The Meridian Memo

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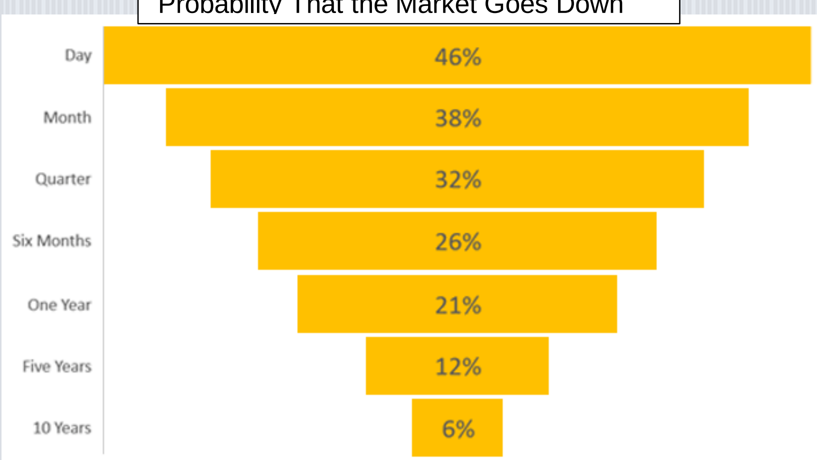
A Summer Letter to Clients: Staying Invested & Being Grateful

There are a number of reasons why a household would want to work with a financial advisor. **Usually it boils down to achieving goals and objectives.** Going deeper, there are always some underlying values behind those goals. As such, households want those goals and objectives achieved regardless of what happens in the market, economy, or world.

Because we want our clients to be successful, irrespective of external circumstances, we are writing this note to emphasize the importance of staying invested. One of the three primary risks that can derail any pre retiree or retiree from achieving their goals and objectives is behavioral risk. In fact, it may be the greatest risk. This certainly includes selling during a bear market because of fear or panic.

Seventy five percent of the time we are in a *bull market* (when the market goes up) and twenty five percent of the time we are in a *bear market* (when the market goes down). In order to

Probability That the Market Goes Down

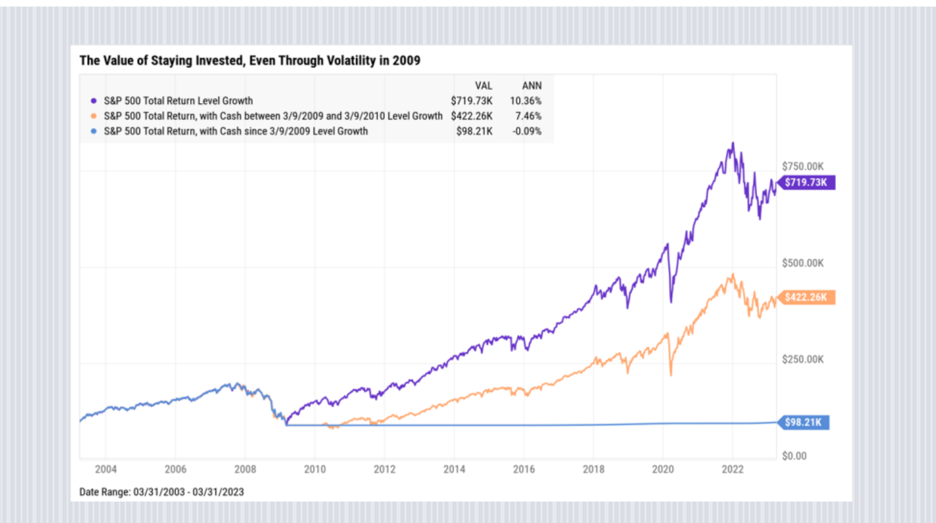


ABOUT US:

Retiree, Inc. (creators of IncomeSolver) has been an important part of Meridian's extended team for several years. Throughout the year we work directly with their lead analysts in order to deliver the best outcomes to our clients by maximizing our use of their best in class distribution planning software. The distribution plans provided by IncomeSolver can in some cases extend financial resources by 10 years in retirement. Because we know what is being delivered by the industry through other planning software, we can confidently say the rest of the industry does not even come close to the outcomes provided by Retiree, Inc.

In April of 2023 it was announced that T. Rowe Price, a global investment management firm and a leader in retirement, acquired Retiree, Inc. We look forward to the resources and investments in Retiree, Inc. that this acquisition will bring about and what it will mean in terms of delivering greater value to our clients.

realize those healthy long term returns that the market provides, one needs to maintain their market exposure throughout the bear market. No one knows the day or hour the market bottoms. **That means market timers will exit and re-enter the market at the wrong time.** There is no reason to lose money in a bear market. **The only way to lose money in a bear market is to cash out during the bear market**. The long term is made-up of a bunch of short terms (yes 25% can feel like a lot). It is necessary to be smart through those short terms in order to be successful in the long term.



The most important factor in total investor returns, even more than annual return percentage, is time in the market. The formula for compound interest is such that the number of time periods (usually counted as years) is the exponent. You don't have to understand the math, but the exponent is the most consequential variable in the equation when it comes to return percentage. A change in it moves the needle more than a similar change in any other single variable. [**P*(1+i)^n)**, where P is the principal, i is the annual interest rate, and n is the number of periods.]

Page 1 has a powerful chart that shows the odds of the market falling over different time frames. **On any given day, it is almost a coin flip whether the market is going to go up or down.** As you go further out and extend the time frames, the chances that the market goes down decreases exponentially.

We can show the same phenomena for other time frames, but the chart above compares the S&P 500 (one of the best measures of the US market) over a two decade period, against an investment strategy that tracks the S&P 500, except that it moved to cash at the bottom of the 2008 bear market and stayed there for one year before venturing back into the market. If one would have stayed invested all the way through the Global Financial Crisis (GFC) to the present he or she would have earned 10.36% annualized returns on their US equity portfolio over the last two decades. The strategy that moved to cash at the bottom of the crisis and stayed there for one year before moving back into the market returned 7.46% per year. Compounding that difference over two decades adds up. Also, if they sold at the bottom of the market during the '07-09 GFC, that means they locked in about a 54% loss from the pre financial crisis market highs.

In the absence of an awareness of market history, moving to cash and staying there until things stabilize *sounds* somewhat safe, even appealing. In actuality, that course of action is one that is more likely to put at risk realizing your goals and objectives, which makes it (counterintuitively) the more risky course of action.

There are a multitude of manifestations of behavioral biases, but one of the most powerful and harmful is **recency bias,** where an investor projects their most current experience into the future. They may think "the market returned 20% the last couple of years. I can depend on that trend continuing." That may lead an investor to take too much risk. Conversely, one may think “the market is down 30% from where it was 1.5 years ago. I better be safe and get out of the market.” Both strategies wrongly extrapolate the most recent past out into the future.

WHAT YOU MAY KNOW ABOUT SUCCESS AND HAPPINESS MAY BE ALL WRONG

This topic at first glance may seem a little off topic but we don't think it is. As a financial advisory firm, we focus on our clients’ finances but we do not do so as an end in itself, but as a means to an end. At the end of the day, it comes down to, how do given financial decisions impact one’s life. For a lot of people that we work with, it's about finding success, however our clients define it, in the next phase of their lives (which is often a post full time work phase).

The following quote by licensed clinical social worker Melanie Yost grabbed our attention.

“Most people look to the future for some milestone of success that will make them happy, whether that is a certain income level or lifestyle change. But as recent research confirms, it's learning to be happy in the present that actually brings about success, not the other way around.”

As a Christian, that does not surprise me. The Scripture is replete with the instruction to be thankful and to be so in all circumstances. We also see the great saints from beginning to end, giving thanks. The best operating manual for any machine is a product of the creator of that machine, and the same goes with human beings as it pertains to operating at the highest level. You certainly don't have to be a Christian to agree with Yost’s conclusion. The fact is empirical.

Shawn Achor, who studied happiness and optimism for 10 years at Harvard, found that happy, optimistic people are usually the most successful people. Sure it's anecdotal, but even from our own experience, the people we know that have risen to the top of companies have been happy and optimistic. I don't know a single negative pessimistic person that has been very successful at anything.

> **“You cannot be negative and grateful at the same time.”**

For a lot of us, we are goal oriented, and we are always moving forward and keeping our head down, perhaps thinking subconsciously that once we reach such and such a destination we will be happy. We may think, once I get my graduate degree; once I get the promotion; once I move to the new home by the coast; once I acquire X amount of dollars, then I will be happy.

Ms Yost gives the example of a childhood friend who had a lot of ups and downs in her life. That friend also had the mindset that “life will be better when.” Until she realized that this was her life not knowing what the future would hold and tired of waiting until some unknowable time to be happy, she decided to be happy now regardless of her current life state. Even without having realized all of her goals, or reached her definition of success, there were things in her life she could do and did do that could bring her happiness. Part of the process was learning to enjoy those things and not waiting for some future that may never arrive until she could be happy.

Perhaps the easiest way to be happy is to be grateful. One thing the research has shown is that you can't be negative and grateful at the same time. They are mutually exclusive sentiments. We would close with the admonition to think of things each day for which you can be grateful.

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