

Thoughts that count

A wonderful ride

Without traffic my house is 30 minutes from downtown Toronto. During rush hour this balloons to at least 90 minutes. For this reason, I seldom make it into the downtown core anymore. When I absolutely have to be downtown, I typically leave my house early in the morning, and try to leave the city before rush hour. Heading back to the suburbs after a recent visit to Toronto I found myself in heavy traffic at 3:30pm trying to make it to the highway before rush hour officially began. I maneuvered my car around construction machinery and orange pylons, looking for a way to escape the congestion. Waiting at a stoplight, I noticed the street to my right appeared to be clear; a miracle! When the light turned green, I turned right and could see a direct pathway out of the city laying before me. Just then, a policeman stepped off the curb, and motioned for me to pull over. I was confused. Had I done something wrong? I rolled my window down, and asked why I was being stopped? He smiled. "You cannot turn right at this intersection during rush hour" he said. Perplexed, I exclaimed "there are no traffic signs indicating no turning and it's not rush hour!" His grin widened. "Sorry pal, I don't make the rules, I just enforce 'em" he smirked as he handed me a ticket for \$125. My confusion turned to anger.

As long as I can remember I have been afraid of heights. In grade 4 my best friend convinced me to try Canada's first standup roller-coaster, *The SkyRider*, and I was terrified. During that initial ride I recall feeling two emotions in quick succession; dread, during the slow climb to the ride's first peak, followed by exhilaration, as endorphins rushed through my body as the ride zoomed along its track. I was reminiscing about this moment recently when I took my two boys (ages 8 and 9) to *Canada's Wonderland* to try the newest roller coaster; *The Yukon Striker*. As we climbed the first hill (245 feet into the air!) I was filled with a mix of fear and excitement once again. As we began to descend, a great smile crossed my face as I thought about the memories my kids and I were creating at that moment. We spent the day running from ride to ride; laughing, joking, having a wonderful time. The kids fell asleep in the car on the ride home, exhausted from fun. I smiled the whole drive. The cost for entry into the park that day for the three of us was \$125.

The fourth quarter of 2018 was the worst 3 month period for the stock market in seven years. In response, investors withdrew funds from the market. American investors were particularly upset; withdrawing more than \$100 billion of stocks in the quarter. Unfortunately, those investors had poor timing. The following quarter, the first quarter of 2019, was the best performing three month period in 10 years. Quite a 6 month ride. Volatility has returned.

An important question: is this volatility a *fine* or a *fee*?

- A *fine* is punishment for doing something wrong.
- A *fee* is something paid to gain something worthwhile in return.

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A fine is a deterrent. The purpose of issuing a fine is to change behavior. The natural reaction to receiving a fine is usually anger, followed by a behavioural adjustment in order to avoid future penalties. You are not supposed to get fines. You are supposed to make decisions so that you avoid fines. Fines for traffic offences work in this way. Not only will I not make a right turn at that downtown intersection again, I will think about that fine every time I am in that vicinity, whether I am in a car or not. I don't ever again want to experience the embarrassment of being pulled over by police nor the financial penalty. This is true even though I feel the fine was unfair. That is the power of a fine.

The cost to take my kids to *Canada's Wonderland* was the exact same amount, \$125, but I don't feel I was fined. I got to have an incredible day with my kids that I will never forget. I would happily pay this fee again. A lot of people agree. Last year almost 4 million people paid the admission fee to attend *Canada's Wonderland*. Few of them felt the cost was a punishment.

In investing, volatility is almost always a fee, not a fine. This is an important distinction. Volatility is not a punishment and it does not indicate an investor has done anything wrong. Viewed in this way, market ups and downs can be more than just 'tolerated', they are in fact a fee worth paying. The reason they are worth paying is because over the longer term, the reward is enormous; you get to reach your life goals. Viewing volatility as a fee instead of a fine is an important part of developing the fortitude to stick around long enough for the power of compounding to work. Investment volatility is not a penalty or a punishment. While uncomfortable in the short term, just like paying to enter a theme park, volatility is a feature of investing, not a bug that can be eliminated. Sure, there are ways to minimize volatility, but it can never be eliminated completely.

So how much is this fee? Rather than expressed in dollars, the fee is primarily psychological. The cost is captured in the fear of declines, panics, manias, recessions and depressions. These are all legitimate fears. However, it is also true that the fear of these things is often worse than the actual event. Returns are never free; they demand a cost. Only those willing to pay this fee will generate a return over and above inflation, which is the only way to maintain and/or grow wealth.

Of course no one is forced to pay this fee. Just like no one is forced to take their kids to *Canada's Wonderland*. I could have taken my kids to the local arcade for \$10 instead and we might have had a good time. But usually, you get what you pay for. Recognizing the fee is worth paying is the trick to managing our response to volatility. If you view the admission fee as a fine, you will find it much more difficult to meet the goals that make life so wonderful.

Your *glad I don't have to go on The Yukon Striker* every day investment advisor,



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