What Should We Expect in 2020? - Transcript

Tom Mullooly: Welcome back to the podcast. This is episode number 289. I'm your host, Tom Mullooly, and I'm flying solo today. I wanted to have this opportunity to speak with our listeners about what's going on in the market. I'm recording this on January 2, 2020, so welcome to the new decade and welcome to the new year, and this is a time of year where if you listened to our podcast last week, or Tim's podcast recently about what to expect at year end and as we head into a new year there's a lot of people out there making predictions. We don't like to make predictions, but I think there are a few things that we should talk about. What I'm going to mention in the next few minutes are things that I've already talked about with a few of you, a few clients who listen to the podcast, and others as well, about things that you should really keep in mind.

I'll start off with a question. How many 30% years do we have in the stock market? I can tell you that in my career, which goes back to the early 1980s, I can't think of too many years where the market posted these kind of gains, and it did it very quietly without a lot of fanfare. I also want to remind people, and we've done this over the last few weeks, let's remember where we were one year ago. The first week of January, 2019, we had just seen the market go down 20% in one quarter of a year. We saw the market hit a high, hit highs at the end of September. Those events happened in one of the last days of the third quarter for 2018, and then the fourth quarter of 2019 started with a Fed meeting where the Fed was raising rates. Market went down pretty steadily through October, November, continued to go down, but not so much.

And then in December, we had a comment from the Fed Chairman Powell who said, "We're nowhere near neutral, and we can be raising rates for many times or several times into the New Year." And that just sent stocks reeling. And so we got to Christmas Eve of December '18. This is a year ago. The Dow and the S&P were down close to 20%. Not quite 20%, but pretty close to down 20%. The mid cap indices, small cap indices, all the other yardsticks were also down considerably, and we hit bottom on Christmas Eve 2018, and we started moving up from there. So even now, if you go back exactly a year to January 2, last year, it was really hard to tell if we were out of the woods, and the market has pretty much marched straight back up.

The problem is, if you just look at a year like 2019 in a vacuum and say, "Hey, the market did 30%. That's awesome." You have to kind of look back and see, "Well, we lost 20% in the fourth quarter, just three months before that." And another analogy or another interesting piece of information that I'd like to share with people, the Dow Jones hit 27,000 in January of 2018. Think about that. 2018, January. It hit 27,000 again in September of 2018. It hit 27,000 again in May of 2019, and we didn't break through 27,000 for good until August of 2019. That's just four months ago. We had a year like 2018 where the market gave us a little to work with, not much. 2019, market was up considerably. You know, if you draw a straight line going back through January of 2018, the market really hasn't moved all that much. We've just kind of been treading in place. These last few months have really kind of put us on the positive side, so it really depends on where you draw the lines. And I wrote a post about this that we can link to in the show notes on my blog, thehumanadvisor.com.

How many 30% years have we had in my career? Just a handful. Some of them have come pretty recently, though. 2017 was not a 30% year, but it was a good year. 2013 was about as close as we could get. The market was up about 28% or 29% in 2013. So what happened in 2014? The market actually had about a 10% or 12% gain through October. People like to talk about the drop in October of 2014 as the Ebola scare. Do you remember that? Do you remember where you were when people started talking about the Ebola virus, and how they were going to close down all the airports, stop people from coming into the country with the Ebola virus? What people fail to mention is that is also the same time that the Federal Reserve finally ended their quantitative easing program. I don't know how people miss that. I guess it's catchier or a little more relatable to talk about the Ebola scare and the market going down 10% in two weeks.

We gave up most of our gains in a very short period of time, and that's really what I want to focus on, is that it's very easy for the market to go up a flight of stairs but go down in the elevator. Markets go down a lot faster than they come back up. You can see what happened in the fourth quarter of 2018. I'm sorry to keep harping on this, but fourth quarter of 2018 turned a positive year, slightly positive year into a slightly positive loss. We had the market up about 10% or 12%, but by the time the year was over, we were down about 5% for the Dow and the S&P 500. Markets can go down a lot faster than people expect.

The next question is, if we don't see 30% years, how many times do we see back to back 30% years? Well, I think you'd have to go back to the Great Depression in the 1930s to find two years where the market put together back to back solid years like that, but everybody was pretty much out of stocks at that point. It was a completely different environment in the 1930s, but I guess one of the main messages to take away this morning is, don't expect another 30% year in 2020. Again, hard to predict, but the odds are against another 30% year coming.

Part of the problem now is that we're getting some calls from folks who say, "Gee, I feel like I've kind of been sitting on the sidelines, or I've had too much money out of the market. Do you think we should get more aggressive?" Market's just gone up 30%. do you think you should be getting more aggressive? Really? It's a question that you could probably answer yourself. The thing that we try and stress to all of our clients is we don't want you to change your investment allocation because the market is up or because you expect the market to be up, or because you expect the market to be down over the next three, six, 12 months. That's not why you change your investment allocation.

If you're an aggressive investor, you have to learn to live with really good markets and really lousy markets. That's the long and short of it. If you're going to be aggressive, you're going to be 90% or 100% in stocks. You better strap yourself on. It's going to be a very good ride, but it's going to be fraught with danger. There's going to be periods of time where your account is not going to be looking very pretty. That's the territory that you're playing in when you sign up to be an aggressive investor. If you're a moderate or conservative investor, we're going to have less money allocated in stocks.

One of the other things that we try to tell clients is, "Look, if you've got money that you're going to need in the next year or two or three, not a good idea to have that in stock market." It's just not. There's plenty of stories online that you'll find where people say, "I want to maximize my savings, and so I'm putting my savings account into electric utility stocks because they pay a dividend." Or, "I'm putting them into some kind of blue chip stocks because they pay a dividend and the bank doesn't pay me anything." The money that's at the bank should be there for a reason, because you need it in the next three, six, nine months or the next year or two. If you need the money in a year or two, you may want to think about a short term bond fund or some other alternative. We often mention high yield savings accounts. You don't need us for something like that. You can find them online and they're FDIC insured. It's worth taking a look, and feel free to call us if you've got questions about that.

Money that's needed in the next one, two, sometimes even three years, you want to think about having that not exposed to the stock market. In addition to that, as I mentioned earlier, if you are a conservative or a moderate investor, it's a good idea to not be ... You're not going to fit the description if you say you're conservative, and yet you have 90% of your money in stocks. That just doesn't line up. And so we want to take a more cautious approach. We want to look at things that are not in the market, and so we'll have discussions about bonds and about different investment opportunities that are out there.

The main takeaway from this section is, please don't consider changing your investment allocation because the market's up or you think the market's going to go higher or the market's going to go lower. You should change your investment allocation when it's time to change, when your situation is changing. Okay? "I'm going to be retiring at the point where I'm no longer working, and I'm going to think about drawing down some of these assets." Okay. Now at that point we need to have a serious discussion about what you've got in the bank and what you've got in savings, and what should properly allocate the rest of your investments for? If you're in your 30s, 40, say you have a civil service or a municipal job, say you're a police officer and you're retiring after 20 years at age 50, you may go on to take another job, but you're probably not going to be drawing down on your retirement accounts probably until you're 59 or beyond. If that's the case, you've got at least another 10 years where you can step on the gas and continue to grow the money.

It's going to have some risk. We're going to see some down periods. We keep saying we're going to have some down periods. We haven't had long down periods in the market, and that's something else I want to just mention. We talk about long down periods in the market. I think about after the 1987 stock market crash, the market got back to its pre-crash levels two years later. It was not until October of 1989 that we got back to where we were. To me, that sounds like an eternity. Two years where we had to wait for the market to get back to its previous levels. You look at where the Dow Jones was in the 1920s before the stock market crash in 1929, it took until 1954 for the market to get back to where it was in the late 1920s. So you're talking about a 25 year period of time.

Also, I believe the Dow Jones hit 1,000 in 1967 for the first time and didn't cross 1,000 again until 1982, so there's another 15 year period where stocks were down and it was very, very hard to make money in stocks. Those kinds of markets, those long-term bear markets, we have not had them in a while, and I think it's worth discussing the fact that after the 1987 stock market crash, the Fed chairman at the time was Alan Greenspan, and he made a statement the day after the crash. I remember seeing it coming across the news tape. Greenspan said that the Federal

Reserve stands ready to do whatever it takes to support the ... He didn't say support the New York Stock Exchange or support the markets, but to basically support the economy. And I'll have to find the exact quote for you.

But since that time, and we're talking over 30 years, there is this concept of what they call a Fed put. The idea with a put is basically, the analogy I use when I'm describing puts to people, if they've never invested in options before, is if you have a car, you have car insurance, when you go out to drive, if you have a car accident, the insurance will help put you back whole. So the idea of a put means to put us back where we were. So there's this talk, I don't believe it, and the Fed will never guarantee it, but there's a lot of people out there that when the market starts going down, they start talking about a Fed put, that the Federal Reserve will do something to backstop stock markets. And I can't say that that's a fact, but it sure is a funny coincidence that when the Fed chairman speaks or the Fed governors are out making speeches, and they talk about the economy and they talk about the stock market, that will often have a direct effect on at least the market direction for that day or that hour. Interesting thing to look at.

Another interesting thing, again, we don't take it as gospel, but we're going into the 2020, which is an election year, presidential election year, and there is an election cycle. This has been going around for almost 50 years, talking about how the third year of a presidential cycle, which is 2019, the year we just ended, how that's usually the best year of the four in the market cycle. The first full year of our presidential term is usually the worst. I'll have to look back over the last couple of election cycles to see how that fanned out. It's eerily prescient in a way that this sometimes does work out. Nobody expected a 30% return in the stock market for 2019. Nobody predicted that. Just kind of fluky how that happened, but it makes for interesting shop talk.

One thing that went missing in 2019 that we had plenty of in 2018 was volatility, and I would certainly expect that 2020 will be a year of normal volatility. What does that mean for you? A year of normal volatility means that we should expect the market to be down at some point in the year 10%. if you go back over the last 90 years, there's been something like 88 times where the market has dropped by 10% or more. We have to get used to the idea of volatility, because we've only had volatility in one direction for the past year, and it's been up. We haven't had much in the way of volatility in terms of moving down. Come to expect that we can get a 5% drop in the market at any time for any reason or for no reason at all.

If it sounds like I'm repeating myself, I am, because I've said this to clients many, many times over the years. You should expect a 10% drop in stock prices at least once a year, and we can get a 5% drop in stocks at any time, for any reason, or for no reason at all. So that would be the kind of typical volatility that you should come to expect every single year.

I heard this morning that it's very unusual to have a strong stock market heading into a recession. Said another way, you usually don't have a recession this close to a strong stock market. Stock market is usually considered a forward looking machine, and so stocks will tend to give you a view of what's to come in the next six months, sometimes 12 months. It's very hard to say exactly, but it's usually a forward looking kind of indicator, and so if stocks are strong now, it should tell you that the economy should be good, but we don't know, and nobody really knows for sure, but I thought that was a nice little tidbit that I wanted to share with folks on the podcast today, that it's very unusual to have a strong stock market and then see the economy turn over into a recession immediately.

These are things that we've been saying for the last couple of weeks to clients. I fully expect that those that don't listen to this podcast are probably going to call and ask the same questions, like, "What do you think is going to happen this year?" And, "Do you think we should be getting aggressive now?" The flip side of that is, "Do you think we should be getting conservative now?" We'll circle back to what I said a few minutes ago. Don't change your asset allocation because the market's up or because the market's down. Please don't do that. You should change your asset allocation when the time is right for you to change your allocation.

If you're in your 40s and you're aggressive, just know that there's going to be good years and bad years. That comes with the territory. We can't guarantee against losses. Nobody can. Don't change your investment allocation because you feel the market's going to make its next move up or down. Please don't do that. You're going to whipsaw yourself out of money, and we don't want to see you do that, and certainly not on our watch. This has been the Mullooly Asset Management podcast. Thank you very much for tuning in to episode number 289, and come back and listen to episode 290 in the next few days. Happy New Year.