## A Generational Buying Opportunity - Transcript

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**Tim Mullooly:** Welcome back to the Mullooly Asset Management podcast. This is episode number 349. Thanks for tuning in. This is Tim Mullooly, and with me today here is Brendan Mullooly. Brendan, happy Friday.

**Brendan M:** Happy Friday. Beautiful day here in Wall Township, New Jersey. Spring has seemed to finally appear.

**Tim Mullooly:** Yeah, spring has sprung.

**Brendan M:** And we are less than a week away from Major League Baseball.

**Tim Mullooly:** Yes, that is fantastic news. A lot of Mets chatter going around in the office and fantasy baseball and all that good stuff. It's good to be back.

**Brendan M:** It's peak optimism for New York Mets fans right now.

**Tim Mullooly:** So this week there's been a lot of talk about the one-year anniversary of when the market bottomed. I think it was March 23rd of 2020. It was when the pandemic crash, Corona crash, people were calling it, stopped.

**Brendan M:** Which is wild, because it only began on February 19th.

**Tim Mullooly:** Right. It seemed like for the last couple of weeks, it felt like the last six weeks of 2021 went a lot faster than that six week stretch during 2020, for sure.

**Brendan M:** I mean, since then markets have done really well. And so just to share some numbers, since that bottom through this week, the S&P 500 is up more than 75%. small caps are up more than 120%. the Qs, so technology large cap stocks mostly, up more than 80%.

**Tim Mullooly:** Yeah. Which are-

**Brendan M:** In a 12-month period, that is nuts.

**Tim Mullooly:** Eye-popping numbers. Yeah. And Nick Maggiulli from Ritholtz Wealth Management had a post detailing all of those numbers as well, and he made the point that we may never see a better one-year rally in our lifetime.

**Brendan M:** He dug into the numbers and showed that there were only two other rolling 12-month periods with better returns in history, and they were in 1933 and 1934.

**Tim Mullooly:** Right. Coming out of the Great Depression.

**Brendan M:** He just said that we might've just seen the equivalent of an investing Haley's Comet.

**Tim Mullooly:** Right, exactly. People talk about buying opportunities. He said, "For a lot of people we could have just seen that could have been a generational buying opportunity." We see the market go down five, 10, 15, 20% every few years. We've outlined how often that happens in previous podcasts and other content, but to see a draw down like what we saw with that speed last year, it doesn't happen very often. And then the subsequent straight up recovery, it happens even less.

**Brendan M:** Right. And to be fair, I mean, it's maybe sometimes tough to remember, but I mean, a year ago, nobody in general was super bullish on things. I mean, it seemed pretty bad. We didn't really know what the economy was going to look like for the rest of the year or how long we were going to be fully shut down with the pandemic really beginning in earnest. And Nick Maggiulli, who again, shared these stats, shared a Twitter poll that he did around this time last year, and he said he asked people how long they thought it would take for the market to recover from the draw down that we were in, and only 11% of people who replied, and these are mostly financial professionals who we're all connected with on Twitter, said only 11% said less than a year. And the rest of the people were one, two years, two to three years, three to four years, and that made up the rest of the poll.

I guess his point and one that I think is worth noting, coming off of such strong returns over the prior 12 months now, is that nobody saw this coming.

**Tim Mullooly:** And Nick pointed out in that article that he wasn't in that 11% that expected it. And I think I remember taking that poll as well, and I said the same thing, outside of a year. You don't expect, as people who study the markets, you know over time we were bound to get back to the levels that we were pre draw down, but you don't anticipate it coming straight back the way that it did. I mean, it went up almost 80% without pause through the end of the year.

**Brendan M:** So I would just use all of this information to remember that it was far from guaranteed that the last 12 months played out like they did. The draw down happened. It was scary. Hopefully you were in a portfolio with an understanding of why and you were able to hang in there and maybe even rebalance at some point during the spring last year and take advantage of prices while they were down. I know that's something that we did for clients.

Now looking in hindsight, don't forget how difficult that period of time was, and don't grow to expect 75% 12-month returns, because as Nick highlighted and we shared here, they're very abnormal. So having the expectations now coming off a 12-month period where the S&P 500 was up 76%, not realistic.

**Tim Mullooly:** Right. Yeah. And I mean, no one knew what the market was going to do on March 24th. We didn't know at that time it was going to stop going down, but it did. And even along the way, like you're saying, there were plenty of people who didn't believe that that was the bottom. They said, "There's more to go. We're going to get another leg down." There are naysayers all the way back up. It's important to keep that in mind when you're looking back on things and setting your expectations from there.

**Brendan M:** Right.

**Tim Mullooly:** I think-

**Brendan M:** We've talked with clients, too, I think, of late in terms of … Not that we're in any sort of big draw down right now, but certain areas of the market, like we talked about on last week's podcast, like technology or small caps are probably around seven to 10% …

**Tim Mullooly:** Maybe 10.

**Brendan M:** … off of their highs while the S&P 500 and the Dow are maybe only down a percent or two.

**Tim Mullooly:** A couple.

**Brendan M:** So not that we're in any period of true turmoil or anything, but to see the market be kind of volatile and stall out here a little bit, when you put it into the context of the prior 12 months that we've had, it seems pretty reasonable that after a 75% move in 12 months, things might calm down a little bit, or for small caps, 120% in a year or so. For them to be in a 10% draw down right now off of their highs they made just last month, I'm not sure that's anything to get overly concerned about. Obviously you like to understand everything that's happening, but nothing that we see as a reason to make wholesale changes to investment plans, for sure.

**Tim Mullooly:** Yeah. Yeah, definitely. And another point that Nick made in the post, after a year where things went straight up from the bottom there, 80, some over 100%, it's easy to feel like an investing genius. He used the phrase, "How a rising tide lifts all boats." When the market in general as a collective whole is going essentially straight up, it's very easy to get an inflated sense of confidence when picking different investments. Or if you try, and if you jump into trading, like we saw a lot of towards the better half of last year and into this year, after the run-up that we saw in 2020, I think people just got a little … Their heads got a little big for their bridges.

**Brendan M:** Yeah. I think one of the hardest parts of investing is weighing the confidence that comes from runs like what we've seen in the last 12 months with the despondence that can come from what we saw just before that with the 20, 30% draw down. And taking those two things, recognizing that you're going to deal with both of them as an investor, and then creating a mix of investments that speaks to your temperament and what you're able to enter, meaning not getting overly excitable on the way up and not getting too upset on the way down. Both are inevitable parts of investing. It's just the matter of how you want to be positioned to deal with them.

**Tim Mullooly:** Yeah. And I think, like you said before, not to expect 75, 80% runs in the market in a 12-month period every single 12-month period from here on out. Like you said, we're experiencing some draw downs in some areas of the market.

I thought an interesting article to contrast what Nick was saying was something that I saw on CNBC about how the headline read that more than half retail investors think that the market is rigged against them. The survey came from Bankrate, and it said that 41% of non-investors feel that way. But also 56% of people that are investing think that the market is rigged against them. This survey came in February, right after the whole GameStop and meme stock explosion, and people felt that the hedge funds and Wall Street were manipulating stocks and all that. The numbers are probably a little inflated from what they typically are, but after a year where we saw some funds and some areas of the market, a lot of areas, return 80, 90, 100 plus percent, it's just funny to me to see that many people think that the market is rigged against them.

**Brendan M:** It's a matter of what game they're playing, because you're playing the game where you're day trading, you're playing against high-frequency traders, hedge funds, the titans of our world. You don't need to play that game to be successful is the point that you're making. You could have had a diversified portfolio over the last 12 months and done really, really well. And for that matter, you could have had a diversified portfolio over the last decade and done really, really well.

But if you choose, instead of being in a somewhat boring investment approach where you're not making a ton of adjustments, maybe rebalancing and making a couple changes over the course of a year, if instead you're making a couple of changes every single day, you're opting into the major leagues when you don't need to play at that sort of level. And quite frankly, yeah, the odds are stacked against you if that's what you're choosing to do, but no one's putting a gun to your head to make you do it.

**Tim Mullooly:** It's like if the market going up 75, 80% is rigged against people, I would love to see what a market working for them would do. You know what I mean?

**Brendan M:** Yeah.

**Tim Mullooly:** It's like, geez, that's still pretty good.

**Brendan M:** Yeah. Yeah, for sure.

**Tim Mullooly:** It's just like short-term memory, I guess, too. People forget, quickly forget, flip the switch from fear to greed back and forth a lot throughout, even throughout a 12-month period. You forget what happened last year, and you're only thinking about what's happened over the last couple of weeks. And again, I think we always run into instances where people are interchanging the terms investors and traders. And I think that that's a distinction that should have been made more in the article.

**Brendan M:** Yeah. People use them interchangeably. And along the same vein as trading and day trading and opting into games that are difficult, I think Michael Batnick shared a really good update to a study that JP Morgan has released in the past. It had some new numbers, and it was called The Agony And The Ecstasy, and it shared a lot of numbers about individual company risk. And so if you're playing that game of picking stocks or trading stocks individually, I think this is some good data. And I've seen this stuff in the past, and this is some of the information that has shaped why I approach investing the way that I do, meaning diversification, ETFs, and not necessarily loading up on single stocks because I think that data like this highlights-

**Tim Mullooly:** The risk is just too great, I think for a lot of people.

**Brendan M:** And I don't think that you need to be doing it to be successful. So just to share some of the information. This study by JP Morgan showed that, first of many stats here, since 1980, more than 450 names have been removed from the S&P 500 due to financial distress.

**Tim Mullooly:** That's a lot, if you think … I mean, the S&P 500 is supposed to be the largest 500 companies in the United States.

**Brendan M:** Right. So just to show that if this happened over 40 years, that means that basically all of the constituents of the S&P 500 index today over the next 40 years, if this is any guide to how things move forward, will be obsolete or gone or companies that we chuckle about that used to be something gigantic and now are-

**Tim Mullooly:** Remember Amazon? That kind of-

**Brendan M:** Right, and just are a shell of themselves. And it seems implausible. I'm sure it seemed implausible in 1982 when you listed off all of these companies, but there's going to be turnover in the index, and if you end up picking one of these companies that is one removed for financial distress, depending on how much you have in it, I mean, you could be taking on a ton of risk there. But since 1980, the index itself has done really well, despite the turnover in these names. And having exposure to names over time that didn't do so hot, they were dropped from the index over time. And I think that's one of the benefits you get by diversifying, and even just using market cap weight, like an S&P 500 index.

**Tim Mullooly:** Right. Yeah. I think there are years and there are instances where a single stock, like I mentioned, Amazon or big tech names over the last handful of years have just been knocking it out of the park. And people get antsy and they're like, "Well, why don't we just own all of this?" And like you said, it's implausible. People can't process the thought of these companies not being around in the future. But to that point, it's almost a certainty over a long enough stretch of time. I mean, these companies might exist in the future, but to say that-

**Brendan M:** … but it doesn't mean they're the top of their industry anymore, either. Just existing.

**Tim Mullooly:** Right. Or they could look completely different from what they are right now.

**Brendan M:** Yeah. So along that same vein, if you think that just piling into one stock that has worked really well of late makes sense, same study showed that 44% of all companies in the

Russell 3000 Index since 1980 have experienced what they defined as a catastrophic loss, which is a 70% or more decline with no full recovery.

**Tim Mullooly:** Wow.

**Brendan M:** Or no recovery at all, meaning the business is gone.

**Tim Mullooly:** If you're looking at the odds, then, of trying to pick one of those 3000 stocks, I mean, 44%, that's almost a coin flip.

**Brendan M:** Right.

**Tim Mullooly:** If you're just trying to pick one out of thin air, you almost have a 50/50 shot of picking a company that will experience something like that.

**Brendan M:** And this might speak to the period of time, too, that the study captures, but to break it down further by sector, 65% of energy companies had a catastrophic loss over that time period. 59% of tech, which has been, I think this is probably skewed because it captures the tech bubble …

**Tim Mullooly:** Tech bubble.

**Brendan M:** … in 2000. But even 14% of utilities had a catastrophic loss of greater than 70%. We hear from folks all the time who think that utilities are as safe as cash and bonds.

**Tim Mullooly:** Like a bond proxy.

**Brendan M:** Yeah. It's like that-

**Tim Mullooly:** That's not the case.

**Brendan M:** Probably, but not definitely, so you should approach it with that in mind.

**Tim Mullooly:** There's still tons of equity risk there.

**Brendan M:** There's definitely risk there. They're going to go down when the market goes down. It's not any easier, even if you delve into some of these sectors. I think the risk is very real. And so to have companies with this sort of risk and to have all or a large portion of your money in one company, I mean, sure, if it ends up being the ones that works out, then great for you. However, I think you're taking a lot more risk than you necessarily need to.

**Tim Mullooly:** That's the the main point for the everyday investor out there who's probably listening to it. It's like it's a need thing. Do you need to take all of this risk? It's need versus want. Some people enjoy all of the risk that comes along with owning individual stocks or they like the high flying octane business of stock picking, but for almost every other person out there, it's just not a necessity.

**Brendan M:** No. And I mean, to take this further in terms of what your alternatives might be, since 1980, looking at the Russell 3000, 42% of the stocks in the Russell 3000 over that period of time did worse than just having T-bills to cash. So, I mean, that's let alone … We talked about the decline, so you should anticipate more volatility when you own an individual stock than an index or even a sector fund or something. So moving out the spectrum in terms of the volatility, that 70% catastrophic decline, that's one thing. But since 1980, 42% of them were worse than just having your money in cash.

**Tim Mullooly:** I think it's eye-opening for a lot of people to potentially see those numbers when you're just drilling down to the individual stocks versus how these indexes overall have performed since 1980, because we're not saying that the Russell 3000, the index itself has been a bad investment since 1980. All of these indexes have posted pretty nice returns over the last handful of decades. So it's the difference between owning the individual parts versus the whole machine.

**Brendan M:** Yeah. And on that note, so over that time period, 66% of the stocks in the index underperformed the index. So you could have beaten two-thirds of these stocks by just owning the index and you would have had way less volatility, way less company specific risks to worry about, and stories to be tuned into along the whole way by just owning the index.

**Tim Mullooly:** And that also means that a third of those stocks were carrying the performance of the index over that time, but how are you supposed to identify what third of those stocks are going to be outperforming?

**Brendan M:** Yeah. I mean, there are a lot of people out there that will tell you that they can and they have very convincing narratives as to why they can, but the studies that S&P Dow Jones do show on a pretty consistent annual basis, and then rolling three, five, 10, 20-year periods to that most active mutual fund managers don't beat their benchmark. And so if those are supposed to be the experts that could guide you to this one-third of stocks that were better than the index, I'm not sure there's a great amount of evidence to support paying them a fee to search for that, really. And they even looked at here. So like 10% of the stocks in the Russell 3000 over that 40-year period were what they termed a mega winner, which was being more than 500% plus what the index did over that period of time.

Could you find one of those and ride the wave the entire time? Sure. I think I'd remind you, though, that most of the companies in the index, even the mega winners, experienced draw downs in the realm of 40, 50, 60, 70%. I mean, you can name all the darling stocks of today, and they've all had their periods of time where they got beaten to a pulp. And I'm not sure that even if you identify one that is one of these mega winners, that you're going to be able to hold it for the entirety of that period of time. It's easier said than done, and it looks like a layup in hindsight, and I'm just not sure that it is.

**Tim Mullooly:** Yeah, absolutely. I think main point here is that stock picking is really hard and it's not necessary in 99% of cases.

**Brendan M:** I looked, and in 1980, the Dow Jones Industrial Average was around seven, 800. And so-

**Tim Mullooly:** Total points. Right.

**Brendan M:** Yeah. So you could compare that to where we are today, and-

**Tim Mullooly:** 32,000?

**Brendan M:** Right. And just to your point, I don't think that's a game that most investors need to be playing in terms of picking the individual companies.

**Tim Mullooly:** Right. So if you just-

**Brendan M:** It may be more fun. It may be something that you enjoy doing, but I'm not sure anybody's financial plan or future wellbeing is predicated upon them nailing one of these mega winner stocks. Odds seem low, and if that's what you need to make your plan work, you should develop a better plan.

**Tim Mullooly:** Yeah.

**Brendan M:** Because that's not a very good one if you're banking on a low probability outcome like that.

**Tim Mullooly:** Right, exactly. If you need to hit that hail Mary, yeah.

**Brendan M:** It's a tough spot to be in.

**Tim Mullooly:** Absolutely.

**Brendan M:** Consider all other options available.

**Tim Mullooly:** This is the last podcast that we're doing before the baseball season starts. We did a podcast right before the football season started, and I asked you to predict what you thought the Jets were going to do, because for listeners, me and Brendan are both Mets and Jets fans. I think your Jets prediction was a little closer to what they actually did. I think you were in the four to six win range. I was wildly optimistic, and I said they were going to go 500 and go 8-8. Clearly that did not happen.

**Brendan M:** No.

**Tim Mullooly:** So let me pose the question to you. Before opening day, how many games do you think the Mets win this year?

**Brendan M:** I think they can do 90, and I think they'll compete for a playoff spot. I don't know that that'll be good enough to win the division because Atlanta looks really good, and quite frankly, I think the entire NL East is very good. So I think 90 wins does it, and I'm optimistic with Steve Cohen at the home now that this can be a new chapter for the Mets. But I stand prepared to eat those words, and as soon as May, I'll probably be grumbling about them.

**Tim Mullooly:** So I'm going to, like my Jets prediction, be a little more bold.

**Brendan M:** Yeah?

**Tim Mullooly:** Just a little bit. I think the Mets could win up to 95 games this year. I think they'll win the NL East. I think Edwin Diaz is going to lead the NL in saves.

**Brendan M:** Wow. Timestamp it. Let's go.

**Tim Mullooly:** Jacob DeGrom is going to win his third Cy Young.

**Brendan M:** I hope you're right.

**Tim Mullooly:** And that's it. That's the last bold prediction I'll make.

**Brendan M:** I hope you're Right, and I-

**Tim Mullooly:** Play off team.

**Brendan M:** And I hope that we can get to the ballpark at some point later this year.

**Tim Mullooly:** That would be great.

**Brendan M:** I would love to be back at Citi Field again in 2021.

**Tim Mullooly:** Same here. All right. That's going to wrap up episode 349 of the Mullooly Asset podcast. Thanks for tuning in, and we'll see you next week.