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The Palos Perspective

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By Charles Marleau CIM® and William Mitchell CIM®

The Cost of Missing Out

Timing the market is challenging, yet we continually see investors succumb to the usual parade of fearful news and ultimately waver from maintaining a long-term perspective. Without a doubt, incessant headlines about rising interest rates, geopolitical threats, inflation, government debt, climate change and concerns about the health of the economy can be worrying; last year was no exception. With rapidly rising interest rates, conflicts in Eastern Europe and the Middle east, rising government debt, rising inflation and uncertainty over a possible recession, undoubtedly there was cause for concern.

Many of the most seasoned market strategists and economists remained bearish on equities throughout 2023 (and into 2024!) while warning of dire consequences for the global economy. Warnings of economic Armageddon aren't unusual and in fact it is often the most outlandish prognostications that attract the most eyes, ears and clicks. Let's face it, fear sells. Unfortunately for some investors, relying on the predictions of "experts" can lead to poor decision making when it comes to investing. Specifically, we are referring to attempts to "time the market". Temporarily pausing or exiting investments in equities with the intention of "getting back in" when markets improve can be a costly endeavor. To have any chance of success, precise market timing for both selling and re-entry would have to be perfect.

Missing the best days in the market has proven to be a costly strategy. We refer to a study from BMO Global Asset Management that reminds of us this fact. The BMO study was based on the performance of the S&P/TSX Composite Total Return Index over a twenty-two-year period commencing on January 1, 2000, and ending on December 31, 2021. The study found that starting with an initial investment of $100,000 and remaining invested for the full period, returns totaled 344.3% and the initial investment of $100,000 became $444,255. If you missed out on the five best days over the twenty-two-year period, your initial investment would have returned 186.5% and become $286,489. Missing the best 10 days resulted in a return of 115.2% and a value of $215,244. Clearly, "timing" the stock market risks missing out not only on the best days in terms of returns, but it also hinders long-term wealth accumulation.

Staying invested in equities has distinct advantages. Investing in public companies offers investors the opportunity to participate in significant long-term growth in the companies they invest in. In addition, equities have historically acted as a hedge against inflation. Investors with suboptimal concentration in fixed income, usually at a cost of reduced allocation to equities, expose themselves to the risk of inflation, which erodes purchasing power. And, for investors who require a steady income flow, dividend paying stocks offer a substitute for interest income that often comes with tax advantages.

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Even for investors who are in or approaching retirement, divesting from equities comes with a risk of the deterioration of their nest egg as well as heightened concentration risk (i.e., less diversification). Historically, equities have shown a higher return profile than bonds and, for that reason, stocks remain a key component of any diversified portfolio. Staying invested through market fluctuations (i.e. no risk of missing out) also enhances the compounding of returns over time, an important factor in creating wealth. Liquidity, which is the ease with which investors can buy and sell shares, is a well-known advantage inherent with stocks. An important aspect of active portfolio management is the process of rebalancing portfolios when economic conditions, or upon a change to individual investment objectives, is required. The liquidity, accessibility, and low cost of transacting on stock markets permit efficiency and flexibility when rebalancing.

It's no secret that markets can be subject to short periods of volatility and price declines. Fear, along with greed, are powerful human emotions which can incite behaviors that are detrimental to successful wealth creation. The Palos portfolio management team has decades of experience in managing investment portfolios. We've been around long enough to know that nobody has a proverbial "crystal ball" and that predicting what will happen in the future is a fool's errand. What we fully comprehend is that committing to a long-term plan, maintaining a disciplined approach to managing risk, optimizing diversification, and continuously seeking new opportunities that result from temporary price dislocations are the most important tools for realizing investment success.

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Chart 1: Palos Domestic Funds versus Benchmarks (Total Returns) [1]	FundServ	NAVPS	YTD Returns
Palos Income Fund L.P.	PAL100	$8.25	0.38%
Palos Equity Income Fund - RRSP	PAL101	$6.76	0.36%
Palos WP Growth Fund - RRSP	PAL213	$8.81	-7.40%
Palos-Mitchell Alpha Fund [3]	PAL300	$10.31	0.97%
S&P TSX Composite (Total Return with dividends reinvested)			-0.12%
S&P 500 (Total Return with dividends reinvested)			1.53%
S&P TSX Venture (Total Return with dividends reinvested)			-0.10%
Chart 2: Market Data [1]			**Value**
US Government 10-Year			4.12%
Canadian Government 10-Year			3.49%
Crude Oil Spot			US $73.41
Gold Spot			US $2,029.30
US Gov't10-Year/Moody BAA Corp. Spread			162 bps
USD/CAD Exchange Rate Spot			US $0.7446

[1] *Period ending January 19th, 2023. Data extracted from Bloomberg*

[2] *Fund is priced annually*

[3] *Fund is priced weekly on Tuesdays*

Weekly Commentary

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Disclaimer:

PALOS

1 Place Ville Marie, Suite 1670
Montreal (QC) H3B 2B6, Canada

T. +1 (514) 397-0188
F. +1 (514) 397-0199

4711 Yonge Suite 504
Toronto, Ontario M4T 2V7

T. +1 (647) 276-0110
F. +1 (647) 343-7772

www.palos.ca