Deja Vu

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"What would you do if you were stuck in one place, and every day was exactly the same, and nothing that you did mattered?"

-Weatherman Phil Connors, Groundhog Day-

This 1993 movie about a weatherman (Bill Murray) stranded in Punxsutawney, Pennsylvania, while tasked with covering the annual February 2 tradition of Groundhog Day as a reporter for a nearby television station ponders that gem of a question. "Stuck in one place…exactly the same…nothing you did mattered." The line above speaks volumes about the current sentiment for a lot of us who follow the markets on a daily basis. Ever since the Federal Reserve put a (temporary?) halt to their multiple interest rate hikes in July of 2023, it seems as though every day is the same. Yes, there has been some moderate price movements here and there, but there is a rather lackluster feel to securities generally.

It's not just stocks. Energy prices (and many other commodities) have stayed within tight trading ranges, currencies have gone dull, many emerging market investments seemingly go nowhere, and even bonds have stalled out. This is also showing up in portfolio returns, or the lack thereof. While the world waits to see what the Federal Reserve will do next (or what they will say next), the general economy is adrift with prices on many securities taking one-step forward, one-step back. Volume has been waning, while volatility (as measured by the "Volatility Index," VIX) has ebbed. It just feels like total complacency.

Of course, the speculating community nearly always "has to do something," and so they do. You can look up any of the biggest company stocks, particularly in high tech, and they are the exception. Those stocks have lots of action! Big volume, big price swings, big headlines, and a near myopic focus on the daily highs. Certain financial news sources breathlessly report on which stocks are "in the buy zone" or "on a break-out" as they attempt to lay out a road map for the uninitiated and expert alike to find what is "on the move," and why not? The financial media has to gather eyeballs in order to sell advertising too! But for the average long-term and well-diversified investor? It is a challenging stretch at the moment. But, getting back to the question at hand:

"What would you do if you were stuck in one place, and every day……"

Here is one answer to that question. There is an old saying on Wall Street, and it goes like this: **"Never 'short' a dull market."** There are many moments when big moves are followed by big lulls, and we may be in one of those periods right now. However, we must not lose sight of our overall long-term goal, which for most of us is the combination of continuing to search out exceptional investments while at the same time being careful enough to not take a big hit. As much as it is both fun and interesting to be a stock investor, there isn't always a great trade to be had at every moment in the markets. Sometimes the better strategy is to sit and wait for opportunities to come to you. Consider what has happened just over the last two years:

The S&P 500 Index, the leading index of 500 of the largest publicly-traded companies, has finally managed to recover (just this past month) to the former all-time high peak of just two years ago.

The Dow Jones Industrial Average, an index of the leading 30 companies from various industries, is currently standing only about 2 ½% higher today than it stood nearly two years ago.

The Russell 2000, a broad index of mostly small companies that are the next 2,000 in size below the top 1,000 stocks (in other words, stocks numbered 1,001 through 3,000) is trading well off of its former all-time high peak and is currently at about the same level as it was three years ago.

The biggest energy ETF is trading off its peak and is at about the same level that it was at nearly two years ago. Further, as mentioned in last month's letter, the price of gold has returned to within 2% of where it traded in 2020 and again in 2022.

Déjà vu!! We've been here before!

As you can see, much time has passed while forward progress has been muted across a broad spectrum of tradeable securities. I could give many more examples, but what all of these have in common is that a major market-topping event occurred at the end of 2021, which then led to a significant pull-back. It has taken till now for the leading indexes to finally return to their prior highs. In the meantime (and of course with the benefit of hindsight), you could have invested in a fixed income product that would have provided a comparable return without all the inherent risk and volatility in between.

Now, we all understand that we cannot predict the future nor would anyone have known at that time that a fixed income product could have performed in line with a large basket of equity assets. BUT, food for thought, if we consider the extent of how overbought some of the leading stocks of today's market may be, and if we believed that the odds of another period of corrective action might lie somewhere ahead, couldn't smart investors agree that perhaps one strategy available to them would be to lean more heavily into those safer fixed-income investments (many paying 4% to 5%+)? Perhaps now might be one of those points in time where the more prudent positioning may be to exercise some patience while waiting for those remaining high-visibility, highly traded, and highly over-owned stocks to return to potentially more favorable valuations? From where I sit, if your long-term goal is to carve out a more moderate but somewhat consistent return without a lot of volatility, this may make good business sense.

I want to close this letter by calling your attention to a very important investment metric. We perform a number of financial analyses proposals each year for many of our client relationships as we try to discover how long their money could last, or whether there might be enough income in their retirement from the principal they've saved, or how to fund a future endeavor, whatever that might be. The starting point is the base capital, and then we must consider additional funds that might be added over time. Although a lot of investors would be thrilled to be getting 20%, 30%, or even 40% (and more!!) per year on their base capital, most of the long-term proposals that we perform result in the discovery that a more steady, less volatile 5% to 6% annualized return can often get them to where they need to go, and with a lot less stress. Furthermore, the power of compounding works with the benefit of time, but nothing is more devastating than experiencing a

20%, 30%, or 40% (or more!) loss of base capital on that long journey to wherever the person seeking the guidance needs to go. In fact, most investors can ill afford to take a hard financial hit and survive it. Once a large loss occurs, one of the biggest obstacles to face is that of renewed and entrenched fear. The tendency of many, following a large loss, is to try to avoid another future loss at all costs, but this often coincides with the aftermath of large market declines which, in the big scheme of things, is often the exact moment when one should be taking on more equity and market risk because this is often the time that certain securities appear to be on sale and cheap again!

Conclusion:
It took two years to traverse from a major bull market high down to a corrective low and then, for some sectors and indexes (but not all), back up around the top again. Now what? The bulls are in charge, complacency is back, speculation is apparent, and some very narrow areas of the market are witnessing near vertical price runs, which frequently coincide with terminal phases of bull markets. A number of market signals are flashing "red" warnings (stretched valuations in certain highly concentrated positions, a low volatility indicator mentioned above – a "contrarian" indicator – the potential that we are still sliding slowly into recession, and more), and these are suggesting to me that this may not be the best time for the average investor to be overweight stocks.

My portfolio recommendation for those prioritizing moderate growth with an eye on capital preservation hasn't changed. Where appropriate, I'd suggest a continuing overweight on short-term fixed income (bonds, CDs, Treasuries); moderate exposure to domestic equity with a focus on more favorable areas for an inflation economy such as basic materials, energy, consumer staples, and health care; some emerging market equity and debt; some exposure to precious metals; and finally, some modest exposure to real estate and some liquid cash. I am currently recommending avoiding (or at least minimizing) exposure to information technology, by far the biggest sector within the S&P 500 Index. It just looks so overbought and over-owned. Otherwise, let's see how 2024 shapes up! Oh yes, one more thing. "*Groundhog Day*" is here, so you can probably find the movie playing on multiple cable channels right now!

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Indices are unmanaged and are not available for direct investment. Past performance is no guarantee of future results. Index returns include the reinvestment of dividends but do not include adjustments for brokerage, custodian, and advisory fees.
The Standard & Poor's 500 Index is a capitalization-weighted index that is generally considered representative of the U.S. large capitalization market.
The Dow Jones Industrial Average (Dow) is an index that shows how 30 large, publicly owned companies based in the United States have traded during a standard trading session in the stock market.
The Russell 2000 Index measures the performance of the 2,000 smallest companies in the broader Russell 3000 Index, which measures the performance of the 3,000 largest U.S. companies based on total market capitalization. The average market capitalization is approximately $490 million, and the median market capitalization is approximately $395 million.
The risk of loss in trading commodities and futures can be substantial. You should therefore carefully consider whether such trading is suitable for you in light of your financial condition. The high degree of leverage that is often obtainable in commodity trading can work against you as well as for you. The use of leverage can lead to large losses as well as gains. There are special considerations associated with international investing, including the risk of currency fluctuations and political and economic events. Investing in

emerging markets may involve greater risk and volatility than investing in more developed countries. When investing in real estate companies, property values can fall due to environmental, economic, or other reasons, and changes in interest rates can negatively impact the performance. When investing in bonds, it is important to note that as interest rates rise, bond prices will fall.