



March 2024

You've got to know when to hold 'em

“When we own portions of outstanding businesses with outstanding managements, our favorite holding period is forever. We are just the opposite of those who hurry to sell and book profits when companies perform well but who tenaciously hang on to businesses that disappoint. Peter Lynch aptly likens such behavior to cutting the flowers and watering the weeds.”

-Warren Buffett, [1988 Berkshire Hathaway Chairman's Letter](#)

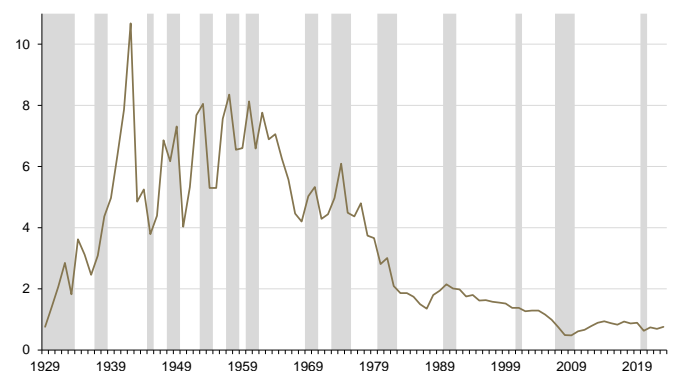
The speed with which news flows into the marketplace these days is astounding, with a wide array of sources providing investors with unprecedented access to information, which can be used in decision-making. The unfortunate reality, however, is that the vast majority of the material entering the fray is nothing more than noise. In the short run, market movements can be dominated by that noise rather than any true signals, which can cause financial asset values to become detached from their underlying fundamentals — the actual fundamentals of a given company change nowhere near as frequently as its equity price.

Investors, however, have increasingly adopted a short-term focus that can result in missing seeing the forest because the view is obstructed by the trees. This is evident by the fact that the average holding period of a stock listed on the New York Stock Exchange (NYSE) has been steadily declining over the last 70 years, with equity holdings now being turned over roughly every eight

months, compared to eight **years** back in the 1950s and early 1960s.

Shortening investment time horizons

(New York Stock Exchange average stock holding period*; years)



*Average holding period is calculated as the inverse of the NYSE Group turnover ratio; shaded regions represent periods of US recession; source: Guardian Capital using data from the New York Stock Exchange and Ned Davis Research¹ to December 31, 2023.

A big reason for this shift is that many investors are less focused on long-term investing and more on short-term trading, seeking to exploit these short-

term dislocations by timing the market for a quick profit. Since equities tend to move together over short periods such as a day or week, these types of trading decisions are “low conviction” concerning the specific stocks involved instead of seeking to either capture or avoid market beta.

These types of company-agnostic strategies can be profitable since catching the stock market's upswings generates positive returns while avoiding the downdrafts would result in improved performance beyond the broad benchmarks — indeed, some high-turnover algorithmic trading strategies have found success with this tactic.

In general, these short-term trading strategies can be fairly low risk, and, with that, the magnitude of the upside of an individual trade is small — high-turnover strategies are typically focused on a high volume of low-return trades.

Research² has argued that there are larger profits to be made by pursuing longer-term opportunities since such investment strategies are being chased by fewer investors and their money.

Of course, longer-time-horizon strategies are inherently riskier since, as John Maynard Keynes once said, “*the market can stay irrational longer than you can stay solvent*” — mispricing can become more aggravated in the short run, forcing investors out of positions before the investment pays off.

Calling a peak or trough in the market is exceedingly difficult, and doing it consistently is near impossible. The unfortunate truth is that the public's investing decisions are typically driven by emotion, which leads to chasing momentum — a strategy that often results in buying the most at the top of the market and the least at the bottom.

Further, one of the most common mistakes investors make is selling at the bottom and turning paper losses into realized ones that permanently impair portfolio capital.

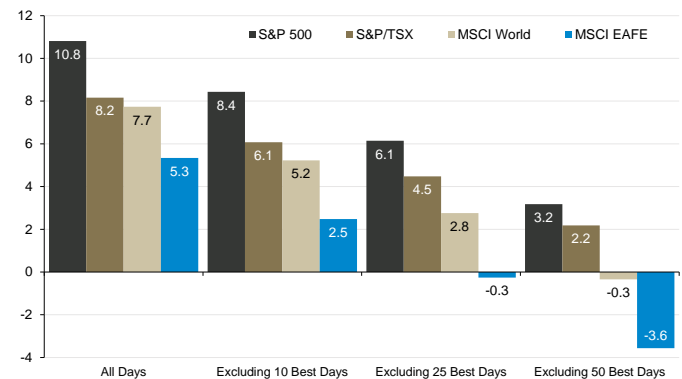
Timing the market is a double-edged sword since it not only requires determining when to sell but also when to buy. Even being a day late rejoining the party can have significant negative performance

implications. Sitting on cash means that investors find themselves on the sidelines when markets recover, failing to participate in the bulk of a market rebound that historically occurs early (and quickly) following a correction.

Research³ has also shown that as much as 96% of absolute return in the market is accounted for by just 1% of trading days, roughly equivalent to an entire year's performance being driven by just three days.

As an example, missing out on just the 10 best-performing of the nearly 10,000 trading days spanning the last three-and-a-half decades reduces annualized returns by more than 200 basis points. That means that \$100,000 invested at the beginning of 1988 would be worth 50% less now strictly if those top 10 days were missed compared to staying invested thanks to the power of compounding.

“Time in,” not “timing,” the market is key
(Equity market⁴ average total return; annualized percent change in US dollars)*



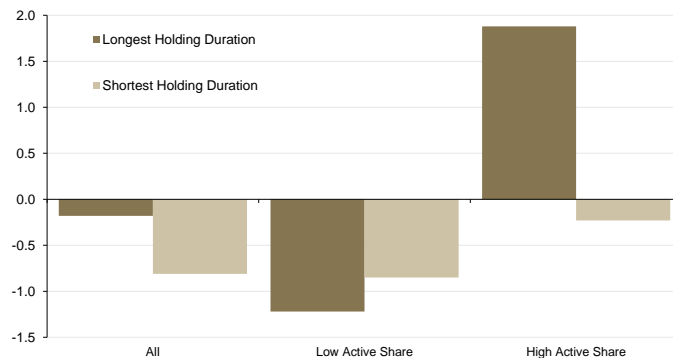
*Based on daily data from January 4, 1988, to December 31, 2023; source: Guardian Capital using data from Bloomberg.

This serves to emphasize the importance of “time in” rather than “timing” the market for investors with longer horizons. Markets have historically shown that they rise more often than they decline and ultimately increase over time, and thus it is more important to participate in market exposure for the many good days than trying to avoid the few bad days.

Further to this point, research⁵ indicates that portfolios that had the longest holding duration for stocks (lowest turnover) outperformed those with the shortest holding periods — and when these longer holding periods were paired with high active share⁶, they generated excess returns of nearly 200 basis points or 2.0%.

Skill and conviction yield the best results

(Excess net returns of US mutual funds, 1990 to 2015; annualized percent change in US dollars)



Source: Guardian Capital using data from Cremers⁴ (Table 2).

In other words, it usually pays to have a skilled investment manager who maintains a disciplined, long-term approach to investing and is focused not on “active trading” but “active management.”

This finding should not be a surprise. True active portfolio management is about focusing on best idea stocks that are believed to have the greatest prospects while eschewing those that appear to offer less upside to generate returns in excess of the broad market. Such a focus on a concentrated number of high-quality stocks requires skilled portfolio managers to have a deeper understanding of each company they own and the underlying drivers of the businesses, meaning that they are better able to differentiate the noise from the signal.

These portfolio managers approach such investment holdings from the perspective of long-term buyers of a business, not as short-term traders, and have a high conviction that the companies the portfolios own can thrive no matter the market environment. As such, they do not typically panic and sell in times of broad-based market turbulence, like a correction or even during

bear markets, instead, they view these periods as opportunities to build positions at even better prices, thus setting themselves up well for the time when markets recover.

This “private equity” approach to public market investing means that portfolio managers look through short-run fluctuations in their holdings’ market prices with the conviction that the investments will ultimately fully reflect their intrinsic values resulting in long-term rewards — again, something evident in the historical outperformance of those mutual funds that have been actively and patiently managed⁵.

On top of the positive performance, another benefit of having an investment horizon measured in years or decades rather than days or weeks is that it means transaction costs are kept low, limiting the erosion of portfolio capital and the drag on portfolio performance.

Mutual fund pioneer Jack Bogle referred to excessive turnover as a “*bogey that investors ought to avoid*” because of its propensity to limit returns — research⁷ has shown a strong negative relationship between aggregate trading costs and fund performance, with the difference in average annual returns for the decade ended 2006 between the highest and lowest quintile of trading costs being nearly 200 basis points.

Similarly, longer holding periods for stocks are typically more tax efficient as well since it means that taxes paid on capital gains are deferred — and note, too, that many jurisdictions tax capital gains on assets held for less than a year more punitively than those on assets held for longer.

The bottom line is that excess return opportunities exist when there is mispricing in the market and these are best exploited by an active portfolio manager who has the skill and strong conviction to invest for the longer run.

David Onyett-Jeffries

David Onyett-Jeffries is Vice President, Economics & Multi Asset Solutions, at Guardian Capital LP (GCLP) and provides macro-economic guidance to GCLP and its affiliates—Alta Capital Management LLC and GuardCap Asset Management Limited.

¹ Data included in this chart has been sourced from the NDR chart for Average Holding Period for NYSE (Years), and has been reproduced, with permission, from Ned Davis Research, Inc. March 27, 2024.

² Shleifer, A., & Vishny, R. W. (1990). Equilibrium Short Horizons of Investors and Firms. *American Economic Review*, 148-153.

³ Seyhun, H. N. (2005). *Stock Market Extremes and Portfolio Performance, 1926-2004*. Towneley Capital Management.

⁴ The MSCI World Index captures mid- and large-cap representation across 23 developed market countries; the MSCI EAFE Index is a stock market index that is designed to measure the equity market performance of developed markets outside of the U.S. & Canada; S&P 500 is an index of approximately 500 stocks designed to reflect the risk/return characteristics of the large-cap US equity universe; S&P/TSX is a capitalization-weighted index designed to measure the market activity of stocks listed on the Toronto Stock Exchange.

⁵ Cremers, M. (2017). Active Share and the Three Pillars of Active Management: Skill, Conviction, and Opportunity. *Financial Analysts Journal*, 61-79.

⁶ Active share is a measure of the difference between a portfolio's holdings and its benchmark index. It is calculated as the sum of the difference between the weight of each stock in the portfolio and its benchmark weight, divided by two. A portfolio that replicates the index has an active share of zero, while a portfolio that owns entirely out-of-benchmark securities has an active share of 100.

⁷ Edelen, R., Evans, R., & Kadlec, G. (2013). Shedding Light on "Invisible" Costs: Trading Costs and Mutual Fund Performance. *Financial Analysts Journal*, 33-44.

All figures in USD, unless otherwise stated. For definitions of the indices mentioned in this document, please contact Guardian Capital LP at insights@guardiancapital.com

This commentary is for informational purposes only and does not constitute investment, financial, legal, accounting, tax advice or a recommendation to buy, sell or hold a security. It shall under no circumstances be considered an offer or solicitation to deal in any product or security mentioned herein. It is only intended for the audience to whom it has been distributed and may not be reproduced or redistributed without the consent of Guardian Capital LP. This information is not intended for distribution into any jurisdiction where such distribution is restricted by law or regulation.

The opinions expressed are as of the date of publication and are subject to change without notice. Assumptions, opinions and estimates are provided for illustrative purposes only and are subject to significant limitations. Reliance upon this information is at the sole discretion of the reader. This document includes information concerning financial markets that was developed at a particular point in time. This information is subject to change at any time, without notice, and without update. This commentary may also include forward-looking statements concerning anticipated results, circumstances, and expectations regarding future events. Forward-looking statements require assumptions to be made and are, therefore, subject to inherent risks and uncertainties. There is significant risk that predictions and other forward-looking statements will not prove to be accurate. Investing involves risk. Equity markets are volatile and will increase and decrease in response to economic, political, regulatory and other developments. Investments in foreign securities involve certain risks that differ from the risks of investing in domestic securities. Adverse political, economic, social or other conditions in a foreign country may make the stocks of that country difficult or impossible to sell. It is more difficult to obtain reliable information about some foreign securities. The costs of investing in some foreign markets may be higher than investing in domestic markets. Investments in foreign securities also are subject to currency fluctuations. The risks and potential rewards are usually greater for small companies and companies located in emerging markets. Bond markets and fixed-income securities are sensitive to interest rate movements. Inflation, credit and default risks are all associated with fixed-income securities. Diversification may not protect against market risk and loss of principal may result. Index returns are for information purposes only and do not represent actual strategy or fund performance. Index performance returns do not reflect the impact of management fees, transaction costs or expenses. Certain information contained in this document has been obtained from external parties which we believe to be reliable, however, we cannot guarantee its accuracy.

Guardian Capital LP is a Canadian-based Investment Advisor registered with the Securities and Exchange Commission. Registration as an investment adviser does not imply a certain level of skill or training. You may obtain a copy of our Form ADV on the SEC's public disclosure website ("IAPD") at www.adviserinfo.sec.gov. The Form ADV and a copy of the supplemental brochure can also be obtained by sending a written request to Guardian Capital LP, Attn: Compliance, 199 Bay Street, Suite 2700 Toronto ON M5L 1E8 or by calling us at 416-350-8899 or 1 (866) 718-6517 or email us at FundInfo@guardiancapital.com.

Guardian Capital LP manages portfolios for defined benefit and defined contribution pension plans, insurance companies, foundations, endowments and investment funds. Guardian Capital LP is wholly owned subsidiary of Guardian Capital Group Limited, a publicly traded firm listed on the Toronto Stock Exchange. For further information on Guardian Capital LP, please visit www.guardiancapital.com. All trademarks, registered and unregistered, are owned by Guardian Capital Group Limited and are used under license.