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Five ways to turn down the noise, stay focussed (and survive Trump)

Key points

- A surge in financial information and opinion along with our natural inclination to focus on bad news is arguably making us worse investors: more fearful and short-term focussed.
- Five ways to help manage the noise and stay focussed are: put worries in context; recognise that shares return more than cash in the long-term because they can lose money short-term; find a process to help filter noise; make a conscious effort not to check your investments so much; and look for opportunities that investor worries throw up.

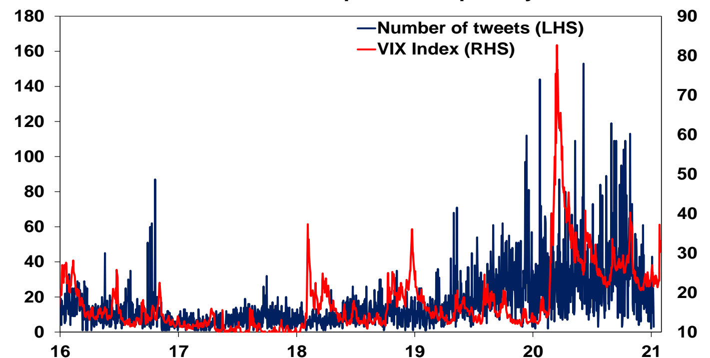
Introduction

One could be forgiven for thinking that the list of things for investors to worry about is more threatening than ever, and that it's getting harder to make sense off. This was an issue prior to coronavirus – with trade wars, President Trump's erratic leadership style and announcements, social polarisation, tensions with China, concerns the Eurozone would break apart, slow growth in Australia, and ever-present predictions of a new global financial collapse. Since the pandemic the worry list has arguably expanded with more macroeconomic and interest rate uncertainty with the surge in inflation and worries about recession, social polarisation giving rise to more populist and right-wing political leaders, geopolitical tensions morphing into serious wars (in Ukraine and Israel), threats to energy supplies, an intensification of tensions with China and ongoing predictions of another financial collapse. And now following the US election we are going to see the return of Donald Trump to the US Presidency, which arguably foreshadows a new list of "worries" as:

- His economic policies are now more extreme – his tariff plans are far bigger than under Trump 1.0; his tax cuts are proposed when the US budget deficit is twice as big as a share of GDP (6.5%) than it was in 2017 (3%); and his proposed deportation of millions of immigrants could push up costs in the US. All of which could threaten higher inflation, higher interest rates and then hit economic activity.
- Global geopolitical tensions are worse than eight years ago, and the US is even more polarised.
- He is likely to be less constrained this time around with less old-style Republican "adults in the room" and an inability to run for a third term.
- And we are likely to see a return to Trump's erratic style of policy making with a renewed focus on his social media posts, with all the noise that comes with that. Through 2020 Trump was averaging 33 tweets a day. That said there was no clear correlation between his tweet volume and the VIX expected stock market volatility index, apart from the common driver for both of the Covid pandemic in 2020.

The confusion around what Trump will mean has gone into hyperdrive lately with, for example, some warning that his policies could mean "less and later [RBA] rate cuts" and others saying they "could bring forward RBA rate cuts" and economists wheeling out models predicting all sort of hits to local GDP from his tariffs. And this from policies yet to be announced.

Number of Trump's Tweets per day



Source: Trump twitter archive, Bloomberg, AMP

To be sure these risks – even before Trump's return – are real and can't be ignored, but the risks around investing generally seem to receive ever higher prominence these days as the digital age enables the rapid dissemination of news and opinion. The danger is that all this noise is making us worse investors as we lurch from one worry to the next. The key to investor success is to manage the noise and stay focussed.

More bigger worries

While there's no denying there are things to worry about and the world is perhaps a messier place than it was pre-GFC, there is a psychological aspect to this that is combining with the increasing availability of information, and intensifying competition amongst different forms of media for clicks, which is magnifying perceptions of worries.

- Firstly, our brains are wired to make us natural receptors of bad news. We suffer from a behavioural trait that has become known as "loss aversion" in that a loss in financial wealth is felt more keenly than the beneficial impact of the same sized gain. The human brain evolved in the Pleistocene age when the key was to avoid being eaten by a sabre-toothed tiger or squashed by a woolly mammoth. This leaves us risk averse and more predisposed to bad news stories as opposed to good. Consequently, bad news and doom and gloom find a more ready market than good news or balanced commentary as it appeals to our instinct to look for risks. So "bad news and pessimism sells".
- Secondly, we are now exposed to more information than ever on how our investments are going and everything else. We can now check facts, analyse things and sound informed with a few clicks. But for the most part we have no way of weighing such information and no time to do so. So, it becomes noise. If we don't have a process to filter it and focus on what matters, we can suffer from information overload. This can be bad for us as when faced with more (and often bad) news we can make the wrong decisions with our investments. In particular, our natural "loss aversion" can combine with what is called the "recency bias" – that sees people give more weight to recent events in assessing the future. A 1997 study by US behavioural economist Richard Thaler and others showed that providing investors in an experiment "with frequent feedback about their [investment] outcome is likely to

encourage their worst tendencies...More is not always better. The subjects with the most data did the worst in terms of money earned."

- Thirdly, there is an explosion in media all competing for our attention. We are now bombarded with economic and financial news and opinions with 24/7 coverage, subscription services, finance updates, dedicated TV and online channels, blogs, chat rooms, comments, podcasts, videos, etc. And following from loss aversion, in competing for your attention bad news and gloom naturally trumps good news and balance. So, it seems that the bad news is worse and the worries more worrying than ever. Google the words "the coming financial crisis" and you are inundated with warnings like "what's coming is worse than a recession", "the coming recession may have already arrived", "recession 2024: what to watch and how to prepare", and "a financial storm is coming that governments cannot fight".

In the pre-social media/pre-internet days it was much harder for ordinary investors to be exposed to such disaster stories on a regular basis. The danger is that the combination of a massive ramp up in information and opinion, combined with our natural inclination to zoom in on negative news, is making us worse investors: more distracted, fearful, jittery and short-term focussed, and less reflective and long-term focussed.

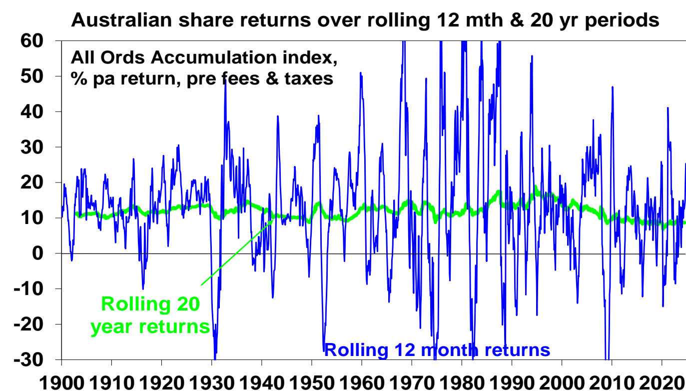
Five ways to stay focussed

To be a successful investor you need to make the most of the power of compound interest and to do that you need to invest for the long-term in assets that grow with the economy and not get blown around by each new worry and fad. But to do this you need to turn down the noise on the worry list and the explosion in investment information and opinion. But this is getting harder. At an obvious level, it makes sense to turn off all notifications on your phone or iPad, but more fundamentally, here are five suggestions as to how to turn down the noise and stay focussed:

Firstly, put the latest worry in context. There's always been an endless stream of worries. Here's a partial list since 1900: 1906 San Francisco earthquake; 1907 US financial panic; WWI; 1918 Spanish flu pandemic (up to 50 million killed); The Great Depression; WW2; Korean War; 1957 flu pandemic; 1960 credit crunch; Cuban missile crisis; Vietnam War; 1968 flu pandemic; 1973 OPEC oil embargo; Watergate; the cancellation of The Brady Bunch; stagflation in the 1970s; the 1979 oil crisis; Latin American debt crisis; Chernobyl disaster; 1987 crash; First Gulf War; Japanese bubble economy collapse; US Savings and Loan crisis; Asian crisis; Tech wreck; 9/11 terrorist attacks; Second Gulf War; the GFC; the Eurozone debt crisis; US trade wars; Trump 1.0; the coronavirus pandemic; inflation; and war in Ukraine and around Israel. But despite this, investment returns have actually been good as shares climb a long-term wall of worry. Since 1900 Australian shares have returned 11.7% pa and US shares 10% pa (including capital growth and dividends). And in relation to Trump we survived his first time around and he still wants shares to go up, not down!

Source: ASX, AMP

Secondly, recognise how markets work. A diverse portfolio of shares returns more than bonds and cash long-term because it can lose money short-term. As seen below, while the share market can be highly volatile in the short-term it has strong returns over all rolling 20-year periods.



Source: ASX, AMP

And invariably the short-term volatility is driven by investors projecting recent events around profits, dividends, rents and interest rates into the future, and so, causing shares to diverge from long-term value. So, share market volatility driven by worries, bad news, and bouts of euphoria is normal. It's the price investors pay for higher longer-term returns.

Thirdly, find a way to filter news so that it doesn't distort your investment decisions. There are lots of ways to do this depending on how much you want to be involved in your investments. If you want to be heavily involved it could mean building your own investment process or choosing 1-3 good investment subscription services and relying on them. Or simply agreeing to a long-term strategy with a financial planner and sticking to it.

Fourthly, don't check your investments so much. The daily movements in US or Australian shares are down almost as much as they are up. So, each day is pretty much a coin toss as to whether you will get good news or bad as markets are thrown around by the daily noise. By contrast, if you only look at how the share market has gone each month and allow for dividends, historical experience tells us you will get bad news less than 35% of the time. Looking only on a calendar year basis, data back to 1900 indicates that the probability of bad news in the form of a loss slides further to just 20% of the time for Australian shares and less than 30% for US shares. And if you can stretch it out to once a decade, positive returns have been seen 100% of the time for Australian shares and 83% of the time for US shares. The less frequently you look the less you will be disappointed, and so, the lower the chance that a bout of "loss aversion" will be triggered which leads you to sell at the wrong time. So, try to avoid looking at market updates so regularly and even consider removing related apps from your devices.

Finally, look for opportunities that bad news and investor worries throw up. Periods of share market turbulence after bad news throw up opportunities for investors as such periods push shares into cheap territory from which strong gains have historically been seen.

Concluding comment

There is no denying that things occasionally go wrong weighing on investment returns. But predictions of imminent disaster are a dime a dozen. My long-term experience around investing tells me it's far more productive to push against prognostications of financial gloom because most of the time they are wrong and end up just distracting investors from their goals. The same logic cautions against getting too gloomy about the return of President Trump (whether you like him or not!).

Dr Shane Oliver
Head of Investment Strategy and Chief Economist, AMP

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