



PRATO CAPITAL



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BREAKING NEWS

What is the primary focus of the financial media outlets? Are they really providing sound advice for the individual investor?

It seems like there is “Breaking News” on the financial news channels every day. What impact does this have on stock prices?

The global stock and bond markets are very efficient at pricing securities. High frequency and institutional traders throughout the

global markets subscribe to real-time news services trying to get any advantage possible. With over \$462 billion traded globally every day¹ and millions of participants buying and selling securities around the world, prices adjust very quickly. In the US markets alone, investors trade billions of dollars in stocks and bonds each day. The new information buyers and sellers bring to the markets help set prices—and with each bit of new information, prices adjust accordingly. When the financial news channels report the news, it is normally followed by how much the price of the security has already changed. The ‘breaking news’ has already happened and the security is already priced accordingly.

Advice from Financial Media

Many of the guests on the financial news channels are professional money managers for mutual funds or large institutional banks. Every day opinions are given on a variety of topics, but almost always the discussion turns to where is the stock market going in the short and long term or what is the hot tip of the day. These experts will almost always give their opinion about the future. **Exhibit 1** below shows how difficult it is to outperform the index benchmarks for these money managers consistently over the long-term.

Exhibit 1.

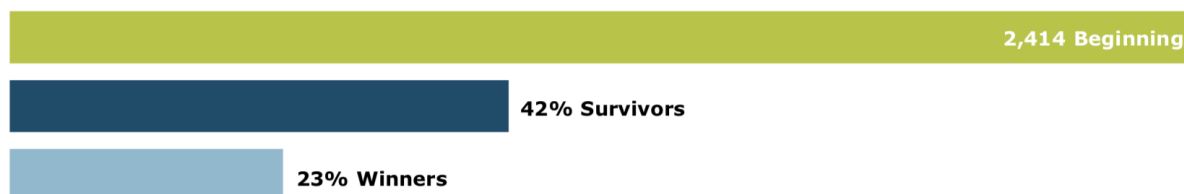
Mutual Fund Survival and Out-performers over the last 20 years

Outsmarting other investors is tough

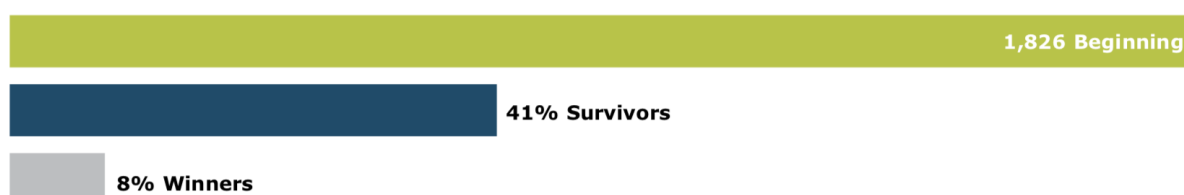
Few mutual funds survive and beat their benchmarks

20-year performance period ending December 31, 2018

EQUITY FUNDS



FIXED INCOME FUNDS



In US dollars. The sample includes funds at the beginning of the 20-year periods ending December 31, 2018. Survivors are funds that had returns for every month in the sample period. Winners are funds that survived and outperformed their respective Morningstar category benchmark over the period. US-domiciled open-end mutual fund data is from Morningstar. See Data Appendix for more information. Past performance is no guarantee of future results.

It would be difficult to keep viewers on the edge of their seats if the guest speakers on the financial news channels continually said that a “Buy and Hold strategy with a diversified portfolio outperforms almost all money managers over the long term”.

No article about the financial news channels would be complete without mentioning those “business news” programs that have lots of energy meant to keep you watching. Whenever you turn away, another bell or horn goes off returning your attention back to the show. There are all kinds of buy and sell recommendations on these shows but none of it is breaking news or beneficial for the individual investor. A study was completed by Jonathan S. Hartley and Matthew Olson of The Wharton School at the University of Pennsylvania on the

returns of the portfolio recommended by one of these shows². The returns for this portfolio are quite unimpressive.

Financial News is Big Business

One of the missions of the Pew Research Center is to research trends in media and journalism. In their latest report on cable news, the three major financial news networks reported profits of \$549.7 million on revenue of \$1.25 billion³. This is big business.

To attract more viewers and boost ratings, some of the financial news channels have tilted their programming towards different market segments. While all the channels will provide continuous stock market updates and commentaries of some kind, the pre- and after-market segments have changed the most. Some of the programs have a political tilt and some have more of an entertainment orientation. All meant to draw viewers which leads to more advertising revenues.

The whole idea for these media outlets is to get you to watch and drive up their ratings. They are trying to maximize their revenues by increasing viewers and market share. They are not providing an edge with stock tips. They are providing entertainment. Speculation and market-timing are subjects that bring viewers back to watch day after day.

Conclusion

The financial news channels are driven by their bottom line. Ratings drive their advertising revenue, and nothing keeps viewers like making someone feel they are receiving 'insider' information.

Paul Samuelson, the first American to win the Nobel Prize for Economic Science, said, "Investing should be more like watching paint dry or watching grass grow. If you want excitement, take \$800 and go to Las Vegas."⁴ For the financial news channels, "watching

paint dry or watching grass grow” is not exciting enough to keep people watching and drive their bottom-line profits.

At Prato Capital Management, we think there is a fundamental difference between investing for the long-term and speculation. Long-term investing based on almost 100 years of research is the engine behind your Financial Life Plan. We find this kind of investing and its results very exciting.

¹ In US dollars. Source: Dimensional Fund Advisors, using data from Bloomberg LP.

Includes primary and secondary exchange trading volume globally for equities. ETFs and funds are excluded. Daily averages were computed by calculating the trading volume of each stock daily as the closing price multiplied by shares traded that day. All such trading volume is summed up and divided by 252 as an approximate number of annual trading days.

² Jonathan S. Hartley and Matthew Olson, The Wharton School at the University of Pennsylvania, <https://static1.squarespace.com/static/568f03c8841abaff89043b9d/t/5734f6e2c2ea51b32cf53885/1463088868550/HartleyOlson2016+Jim+Cramer+Charitable+Trust+Performance+and+Factor+Attribution.pdf>

³Compiled by Elizabeth Grieco; Pew Research Center, Journalism and Media; <https://www.journalism.org/fact-sheet/cable-news/>; July 25, 2018

⁴. Paul Samuelson, “Mutual Funds Report; Just Relax, Put Your Feet Up, and Make Money,” New York Times (April 2004).

PAST NEWSLETTERS



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