LEWIS
WEALTH MANAGEMENT

Newsletter

October 13, 2023

Executive Summary

The world is a very stressful and unstable place right now, and we are struggling to adapt.

If stressful events cause you to question your portfolio and you are considering changes, it is best to be calm and use a process to help make these decisions.

When helping clients, I typically think about financial goals, time horizon, investment philosophy, historical context and perspective, capital market impacts, and costs.

As for investment philosophy, I think about asset allocation, investing (not speculating), consistent exposure to capital markets, diversification, and avoiding panic and catastrophizing.

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Market Data as of September 30, 2023

		YTD 2023
US Equities	S&P 500 ETF	12.98%
International Equities	MSCI EAFE ETF	6.56%
Emerging Markets Equities	MSCI Emerging Mkts ETF	1.28%
US Bond Market	iShares US Core Bond ETF	-1.03%
Commodities	S&P GSCI Comm ETF	6.25%
Real Estate	iShares US Real Estate ETF	-5.14%

There is a lot going on in the world right now. It is a very stressful and unstable place.

There is a new war in Israel against inhumane terrorists using horrifying tactics that scare us all. The war will cause suffering and trauma for civilians on both sides. Our hearts are broken. There is an existing war grinding on in Ukraine. There is unprecedented political division here at home. We are approaching another contentious political campaign season. ***We are struggling to adapt to an increasingly volatile world.***

Many of us are fearful and anxious. Others may become angry and project strength to mask their fears. It is instinctive to seek safety.

While financial concerns are not always first and foremost in our minds, some will eventually wonder whether the current situation will impact the capital markets and their long-term goals. Our desire for safety can lead us to question our investment decisions, especially when markets are volatile.

Our urgent desire for safety is at odds with our need to take the necessary investment risks to earn a long-term return. That need to take risk can be thrown out the window in a moment during periods of volatility and stress.

In my experience, this is when investors are vulnerable to making mistakes. I'm not saying that all moves to safety are wrong—sometimes that is the right decision. But as investors, we need to slow down and distinguish between wisdom and panic and between smart and dumb money moves. This can only occur when we are calm and have a logical process in place for thinking about our investment decisions.

Here are a few things I think about when dealing with client portfolios during stressful times.

Remember Your Financial Goals

Remember your long-term financial goals, because this is why you are investing in the first place. Make sure your investment decisions are consistent with those goals.

Acknowledge Your Time Horizon

Your time horizon is at least as long as your lifetime because that is how long your money must last. It may even be longer if you have children or charities that you care about. Short-term losses and setbacks are part of any successful long-term investment experience. Smart investors understand that markets recover. They play the long game.

Lean on Your Investment Philosophy

Make sure your investment decisions are consistent with your investment philosophy. This is what discipline is all about. I look to the following for guidance.

a) Asset Allocation

Asset allocation is the process of deciding how much of your portfolio to invest in each of the different investment types, or asset classes—equities, fixed income, and even some alternative investments. ***Asset allocation is your first investment decision because it is the most important. Maintaining an asset allocation requires discipline, and that is very important.***

b) Investing, Not Speculating

Investing creates real wealth. This wealth is created when natural resources, skilled labor, intellectual capital, and financial capital are skillfully combined in an enterprise to generate profits. As investors, we want to capture some of that wealth and make it our own.

Speculating is not investing. It involves making a bet against someone else that the value of something is going up or down, usually on a short-term basis. Because there are two sides to every bet, there is a winner and a loser. It’s a zero-sum game. At the end of the day, no real net wealth is created.

We are better off investing the vast majority of the time and minimizing speculation. Market timing and pulling money in and out of the market in response to stressful events are speculative. We have a much better chance of financial success when we act as long-term investors and occasionally use a small amount of conservative speculation to hedge our bets and reduce volatility.

c) Consistent Exposure to Capital Markets

To earn a good long-term rate of return, you generally need consistent long-term exposure to capital markets. ***Investors who jump in and out of the markets typically underperform.*** Markets are very adept at quickly reflecting current information, including the information you are relying on. If you think you can outsmart thousands of other market participants, you may be ***overconfident***.

d) Diversification

Diversification means not having so much of one thing that it kills your investment portfolio and your financial goals if the market moves against you. ***Diversification is the only free lunch in the investment business, and you should take advantage of it.*** Never get caught flat-footed by holding too much of one thing at a time.

e) Avoiding Panic, Euphoria, and Catastrophizing

One interesting thing about investing is that we often must do the opposite of what our gut is telling us to do. It is okay to feel fearful or even greedy; we just should avoid making investment decisions based on those emotions.

We should also avoid catastrophizing. That means creating a hypothetical series of events that leads to a catastrophic outcome and making decisions based on that hypothetical outcome. I'm very good at this myself. Trying to anticipate what might happen next is important, but it is very difficult to do, and we should not cross the line into making decisions based on remote possibilities.

Gain Historical Context and Perspective

Put the stressful event into historical context. Do a little objective research. Has the event ever happened before? If so, when did it happen? How long did it last? How did markets react and recover? Answering these questions often helps put the current stressful event into perspective.

Consider the Potential Impact on Capital Markets

Without catastrophizing, what could be the probable economic impact of the event? Since stock prices are a reflection of a company's future cash flow, how will the event realistically impact that cash flow? Not all adverse events impact the capital markets.

Consider Costs, Especially Opportunity Costs

What is the cost of being wrong? And don't forget about opportunity costs (that is, the return you would have earned if you had stayed put). How can you unwind a decision if you later change your mind? Carefully consider the arguments for and against your decision.

As chaotic events unfold around us, I hope this framework is helpful when you decide the time is right to think about your money in the days and weeks ahead.

If you have questions about your portfolio or your long-term financial plan, give us a call.

Thank you.

D. Austin Lewis