Six New Year’s resolutions for investors

Weekly Market Compass | January 4, 2023

Kristina Hooper
Chief Global Market Strategist

“

What drove stocks in 2022?

The Federal Reserve and other central banks tightened far more than expected because inflation was far worse than expected.

Looking ahead

I believe that, when all is said and done, 2023 will be a better year for investors than 2022.

2023 resolutions

I offer six New Year’s resolutions for investors to consider as we contemplate the year ahead.

To borrow a phrase from the late Queen Elizabeth, 2022 was truly an “annus horribilis” for both stocks and bonds. To put it simply, the Federal Reserve and other central banks tightened far more than expected because inflation was far worse than expected. In this week’s blog, I offer a brief post-mortem on 2022 and a few New Year’s resolutions for investors in 2023.

What drove stocks in 2022?

As you may recall, Federal Open Market Committee (FOMC) members didn’t expect to tighten nearly as much as they did in the past year. In December 2021, the FOMC’s “dot plot” showed a median expected fed funds rate of 90 basis points by the end of 2022.[1] In reality, the fed funds rate finished 2022 at 4.33%.[2] It was this very surprising and aggressive monetary policy tightening of 2022 that negatively impacted the pricing of both stocks and bonds in many major markets.

In addition, Chinese risk assets came under pressure from the double whammy of a major COVID wave in the spring of last year, which resulted in lockdowns and disruptions, as well as a resurgence of issues in the property sector.

And the past month turned out to be a December to remember, but that meant different things in different markets. US stocks posted significant losses, experiencing substantial price erosion, helped by a hawkish FOMC press conference on Dec. 14.[3] However, Chinese stocks posted significant gains during the month, as policymakers rolled back COVID-19 regulations, paving the way for a robust re-opening of the Chinese economy.[4]

2023 resolutions

I think now is an appropriate time to share some proposals for New Year’s resolutions for investors:

1. Don’t get spooked by tough times.
Arguably the biggest mistake made by investors during the Global Financial Crisis was to exit equities near the bottom, thereby locking in losses and missing out on participating in the strong stock market rebound that followed. We’re likely to have geopolitical, economic and market events that will strike fear in the hearts of investors in 2023. Remind yourselves that over time, no matter what the event, from the Great Depression to the Cuban Missile Crisis to the Gulf War, the stock market has had a way of shaking it off (of course some events took longer than others to shake off) and continuing to climb higher.

2. Expect the unexpected from the markets.
In looking at asset class and sector performance by calendar year over time, it’s clear that markets can shift quickly; today’s leaders can be tomorrow’s laggards, and vice versa. Ensure your portfolio is well-diversified — consider a range of assets across and within the

three major asset classes. In particular, ensure adequate exposure to areas that appear poised to perform better on a relative basis — in my view, this includes emerging markets.

3. Don’t wait for “perfect” entry points into the stock market.
I keep getting asked if the stock market has bottomed yet; investors are clearly looking for that perfect time to jump in. The reality is that we won’t know the perfect entry point until it’s in the rearview mirror. I believe we are likely to see significant volatility early in the year as we wait for greater clarity on when the Fed will hit the pause button. I also expect earnings to be downwardly revised in coming months, which should also spark volatility. Whether a retail or institutional investor, dollar cost averaging can be a prudent option, especially in this kind of market environment.

4. Look for income potential in bonds and beyond.
I expect modest gains — and significant volatility — for major asset classes in 2023. However, the positive byproduct of aggressive Fed tightening is that income is far more abundant than it was when we began 2022. Investors may benefit from ensuring adequate exposure to fixed income sub-asset classes such as investment grade credit, municipal bonds and higher quality high yield bonds that have relatively robust yields. And don’t forget the income potential of dividend-paying stocks and real estate investment trusts (REITs). In an environment of low or non-existent capital appreciation, income can make a significant difference in total return, and I believe the benefits of diversification also apply when it comes to sources of income.

5. Create an investment plan and stick with it.
I saw firsthand the value of an investment policy statement when I sat on the board of a small private endowment 20 years ago. The investment policy statement created structure and discipline. Key portfolio decisions such as asset allocation bands and the annual “draw” were decided upon in an emotionless vacuum. When the Global Financial Crisis occurred and some committee members got spooked, the investment policy statement guided the portfolio — think of it as creating “guardrails” — as markets moved and emotions ran wild.

6. Apply Stoic principles to investing.
My older son, a junior in college, has for some time been espousing the virtues of Stoicism, an ancient philosophy, for application by college students seeking a way to juggle their lives. It got me thinking … Stoicism also has practical applications for investing today. Stoics believed it was important to put life into two broad categories: that which you can completely control and that which you cannot control (either completely or partially). Stoics believed it was important to focus on the things you could completely control. In investing, that includes creating an investment plan, adhering to that plan, and ensuring adequate contributions — long-term portfolio performance and the achievement of investing goals will be a byproduct of these controllable actions combined with the uncontrollable path of markets.

Looking ahead
As we look ahead to 2023, I expect the investing environment to improve as the year progresses, and I believe that, when all is said and done, 2023 will be a better year for investors than 2022. (Of course, that’s not saying too much, given how abysmal 2022 was.) But I do believe the resolutions I shared above can be helpful no matter what kind of year we get. And so I will finish this blog by

simply wishing you all the best in the year ahead. My New Year's resolution is to continue trying to make this weekly blog live up to its title — Weekly Market Compass — as we navigate the year's economic and market developments together.

Notes

[1]Source: Federal Reserve as of Dec. 15, 2021

[2]Source: Federal Reserve Bank of New York as of Dec. 30, 2022

[3]Source: S&P Dow Jones. The S&P 500 Index price return was -19.44% for 2022 and -5.9% for December.

[4]Source: MSCI. The MSCI China Index price return was 5.16% for December.