

Episode 55 Technical Analysis is Technically Wrong

Bob French 00:00

The purpose of Retire with Style is to help you discover the retirement income plan that is right for you. The first step is to discover your retirement income personality. Start by going to risaprofile.com/style and sign up to take the industry's first financial personality tool for retirement planning. Do you prefer Calvin Ball? Or Whose Line Is It Anyway? Either way, a lot of people sure seem to like to make up the rules as they go.

Alex Murguia 00:49

Hello, everyone. Welcome to Retire with Style. I'm Alex and I'm here with our trusted companions. Wade and Bob. Hey, how are you guys doing today? That's for you guys. Yeah.

Bob French 01:08

These are these are wearing intros here.

Alex Murguia 01:11

But thank you for that. Thank you for that initial enthusiasm. I'm no longer a guest. No, you are you okay? You're in that? You're in that? What do you what do you pledge you're pledging? You see, I thought it would go the nice way. I'm one of the characters. No, no, no. You're like, you're like, what was it like? Charo on The Love Boat? You come on a lot as the guest is here. I know, right? I don't know. brings me back to the halcyon days of my youth. Hey, I got Oh, yeah, that's our word for the day. I was I was listening to the last podcast, Bob, and the last two halves had he has thrown out some zingers. Let's see what he comes up with today. It'd be it'd be nice. It'll be nice. All right. So what are we talking about today, Bob?

Bob French 02:10

So this should be I think this will be a fun one. This is talking about technical analysis. So this is, you know, basically, it's the one with all the crazy charts. So technical analysis is, you know, when you see people talking about, you know, all of these really weird things about trying to predict what kind of an individual stock or maybe an index or something will be doing, based on what how it's moved in the past and relative, usually relatively recent past. That's technical analysis. It's using those those charts. So price movements, and also, you know, the liquidity and some of those types of things, to really try and get a sense of, you know, what's going to happen next, how is the market going to be moving in the usually relatively near future? So I think I can just get the get the joke out of the way first, it doesn't work. But it's still really, really common. And yeah. So to put a little bit more,

Wade Pfau 03:22

I thought you're gonna teach us the techniques you use for your own trading today. You're saying that that's not the case.

Alex Murguia 03:28

That's a big negative.

Bob French 03:30

You know, CNBC and stuff. They're real big fans without Alex.

Alex Murguia 03:37

Yeah, yeah.

Bob French 03:39

Has pretty charts. It's got good visual,

Alex Murguia 03:41

Has the pretty charts, got the crazy charts. There's a couple things here because we did get this one tweak. We were talking about, oh, dividend stocks, we're talking about dividend stocks. And you know, there's nothing special with dividend stocks. I think it's more of a marketing play. For the reasons we outlined in the in the podcast, or it's a to behavioral kind of thing, where you like, you know, compartmentalizing things, but you know, it can bring on more risks and when it's worth, etc, etc. But someone wrote in saying, why don't we Why didn't we bring somebody in that could talk about the other the flip side of that story? Right? Well, it's our podcast, right? And we don't know, there's a sense that if you bring somebody in to provide a counter argument, then the counter argument is equally weighted, you know, like the 50% of the people follow it and 50% of the people don't follow it, right. For technical analysis, there's no way in hell that we're going to bring in someone to bring in that proponent thought, you know, much the same way that I wouldn't bring in somebody here, where there's somebody in the medical profession and then somebody's talking about voodoo. It just no matter how much the dark arts can attract somebody, it's just not something that you know that professionally we can do it I do have a question for Wade. And Bob, since you brought this on, you both have CFAs Chartered Financial Analysts. Can I ask you at designations so we don't get sued. But can I ask you, as soon as you get your CFAs? How quickly did you want to get your CMTs? Chartered Market Technicians? How quickly was it that you decided I'm gonna do this one, this is the Triple Crown.

Bob French 05:31

It was tough passing on the so.

Wade Pfau 05:36

But in the CFA designation, they do teach you about technical analysis. It is it's kind of schizophrenic, where they teach you that markets are random, and you can't really do this sort of thing. But at the same time, they also teach you the technique here. So I guess there's a little bit

Bob French 05:51

we're going to do this or not, or at least follow the patterns. So

Alex Murguia 05:57

I don't know. To me, it's, there's a little bit of, you know, point blank, let's get it all the way, right. And if you don't like what we say, you can change, you know, listen to some other thing. But the reality is, is kind of lazy thinking, you know, I don't know what would possess anyone to get a CMT, frankly, professionally, and mentally, you may be someone listening in and hating me, and that's fine, you know, get in line kind of thing. But really, what what would it's almost like, the person that got the CMT was a person in when they were taking the CFA, they failed. So they got to see him tea, because that's what was left. You know, and they probably why they were taking the CFA, were marking, were noticing patterns in the in the in the answer sequences of ABC or D. And just like answering in that way, that's my as my take, what do you think?

Bob French 06:55

I know, I think I will be honest, I think everyone does look for those patterns on those scans. Let's, let's just all be honest with ourselves. Here. We are looking there. We are making sure that you know, I haven't said be in a while I gotta watch out for that. Yeah.

Wade Pfau 07:16

Just as effective to

Alex Murguia 07:18

exactly just as effective as well. Let's go. Let's go into the reasons why. Because I now with my serious cap on but not really know, this is, look, it's an easy kind of thing. It's very easy. It's almost like the cliffnotes of cliffnotes, where there's no math involved and how easy it well, there's a sense that there's numbers involved, but there really isn't. And it's very easy in a new show, to talk about resistance levels and ceilings and bottoms and floors and whatever, right? It just is, you don't you don't need to do a lot of homework behind it. And so it's an easy thing. And it gives us the sort of false sense of what's the word here called quality analysis? And you know, behind it when there's really not, I mean, there really isn't. And, you know, Bob, take it away, why why isn't there?

Bob French 08:10

Why isn't there that level of analysis? Where, was the question?

Alex Murguia 08:15

why why why is this kind of a crock really, and

Bob French 08:19

A good way of starting this is, you know, if we break this down and look at it from from their point of view, you know, what are for the kind of the four big assumptions that technical analysis is making here, then we can kind of start from there and start pulling it apart a little bit. So the first big one is prices are determined by supply and demand. That's really what they're looking at with those charts. You know, how's the price moving?

Wade Pfau 08:46

That sounds reasonable.

Bob French 08:47

That's perfectly reasonable. Yes, yes. We're done. We don't need to go any further. Prices are determined by supply and demand. And sure, yes, good. Number to supply demand is good. Yep. Both have rational and irrational components there. Again. Yeah. Okay. Check that box. But this is the one where I start thinking, okay, yes. But where are you going with this? The next up is it's difficult to sort out why shifts in supply and demand occur, but those shifts can be observed in stock price movements. Again, sure.

Wade Pfau 09:36

That sounds reasonable. Okay.

Alex Murguia 09:38

I'll add this one. Now you add the wrinkle of after the fact maybe posthoc. Yep. That that's the only thing I would add in parentheses there.

Bob French 09:47

Exactly. This is where we started

Wade Pfau 09:49

Well anytime te price changes. It's a shift in supply and demand,

Bob French 09:52

Yeah no, again, on its face, that statement is absolutely true. But you have to start wondering, okay, well, why Why are we making this statement? What are we going to try and do with this statement? It's when you start getting those Slippery little arguments thrown in the in political conversations type of thing. And then this last one is where it all falls down. Security prices move in trends that lasts long enough for investors to act on them. So that knowledge of the past impacts what will happen in the future. That's simply not true. That's simply not true. Because all of that information has already been incorporated in the prices. You know, all about

Alex Murguia 10:40

Bob, I can show you how my 20 year historical, whatever model has has outperformed. So I take umbrage with your assumption there.

Bob French 10:53

Well, um, you know, if you did, you know, I mean, and we'll talk about this later on with some other stuff. But, you know, all of this is random. You know, all you're telling me is, you're really good coin flipper, you know, you got lucky for a long period of time. We're not talking about all of those other people who didn't get lucky, who, you know, didn't do well over the past 20 years, or whatever number of years you want to talk about. At some point, someone's going to do really well, just by chance.

Alex Murguia 11:27

And I'll just, I just did it kinda like the socialize. I'm thinking about if someone's listening in and he's a big proponent. They may say something like that. But you'll we'll answer this in detail later. Yeah, we can continue with the Yeah. Sort of the foundational pieces.

Bob French 11:45

Yeah. So you know that that idea, that knowledge of the past, tells you what's going to happen in the future? Again, just straight up does not work. I don't know how to say it any more clearly, we can get into kind of why and all this type of stuff. But most people agree with that statement. Even I bet if you were to ask a lot of technical analysts, they would agree with that statement, not realizing what they're agreeing to

Wade Pfau 12:13

Yeah and maybe there's patterns, but the idea that you can discern those patterns in a way that no one else has done, which is where it all starts to fall apart immediately. Because once this sort of these patterns emerge, even if they work as soon as people know about them, that's going to create a problem on a forward looking basis, right?

Alex Murguia 12:32

Wade, I don't buy a stock I was gonna buy. I don't know, I was gonna buy Tesla, you know, at the beginning of the year, but I didn't want to buy it because it had gone down so much. And it just wasn't ready for me to buy it. So I waited two weeks, it went up, I bought it and now it's up another 60%. So they're, you're wrong.

Bob French 12:54

So you just gave up those two weeks of returns then huh?

Alex Murguia 12:58

No, I'm just thinking it's a bit of a straw man that I'm providing. But the reality is, I think that's people think that, you know, we get that kind of feedback. No, but you know, I, I never buy a stock, I look at it for the last for the previous two weeks to see where it's going before I buy. And you know what that works for me?

Bob French 13:19

So part of that, I would say is, there's always the tendency stocks tend to go up over time. You know, so there's, there's always that there's a tilted random walk. It's not a big tilt, but you know, it's there. And you also, were really good at fooling ourselves. You know, we've talked to you guys have talked about behavioral kind of finance and behavioral biases. We're really, really good at fooling ourselves. You know, we don't remember when we screw up or we choose to forget, when things don't work out, or there's a reason it didn't work out. It wasn't my fault. You know, who could have predicted what Elon Musk said? Well, actually, that one, probably no one can, but but there's always something else happening.

Alex Murguia 14:13

Here you go. I hear the academics talking about, okay, it's gonna be about these sorts of theories that don't pan out. And you know, they knock me down because I'm using momentum. I get it.

Bob French 14:25

Yep. That's right. We're just we're just mean people. No, I mean, people say that, right? I mean, you hear that. momentum is, momentum is an interesting case. And it's because there is some some stuff in the data where, you know, in you can use all sorts of different screens and things like that. But, you know, stocks that have done well in the past, by and large over kind of a diffuse, diversified portfolio, tend to do better than stocks that have gone down relatively recent. Certainly in the past, and this is actually one of the really, really big questions in finance and investing right now, what's going on here? Because it's very, very firmly in the data, you know, there's a relatively big premium, depending on how you slice and dice things. But why, you know, why are we seeing that? You know, we understand why stocks have a higher return than bonds. And we understand why, you know, value stocks over the very long term have a higher return than growth stocks on average.

Alex Murguia 15:37

And we're going to be speaking about this.

Bob French 15:39

In, you know, yeah, the way we're kind

Alex Murguia 15:41

These episodes we're kind of knocking down kind of certain pillows, pillars that we're going to be standing.

Bob French 15:48

So the question now becomes, okay, all of that's really great. Why do stocks that have gone up relatively recently? Why do they outperform stocks that have gone down relatively recently, and vice versa, and vice versa? You know, it's a premium. So it's, you know, the returns are the good stuff, minus the returns on the bad stocks. So you can still, as we've seen last year, with the value premium, both sides of that equation were negative, everything went down. But the value premium was still pretty darn big. But going back to momentum, I think, most, at least intellectually honest people who are doing momentum, you know, AQR and all these other firms. They'll be among the first to admit, yeah, I don't really have a good story for why. I just know it's there. I just

Alex Murguia 16:47

Wade, it's supply and demand, it's supply and demand.

Bob French 16:52

We don't know it, maybe it is, you know, maybe there's some media effects. Maybe there's some analyst effect, who knows, we don't have a good story yet. And they're simply saying, Okay, we've got, I don't know, 30 years of data, data on this jagged nation, Tim was, I believe, in 91. That was the kind of the first paper really talking about this momentum effect. We've got 30 years of data where everyone knows about this, and it's still there. So the chances of it going away are relatively small. On the other

hand, you have people like myself, who look at this and say, Yeah, that's really weird, it's probably not going away. But before I want to put my money there, or put clients money there, I want to have some understanding of what's actually going on here. Given that we have all these other kind of other ways of approaching this. So there's a lot going on there.

Alex Murguia 17:46

So I think if someone's attending, I think one of the key points you made is that you're looking at this from a portfolio construction level, not necessarily individual stocks. This isn't what we're talking about. Right now. It's not real technical analysis, per se, but it's more like, there's a funny little thing called momentum in the stock market. And the reality is, is that it does exist, but there's no story behind why. And that's important at the fundamental level, because it helps gives this foundational reasoning why why why something is there. If not, you're always in danger of data mining, you know, you're always in danger of doing kind of silly things, you know, from a scientific scientific perspective. Now, could it be used within the portfolio construction construct in a diffuse way? Yes, it can be. And we'll get into that later on. But this is not the technical analysis that we are talking about, you know, we're talking about, you know, how it can be used on potentially portfolio construction and using it to our advantage in addition to the other complementary factors. But in terms of what you're listening to on CNBC, where they're talking about head and shoulders, this and that, and all that kind of stuff. That's silliness. That's something completely different. And we were alluding to it earlier, I don't know why it's so pervasive within the industry, because studies will show over and over that, that it is silliness, you know, we're not going to just review them. And frankly, even if we did, I don't think it would matter because at the core, the story behind it kind of just doesn't hold and so there's, it's not necessary. But Bob, what what do you what are Wade, what what, I don't know, just on a personal level, what do you think are some of the reasons that, you know, it's taken advantage of for, you know, what are your big advantages that you could see, let's say if it did work, that they have, you know, that people kind of hang on to

Bob French 19:49

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Wade Pfau 20:12

Right, yeah, I think Bob talks about a couple of potential advantages that are identified. This is even

Bob French 20:19

Wait since we talked about this. Above, you mentioned that this is in the CFA curriculum. These four advantages are literally from the CFA curriculum. So

Alex Murguia 20:31

Wow.

Wade Pfau 20:33

It's quick and easy.

Alex Murguia 20:35

It's quick and easy. I like that.

Wade Pfau 20:39

It doesn't require digging into company balance sheets, you don't have to worry about accounting data and price to book ratios or anything like that.

Alex Murguia 20:47

SMAP.

Wade Pfau 20:51

It does bring in the idea that there's some sort of psychology because of that this idea that there is a rational and irrational factors that work in determining the movement of prices. And it gives you some clues about when to buy and sell particular assets. Yeah, so those are the advantages. But let me think about does it work? It'd be the big question.

Alex Murguia 21:13

We'll teach you how to trade in the stock market without teaching you anything actually about the stock market? Right? It's kind of a lazy person's way of thinking. And just if you take a step back, every freaking scam in the world, when you peel the onion far enough, it's about hey, look, lots of money. No work. Here you go. Right. I mean, I don't know. There were those commercials. I don't know. Whatever happened, I think was I will teach you to trade or something like that. On weekends, those those infomercials where it's a red light green light yellow light signal, you get a green light, you buy red light, you sit you sell yellow light, I don't know, maybe right. And they would teach people this and they would bring them into these hotel ballrooms and stuff like that. And they made money by, by, you know, by preying on the marks really, at the end of the day, no one made money on I'm sure of doing this, even though they had these testimonies, which I don't know how they would do it legally, but whatever, right? But the reality is, is that it's just it's, it's silly, you know, in these levels, they they really, the four big advantages is quick and easy. doesn't include data. You can go home now incorporates psychological factors, and it tells you when to buy and sell. I mean, it's like a genie. Right?

Bob French 22:36

Yeah, no, my favorite example of this is one of the big kind of systems of how people do this was called the Dow Theory. And it was graded back, I want to say in the 30s, based off of Dow, you know, editorials that he wrote, the guy who created the Dow Jones indices. There was a, you know, pretty soon after it kind of was systematized, there was someone who, in the 30s went back and looked at okay, how did this actually do? It was, what was his name was Alfred Coles. He looked at Okay, is it better to buy and hold a bunch of stocks, you know, over this this time period? Or was it better to follow this Dow Theory, and, you know, from the period 1902 to 1929, buy and hold one. So all the way back in, I think it was 1934, we knew this thing didn't work. People are still using at least a modified version of Dow Theory. Right now, nearly 100 years after it was already shown it didn't work. But it gives you

Alex Murguia 23:51

It's really fancy the word theory is in it, it must work.

Bob French 23:53

it's much theory. It gives you one of the big advantages, it gives you definite answers. A lot of the other ones you give to people following the same approach, the same set of information will give you different answers. Most of the time people do in the Dow Theory get the same answers. So it's much more scientific.

Alex Murguia 24:12

I think something that yeah, that brings to mind when you're talking about this because there are you know, people can look can look backwards into data and identify patterns that actually did work. You know, they can do that they can look at you know, they can provide these backward looking sort of machinations and say, Aha, here it is, right? And then they you know, they go forward and when they do or they publish an article on it, everyone knows about this. And when those things happen, they kind of they kind of like when it could be random but more importantly when everyone kind of knows about it dies out I know Swedroe Oh loves to write about. I forget the article that he points out but something along the lines of their their various trading strategies that you can look back and figure out oh, wow, it did work. But as as, but they're done again, post hoc, they're done after the fact. Because there's no story because there's no like risk story behind it, because there's no this overarching kind of thing. And you said something interesting about trend in general. But when you start really, you know, giving it these sort of interesting twists and turns to these strategy, because there's no real story behind it, it kind of dies out once it gets surfaced. And these folks have this idea, and I'll say it one more. And these folks, then these technical rounds have, effectively a get out of jail card, which is, oh, I just need to refine my model now. But if you're constantly refining a model, constantly refining a model, because it no longer works. Remember, you never had a foundational story for why it should even manifest to begin with. So if you're constantly refining, constantly refining, constantly refining, then after a few years, your model looks something completely different than what you started with. It's almost like give the value a value moment, a value factor strategy became a growth strategy without knowing after a while, you know, I mean, like, it's, it's, you're giving yourself that get out of jail card to kind of resubmit, and revise, revise and resubmit, revise and resubmit, when, in fact, there shouldn't have it shouldn't have even it should have been, like, rejected from the very beginning.

Bob French 26:19

Absolutely. Yeah. I mean, it's, it's entirely data mining, and not even good data mining at that.

Wade Pfau 26:29

Yeah, and just so data mining is if you look at data long enough, you can see some sort of pattern and whether or not that pattern reflects something that has a true economic story behind it, or whether that pattern is just the result of randomness. Like it's plenty of when you look at clouds, you can see images or faces or things, and that's called pareidolia. And I had to look that one. Pareidolia, it's the picking up at the clouds and seen a face or are seen an image in something where there's clearly not an image, that human brain is designed to recognize patterns in randomness. And that's what I think a lot of this technical analysis is, is if you look at random data, eventually you're gonna see some sort of pattern in it. And that's then does that pattern mean anything? And is it useful on a forward looking basis is no big question. At that point.

Alex Murguia 27:31

I agree. I think look, I think what really put this to rest for me, and I don't, I don't know, the study, I thought my head anymore, because once I read it, not that I read it, but once I read about it, I'm more of a abstract kind of guy. And I go to the conclusions afterwards. But once I came across it, I was like, Okay, there's nothing here time to move on. You know, and I don't bother. But there was a study that that effectively, you know, gave random patterns to folks literally gave random patterns to professional Chartist. All right. And then gave stock patterns to those professional Chartist. And it asked them to indicate which ones fake and which one's real. You know, where I'm going with this, they, they couldn't tell the difference. All right. And so sit back and think about that for a second. You know, all the people that are listening in and they're thinking to themselves, yeah, but what if, yeah, but you know, that kind of thing, right? So think about if I were to give, I would do create random, like heart rates, you know, what do you call that thing when you take, you know, your heart, you EKG, right, you get an EKG, right? Remind me Bob to go to the doctor after this. Yeah, you get random, like heart rate patterns, right? You create them, you create random ones, just so you're ever you just go crazy, right? And then you have actual EKGs and you show them to a doctor, I think you'll get a completely different sort of result, they would know like, hey, this person should have been dead 10 years ago, versus Okay. The first and you know, whatever, right? And so, if a professional cannot tell a difference between just random charts and an actual stock pattern, and the random charts they were giving it all this is the Head and Shoulders whatever this is the dead cat, whatever, you know, that kind of thing. What does that tell you about the profession? It's a joke. You know, you need to run and like when you hear this thing on like I Yeah, CNBC when they get into the hole, oh, well, the the s&p is definitely hitting on resistance. And I wouldn't buy until it it drops below this because that's the sweet spot. Guys have no clue what the hell they're talking about. They really don't. They're just saying that because it fills up air time. And it's easy to say and it comes across like this air every addition but it's it's just like complete silliness. You know? it to a degree that it's professional, irresponsible, but you know, they go ahead and do it because it's easy. It's easy, and it's sometimes you gotta like, strip out the the reasoning to its basic core. And it's just lazy, easy thinking. And that has been the cause of who knows how much lost money, which is the real issue here. You know, at the end of the day, we're not trying to lessen and I wish it were, there'd be a lot more people with, with, you know, with more assets in their retirement accounts. But the fact is that the inverse occurs. And so, you know, it's one of those that we can't be nice and just Oh, okay. It's another way of doing things. No, it's an irresponsible way of doing things.

Bob French 30:44

Yeah, yes. Plus, it takes a lot more time than doing it right. So

Alex Murguia 30:51

Yeah, I mean, and so you gotta ignore that, you know, from the standpoint of, oh, I don't want to put money in because we're in a, I don't know, cup saucer chart or whatever. I don't know, I think there is something called cup saucer.

Bob French 31:07

No, there is one. There is a cup and saucer chart. Yeah,

Alex Murguia 31:13

I will say this. And Bob and I share this. I love the names that they give them. I love the names. I wish. I wish we had like creative names like this indexing strategy. But, I mean, what I know but even these names, give it the sense of like, trade floor, sort of savviness which it's silly. I mean, Bob what what are some gems here?

Bob French 31:44

Yeah. Yeah, some of my favorites are bollinger bands, detrended price oscillators, vortex indicators.

Alex Murguia 31:57

Well go on, go on sorry, this

Bob French 31:59

triple lending my my favorite is the ultimate oscillator. We also got kaput curves. donchian channels. Okay, but Wade, I've got a question for you. Which one do you think it was?

Wade Pfau 32:18

I'll triple lindsay Sounds like a figure skating jump.

Alex Murguia 32:22

No. It's made up but it's not a figure skating jump. Come on. Wade, Wade. Triple lending.

Wade Pfau 32:32

Is that where you start backwards spin three times and land.

Alex Murguia 32:37

It's from the movie. Back to school. It's a Rodney Dangerfield movie. He goes back to school to he's like a guy from the streets, right? Never went to college, etc. But what successful plumbing was the plumbing thing. We've been talking about it lately. He he joins us that he joins his son and you know, one of these kind of father son movies. And he was a he was famous for jumping off like, like piers in like jersey shore or something like that. And so he joins the swim team. And the swim team is losing and his sons on the swim team and so Dad, you got a job. You got to come back you still qualify for the NCAA is? And so he says all right, fine. And his famous jump was the triple ending so you have Rodney Dangerfield doing these backflips? I think it was on three boards hence triple and and I legend is born way there you go the triple Lindy.

Wade Pfau 33:39

So that right answer.

Alex Murguia 33:41

Yeah, you gotta you gotta give me your full credit.

Bob French 33:51

But so, yeah, but we can make jokes about all this stuff. But it's really easy to do quite a stretch to come up with this joke here.

Alex Murguia 34:02

You have the dungeon channel. What is that?

Bob French 34:05

You know, I don't even remember I came up with this list a while back. But I you know,

Alex Murguia 34:11

that sounds like Lord of the Rings. And you're trying to go into you know how they went into the tunnels that were dangerous. It sounds like oh my god, we got to go through the donchian channel. Sorry Bob.

Bob French 34:25

We'll leave it there. But I think broadly, one of the things that you're going to find when you start looking at these things is technical analysis really falls into two broad viewpoints. And they basically cover the entire spectrum. So there's contrarian views, which are investors are usually wrong. So do the opposite. And then there's the quote unquote, Smart Money view, which still says everyone's dumb. Most people are still wrong, but The smart people know what they're doing. So follow the smart people follow the institutional folks. Now one thing I'll call out, how big do you think the institutional market is relative to say, the retail market, it's pretty massive. So between those two ideas, do exactly the opposite of everyone, or do what the institutional money is doing. You basically have everything you can do pretty much whatever you want, and it will fall into one of those two categories. And, you know, we can get in, I don't want to get into all the different theories. We already talked about, you know, there's we mentioned Dow Theory earlier on. But there's things like Elliott Wave Principle and stuff like,

Alex Murguia 35:47

Going, going back to that comment. I'm just trying to make sense that because the first time I'm hearing in this manner, are you saying that they cover both angles? So the theories, the broad viewpoints cover the entirety of market participants? Yeah. Hence, what does that mean? Because I kind of think you kind of think it, but I'm not 100%. Sure.

Bob French 36:09

What that means is you can justify whatever you want to do. You know, it's it's one of those where it's a theory, or it's a solution in search of the theory to get you to that solution. You know, if you think that Cisco is going to do well over the next week, whatever you want to call it. There's something in that chart, there is some theory out there that will say this chart says Cisco is gonna go through the roof. You know, there's also some theory out there that says Cisco is about to crash and burn, using the exact same set of data. And it's just a matter of, Okay, which one do you pick? You can pick?

Alex Murguia 37:02

Which one? Can you which one can you identify after? Because there's always four? Absolutely. Before, it just depends if you're a pessimist or an optimist, I guess, right?

Bob French 37:11

That's the fact of what it comes down to. Yeah,

Wade Pfau 37:16

this Smart Money view, is it? What's the modern world of technical analysis is that people are supposed to do this on their own. Are they supposed to buy funds, where they are the experts running? analysis for the year?

Bob French 37:29

Are you selling a book to tell them how to do it themselves? Are you selling a fund?

Alex Murguia 37:34

A smart money view, was like that guy. I remember Laszlo barrini. I don't know if he is still around, but he will follow the institutional fund flows. Yep. You know, that, that kind of thing. I think they even mentioned him in the book, predators ball, where she was like, equities in Texas, was like, investment bankers that were terrible. They sent them down to Texas to work on equities. And I think Barrini could have been part of that group. You know, that that kind of thing. But, yeah, I mean, he was a money manager that made his living off of just selling the idea that I'm following institutional fund flows, you know, and the reality is this, if you're, if you, the folks that make the most money off of these trend following strategies, are newsletter publishers. That's it, you know, and those folks aren't regulated, as advisors, you know, their publishing companies, they can write whatever the heck they want, over and over, and over and over. And it's not like if you're, if you're, and if they shoot out 10 potential things that could, that can work, right. And two months later, one of them works, they're going to point out, hey, our strategy worked for etc, etc, etc. And then the ones that didn't, they're just gonna bury them, and you're not going to hear from them again. And they're going to perpetually Polish stuff like that over and over and over. Or they're going to say, hey, our three stocks returned 10,000%, over the last 10 years or something like that, because out of the 500 stocks that they recommended, one of them happened to be Amazon, right? I mean, it's very easy, and they're gonna they're gonna point to some sort of trend following strategy that that led them to that thinking. You can do that when you're publishing newsletters because you're just not held accountable. It's simply like CNBC to they're not held accountable. Nobody goes back to CNBC and says, Hey, Tuesday, three months ago, you said this, based on the resistance levels, and guess what, it didn't work out. So now what are you gonna say have a coconut smile and move on? You know, that that kind of thing. And so, yeah, I don't know. I don't know where I went with that. Other than like, yeah, they're giving themselves they're giving themselves always a get out of jail card. You know, by by the way that they're, they're presenting this and Bob was 100% Right there. Are there solutions if you will in search of something?

Bob French 40:04

If you're looking for more personal advice, please know that our show is sponsored by McLean Asset Management. Learn more at McLeanam.com. That's McLeanam. com. McLean Asset Management is a wealth management firm where we help you design and implement the right retirement plan for you. So the I think the most important there was a coconut smile. Where's where's that from?

Alex Murguia 40:33

Bob man? Commercials, man. commercials have a crooked smile. And it's actually a reference to Eddie Murphy. I think it was delirious. The standard showed the day you asked, right. Eddie Murphy delirious, and he Eddie Murphy would cuss a lot, right. And so at the time Bill Cosby got in his case of all people, Bill Cosby, right. Because we got in this case for like cussing, because we always presented himself as the family man's comedian. The irony is deep for, you know, the family, man's comedian, etc, etc. And Eddie Murphy wasn't having it. At that time. You got to remember Eddie Murphy was like, the star of Saturday Night Live had a best two best selling album stand up and was on the top move. You know, it was number one box office person. And so he's there at top of the world. And he's like a booker. And he's talking about the story how Bill Cosby contacted him about cussing. And Eddie Murphy just says, Bill, enter cuss phrase, have a coconut smile. And that became kind of a soundbite if you grew up in the 80s. So that is a side note side note. Bob has never seen the godfather. That's right, which I think is a failure on many levels. Wade, have you seen The Godfather?

Wade Pfau 41:56

I have.

Bob French 42:00

Let's let's set the stage here. So Alex, you could probably tell his undergrad degree is actually in film major in school, which actually I think tell you a lot. A lot about him.

Alex Murguia 42:15

But everyone just dropped off the podcast.

Bob French 42:22

Godfather at this point, it is your pure spite that keeps telling you I have to so I will not do it.

Alex Murguia 42:30

Well, I mean, it's art. No, but Bob initially said, Oh, it's because it's beyond my time. But you know, that kind of thing? And I'm like, That's a silly answer. Because, yeah, but so what it's a stupid answer, because it's not like I've seen sort of, uh, you know, I wasn't born during Citizen Kane. I wasn't born during rush Oman. I wasn't born during whatever, you know, all these movies at at a certain point. It's your job as an American citizen. to In fact, I showed it to my kids, I want to say about a month ago, you know, simple because it's, how can you not? It's art. Godfather two is coming up. But how do we get into this? Oh, you asked me about how a coconut smile. Wade, I don't know. What do you think about this whole godfather nonsense?

Wade Pfau 43:19

Yeah, I haven't seen Godfather 2 yet.

Alex Murguia 43:21

You haven't seen God? Oh, my goodness. Wade. Godfather 2 in many ways is better than Godfather 1. It's It's amazing. It's an amazing film. I mean, I'll just leave it at that. I'm just now I'm stunned. Let's go back to technical analysis. I don't know how to recover from this movie choice of you too.

Wade Pfau 43:43

Yeah, yeah. So why doesn't this. What are the reasons why why shouldn't technical analysis work in practice? I guess that's really the main thing we should make sure we've covered in enough depth to not have the entire episode BS bashing on technical analysis without any sort of reason why we don't think it's a good system.

Alex Murguia 44:10

Voodoo is not a good enough reason for you Wade?

Wade Pfau 44:13

Well, Bob, you've pointed out Yes, since the 1930s, there's been these studies that just show the stock market, it's really a random walk with drift that's is a long term investor, we do expect the economy to grow and for stocks to rise over time. But for any given day to day movements, the idea of the random walk is we don't know if tomorrow's stock movement would be up or down. Technical analysis tells us we do know we can predict we have a much better than a coin flip chance of knowing future directions in a manner that goes beyond just the general trend upward over time. And if that's the case, like if that's kind of the whole the whole point of this conversation is if there was some way to be able to predict better than a random chance what the market was about to do, wouldn't that cause people to use that technique in a manner that then wipes out the ability to have that predictive power, it will get baked into the price. I think that's ultimately, if if people know about technical analysis, everything that we know about technical analysis, even if it was correct, should get fed into today's current price in a manner that there's no way for any additional predictive power to be there. Because if there was, we'd use it. And we'd, if we predicted that the market should go up tomorrow, we buy the stock today. And that pushes the stock up today such that then tomorrow becomes random. And that's the biggest problem with something like technical analysis, right? It just simply doesn't provide any sort of mechanism for us to think there is still predictable power beyond what we already know.

Bob French 45:52

Exactly.

Alex Murguia 45:53

I agree. And I want to, I want to say how that echoes, the previous comments, and why that's important, just on a foundational level from an investing framework level, right? So there is no persistency. Right? There is no persistency. Because there's no economic reason for there to be this sort of advantage, right. And this is different than, let's say the value premium where people know about the value premium. But it still persists, right? And so we'll get to that later, when we talk about value investing, right? But there is no persistency here. And so that's the ultimate, it's rudderless. Because of that, the second piece to bring out and this is when Bob was making his point about smart money and contrasting contrarian views, you can have these two view, viewpoints about it sets yourself up on a human level to give yourself this out. Because you can then provide why it went up based on technical analysis or why it didn't work based on technical analysis, and then you need to refine your model, but you'll get it next time. And that's just, you know, that's like what a Flim Flam man sort of does. You know, when, when he's setting you up for a con really, ultimately, and so you just need to be aware of those things that if there's no when there's no science behind it, you know, it looks like it's sciency.

Because look at these charts, and all that. But when there really isn't any, anything there from an anchoring perspective, you just simply need to move on. It's as simple as that. And I think Wade said it wait is pointing out the persistency. And the reasons that we said earlier in the podcast, our lack of a foundation and this openness for various various interpretations that are very convenient. It sounds like astrology to me at that point.

Wade Pfau 47:57

And ultimately, that's kind of it follows along the same sort of category. It's, like I said earlier, the human mind is designed to look for patterns, even if they're finding those patterns in what's otherwise random. And thinking you see all these patterns and stock market movements, it just seems to me like it's taking that same sort of natural human tendency in the direction of trying to predict stocks in a manner that just can't really be done in practice, and that we've known since at least like the 1930s that can't be done in practice. And, and that's really all there is to say about technical analysis.

Alex Murguia 48:33

Yeah, no, no, no, I agree. Let me let me maybe bring it to a little practical thing. Bob, have you ever used technical analysis in any way shape or form to get into or out of a position?

Bob French 48:47

No, no, I have not Alex

Alex Murguia 48:50

Okay. No, no, fair enough. I'm just Yeah, and this is not like dollar cost average or this or that this is just like have you ever thought hey, I've got money's burning in my pocket? I want to put it in but not yet. I'm just so people know that we walked this talk you know, weigh yourself and I didn't ask anyone beforehand so I'm flying blind here to imagine a weight says yes all the time. But you did use this any in any way shape or form

Wade Pfau 49:21

No, no, this the general ideas Doc's hopefully will go up over time. And so if you have money to invest, just put it in the market don't try to say Oh, next week, it's gonna be a better investing environment

Alex Murguia 49:32

Yeah when it hits the moving day average or something like that. Alright, yeah. myself. I think you know my answer. It's a big no. So there we are. Anything else for today?

Wade Pfau 49:46

No, that'll do it. But we maybe preview what's coming next, Bob. Going to be going through technical analyst

Bob French 49:52

next week, we're actually going to talk about, I think something that's actually a lot more interesting, which is fundamental analysis. Which is when people are trying to predict what a stock price or a price level or whatever it might happen to be, should be at. Now, it doesn't work for most people. But it does

provide some really, really important stuff going on on the markets. And we're gonna dig into what exactly that means next week. But it's a much, much more interesting story to tell than technical analysis. It just don't work. Fundamental analysis. It works depending on your definition of work.

Wade Pfau 50:38

And that's where we have to start digging into balance sheet

Alex Murguia 50:44

You actually have to do work unfortunately,

Bob French 50:46

There are actual spreadsheets involved in this one,

Alex Murguia 50:49

so yeah, but Bob, your wizard at Excel.

Wade Pfau 50:55

So thanks, everyone. Now, I was looking for something quick and easy. It sounds like fundamental analysis may not be the one.

Alex Murguia 51:09

All right. All right, everyone. Thanks again. appreciate you spending the time with us and we'll catch you next week.

Wade Pfau 51:17

Yep, take care everyone.

Bob French 51:19

Wade and Alex are both principals in McLean Asset Management and Retirement Researcher. Both are SEC registered investment advisors located in Tyson's Virginia. The opinions expressed in this program are for general informational and educational purposes only and are not intended to provide specific advice or recommendations for any individual or on any specific securities. To determine which investments may be appropriate for you. consult your financial advisor. All investing comes with a risk including risk of loss. Past performance does not guarantee future results.