Market Update

September 2020

Important Topic: Common investing mistakes or We are only human after all

As human being we are wired to survive. Many of our physiological responses help us navigate a dangerous and complicated world. The field of Behavioral Sciences studies how our instinctive reactions help us in most areas but can lead to disaster when investing. In short, we need to set aside our emotional and instinctual responses when investing. Here of some of the common mistakes:

Anchoring or Confirmation Bias:

We like to have our opinions confirmed by others, especially so-called experts. Because of this, we will search and find information, data and analysis that confirms our opinion.

If you talk to someone about almost any topic, they will present a lot of evidence to support their view, but ignore any evidence to the contrary. The fact that there are very smart people who hold the exact opposite opinion should be reason for humility not confidence.

Gambler's Fallacy:

There is a tendency among people to think that when a coin has been tossed five times and it lands on heads five times it is much more likely to land on tails the next time. This is totally incorrect. The odds of it being tails are exactly what they were the first five times: 50-50. Each flip occurs separately and independently of the others. And just because the market has been up or down the past several days or weeks, doesn't necessarily mean it has to do anything one way or the other.

Hindsight Theory:

When we look back over history, we tell ourselves that we knew something was going to happen before it did. The internet bubble that burst in 2000 is a powerful example. People now claim that they saw it coming. They just knew that the market had reached unsustainable heights, and that the bubble would burst, but just did not act. We quickly forget how we also felt excited and optimistic that the markets were going higher still.

Rearview-mirror Effect:

We tend to be most influenced by what has happened recently instead of what is happening right now. As the market goes higher, individuals (and institutions – run by humans after all) tend to become more and more bullish; and when the market has sold off for an extended period, they become more and more reluctant to buy. Yet success in investing is tied to ignoring recent event and finding opportunities for the long term.

Self-attribution Bias:

We have a tendency to congratulate ourselves for our own brilliance when we succeed but blame others for our failures. When a stock we picked goes up, it is because we are clever and made the right choice. When a stock we picked goes down, it's the economy, the Federal Reserve, the wrong advice or those hedge funds that made things go wrong.

Disposition Effect Bias:

One of the worst tendencies of investors is to sell winners far too soon and hold on to losing investments. But if you take 10% profits on your winners but continually take huge losses on your losers, holding onto the belief that it will come back, your overall results will look pretty bleak. Sell when it is time to sell based on a current assessment and completely disregard your initial cost.

Familiarity Bias:

This happens when an investor focuses on familiar or well-known investments even though more gains can be made through diversification. It is important to cast a wide net.

Trend-chasing Bias:

Past performance does not indicate future success. So, just because a company did well in the past does not mean that that trend will continue.

Unfortunately our brains are too heavily influenced by our emotions and instincts, making it a questionable investment tool. Instead one must train it to feed on data, logic, and fundamentals.

The solution: A Financial Plan

An established plan, including a rebalancing program that dictates buying and selling, removes emotion from the process. The plan's process buys when markets are underperforming (inexpensive/low) and sells when markets are overperforming (expensive/high).

Market Update: September 2020 - The Rally Takes a breather ..

The market has taken its first breather since the rally began in March. While some high flying stocks declined a noticeable amount (Tesla fell 15%), most companies have moved little.

Interestingly, over the last few weeks we have seen lesser known names start to recover. Until this time the market rally has been led by a few well-known names who, in most cases, benefited from the Covid-19. A broader recovery is an excellent and important step and supports the V shaped recovery that is so far underway.

Additionally, the underpinnings of the rally remain – government stimulus, low interest rates and better economic data than expected. As such we expect that the rally to resume.

However, not without some hiccups and volatility!

Specifically, while the Canadian government has extended its benefits, the US government has not. Some form of package is still expected but the delay has added to the volatility.

Further the US election is triggering a lot of fear. The amount of intellectual capital being spent imagining many of the possible complications is as endless as it is meaningless to our portfolios. Please understand, no matter who gets elected and no matter his policies, superior companies should continue to thrive. Our managers buy such superior companies. My expectation is that in six months the election will be a memory and the market will have moved on, focusing on the expected profitability of 2021 and beyond. It is important to take any political convictions (any emotional issue) completely out of your investment decision making.

Looking Forward

The markets are likely to remain quite volatile. The near future remains quite unclear and the election will be viewed, temporarily, as important.

As for our investments, we like the positions we hold – quite a bit – and we are continuing to buy, though very selectively.

As always we remain convinced that superior companies and investments trading at attractive valuations are sound and provide attractive long-term returns. We remain focused, selective and patient.

For the quarter, the bond market was up 0.4%, the Canadian market was up 4.2%, the US market was up 8.6%, International markets were up 5.1%, the Emerging markets were up 8.5%, the Real Estate market was up 2.2% and the preferred market was up 10.3%. (Reuters 9/30/20)[1]

Year-to-date, the bond market was up 7.7%, the Canadian market was down 2.4%, the US market was up 3.8%, International markets were down 7.2%, the Emerging markets were up 3.8%, the Real Estate market was down 20.4% and the preferred market was down 2.2%. (Reuters 9/30/20)[1]

Have a great month and let us know if there is anything we can do for you,

- Meir

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(1) Indexes shown

- Bonds FTSE Canada Universe Bond Index
- Canadian Equity - S&P/TSX 60 Index
- US Equity – S&P 500
- International – MSCI EAFE Index.
- Emerging Markets – MSCI Emerging Markets Index
- Real Estate – Dow Jones® Global Real Estate Index
- S&P/TSX Preferred Share Index

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