

## Chasing High Flying Stocks Risks Meme Reversion

As the pandemic dragged on, many people started new hobbies, including baking sourdough bread and binge watching television. Some even tried day trading meme stocks (a meme stock is a stock that gains popularity among retail investors through social media).

With stimulus checks in hand, commission free trading platforms widely available, and time to spare, some retail investors opened brokerage accounts and downloaded trading apps. For example, new Robinhood accounts more than tripled from the start of the pandemic through March 2022.

Some of these new investors dove into the market for entertainment purposes and potential riches, but many dropped out after experiencing the reality of the roller coaster of short term trading. While it can be difficult to tune out the “get rich quick” hysteria, doing so may save you and your finances from being taken on a wild ride. The potentially smoother journey that diversification

offers may be less entertaining, but it generally makes for a better experience.

The infamous meme stock AMC Entertainment Holdings serves as an example of how investors’ experiences with the same security can be dramatically different. Let’s talk about hypothetical investors who bought AMC on January 27, 2021, when the stock hit a record trading volume of 1.2 million shares and closed at \$19.90 per share. Investors who sold on June 2, 2021, on the second highest trading volume day, at the all time high closing price of \$62.55, had a gain of 214%.

On the other end of the spectrum are those investors who held onto AMC through many wild swings, thinking that the stock was on its way to the moon. But after a tumultuous year, they finally gave up and sold AMC on January 31, 2022, at a 19% loss. Meanwhile, over the same one year period, the Russell 3000 Index gained 18% with far less volatility.

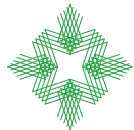
### The Harder They Fall

#### Drawdowns of Meme Stocks

Stocks	Peak Price	Peak Price Date	Maximum Drawdown	Maximum Drawdown Date	Close as of May 31, 2022
AMC Entertainment Holdings	\$62.55	6/2/21	83%	5/11/22	\$14.34
Eastman Kodak Company	\$33.20	7/29/20	70%	1/28/22	\$4.62
GameStop	\$347.51	1/27/21	88%	2/19/21	\$124.74
Workhorse Group	\$41.34	2/4/21	94%	5/11/22	\$3.09

Past performance is not a guarantee of future results.

Source: Bloomberg and Dimensional



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Our example of AMC uses the benefit of hindsight to show that riches are not guaranteed and deciding when to sell is easier in theory than in practice.

To have the chance of striking it rich on a single stock, you must pick the right one before it goes up. Of the names in the Russell 3000 Index, less than 2% (46 names) gained 200% or more over the course of any two week period from March 2020 through May 2022. As shown in the table, some of these names were notable meme stocks like AMC, Eastman Kodak, GameStop, and Workhorse Group, each of which is down substantially from its high.

In fact, approximately 30% of the 46 names ended up underperforming the Russell 3000 Index through May 2022. And only about 25% of the 46 names went on to subsequently outperform the Russell 3000 Index through May 2022. So the key takeaway is that holding a diversified portfolio with many names decreases the probability of a permanent loss and

increases the likelihood of owning stocks that drive market performance.

Even within our retrospective sample of stocks with very high short term returns, market outperformance is not guaranteed. And, of course, without the benefit of hindsight, the odds are heavily stacked against the meme stock investor. Chasing individual names in hopes of catching a meme stock phenomenon may be tempting, but market data indicates that you are taking a big risk.

We feel that you would be better off investing for the long term in a diversified portfolio specifically designed to meet your individual wealth management goals. As you do this, it is important to always keep these three investment principles in mind:

- Diversification has been called the only free lunch in investing
- Uncertainty is part of investing
- Investments should be aligned with goals

### Contact us with any questions or comments

800.586.0600 or 310.772.2600 or by email

Bruce Mandel, bmandel@wealthenhancement.com

Tom Doxey, tdoxey@wealthenhancement.com

Maxwell Kayajanian, mkayajanian@wealthenhancement.com

Peter deMartino, pdemartino@wealthenhancement.com

Joel Callagan, jcallagan@wealthenhancement.com

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