



# *Soundings*

## What's New - August 2020

Quote of the month:

*"It is good to have an end to journey toward; but it is the journey that matters, in the end." Ernest Hemingway*

That Hemingway kid sure had a way with words. I'm a little embarrassed to admit that I'm finally reading my first of his works, *The Old Man & the Sea*. Great read, and an easy one at just over 120 pages. In the quote above, whether "Papa" was referring to a particular adventure or using *journey* as a metaphor for life, how sad it is that in the end, he took his own.

If music was a metaphor for the stock market, last month it was *the Song Remains the Same*. The tech-heavy NASDAQ composite index, once again outperformed both its salty grandpa, the Dow Jones Industrial Average, and its stodgy uncle, the S&P 500. The U.S. economy contracted 9.5% through the second quarter, the worst single-quarter decline in GDP since the Commerce Department started tracking it in 1947. It was completely expected, we shut the country down. But it's important to recognize what that dip represents. It does not indicate the economy's current trajectory, just the most stringent period of pandemic lockdown. "GDP is a backward-looking number, and we expect to see a sharp rebound in the third quarter despite recent upticks in COVID-19 cases slowing economic momentum," says RJ Chief Investment Officer Larry Adam.

Many a forecaster has lamented that stock returns in the next decade aren't going to match what we've seen in the past. Are they right? Could be, but Sam Ro, Managing Editor of Yahoo Finance suggests otherwise. His piece, "Why the next decade of stock market returns could blow away expectations", is featured in this month's *Market & Economic Commentary*. It's a great read, contrarian pieces usually are, and I highly recommend you give it a look. First, the numbers...

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# Market Update - Year to Date Returns

<u>Major Indexes</u>	<u>(As of 08/01/20)*</u>
Dow Jones Industrials	-7.4%
S&P 500 Index	1.3%
NASDAQ	19.8%
DJ Global ex US	-8.5%
Russell 2000 (small cap index)	-11.3%
Barclays Capital Aggregate Index (Bonds)	6.4%
XAU (gold/silver)	44.5%

Source: The Wall Street Journal

## D.A.L.I. Signals - 08/01/2020

Fixed Income	Cash	Dom. Equities	Currency	Commod	Int'l Equities
<b>232</b>	<b>222</b>	<b>209</b>	<b>162</b>	<b>144</b>	<b>117</b>
21.4%	20.4%	19.2%	14.9%	13.3%	10.8%
(-6)	(-21)	(-2)	(-10)	(+27)	(+9)

Source: Nasdaq Dorsey Wright

- Inclusion of these indexes is for illustrative purposes only. Keep in mind that individuals cannot invest directly in any index, and index performance does not include transaction costs or other fees, which will affect investment performance. Individual investor's results will vary. The Dow Jones Industrial Average (DJIA), commonly known as the "Dow", is an index representing 30 stocks of companies maintained and reviewed by the editors of the Wall Street Journal. The S&P 500 is an unmanaged index of 500 widely held stocks that's generally considered representative of the US stock market. The NASDAQ Composite is an unmanaged index of securities traded on the NASDAQ market. The DJ Global ex US is an unmanaged group of non-U.S. securities designed to reflect the performance of the global equity securities that have readily available prices. The Russell 2000 index is an unmanaged index of small cap which generally involve greater risks. The Philadelphia Gold and Silver Index (XAU) is an index of sixteen precious metal mining companies that is traded on the Philadelphia Stock Exchange.
- The Barclays Capital Aggregate Index measures changes in the fixed rate debt issues rated investment grade or higher by Moody's Investors Service, Standard & Poor's, or Fitch Investors Service, in that order. The Aggregate Index is comprised of the Government/Corporate, the Mortgage-Backed Securities, and the Asset-Backed Securities indices.
- DALI is a proprietary matrix created by Dorsey Wright & Associates, an independent 3<sup>rd</sup> party. It presents the relative strength relationship of six broad asset classes or "teams", domestic equities, international equities, commodities, fixed income, cash, and currencies. Each are represented by an equal number of ETFs. Each team play against each member of the other teams, with net victories tallied in an effort to rank each asset class team by order of overall strength. Raymond James is not affiliated with and does not authorize or sponsor any of the listed websites or their respective sponsors. Raymond James is not responsible for the content of any website or the collection or use of information regarding any website's users and/or members.
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# Market & Economic Commentary

## Could the stock market deliver extraordinary returns over the next decade?

As we've written before, some of the more widely-followed stock market forecasters believe the average annual total return for stocks, which includes dividends, will be far below the 10% level investors might expect for the risk and time commitment. In a rigorous 40-page research note to clients last week, Goldman Sachs strategists led by David Kostin concluded as much after considering valuations, bond market forecasts, investor allocations, dividend growth expectations, and the outlook for the economy. "We estimate the S&P 500 will deliver an average annualized total return of 6% during the next 10 years," Kostin said. "We estimate 25% of the return will come from dividends and 75% from price gains."

However, it was the risks Kostin's team identified that really caught our attention. "One [risk] warrants mention in particular," Kostin wrote. "It is challenging, and arguably impossible, to forecast with accuracy the long-term return of an index when firms that may be added to the benchmark in the not-too-distant future may not yet have been founded."

Maybe it goes without saying, but the stock market doesn't represent a fixed set of corporations. It sees lots of turnover. The big market indexes, like the Dow Jones Industrial Average and Standard & Poor 500, regularly drop laggards and replace them with up-and-comers. It's something we've explored in this newsletter before. "The S&P 500 index changes over time," Kostin wrote. "Since 1980, more than 35% of S&P 500 constituents have turned over during the average 10-year period."

In fact, this is one of the reasons why Kostin's team was so off with their forecast for long-term returns when they last published them eight years ago. "In July 2012, we predicted US equities would generate an 8% annualized return during the coming 10 years, with a range of 4%-12%," he wrote. "S&P 500 actually returned 13.6% annually since we published our report eight years ago."

Among the companies that were to be added to the S&P was Facebook, which today boasts a market cap of \$690 billion and is the fifth largest stock in the index. "To put the index turnover in the context of long-term US equity returns, consider that since we published our original forecast eight years ago, 170 new constituents have entered the index while an identical number of stocks exited the benchmark," Kostin said. "The new companies now represent 17% of the S&P 500 index capitalization. Examples of current constituents that were not in the S&P 500 index in 2012: Facebook (FB, entered index in Dec-2013), Paypal, Jul-2015), Broadcom, May-2014, and ServiceNow, Nov-2019)."

Neither the S&P 500 nor the business models of the S&P 500 companies are fixed. They're all changing to adapt to and capitalize on the rapidly evolving business environment. In recent months, we've all learned how unpredictable that environment can be. We've also learned about how some companies were better at adapting than others. We've also seen stocks surge at a pace almost no one could've predicted. And so can we really be that sure that the next decade of returns will be lackluster? Certainly not.

**Sam Ro, Managing Editor, Yahoo Finance, "Why the next decade of stock market returns could blow away expectations", Morning Brief, July 20, 2020**

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## On a Personal Note

As you heard last month (thanks, Pops), I am a COVID-19 survivor. I was lucky and didn't have much for symptoms but I took all of the proper precautions to keep my cooties to myself. That translated to a two-week stay-cation on my couch. That might sound pretty good to some, but for me, it was far worse than my symptoms. I'm a doer and have a really hard time sitting still. So, the night before my "release date" from quarantine I decided I couldn't spend another second there. Six hours later I was on my way up to North Carolina with my great friend Chris and his loyal pup, Joe. Normally, I am such a planning freak that I won't hit the road without knowing what I'll be eating for lunch three days in the future. This time, in my haste to shove off, I decided to wing it. I picked a stretch of mountains right off of the Blue Ridge Parkway and headed North.

When Chris, Joe, and I arrived at our destination a few hours before dark, we faced the consequences of my lackluster planning. Literally from head to toe, I dropped the ball on gear. Boots, left on my front porch; pants, which would have been nice for the low 50-degree temps at night, ditto. You get the picture. As we hit the trail, we passed a sign that we interpreted to say: **WARNING: IF YOU DO NOT HAVE A BEAR CANISTER FOR YOUR FOOD YOU WILL BECOME BEAR FOOD.** Can you guess who didn't have a bear canister? Another victim of my hurried packing that morning. But onward we marched.

What's got me hooked on the mountains and hiking in general is not just the beautiful scenery. It's also the people you meet along the way. Chris, Joe, and I were wrapping up a 12-mile day and stumbled into a primitive campsite just off the trail. We were exhausted and decided to make this our home for the night. As we began unpacking, a couple happened upon the same campsite. We introduced ourselves and when we realized that there probably wasn't an axe-murderer among us, everyone opened up. Cam, a hemp farmer, decked out in dreadlocks and tie-dyed bandana, turned out to have the same obsession with music as Chris. Reared in Vermont, he was currently working as the head honcho on a farm in the heartlands of South Carolina. His girlfriend Meredith was a beach bum like us, from the South Carolina coast. She was a bartender and creator of her own line of clothing. Turned out that they were winging it even more than us and just jumped on the trail where they saw others leaving, so we told them where they should camp for the best views. On a whim we decided to join them, figuring that if they really wanted to kill us, they probably would have done so by now. After adding on another three miles to our day, we made it to Black Balsam Knob and set up camp with a beautiful unobstructed view of the mountains around us.

Not far from us was a bushy-bearded guy who looked like he could snap a tree in half with his pinkie toe. I felt kind of bad for pitching our tents near him, as he looked like he wanted to enjoy the night in solitude. But when Brian came over to chat after meeting Chris, I quickly realized he was going to fit nicely into our eclectic squad. A former Army helicopter pilot who now flew for the U. S. Forest Service, he was one of the nicest, most genuine, and caring people I'd ever met. The six of us watched the sunset, moonrise, and since it was July 4th, had the most impressive fireworks show in all of the tiny ant cities four thousand feet below us. Thankfully, I did not forget the bourbon. Priorities. As we sat around the fire and shared stories, I couldn't stop thinking about how we all ended up on that mountaintop, that night. We were the most rag-tag group of misfits: A hemp farmer, helicopter pilot, bartender, videographer, financial advisor, and good boy (Joe). We had just met but it felt like we were lifelong friends.

Driving home the next day, I kept thinking about our experience. Despite all of the crazy going on in the world today, the average, random person is very likely a pretty good soul. We live on a beautiful planet, in a wonderful country, with amazing people all around us. I hope you can find some time over the summer to get away from the evening news and see it for yourself.

Warmest regards, *Collin*

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