The Optimistic Investor

FOCUS ON WHAT REALLY MATTERS

Overview

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Welcome Back

Last quarter we focused on the importance of making investment decisions based on our long-term goals. We looked at the fickle nature of market sentiment and how the media fixates on things that don't really impact long-term investment success. And we explained how having a plan helps us stay grounded and make good decisions through uncertain times.

This quarter we come back to uncertainty to highlight that it is an inescapable part of investing and the primary driver of our long-term returns. We then examine the ways uncertainty can play out in financial markets and reinforce that our understanding of these dynamics allows us to be prepared for whatever the future might bring.

We hope you enjoy the essay!

The Only Certainty We Have Is Uncertainty

As we approach the end of 2024, most people are aware that it's been a great year for equity investors. Inflation has continued its downward trend, labor markets and economic growth have remained firm, and corporate earnings have been strong. Thus, as of market close on December 20th, global equities are up more than 17% for the year.[1]

With such strong performance, it's easy to forget that as we turned the page on 2023 there was much concern about what this year would bring. Many economists and pundits were still talking about an "inevitable" recession, and there were potential government shutdowns looming, wars intensifying in Ukraine and the Middle East, and a presidential election ahead.

Reflecting on how this year began provides a great opportunity to revisit the importance of uncertainty to our long-term success as investors. Frequent readers of these memos will know that: (a) diversified portfolios of companies (*i.e.*, stocks) have historically generated much better returns over time than other types of investments; (b) we ***need*** those premium returns to outpace inflation, grow our wealth and keep our long-term plans on track; and (c) we ***earn*** those premium returns through our willingness to bear uncertainty.

At the beginning of this year, most of us felt a lot of uncertainty about what 2024 would bring. The inflation-induced bear market of 2022 was still fresh in our minds, and the factors noted above offered plenty of ways for markets to turn downward. But the existence of potential market disruptions is not something that's unique to 2024.

There is *always* a cloud of uncertainty hanging over financial markets. Sometimes we're more aware of uncertainty and the cloud seems darker, but you can always create a list of current issues with the potential to cause significant market disruption. As financial writer Nick Murray has put it: "uncertainty – in the markets and indeed in the world – is the only certainty. We don't seem to move from periods of uncertainty to periods of certainty; rather we go from one 'crisis' to the next."[2]

As long-term investors, we must recognize that uncertainty is unavoidable. And we need to embrace the fact that it's what ultimately drives the long-term returns we need to be successful.

Investment management firm First Trust publishes a great slide that we often use to discuss these points with clients. It shows the growth of the S&P 500 from 1970 through 2024 and overlays that chart with notable events and crises from those years. Because of the font size, we've reproduced the slide as Exhibit 1 at the end of this memo. Please take a minute to look it over before you continue reading.[3]

> ***Uncertainty – in the markets and indeed in the world – is the only certainty.***
>
> ***~ Nick Murray***

[1] Data source: Morningstar - MSCI All Country World Index NR USD up 17.86% YTD (accessed 12/22/24).

[2] Murray, Nick. *Around the Year With Nick Murray*. The Nicholas Murray Company, Inc., 2016, pg. 468.

[3] You can access the original chart and disclosures here.

One thing that Exhibit 1 probably reinforced for you is that Nick Murray is right. The world really does seem to move from one "crisis" to the next without ever taking a breath. Hopefully, though, you also noticed that a lot of these crises don't impact markets in a meaningful way. As Exhibits 1 shows, many awful things that happened over the past 55 years, including some wars, environmental disasters and major political scandals, didn't cause the S&P 500 to decline.[4]

This is the first key point about uncertainty: even though there are always looming issues that *could* lead to broad market declines, most of them never actually *do*. Bad things happening (or potentially happening) in governments, economies or the broader world don't necessarily translate into market distress. And that's why it's always a mistake to change our long-term investment plans based on current events. We simply don't (and can't) know how markets will react as future events unfold, and the cost of making a guess and being wrong is simply too high.

Consider 2024 as an example. People who let their fear of uncertainty prevent them from investing in globally-diversified equities this year missed out on ~ 17% returns. That's a hefty opportunity cost (likely in the hundreds of thousands of dollars for affluent investors) that will reduce their lifetime returns and lower their probability of long-term success. Fortunately, if you're reading this, you probably didn't make that mistake and have reaped the substantial benefits of bearing this year's uncertainty.

We must remember, however, that not all years turn out like 2024. Sometimes looming issues unfold in a way that drives broad market declines. Exhibit 1 reflects numerous examples of this, including three bear markets where the S&P 500 went down ~ 50%.[5] But the chart also makes clear that all those declines were temporary and the S&P 500 experienced tremendous growth *despite* them.

This is the second key point about uncertainty: when it has led to market disruption, the declines have always been temporary. Exhibit 1 makes this very clear. It shows that a $10,000 investment made on 1/1/1970 would have grown to $2,921,767 by 9/30/2024. That reflects an average annualized return of ~ 10.4%, which is right in line with the long-term average for the S&P 500. And that average return *includes* all the bear markets we've experienced since 1970. Exhibit 1 is thus a great reminder that our willingness to bear uncertainty and endure occasional declines is truly how we *earn* the returns that grow our wealth and keep our plans on track.

To sum all of this up, we'll never be able to escape uncertainty as investors. It will always be with us. Sometimes markets will look right past it and continue their long-term climb like they did this year; other times it will cause market disruptions, and we'll experience extended periods of decline on the way to longer-term gains.

Thankfully, our awareness of these dynamics allows us to be mentally and financially prepared for the periods of market distress that uncertainty sometimes brings. We know past declines have just

[4] Many of you will remember the Y2K "crisis" that gripped the country as we transitioned from 1999 to 2000. Exhibit 1 doesn't show Y2K, most likely because the dot.com bubble began to deflate in 2000. But Y2K is a great example of a "crisis" that proved to be a total non-event.

[5] These were 1973-1974 (OPEC oil embargo and resulting inflation), 2000-2022 (implosion of the dot.com bubble), and 2007-2009 (global financial crisis).

been temporary interruptions of the long-term growth trend, and your plan accounts for the occurrence of such episodes in the future. That means your portfolio is set up to meet your needs and keep you on track for success through both the good times and the rough stretches.

So, as we close the book on 2024, let's be thankful for a great year and take comfort in knowing that we're prepared for whatever 2025 brings our way.

Innovation & Good News

1) Quantum computing has huge potential to drive future innovation. In time, quantum computers will be able to perform tasks and solve complex problems that are far beyond the capabilities of today's most powerful supercomputers. Earlier this month, Google announced a new quantum chip (called Willow) that reflects some major steps towards a scalable quantum computer.[6]

2) Google also recently published test results for a new weather forecasting model (called GenCast) that's based on machine learning. GenCast was more accurate than the leading current model in 97.2% of cases, plus it was better at predicting extreme weather and generated forecasts much faster.

3) Last month Neuralink (Elon Musk's brain implant company) announced approval of a study to see whether it's implant can allow patients to control robotic arms using their thoughts.

4) A recent study found that many hard-to-treat cancers contain loops of genetic material – called ecDNA – that help tumors survive and develop resistance to treatment. A new drug is already in early-stage trials that can target and destroy cells containing ecDNA.

5) Data shows that progress in diagnosing and treating cancer has had a significant impact over time. The likelihood of an American dying from cancer at any given age has declined by one-third since 1990.

6) In another example of the power of innovation over time, we recently learned that the measles vaccine has saved 94 million lives over the past 50 years.

Financial Planning Updates

Retirement contributions – don't forget to adjust your retirement savings for the 2025 maximum contribution levels:

401(k), 403(b), and Thrift Savings Plan accounts will have a limit of $23,500, plus an extra $7,500 for those age 50 and older.

Traditional and Roth IRAs will have a limit of $7,000, plus an extra $1,000 for those age 50 and up.

Charitable giving and gifting in 2025

Qualified charitable distributions will be limited to $108,000 per person.

The *annual gift tax exclusion* will increase to $19,000, and the *lifetime exemption* from federal gift and estate tax will increase to $13,990,000.

[6] If you'd like to learn more about quantum computing, IBM provides an in-depth overview on its website, which you can access here.

KOOMAN & ASSOCIATES

Important Disclosure Information

This memorandum is not intended as a substitute for personalized investment advice from Kooman & Associates, LLC ("K&A"). To the extent you have questions about the applicability of any specific issue discussed herein to your individual situation, you should consult with a professional advisor of your choosing.

Nothing in the foregoing discussion should be interpreted as a recommendation to buy, sell or hold any specific security. Please remember that past performance and events may not be indicative of future results.

All investments and investment strategies involve different risks and there can be no assurance that any specific investment or investment strategy, including those recommended or undertaken by K&A and/or discussed in this memorandum, will be profitable or suitable for your portfolio or individual situation. Moreover, due to various factors, including changing market conditions and/or applicable laws, the foregoing content may no longer be reflective of our current opinions.

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A copy of K&A's current written disclosure brochure (Form ADV Part 2A) discussing our advisory services and fees is available for review upon request or at www.kooman.com.

Please remember to contact us in writing:

- If there are any changes in your personal/financial situation or investment objectives, so we can review, evaluate and/or revise our previous recommendations as needed; or
- If you would like to impose, add or modify any reasonable restrictions on our investment advisory services.

Unless and until you notify us, in writing, to the contrary, we will continue to provide services as we do currently.

Please also remember to advise us if you have not been receiving account statements (at least quarterly) from your account custodian.

Crisis and Events

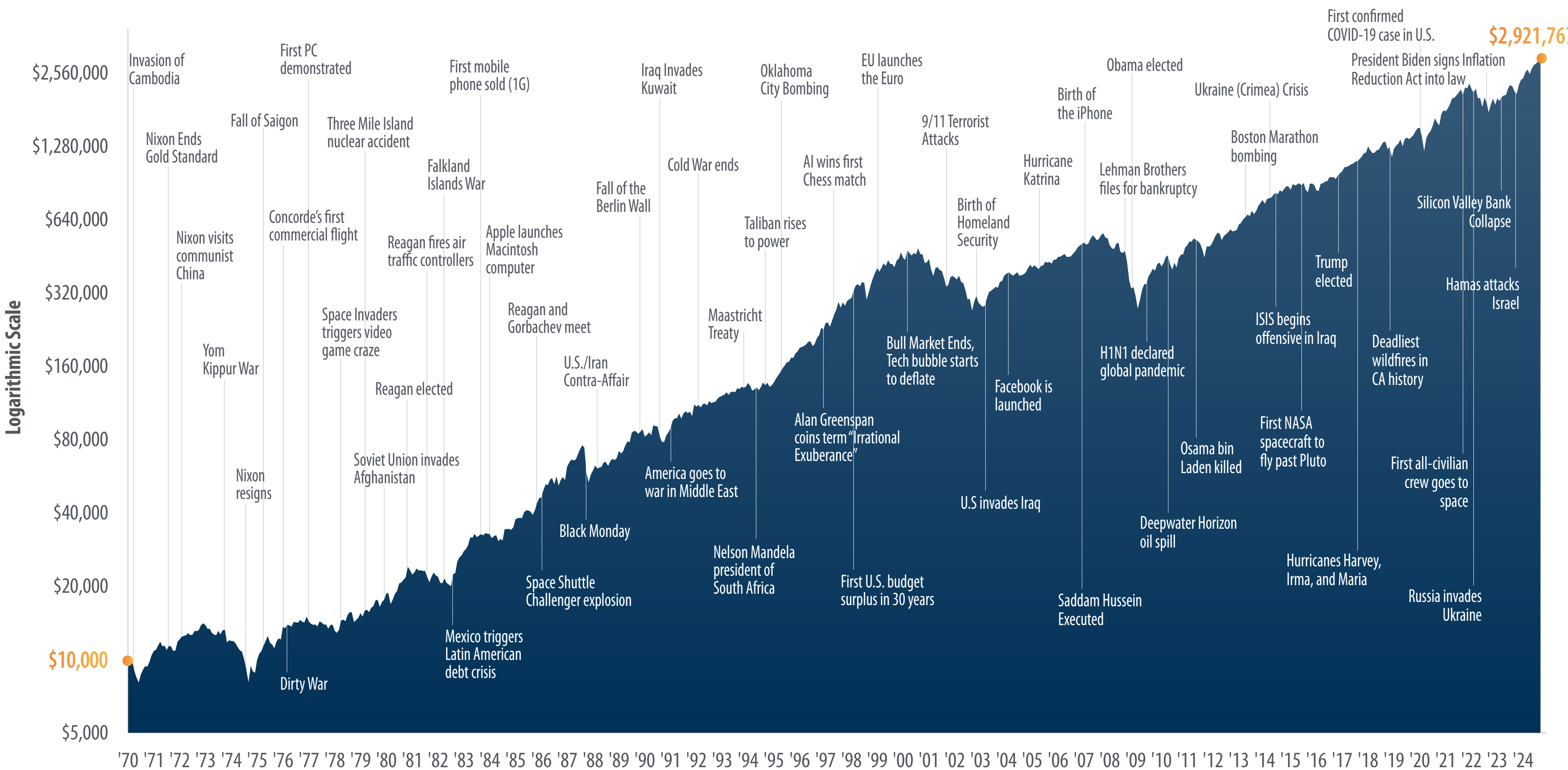
S&P 500 Index: Since 1970

Exhibit 1

First Trust

This chart shows the growth of $10,000 based on S&P 500 Index performance over the last several decades. We believe looking at the market's overall resiliency through major crises and events helps to gain a fresh perspective on the benefits of investing for the long-term.

The average annual total return of the S&P 500 Index for the period shown below was 10.90%.



Source: First Trust, Bloomberg. Data from 12/31/1969 - 9/30/2024. **Past performance is no guarantee of future results.** This chart is for illustrative purposes only and not indicative of any actual investment. The S&P 500 Index is an unmanaged index of 500 companies used to measure large-cap U.S. stock market performance. Investors cannot invest directly in an index. Index returns do not reflect any fees, expenses, or sales charges. Stocks are not guaranteed and have been more volatile than the other asset classes. These returns were the result of certain market factors and events which may not be repeated in the future.

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