Steadyhand

Everyone is scared and prices are down — and for long-term investors, it's a beautiful thing

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By Tom Bradley

My grey hair and creaky knees should tip you off that I've been doing this awhile. I started as a stock analyst in 1983, which coincided with the beginning of a major bull market. Indeed, my whole career has had a tail wind behind it in the form of declining interest rates. As a result, bond and stock returns have been excellent.

Along the way, however, there were a few bumps in the road. As a cocky, young analyst, I sat on the edge of the trading desk and watched the market meltdown on Black Monday (1987). I was CEO of one of Canada's largest investment management firms when the tech bubble burst. And wouldn't you know it, we were just getting started with Steadyhand when the financial crisis hit.

Those were the doozies that I'll never forget, but there were lots of lesser declines along the way. This brings me to the market gyrations of the last ten days. This explosion of volatility doesn't belong on the list, at least not yet, but perhaps it's a good time to dust off some truths about bad markets.

1. Going through down markets is a necessary part of being an investor. It's not a matter of 'if' a bear market will occur, but 'when'.

2. Despite the inevitability, there's no certainty as to a bear's timing, depth, shape or character. Therefore, it's not to be avoided, at least not if you want to participate in the equally unpredictable up markets.

3. You won't know until after whether the initial declines (like last week's) turn out to be an imperceptible blip on a long-term chart (most are), or the beginning of a more fundamental adjustment. Today, many argue that a serious decline is not possible because of the strong global economy. Others point to historically high valuations, rising interest rates and excessive speculation as catalysts for a bigger selloff. Unfortunately, Mr. Market doesn't issue warnings or hand out a program.

4. Don't believe everything you read. In a highly charged market, the quality of information is generally poor. There's plenty of it, but it's more reaction than in-depth analysis.

5. There will be comparisons made to previous cycles. It's a favourite pastime of economists and commentators. From my experience, cycles are too different (economic backdrop, sector leadership, capital flows and valuation) for them to be of any use.

6. There's one thing that's the same with every bear market. It starts with bullish investor sentiment, what Warren Buffett refers to as greed, and ends with extreme bearishness (fear). Art Phillips and Bob Hager, two of the founders of Phillips, Hager & North, taught me to use investor sentiment as a contrarian indicator. For example, if my cab driver or golf buddy are recommending a stock, it's time to be careful. Investor sentiment is a gut check that makes sure you're not charging off the cliff with the herd.

7. Don't get too entrenched on one point of view. The late Peter Bernstein was my touchstone on this. He said, "In calmer moments, investors recognize their inability to know what the future holds. In moments of extreme panic or enthusiasm, however, they become remarkably bold in their predictions."

8. There's no time for gloating. Bear markets are a godsend for long-term investors. Everyone is scared and prices are down — it's a beautiful thing. But if you get too caught up celebrating a stock you shorted, or bragging about your timely selling, you'll miss the opportunity. Down markets have a way of changing

relative valuations between stocks, industries and geographies. You must be ready to shift gears.

9. Don't spend all your money in one place. I'm a big believer in taking baby steps. If prices move into an attractive range, get started, but keep some buying power in reserve. Prices could get even better.

The drama of last week may not amount to anything more than a blip, but it was a good wake up call. If you found it alarming and couldn't sleep on Monday night, then you have some work to do. There's no excuse for not being prepared for the next bear market.

Tom Bradley is the President of Steadyhand. A version of this article was published on February 10, 2018, in the National Post.