CHIConomics, Intro Pod Transcript

Chloe Mintz: Hi there, this is Chloe Mintz, one fourth of CHIConomics. I apologize, my voice feels a bit raspy at the moment, but I'm bringing to you one of our, I'm going to say, first pseudo podcast episodes for our CHIConomics site. So, I'm going to be bringing in my dad. This is, in fact, reverse nepotism because this just might be his big break. Just kidding. But anyway, I'm bringing in my dad, who is a financial advisor, particularly a portfolio manager for mid-cap stocks, which are mid-capital companies that people invest in – anywho… we're going to be talking a little bit about what are some good tips for new investors, particularly our demographic, which is the girls, the gays and theys? But really anyone who's been traditionally excluded from the financial sector and how they can get involved themselves and feel a bit more included and start taking control of their financial life, if you will. So very excited to be here; let's go ahead and get started.

CM: Question number one – are you rolling? – Okay. What advice do you have for new investors, particularly the girls, the gays and the theys? Those who are traditionally excluded from–

Eric Mintz: You know, I don't think investing necessarily. I think everyone's well, I guess if you have certain, you know, ideals that you want to align with [for] companies that you invest in, I guess you should research the companies that you think are consistent with your social beliefs. If your goal is to maximize the returns on your investments, then that necessarily wouldn't be the top priority, I guess. So I don't really follow too many, I guess, ESG related strategies. And I think there's a thing that's pretty popular, at least with the ESG movement that we had a couple of years ago that was called greenwashing, where they were saying that they were aligned with certain philosophies over environmental concerns and such, and actually the investments that were being made were contradictory. So, yeah, really – you really need to be leery of Wall Street and just people that try to package things as a certain strategy or products without making sure that it actually adheres to what you believe those principles are. So that's a little trickier. I'm sorry if I didn't answer this question directly, but it's definitely like a little trickier lay of the land to make sure what you're actually getting in a packaged investment from Wall Street is what it claims to be. So I guess just in general, anyone starting a portfolio, I think more broadly, you know, they say you need to be concentrated, i.e. have a lot of your money in, you know, a single stock or something to build a lot of wealth. And that's true, but you can also lose a lot of wealth. So I definitely think that one of these ETFs, exchange traded funds, which actually is a basket of companies, is certainly a really good starting point. And obviously there's a tremendous amount of money in the S&P 500, but the problem with the S&P 500 right now is that it's heavily concentrated in a handful of securities. We've never seen this type of concentration. These big five mega-cap tech companies are about 40% of the actual S&P 500. So that's something to be concerned about, I guess, to some extent. But, you know, actually, I do like mid-cap stocks.

CM: Can you define that?

EM: Those are companies that are kind of in that their market capitalization, which is the share price times, the shares outstanding, the equity valuations, the market caps of those companies are probably, the median would be about $20 billion. But the range actually can vary a bit. The low end would probably be $10 billion going up, although the largest company in the benchmark currently is [unclear], which is $150 billion. That's another thorn in my side. Ideally, a company is about a $20 billion market cap that has a really good growth trajectory and is going to become the next, you know – it's an interesting asset class, mid-cap stocks, because a lot of people focus on large cap and [they assume] they will have some allocation to small cap and they will just assume that their small cap manager actually kind of shoots up into the mid cap realm and that the large cap managers will shoot down into the mid cap realm. So they almost would have it covered. But I actually don't think that's the case currently because of that concentration with those mega-cap tech companies in the large cap benchmark. I think a lot of people are in those names. I definitely think it's actually one of the best things about the mid-cap. Yeah. Returns overall. I think they historically have done better than small-cap even during the up years, but they don't have these as severe of a drawdown. when the market goes down. And small caps can go down like 30 or 40%, and mid-caps have maybe gone down 20% recently. And obviously everything can change. These are just historical returns, but it's been a bit better of an asset class that you do get the upside without as much of a drawdown which you will go through. So that's kind of the group that I think would make sense for somebody looking to buy an ETF. You could just buy the Russell MidCap ETF or Mid-Cap Growth ETF or mid-cap value ETF. And that would be a good spot without having all that concentration in those mega-cap tech stocks.

CM: If these new investors were unable to afford a financial advisor, are there any apps that you'd recommend that they go to that it's easily accessible?

EM: Yeah, I don't, I don't really know too many apps but I definitely don't think you – I don't think you need a financial advisor, honestly. It's because these ETFs had such low fees. Whoever charges the lowest commission and then the lowest – yeah, I don't think you would need to, you just need a discount broker. I don't know. I guess that's like a Schwab or something. I don't even know, actually. I'm sorry. Fidelity – Fidelity probably has a very low no-fee account. Yeah, you don't need to have an advisor. I think that advisors basically hold your hand when stocks inevitably go down. Okay. But the easiest thing to do is just not to look at it when things go down.

CM: That's really good advice

EM: You know, it's funny, I feel like everyone says, "Oh, real estate is such a great investment class." People, you know, own all this real estate property that has done so well. And I guess the majority of wealth is built on real estate, and for real estate, you know, you use a lot of leverage, meaning people, you know, take on debt to get things, you know, to buy things. And then they don't always sell when the market crashes, you don't necessarily have to sell, even after the event we saw during like the big financial crisis in '08-'09, the housing thing, like a lot of you know the so-called "pretend and extend" where they didn't really – I mean, they did close out a lot of, you know, non-performing loans but a lot of people got away with some stuff there. So anyway, the point is, if you can't really see the price dropping, you don't know how bad it is, then you just kind of forget it, especially if it's an index fund, if it's like a single stock and maybe there's like a, you know, an existential threat to the company and it's going to go out of business or something. Or you can get like, like Peloton right? One where the stock got completely clobbered and you just kind of forgot about it. And now look, it's come up. Good for you!

CM: Good for Peloton. And I think, looking at the current economic climate, do you have any insights as to how that might be changing our opinions of investing or advice there?

EM: Well, I think there's a couple of things here. Right. So, one, the economy, the stock market is not the economy.

CM: Right.

EM: That's, like we've been in bad economies and the stock market's done great. We've been in good economies and the stock market's been kind of terrible. And it's all about expectations of what the future is going to hold. And, you know, right now, obviously, stocks are at very high levels and there are people who have a very optimistic view that we're not going to go into a recession in the next 12 months. And I think, you know, in any given year, the odds of going into recession are about 20%. So it's probably a little bit below that. But people, you know, economists are wrong all the time. So it's a little bit tricky, to, you know, put a lot of weight in these economic forecasts. But the one thing that I do, that I find especially interesting right now is this idea that the Fed is cutting interest rates. So interest rates are going down. And, yes, the Fed has cut the Fed funds rate twice so far, once for 50 basis points, once for 25 basis points. That's 75 basis points. But at the same time, the ten year Treasury yield has actually gone up and that's what kind of drives mortgage rates. And that's a big, that's a huge deal. That's a much bigger deal in my mind than the Fed funds rate. So it is an interesting environment because people are like, "oh, the interest rates are going down," but they're actually the most important part of the curve. For, a lot of investment is actually going up. So that's, that's kind of a weird dynamic in the current environment. I can't recall, necessarily, the last time that happened. So anyway, that's unique. But you know, for investing, it's, really, you have to understand that it's not, you know, the economy. And actually it's probably when the economy's in its worse shape, that's when it's absolutely the time to buy stocks – actually, the best time to buy a stock is when the market is forecasting a recession, i.e., stocks are down 20%, and there is no reason we avoid the recession. Those are like the best buying opportunities and clearly we're not faced with that and we may not be faced with that type of opportunity in the next 12, 24 months. I don't know. But that's really the sweet spot of making timely investments. So without that real necessary opportunity, what they do – [here's] a good strategy: if you have money and you want to invest, it is what they call dollar-cost averaging. So just put a little bit to work every month over the next 12 months and you know, you'll come up with various prices, hopefully the average effect of that will – a relatively good price to build on from there if you're not seeing, you know, a highly compelling entry point in the market overall right.

CM: But for an average like expense allocation, like per month, is there a particular amount that you would recommend, or is that just particular to each individual?

EM: It's definitely particular to each individual. But I think, you know, and hopefully you've learned this, there is obviously – the effects of compounding are so significant. Compounding, meaning building on the gains,

CM: Like 2% to 5%

EM: Yeah. If you put in, you know, $100 last year and it was up 25% and then $125, and then it's up another 25%. Now you're going to make more than $25 in gains in 2024. So that's – the best thing to do is to, especially when you're at a very early age in your career and everything, is to get as much money into the market as possible.

CM: I guess this question is more for me, but how contingent is, I suppose, like the wellbeing of the market and the economy dependent on or contingent upon consumer behavior as opposed to economic policy and initiatives?

EM: Yeah, that's a good question. I think you would say broadly that a good stock market is indicative of good, overall, what you would consider would be financial conditions, healthy financial conditions. And certainly the stock market is a good barometer for consumer confidence overall. And obviously, a lot of people have money in 401ks and various retirement savings plans that, you know, they do get a boost of confidence when they see those assets performing well, so it is very important. And it's almost like a, you know, it's, I don't want to say a virtuous cycle, but you definitely need good asset prices and you don't want things to be too crazy. And I mean, like this cryptocurrency stuff – I don't have a great feel for it. But obviously there's signs of excesses and things that, you know – excessive risk taking. Right. That's not, those don't [typically] end well. And that is a concern that when you see something get a little out of hand, that it could lead to a pretty severe correction in those asset prices that will then feed on itself and lead to a retracement in consumer spending, because consumer spending is such a significant overall percentage of GDP in the U.S. economy.

CM: Right. Thank you so much.

EM: Ask me another question.

CM: Okay, I do, actually, have another question – but just in case this was not going to be helpful – I was kind of confused by, we were talking about the Fed rates, and you were saying that this other rate, the Treasury bond, the ten year Treasury bond, was more important. Is that also affecting inflation or is inflation more so like a product of the federal funds rate?

EM: That's a great question. So this is all about the yield curve, right? So the Fed controls the overnight rate, right, that lends to banks. Right. And they tried to, and I think they did to some extent, go out and actually buy in the open market longer maturity securities like these ten-year, five-year maturity [rates] that did actually help bring down the interest rates on those, on that part of the curve. To some extent, I don't know how meaningful it was, but by all means, the ten-year yield is influenced by expectations for inflation, expectations for economic growth, and kind of a flight to safety, if you will. Yeah, so the Fed cuts rates [and] people think growth is actually to stimulate the economy because you've got that faster growth and they think inflation is going down. They might think it's going, I don't know if they think it's going down necessarily, but they don't think it will, hopefully, they don't think it's going to go up significantly – so because they think it's manageable and it's getting closer to the target, that kind of pushed up the ten-year rate [that] growth component to it. So I guess the comment kind of comes back to how do you want to unpack? And there are various ways of analyzing the yield curve and what is moving the ten-year treasury? The ten-year treasury is significant because it really is your, quote unquote, risk free rate of return that you would kind of value, uh, you know, all other assets off of. And it is the product that, I guess, most directly influences mortgage rates. And so because the tenure has gone back, mortgages are a huge deal because housing is such a huge [deal].

CM: I guess I am also confused as to why I think the – if we're expecting the economy to, or for there to be more stimulation in the economy, why would mortgage rates still be going up? I feel like mortgage rates go up when you're of the opinion that the person buying the mortgage is not going to be able to pay off the mortgage at a particular time. So they have these higher interest rates – but assuming there's like stimulation in the economy…

EM: Yeah. That's you know, you're right. So for certain, depending on what your credit score is, if you have a poor credit score, [and] you can still get a mortgage, the mortgage rate is always going to be higher than, let's just say, the national average – and I'm just using the national average, which I think is, you know, close to 7% for a mortgage rate – so excluding the idiosyncratic credit dynamics of the individual borrowers, the national average for a mortgage is half, is still higher than it was before the Fed started cutting interest rates. So now we're thinking growth is going to accelerate and because growth is going to accelerate, the ten-year treasury goes up, and it's almost it's like a modulation – [or] almost like a self-correcting – but it's a weird dynamic because that's kind of, that's the more important throttle on the economy. And it almost raises the question of "do you really need a Fed and what is the Fed actually doing?" Because honestly, I mean, if you think about the most credit sensitive areas of the economy that the Fed should, quote unquote, be able to influence would be mortgage rates and, you know, auto loans. I mean, those are the big things. And I think since they started cutting, both of those rates have gone, actually, up so... And I think, you know, I think there is a dynamic there, too, where you've got people thinking that, you know, this new administration coming into the White House is, you know, going to be pro-growth and that would also lead to higher interest rates. And by pro-growth, I mean, you know, reduce regulatory things and move the economy.

CM: So how would that be raising interest rates?

EM: Longer term interest rates would go higher on the prospects for faster GDP growth. Does that make sense?

CM: I think so. Like because of the growth in the economy, to like curb a bubble or like a peak or anything like that, that's why interest rates go up, to manage the stimulation in the economy.? So there's not too much action?

EM: Yeah, I, you know, I think that's a good way of looking at it, but I don't know if that's necessarily exactly what's happened, but it is to some extent. Yeah, no, I think that's right. I mean, like, what would you say? You're going to loan the government money for ten years, what would you expect them to pay you in interest? It's a really good question.

CM: Well, it depends on how much I'm lending..

EM: $100

CM: Okay, 2%.

EM: 2%?

CM: I want to keep it really low for them.

EM: For the next ten years, you will get $20 [total]. That's not good. I mean, that's what it was before. It was like 50 basis points at one point. I think it was ridiculous. It's crazy. And for some countries, there's been negative interest rates, you have to pay them. Oh, goodness, that was a crazy time.

CM: I have two more questions – and they're kind of, I'm trying to visualize the graphs that we [made] in my head – but [for] the first one, I was looking at either at the FRED or the Bureau of Labor Statistics, like their online data portal, and I was looking at the CPI indexes. I was looking at all items in U.S. city averages, then services and commodities and the inflation rate for services and all items had gone up whereas commodities had gone down, like relative to – I think it was September 2024 to October 2024. I just didn't know why that was.

EM: Commodities are really a global phenomenon, and especially oil and especially influenced by China, which has been pretty weak in the economy overall. So that is one of the big components of commodity prices going down. Services inflation really is a U.S. labor market dynamic. And, you know, we've got very low unemployment even now. It's gone up a bit, but it's still, you know, 4% or something. The labor market is pretty tight and people, you know, need to pay for all the other things that have gone up significantly, like the rents and the grocery store and all that. So, yes, gas prices are down and a lot of like steel, a lot of commodities are down, but wages are still kind of pushing higher and people are, you know, dealing with, you know, like the rate of inflation has kind of peaked out, but the actual overall price index is still at a very high level.

CM: I see, I see. Actually, that does make sense to me, though. And I'm looking at our other graph. We're looking at the rise of ETFs relative to mutual funds, how a lot of people were investing in mutual funds for a time, but now they've transitioned to like ETFs. Can you explain that?

EM: It's tough to beat the market, right? It's kind of – so why would you pay an active manager, somebody who's trying to beat the market, you know, a 50 basis point annual fee when you could invest – and they don't beat it – when you can just invest in the ETF, that charges five basis point fee and they will beat it. I shouldn't say "they," it's the computers.

CM: That actually makes me really worried.

EM: It is very worrisome. It is kind of crazy. I'm like –

CM: What job are you going to have?

EM: Yeah, what job are you going to?

CM: All right. But that was all they had for you.

EM: Oh, thank you.

CM: Thank you. That was really insightful.

EM: I enjoyed talking to you.

CM: I enjoyed talking to you.