MDDS Connections for Metro Denver's Dental Profession

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By **Steven Karsh**

Indeed, we are living in unprecedented times as we enter a new phase of the pandemic. A look at the economic landscape tells us we have (for now):

1. Record levels of economic stimulus - both fiscal (government spending) and monetary (Federal Reserve)

2. Historically low interest rates

3. Increased inflation expectations

4. High unemployment

5. Stock market at an all-time high

So, what does this mean for our portfolios? The simplest answer and the one that no-one likes is, "we don't know." Predicting what is going to happen in unprecedented times is extremely difficult, let alone in "normal times;" however, if we have a plan and stick to it, the individual factors above should have little impact on the long-term outcome.

Who would have predicted 18 months ago that stock markets would be making new record highs after going through the pandemic when the global economy was essentially closed for business? My guess is not many, and those who did, were not on record and, most likely, it was wishful thinking. If we look back now, it's not that difficult to understand why. The economy was humming along before the pandemic with record low unemployment and all-time high corporate earnings. A year and half later, there has been a flood of cash put into the economy from the government and the Federal Reserve. People are spending their stimulus checks, companies are spending their stimulus money, borrowing money is extremely inexpensive with low interest rates and companies have learned how to adapt to new working conditions, resulting in better profitability because of the pandemic.

A deeper dive shows us companies like Facebook, Google, Amazon, and Netflix all did extremely well during the pandemic. This was not a surprise as people were at home; children were on social media, parents were shopping on Amazon, families were binge watching every show possible and everyone was using Google trying to stay up to date.

But what about other companies neglected during the pandemic? As we started to turn the corner on the virus, other companies have started to perform well over the past six to nine months. Smaller, more economically sensitive companies that had more challenges during the pandemic, but managed to survive, have seen a resurgence as economies around the world have started reopening. Over the long term, investors look for value and they have been finding good companies at relatively cheap prices to put into their portfolios. This has led to markets making new highs which have some concerned. The good news is that corporate earnings have rebounded and are starting to justify their valuations. With more stimulus money potentially on the way, along with the money that has yet to be spent, valuations may not be as overvalued as some may think if we are looking forward to the next 12-18 months.

This leads us to the next question and something we have started seeing signs of, "what about inflation?" With all the money injected into the economy should we expect inflation to be here to stay? Food prices are up, housing prices are up, car prices are up, just about everything seems more expensive. Whether this is temporary inflation or long-term, we don't know. Once most of the supply chains around the globe get back up to speed, it's possible prices may come back down, but in some industries, higher prices may persist for an extended period of time.

What about low interest rates? Well, for companies and consumers who want to borrow, it's great; for those who depend on fixed income to live, it's bad. When you throw in higher inflation, it's even worse for investors who are dependent on fixed cash flows since they are less valuable as inflation decreases their purchasing power.

With that as a backdrop, as an investment advisor, I am constantly asked, "what should I do with my portfolio?" Regardless of the economic environment my answer is always the same, "Have a long-term plan and stick to it." One can never predict the future. Build a diversified "all weather" portfolio that is poised to do well over the long term, regardless of the economic environment and most importantly, is commensurate with the level of risk with which you are comfortable.

The graphic below shows the various types of investments and the different roles they plan in the portfolio.

Maximize Return at an Appropriate Level Of Risk

Role	Growth Engine Support spending needs while maintaining corpus over the long term	Diversifiers Mitigate volatility while attempting to improve risk/return profile	Inflation Sensitive Stable value or appreciation in rising inflation environments	Deflation Hedge Stable value or appreciation in economic contraction (e.g., deflation), flight to quality
Examples of Asset Classes	• Global Public Equities • High Yield Credit – Public and Private (Illiquid) • Private Equity	• Low Correlated Hedge Funds • Absolute Return-Focused managers • Reinsurance • Floating Rate Corporate Loans	• Midstream Energy • Infrastructure • Natural Resources • Real Estate	• High-Quality/ Intermediate-and Long-Term Fixed Income • Cash

Every investment in the portfolio is not going to go all up or all down at the same time. If it does, your portfolio is not well designed. By nature, some parts of the portfolio are going to disappoint because the environment is not conducive to that asset class. Economic factors are constantly changing and having a good mix of each category should protect you from large losses, while still earning a desired return regardless of the economic factors at play. This should help you to achieve your long-term goals – even in unprecedented times! ■

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