



It's nuts to think your current portfolio will hold up when the next downturn hits

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Let's just agree on this first.

Most portfolios today are not optimized. They're stuffed with too much risk, tangled up in illiquid bets and padded with assets that are – let's be blunt – overvalued. That's fine when markets only go up. It won't be fine when gravity kicks in, which it will.

If only markets functioned like my roll of dog poop bags, where the sticker clearly warns: three bags left.

Several core metrics suggest equities are priced well above historical norms. The Shiller CAPE ratio is nearing 40 – more than double its long-term average of 17. Such levels have often preceded weak returns. The Buffett Indicator, at roughly 200 per cent of gross domestic product, also flags stocks as far more expensive than the economy beneath them.

Anecdotal information is sending us warning signals: evidence of heavy retail participation in the stock market, elevated meme stocks and the notion that "it's different this time." The recent string of fund gating notices, restricting investors ability to sell or withdraw money from funds, are signals, too, as they can be evidence that

valuations don't allow for asset sales without loss recognition or problematic liquidity mismatches. At a minimum, they likely expose a fragility.

High CAPE ratios, concerns about public and private fundamental valuations, and signs of fragility do not go well together.

The problem of inaction

What keeps investors frozen isn't a lack of risk awareness – it's paralysis. Go to cash? Rebalance? Let it ride?

The truth is, nobody knows how long this party lasts or what will end it. Is the gold rush actually a crowded store of value trade? Will it be fundamentals snapping back, a private equity bubble shell game reveal, gating headlines sparking asset sales? Take your pick.

What we do know is this: When the turn comes, there will be no one to blame for a lack of preparedness but ourselves.

The myth of staying invested

Plenty of smart people have been warning us to pause, or better yet, to act. Fundamentals still matter, even if technical factors drown them out for a while. And right now, the technicals are winning: record index levels, mega-cap concentration, a chase for yield and price momentum that is feeding optimism.

Elevated valuations set the stage for heightened sensitivity to earnings disappointments, policy shocks or deteriorating macro data.

Against that backdrop, we've all been told that "staying invested" is the only way. Really? The largest asset management institutions love the mantra – it keeps your money in their products and their fees flowing. They repeat it with near-religious fervour. It's convenient, isn't it?

But consensus can be dangerous. Smoking was once healthy, bloodletting was medicine, and yes, cocaine really was in Coca-Cola.

The point here isn't market timing. You don't need to guess the day the roller coaster jumps the rails – you just need to reposition safely before it does.

So, what should you do?

Go to cash? No.

Rebalance? Yes, as a start.

Let it ride? Only in carefully chosen assets, while protecting the rest.

Here's what that looks like in practice:

- **Add defence:** Staying invested doesn't mean staying unprotected. Mix in stability with reasonably valued stocks, low-volatility investment-grade bonds, or a transparent, semi-liquid mortgage fund instead of something opaque and illiquid.
- **Favour safety:** When valuations stretch, margin of safety matters. If picking funds, look for a proven "downside capture ratio" near zero – or better yet, negative – so they fall less, or even gain, when markets drop. If picking stocks, consider looking for compelling price-to-earnings versus their industry.
- **Demand Sharpe:** In easy markets, risk feels invisible. Now is the time to choose managers delivering more return per unit of risk, ideally with a Sharpe ratio of 1, or more.
- **Check track records under stress:** Don't just chase bull-market heroes. Look for managers who protect capital through downturns; monthly returns (always after fees) versus benchmarks can tell the true story.
- **Use smart beta:** You don't need the whole index just because it's "what everyone owns." There are smarter substitutes with built-in defensive tilt.
- **Be intentional with illiquidity:** If you've got conviction in a private deal, great – but balance it with extra liquidity now. With valuations stretched, flexibility will be king when new opportunities emerge.

Clairvoyance isn't the point

This isn't about knowing exactly when the party ends. It's about not being the one left to clean up the mess. Unfortunately, we can't rely on poop bag stickers for that.

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