

## OUTSIDE THE FLAGS

**Jim Parker,**  
Vice President  
DFA Australia Limited



NOVEMBER 2015

# Second-Hand News

Why don't the media run more good news? One view is bad news sells. If people preferred good news, the media would supply it. But markets don't see news as necessarily good or bad, rather in terms of what is already built into prices.

One academic study appears to confirm the view that the apparent preponderance of bad news is as much due to demand as to supply, with participants more likely to select negative content regardless of their stated preferences for upbeat news.<sup>1</sup>

“This preference for negative and/or strategic information may be subconscious,” the authors conclude. “That is, we may find ourselves selecting negative and/or strategic stories even as we state that we would like other types of information.”

So an innate and unrecognised demand among consumers for bad news tends to encourage attention-seeking commercial media to supply more of what the public appears to want, thus fuelling a self-generating cycle.

Insofar as consumers of news are investors, though, the danger can come when the emotions generated by bad news prompt them to make changes to their portfolios, unaware that the news is likely already built into market prices.

<sup>1</sup> Trussler and Soroka, “Consumer Demand for Cynical and Negative News Frames.” *International Journal of Press/Politics* (2014)

This is especially the case when the notions of “good or bad” are turned upside down on financial markets. For example, stocks and Treasuries rallied and the US dollar weakened in early October after a weaker-than-expected US jobs report. Some observers said the “bad news” on jobs was “good news” for interest rates.<sup>2</sup>

Conversely, a month later, stocks ended mixed, bonds weakened and the US dollar rallied after a *stronger*-than-expected payrolls number. While an improving job market is good news, it was also seen by some as cementing the case for the Federal Reserve to begin raising interest rates.

In both cases, the important thing for markets was not whether the report was good or bad but how it compared to the expectations already reflected in prices. As news is always breaking somewhere, expectations are always changing.

For the individual investor seeking to make portfolio decisions based on news, this presents a real challenge. First, to profit from news you need to be ahead of the market. Second, you have to anticipate how market will react. This does not sound like a particularly reliable investment strategy.

Luckily, there is another less scattergun approach. It involves working *with* the market and accepting that news is quickly built into prices. Those prices, which are forever changing, reflect the collective views of all market participants and reveal information about expected returns.

So instead of trying to second-guess the market by predicting news, investors can use the information already reflected in prices to build diverse portfolios based on the dimensions that drive higher expected returns.

As citizens and media consumers we are all entitled to our individual opinions on whether news is good or bad. As investors, though, we can trust market prices to assimilate news instantaneously and work from there.

In a sense, the work and the worrying are already done for us. This leaves us to work alongside an advisor to build diverse portfolios designed around our own circumstances, risk appetites and long-term goals.

There’s no need to respond to second-hand news.

<sup>2</sup> Hulbert, “How Bad News on Wall Street can be Good News.” *WSJ MarketWatch* 5 October 2015.



“Outside the Flags” began as a weekly web column on Dimensional Fund Advisors’ website in 2006. The articles are designed to help advisors communicate with their clients about the principles of good investment—working with markets, understanding risk and return, broadly diversifying and focusing on elements within the investor’s control—including portfolio structure, fees, taxes, and discipline. Jim’s flags metaphor has been taken up and recognised by Australia’s corporate regulator in its own investor education program.

For more articles, visit Dimensional’s client site at [my.dimensional.com/insight/outside\\_the\\_flags](http://my.dimensional.com/insight/outside_the_flags)

This material may refer to Dimensional Australian Resident Trusts offered by DFA Australia Limited. These Trusts are only available to persons in Australia and New Zealand in accordance with a Product Disclosure Statement (PDS) for the Trusts. The PDS is available from DFA Australia Limited as the issuer of the PDS, (ABN 46 065 937 671, Australian financial services license no. 238093) or by download from [www.dimensional.com.au](http://www.dimensional.com.au). Investors should consider the current PDS in deciding whether to invest in the Trusts, or to continue to hold their investments in the Trusts. Nothing in this material is an offer of solicitation to invest in the Trusts or any other financial products or securities. All figures in this material are in Australian dollars unless otherwise stated.

Dimensional Fund Advisors LP (“Dimensional”) is an investment advisor registered with the Securities and Exchange Commission.

All expressions of opinion reflect the author’s judgment at the date of publication and are subject to change without notice in reaction to shifting market conditions. This material is provided for informational purposes, and it is not to be construed as general financial product advice nor an offer, solicitation, recommendation or endorsement of any particular security, products, or services.

©2015 Dimensional Fund Advisors LP. All rights reserved. Unauthorised copying, reproducing, duplicating, or transmitting of this material is prohibited.