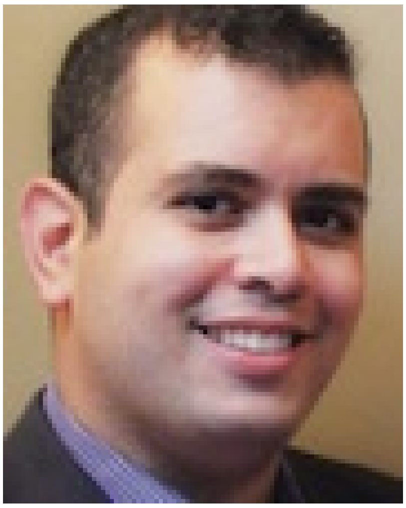
'A Dangerous Time in History'

By Michael Gayed *Thu, Feb 23, 2017*

The current investment narrative is based on the assumption that Trump will be a reflationary president, says our guest columnist, the chief investment strategist at Pension Partners LLC. He urges us to start questioning our news-based assumptions.



We have entered a dangerous time in history. A time when the truth changes every day.

The amount of misinformation being spread daily is nothing short of remarkable. It seems like everything is "fake news" now, independent of who reports it. Rather than seek out the truth, confirmation bias results in the spreading of lies with little thought as to whether one's existing beliefs are rooted in reality, or are complete fantasy.

What is worse is that the speed with which this misinformation is spread trains our brains not to use Kahneman's "System 2" part of the mind (which is analytical). Rather, everyone now simply reacts and moves on to the next distraction.

What does any of this have to do with investing? Absolutely everything.

At some point, the market prices in the actual truth, but only after overreacting in both directions. In between those two points, buy and sell decisions are made based on reactions not only to the recent past, but also to the narrative constructed around it. It is far easier to react to something that sounds like it makes sense rather than to think about nuance—or even ask if the information presented is fiction or non.

The narrative now in the investment community is remarkably void of any questioning of logic, or of any actual information. Interest rates will only go up, stocks will only go up, inflation is going to skyrocket, and volatility is going to remain historically low.

Why does everyone believe this is the future? Because interest rates have already gone up, stocks have already gone up, inflation has already gone up, and volatility is historically low.

The narrative reacts to what has already happened, and spreads like wildfire across the media. Investment decisions are then based on the story, rather than the fact that meanreversion dictates the exact opposite.

Yes, rates may go up, stocks may go up, inflation may skyrocket, and inflation may go up. But realistically, it is hard for any of these to continue the way investors believe.

Why? Because the narrative is predicated on Trump being a reflationary president through tax cuts, infrastructure spending, and regulatory reform.

My biggest problem with this is that 1) Seemingly everyone believes that this is a certainty, and 2) Seemingly no one is addressing the not-so-alternate-fact that the current fiscal year-end 2017 US federal government debt is estimated to be $20.1 trillion. And that's before any new legislation is passed. If Trump has his way, the size of that debt will explode.

Somehow, disturbingly, no one is discussing the potential that tacking on even more government debt is long-term deflationary (see Japan), represses long-term growth (since you're pulling it forward), and tends to increase overall asset volatility.

But who cares, right? Someone says something we agree with that confirms our own biases and beliefs, and it only reinforces our belief that what we think is true. Independent thought is impossible when we're inundated with information that confirms what we think, rather than what is actual reality. And when those beliefs are proven false, a new narrative is constructed to fit a new set of beliefs—which are again based on recent events.

We must, as investors (but more importantly as members of society), stop changing the truth to fit the moment. We must stop reacting to every bit of information and instead make sure the information is valid. We must stop believing in false narrative. Perhaps most importantly, we must stop doing this to ourselves.