MAY 7, 2024

RZHadvisors

RZH INSIGHTS

"IN SPITE OF THE COST OF LIVING, IT'S STILL POPULAR"

“In spite of the cost of living, it’s still popular” - Kathy Norris

This witticism aptly captures the current state of the U.S. economy, where inflation remains persistently high. Americans, renowned for their robust spending habits, continue to prioritize maintaining their lifestyles, further complicating economic predictions.

This has led to increased market volatility over the last few weeks as pundits extrapolate this to mean that the Federal Reserve will be slower to lower interest rates than previously anticipated. Through March of this year, the stock market rallied assuming Fed rate cuts were imminent. However, an abrupt change in perception led to a recent 5.3% decline in stock values over three weeks, with bond prices also dropping as interest rates rose. [1]

I usually find it less necessary to write newsletters during bullish market phases. Research indicates that overloading investors with information can sometimes lead to unneeded anxiety. As Warren Buffet’s longtime partner, Charlie Munger, once said “the first rule of compounding is to never interrupt it unnecessarily.” (Charlie was a national treasure who we sadly lost in November, just days away from his 100th birthday. Warren credits Charlie with much of Berkshire Hathaway’s success.)

So, when my phone started ringing more than usual lately, with clients nervous about this new (downward) volatility, I knew it was time to reach out.

The Fed's goal going into 2022 was to defeat inflation through "demand destruction." They took a sledgehammer to the economy, using 11 interest rate hikes and quantitative tightening to break inflation. The Fed rate hikes which began on March 17, 2022, also created a dreaded "inverted yield curve" which the media assured us would throw the country into a recession at any moment. We were told to brace for a "hard landing". Robert Shiller paraded around on TV, his CAPE Ratio - which implied that stocks were grossly overvalued, was surely correct and famed money manager Jeremy Grantham (on August 31, 2022) said this would lead to "an epic crash." Since then, other headlines have tried to separate our clients from their investments and seek the perceived safety of cash.

The inflation mania peaked soon after, in the fall of 2022, and despite these dire forecasts our advice remained steadfast. I wrote a newsletter on September 27, 2022, reiterating our continued guidance to stay focused, continue working the plan, and not change course because of doomsday predictions. I wrote: "I believe that making investment policy based on predictions, instead of evidence, is very dangerous." "The worst plan is the one not followed – especially in the face of provocation such as this market environment and media hysteria." Current events, and the market's gyrations in response, are the third rail of investing.

Fortunately, RZH clients heeded this advice and those in the public who panicked, adrift without an advisor, missed out on a stock market advance of 45% since my September 2022 newsletter.[2] Yes…over the next 19 months or so, the S&P 500 (with dividends) produced over four years' worth of average returns.[3] There was no "landing" at all, hard or soft. The US economy just kept cruising, corporate earnings kept growing and stock prices followed suit.

This reinforces our philosophy that a thoughtfully crafted, plan-driven, stress-tested portfolio makes current events irrelevant to what we do. And it further reinforces our mantra; the markets cannot be consistently timed, and the economy cannot be reliably forecast.

As we face 2024, we expect continued volatility, influenced by global conflicts, domestic unrest, sticky inflation, and a presidential election which is sure to be a spectacle.

So, during such times of fear and uncertainty, it is always prudent to revisit some core tenants of our investment philosophy:

General Principles of the RZH Investment Philosophy

- We are goal-focused and planning-driven, as sharply distinguished from an approach that is market-focused and current-events-driven. We believe long-term investment success comes from continuously acting on a plan. Investment failure often results from continually reacting to current events in the economy and the markets.

- History has shown that the economy cannot be reliably forecast, nor the markets consistently timed. You and RZH are long-term investors, working steadily toward the achievement of your most cherished lifetime goals. We make no attempt to forecast, much less time, the equity markets; these efforts have a historically extremely low probability of success.

- Understanding investors' inability to consistently time the stock market, we believe that the only way to be sure of capturing the full premium return of stocks is to ride out their frequent but ultimately temporary declines.

- Factors which add a significant amount of value to an investment plan are: keeping costs low, being diversified, focusing on tax efficiency, staying liquid, and matching asset allocation and investments with objectives.

- Our essential principles of goal-focused portfolio management remain unchanged:
    a. The performance of a portfolio relative to a market benchmark is largely irrelevant to long-term financial success.
    b. The only benchmark we should care about is the one that indicates whether we are on track to accomplish your financial goals.
    c. Risk should be measured as the probability that we will not achieve your goals.
    d. Investing should have the exclusive purpose of minimizing the risk of not achieving your goals.

Our mission remains - to help our clients and their families embrace life to the full extent of their wealth, knowing they have a plan in place which makes short-term market fluctuations irrelevant to their financial security.

We are always here for you and continuously available to discuss market dynamics or how your financial plan and portfolio is prepared for future uncertainties.

Thank you for being our clients and trusting us with your financial journey, it is a genuine privilege to serve you.

Best wishes for a wonderful summer!

Carl

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Principal, Chief Investment Strategist

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1. Performance calculated using Vanguard S&P 500 ETF (“VOO”) closing price as proxy for S&P 500 Index for the period March, 28, 2024, through April 19, 2024, assuming dividend reinvest. Full calculation methodology available upon request.

2. Performance calculated using Vanguard S&P 500 ETF (“VOO”) closing price as proxy for S&P 500 Index for the period September 27, 2022, through May 6, 2024, assuming dividend reinvest. Full calculation methodology available upon request.

3. “Average returns” refers to average annual returns of the S&P 500 index from 1926-2023 of 10.1% as published in the Dimensional Fund Advisors Matrix Book, Historical Returns Data.

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