James Gauthier

Wed, May 24, 2023 2:48PM • 17:35

SUMMARY KEYWORDS
returns, stocks, investing, people, trend, investment, market, fees, myth, fund, gic, portfolio, guaranteed, bonds, alternative, passive, products, higher, fall, active

SPEAKERS
Pat Bolland, James Gauthier

Pat Bolland 00:00
Welcome back to the just word podcast. You know, a couple of decades ago, there was a great TV show called Mythbusters. Well, we're going to do kind of one of those things debunking some investment myths with James Gauthier, Chief Investment Officer at Justwealth Financial. And he joins us right after this word from our sponsor. James, great to see you again.

James Gauthier 00:32
You're too good to be here.

Pat Bolland 00:34
I guess you've become our official myth buster.

James Gauthier 00:38
Well, let's hope so.

Pat Bolland 00:41
All kinds of myths in the investment industry, and one that's particularly pertinent right now, because it is May, is the old sage 'Sell in May and Go Away' What do you think about that?

James Gauthier 00:53
Yeah, people love to have phrases that rhyme. That's a good line, I'll give it that. It's a great rhyme. And people have been saying it forever. And it really goes back to you know, people found out that market, corrections tend to happen, or at least the bad ones have tended to happen in the month of September in October. So people that you know, typically go on vacation in the summertime would say, Well, you can just sell things in May and go away, and then come back after the drops, and then buy stuff cheap in the fall or the winter, you know, whenever you get around to it. So there is kind of a rationale to why people would say something like that. And if you historically test returns, backwards, month over month, there is a slightly higher performance between the months of November and April, compared to May to October. But the performance returns from May to October are not negative. Over time, they're still

Transcribed by https://otter.ai

positive. In what the phrase suggests, Sell in May and go away is basically you should time the market. That's really what it's suggesting. And most people would know if they do any research or find credible studies. Everybody should know that market timing does not work. And it doesn't matter how many times you say it, or how many times you read it, people still do it. It's bad for them. But, you know, sometimes you just can't You can't fix every problem.

Pat Bolland 02:21
Well and the lows in the marketplace aren't necessarily guaranteed to be in the fall in the first place. And then getting the exact day right is almost impossible. You got to be in the market all the time to get all the ups, don't you?

James Gauthier 02:35
That's right. I mean, if you stay invested in the long term or time in the market, you will come up ahead as long as the markets continue to go up, which historically they always have. So yeah, suggesting to get out of the market for a short period of time is is not great advice. Whether it rhymes or not,

Pat Bolland 02:53
You know, okay, so the next myth is that 'Now is a good time to buy GICs'. And I'll admit, guaranteed investment certificate sitting at 5% is a pretty attractive return over the short term. What are your thoughts on that? It's not really a myth, but maybe a rumor.

James Gauthier 03:11
Yeah, it's topical. I mean, we see it we see people asking, you know, how are you going to be GIC returns? Well, here's the thing with GIC returns GICs tell you the return in advance of actually making your investment they tell you upfront, you're gonna make 4% for one year or three years or five years, whatever the term is. So it and it is guaranteed as long as you know, there's no bankruptcy and you have more than what's insured by the CDIC. It is a guaranteed return. But what they don't tell you about GICs is that your your liquidity is gone, the money you can't touch, or you're going to have to take a significant penalty in terms of the money that you make. It's taxed at your highest marginal tax rate if applicable. And then you run into reinvestment risk risk. What do you do when the term is up? If interest rates go down between now and the maturity of the GIC, you might get 4% Now, but you're stuck getting 1% in the future like it's been in the past several years. So there's all kinds of risks and inconveniences that that come with it. And the trap that people fall into is looking at historical returns from other investments say you know, a mutual fund or an exchange traded fund, they say this, this has made only 2% in the last five years but I can get a five year GIC going forward for 4%. That's that's an easy decision. But you're not comparing forward looking return with a forward looking return. You're comparing a forward looking return with a backward looking return. You can't change what's happened in the past. And there's no guarantee that a 4% return on a GIC is going to be any better than what that comparable product you're looking at might be that might be going to get you eight or 9% Because it's had it's coming off Pour period. So it's likely to have a good period going forward, because in the long run GICs will always be the lowest return. So it's never good advice to recommend investing in a GIC.

Pat Bolland 05:11

Transcribed by https://otter.ai

Yeah, and looking at those long term returns on the, you know, TSX composite or the s&p 500, you're looking at 7,8, 9 percent. I mean, it depends on the index you're looking at, but significantly higher than what you're getting in those GICs. Interesting.

James Gauthier 05:25
Bonds are higher, too.

Pat Bolland 05:26
Yeah, yeah. Good point. Here's one that I'd love your opinion on. 'The trend is your Friend', meaning the stocks are gonna go up, they're gonna continue to go up, and vice versa, I suppose if they're going down, they're gonna continue to go down. What do you think?

James Gauthier 05:43
Yeah, there's, there's gonna be two interpretations for that. So the trend is your friend. Yes, it's technically referring to technical analysis, which would says, you know, at the momentum, momentum is always going to work in your favor. And that's the way momentum traders or momentum investors work, they keep buying things, on the prospect that things will go higher, or the trend will continue. But inevitably, every trend will change course, it will go the other way. And it always comes without notice and without expectation. So for those people that get in late on the trend, they're just setting themselves up for a hard fall. So trend investing is no really better than any other type of investment strategy, it works for a while, and then it won't work. In the long run, it's probably going to generate the market return, and you're no better off because of it. And if it's forcing you to have turnover or get off your other strategies that that are more proven for long term investing, then it's probably not a wise idea. The other interpretation of a trend would be more like a fad, or by what's hot. So not necessarily one particular investment but a theme like cryptocurrency or cannabis stocks or technology stocks in the 90s. Jumping into these fads or trends, you know, right at the wrong time when a bubble is forming, is another way to set yourself up for a complete disaster. And it's quite topical, that you asked this question today, because for the first time, I saw advertised on CNBC this morning, a new ETF offered by some American company, investing in AI. So AI is the latest buzzword and its people are anybody who's funneled the tech sector would know that it's generated some pretty good returns so far this year. And now everybody's hopping on the products are going to start coming out, you got to get in an AI you got to buy the AI ETS, you got to specialize put everything into AI because that's the future. While all these wonderful promises will work until they don't, the bubble will burst. And eventually people are going to lose money. So never never never get caught up in these trends, because it will always result in disappointment,

Pat Bolland 07:55
Artificial intelligence leading to artificial results until the rug is pulled out from underneath you. Okay, yeah, not only are you a money manager, you're a portfolio manager. So how about some comments that, and myths, that are associated to portfolios? In particular, things like 'Lower Fees mean Higher Returns?

James Gauthier 08:18

Transcribed by https://otter.ai

Yeah, well, returns are, or at least they should be if they're done according to industry standards, returns are produced net of fees. So anything, anytime you see returns published in a newspaper, or the internet or any other media source, those returns should be stated after fees. So it stands to reason, if you have higher fees, that's going to be a bigger hit on the performance of the funds. And there's a lot of commercials and advertising and, and competitors of ours that are out there advertising saying, you know, trust our Loafie approach don't pay high fees, because it's not going to benefit. Well, the fact is, in our case, just well, it's worked. A low fee approach has resulted in industry leading returns, but others have not had the same results. Some of the other online competitors which have the same low fees, as we do charge a very low fee, invest in the same types of products that we do exchange traded funds, they have returns that are below the high fee products. So you really have to be careful it's not just about fees, low fees, do not guarantee higher returns, high fees will cost more but you might be getting you know a in an inferior product by investing with something with low fees so you have to be very very careful. You know what the the lower fees mean? Are you compromising on something else? So always be sure to look and compare and do your homework and don't just take some marketing verbiage for it.

Pat Bolland 09:55
Okay, here's one that might be closer to your heart near and dear 'The 60/40 Portfolio is Dead', in other words 60% in stocks to get your growth and 40% in bonds, is it dead then?

James Gauthier 10:09
No, no, it's alive and well. 60/40 I mean, that is the typical balanced portfolio, it's the most commonly selected portfolio, it's an average level of risk, it's which, you know, most pension funds tend to invest around, it's just very appropriate for a large proportion of investors. Some might be more aggressive, some might be more conservative. But every once in a while, people that offer products that are not part of the standard portfolio or alternatives, like to say the 6040 is no good, you need to get into alternatives, which are typically higher priced. And you know, they're they're making marketing pitches to try and sell their products. And most people who are traditionally invested in 60%, stocks and 40%, fixed income, don't really know about alternatives. So for them to try and get in and get a piece of their pie. They just say 60/40 is dead. And the timing of all of these comments are coming right after a year 2022, where both bonds and stocks were down. So this is the kind of the case where Tron they're trying to be opportunistic, and trying to strike while the fire is hot. You know, when when bonds and stocks both did poorly, that's the best time to introduce, well, you gotta invest in something different. And just so happens, we've got all these alternative alternative products, like real estate, or private credit, or private equity, there's all these asset classes where they're charging big, big fees, to try and get your assets and, and the returns that they produce. Because they are private, a lot of these alternatives it hedge funds fall into this category as well. They're not regulated the same way. As public equities, the pup the stocks and bonds, which are public securities, they're marked to market daily, so they have a very clear track record, they everything is traceable. And the accounting for everything is, is up to standards, private is not regulated the same way it's based on, you know, the case of real estate quarterly valuation, so the price has never changed. And it looks like a very stable investment. But if you compare a real estate, a building, in a private real estate fund, and a building in a public REITs, or a real estate investment trust, the price of the real estate investment trust building goes up and down all the time, because it's marked to market daily versus the valuation in a private fund. It doesn't change.

Transcribed by https://otter.ai

So it looks like a stable investment. But it's subject to the same pricing conditions, liquidity conditions, and everything else. So apples to apples, you know, you're not making the same comparisons, and to try and make some of these arguments that that they should be displacing traditional assets is completely false.

Pat Bolland 12:58
Okay, but to be fair, the 60/40 is not dead as you indicate. But it can be tweaked a little bit. In other words, depending on your age, you might have more in bonds or stocks, but we're talking about 50/50 or 70/30, or something like that, aren't we?

James Gauthier 13:13
Well, I mean, there's a natural progression of the risk that you take in your portfolio. So yeah, over time, your asset allocation should change when you're a bit younger, maybe you should be 80/20, a little more aggressive, more stocks in the portfolio as you get older. And you can't really take the risk, because you're dependent on the income, you might shift the more fixed income to the 40/60. But I think the 60/40, all the companies that are saying 60/40 is dead, or alternative asset providers, they're the only ones saying this, it's not anybody else. And it's like I said, they're kicking the horse when it's down, because you're coming off the year 2022, where both stocks and bonds are down. So they're trying to be opportunistic, if you look at longer term returns, so even with the bad year 2022, both stocks and bonds down portfolios, the 60/40 was probably down about 10%. In 2022, if you look at five year returns, they're still six and a half 7%, depending on the provider. So, you know, that's exactly what you would expect long term. So don't get hung up by the need to get into alternative products that are expensive and not necessary.

Pat Bolland 14:25
Okay, I saved the last and the best 'Active versus Passive Investing' And let's define those first act of being an active manager that changes on a day to day basis or not, and passive meaning an index, the Standard and Poor's 500 or the TSX composite. Is that a fair definition?

James Gauthier 14:48
Yep, that's that's pretty accurate. What what I would say is, I mean, passive attempts to replicate a market return. So the S&P 500 If it goes up 10% Your passive return is going to be 10% If you're an active investor, however, you're attempting to beat the market, so you're going to be different than the market, you're going to make a bet on something. It could be a sector, it could be a stock, it could be an investment philosophy. It could be a trading strategy, it could be any combination of those. But the idea is active is different than the market. And the attempt is to try and beat it. So I'm not sure what the myth is here. But

Pat Bolland 15:29
Well, you know, the active managers would say that they beat passive on a consistent basis. And I don't know how that's possible, given that the fees to have an active manager might be higher than just an index replicator.

James Gauthier 15:46

Yeah, so I mean, if you watch any commercial, from an investment provider, they'll say, you know, our research process or our proprietary way of valuing stocks adds value. So it's a lot of, you know, word smithing and a lot of promise and, like, they can't say anything illegal, or make guarantees, but they can say all kinds of things that make you think that they're going to add value to the market return, the empirical evidence, consistently over time, has 100% proven that it is not true. So there's, there's an organization called the evidence based investor, it's run by a guy named Robin Powell out of the UK. And, and so Evidence Based Investing is very much what we believe in. And he came out, I want to say about a year ago and said, the debate is over. I am not going to talk about this anymore, because there is no evidence whatsoever that active management adds any value. Every single credible study will show that passive management delivers better returns in the long run. But every commercial you see, says the exact opposite. So I don't think it's ever going to change the market is never going to change. I mean, obviously, you know, an active manager is not going to come out and say sorry, we can't beat the index require funds anyways. No, they're not going to happen. But, you know, as long as they're not saying anything illegal, regular regulators will allow it to happen.

Pat Bolland 17:19
But there's another myth that you just busted James, thank you.

James Gauthier 17:23
My pleasure, love doing it.

Pat Bolland 17:26
James Gauthier, Chief Investment Officer at Justwealth Financial

Transcribed by https://otter.ai