THE ONLY CERTAINTIES IN LIFE ARE DEATH AND TAXES ... AND MARKET VOLATILITY

How to Ride the Wave During a Volatile Market

During volatile times, many investors get agitated and begin to question their fundamental investment decisions and choices. This is especially true for those investors who monitor their portfolios daily and/or feed into the minute-by-minute media magnification. The temptation to pull out of the market and wait on the sidelines until it seems safe to dive back in can be a strong one. However, attempting to time the market can be extremely difficult.

Our job is to help you make your investment decisions in a less or even non-emotional manner and maintain your focus on your personal situation. It can be very helpful to understand that equity market volatility is a normal part of the investment experience and is inevitable. Equity markets can always move up and down, especially over the short-term, leading to our headline that the only certainties in life are death, taxes and market volatility!

Your investment portfolio should include a plan that maintains a long-term horizon and ignores the short-term fluctuations (i.e., volatility) of your equity investments. If the daily swings in the stock market seem too chaotic, remember these movements are near impossible to fully predict. For many investors, there is no reason to even subject themselves to daily market headlines. If you have a long-term investment horizon for your equity holdings of at least five years, chances are the current volatility will pass – possibly in a couple of weeks, months, or in at least a couple of years. Here are some points to remember:

▶ **Try to keep things in perspective.** Market pullbacks (typically defined as between 5-10%), corrections (defined as 10-20%) and even bear markets (defined as 20% or more) are a normal part of the stock market cycle. According to Guggenheim, the S&P 500 has declined between 5% and 10% 78 different times since 1945. The average time it took to recover to its previous highs was about only one month.

▶ **Volatility and risk are not the same thing**. When a stock is "volatile," it means that it tends to make big moves (up or down). When a stock is "risky," it means that it can lose money (go down). In financial terms, risk is the potential permanent loss of money whereas volatility is how rapidly an investment tends to change in price. Volatility does not just imply risk of loss. Volatility simply refers to the price action. Some investments may be more volatile than others. As an investment category, equity investments are much more volatile than a bank deposit, but that doesn't mean an investor should avoid equity investments. A more volatile investment does not necessarily mean it's riskier in the long term. Investors should always discuss with their financial advisor the potential of short-term volatility affecting the daily value of their investments and plan their investments accordingly.

▶ Short-term movements of the market are unpredictable and do not abide by any average. Equity markets are never going to produce straight line returns for investors. For example, in 2017, the stock market had an unusual year in which it did not deliver a correction of 5%. Meanwhile, the fourth quarter of 2018 brought investors the steepest correction in a decade following a greater than 10% decline in the first quarter of last year.

At any time, the equity markets could see a market correction (a retreat of 10% or more). Here are four facts that can help investors understand market corrections:

FACT 1: Corrections are part of the investing experience.
Since 1950, the S&P 500 has undergone 37 separate stock market corrections of at least 10%, not including rounding (i.e., declines of 9.5% to 9.9%). Considering that it's been over 69 years since 1950, this works out to a correction, on average, every 1.87 years.

FACT 2: The average length of those corrections was about six months.
According to data from stock market analytics firm *Yardeni Research*, the S&P 500 has spent 7,135 calendar days in correction since the beginning of 1950. Since then, there have been 37 corrections of at least 10%. This works out to an average resolution time of 192 days, or slightly more than six months. Of these 37 drops in the market, 23 of them have been resolved in 104 or fewer days, with only seven lasting longer than 288 days. Eleven of the 14 instances that lasted longer than 104 days occurred between 1950 and 1984.

KEY POINTS

- Market volatility is not the same as market risk
- Corrections are a part of the investing experience
- Beware of media magnification
- Avoid making emotional decisions
- Focus on your personal goals and call us with any concerns

S&P Index Since 1950

FACT 3: "Rally" days outnumber correction days 2.55-to-1 since 1950.
Since 1950 until May 13, 2019, there have been a total of 25,335 calendar days and over 69 years of data. During this time span, the S&P 500 has spent 7,135 of those calendar days tumbling from a peak to a trough. For the other 18,200 calendar days, the S&P 500 has spent its time rallying from these correction lows. This ratio of upward momentum (18,200) to correction (7,135) is a healthy 2.55-to-1.

FACT 4: Big up days occur within two weeks of big down days 60% of the time.
J.P. Morgan Asset Management released an annual report titled, "Staying Invested During Volatile Markets." This report looked at the S&P 500 over the trailing 20-year period and calculated what an investor would have made had they stayed invested versus trying to time the market by jumping in and out when they saw the first signs of trouble. Oftentimes, missing the S&P 500's 10 best days means losing more than half of your would-be 20-year returns, missing around 30 of the best single-session gains, and resulting in a loss over the 20-year period.

BEWARE! OF MEDIA MAGNIFICATION

One of the biggest challenges that investors face is how to tune out the magnification of financial issues by the media. With thousands of media outlets all thirsty for viewers and clicks to their storylines, some outlets resort to scare and fear tactics to attract an audience. The knowledge that volatility is a part of the investing experience can be one of your strategic tools to use during periods of fluctuation.

Yet, it can still be difficult to make rational investment decisions when the media is behaving like Chicken Little and calling for unnecessary panic. During these times, it is prudent to resist the temptation of watching news reports and obsessively watching your portfolio performance. Adhering to a long-term investment plan often requires taking the news with a grain of salt and putting spur-of-the-moment advice of others on the back burner.

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FIVE STAR TIP

AVOID THE HERD MENTALITY

A powerful influence to avoid is the **Herd Mentality**. With easy access to many news sources and media outlets, anyone can be easily influenced by potentially misleading information, abandon reason, and simply follow the crowd. Once you are aware of this pitfall, it's important to avoid it and remain focused on executing an investing strategy that is most appropriate for your situation. Sometimes the most difficult thing to do in investing is nothing at all. Nobel Laureate Daniel Kahneman, considered the father of behavioral economics, suggests that, *"we would be better investors if we just made fewer decisions."*

Too often emotion, not logic, can eclipse investing habits, so the first step in declaring your mental independence is realizing how these influences, known as biases, affect us. Sometimes, the closer you put a short-term lens to your investments, the more likely you are to consider decisions that deviate from your long-term strategy.

WHAT TO DO IN A VOLATILE MARKET

In volatile times, many people tend to overreact and make decisions that may not be in their best interest. However, panic is not a plan, just an emotional reaction. During volatile markets, one of the best courses of action is to ask questions of both yourself and your financial advisor.

Start to revisit your plan by asking yourself these four questions:

- **Have my financial timelines changed?**
- **Have my financial goals changed?**
- **Has my risk tolerance changed?**
- **Any recent life-changing events in my life?**

If you answered "YES" to any of these questions, contact us to review these changes. An investor needs to build a plan that includes risk awareness. One of our primary responsibilities as your financial advisor is to provide consistent communication and monitoring of your situation. If you have concerns, some questions you should ask of us include:

- **Can we review my financial plan?**
- **Can we revisit my risk tolerance?**
- **Are my investments diversified?**
- **What are my fixed income investments?**
- **Has the volatility presented any good opportunities?**

While equities have risen, the continuing backdrop of a weakening economy, trade war fears and interest rate concerns always offer the opportunity to review your plan. Today's traditional fixed rates might not help many investors to achieve their desired goals, so most investment plans may need to still include a strong mix of equities. Markets can continue to rise but they also could head lower. At the end of the day, investors should always put their primary focus on their own personal goals and objectives. If anything has changed for you, please let us know.

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A good financial adviser should help make your financial planning journey easier. Our goal at HFS is to understand your specific goals and dreams and then offer direction and strategies to help get you there.

While we cannot control financial markets or interest rates, we regularly monitor your portfolio and consistently communicate with you in a way that's simple, streamlined and easy to understand. We do keep a watchful eye on economic, tax and investment issues and offer every member of our team continuing education on issues that can impact our clients. One of our primary objectives is to take the emotions out of investing and help you maintain a focus on your personal situation. We can discuss your specific situation at your next review meeting, or you can call to schedule an appointment anytime.

As always, we appreciate the opportunity and are honored to work with you and helping you to achieve your financial dreams and goals.

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