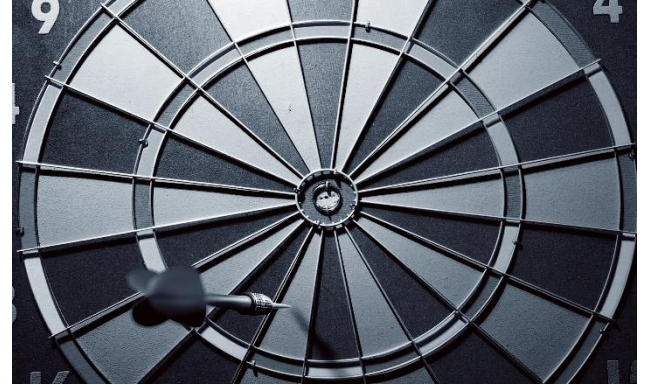




## Market Commentary: Silly Predictions, Reasonable Trends and Short-Term Risks January 2023

Moore's Law was actually a prediction, not a law as we tend to think of them. The long-term prediction was that the number of transistors in a dense integrated circuit would double every two years. The prediction has, for the most part, stood the test of time. Yet, there have been a number of risks to the prediction, such as miniaturization and the issues that come with it, that the industry has so far been able to overcome. A couple of years ago, IBM produced a transistor smaller than a strand of DNA<sup>1</sup> (how is this possible!). But will the industry reasonably be able to miniaturize any further? The prediction is currently being stressed.



The new year typically comes with market predictions. Will 2023 be a good year for the market? If you go with the collective market pundits willing to throw out a number, then YES! Unfortunately, that has been the answer for the last 20+ years running. Short-term predictions are hard and, frankly, often silly in a market context.

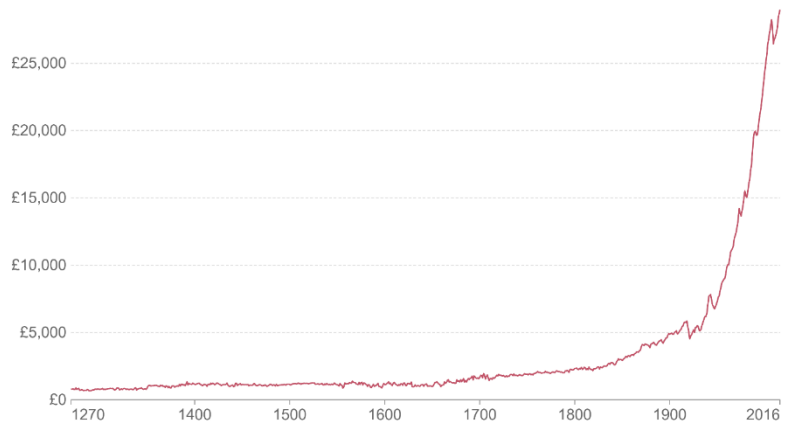
A better exercise is to review some much longer-term trends in the market prior to zoning in on current perceived risks to those trends continuing. Much like what Gordon Moore did when developing Moore's Law, he made a reasonable prediction based on the patterns he saw within the growing semiconductor industry and the existing science of the time. The industry then regularly identified risks to the prediction and (thankfully) were able to overcome them.

This also aligns better with the ultimate goal of most investors who should be thinking long term rather than in annual silos. One year is simply not a realistic investment time frame for most investors or strategies. Over the long arc of history the world has generally become wealthier, with a rather large jump after the industrial revolution. We build upon the feats of past generations, constantly innovating and sometimes inventing or discovering, resulting in modern luxuries that were inconceivable in the past.

A portion of invested capital is simply money squirreled away for future use for subsets of constituents (e.g., pensions, savings) while another portion is the discretionary capital of well-off individuals who make more than they spend.

### GDP per capita in England

Adjusted for inflation and measured in British Pounds in 2013 prices.



Source: Broadberry, Campbell, Klein, Overton, and van Leeuwen (2015) via Bank of England (2020)  
Note: Data refers to England until 1700 and the UK from then onwards.

OurWorldInData.org/economic-growth • CC BY

<sup>1</sup> [IBM's new 2-nm chips have transistors smaller than a strand of DNA \(newatlas.com\)](https://www.newatlas.com/ibm-2-nm-chips-transistors-smaller-dna/)

<sup>2</sup> A reasonable snippet expressing the growth of wealth, albeit for one country.



When one gets to the root of it, that capital is invested directly into assets—such as companies and real estate—that are expected to grow in value. It's also lent to governments, and hopefully provides benefits to its constituents (such as roads and infrastructure) as well as to the companies, governments, and individuals who lend the money in exchange for interest payments, as well as the return of capital.

As a whole and over time, equity values have increased and lent money has been returned. This is despite various country and company failures, such as Japan and Enron, and large macro-level events that negatively affected performance over shorter time frames at least from a context of the long arc of history (for example, WWII, '70s energy crisis, Dot Com bust, 2007-2008 Financial Crisis).

Given the long-term trend is expected to continue, and diversified investments continue to generate returns for investors as they have in the past, what can upend the trend?

One of our favorite lists of risks are those produced by the [Eurasia Group](#).<sup>3</sup> In 2022<sup>4</sup> they had US Midterms as risk #3 and Russia as risk #5. Note that these are risks, not inevitabilities. Thankfully, the US Midterm risk did not pan out. Russia unfortunately did. The Eurasia group does not make "predictions." It did not state that Russia would definitely attack all of Ukraine, but the report did state that "Russia is on the verge of precipitating an international crisis," and defined the nuances and potential forms of precipitation.

The top two risks on Eurasia Group's 2023 list<sup>5</sup> are (1) Rogue Russia and (2) Maximum Xi. Putin is caught in a corner. The war he started is going disastrously for Russia. This risk is obvious, but the outcome is not, with a range from the war unexpectedly ending (coup?), to a nuclear Armageddon. Meanwhile, Xi Jinping has consolidated power in China with "few checks and balances left to constrain him and no dissenting voices to challenge his views, Xi's ability to make big mistakes is also unrivaled."<sup>6</sup> Between seeming missteps with "Zero Covid," terrible demographics, and weakening growth, China has a host of issues that one human being in control of 1.5 billion people will decide how to navigate. Eurasia Group assists in understanding some reasonable range of outcomes based on their expertise. This further assists us in gauging why and how a part of the market may be valued and whether it may make sense to hedge an exposure.

In summary, short-term predictions and arbitrary time frames are designed to capture one's attention but are typically as reliable as those made by any fortune teller. We believe an appreciation of where we have been, the longer-term trends, and an assessment of risks that can upend those trends, provides value in best constructing, managing, and understanding the potential risk and reward of one's portfolio.

***IMPORTANT DISCLOSURE:*** *The information contained in this report is informational and intended solely to provide educational content that we find relevant and interesting to clients of Fountainhead. All shared thought represents our opinions and is based on sources we believe to be reliable. Therefore, nothing in this letter should be construed as investment advice; we provide advice on an individualized basis only after understanding your own circumstances and needs.*

<sup>3</sup> <https://www.eurasiagroup.net/>

<sup>4</sup> [Eurasia Group | Top Risks 2022](#)

<sup>5</sup> [Eurasia Group | The Top Risks of 2023](#)

<sup>6</sup> [Eurasia Group | Maximum Xi: Eurasia Group's #2 Top Risk of 2023](#)

