CUMBERLAND
Private Wealth

Three Principles for staying a step ahead of the market.

Cumberland Private Wealth Management Inc.

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The dramatic March 2020 stock market correction reminded us of the 2008 financial crisis, the 2000 tech collapse, the 1987 market crash and the 1974 recession.

Although the global pandemic has introduced some unique challenges, the similarities to previous events are striking, including doomsday media headlines, investors running for the exits, then markets rebounding more quickly and powerfully than many expected, producing significant gains along the way.

The question is: Why do some investors sell at the bottom and lock-in catastrophic losses, while others get into position for a recovery? And why do most sit on the sidelines while a small few profit from these historic rebounds?

We believe certain investors succeed because they have sound investment principles to guide their decisions and the experience to act with confidence.

At Cumberland Private Wealth, our investment principles have endured through decades of economic cycles. They give us the courage to capitalize when others are fearful, to consistently protect capital, and to keep our clients a step or two ahead of the market.

Here are three of those principles.

Principle #1

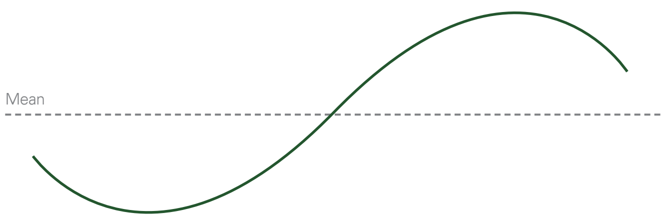
Values revert to the mean.

Greed pushes market values to record highs. Fear drives them to new lows. But eventually, values revert to the mean. Trends change direction and equilibrium is restored.

This chart illustrates the historic trends of stocks, bonds, gold and real estate over the past several decades. They have all seen highs and lows at different times. Astute investors are cautious when an asset is trading above the mean and look for buying opportunities when it is trading below the mean.

Eventually, trends change direction and market values revert to their long-term average.

Asset class	Current bull market
Bonds	40 years
Real Estate	25 years
Gold	5 years
Stocks	0 years



Asset class	Previous bottom
Stocks	2020
Gold	2015
Real Estate	1995
Bonds	1980

In 2000, euphoric investors who believed "this time is different" drove Internet stocks with insignificant earnings to sky-high valuations. They eventually came crashing back to Earth.

In 2009, panicked investors who believed we were seeing "the end of capitalism" sawed stock markets in half, only to have them roar back with record gains over the next few years.

Similarly, in March 2020, nervous investors, fueled by media, behaved as though civilization was about to collapse. Many sold at the very worst time and made their own worst-case scenario come true. Less than eight months later, the first vaccine was announced and markets set new highs.

At Cumberland, we know we can't predict the exact timing and scale of events that will take place. We can, however, identify when broad markets and specific stocks have drifted far from their means and may have disconnected from reality. Through our experience over many cycles, we can seize these moments to capture opportunities while still protecting capital.

Prices that deviate too far from the mean will eventually correct themselves.

Principle #2
Negativity reduces risk.

Investors make decisions based on how they think the world will unfold over the next 6-12 months or longer. In other words, the market activity you see today is actually a reflection of the future most people are expecting to see tomorrow.

This creates a fascinating paradox. Namely, that it is generally safest to invest when people are feeling the most negative about the future. In reality, those doubts are already factored into today's prices, and that means there's often nowhere to go but up.

Conversely, when the broad consensus is a rosy future, extra caution is warranted. In today's world, you could update an old adage by saying it's time to sell when your Uber driver gives you a stock tip.

The following table illustrates the dynamics at play. If an expected piece of bad news actually comes to pass, everybody says "I told you so" and the market is typically unmoved or doesn't change. If the news fails to materialize, the market often breathes a sigh of relief and moves higher.

	When bad news *does* come true	**When bad news *does* not come true**
Impact on the market	***Neutral*** The market stays flat, as the bad news was already reflected in current prices	***Positive*** The market can now rise, as the expectation of a negative outcome has been removed

This phenomenon explains why, when the U.S. government did not fall off a fiscal cliff after 2009, the stock market was able to recover and subsequently climb more than 350% over the next decade.

At Cumberland, we believe the key to making gains and protecting capital is a willingness to go against the herd and to be right in our assessments. So, in the darkest times, we look for opportunity, while fortifying our positions in the easier times.

Widespread beliefs create risk and opportunity when they deviate from reality.

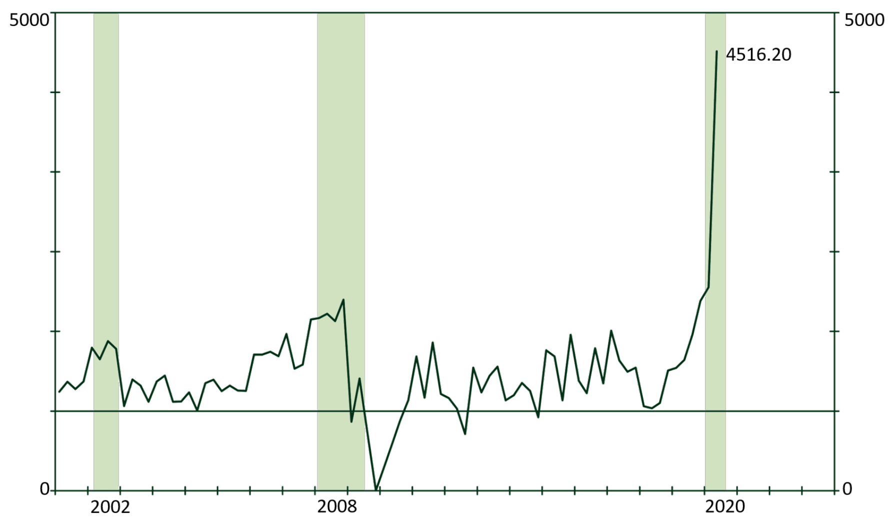
Principle #3
Liquidity beats economics.

The flow of money, known as liquidity, has a greater impact on the direction of the market than traditional economic indicators such as GDP and manufacturing statistics. This is why economists often make poor investors.

In fact, there is evidence of an inverse relationship between the performance of the economy and the performance of the markets, especially at their extremes. Markets tend to hit bottom and turn higher while the economy is still in recession. Markets tend to peak and turn down while economic growth is at its highest.

In times of economic weakness, central bankers increase the money supply, and this extra liquidity pushes up stocks and bonds. When the economy strengthens, those funds tend to flow out of the market as businesses use them to buy inventory, plants and equipment.

Change in cash held by US households in $billions



Cash + Checkable Deposits + Savings Deposits + Time Deposits + Money Market Funds

Source: TD Securities

In 2020, the U.S. government provided $2 trillion in stimulus, creating the first recession in history where average household discretionary income actually increased.

The chart above shows a dramatic increase in personal savings, which helped fuel the market rebound.

At Cumberland, we closely watch the quantity, direction and velocity of money flows in order to understand current and potential market moves. We believe that placing too much emphasis on economic forecasts can blind investors to the very powerful currents of money flows and their impact on the markets.

Money flows often have more influence than economic growth on the direction of the market.

See our principles in action.
Making the right calls.

As our clients can attest, our investment principles have helped us to anticipate and navigate some of the most crucial market cycles in recent history.

- We correctly traded out of stocks and into real estate in the late 1990s.
- In 1999, we sold U.S. equities ahead of the Tech Bubble bursting, and allocated significant capital to Canadian equities, which subsequently surged.
- In March of 2009, we bought depressed commodities and smaller companies, capturing a gain of about 38% by the end of the year.
- In the spring of 2020, we had the resolve to stay invested rather than go to the sidelines, allowing us to participate in the rebound and later profit from both growth and out-of-favour value stocks.

Today, many investors own pre-packaged portfolios made with ETFs and other passive investment vehicles. As experienced investors, we see weakness in this approach, as it can make it difficult to respond to changing market conditions. This can result in misallocated capital, missed opportunity and undesired risk exposure.

At Cumberland Private Wealth, we believe there is no substitute for hands-on, active portfolio management.

Our clients benefit from time-tested investment principles and a team with the experience to make the right calls, alongside sophisticated wealth planning.

Experience the Cumberland difference for yourself right now.

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*Cumberland Private Wealth refers to Cumberland Private Wealth Management Inc. & Cumberland Investment Counsel Inc.