STRATEGIES

# *Forget Stock Predictions for Next Year. Focus on the Next Decade.*

Wall Street's market forecasts for 2023 are worthless, our columnist says. But the long view is much clearer.

**By Jeff Sommer**
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The Federal Reserve raised interest rates again on Wednesday, but by less than it has in previous rounds this year. A day earlier, the government reported that the annual rate of inflation, though still painfully high, dropped a bit in November, to 7.1 percent from 7.7 percent in October.

If you want to know what these, and other economic developments, mean for the stock market in the year ahead, there are plenty of forecasts coming out of Wall Street.

It is December, after all, when investment strategists gear up and produce earnest, specific forecasts for where the S&P 500 will be at the end of the next calendar year.

With inflation soaring, the Fed raising interest rates, Russia's war in Ukraine and China's decision to drop its "zero Covid" policy, a recession all but certain in Europe and increasingly likely in the United States, clear maps of the future would be particularly welcome now.

But that's not what the one-year forecasts from Wall Street are providing.

These attempts at clairvoyance are stymied by a fundamental problem: It's simply impossible to forecast the path of the markets six months or a year ahead with accuracy and consistency, as many academic studies have shown. That the financial services industry continues to label these unreliable numbers as forecasts is a triumph of breathtaking chutzpah — a technical term for shameless audacity.

It goes a long way in explaining why the vast majority of active investment managers can't regularly and convincingly outperform the market — a failure I reported in a recent column about mutual funds. If you have no idea where stocks are going, it doesn't make much sense to place specific bets on them, as active managers do.

**Accepting Uncertainty**

These annual reports often contain impressive erudition. I pore through this stuff compulsively in search of nuggets that I can file away for some future column.

But with a high degree of confidence, I will repeat a prediction I've made before: The consensus forecast this year will be wrong.

Read these things if you find them interesting, but don't rely on them — or those who produce them — to guide your investing.

Instead, embrace uncertainty.

Accept that you need to invest without knowing what will happen to your money over the short term. So be sure, first, to put aside enough money in a safe place, like a bank account or money-market fund, to pay the bills in the months ahead.

But because the stock market tends to rise over long periods, and because bonds are now generating reasonable income (as I explained last week), it's wise to invest for a horizon of a decade or more in low-cost index funds that track the entire stock and bond markets.

Don't base your investments on specific predictions of where the stock market is heading over the short term, because nobody knows. Making bets on the basis of these forecasts is gambling, not investing.

**The History**

Consider how bad Wall Street forecasts have been.

In 2020, I noted that the median Wall Street forecast since 2000 had missed its target by an average 12.9 percentage points a year. That error over two decades was astonishing: more than double the actual average annual performance of the stock market!

Imagine a weather forecast as bad as that. A meteorologist says the high temperature the next day will be 25 degrees Fahrenheit and it will snow, so you dress for a winter storm. Actually, the temperature turns out to be 60 degrees and the skies are clear. That's about the level of accuracy for Wall Street strategists through 2020.

They continued their errant ways the next year, issuing a median forecast of 3,800 for the closing level of the S&P 500 in 2021. But the index ended the year at 4,766.18, an error of about 25 percent. In a word, the forecast was horrible.

The forecasts for 2022 look inaccurate, as usual, though we won't know for sure until the end of this month. A year ago, the Wall Street consensus was that the S&P 500 would reach 4,825 at the end of 2022, a modest increase from 2021. But at the moment, the index is hovering around 4,000. In other words, a year ago, strategists were saying that 2022 would be just fine for stocks. It hasn't been.

**The Future**

After forecasts that were too low for 2021 and too high for 2022, Wall Street strategists are holding steady for 2023. The consensus is that the S&P 500 will end the year at 4,009, roughly around where it has traded in recent days.

That could be right. Who knows? But if it does turn out to be correct, it will be an accident, not the result of uncanny knowledge about 2023.

This inability to forecast the future goes way beyond Wall Street. Pandemics are part of human history and we know there will be more of them. But no one was capable of anticipating the specific Coronavirus pandemic that started in 2020, or the 6.6 million deaths, 646.2 million cases, and the complex economic and financial damage it continues to cause.

Wall Street didn't know that Vladimir Putin would order Russia's invasion of Ukraine this year — or that fossil fuel companies would end up leading the stock market in 2022. The war in Ukraine and China's attempt to shift from its Covid lockdown policy will both influence the stock market in the United States in the year ahead. But how, exactly? We can guess, but anyone who claims to know is delusional.

No doubt, enormous changes that aren't visible yet are coming in 2023. Inflation and interest rates preoccupy financial markets now, but there is no assurance that will be the case a year from now.

Lack of specific knowledge about the future is a fact of life. Guessing, or betting wildly, isn't a prudent solution.

Instead, diversify. Hedge your bets so you are prepared whether specific markets move up or down, and be ready to ride out extended losses, like those of 2022. This strategy has been painful this year, though it has paid off over longer periods.

A simple, classic investment strategy — a diversified portfolio made up of broad stock and bond index funds, with 60 percent allocated to stock and 40 percent to bonds, did terribly in 2022. The Vanguard Balanced Fund, which takes just this approach (though it is limited to U.S. and not global assets, which I'd favor), has lost nearly 14 percent this calendar year.

But even including this year's awful returns, this portfolio has gained more than 6 percent annualized, over the last 20 years. At that rate, it doubles in value every 11 or 12 years. There is no guarantee that it will continue to generate those returns in the future, but Vanguard said this week that it probably would.

Vanguard doesn't bother with year-ahead market forecasts because it recognizes that they are pointless. It does make estimates for market returns over a 10-year horizon. Stock market projections of longer duration have much greater accuracy than those for the next six months or a year, as Robert Shiller, the economist, demonstrated in the 1980s. He was recognized for that insight when he received the Nobel in economic science in 2013.

At the moment, Vanguard's 10-year outlook is fairly auspicious. The falling markets of the last year have led to better stock and bond valuations.

It's possible to be intelligently optimistic about financial markets over the next few decades, without knowing where the markets are heading over the next year. I wouldn't bet on any single financial asset just because a Wall Street expert says it is about to rise.

Using your money that way — whether you are buying stocks, bonds or far less solid assets like cryptocurrency — is gambling, not investing. But if you stay humble, invest in the total stock and bond markets and manage to hang in for decades, your chances of prospering are much greater. That prediction is reliable.