EQUIUS ASSETCLASS[SM]

Modern asset class investing principles, research, and perspectives for long-term investors

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Keep Market Declines in Perspective

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During our traditional period of family gatherings, parties with friends, religious celebrations, and general good cheer, the stock market gods decided to remind everyone that stocks are risky. The market drop of 9.0% in December—following a 6.8% drop in October, with a brief feel-good bounce of 2% in November—has created unwelcome anxiety for many investors.

Equius clients know that we should expect these kinds of market declines and must endure them to reach our long-term financial goals. But that knowledge does little to reduce anxiety, particularly when headlines scream "Worst December since the Great Depression!"

Here's a different perspective to consider: Since a decline of 0.13% in February 2016, we have enjoyed 29 months of positive returns and only 5 months of negative returns for the S&P 500 through December (a total return of 243%). *This has been an extraordinarily positive period for the U.S. stock market.*

So, while acknowledging that declines like we experienced in October and December are no fun and create real anxiety, there are right and wrong ways to deal with them, depending on your seat at the show.

If you are new to asset class investing, understand that this decline should be viewed in the context of your investment experience over the past 10 years or more. Asset class investing isn't the reason for the drop in your portfolio value, and, unlike how you may have invested before, it wasn't bad stock picking or market timing decisions on our part that caused it. We engage in neither, for good reasons.

If you are still in the accumulation phase of your investing, you should look at the decline as an opportunity to purchase stocks at significant discounts. The money you invest at these lower prices has a higher expected return than money invested at higher prices. Don't blow the opportunity, even if you think a better one will present itself in the coming months. If you add to your portfolio often (if possible) and consistently, periods like this become insignificant over time.

If you are retired and living off your portfolio, take necessary distributions from the short-term, high-quality bond side of the portfolio as much as possible. We keep risk relatively low with our bond investments for this reason. Taking additional economic risk with high-yield junk bonds or interest rate risk with longer-maturity bonds can compound the risk we already accept by owning stocks.

Even if you're not withdrawing, our discipline of rebalancing your portfolio during times like this allows us to take money from the bond side and apply it to the stock side. This maintains the portfolio risk we agreed upon while taking advantage of lower stock prices when we can.

Above all, avoid big mistakes. Active management isn't the answer in this era of efficient markets. It adds more cost and uncertainty and seldom delivers on its promise. Consistently successful market timing is exceptionally rare and is often incredibly frustrating (if you have doubts, take a small portion of your investments and try it).

Risk and return are directly related. If you want stock market returns, you must accept stock market risk. Advisors who claim they can provide you with market returns with less risk (other than what we can achieve from efficient diversification) are making a bad bet with your money.

Remember, wealth lost from misguided decisions is wealth that will not continue to compound over your lifetime. The only way to "make it up" is to subject all or part of your remaining wealth to higher risks than you have, up until now, deemed acceptable.

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