Ignore the Dramatic Media Predictions

On March 4th, Jim Rogers, who gained fame working with legendary investor George Soros but gained more fame by appearing frequently on television, told Bloomberg, "there is a 100 percent probability that the U.S. economy will be in a downturn this year." [1]

Then in May, despite being famously wrong since 2010 according to *Fortune* magazine, Société Générale analyst Albert Edwards was featured in -- yes *Fortune*, where he predicted a 75% stock market drop in 2016. [2]

As with all media, the financial media must entertain to hold its audience and so features dramatic prognosticators. A prediction that stocks and bonds will have typical, average years does not make for good television and does not make an analyst famous. But typical and average is a good summary of what happened to total returns in 2016.

While 2016 opened with concerns over oil prices, China's economic slowdown and a dramatic U.S. election, the economy was not so bad. The U.S. recovery was on firm footing, stock valuations were reasonable, inflation was contained, unemployment was near a 50-year low, and there was little chance of recession (by the metrics we watch).[3] Despite solid economic fundamentals, media stories were dire.

Acting on the recommendations of the financial media in 2016 could have been deadly to portfolios. Stories predicted high-yield bond defaults and banking collapses triggered by the energy sector. Those following the crowd and exiting the energy sector and high-yield bonds were crushed. Energy led U.S. industry stock sectors in 2016 with a 23.7% return.[4] High-yield bonds led all U.S. fixed income categories with at 17.1% return.[4]

Meanwhile, in January the media touted the superhot biotech sector. Biotech stocks returned 34% in 2014 and 11% in 2015, a year with few gainers.[4] Given that, one could have been tempted by the January Zacks Equity Research article, "5 Biotech Stocks Ready to Crush the Market in 2016." [5] The best of those five stocks lost 3%, the worst lost 57%. CNBC's biotech stocks listed in the January article, "These Are the Biotech Stocks to Own in 2016" did no better.[6]

> *"The less you indulge in financial media…,the more successful an investor you are likely to be."*
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> \- Larry Swedroe, Director of Research, Buckingham Strategic Wealth [7]

We cannot always calculate the damage caused by fame-seeking analysts like Rogers and Edwards and their media enablers, but sometimes the evidence is apparent. Oppenheimer analyst Meredith Whitney gained fame in 2007 by correctly making a negative call on Citigroup. Despite being ranked 1,205th out of 1,919 analysts in 2007, Whitney appeared dozens of times on television from 2009 – 2011. CNBC described her as "a Rock Star with cover-girl looks." [8] While her predictions of subsequent banking collapses repeatedly proved wrong, her appearances only increased.

In December, 2010 television show *60 Minutes* featured Meredith Whitney predicting "50 to 100 municipal bond defaults" resulting in "hundreds of billions" in losses.[8] *60 Minutes* has among the oldest audiences in television, and retirees are among the largest amateur holders of municipal bonds.[9] Following the broadcast, huge losses were dealt to retirees and the elderly as they rushed to sell their bonds at unnecessarily low prices.

And who is on the other side of these trades? Often, it is large, sophisticated banks and traders who do not base their decisions on television show commentary. They profit from it, happily buying low from amateurs selling on fearful news.

We have long suspected that the media drives some level of wealth away from amateur investors. Now, John Morgan, an economics professor at the U.C. Berkeley Haas School of Business, is studying this phenomenon, dubbed the "CNBC Effect." He demonstrates how programs like CNBC's *Mad Money with Jim Cramer* do more harm than good. His research concludes that investors would be better off ignoring the media. Those using public information for investment decisions can expect a payoff 12% lower than those using no media information.[10]

This a difficult topic because we are encouraged to stay informed about the economy and our investments. But investors should understand the biases and rationale behind media stories. Independent research firm DALBAR shows that, due to poor behavior, investors on average lose nearly half the returns they could achieve with a simple index fund.[11] They sell investments low when fear is prevalent and buy back at higher prices.

The urge to act on advice we see on television or read in the news is compelling. But sticking to a well-diversified portfolio and well-designed financial plan while ignoring the media drama will help investors achieve higher returns and reach financial goals.

> *"Simply put, don't read, listen to, or otherwise ingest most financial media related to market predictions."*
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> - Warren Buffett, Berkshire Hathaway annual report paraphrased by Motley Fool, March, 2014

Notes and Acknowledgements:

1. Bloomberg, March 4, 2016
2. "Here Comes the Biggest Stock Market Crash in a Generation," Fortune, February 2, 2016
3. Sharper Granite Research, S&P 500 Index total return, December 30, 2016; Sharper Granite, *Spring 2016 Letter on the Economy*, p. 6
4. Total return index data as of December 30, 2016: MSCI ACWI, S&P 500 Index, Barclays Aggregate U.S. Bond Index, Barclays High-yield U.S. Bond Index S&P Sector Indexes, MSCI Europe Index. November 9th data is S&P 500 Index total return.
5. "5 Biotech Stocks Ready to Crush the Market in 2016," Zacks Equity Research, January 11, 2016
6. "These are the biotech stocks to own next year: Pro," CNBC, January 3, 2016
7. "It's Okay to Ignore your Portfolio," Larry Swedroe, July 22, 2015
8. "Best and Worst Predictions of the Past 25 Years," CNBC, July 1, 2014
9. "100 Oldest and Youngest TV Shows," The Wrap, May, 2015
10. "Undermining Investor Decisions," *BerkeleyHaas*, 2016; "Experiments on the Social Value of Public Information," 2012, Professor John Morgan, U.C. Berkeley Haas School of Business
11. DALBAR's Quantitative Analysis of Investor Behavior 2015

All forms of securities investing involve risk of loss for which clients should be prepared. There are no guarantees or insurances of principal preservation and market fluctuations of any level may occur and impact portfolio value. Past performance is not a good predictor of future performance. [Spring 2017]