



Investment Lessons From 2021

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Lesson 1:

Valuations Cannot Be Used to Time Markets

We entered 2021 with Shiller CAPE 10 at 34 vs. historical average of 17

We had been above 34 just once, in the late 1990s, which was followed by a bear market, leading many to predict a bear market in 2021

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Valuations Cannot Be Used to Time Markets

- When the CAPE 10 was above 25.1, real return over next 10 years averaged 0.5% about the same as the long-term real return on 1-month Treasury bills and 6.3% below long-term real return
- There was still a wide dispersion of outcomes
 - Best 10-year forward real return 6.3%, just 0.5% below historical average
 - Worst was -6.1%
- While high (low) valuations predict lower (higher) mean returns, there are still wide dispersions of outcomes, making timing a loser's game
- High valuations don't always predict negative equity premium, just lower equity premium

Source: Cliff Asness, "An Old Friend: The Stock Market's Shiller P/E," November 2012. <https://www.aqr.com/Insights/Research/White-Papers/An-Old-Friend-The-Stock-Markets-Shiller-PE>

Lesson 2: Active Management Is a Loser's Game

Vanguard's 500 Index Fund returned 28.8%, outperforming 76% of active funds

There was massive dispersion in returns, providing opportunities to outperform

10 stocks within the S&P 500 Index were up at least 118%

Lesson 2:

Active Management Is a Loser's Game

10 Best-Returning S&P 500 Companies in 2021

Ticker	Company	Return (%)
DVN	Devon Energy Corp.	196.1
MRO	Marathon Oil Corp.	149.7
MRNA	Moderna Inc.	143.1
FTNT	Fortinet Inc.	142.0
SBNY	Signature Bank	141.5
F	Ford Motor Co.	137.5
BBWI	Bath & Body Works Inc.	133.7
FANG	Diamondback Energy Inc.	127.4
NVDA	Nvidia	125.5
NUE	Nucor Corp.	118.4

For illustrative purposes only and should not be construed a recommendation of the above securities. Performance is historical and past performance is not an indication of future results.

Source: <https://www.marketwatch.com/story/these-are-the-best-performing-s-p-500-and-nasdaq-100-stocks-of-2021-11640874815>

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10 Worst-Returning S&P 500 Companies in 2021

Ticker	Company	Return (%)
PENN	Penn National Gaming Inc.	-40.6
LVS	Las Vegas Sands Corp.	-36.7
GPN	Global Payments Inc.	-36.7
VTRS	Viatis Inc.	-27.6
MKTX	MarketAxess Holdings Inc.	-27.6
ATVI	Activision Blizzard Inc.	-27.3
CTXS	Citrix Systems Inc.	-26.4
WYNN	Wynn Resorts Ltd.	-23.6
IPGP	IPG Photonics Corp.	-23.0
FIS	Fidelity National Information Services Inc.	-22.2

Lesson 3:

Don't Make the Mistake of Recency; Last Year's Winners Are Just as Likely to Be This Year's Dogs

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Index	2020 Rank/ Return (%)	2021 Rank/ Return (%)
Domestic Indexes		
S&P 500 Index	2/18.4	2/28.7
MSCI US Small Cap 1750 (gross dividends)	1/19.2	6/21.1
MSCI US Prime Market Value (gross dividends)	8/1.0	5/26.9
CRSP US Small Cap Value (gross dividends)	6/5.8	3/28.2
Dow Jones Select REIT	11/-11.2	1/45.9
Bloomberg Total Return Commodity Index	10/-3.1	4/27.1
International Indexes		
MSCI EAFE (net dividends)	5/7.8	9/11.3
MSCI EAFE Small Cap (net dividends)	4/12.3	10/10.1
MSCI EAFE Small Value (net dividends)	7/2.1	8/11.6
MSCI EAFE Value (net dividends)	9/-3.1	7/11.8
MSCI Emerging Markets (net dividends)	3/18.3	11/-2.5

Lesson 4:

Gold Isn't An Inflation Hedge Over Your Investment Horizon

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- Gold ended 2020 at \$1,894
- Inflation rose 7%
- Gold fell 3.6% to \$1,825

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The background of the slide features a misty, layered mountain range in shades of grey and blue, creating a sense of depth and atmosphere.

Lesson 5:

The Investment World Isn't Flat, and the Diversification of Risky Assets Is as Important as Ever

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	A	B	C	D	E
Year	S&P 500 (%)	MSCI EAFE (%)	MSCI Emerging Markets (%)	A-B (%)	A-C (%)
2000	-9.1	-14.2	-30.6	5.1	21.5
2001	-11.9	-21.4	-2.4	9.5	-9.5
2002	-22.1	-15.9	-6	-6.2	-16.1
2003	28.7	38.6	56.3	-9.9	-27.6
2004	10.9	20.2	26	-9.3	-15.1
2005	4.9	13.5	34.5	-8.6	-29.6
2006	15.8	26.3	32.6	-10.5	-16.8
2007	5.5	11.2	39.8	-5.7	-34.3
2008	-37	-43.4	-53.2	6.4	16.2
2009	26.5	31.8	79	-5.3	-53.5
2010	15.1	7.8	19.2	7.3	-4.2
2011	2.1	-12.1	-18.2	14	20.1
2012	16	17.3	18.6	-1.3	-2.6
2013	32.4	22.8	-2.3	9.6	34.7
2014	13.7	-4.9	-1.8	18.6	15.5
2015	1.4	-0.8	-14.6	2.2	16
2016	12	1	11.6	11	0.4
2017	21.8	25	37.3	-3.2	15.5
2018	-4.4	-16.1	-16.6	11.7	12.2
2019	31.5	22.4	15.8	9.1	15.7
2020	18.4	8.3	18.7	10.1	-0.3
2021	28.7	11.3	-2.5	17.4	31.2

Lesson 6:
**Hedge Funds Are
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	2021 Return (%)
HFRX Global Hedge Fund Index	3.7
Domestic Indexes	
S&P 500	28.7
MSCI US Small Cap 1750 (gross dividends)	21.1
MSCI US Prime Market Value (gross dividends)	26.9
CRSP US Small Cap Value (gross dividends)	28.2
Dow Jones Select REIT	45.9
International Indexes	
MSCI EAFE (net dividends)	11.3
MSCI EAFE Small Cap (net dividends)	10.1
MSCI EAFE Small Value (net dividends)	11.6
MSCI EAFE Value (net dividends)	11.8
MSCI Emerging Markets (net dividends)	-2.5
Fixed Income	
Five-Year Treasury Notes	-2.7
Long-Term Year Treasury Bonds	-5.4

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	Annualized Return 2002-2021 (%)
HFRX Global Hedge Fund Index	2.2
Domestic Indexes	
S&P 500	9.5
MSCI US Small Cap 1750 (gross dividends)	10.5
MSCI US Prime Market Value (gross dividends)	8.3
CRSP US Small Cap Value (gross dividends)	11
Dow Jones Select REIT	10.4
International Indexes	
MSCI EAFE (net dividends)	6.3
MSCI EAFE Small Cap (net dividends)	9.9
MSCI EAFE Small Value (net dividends)	10
MSCI EAFE Value (net dividends)	4.9
MSCI Emerging Markets (net dividends)	9.6
Fixed Income	
Five-Year Treasury Notes	3.9
Long-Term Year Treasury Bonds	7

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Lesson 7:

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- 1926-2021: Monthly correlation of S&P 500 Index to long-term (20-year) Treasuries was just 0.06
- Zero correlations means that there is no correlation of returns
- 5 years: Both S&P 500 and 20-year Treasuries produced negative returns
- 21 years: S&P 500 produced a positive return and 20-year Treasuries had negative returns
- 18 years: S&P 500 produced negative returns and 20-year Treasuries produced positive returns

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Source: Ken French's data library, http://mba.tuck.dartmouth.edu/pages/faculty/ken.french/data_library.html#Developed



Lesson 8: Don't Let Your Political Views Influence Your Investment Decisions

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2012 Study "Political Climate, Optimism, and Investment Decisions"

- Investors' optimism toward both the financial markets and the economy is dynamically influenced by their political affiliation and the existing political climate
- Individuals become more optimistic and perceive the markets to be less risky and more undervalued when their preferred party is in power—they take on more risk, overweighting riskier stocks and trade less frequently
- When the opposite party is in power, individuals' perceived uncertainty levels increase and investors exhibit stronger behavioral biases, leading to poor investment decisions

Source: <https://www.sciencedirect.com/science/article/abs/pii/S1386418117301155>

Lesson 9:

**Diversification Is Always Working;
Sometimes You Like the Results and
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Domestic Indexes	
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International Indexes	
MSCI EAFE (net dividends)	11.3
MSCI EAFE Small Cap (net dividends)	10.1
MSCI EAFE Small Value (net dividends)	11.6
MSCI EAFE Value (net dividends)	11.8
MSCI Emerging Markets (net dividends)	11/-2.5

Lesson 10: The Strategy to Sell in May and Go Away Is a Myth

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- 1926-2021: Source of the Myth
 - November-April: Equity premium 5.9%
 - May-October: Equity premium just 2.6%
- Premium more frequently negative May-October
- November 1926-October 2021
 - S&P 500 returns 10.5%
 - Sell in May and Go Away returns 8.5%
 - May-October 2021: S&P 500 returned 10.9% vs. 0% for 1-month Treasury bills; 10th straight year of underperformance

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Summary

- Even smart people make mistakes
- Differentiating themselves from fools, smart people don't repeat the same mistakes
- 2022 will surely offer us more lessons, many of which will be remedial courses
- The market will provide opportunities to make investment mistakes
- Avoid making errors by knowing your financial history, ignoring the noise of the market, and adhering to your well-thought-out plan

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