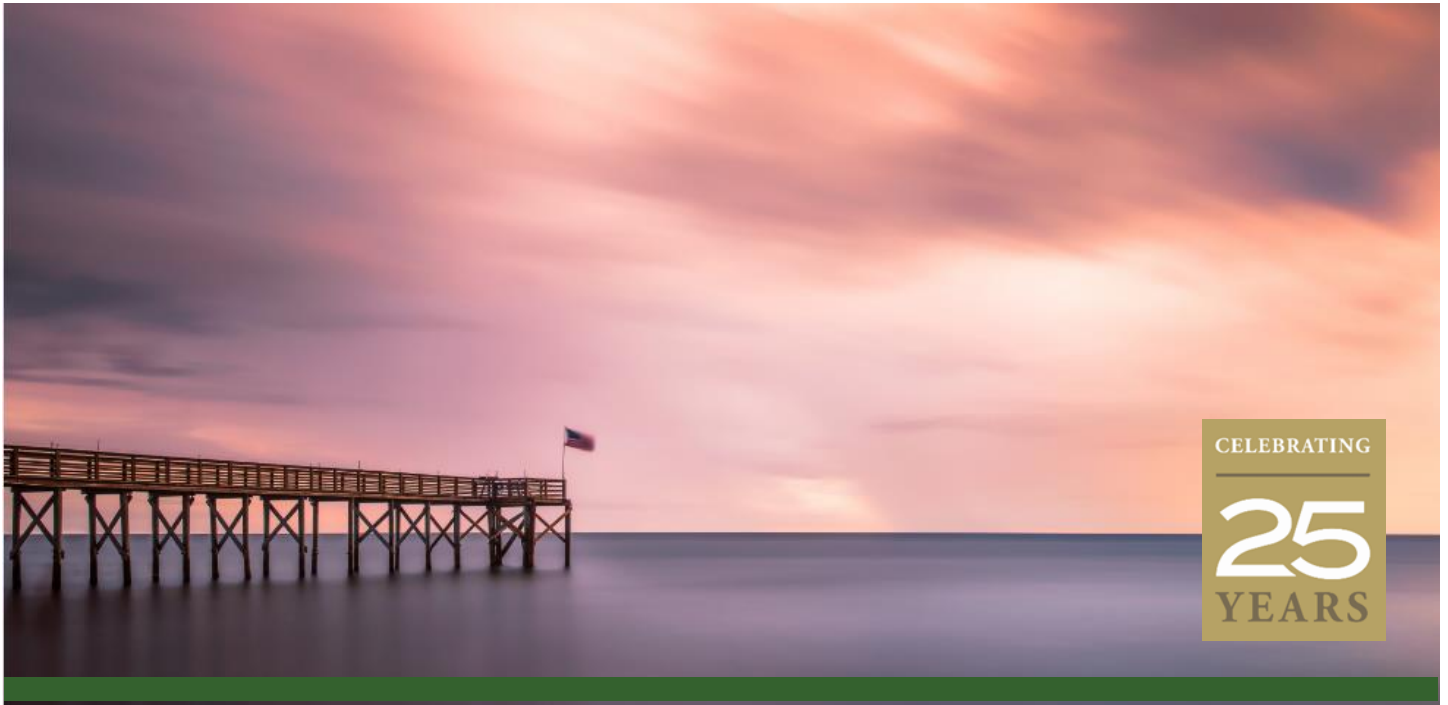

Investing Is Always a Risk; Invest Anyway

"The four most dangerous words in investing are, 'It's different this time.'"

- Sir John Templeton

The stock market is full of risks right now. A global recession could be just around the corner. Higher interest rates have led to increased borrowing costs for both individuals and corporations. US stocks, especially technology stocks, are trading at high valuations. Higher oil prices and low unemployment could lead to higher levels of inflation. And hovering above all of these economic risks is the constant threat that an unfavorable turn in domestic or foreign politics could increase tariffs, shock currency markets, threaten the solvency of foreign government bonds, throw corporations into an atmosphere of regulatory uncertainty, or lead to the disintegration of one or more multinational economic agreements. With all of these negative risk factors clearly in view, it seems wise to stay away from the stock market until the coast is clear and the risks have receded. The only problem with this strategy is that when it comes to the stock market, the coast is never clear and the risks never disappear; they are *always* present.

How markets work

Investing in stocks always has been, and always will be, a riskier venture than investing in bonds, keeping your money in an insured bank account, or burying cash in the back yard. This elevated risk is precisely the reason why stocks offer higher expected returns than bonds or cash - the return is compensation for accepting the always-present risk that a particular company could fall on difficult times or the stock market in general could experience a prolonged decline.

However, being aware of the particular risks that the market is currently facing does not give you the ability to predict how stocks will perform in the future. The primary function of the stock market is to allow investors to account for all of the risks that corporations are currently facing and to determine an appropriate price for each individual stock *with those risks in mind*. The investors who determine market prices are aware of all of the risks that you are concerned about, and many more risks that you never even considered, and they account for these risks when they determine fair market prices. So, those risks that concern you are already reflected in market prices and for that reason they do not justify avoiding the market.

Maybe it's different this time

Although you might accept that the markets are aware of the relevant risks, you still may be asking yourself:

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"What if it's different this time?" This is a very natural and understandable question, but the simple answer is that the market has been working in this way for hundreds of years, and despite your own personal reservations, it's not different this time.

On any given day, throughout the entire history of the stock markets, it has been possible to identify dozens of risks and to cite these risks as reasons not to invest. Yet, over numerous political and economic cycles the market has continued to climb higher. Recession, interest rates, market valuations, inflation, and geopolitical events are all very real risks, and investors in stocks are never shielded from these risks; they are a fact of life. But capitalism has always overcome these risks in creative and unique ways, and there is no reason to believe that the next time will be any different. Capitalism works, and it has always found a way to increase wealth in the end.

Excuses are not reasons

All of these "reasons" to avoid investing in stocks are actually not reasons at all; they are excuses driven by fear. And, while fear is quite natural, it tends to be detrimental to successful long-term investing.

Warren Buffett states the case well: "In the 20th century, the United States endured two world wars and other traumatic and expensive military conflicts; the Depression; a dozen or so recessions and financial panics; oil shocks; a flu epidemic; and the resignation of a disgraced president. Yet the Dow rose from 66 to 11,497."

We agree with Mr. Buffett; there will never be an easy and risk-free time to invest. On any given day there are many risks that could cause the market to decline, and you must accept these risks if you wish to profit from the higher expected returns offered by equities. And, if you wait for the risks to disappear before you invest, you will invariably notice that the market rises before those risks are gone, and they are quickly replaced by new risks and concerns.

Your best strategy is to make a long-term decision regarding how much of your portfolio you are willing to invest in higher-risk equities versus lower-risk bonds. Then, embrace the risks of the equity portion, knowing that these risks are the very reason that equities reward you with higher expected returns.

The risk will always be there, but history has demonstrated that the additional returns compensate investors well. You can still come up with your own list of reasons not to invest in equities, as long as you understand that you should invest anyway.

Heritage Investment Group provides wealth management and investment guidance to high-net-worth individuals, families, charitable foundations and qualified plans. We provide seasoned financial guidance, with respect and integrity, backed by a disciplined investment process. Since 1993 we've built our firm on a strong foundation of family and friendships with guiding principles of ethics and integrity.

The original version of this article was written by Heritage for the Sep/Oct 2018 edition of The Light, a local magazine serving Broward County, Florida.

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