NAPLES GLOBAL ADVISORS

MARKET INSIGHTS

THIRD QUARTER 2024

> ***The big money is not in the buying and the selling, but in the waiting.*** - Charlie Munger

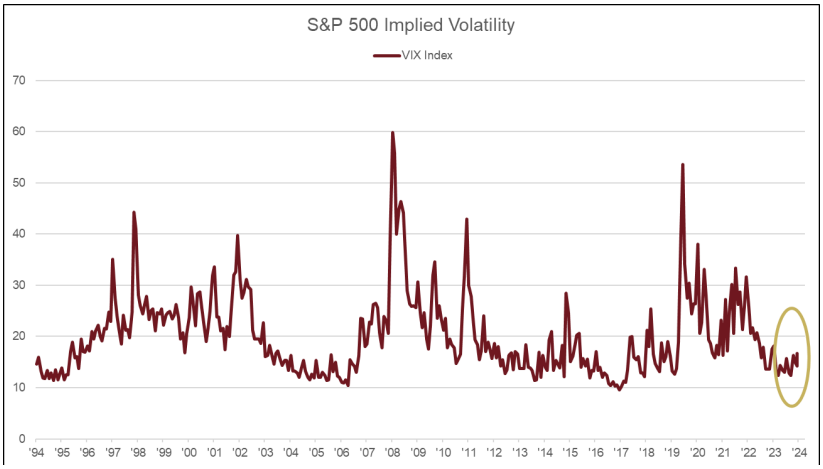
Wyatt Russo, CFA

Principal & Portfolio Manager



Setting monetary policy has been compared to taking a shower where the temperature has a delayed response to any adjustment being made. Think of the water being a little too cold and turning the water hotter, only for it to then be scalding. It is not always easy to get just right. This is the dilemma facing central bankers; they cannot let the economy run so hot that high inflation persists, but also not so cold that it dips into a recession. The shower analogy plays to the notion that monetary policy feeds through the economy in "long and variable lags."[1] The phrase was coined by economist *Milton Friedman* and has been cited by current Federal Reserve Chair *Jerome Powell*. After the Fed embarked on the most aggressive hiking cycle in decades and kept rates elevated for the last year, it appears these lags are reaching main street. There is evidence that the labor market is softening and inflation is moderating. This combination has given the Federal Reserve the assurance needed to pivot their stance, and that's just what they did on September 18th by cutting interest rates 50 basis points.

This regime shift comes during a time with increased debate on the forward path of interest rates, the political landscape, and the health of the economy. The backdrop can make it *feel* like we are in a period of intense volatility. We believe it is our job to zoom out and contextualize the investing environment, and 30 years of data helps us keep a healthy perspective. The chart below depicts the VIX Index, a volatility gauge of the S&P 500, with higher readings representing increased expected volatility for the stock market. We circle 2024 to show that current conditions are not exceptionally volatile compared to historical levels. The rapid spikes seen over the last three decades are a reminder that, for long-term investors, periods of volatility are not unprecedented. While it is difficult to identify when they will occur, periods of elevated volatility can be expected over any meaningful time horizon.



Source: Bloomberg

Despite the numerous periods of extreme volatility, the S&P 500 total return over the same 30-year period was over 2,000%, or 10.8% annualized. The key takeaways are to maintain a **comfortable asset mix** and to **stay the course**. Investors didn't receive the benefit of this attractive return if they changed course every time volatility increased. In periods like the current, it can be natural to want to act. However, we are reminded of a quote from the late Berkshire Hathaway legend *Charlie Munger*. "The big money is not in the buying and selling, but in the waiting". [2] We do not get complacent, rather we look at companies through the lens of fundamental analysis. Our assessment is grounded in whether our rationale for owning a business has changed rather than being beholden to market swings. That said, our investment philosophy must adapt to the environment we are provided. We are cognizant of the increase in single-stock volatility and higher dispersion of returns, which is why we remain committed to logical diversification and sensible position sizing.

Whenever volatility moves higher, commentary on private equity and private debt intensifies as asset classes that present the opportunity to earn higher risk-adjusted returns. Private investments can provide attractive returns and

serve a critical function in financial markets, but only having to provide periodic valuations may understate volatility. *Cliff Asness* of AQR has dubbed the infrequent mark to market of private assets as a form of "volatility laundering."[3] Said differently, not valuing an asset does not mean its value isn't changing day to day. We can appreciate the emotional benefit of seeing a stable value when other assets are experiencing large price moves, but we also want to approach investing in an intellectually honest manner. There is the possibility of an innate fiduciary conflict of interest where the manager of an asset is also the party providing the valuation. A higher valuation leads to higher fees for the manager, representing a potential misalignment of incentives. Public market valuations, volatile or not, allow for a more transparent process. Our sense is we are better off not trying to solve this debate and remain consistent in our thinking that when we are investing, we are not buying stocks but rather companies. Though we are public market investors, in a nod to a private market investment approach, we want everything we own a piece of to be something we would be excited to own all of.

One ipotential source of increased volatility on everyone's mind is the upcoming election season. We certainly recognize that elections are economically and fiscally impactful, and subsequent policy implementation can influence industries and companies. However, we remain steadfast in our belief that asset allocation has historically been the most important investment decision and that portfolio management should remain apolitical. Our aim is not to predict who will win upcoming elections or whether interest rates will land at 3 or 4%. Our aim is to build all-weather style portfolios comprised of high-quality companies that will continue to serve our clients' needs irrespective of who is in the White House.



Source: Gulfshore Business

To close, we want to highlight a few internal developments and accomplishments. We are excited to welcome *Amy Tancreto*, Operations Officer, and *Julia Lang*, Client Services Officer. Amy and Julia bring valuable experience and we believe our clients will benefit greatly from their contributions. Additionally, *Sara Perkins* attended the Florida Trust School this summer, and Kerry Geroy participated in the Attorney Trust Officer Liaison Conference. Both initiatives strengthen their already deep knowledge in assisting our clients with wealth strategy. And a big congratulations to *Greg Debski* who was recently named to the Gulfshore Business 40 Under 40.

When "we say around the globe, around the corner," it isn't just a catch phrase; we strive to invest with a global lens but remain deeply ingrained in our local community. With that in mind, the NGA team recently participated in the Coastal Clean Up. Lastly, two colleagues from our portfolio management team are heading to London in early October to meet with companies headquartered in the United Kingdom. European valuations remain depressed compared to other developed markets, and we are eager to revisit the opportunity set. We include these updates not to pat ourselves on the back, but to highlight our commitment to increasing our collective knowledge and capabilities to better serve our clients. As always, we thank you for your continued trust and confidence.



[1] Asness, Cliff. "Why Does Private Equity Get to Play Make-Believe with Prices?" Institutional Investor, Institutional Investor, 20 Dec. 2023, www.institutionalinvestor.com/article/2bstqfcskz9o72ospzlds/opinion/why-does-private-equity-get-to-play-make-believe-with-prices.

[2] Culbertson, J.M. "Friedman on the Lag in Effect of Monetary Policy." Friedman on the Lag in Effect of Monetary Policy, The University of Chicago Press Journals, www.journals.uchicago.edu/doi/pdf/10.1086/258396#:~:text=Friedman's argument on the policy,the lag is rather variable. Accessed 30 Sept. 2024.

[3] LaMonicMonica, Mark. "The Wisdom of Charlie Munger." Morningstar Australia, 27 Mar. 2024, www.morningstar.com.au/insights/personal-finance/243253/the-wisdom-of-charlie-munger.

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