Quarterly Insights

Exciting Stocks Are Not Always the Best Investments

By Daniel Campbell, CFA

As 2023 was the year of the Magnificent Seven[1] – a small group of tech stocks that captivated the media with their eye-popping returns – investors are questioning whether that performance will continue. They might also fear that they could be missing out by not allocating more of their portfolio to those high-performing stocks.

First, let's consider what sparked the strong performance. At the start of 2023, the term Magnificent Seven didn't exist, at least not related to stocks, but by the end of the year, the moniker was dominating headlines as the returns for this small group of companies began to soar.[2] Most of them benefited from the buzz created by OpenAI's ChatGPT model and stories about how artificial intelligence (AI) could reshape the way the world does business. Investors felt these stocks could be best poised for growth from the new technology.

But the Magnificent Seven also benefited from another tailwind: along with the broader stock market, they were recovering from sharp price declines in 2022. On average, the Magnificent Seven stocks fell 46% in 2022 compared to just an 18% decline for the S&P 500. NVIDIA at one point lost over 60% of its value; Meta lost over 70%. In fact, over half of the Magnificent Seven companies haven't even outperformed risk-free Treasury bills since January 2022.

Hypothetical Growth of $1,000 from Jan. 1, 2022 through Feb. 29, 2024

Name	Ending Value	Investment Low
NVIDIA (NVDA)	$2,694	$382
Meta (META)	$1,459	$264
Microsoft (MSFT)	$1,255	$641
S&P 500 (VOO)	$1,105	$759
T-Bills (BIL)	$1,073	$1,000
Amazon (AMZN)	$1,060	$491
Apple (AAPL)	$1,031	$708
Alphabet (GOOGL)	$956	$576
Tesla (TSLA)	$573	$307

Source: Morningstar. Performance is historical and does not guarantee future results.

This highlights a key challenge of investing in stocks: good companies don't necessarily make good investments. That's because every company is worth its value today (which we can measure) plus some story about how much money it will earn in the future. And every company is priced based on how believable people find that story. As stories change, or as people lose faith or gain conviction in the story, we see swings in the stock prices of the underlying companies.

Although the Magnificent Seven companies may emerge as the leaders in the AI space, we believe most investors are better served by investing across many companies in a variety of industries. In other words, while we want to own these companies, we don't want to own only these companies. That's because it's difficult for the same companies to keep outperforming over the long term, and it's a gamble for investors to try to predict which ones will.

[1] The Magnificent Seven stocks include Alphabet, the parent company of Google, Amazon, Apple, Meta, the parent company of Facebook, Microsoft, NVIDIA, and Tesla.

[2] NPR. "Wall Street calls them 'the Magnificent 7': They're the reason why stocks are surging." Dec. 13, 2023.

ETFs Make It Easier to Invest in Bitcoin. Should You?

Alex Kluesner, CFA

The allure of bitcoin and other cryptocurrencies continues to pervade the investment landscape, and in January, the SEC approved the first exchange-traded funds (ETFs) that trade directly in bitcoin, making the digital currency more accessible than ever. Before deciding whether investing in one of these funds is right for you, let's review the history.

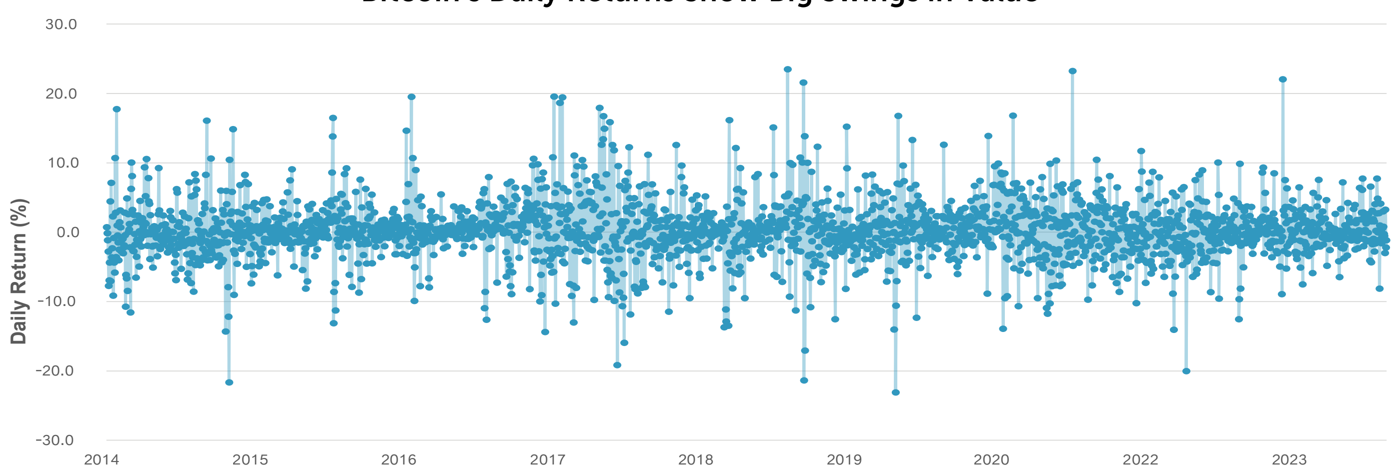
A history of attractive returns

Even though bitcoin's performance history has a limited time frame — it was first created in the late 2000s — its returns have rewarded early buy-and-hold investors and have enticed new investors. Since February 2014 through last year's end, bitcoin has increased an average of nearly 50% a year, far outpacing the returns of global stocks and bonds. To put this in dollar terms, if you had invested $1,000 at the start, it would have grown to $52,426 by the end of 2023, compared to $1,830 and $1,216 for stocks and bonds, respectively.

But investing in bitcoin comes at a price: major volatility

One of the biggest risks of bitcoin is simply losing your original investment. Bitcoin and other cryptocurrencies are known for their dramatic price swings. For example, an investment in bitcoin has experienced a loss of 50% or more in seven of the last 10 years. There have also been 40 days during the last 10 years when bitcoin fell 10% or more, and the steepest drop in a single day was over 23%. On average, bitcoin moved by 5% or more once every six days. Over the same 10-year period, there was only one day where the U.S. stock market fell more than 10%, and it moved by 5% or less on all but 13 trading days. This shows that the level of variability in the bitcoin market poses a significant behavioral hurdle to all investors.

Bitcoin's Daily Returns Show Big Swings in Value



Choose carefully

Ultimately, the benefits of allocating a portion of your portfolio to bitcoin must outweigh the potential costs. Bitcoin is a speculative investment with limited data to guide investors on making sound decisions. You should not invest more than you are willing to lose.

Sources: Ken French Data Library, Morningstar, February 2024. Returns are annualized based off monthly returns from February 2014-December 2023. Start date chosen due to data availability. Returns are based on index data: Bitcoin (S&P Bitcoin PR USD), Global Stocks (MSCI ACWI IMI PR USD), Global Bonds (FTSE WGBI Hdg USD), U.S. Stocks from Ken French Data Library U.S. Market returns. For informational and educational purposes only and should not be construed as specific investment, accounting, legal or tax advice. Indices are not available for direct investment. Their performance does not reflect the expenses associated with the management of an actual portfolio nor do indices represent results of actual trading. Information from sources deemed reliable, but its accuracy cannot be guaranteed. Performance is historical and does not guarantee future results. All investments involve risk, including loss of principal. Certain information is based on third-party data and may become outdated or otherwise superseded without notice. Neither the Securities and Exchange Commission (SEC) nor any other federal or state agency have approved, determined the accuracy, or confirmed the adequacy of this article. R-24-6961

Protecting Your Portfolio in a Presidential Election Year

By Jared Kizer, CFA

The 2024 presidential election is set to be a repeat of the Biden versus Trump contest of 2020. With both houses of Congress up for grabs, the stakes are high for either party, so it is understandable for the U.S. public to be nervous. Regardless of how the election plays out, political tensions will likely remain elevated throughout the next president's term, adding to an already contentious global political climate. Against this backdrop, many investors are anxious about the possible impact on financial markets. Here's what to keep in mind this election season.

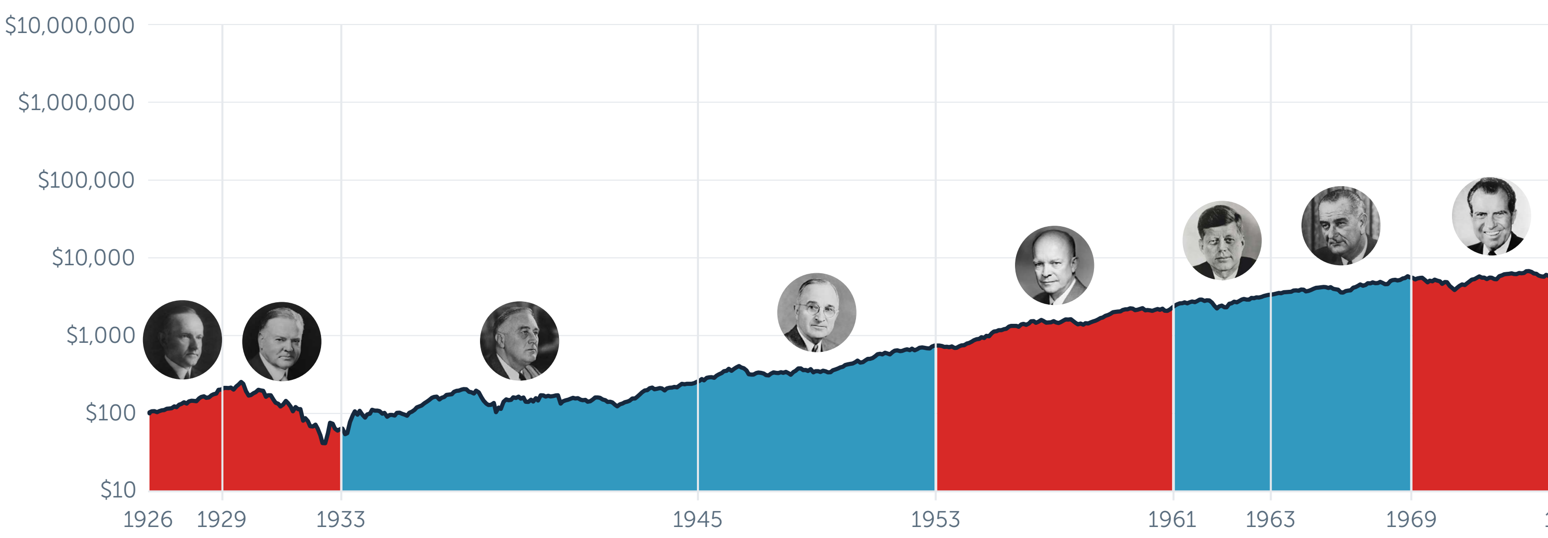
1. **Geopolitical risks are already priced into markets.**

   For financial markets, geopolitical risk is not new. While there have certainly been periods when geopolitical risks were perceived to be more elevated, global markets are continuously pricing in these risks. For as long as markets have existed, stock prices have endured the risk of world wars, regional conflicts, revolutions and countless other geopolitical events. The historical record helps investors understand the risk in most traditional stock and bond allocations. However, it's still possible that new events may reshape the historical record. When investors begin to worry that political risks are rising, we encourage them to think through this question: Setting aside the upcoming election, are you comfortable with the historical risks that your allocation has exhibited? If you aren't sure, a good first step is speaking with your financial advisor to better understand the historical risk profile of your asset allocation. This can help you decide whether you are exposed to more risk than you're comfortable taking.

2. **Election outcomes have little impact on stock markets, and the U.S. economy is better poised to withstand a global slowdown compared to other economies.**

   For the U.S. stock market, there is abundant evidence that the outcome of a presidential election has not systematically impacted the market one way or the other. What matters more are the federal policies pursued during the next administration's term. However, just like with geopolitical risks, the markets price in how such policies could impact economic growth, inflation and other indicators.

Hypothetical Growth of $100 in U.S. Stocks Since 1926



Source: Ken French Data Library for U.S. stock returns. Party information sourced from Office of the Historian and the Clerk of the House's Office of Art and Archives. Indices are not available for direct investment. Their performance does not reflect the expenses associated with the management of an actual portfolio nor do indices represent results of actual trading. Information from sources deemed reliable, but its accuracy cannot be guaranteed. Performance is historical and does not guarantee future results. All investments involve risk, including loss of principal.

Regardless of who's in power, we believe the biggest long-term economic challenge for future administrations is the U.S. government's growing size, both from a fiscal and regulatory perspective. With both parties divided on how to address the government's growing debt, this will likely lead to slower global economic growth. Keep in mind, however, that the U.S. economy is much better positioned than virtually all other developed governments and should still be more resilient to fiscal risks compared to most economies.

3. Investors benefit from favorable stock market pricing conditions.

While we covered how markets price in a range of political and economic risks, investors should also consider how a company's stock price compares to the earnings it generates. Across most asset classes, the news is positive. Although U.S. stock market valuations are above their long-term averages, most other broad asset classes — including the U.S. bond market, global developed stock markets and emerging stock markets — are relatively close to historical valuation levels. Even for the U.S. stock market, while large-cap stocks are mostly above their historical valuation levels, smaller and more value-oriented companies have valuation levels closer to their historical averages. This leads to our final point: the importance of diversifying and avoiding the temptation to chase the investments with the highest returns.

4. Diversification is your friend – especially during uncertain times.

While elections have the potential to reshape policies and legislation, it's difficult to predict which sectors or industries could benefit. The most effective way to manage risk, whether geopolitical or otherwise, is broad diversification. In the current environment, U.S. large-cap stocks have made a comeback after struggling in 2022. Because of that recent strong performance, some investors may be tempted to lower their allocation to other types of stocks, like foreign stocks and smaller-company stocks. The outcome of the election will not influence whether these trends for stocks continue, and no one can successfully predict which stocks will outperform over the next year. That's why we believe investors should maintain their allocations across global stock markets, as well as to high-quality bonds with relatively short maturities. They might also consider some allocation to inflation-protected Treasury bonds. Finally, depending on their risk profile, some investors may want to consider allocating to alternative investment strategies. While alternatives may not be appropriate for all investors due to their complexity, some strategies are less exposed to geopolitical risks than broad stock and bond markets.

If you still feel concerned about how the 2024 election could impact your portfolio, speak to your financial advisor about lowering your risk exposure and making sure your portfolio is well diversified. It doesn't hurt to take a break from following the election coverage either.