The Market Has Been Feasting, and Like You, It Needs Time to Digest!

Every year, as I approach the Thanksgiving table, I am flooded with happiness and wonderful memories. I have always loved and celebrated this holiday, no matter where in the world I have been. During my time living in Italy, France, and Spain, I would carefully prepare a Thanksgiving meal for my professional water polo team and staff. I cooked turkey, stuffing, mashed potatoes, pies, and all the rest, for a little over twenty people each year. It was no simple task! Acquiring a turkey or two of adequate size in Western Europe was quite an undertaking.

I will never forget the look that my local butcher in Italy gave me when I asked in the most humble form of conversational Italian for two 22-pound turkeys.

He gasped - his face and jaw hung open.

The butcher, who was short and sturdy, began to wave his arms and laugh. He told me he had never seen or heard of a turkey that size and needed a few hours to call around to some of the farmers he knew in the area outside of my town of Recco. He made sure to tell me that he would also ask if any of the farmers had seen Big Foot or the Loch Ness Monster as well! We both laughed, as we did almost every time I visited his shop.

When I returned, the entirety of the shop’s staff was there to tell me the good news. In a town about 60 miles away there was one farmer that had 2 turkeys that where each around 18 pounds. I raised my arms in victory and asked when they could arrive. “Tomorrow,” he replied. The Thanksgiving feast was on! He had one final question, “Do you want the feathers on?”

When I had collected the featherless turkey and the other ingredients, I began crafting the meal together, usually by myself. I closely followed all of the recipes from my childhood trying my best to make sure that I shared my American tradition in the most authentic way possible. After what seemed to be 9 straight hours of cooking, the meal was ready!

I gathered my teammates around the table covered in Thanksgiving delicacies. They all chose a chair and eagerly served themselves, curious to try the meal I had been talking about for most of the month leading up to that day. I sat and watched their reactions as they tried many of these dishes for the first time. It brought me such joy to share this tradition with them. It made me feel like I was home.

As I think of feasting this week, I reflect on a fantastic analogy that Ken has used to illustrate the market consolidations that we have seen this year. These sideways, range-bound movements can be likened to the feeling that we all get after consuming massive amounts of our favorite fare while at the Thanksgiving table. The market has had a seat at the Thanksgiving table for a majority of the year. Feasting and digesting, feasting and digesting, feasting and digesting.

How much can the Market eat? How much is left to feed it?
Balancing Market Risk and Opportunity Risk

“What should I be doing right now?” That, or some version of it, is THE question we are getting asked at the moment, prompted, no doubt, by the approaching end to the year and the fact that the S&P 500 has basically gone nowhere over the last month while remaining near its all-time high. My typical response to these inquiries has been to ask some questions of my own, including:

- What are you looking to get out of the stock market?
- Are you more of a short-term trader or long-term investor?
- If we knew that the S&P 500 was only going to fall 5-7% before rallying back up to new highs, what portfolio changes, if any, would you want to make?
- Are you more concerned with protecting what you have or growing what you have?

These are the kinds of questions that every market participant should ask themselves BEFORE they ever commit a dollar to stocks. When making a decision to invest, start by reviewing your goals and strategy. How to approach a market like this one is very dependent on how much risk you are willing to take right now. The tradeoff between risk and reward is one of the most fundamental concepts of participating in the financial markets, yet it often goes overlooked or becomes lost among the day-to-day fluctuations. Without risk, there would be little to no reward, and generally the more risk taken, the more reward paid out if things turn out the way you want them to (of course, the opposite is also true if things don’t turn out the way you want them to). However, there is also a tradeoff between assuming market risk and the opportunity cost of not assuming such market risk. What exactly does that mean? To illustrate, picture a seesaw. On one side we have market risk or the potential losses if the market were to go down. On the other side, we have the opportunity risk or the potential gains given up if the market were to go up and you don’t have sufficient exposure to it. This relationship is probably THE key to investing in the stock market, and each individual must find a way to balance the market risk and opportunity risk in a way that fits with his or her goals. For some, that may mean getting more defensive right now because, after almost two years of a straight-up stock market, they are more concerned with capital preservation than growing the pot even more. For others, missing out on additional upside is the bigger risk and they will, therefore, need to remain exposed to stocks as much as they can stomach. The right balance between those two risks is one answer we just cannot give. However, to help answer the original question of “what you should be doing right now,” it is important to remember that we still firmly believe that this is a secular bull market and that stocks will go higher in the months and years to come. Yes, we still advise caution in the near term with breadth weakening and the averages remaining extended, but that still could mean that the best course of action for many accounts is to not do anything at all right now. If you want to get more defensive then that is perfectly alright, but you will have to do so knowing that if stocks surprise once more to the upside, you will likely underperform. The markets are fluid and subject to change, of course, but right now the questions to ask yourself as explained above are how we feel investors should approach things moving forward.

Finding the right tradeoff between market risk (exposure to losses) and opportunity risk (the market going up without you) might just be the primary fundamental consideration when it comes to investing. However, when the major averages are extended and there’s not a lot of “value” to be found, the decision becomes even more important because there’s likely less margin for error and the odds increase of having to sit through SOME period of market weakness. Investors who put more emphasis on growing their portfolios may feel opportunity risk is the bigger risk and may therefore remain nearly fully invested, while those more concerned with market risk and protecting what they have will probably want to get more defensive. There is no “right” mix between the two for everyone, but there is a definite tradeoff since limiting one type of risk generally means increasing the other.

So I ask you, how hungry are you? How full are you? Are you ready to sit back and digest? Are you preparing for a long cold winter? If we all knew the answers, we wouldn’t have to ask the questions! I welcome you to reach out to me so that I can help you to find the answers to these questions.

The South Group wishes you and your family a very happy Thanksgiving.

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