Long-Term Investing Trumps Short-Term Fears

By: Nick Lewandowski, CFP® *November 2016*

We are cursed to live in interesting times. This election cycle presented us with two candidates, who, by all accounts, were the two least popular in American history. On November 8th, the American people elected Donald Trump the 45th President of the United States of America. Depending on who you ask, this either spells certain doom for the American way of life or heralds a new era of political and economic revival.

Predictably, markets around the world reacted strongly to what was largely an unexpected outcome. They fell. To sample a few headlines:

"Stunning Trump presidential victory has Wall Street's 'fear gauge' jumping,"

"Trump wins election but the shocks for stocks aren't over yet,"

"Solar stocks tank and lead broader energy sector lower."

We can expect to see more headlines like these in the coming days and weeks as financial markets attempt to price the impact of a Trump presidency. I cannot begin to tell you where the markets will end up in 2016, beyond the rather trite observation that price moves up and down are likely to be larger than usual in the short-term.

Uncertainty is frightening in both life and investing. In times of political and economic upheaval, it is, therefore, prudent to tune out frightening headlines and focus on long-term plans and outcomes.

For long-term investors such as ourselves the outcome of this election, or any election, should ultimately have a negligible impact on our investment portfolios. In the last hundred years, the diversified investor's portfolio has endured two world wars, multiple oil booms and busts, natural disasters, various and sundry financial crises – not to mention the standing possibility of human extinction via nuclear war.

Despite innumerable social, political and economic perils the diversified, long-term investor has not only survived but prospered.

How? By focusing on the mathematically irrefutable fact that in the long run, the odds are in the diversified investor's favor.

Joachim Klement, CFA, put this into sharp perspective in a recent blog post (https://blogs.cfainstitute.org/investor/2016/11/01/dumb-alpha-do-the-right-thing/). He notes that, assuming one invests roughly in line with the historical average performance of the US market:

"[t]he probability of a positive return over any given year is 93%. As a result, an investor who evaluates the portfolio once a year will experience a loss once every 10 years or so. If the same portfolio is evaluated quarterly, a loss will occur about once every four quarters, or once a year. And if that portfolio is evaluated daily, roughly 120 days a year will register losses.

It takes superhuman discipline not to change a portfolio when you are confronted with losses 120 times a year. But the best returns, in the long run, are achieved by adhering to a well-diversified investment strategy that lets you reap the benefits of the different risk premia available to long-term investors."

A better-known commentator extends that logic to our present circumstances:

"It's an election year, and candidates can't stop speaking about our country's problems (which, of course, only they can solve). As a result of this negative drumbeat, many Americans now believe that their children will not live as well as they themselves do.

That view is dead wrong: The babies being born in America today are the luckiest crop in history.

American GDP per capita is now about $56,000. As I mentioned last year that – in real terms – is a staggering six times the amount in 1930, the year I was born, a leap far beyond the wildest dreams of my parents or their contemporaries. U.S. citizens are not intrinsically more intelligent today, nor do they work harder than did Americans in 1930. Rather, they work far more efficiently and thereby produce far more. This all-powerful

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trend is certain to continue: America's economic magic remains alive and well."

That, of course, is from Warren Buffett – commonly regarded as the greatest living American investor – in his most recent annual letter to shareholders (http://www.berkshirehathaway.com/letters/2015ltr.pdf).

In fact, as a long-term investor you are better served to heed Mr. Buffett's letter than anything CNN, Fox News, The New York Times, Bloomberg, CNBC and their ilk have to say about election results, markets, and in particular, strategies for investing your hard-earned capital.

Financial news stories are produced to attract clicks, page views and eyeballs (whatever advertisers prefer to pay for). Promoting positive investor outcomes is a distant secondary or tertiary concern – if it is a concern at all. This misalignment of incentives takes on critical importance in times of short-term political and economic stress, when the news media implies investors must *do something or face certain disaster!*

In fact, just the opposite is true.

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