# Ep64: The Next 900 Days: A Conversation with Liz Young, BNY Mellon

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PATTI BRENNAN: Hi, everybody. Welcome to "The Patti Brennan Show." Whether you have $20 or $20 million, this show is for those of you who want to protect, grow, and use your assets to live your very best lives.

Joining me again today is Liz Young. Liz is a Director of Market Strategy for BNY Mellon. We are so lucky to have Liz with us today. If you haven't listened to the prior podcast, turn this off right away. Listen to the podcast that we just released so that you can get a feel for how amazing she is and how bright she is and what she thinks in terms of what to expect the first 90 days of this year.

Then today, what we're going to cover is, what do we expect for the next 900 days? Liz, thank you so much for joining us.

LIZ YOUNG: Glad to be here again. I don't get to be president on this one, though, do I?

PATTI: As far as I'm concerned, you're in. I think you're amazing.

LIZ: I think I just want the job for 90 days. I don't think I want it for 900. Just a brief appearance in the White House is fine for me.

PATTI: That's all we really need, Liz. You can tee it up. Then, all the things that you talked about in the prior podcast, you're going to fix everything. Then from there, the economy will take care of itself.

LIZ: Right. Perfect.

PATTI: We talked about short term versus long term. Now, let's talk about something that is sometimes painful, and that is this concept of diversification. When we're managing portfolios to make them work for a client's financial plan, part of that involves diversifying their assets.

I will tell you, Liz. It's been hard over the last five years, because the S&P 500 has been the only game in town, or I should say the best game in town. Again, we are not rearview-mirror investing. We understand that that is the way that it was, but let's look forward together and think about, "Diversification is a principle that works over time, maybe not every time, but it does work over time."

Looking forward to the next 90 days – and I'm going to interject a concept or a thought – especially as it relates to where we are with the dollar and currency. Especially also as it relates to international investing, which is, frankly, the area that hasn't done nearly as well as the US stock market.

What do you think about the value of the dollar, the currency? What kind of an impact does that have for that part of a person's portfolio?

LIZ: Let's take a step back and do a quick lesson on diversification. I realize that it's been used as a term "deworsification" too with clients because there are asset classes that seem to work against them all the time, or maybe they act like a drag on the portfolio, or as you pointed out, the S&P 500 has outperformed everything else, why do I bother with anything other than the S&P 500?

First and foremost, diversification is the combination of a number of different asset classes, and the intention is that those asset classes do not behave like one another, which means when one is up, there's going to be another that's down.

That is exactly how it's supposed to work. A lot of times when clients are using certain types of assets, and I'm thinking about things like alternatives or fixed income, and they're looking at them and expecting them to perform well at the same time that their equity portfolio performs well, they end up disappointed.

What I would call that is user error. If you're using certain parts of your portfolio to perform well in up, down and sideways markets, please let me know what parts of the portfolio can do that because [laughs] there's not a lot of asset classes that can do everything.

Diversification is meant to have some cylinders hitting while other cylinders aren't. That's rule number one. To your point about the dollar and international investing, first, looking at the strength or weakness of the dollar is something that I like to usually compare to, we talk about the VIX index a lot, so the volatility index, as the fear index.

I actually think it's the dollar that's the fear index because the US dollar is looked at around the globe as the reserve currency, as the safe haven currency, and any time there is global fear, you're going to see strength in the dollar because there's more appetite for the dollar, and there's more appetite for liquidity in the dollar.

As the dollar has weakened over the last six months, that's much more an indication of fear subsiding around the globe than it is of anything else. You could argue that there's some headwinds on the dollar, things like the trade deficit, the budget deficit in the US.

Yes, that's true, but that's more of a longer term force, and something that I would call a strategic force, not a tactical short term force that's going to cause a three-to-six month pull back. Looking at the weakness that has already happened in the dollar, into 2021 we do expect it to either stay in that weak range, I would say at best, stay in that weak range if not get weaker.

Especially with a blue wave in Washington. As the dollar weakens, and as it's already weakened, what that does is it creates a tailwind for international investing, and specifically for European equities and Asian emerging markets. That's both debt and equity.

When you look at emerging markets and Europe, they're actually very intertwined. The European consumer buys a lot of stuff from emerging markets. As that European consumer comes back in this global recovery, emerging markets benefit from that.

Then you have to think about the entire supply chain, all the stuff that European consumers buy from emerging markets have to be moved from emerging markets back to Europe. You're going to have trucks. You're going to have trains. You're going to have planes that carry everything. That's the transportation sector.

There's all sorts of opportunities wrapped up into that theme, and the weakness of the dollar just further accentuates the attractiveness of international investing. The fact that the S&P has done so well makes the valuations on the S&P a little bit less attractive as compared to European equities and emerging market equities.

PATTI: That's really interesting. Let's go back to the weakening of the dollar. How weak is weak? How much did it decline, and was that relative...was that a lot? Relative to other periods?

LIZ: You wouldn't expect something like the US dollar to have a ton of volatility in it because it's the US dollar. We're talking about the most influential and important currency around the globe, and many things are denominated in dollars.

Many global commodities are denominated in dollars. Obviously, the circulation of dollars is influential in all central bank operations. You wouldn't expect it to have big moves, but I believe over 2020, it fell somewhere between 11 and 14 percent. I'm not sure what the exact number was at the end of the year.

That is a pretty big move, but you also have to remember that it rose a lot because of all the fear that happened in the beginning of the year. When you saw what happened in

March, the dollar saw a lot of strength because that pandemic was globally reaching.

It wasn't something where if we look back on the financial crisis, that began in the US. We started it, right? Then the rest of the world unfortunately caught it. This was something that was a global pandemic that hit us all. It was a completely exogenous shock, meaning it wasn't due to excessive risk taking in financial markets.

It wasn't due to one particular region doing something wrong economically. It was completely exogenous, external, out of our control. Had nothing to do with the economy or the markets, but absolutely affected all economies and markets and actually almost exactly the same time, maybe within 30 days depending on the spread but almost exactly the same time.

That was global fear that took hold. When global fear takes hold, there's really only asset that everybody's going to want, and that's the dollar. There was a ton of strength, and then as that fear let air out of the balloon and everybody took a step back, Armageddon wasn't coming, maybe a depression wasn't coming. Then you started to see a falloff in the dollar, but that's not a bad thing.

I think that's one of the things that I want people to remember, that a weaker dollar is not necessarily a bad thing for the US economy.

PATTI: Very interesting, and really an important point also. When we look at the value of the dollar, we think about international investing. One of the other things that I've heard is that with this kind of stimulus, with this much money sloshing around, the value of our currency can also go down with that. Is that an accurate statement?

LIZ: Yes, because when you think about all the money that's sloshing around, so what we've done is we effectively put more dollars into circulation. The dollar that you're holding in your hand, and there's a stat.

I don't want to quote it exactly because I'm not exactly sure what it is. I want to say it's something like 70 or 80 percent of the dollars in circulation have been put into circulation in the last, I don't know, 10 to 15 years or something.

As we print more and more dollars, the one that you're holding in your hand becomes less valuable because there's so many more out there. Then you've got basically what's more money chasing the same amount of goods, which is deflationary by nature because all this kind of money flying around and everything that you had before is just worthless because there's so much abundance of money.

What that does to the value of the dollar, obviously, is puts pressure on it. What happened in this pandemic in particular is that you've competing forces. Sometimes one force wins even if that doesn't make economic sense.

The force that won that was driving strength in the dollar was fear as I mentioned before. As we move forward and as the economy gets healthier, what you might see is that all that spending and all that printing is actually putting pressure on the value of the dollar, which...

This is a completely separate conversation, but something that's driving that cryptocurrency trade because people are looking at crypto and saying, "Is that a better store value than the US dollar now given the fact that we've just printed endless amounts of dollars?"

It's going to change the way we think about what is currency, what is the strength of currency, what are the stores of value other than currency in this kind of strange, constant policy-support environment.

PATTI: It is so interesting that you bring up the competing forces. As the fear begins to decline, as people get more and more comfortable with that, is it safe to say that there's some pent up demand and that we could go hog wild with all these extra dollars that we all have?

We know that the savings rate in the US broke a record last year. I think right now it's about 13 percent, which is historically very, very high. We've got lots of money and savings, what happens when we are all back traveling and doing the things that we were doing pre-COVID.

What could happen then? Is there a unintended consequence or a potential consequence that people need to be aware of?

LIZ: Yes. First and foremost, I think it's important to point out that we don't all have a lot of money sitting around. This crisis has affected different levels of economic wealth in many, many different ways.

There is a large subset of the population and the economy that's suffering quite a bit, and is not liquid and is still really pinching pennies. Then we've got food banks with the highest demand they've ever had.

There is definitely a part of the economy that continues to need that support.

PATTI: Liz, can I just...

LIZ: On the other end of it...

PATTI: ...can I just say one thing to you?

LIZ: Sure.

PATTI: This is why you should be president, because that was such a wonderful acknowledgment of what we hear in the media, what we hear and we read. I'm reading it too. Savings are going through the roof, etc., but, you're absolutely right.

There are a lot of people out there who are not, don't have a lot of money in savings who are still struggling. I think it's important to acknowledge that. It's important to acknowledge we're not out of the woods yet, and we are a nation that is there to support the most vulnerable among all of us. Thank you for bringing that up. I think that's wonderful. Thank you for saying that.

LIZ: Sure. That's the part of the economy that benefits the most from that fiscal support. A $600 check may not mean a lot to somebody who makes a million dollars a year, right? You're not going to get one anyway. A $600 check to a family that's struggling and trying to make ends meet and feed people every single night of the week is a lot of money. We have to keep that in mind.

Of the haves, we talked about the have nots. Of the haves, the savings rate did get really, really high. Understandably so. Not just because of fear, but also because we just had nowhere to go and nowhere to spend it.

PATTI: Sure.

LIZ: Nothing was open, so what are you going to buy? There was a period of time where there literally was no activity happening at all. That savings rate has come down slightly since the earlier part of 2020, but it's still elevated again partially because there wasn't really anywhere to spend it, or there wasn't as much opportunity to spend it.

We do expect that as the recovery drags on and continues through this, that you'll see a reduction in that savings rate around the globe. It's going to be this reboot in activity and this reboot in demand. That's a wonderful thing. I think there are some people that are still underestimating how strong that reboot is going to be.

One of the things that I want people to keep in mind is that what it could cause is inflationary forces, but they hopefully are transient. What I mean by that is as demand picks up again and as that savings rate falls and people start spending, it may happen very, very quickly. It may happen in a huge burst or a couple big bursts of that level. It's the supply...

PATTI: Kind of like the way it happened in terms of the way that we all pulled back. That was a sudden stop in economic activity. We were in our homes. We couldn't spend the money.

LIZ: Right, exactly. As it restarts, there's probably some seasonality effects, right? People travel more in summer than they do at other times of the year. Anyway, but what could happen is as that demand comes back, if the supply chain isn't ready to meet the demand, you're going to see little bursts of inflation.

You might see some readings on the inflationary metrics, things like CPI, PCE. Those are the ones that get reported. You might see some readings that are above what we're used to. Granted, we are used to some very, very low numbers, but you might see some numbers that are higher than that.

It could cause jitters in risk markets every once in a while. I just want people to be ready for that. Not that it's something that's going to cause a recession. Not that it's something that's detrimental or going to derail the recovery, but it could cause some jitters because we're not accustomed to seeing that.

It could also cause some volatility in the yield curve or the treasury yield levels. As the treasury curve moves around and tries to find the right spot, maybe the Fed controls it and controls the volatility to some degree. But as it moves around, that could affect risk markets as well.

I think it's something to just be on the lookout for. I think if we're prepared to see that, it won't be as scary as when it happens.

PATTI: That is so good. Again, we're just creating some reasonable expectations. Hopefully it doesn't happen, but if it does, it's nothing that we need to freak out about. Regulators, everybody's aware that that's a possibility.

Let's continue this theme of Americans and social responsibility. Let's talk a little bit and let's end today with this idea of the socially responsible investing. It's really beginning to get some legs, isn't it?

LIZ: It certainly is. Anybody who hasn't been paying attention to it should listen up.

PATTI: Yup. OK, we're all yours Liz Young.

LIZ: One of the things that we have talked about on my team as a theme for the next one to three years is the idea of ESG. That's environmental, social, and governance. Frankly, it's something that the US is behind on.

I think we get caught up in our own politics on this way too much. It becomes a very political conversation in the US. Whereas if you'll look at what happens in Europe, it's not a political conversation. They just accept it as reality.

There've been regulations put in place in regions like Europe that require companies to abide by certain metrics and have to meet certain codes in order to stay in business and in order to remain open. I think that that trend probably comes to the US sooner than later.

What could happen in the early days of that is that there are some corporations that are going to have to spend in order to keep up with the ESG theme, and in order to keep up with regulations that could come on an ESG perspective.

Now, this is not just environmental, I think that's the one that we're used to talking about and thinking about things like clean energy, and will companies be required to not dirty the environment, of course, but there's also this huge force of social that has taken the world by storm, unfortunately, kind of a violent storm last year.

The social piece of that, and the idea that even the NASDAQ exchange is looking at requiring companies to have one female or one person of color on their boards. There is a social aspect of this, too.

That's going to require companies to shift the way they do business, shift the way their leadership looks, shift the way that they communicate, and some of it is going to require spending. It could put pressure on corporate profits that are most exposed or most vulnerable to that in the short-term.

That being said, the reason why I said if people haven't thought about it, haven't accepted it as a reality, it's time to listen up is because the next generation that's coming in as investors, and as consumers, and as the ones that we need in order to keep this economy moving is millennials. They are a huge generation.

They care a lot more about ESG than the baby boomers did. This is a theme that from an investor appetite standpoint, they want companies that are ESG compliant, they want responsible companies that they feel good about, they also want to work for companies that are ESG compliant and that they feel good about.

We have to think about that going forward, and that's beyond one to three years. That's a decade down the road as well, but it's a trend, it's a theme, it's a force that is here to stay, it's not going anywhere, and as the millennials enter the economy in a big way, it's just going to get stronger.

PATTI: Your point about ESG in the US versus say Europe is really interesting. I also understand that in Europe and in many international countries, there is no such thing as an ESG fund, because every corporation, every entity out there, if they're going to remain in business has to be ESG.

This concept of segregating a part of the portfolio so that it is ESG isn't as important on the international side as it may be on the US side. Where, to your point, we're just beginning to focus on this. What's your thought about that?

LIZ: There are a few firms that do focus on investing solely on an ESG standpoint, and there are funds that will call themselves that. I do think that your point about...It starting to be a part of the investment process that's accepted both internationally and in the US is probably where the world is headed.

There's different ways to do it, though, and I don't want to get too far into the nitty-gritty of how you investors, an active investor or what we call the buy-side.

You could do it as an initial screen, where you won't even consider companies that are not ESG compliant, or you could do it as a backend screen and make sure that the governance is in line that there is no big red flags. Those are two very different approaches.

In the US, if you look back historically, and I was a due diligence analyst when some of this was still popular to do. It used to be what we call a negative screen. We would say something was ESG or whatever people wanted to call it, it was a negative screen.

What that means is you take a basket of securities, and you remove the ones that are in the industries that you don't like. At that time, a lot of it was driven by Catholic Diocese. They removed firearms, they removed contraception, they removed a bunch of other things that they didn't agree with.

Nowadays, it's more of a positive screen. When you look at ESG from a positive perspective, you're going out and saying, "We want companies that are driving this clean energy revolution. We want car companies that are driving that revolution. We want solar companies. We want wind companies."

It's positive in the sense that you're purposely picking companies, or picking funds, or picking management teams that align with the values that you want to align with, rather than taking a basket of securities that's pre-canned and plucking out the ones you don't want.

It's a totally different approach, and I think that it's where the future goes.

PATTI: It's an excellent, excellent point, and we started talking in our podcast together about the next 900 days. I think you've laid the groundwork for even longer that as we begin to pay attention and understand here in the US that that really is the future, and the companies that kind of, "OK, listen up, buck up," it is time for you to pay attention to this as a corporation.

It is those companies that will be embraced by, again, millennials and people who may not be a millennial, but the general public, because they understand and we understand that that stuff really matters. Those corporations that can really gear their future with that as a core value within the company, hopefully, their business is going to prosper even more because of it.

LIZ: That's absolutely true, and prosper from different directions. As I mentioned before, it's not just from an investment perspective, it's where do people want to work, and where is your labor force going to come from? What's your opportunity for gaining talent, retaining talent? What about your consumer base?

Do people want to buy your products? Not just do they want to buy your stuff, do they want to buy your stuff off the shelves, because it makes them feel good? Do they want to get their paychecks for you? Companies have to think about it on a lot of different levels.

PATTI: Wonderful stuff, Liz. Thank you so much. You have been amazing over this podcast as well as the prior one. I just love your perspective. You're very real. You understand where people are today and what they're worried about.

The things that we're all worried about are very real, so we need to listen and pay attention to that. What I also love about your approach is you're very forward-looking. Again, not just 90 days or even 900 days, but 5 and 10 years from now.

How is our nation? How is our market? How our companies...How's the world being shaped, and by what? Liz Young, what a privilege it has been to have you as our guest today. You're the market strategist for Bank of New York Mellon. My goodness, how lucky are they to have you.

LIZ: Thank you.

PATTI: So are we, by the way, so are we. This was a big deal. Thank you so much for joining me today. For all of you who are also listening, thank you for your time. Your time is valuable. Your feedback has been amazing for these podcasts. We want to keep it real and fresh.

I appreciate you taking the time to listen to us today. Again, as always, any questions? Go to our website, keyfinancialinc.com. Let us know how we can help you. Whether it be on future podcasts or for you and your family, we are in the business of being stewards of people's wealth. That's what we're all about.

I think that these insights can help us to do that even better. Thank you so much. I'm Patti Brennan. We'll talk to you again in the next podcast. Take care now.