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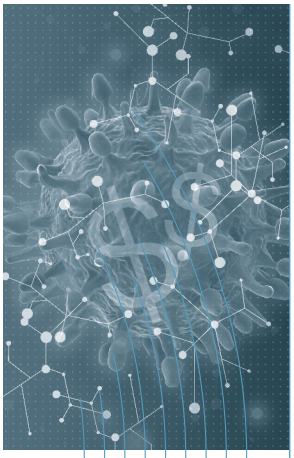
Wealth Advisors

The Market's Epidemic



By Steven RINN, CFP®
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Extreme market volatility is largely due to unexpected events, not known risks. As the coronavirus pandemic sweeps the globe, the short-term unpredictability of crisis markets is again in evidence.

The coronavirus was not in the plans of consumers and businesses, not included in economic forecast even three, six or 12 months ago, and continues to evolve as a health as well as market risk. No one expected an epidemic to trigger the next bear market—or cause an economic slowdown. But it is important to recognize that, as we go through one of the more substantial market events in the last decade, we have been here before; while the cause is unique, the volatility is not.

The stock market is a business valuation tool. Buyers and sellers—that is, investors—attempt to find the correct valuation for publicly traded businesses based on current and future expected cash flow. By its very nature, such an initiative is unpredictable in the short term, more predictable in the long term—in particular if you buy financial assets that have provided positive returns over long periods of time. Our current period of unpredictability, this round of cash flow uncertainty, is being driven by virus-related supply chain disruptions and a slowing in consumer spending. The range of possible outcomes for businesses is wide, leading to extreme moves in the financial markets.

It is extremely difficult to value a business minute by minute when uncertainty reigns. As clarity increases over the coming weeks, volatility will begin to decrease and the range in outcomes will likely constrict. As volatility subsides, consumer confidence and spending increases, which reignites corporate profitability. It could take some time as the coronavirus disruption moves through the global financial system, but trying to time the events or short-term outcomes and therefore the markets is not recommended. They are unpredictable as to how long or how impactful to the economy they could be. Speculating on the outcome could result in long-term damage to your portfolio.

History argues convincingly that a short-term decline in stock market values will reverse itself as economic growth continues in the coming years.

In the past 20 years we experienced 12 epidemic-related events. The S&P 500 Index at six months following the beginning of the epidemic was higher in 11 of the 12 cases, with an average return of 8.8 percent. At 12 months, the S&P was up in nine of the 11 cases for an average return of 13.6 percent.

Our Perspective

At HBKS, our fiduciary commitment is to build a client's portfolio based on the client's goals and objectives. We take into account historical volatility, or risk, and build the accounts with these types of events in mind and the knowledge that they are likely to occur. We rebalance client accounts regularly, conscious of valuation, but we don't try to time markets. The high levels of volatility resulting from unexpected events make timing futile.

Volatility can be mitigated by a diversified approach to allocation, blending investments in stocks and bonds and other investment vehicles to provide the highest probability of reaching a client's long-term goals. There is a great deal of emotion when it comes to extreme market movements, but neither emotion nor volatility should alter a sound strategy. The coronavirus epidemic will pass as others have. History argues convincingly that a short-term decline in stock market values will reverse itself as economic growth continues in the coming years.

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Steve Rinn is a principal and senior financial advisor in the HBKS® office in Erie, Pennsylvania. He is a lifetime resident of Erie, began his career there in 2003 and joined HBKS® in 2005. His expertise extends to comprehensive financial planning, retirement planning, insurance and asset management.

Steve earned his Bachelor of Science degree in financial services from Edinboro University. He is a CERTIFIED FINANCIAL PLANNER™.