Flash Market Update 29 November 2021

Omicron

Everyone is talking about how markets sold off last Friday on news of the omicron variant. First, let's put the market move in perspective: Equity markets (S&P 500) declined 2.2% on Friday, and are rebounding today.

Why did markets drop?

When you have the market at record highs, any bad news will be used as an excuse to sell. This was a classic case of greed meeting fear, and because there was extreme greed, it was easy for fear to win.

Fear also won a few other battles this year. In January, markets dropped 2.6% on fear of the Fed turning hawkish. And in September, they dropped 2.6% on fear of China. Anyone who exited after the drop in January would have passed up on 24% subsequent gains in the S&P 500. While we do not encourage short term assessments, someone exiting in September would have left 5% gains on the table net of Friday's 2.2% decline. Fear may win a few battles but not the war.

We have also mentioned that markets do not go up in a straight line. Under most market conditions, we expect markets to appreciate like a bunny hopping upwards. Friday's decline is such that the bunny has not even landed its latest hop compared with the hops we have experienced in January and September. Going through volatility is to be expected, and given there has been a streak of 7 positive months this year, the recent declines should not be a surprise.

Source: Bloomberg

That is the logical and non-emotional way one should treat investing. But we know that is a tall order. **It is a natural human propensity to amplify the bad, and understate the good when fear kicks in**. This is basically loss aversion at work; the response to losses is stronger than the response to corresponding gains. It took Nobel prize winner Daniel Kahneman to formalize this phenomena but unlike other Nobel prize research, not many are able to take advantage of it.

Daniel Kahneman's work on loss aversion was not targeted on investing. It was about how humans (and monkeys) make flawed decisions by feeling the bad more than the good. As the world is now working to learn more about omicron, there are a few identified characteristics: aggressive, milder, less lethal. It would not be a surprise that people single out "aggressive" and respond to it, while underappreciating that omicron is milder and less lethal. Who knows one day, omicron might even be overlooked like the common flu?

We are not trivializing the impact of omicron. In fact, the world has a very recent reminder about the impact of viruses from last year. **There are two possible scenarios**

1. **Omicron is not as serious as feared** for which our portfolios are well-positioned in terms of benefitting from economic expansion. We have maintained that the journey would never be smooth, and this is one of the bumps on the road. At the same time, **we are diversified to manage these bumps through our healthcare exposure.**
2. **Omicron turns out to be a black swan event** that triggers another bear market. Our FAM series is structured to benefit from growth while maintaining diversification using healthcare and alternatives to ride out a bear market. For investors who are really concerned about omicron causing another bear market (or any future bear market), the Meranti funds with dynamic risk mitigation allow them to stay meaningfully invested while addressing the losses from a market crash.

Actually, if omicron is really going to kill you, it may be better to check that your finances are in order. Ensure that you have sufficient insurance to pay medical bills, and coverage that pays out enough so that your family's needs are met. So ensure you are adequately covered, and invest the rest.

It is natural for ongoing news to instill fear in investors, nevertheless they will do themselves a disservice by succumbing to those fears and bailing out on their investments. That is why we keep emphasizing 'prepare, don't predict'. If we are prepared, other people's loss aversion will be our opportunities.