RESOLUTE FINANCIAL

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Resolute Connections

Welcome to 2018, we hope your year is off to a great start. With the bull market continuing we thought we would present a series of articles on the market. *When the Index Beats the Algorithms* reviews a famous bet Warren Buffet made with a hedge fund manager, he just collected on it. *False Visions of the Future* discusses those financial experts who seemingly know everything about the markets, and how the markets will perform in the future, you might want to avoid their advice.

If you are looking for help navigating the markets check out - *Professional of Sales Agent? You Decide*, before you hire an advisor. And *Eerily Quiet on the Market Front* reviews the current market calm, whether this is normal from a historical perspective, and presents the case one might want to prepare for a more volatile market.

If you have any questions about anything we have covered in the articles below, or a specific situation please feel free to give us a call, or visit our website, www.ResoluteFinancial.com.

When the Index Beats the Algorithms

You might wonder why there wasn't more media coverage of one of the most interest bets ever made in the investment world. We're not talking about betting on a company; this bet was made between Berkshire Hathaway chairman Warren Buffet and a hedge fund called Protégé Partners, on whether a basket of hedge funds managed by algorithms and super investors would beat a simple S&P 500 index fund over a period of 10 years—which happened to include the Great Recession and one of the longest bull markets in history. Each side put about $320,000 in 2007, with the proceeds—including all gains—going to charity.

The final score wasn't even close. The index fund gained 7.1%, compounded annually. The basket of hedge funds returned a below-average return of 2.2%.

The original intent of the bet was to prove a point: that it is usually impossible to outthink the market, no matter how smart you are, no matter how cleverly you use derivatives, hedging and futures contracts. Yes, Buffett has been outperforming the market for most of his career. But he has unusual access to deals, and extraordinary patience—which can be more powerful than algorithms when it comes to beating the market.

False Visions of the Future

The financial experts know a lot more about the markets and how the markets will perform in the future than the ordinary rest of us. Right?

As it turns out, the predictions made by financial experts are no better than those made by gypsies looking into crystal balls, soothsayers gazing at the entrails of a sacrificed animal or wizards with tall caps who gaze into space. In fact, the financial experts might even be LESS reliable than those other charlatans.

The reason we don't know this is that we all read the annual predictions made by so-called market experts, but nobody ever goes back to see if those predictions ever came true. Well, almost nobody. Larry Swedroe, an economist and director of research for Buckingham Strategic Wealth, spent much of 2017 compiling predictions that were made with a great deal of certainty, and recently gave what might be called a "guru scorecard" of results.

One popular prediction was that bond rates would rise dramatically in 2017, causing bond investors to book significant losses. Actual result: the Vanguard Long-Term Treasury Index returned 8.6% for the year, and the Vanguard Intermediate-Term Treasury Index gained 1.7%.

Another popular prediction: that the inflation rate would rise significantly—which also didn't happen in 2017. Swedroe notes that economists expected stocks to provide moderate single-digit returns, the dollar to strengthen and emerging markets to get socked by the potential for trade wars. None of these predictions actually came to fruition.

In all, out of six "sure things" that the gurus predicted, just two actually happened: small cap stocks did indeed underperform large-cap stocks in 2017, and the U.S. economic growth did strengthen in 2017 over 2016—albeit modestly.
Swedroe has been keeping track of "sure things" that pundits have predicted, and whether they actually turned out to be true, since 2010. You can see from the chart that of 62 significant predictions in that time period, 43 turned out to be wrong.

Larry Swedroe's Predictions vs. Reality: the shame of Gurus

Year	Number of Sure Things	Yes/True (+)	No/False (-)	Tie/Draw
2017	8	2	6	0
2016	8	2	6	0
2015	8	3	4	1
2014	10	3	7	0
2013	7	2	5	0
2012	8	3	4	1
2011	8	1	7	0
2010	5	1	4	0
Total	62	17	43	2

If you're looking for more evidence, consider experts predictions of where 10-year bond rates will go each year since January 1, 2008. At the beginning of each year since 2008, the forecasters have done essentially the same thing: predicted that bond rates would go up significantly during the course of the upcoming year. Actual rates, with the exception of one year, actually fell significantly short of the predictions. (That year, 2013, the consensus was dramatically wrong on the downside—but still dramatically wrong).

All of this is worth remembering next time you hear a pundit or market guru make a confident prediction about what's going to happen in the markets. Based on past history, you could have done better if you'd relied instead on a gypsy fortune teller.

Professional or Sales Agent? You Decide.

You've probably read a dozen articles that tell you how to tell a good financial planner from a salesperson or product-pusher, but the truth is, the salespeople and product pushers are so good at looking like the real thing that most articles fail to unmask the pretenders. Not the case in a recent article by Liz Weston, columnist for NerdWallet, a very helpful financial website frequented most often by Generation X and Y consumers.

Weston says that brokers and salespeople will allow their customers to believe that they are required to act in your best interests, when in fact they are actually held to a much lower standard; if you need to invest, then it is "suitable" to recommend a high-commission annuity, non-traded REIT or other product which a real financial advisor, held to a higher fiduciary standard, would never consider recommending. Weston's first piece of advice is: if your "advisor" recommends anything other than a portfolio of low-cost, high-integrity mutual funds or ETFs, run for the exits and remember to hang onto your wallet when you do. Also watch out for "proprietary" mutual funds; that is, funds managed by the employer of the "advisor" who is earnestly recommending them.

Weston also notes that some product salespeople claim that their services are free, or dirt cheap. You never see the commissions that they earn, or incentive payments or other sly under-the-table compensation which actually makes the relationship much more expensive than an honest advisor relationship. Weston notes that advisors who don't register with the Securities and Exchange Commission as registered investment advisors, who don't have the CPA or CFP designations after their names, should be presumed guilty until proven innocent. Ask them if they're willing to promise to act as a fiduciary in writing. The Committee for the Fiduciary Standard has created a fiduciary oath that advisors can download and sign.

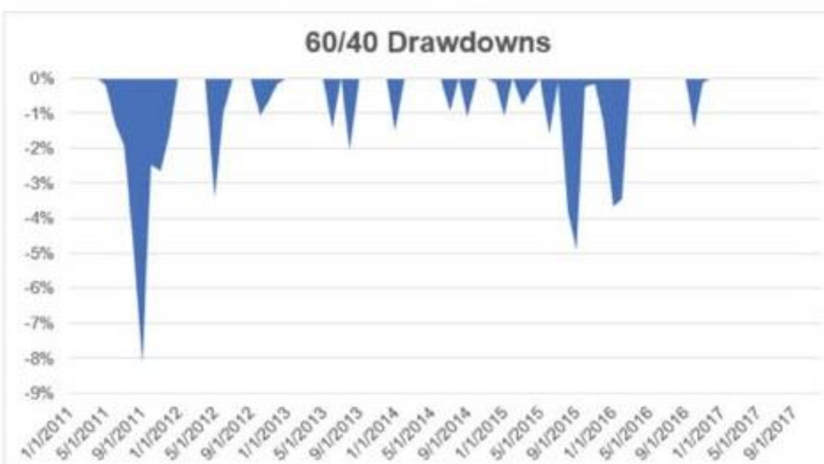
The key message here is that conflicted advice can cost you considerable amounts of money.

Eerily Quiet on the Market Front

While the U.S. stock market tests new highs, and valuations keep rising farther above long-term averages, you may not have noticed something very odd about our current bull market. The last six and a half years have set a record for having the lowest amount of market volatility, and the past 299 trading days, starting in November of 2016, has set an even bigger record for low volatility. The markets have been eerily quiet for longer than they ever have been before.

To see what this means, look at the first chart, which shows the losses (aka "drawdowns" in professional investor speak) for stock market investors since January 1, 2011. The blue spaces represent market pullbacks—a euphemism for temporary losses—that a 60/40 (U.S. stocks/U.S. bonds) has experienced over the last six years. Two things jump out at you; first, investors in this very basic portfolio haven't experienced portfolio losses greater than 5% since September of 2011—more than six years ago. Even spookier is the back end of the chart, which shows essentially zero drawdowns since the end of last January.

Chart 1: Portfolio Volatility Since January 1, 2011



The second chart illustrates the longest time periods when the markets remained within 3% of an all-time high, which basically means that there were gains without a significant downturn. The previous record, 241 trading days, was set between late

January 1995 and early January 1996, and the chart shows other records going back to 1961. The longest streak, which is still ongoing, is the time period since November 7, 2016.

S&P 500: Longest Streaks Within 3% of an All-Time High (1928 - 2018)			
Rank	# Trading Days	Start Date	End Date
1	299	11/7/2016	1/16/2018
2	241	1/26/1995	1/9/1996
3	162	7/7/1993	2/23/1994
4	131	11/26/1963	6/3/1964
5	120	9/2/1965	2/23/1966
6	114	12/17/1964	6/1/1965
7	105	1/27/1983	6/27/1983
8	91	3/19/1985	7/26/1985
9	87	6/29/2016	10/31/2016
10	82	10/19/1992	2/12/1993
11	76	2/18/1959	6/5/1959
12	75	4/15/2014	7/31/2014
13	73	8/21/1928	12/5/1928
13	73	4/29/1997	8/11/1997
13	73	3/16/2015	6/26/2015
16	72	1/10/1961	4/21/1961
16	72	10/10/2013	1/23/2014
18	69	8/9/1963	11/15/1963
19	68	9/27/1961	1/4/1962
19	68	7/10/1989	10/12/1989

What does this mean? It's impossible to predict the future based on this kind of data, but it does indicate that the U.S. investment markets have been behaving strangely, and it suggests that we are long overdue for at least a moderate correction. When that will come remains a bit of a mystery, so let's celebrate our good fortune up to now, and recognize that it won't last forever.

Source:

Bob Veres Inside Edition Newsletter

For more information on these topics or for a free consultation, contact Resolute Financial, LLC at (978) 463-8771 ext. 1003.

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