Recession: The Only Way Out is Through - Transcript

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Tom Mullooly: Welcome back to the podcast. This is episode number 347. 347. Thank you for tuning in. I am Tom Mullooly, and joining me today are Tim Mullooly and Brendan Mullooly. Hey, guys.

Tim Mullooly: Hello.

Brendan M: Hey.

Tim Mullooly: So it feels like every day for the last couple of weeks has been a one-year anniversary of some crazy news headline that's come out. Specifically today, we're recording this on March 11th, one year ago today on March 11th, 2020, the NBA canceled their games. I think it was the first time that they did that. Tom Hanks came out and said that he had tested positive for coronavirus, and the World Health Organization officially declared the coronavirus a global pandemic. I feel like when these things happened, that's when everyone realized that it was real.

Tom Mullooly: Yeah, it took on a lot more of a serious tone when we started seeing these headlines. And I don't know about you, but I thought that this was starting to slip out of control.

Brendan M: It seemed like it was just going to be something we hadn't dealt with before.

Tom Mullooly: Yeah. The clean version of the line is this stuff's getting real.

Tim Mullooly: Fast-forward to today, March 11th, 2021. One of the news headlines was how a JPEG file sold for $69 million yesterday. GameStop price action went from like 350 bucks to $190 in 40 minutes. So we went from deep despair in the market to just silly, silly stuff going on in the matter of 365 days.

Tom Mullooly: I know that even within that 365 day span, we had conversations with folks that ranged a year ago from extreme fear to extreme greed at the end of the fourth quarter last year. So, we've seen the full spectrum of emotions from investors, just in a very, very short period of time.

Brendan M: We had like a full market cycle in a calendar year. So kind of neat from that perspective, not that you want to experience, especially the negative parts that we were in the thick of about a year ago today. But to see the draw down the rebound, different parts of the market working at different points in time that normally had been a more drawn out process as part of a recovery after a draw down. The drawn down itself being six weeks was faster than basically anything we had seen before. We've taken a round trip and maybe then some, as Tim alluded to, with some of the speculative stuff that's been going on for the last several months.

Tim Mullooly: Yeah. And Ben Carlson at Ritholtz, I feel like he is constantly tweeting over the last year just that point, how remarkably fast markets are moving in today's day and age. Things used to be a lot slower. I guess you can attribute that to technology and just the environment that we're in. I saw a tweet today that said the Dow is up almost 2000 points in a week.

Tom Mullooly: And it's only Thursday.

Tim Mullooly: And you mentioned how, when I was born, the index itself was at like 3000.

Tom Mullooly: It was 3,200 when you were born, and now, it closed last night at 32,000. So that's pretty notable.

Tim Mullooly: Yeah, definitely. I think we've seen some volatility over the last couple of weeks, especially we talked about it on the video with the NASDAQ and technology stocks cooling off over the last few weeks. We've seen them rebound this week. But just to keep going back to this time last year, there was a tweet from Morgan Housel that outlined what the Dow did in March of 2020. Just to outline how volatile it was, there were days where it was plus 8%, minus 3%, minus 5%, minus 6%, plus five, minus 13, plus nine, minus 10, minus six, plus five, minus eight. And those were single day moves. I mean, there was a day during March of 2020 where the Dow was down 13% in one day.

Tom Mullooly: Yeah. That would be a bad year.

Brendan M: The last couple of weeks now we're seeing people getting nervous over draw downs in the NASDAQ especially that didn't even equate to that one week that you just talked about.

Tim Mullooly: Yeah, it barely touched 10%.

Brendan M: How quickly we become comfortable returning back to the norms. Not that you would anticipate those daily moves that we saw last March on a regular basis, but relatively compared to everything we're seeing today, that seems like nothing is what we're dealing with today.

Tom Mullooly: Yeah. We've all run into conversations that we've had with folks who see the market hit highs and then it backs off and they say, "That's my money. That's gone." Is it really? And I think that's what happened. Sorry to cut you off. But the values increase, they see it on the statement, and then they see it go down and they're like, "Wait, wait, wait. We should be protecting that. I like that number. We want to keep that."

Tim Mullooly: Yeah, I think it just depends on how people look at their accounts. One of the messages that you and Brendan delivered in the podcast last year was how these losses at the time in March of last year were only real losses if you sold and locked in those losses. So that on the flip side, it's similar. That money is technically only yours if you want to sell stocks or your ETFs at these prices and lock in those gains, so to speak.

Brendan M: Yeah. I mean, I think if you're comparing your account to the high water level on a regular basis, you're going to be disappointed more often than not because you could look through market history and the percentage of days that market indexes are hitting new all-time highs is very small in comparison to when they're in some sort of a draw down. A new draw down can be 1% or 2% off of the highs, or it can be 30% off the highs, like what we saw last year. Much more of the time is spent beneath the highs than reaching new ones. So pretty easy to be disappointed if that's going to be the bar, new all time high every time I log in to look.

Tom Mullooly: It just doesn't work that way. That's not based in reality.

Brendan M: Wish it did, but it's not.

Tim Mullooly: Since we were going to look back on what happened this time last year, I looked at the podcast that we recorded this week last year on March 13th. So a couple of days from now will be the one year anniversary of this podcast. The title was, What Do You Say to Worried Investors? And I think we were in the midst of the sell-off because it was the middle of March. So there were still a couple of weeks to go. I think you noted in the episode that the market was down about 25% at the time. And we all know that it got down to about 35% on some of the indexes. And I think the main message that Brendan delivered to answer that question, what do you say to worried investors, was just to make note of how you feel in this moment, and if you're really scared and you really want to do something with your account now, or then, might not have been the time to do it, but when things recover, and they will recover and we know that they did, to then look at your allocation and make adjustments then.

For people listening that might've freaked out during the downturn, do you want to make adjustments like now? Now would be a better time, I think, to really recalibrate the risk that you want to take in your portfolio.

Tom Mullooly: I had one incident, the same client, both conversations, called me around this time, and he was literally yelling into the phone, "The market's down another 2000 points, man." And I gave him that very approach, that when this market does recover over time, we should rebalance and lower the amount that you have at risk. And when I called him in September to do that, his response was, "What for? The market's going up."

Brendan M: And it's our job as an advisor to remind that person that they were worried sick in March. And so that's obviously a mismatch between the risk tolerance and what the account is aligned to do. And you've got to strike some middle ground, because if you were worried sick, screaming about the stock market, you're obviously in the wrong stuff. That should never be something that happens to you. If those are the emotions that you have when you look at your investments, then there's obviously something wrong with what you're doing. It's a mismatch for you. You cannot handle it. So you've got to figure something else out. And that's fine. You can do that.

Tim Mullooly: Leading up to last year, there hadn't been really that many stress tests for a lot of people for their account in terms of serious draw downs, more than 20%. So a lot of people, to be fair, might not have known how they were going to react because they hadn't gone through it in a really long time. But when something like this has happened, I think you need to learn the lesson and not just brush it off because then the next time, and it's going to happen again at some point, for whatever reason, you don't want to be in that same situation where you're freaking out again, you can't sleep because your account is dropping and you have too much risk.

Tom Mullooly: What happened last year in 2020, I think really was very fluky in the sense that you look at some of the high growth, high return funds that carry a lot of risk. For the year 2020, some of these funds posted gains of 40 and 50%. But if you actually dig in a little further and look back to where they were at the end of March or the beginning of April, those funds were down 35, 40, in some cases 50%, and they finished the year posting a gain of 40 and 50%, which means that from the bottom, these super aggressive funds were up 75, 80, in some cases 100% off the bottom. That should be completely unexpected. Those are, I mean, eye-popping returns and we should not come to expect those kind of things.

So I think part of our job is putting this in perspective for people that if we have a fund that's tied to high growth names and it's a lot of risk and it's down 9% or 10% in the last couple of weeks, let's put this perspective and see what's happened to this fund over the year, just use the year 2020.

Brendan M: Right. If you want to be in stuff like that, that's par for the course. That's a hiccup. That's nothing. If you're worried about 10% draw downs and you're investing for high growth, again, mismatched. That's not possible if you're not willing to tolerate volatility like that.

I think to piggyback on what Tim was saying a moment ago, I think it's important to take the experience of last year and recognize that it's always on the table when you have money in stocks. But I also think that it's important to, when you're constructing a portfolio, consider historically how frequently that's happened. So the feelings are very real. We should always anticipate that it's going to happen. However, don't build a portfolio that expects that is going to happen every single year. Because listen, I can't predict the future, but I don't think that that's the way you should construct things. But you should anticipate some kind of market action like that once a decade, for sure. We've seen draw downs above 30% sure. They're going to happen to the stock side of your portfolio. So you've just got, in my opinion, pretty friendly stress tests of it in the sense that it happened and then it recovered, and pretty nicely, over the remainder of the year.

Tom Mullooly: And recovered immediately.

Brendan M: So, take that for what it's worth and don't ignore it just because it did recover quickly this time. That sort of draw down can happen, will happen in the future, and it doesn't have to rebound as fast as it did.

Tim Mullooly: One of the final sentiments that you had in that episode last year was how there's no real substitute for experience. And that speaks to what you just said. We all experienced what happened last year together. It doesn't mean that it needs to shape your entire investing philosophy moving forward, but you definitely want to take note that, hey, that happened.

Tom Mullooly: There's something else. And I know I've caught myself saying this on podcasts and videos as well. Oh, we're going to go through a recession and it's going to be a short recession. Well, I think a lot of people are so wrapped up in the pandemic that they overlooked the point that we did stumble into a recession and a fairly deep one. It was sharp and deep, and we're already showing signs of recovering from it. Honestly for a lot of people, we got through it unscathed. Yes, there's still 10 to 12 million people out of work. Yes, the U-6 unemployment is around 11%. That's nothing to make light of, but as a whole, we're starting to see signs of recovery. That's pretty quick.

Tim Mullooly: Yeah. It's definitely quick if you go by the historical averages and textbook definition of what a recession is. My takeaway from that is, is that the textbook definitions and everything are great, but in real time, they don't mean anything.

Brendan M: Right. We have a recessionary period here where everybody who didn't freak out with their investments made money in stocks. So go figure on that, because normally we're trying to anticipate the next recession so that presumably we could do something to sidestep damage in the stock market that should correspond with it.
It didn't happen this time.

Tim Mullooly: It doesn't mean it won't happen differently next time, or it could happen exactly the same next time, but it's-

Brendan M: Exactly. So I'm not sure that there's … For all of the effort and mental bandwidth wasted, in my opinion, trying to figure out when the next recession is going to happen and why and what you should do as a result, just I'm not sure that that's really worth anybody's time because it's not predictable, and they are a virtual certainty to occur and multiple times over the course of even just a retirement time horizon, but let alone an entire investing time horizon. So you're going to have to deal with these things and sometimes they don't play out the way that you would expect even.

Tom Mullooly: It's the only recession that I can recall where we knew we were going into a recession as it happened. That normally doesn't happen. And we can almost pinpoint the date and time when we're emerging from this recession as well. That also never happens. So it's really unusual because you don't really know until you go back in time and, oh yeah, there's where we had two quarters of negative GDP growth. So that's where the recession began. Go back to the beginning of that period. It's the first time I can ever recall saying, "That's where it started and that was just a few weeks ago." That's really unusual.

Tim Mullooly: Yeah. And I think for what's more important for me as an advisor is realizing that we technically were in a recession. But I would say even some areas of the economy were definitely not in recessions. Some of them were in deep recession. Some of them weren't. Some people were in personal recessions and some people weren't. You could be living next door to someone and they're in a recession and you're doing just fine. I feel like almost nothing that happened last year made textbook sense.

Tom Mullooly: Now we have some folks that are in the real estate business. They sell individual properties. They had a great year. We have other people are in the restaurant and catering business. They had a zero, a negative year. So you're right in the sense that this was an unusual recession because it didn't hit all of the economic sectors equally with a 10% slowdown or a 15% slowdown. Some businesses, as you said Tim, fell straight to zero. Others actually increased. So each one's going to be a little different.

Brendan M: I find it interesting that because the market recovered quickly and because I guess the recessionary environment was different depending on who you are and what you do for a living, that I think there's a lot out there of people saying that the market draw down doesn't count because it recovered too quick or the recession doesn't count because this anecdote or that anecdote. And I think that's BS because what those people are trying to say is that they didn't see it coming because it was weird this time. And it's weird every time. So the lesson there isn't isn't that it didn't count. It's just that the people who proclaim that they can predict market downturns or recessionary periods are full of crap.

Tom Mullooly: Yeah, they are.

Brendan M: That's what I take away from that. And then they try to rewrite the rules to say that it wasn't the thing that they said it was going to be because-

Tom Mullooly: Let me go back in time and rewrite it. Yeah.

Tim Mullooly: On that point, there was an article in Think Advisor that Tom pointed out to me. I forget the guy's name.

Tom Mullooly: Harry S. Dent. He's back.

Tim Mullooly: Yeah. So apparently the world is going to end in June. All of the numbers, they're fake GDP numbers. All of the data that's been coming out is fake. Everything is a bubble. So logically in my head, if everything is a bubble, wouldn't nothing be a bubble too? He was saying real estate, Bitcoin, the market, stocks, bonds, everything is a bubble and it's all going to burst in June, but then we're going to come out rosy. I think he said it was like the new spring or something in 2023 or 2024.

Tom Mullooly: We'll link to it in the show notes.

Brendan M: Rinse, repeat. Once a year, this dude comes out and says this stuff, and everything's in a bubble except for whatever he's shilling at that point in time.

Tom Mullooly: He sells a lot of books. He definitely does.

Tim Mullooly: He had a book that came out last year and it was about bubbles and asset bubbles.

Tom Mullooly: The amazing thing is I was reading the article. I'm thinking to myself, wait a minute. He's saying in March that the entire financial community is going to collapse, but then by June, we'll be back. Didn't that happen last year?

Tim Mullooly: Right.

Brendan M: Yeah, kind of. Yeah.

Tim Mullooly: Where was that last year?

Tom Mullooly: Yeah, we could have really used that.

Tim Mullooly: Right. He's a year late.

Tom Mullooly: Recessions take on all different shapes and sizes, all different lengths of time. We never know how deep a recession will be for you or for the sector of the economy you're in, or will it harm everybody the same. We don't know when these things happen.

Brendan M: Consider it personally and figure out how you're going to get through it, not how you're going to sidestep it. That's imaginary unicorn land. Let's figure out realistically when this happens, what it might look like, and what the worst cases are and how we can protect against those that you're not self-destructed because of a rough period of time.

Tom Mullooly: I've said this many times on the phone and in person to clients when they're going through a tough time, whether it's a recession or a personal problem or whatever. The only way is through. You can't sidestep a recession or you can't sidestep some of these problems. The only way is through. We'll get through this. We got through last year. We're going to be okay.

Tim Mullooly: That's going to wrap up this episode, episode 347 of the Mullooly Asset podcast. Thanks for listening. We'll see you next week.