Intelligent Considerations During Short-Term Market Volatility

Remaining calm and objective can be hard to do when markets enter periods of heightened volatility.

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As we've witnessed time and again, markets are prone to wild swings based on a variety of influences, including geopolitical events like Brexit, which roiled global markets recently. Even knowing market volatility is a normal occurrence provides no comfort when your retirement nest egg is at stake. There's no magic elixir for dealing with the ups and downs of the stock market, but adhering to a disciplined investment strategy and focusing on long-term financial objectives can prepare you psychologically to handle short-term declines in asset prices. The key elements of any investment strategy include understanding your own risk tolerance, having a diversified portfolio, rebalancing your portfolio over market cycles and focusing on the long-term.

Undeniably, investor risk tolerance trends toward being more aggressive in rising markets and becomes more conservative during market downturns. Psychologically this appears to make good sense, but pragmatically it is the opposite of how investors should act and feel. As many investors have learned the hard way, becoming overly optimistic about investing during good times can be as detrimental as worrying too much about the bad times. The right approach during all kinds of market conditions is to be realistic and understand your risk tolerance. Avoid letting the ebb and flow of the markets deter you from sticking to your investment strategy. Investors must recognize a diversified portfolio containing stocks, bonds and alternatives will likely underperform stock indexes during strong bull markets and must not allow swift market downturns to push them predominantly into more conservative assets like cash. Too often, investors allow the whim of the markets to sway their emotions and the composition of their investments. Resisting the temptation to become too aggressive during strong markets and staying invested during downturns is so very important to continued success.

Likewise, maintaining a diversified investment portfolio – one that is aligned with your risk tolerance - is crucial for long-term investors. Portfolios should include a variety of asset classes including domestic and global equities of varying capitalization, fixed income, and alternative investments including real estate, managed futures and hedged equity. Investment portfolios diversified among these asset classes contain investments that won't always correlate with stock performance.

This is not to say that investors should fail to make strategic shifts to their investments or rebalance portfolios over time. Working with an experienced financial advisor is beneficial to ensure consistent rebalancing and making appropriate strategic changes to asset class weightings based on the economic environment. Rebalancing is so important to investing success as it inherently promotes the tenet of buy low sell high. A diversified allocation will at any given time have some investments doing well, others holding steady, and some in decline. By periodically rebalancing, investors take gains from assets that have grown beyond their target weighting in the portfolio and then deploy those gains into assets classes that have dropped or others that have held steady. Conversely, when stock indexes decline, rebalancing shifts money from conservative assets like bonds into equities while they are down. This process over time and through market cycles is crucial.

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As the market gyrates up and down it is easy to become focused on day-to-day returns. Avoid the temptation to pull out of the market when losses mount. Keep your eyes on your long-term financial goals and your overall portfolio and don't let the market deter you from your course. Stay invested, rebalance, have a strategic mind set, and be consistent with your goals and time horizon.□

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