

The Riverwood Wealth Management Group at Morgan Stanley

News and Views

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Hello again! During a recent meeting with a client, I was asked about a prediction, or forecast, made by a person speaking for a large well known financial institution. The names are unimportant, but what is noteworthy to me is that this client remembered to specifics of the prediction. In my opinion, the prediction was memorable because it was somewhat bold. It called for a market result over the rest of the year that was far different than other published forecasts. It seems reasonable to assume that others employed by similar firms in similar positions have access to similar information. If so, one might assume that the ways they interpret that information would somewhat similar, as would be their forecasts. Why then would there be an outlier? Of course, someone needs to have the highest forecast, just as someone needs to have the lowest, but even those outlier predictions tend to be relatively close to the group think.

There is the chance that this specific forecaster has better skills, keener insights, and a sharper intellect than all his/her peers at other firms. That is possible, but if it were true wouldn't this person simply trade their own account on this insight as opposed to sharing it with the world? Another possibility might be that this person (or this firm) made the decision that they want to be noticed. They wanted to stand out from the multitude of others and be talked about. How better to do that than to be markedly different? Drawing attention to you and/or your firm may help generate readers and even new clients.

I think it fair to consider just how accurate this person has been in the past. How often do they make forecasts, how often are they right (or close), and how often do they "adjust" their forecasts? Over the years I have noticed that many of those in the prediction business make multiple adjustments to their predictions, and it is typical that these adjustments tend to be announced with less fanfare than the original prediction. For example, let's say that analyst "A" has made a prediction that something (usually an index or a security) will rise 100% by year end. Several months into the year it seems as though this is not happening, and the analyst will adjust the forecast down, often citing some recent (convenient) external event as the cause. This can happen multiple times until the final forecast made sometime late in the fall is calling for a 10% rise from the original starting position. Should that happen, the expert will tally that prediction as a success, but what good did it do anyone? Seems kind of like calling for rain every day until does rain.

I am not trying to pick on forecasters, after all it is an impossible job. I am just not certain the value they provide. Imagine periods when forecasters have made dire predictions calling for bad markets. Such views doubtless results in some "getting out" of the market to avoid the bad period. If that bad market does not manifest those that got out are left watching and need to make a tougher decision...when to get back in. Despite all this the predictions continue to be made. The rewards can be very tempting as being correct just once on some bold call in which you were the only one to call for "x" to happen can build a reputation that could last a lifetime. Add to that the luck to have your timing on making such a prediction be perfect. For example, publishing a prediction in July that the market was going to correct in August, and having that occur, could result in promoting the analyst into legendary status. All this despite the fact that this analyst may have called for a correction every year for the past 10 years, and none had previously occurred.

It won't surprise you to know that we do not center our market decisions around the forecasts made by anyone. For starters, such forecasts would have different implications for 30 years old than they might for a 70-year-old. As we often point out, every investor has their own set of circumstances, goals, and tolerance to risk...and those are the traits that should dictate investment allocations and guide us in our efforts. Some of my favorite quotes centered on the fallacy of forecasts prediction are on the next page. I hope you enjoy them. Thanks for your time, please feel free to call anytime.

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"Those who have knowledge don't predict. Those who predict don't have knowledge."

- Lao Tzu

"It's tough to make predictions, especially about the future."

- Yogi Berra

"The function of economic forecasting is to make astrology look respectable."

- John Kenneth Galbraith

"Forecasts may tell you a great deal about the forecaster; they tell nothing about the future."

- Warren Buffett

"Forecasts aren't worth very much, and most people who make them don't make money in markets."

- Ray Dalio

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