Economic and Market Insights

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Reasons *not* to be a momentum investor even with U.S. markets reaching all-time highs

As part of a series on how advisors can deliver value to their clients, Nick Fafoglia, CFA®, a senior Investment Portfolio Manager at The Commerce Trust Company, helps investors re-examine their underlying motivations in making buy-sell decisions for their portfolios.

Q. One prominent fund manager said recently to "sell everything" and another said the Dow Jones Industrial Average will hit 20,000 in 12 months. What should I be doing in my portfolio when two so-called experts have such polar opposite views?

A. We tell clients to simply stay with their long-term asset allocations. The three major U.S. stock markets indeed reached all-time highs recently, the first time that's occurred since 1999. While it's certainly tempting to get caught up in the psychology of the stock market's rallies or declines, remember that no one can perfectly time the market. So we remind our clients it is generally to your advantage to stick with your current asset allocations over the long term to achieve your particular portfolio goals.

Q. What if I miss the upward momentum of the market?

A. Momentum investing aims to take advantage of existing upward trends in the market, but it is by definition a short-term strategy. Long-term investors dial back their attention on the day-to-day gyrations of the market and consistently check in with their investment advisors for what's relevant for their portfolios. Usually, people are rational in attempting to maximize their wealth, but bull or bear runs often suspend our critical thinking. Emotions and psychology influence our decisions, causing us to behave in unpredictable or irrational ways.

Q. How can I reduce the urge to follow the crowd as an investor?

A. Remember that investors who employ a herd-mentality strategy constantly look to buy and sell in pursuit of the newest and hottest investment trends. The thought is that if everyone is buying, it must be a good decision. However, as the various stock market bubbles over the decades have painfully illustrated, it is usually not a very profitable investment strategy over the long haul.

For example, those who stayed consistently invested in their market allocations after the Great Recession were rewarded eventually. In March 2009, the trough of the Great Recession, the Dow was at the 6,547.05 level and the S&P 500 was at 676.53, 12-year lows at the time. If investors consistently remained true to their allocations after that point, they would have meaningfully participated in the current 7-year runup to 18,500+ and 2,100+, respectively. Investors should work with their advisors to allocate their portfolios on what is appropriate for their risk tolerance, age and personal financial goals. Keeping it simple works.

<u>Takeaways:</u>

- In an up-market trend, your current allocation is likely catching at least some of the benefits of the recent runup.
- Retain perspective. Short-term approaches don't usually yield the best investment results.
- Your goals are those family and financial objectives that are the focal point of your financial plan – not some number in a stock index. Preparing for what you want to do in retirement, helping your children or grandchildren, or making a difference in the community is what your investment plan should be all about.

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