Six mistakes investors should avoid in 2020

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It’d be all too easy this year to fall into these traps and derail your long-term plan.

Political noise will only get louder as the year races toward the November U.S. presidential election.

**Question is:** How much of an impact could the roar of the campaigns and any of the potential next presidents actually have on the markets?

**Our view:** Not enough to derail your plan.

In fact, number 1 on our list of mistakes for investors to avoid in 2020 is:

- Getting distracted by the election

The other five mistakes that could reduce long-term investors’ chances of reaching their financial goals are:

- Assuming portfolios will generate the same strong returns
- Holding too much cash
- Ignoring secular growth trends
- Giving up on stocks outside of the United States
- Assuming the U.S. dollar will stay strong forever

And here are the reasons why you’ll want to follow these “what not to do in 2020” tips for investors:

**1. Don’t be distracted by the election**

History tells investors not to overreact to presidential candidates.

In 2016, many people thought President Trump’s election would usher in a global recession. Previously, many thought the Obama presidency would crush equity markets. Investors who acted on these fears would have missed returns of over 60% (from Trump’s election), over 150% (from Obama’s second term), and over 400% (from Obama’s first inauguration).
This election year a few progressive candidates are vowing to re-make American capitalism. Their campaign rhetoric suggests such potential risks to the markets as higher taxes, a more stringent regulatory environment and policies that work to elevate labor relative to capital.

These risks are real, but we don’t think that the likelihood of the policies being adopted is high enough to derail long-term investment plans. And, while a snapback from Trump to a Democratic president would likely generate volatility; it is unlikely to last. (For more on this topic, see the 2020 Outlook).

2. Don’t assume portfolios will generate the same strong returns.

Over the next 10–15 years, we expect returns of only 5.6% per year for U.S. large cap equities. This is less than half of the ~13.5% rate investors have enjoyed over the last 10 years.

To translate this difference to dollars—at a 13.5% annualized rate, a $100 investment would grow to $354 over 10 years. At a 5.6% annualized rate, $100 grows to only $172.

For some, expectations of lower returns may not mean they should change their portfolios. Their current allocation still could be appropriate to achieve their intent for their wealth.

Concerned you may not be so fortunate? We recommend reviewing your plan to ensure your current investments are still likely to do the job you expect. If they are not, adjustments can be made.

3. Don’t hold too much cash.

Many were tempted to move into cash during the last two years. The Federal Reserve was raising interest rates, so cash provided a yield that could compete with inflation. Cash also seemed like a safe place to hide as investors feared a recession was imminent.

Indeed, more than $1 trillion dollars have moved into money market funds since the middle of 2017.

But now those investors who moved into cash face two problems:

- **Cash is not currently competitive with inflation.** After the Fed’s three interest rate cuts in 2019, cash rates are below inflation (where they have been 95% of the time since the 2008 Global Financial Crisis). We don’t expect the Fed to start raising rates anytime soon, so it’s likely inflation will beat cash again in 2020.

- **There may be better ways to protect investments than by moving to**

![10-year trailing returns of U.S. equities and our assumptions](source: Bloomberg, Ibbotson. December 2019)

![Investors still herding to cash even though the Fed has cut rates](source: Investment Company Institute, Bloomberg Financial L.P. December 2019)

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cash. Over the last 18 months, we made significant changes in the portfolios we manage to add more protection. We did not move to cash. Instead, we preferred such choices as “core” bonds (i.e., U.S. Treasuries and investment grade corporate debt). From the beginning of 2018, when money market assets inflows really started to accelerate, cash has returned 3.7%. Meanwhile, 7- to 10-year U.S. Treasury bonds have returned 9.5% and longer-term Treasuries have returned 14%. Don’t like bonds? We also favored gold, which is up 12.5% over the same period.

So look carefully at how much cash you hold in 2020 to ensure it fits with your larger plan. (For more on how to evaluate how much cash you want to hold, see The bucket list: Too much—or too little—liquidity?)

4. Don’t ignore secular growth trends.
Another way to combat lower future returns is to expand investments, beyond aggregates and indices, into specific secular growth trends.

Take the automobile industry as an example. While global auto sales contracted in 2019, electric vehicle sales grew by over 25%. We expect companies involved in producing next-generation vehicles to translate this trend into above-market earnings growth and outpace the broad market over the next 3 to 5 years. Despite the sales growth, it hasn’t been smooth sailing for investors in the space, but we think that now may be the time for investors to focus on the electric vehicle industry.

Other areas of growth we are looking at include e-commerce, software and emerging markets.

We also are focusing on companies that innovate to generate new products and services. When investors hear “innovation,” they usually think of tech first; but it isn’t just a technology story.

Recall that only recently “athleisure” wasn’t part of anyone’s vocabulary, let alone wardrobe. Now, Lululemon has everyone wearing sweats and yoga pants around town and the company’s stock has tripled in value over the last two years.

Obviously, not every company will generate that return in such a short period of time. Still, it can be lucrative to identify companies that are not only innovating but also translating innovation into earnings growth.

5. Don’t give up on stocks outside of the United States.
U.S. large cap equities have outperformed equities in the rest of the developed world by 174% over the last 10 years. Last year saw more of the same. U.S. stocks gained 10% more than developed market stocks outside the United States in 2019.

Naturally, many investors are wondering now whether it’s worth holding stocks outside the United States. We think it is.
After all, holding them along with U.S. stocks reduced volatility—even while developed market equities outside of the United States significantly lagged in price terms. And it is critical to investing success to reduce volatility so that returns can compound more efficiently.

For example, since 2010, the MSCI USA index has had an annualized volatility of ~14%, while an equal weighted portfolio of 50% MSCI USA and MSCI World ex-USA had a volatility of ~13.8%. When you extend the sample back to 1991, the addition of ex-U.S. stocks to portfolios reduced volatility from 16.6% for the United States alone to 15.3%.

Looking ahead, three trends could make markets outside the United States more attractive in 2020:

- Stabilization in the global industrial sector should benefit stocks outside of the United States, given their larger exposure to manufacturing.
- We expect central banks to maintain an easing bias and bond yields to remain low. This combination could offer support to equity markets outside the United States that have relatively high dividend yields.
- The U.S. dollar is likely to weaken slightly in the year ahead. This would provide a tailwind for non-U.S. markets and would provide U.S. dollar-based investors an added benefit on un-hedged positions.

6. Don’t assume the U.S. dollar will stay strong forever.

We don’t expect the U.S. dollar to lose its reserve status in a “cliff’s edge” moment. However, we think it is prudent now for investors to consider diversifying currency exposure as they would stock exposure. Also, for some global families and institutions, determining the right mix of currency exposure to mitigate the impact of sudden changes in currency values is an often overlooked consideration in an overall investment plan. We offer this advice because there are signs that the U.S. reserve currency status isn’t as unassailable as it once was:

- The world’s economic center of gravity is moving from the United States and Europe to Asia.
- Twenty years ago, the U.S. dollar accounted for around 70% of global central bank reserves. That share is now down to 60%.
- A number of jurisdictions, including China, Russia, and the Euro Area, are establishing cross-border payment systems that avoid the U.S. dollar.

There also are some immediate reasons why the dollar may weaken in 2020. The economic outperformance of the U.S. in the last two years has attracted flows into U.S. dollar-based assets, and the currency is ~15% overvalued relative to its history. We expect this performance gap to narrow, and dollar outflows to follow.

Put it all in context

Of course, to stay on track to reach our long-term financial goals, we have to articulate the intent of our investments, have a plan to get them there, and be sure to check them regularly. That is why the number one recommendation we have to start your year off right is to speak with your J.P. Morgan Advisor to make sure your wealth strategy is up to date—and your investments are aligned to support them.
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