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HOW SHOULD INVESTORS RESPOND TO RECENT VOLATILITY?

Volatility Returns: No Need To Panic

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ASK TYLER

Volatility has returned to world financial markets. In fact, one volatility index saw its second largest jump in 32 years. What to make of all this?

Actually, recent declines do not catch us surprised. To start, market volatility, sell-offs, excessive surges and periodic crisis are all normal. Historically, US equities tend to have 10% declines every 9 months on average.

What is not normal are years like 2017 where the US stock market's maximum decline from peak to trough was just 3%. It was quite the run. But during these periods, investors must not lose sight of context nor become complacent with current conditions.

What's Happening

Heading into 2018, Forstrong's Investment Team was expecting volatility to emerge. Why? First, despite relatively robust global growth, investor expectations had become too high relative to the fundamental outlook. As we wrote in the December 2017 issue of Super Trends and Tactical Views (read here):

"... from time to time, markets run ahead of themselves, setting themselves up for a stumble. The issue today is that the underlying fundamentals and the behavioural side of markets are showing conflicting signals. In this environment, the right thing to do is reduce risk and rely on global diversification for defense."

Secondly, many global Super Trends are now shifting. Household incomes are finally rising. Fiscal stimulus levers have been engaged. And, animal spirts are back. The game is changing.

During these transitions, heightened volatility typically surfaces as new leadership takes hold.

What To Do

The drop on Monday triggered a number of panic-type readings. During times like these, it is always useful to revisit the role of the portfolio manager: why do clients pay us to manage their wealth? It is not for flawless clairvoyance. Rather, we are paid to anticipate probable risks, prepare for opportunities and, importantly, not lose our proverbial minds when everyone else has lost theirs.

More often than not, large declines from a high tend to lead to capitulation that creates a strong rebound. In order to successfully navigate these dynamics, a disciplined decision-making framework that can extract emotion from the process is crucial. Forstrong's investment team remains committed to this approach.

Looking ahead, the best possible defense against market volatility continues to be wide global diversification with an orientation to the longer-running macro themes playing out in the world economy (the rise of the Asian consumer, inflationary dynamics emerging, etc.)

Our global ETF portfolios have already been positioned for such trends and shifting regimes, with an ultimate goal of avoiding the "*big mistakes*" and continuously adapting in an era of new realities. That remains the best way to secure the financial futures of your clients.