Seymour Investment Management

January 17, 2020

2019 saw strong results for most global equity markets. The S&P/TSX Composite Total Return Index ("TSX") was up 3.2% for the quarter and 22.9% for the year. Global results were similarly strong with the MSCI World Index up 24.9% and the S&P 500 up 28.9% for the year.

The strong returns during the year were aided by the positive environment for equity growth: stable inflation, modest economic growth and accommodative interest rates. These tailwinds propelled equity returns well ahead of other asset classes for the year.

The positive results posted by markets in Canada and around the world were met with little fanfare

The Most Hated Bull Market in History

There is an old saying that "markets like to climb a wall of worry." The positive results posted by markets in Canada and around the world were met with little fanfare. There was no frenzied trading or euphoric investors to be found. Instead, a subdued cloud continues to hang over much of investors' overall sentiment. Despite posting strong and in some cases record results over the course of the past decade, this bull market appears to be one of the most hated bull markets in history!

What has long since been heralded as a conventional and widely accepted observation – that over the long-term stocks are a prudent place to invest your money - has felt more like a reckless and contrarian view over the course of this bull market. This wall of worry has led to many investors missing out on the wealth building, compounding effects of equity growth. As is the case, for much of the past decade, headlines have been dominated by reasons to worry: from politics to international disputes, sovereign debt to trade wars. Yet in the face of these negative headlines and fearful sentiment, the economy has grown and so have equity markets.

Fewer people are invested in stocks today than before the 2008 meltdown

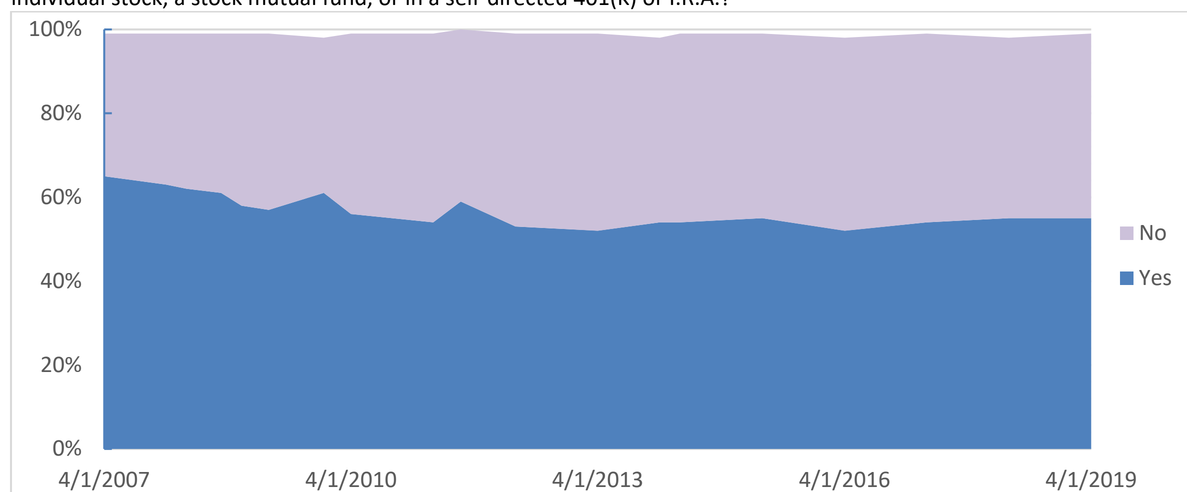
The subdued and apprehensive response by investors is likely a result of the psychological and financial toll the 2008 financial crisis took on investors. The crisis and the ensuing recession has left an enduring and significant impact not only on investors' sentiment but also on their investing strategies. Investors' optimism has been replaced by excessive skepticism.

As a result, fewer people are invested in stocks today than before the 2008 meltdown. The graph below details a declining level of participation in equity investing from 65% in 2007 to 55% in 2019. This trend

illustrates investors' choice to forgo potentially higher returns in favour of lower volatility. In a climate of historically low interest rates and strong equity returns, this has contributed to a widening gap between those invested in the market and those sitting on the sidelines.

Appendix 1: Participation in the Stock Market

Gallup Poll: Do you, personally, or jointly with a spouse, have any money invested in the stock market right now – either in an individual stock, a stock mutual fund, or in a self-directed 401(K) or I.R.A.?



Source: Gallup Polls: In Depth Topics A to Z: Stock Market 2019

The number of Americans under the age of 35 that have money invested in the stock market has dropped from 52% prior to the 2008 financial crisis to 35%

Similar psychological effects have been noted before. Even into the 1960s, investors who were young during the Great Depression, were significantly less likely to invest in stocks. Economists Stefan Nagel of the University of Chicago and Ulrike Malmendier of the University of California, Berkley, and have found that these financial shocks can shape a cautious and skeptical investing outlook that can last for decades.

We can see that trend shaping with the current generation. *The New York Times* reported, based on Gallup survey data, that in the last decade the number of Americans under the age of 35 that have money invested in the stock market has dropped from **52% prior to the 2008 financial crisis to 35%.**

It is no surprise then that these remarkable years for capital markets have enticed little new money to the table. 2019 saw $4.6B in net outflows from equity specific ETFs and mutual funds per data from the Investment funds Institute of Canada ("IFIC"), a trade association for regulated funds in Canada.

Those who stay the course through the natural ups and downs of market movements are rewarded with long term results

As it stands, investors are sitting on record levels of cash. Statistics published in Investment Company Institute's ("ICI") Third Quarter report, detail that Worldwide Money Market holdings sat at 12% of total net assets, representing a total of $6.6 trillion globally which includes $3.4 trillion in the US. Recent trends and projections into 2020 suggest that these large cash piles may be drawn on as investor sentiment stabilizes and investors are encouraged by the unattractive low interest rate alternatives and relatively attractive equity returns.

Overall, it is an important lesson that throughout the noise and the sentiment, the politics and the uncertainty, the market continues to climb a wall of worry. We are reminded that although we cannot time the market, history tends to favour the consistent investor. Those who stay the course through the natural ups and downs of market movements are rewarded with long term results.

What Happens After a Good Year?

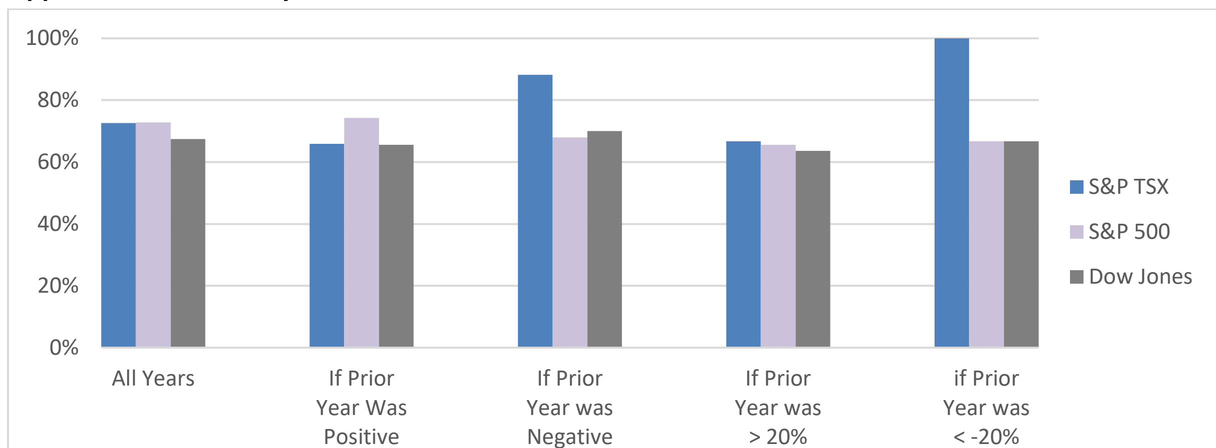
Following a year that brought above average returns, a question often asked is 'what happens next?' Does a good year mean a correction is around the corner?

The answer to that question lies in our often touted response: one cannot predict the markets over the short term. However, over the long term we can take advantage of the positive trends that work in the favour of those who stay invested.

A strong year does not significantly change the odds for the following year

As we have detailed in previous letters, roughly two out of three years are positive and one out of three is negative. Interestingly, an exceptionally strong year does not significantly change the odds for the following year. This is detailed in the graph below which highlights the percentage of years that were positive under various scenarios for the S&P TSX since 1958, and the S&P 500 and Dow Jones Index since 1928.

Appendix 2: Probability of a Positive Year



Source: Seymour Investment, Hulbert Ratings, S&P TSX Total Return Index, S&P 500 Index, Dow Jones Index Data

Even with an exceptional year like 2019, where returns were over 20%, the following year has an average 65% chance of being positive

Approximately 72% of the time the market is up on an annual basis. Notably, the market is up more than two thirds of the time regardless of what happened in the preceding year. Even with an exceptional year like 2019, where returns were over 20%, the following year has an average 65% chance of being positive.

A healthy stock market will always exhibit volatility. Although we do not know when, we do know negative years will be part of normal market movements. But more importantly, we do know that the positive years, like 2019, will outweigh those negative years over a long term investment horizon.

Please, as always, do not hesitate to reach out should you have any questions.

Sincerely,
The Seymour Team