

Demystifying Investment Myths



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MYTH 2: New high means the stock market is going to crash

It must seem odd that I will talk about market highs when clearly the market has been volatile and suffered the consequences of the current geopolitical turmoil. However, this so-called “fall in the market” has given several investment gurus the validation they needed – as per their prediction the “market reached a new high and crashed”.

The reality is that markets do reach highs all the time and of course one of those is going to be the high before the next fall, or “crash” if you prefer. Here is the data from the US Markets, over the last 100 years or so the market reached a high every 20 days.

Number of days market reached a high in past decades

Decade	New Highs
1950s	141
1960s	224
1970s	35
1980s	190
1990s	310
2000s	13
2010s	241
2020s	102

Data: Yahoo!, My Calculations

(Source: Ben Carlson, A Wealth of Common Sense)

Investors' “Record-High” anxiety is fuelled by the financial journalist reporting, often indicating that the Laws of Physics apply to financial markets – i.e. gravity applies to all physical things and what goes up must come down.

The news headlines often propagate this thought, here is a sample of some of the headlines:

“Stocks Head Back to Earth,” Wall Street Journal 2012 1

“Weird Science: Wall Street Repeals Law of Gravity,” Barron's 2017 2

... low-interest rates have “helped stock and bond markets defy gravity.” Los Angeles Times 3

This can cause some investors

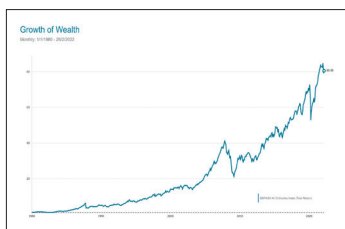
to shy away fearing an imminent crash and the fear of buying stocks at their peak.

But shares are not physical objects that are kept propped up with some effort or support.

It is important to remember what drives the prices of shares – the prices are based on the expected earnings and dividends from these companies.

If the expectation is that a company will continue to grow and be profitable, given there are thousands of business managers and employees who go to work each day to work on projects to produce goods and services that are of value to us, the share price will reflect this and rise.

Of course, there will always be some companies/ideas that may end in failure but as the chart below indicates, the markets will tend to reward investors for their capital:



A new high or low for that matter should be treated with neither excitement nor alarm but as an indication of the collective judgement of the market on what the earnings and returns for tomorrow look like.

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