



Principle-Based Investing

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Introduction

Investing is a long-term endeavor filled with uncertainty, but history provides valuable insights into market behavior. The following time-tested principles are based on decades of market performance and investor behavior. Our premise: short-term predictions are useless; principles must guide us. Here are my highest-conviction principles that I believe should guide investor decision making.

Don't Play Politics with your Portfolio

Politicians are temporary. Fundamentals are enduring. No matter how bad it gets, the republic will survive. Whenever politics are discussed, emotions will run high. However, the economy will likely continue to grow over the long term no matter who is in charge because the fundamental strengths of the U.S. economy will most likely remain in place. Every day in America, including the day after each election, approximately 160 million Americans get up, and go to work. And those workers produce more than \$30 trillion in annual economic output each year. Corporate profits, which belong to shareholders, will likely continue to grow, leading to an increase in the value of share prices, which comprise the stock market. A portion of those earnings will likely continue to be distributed to shareholders in the form of a dividend, all of which reinforces the value of staying invested. Now if you don't believe me, think about this: That \$30 trillion gross domestic product number I mentioned, which is the value of all goods and services produced annually in the U.S., was just \$13 trillion in 2005. Since then, we've experienced the worst financial crisis since the Great Depression and a global pandemic that literally shut down the global economy. So, if someone tells you it's time for you

to make drastic changes to your portfolio because so-and-so is running the country, just respond with this simple phrase: The republic will survive.

Maintain a long-term perspective. Short-term predictions are useless

It's almost always a mistake to make a long-term investment decision in reaction to short-term events. Short-term predictions are useless. Maintaining a long-term perspective is essential to investment success and allows us to remain calm in times of trouble. Time is an investor's greatest ally. Emotion is his greatest enemy. Knowing and understanding the lessons of history gives us confidence and provides a guidepost to make well-thought out investment decisions. To be prudently hopeful, or sensibly optimistic in difficult times is not casual or careless, it is a strategy that has won the day, time and time again.

Experts are notoriously bad at predicting the market. Research by Trivariate Research published in the FT on March 3, 2025 indicates that, over the past 24 years, stocks highly rated by analysts have underperformed the overall stock market, while those with lower ratings have performed better. Researchers Campbell and Moore, in a paper titled, "Overprecision in the Survey of Professional Forecasters" analyzed 16,559 predictions of major U.S. economic indicators in The Survey of Professional Forecasters, the collection of forecasts that has served as a kind of national benchmark since 1968. They found that forecasters reported 53 percent confidence in the accuracy of their forecasts but were correct only 23% of the time. Despite this evidence, investors pay close attention to media pundits, many of whom are chosen for their delivery rather than their accuracy.

A long-term bet against the U.S. stock market has almost always been a bad bet

The odds of market growth increase over time. Historical data supports the notion that staying invested is a winning strategy:

- 74% of calendar years since 1926 have seen market gains.
- 83% of three-year periods have been positive.
- 88% of five-year periods have been positive.
- 94% of ten-year periods have been positive.

The only two negative ten-year periods were during the Great Depression and the Great Recession. A bet against the U.S. stock market has almost always been a bad bet.

Market Declines are a Normal Part of the Investing Process

Stock market corrections are normal. Since 1900, there have been 125 corrections of 10% or more, averaging more than one per year. Even during the strongest market periods, pullbacks are common. Here's what you should know about market declines:

Market declines are normal, frequent and not a reason to sell quality investments

Market declines begin and end without warning

Market declines can be the long-term investor's best friend, because they can give you an opportunity to buy good investments that are lower in price

If you can't predict market declines, you must prepare for them. The best way to prepare is to own high-quality investments in a diversified portfolio you can buy and hold for the long term.

From 1980 to today:

- 75% of years had positive returns.
- 58% of years experienced a 10%+ intra-year decline.

Once market declines have run their course, there are usually two types of investors. Those who say, "I wish I had." And those who say, "I'm glad I did."

Time in the Market is more important than Timing the Market

Historically, investors tend to panic during downturns, selling at the worst possible times. Consider this:

- \$10,000 invested in the S&P 500 in 1980 grew to over \$1.2 million by the end of 2023.
 - Missing just the 30 best days would have reduced that to \$212,000—a loss of nearly 80%.
 - The best-performing days often occur during bear markets, when investor fear is highest.
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The key to surviving market declines is not predicting them, it's having a sensible plan in place before they happen.

Investment management is not just about earning high returns. It's about earning competitive returns and managing risk. Investors should only own investments today that they'd be comfortable holding in a market decline tomorrow. The best way to withstand volatility is to maintain a well-diversified, professionally managed portfolio that aligns with risk tolerance. Most investors overestimate their risk tolerance when markets are rising and panic when they fall. The right asset allocation is the one an investor can stick with through good times and bad.

Bad News Will Be Exaggerated, and Most of It Won't Matter in the Long Run

Financial media thrives on sensationalism. While surprising news events will emerge, most short-term concerns will fade into history. Two university professors, Robert Lichter and Ted Smith researched 17,000 economic stories broadcast on the three major networks – ABC, CBS and NBC. Do you know what they found? The networks convey a relentlessly negative view. The professors found that roughly 85 percent of economic news stories “had a negative tone.” In fact, the professors found that the highest periods of negative reporting came when the economy was expanding! Their findings were published in an article titled, “Bad News Bears” in 1993. Investors should focus on controllable factors, such as

asset allocation, diversification, the quality of their investments, and investment costs rather than reacting to headlines.

Most stocks are losers

Stock picking is much more difficult than most people realize. A handful of today's companies will keep pace with the overall stock market, many more will not. According to a research paper titled, "Do Stocks Outperform Treasury Bills?" conducted by Arizona State University professor Hendrick Bessembinder, only 4 percent of all publicly traded stocks outperformed the paltry return of a one-month Treasury bill since 1926. He found that, of the 26,000 stocks that appear in CRSP's database, just 86 provided half of the aggregate wealth creation, 282 were required to reach 75%, and 983 account for the full 100%. That's it. Less than 1,000 winners, and 25,000 losers. Many of today's most popular stocks will likely underperform in the years ahead, while today's out-of-favor stocks or companies that have yet to be discovered may be tomorrow's leaders. The same applies to countries, asset classes, and investment styles. The lesson is clear: In order to be a successful stock investor, your portfolio's diversification must be wide and broad. A few dozen stocks will likely not be enough. Hundreds if not thousands are much more preferable. The best way to achieve this diversification is to own mutual funds or exchange traded funds that have a healthy dose of stocks that across multiple sectors and industries, including smaller companies that might be tomorrow's winners.

Conclusion: Principle-Based Investing Will Prevail

Despite endless predictions of market doom, the principles of discipline, diversification, and patience have consistently rewarded investors. The market will have its ups and downs, but history shows that optimism, long-term thinking, and staying the course are the best strategies for wealth accumulation.

Final Advice: Stay invested, stay diversified, and focus on the long term.

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