate cuts from central banks (with more expected in the coming weeks) likely to help accelerate that process.

Further to this point, there is good reason to believe that can be expected to play out, and fairly rapidly so. China, the epicenter of the coronavirus outbreak has seen the number of confirmed cases of Covid-19 stabilize (and number of existing cases decline as more people recover) and activity in the country is starting to normalize — though, it remains far from normal. Against this, Chinese stock markets actually rallied more than 5% last week and returned to positive territory for the year (though, that is back in negative territory after today’s volatile session).

In other words, this too shall pass, just as it has in all previous instances of viral contagion — and there are very few instances ever where “this time is different” ends up being true.

March 9, 2020

Of course, we are not through this yet. We are in the thick of a tantrum, with each trading session seemingly dragging on endlessly amid flashing red on the screens akin to a screaming newborns face.

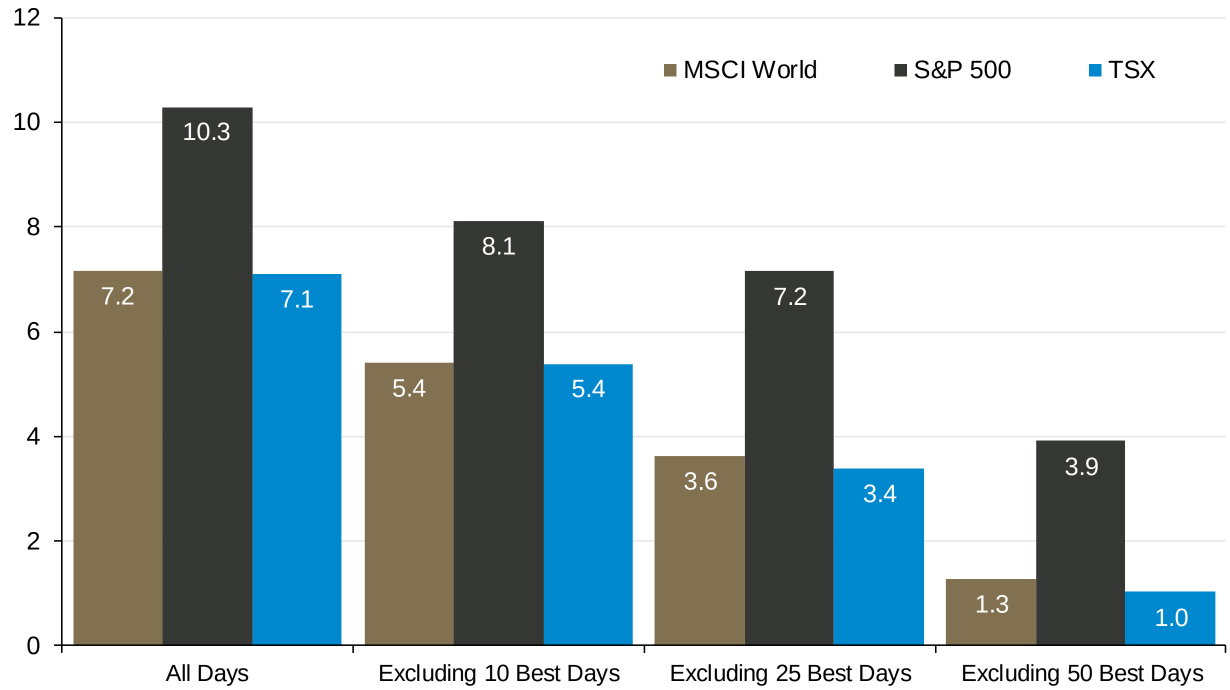
But while such an environment can prompt investors to want to pull their money out of the market and stuff it in it their mattress for safe-keeping until the dust settles, history has shown time and time again that allowing emotion to drive the investment decision making process is bad for investors' wealth, as short-sighted and undisciplined reactions to short-term events can carry significant negative implications for long-term portfolio performance.

It is never apparent when the dust has settled. For example, there was no discernable reason why exactly 11 years ago today marked the low point for global stock markets in the aftermath of the financial crisis. Being in cash in the days leading up to that secular market bottom may well have felt like a great move, but it also meant that these investors found themselves on the outside looking in as markets recovered — and being even a day late with respect to rejoining the party can have significant negative performance implications in the long-run.

As the chart below shows, missing out on just the 10 best days over the 8,400 trading days spanning the last three decades reduces annualized returns by roughly 2 percentage points. In other words, $100,000 invested 30 years ago would be worth 40% less now strictly if those top 10 days were missed.

Time In, Not Timing, the Market is the Key to Building Wealth

(annualized total return in US dollar terms)



Based on daily data from January 4, 1988 to February 28, 2020
Source: Bloomberg, Guardian Capital

Seasoned advisors will tell you it is always better to remain unemotional with respect to managing finances, instead taking a disciplined and long-term approach to asset mix decisions with strategic portfolio allocations serving as a tether to rein in impulses. Advisors will speak with investors to stay the course, and stay within their long-term risk profile laid out in their Investment Policy Statement. No need to deviate from your baselines, created during more sane times I may add, and sell risk assets (which are now looking comparatively inexpensive relative to a month ago, with valuation metrics like price-to-earnings ratios now consistent with historical averages) to dive full board into cash or safe havens (for which market yields sit at all-time lows, setting investors up for a prolonged period of meagre returns going forward) in an effort to protect their investments.

With the benefit of hindsight, those days without market exposure will become more and more noticeable as the years pass and that time cannot be made up.

The days are long, but the years are short.

March 9, 2020