StraightTalk
PROVIDED BY STRAIGHTLINE FINANCIAL OF RAYMOND JAMES
VOLUME 1 FEBRUARY 2024

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What We Think We Know

The world is awash in information today, a good part of which is misinformation. Some of this is easy to spot, such as the email from someone in Africa informing you that $10 million has been left to you in some international bank, and all you must do to claim this windfall is wire them $5,000 to cover the costs of getting “your money” to you.

Other misinformation is much harder to identify, and you must search several sources assiduously to determine the truth. But the most problematic misinformation is what we know to be true…that isn’t. Hence the title of this newsletter, and the discussion of what we *think* we know.

The top of this list is easy – “Stocks Are Riskier Than Bonds.” You could probably find more than one million entries in textbooks, articles, investment brochures, and advertisements telling you this, so do not feel bad for thinking that it is true. Take a moment right now to open your purse or wallet and pull out one of the bills inside. It does not matter which one, it could depict George Washington or Benjamin Franklin. Now say out loud what this piece of paper is. If you said money, you are part of the 99% who get this question wrong. It is *purchasing power* in the form of currency. Money throughout the ages has taken many forms: shiny metals, beads, feathers, precious stones, checks, and even cigarettes for World War II soldiers. Currency is simply a unit of money, used as a medium of exchange, and it *is only good for what it can buy*.

Let’s assume your grandmother left you a valuable sum of money – but not in a bank, she put it in a box underneath her home 75 years ago. This has just been discovered, and you are delighted to receive this bequest. The problem is, and some of you already know where I am going with this, the dollars in that box are only worth 25 cents each in today’s world. The *dollars* have not changed, but their *purchasing power* has. Almost everything we buy, and almost every expense in our lifetime faces pressure from inflation every year. If you define risk by tracking the number of dollars you have at any given time – then anything that fluctuates up or down becomes risky, and anything that stays stable in price is safe. However, given that there have been exactly zero years in my life with no inflation, a better definition of safe is *anything that preserves or increases your purchasing power*. Therefore, things that lose purchasing power over time become easy to define as risky. Owning the great companies has always outstripped inflation, not only preserving purchasing power, but increasing it. Bonds and CDs that mature at the exact same number of dollars three decades from now – when prices will have doubled, are anything but safe. Reducing your standard of living in retirement because you are surviving on a fixed dollar income in a rising cost world is not the American Dream, and is decidedly <u>not</u> what we have as a goal in your financial plan.

Another of the things we think we know – “The Current Administration is Killing the Oil Business.” While the President did say during his campaign in 2019 that he wanted to end fossil fuel – the reality is far different. In December of last year, S&P Global Commodity Insights reported that “America is *exporting* the same amount of crude oil, refined products, and natural gas liquids as Saudi Arabia or Russia *produces*.” The report lays out that in the fourth quarter, the U.S. produced a record 13.3 million barrels of crude and condensate per day, more than any country in history. This is primarily due to amazing technological improvements in hydraulic fracturing and horizontal drilling (“fracking” for short) – and is yet another example of why, in our portfolios, we own the great companies and not the governments.

Another recent thing we think we know is "Inequality is Rising." You could be forgiven in thinking this is true because it has become a widely covered media topic over the last several years. In fact, according to author and psychologist Steven Pinker, the number of *New York Times* articles that mentioned "inequality" increased tenfold between 2009 and 2021. Given that this is an election year, I am guessing that trend is unlikely to change.

However, I recently read a report on this topic from the CATO Institute that shows, in several categories, that the global inequality gap continues to narrow. That report states, "As momentous as the global decline in income inequality is over the last two decades, measuring inequality by metrics beyond just differences in income is a more accurate way of measuring differences in well-being. Our Human Progress Index considers income, and seven additional metrics: life span, infant mortality, nutrition, environmental safety, education, internet access, and political freedom. Under a variety of specifications, the data on these metrics unambiguously show a decline in overall global inequality."

The report concludes that people are tolerant of unequal distributions of income if there is a perception that the distribution reflects merit, and if social mobility is possible. In my opinion, there is no place on earth with greater social mobility than this country, as witnessed by the simple fact that millions of the world's citizens risk everything trying to gain entry here every year. Additionally, economist and former Senator, Phil Gramm, co-wrote a book on inequality in 2022, which states that "income inequality is lower today than at any time in post-World War II America."

There is one other important thing we think we know – "We Like To Buy Things On Sale." Last month, the National Retail Foundation detailed that 200.4 million Americans shopped (either online or in actual stores) during the five days of the Black Friday weekend. Why did roughly 75% of all American adults rush to shop, and spend record amounts of money over just those five days? The obvious answer is because retailers in almost every shopping category lowered their prices!

We know that in every single aspect of our economic lives we behave this same way…we are more attracted to the goods and services we need or want when prices are reduced. Put another way, the more the price falls, the greater our interest in buying. And the converse holds true, the more prices go up, the less interest we have in paying up, so we postpone those purchases.

This holds true in all areas of our economic lives, but not in the most critical area of our financial lives, *investing our lifetime accumulation of money*. Here we behave in an opposite fashion, despite assurances that we all "like to buy on sale." The data shows that people flock towards the areas of the markets that have seen the most dramatic price appreciation – think of the dot-com era, the recent meteoric rise of the "Magnificent 7," or worse, the insanity of gambling in cryptocurrencies. And the data shows that people urgently sell out of even the soundest of investments when the price falls. Easy panic-selling examples like 2008, the election in 2016, the Covid quarter of 2020, and the 2022 inflation-backlash year spring to mind. So, while we think that we always like to buy when prices are low, the stock exchange remains the only place on earth where, when every few years there is a big sale, everyone runs screaming out of the store.

And just as it is likely that the "news" this year will contain things we think we know, there is also a chance of a temporary decline in market prices. Let's all discard any doomsday warnings given about price declines, and pledge to focus on the truth. And the truth is, the essential imperative of a profit-seeking company is to preserve its owner's capital, and there is no force on earth that can compel it to continue to lose money. Instead, the goal is to always innovate, and reinvest profits to grow owner's (shareholder's) wealth. So, all we must do is remember that truth, ignore what we *think* we know about prices, and let the miracle of compounding occur…

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