The Importance of Staying Invested Throughout Market Cycles

Economic Insights | October 30, 2018

Key Takeaways:

- The October selloff is due to a number of factors: earnings guidance, interest rates and tariffs.
- Corrections and bear markets are part of the stock market experience.
- Staying invested is generally a better approach for achieving goals than market timing.
- Investors with patience and a disciplined asset allocation strategy have generally been rewarded over time.

The recent market selloff has many investors wondering if they should move their portfolios to the sidelines until things settle down. However, pulling your money out, even temporarily, could negatively impact your financial well-being in the long run.

Let's take a look at what's behind the recent volatility and the importance of staying invested.

The October Correlation

The recent volatility is primarily a result of concerns around Fed tightening and the uncertain economic impact of the trade war with China. Many investors and analysts had expected third-quarter earnings to offset these concerns, but that hasn't happened. While many companies have reported average earnings growth of 25% and top-line revenue growth of over 8%, some high-profile businesses have missed their sales-growth estimates. Others have warned of slower growth in the coming quarters. In addition, some company executives reported margin pressures due to higher raw materials costs caused by tariffs, increased labor expenses and logistical bottlenecks.

While these cost pressures were expected, the slowdown in the growth rate of capital spending was somewhat surprising. It appears the uncertainty surrounding the trade wars may be causing businesses to postpone or cancel capital projects. Without a corresponding uptick in productivity, wage-based inflation increases the likelihood the Fed will continue to raise rates aggressively, well into next year.

Source: Factset

CERITY PARTNERS

The Challenge of Market Timing

During periods of volatility such as this, many investors change their market exposure, shifting to more conservative securities. Often referred to as market timing, this strategy is notoriously difficult and should remain in the realm of short-term traders. For market timing to work, you not only have to time the exit correctly but also nail the re-entry. Since no one knows for certain how the markets will perform on any given day, knowing the "right time" to move assets is virtually impossible.

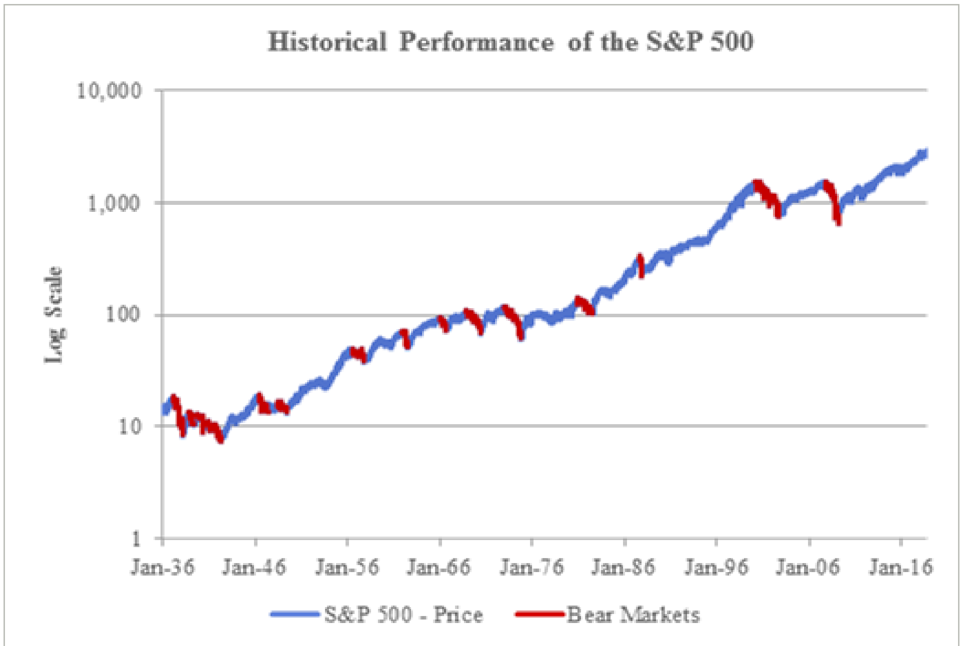
Also, markets tend to accumulate sizable gains in the immediate lead up to market peaks. Investors who exit too early forgo these returns. It's tempting to think you'll be able to buy-in at a lower price at the start of a recovery, but in practice, it proves more challenging.

We believe a better approach is to make smaller, more deliberate changes to your portfolio. Based on our near-term market views, we identify opportunities to adjust your tactical asset allocation without compromising your long-term investment strategy.

Stocks' Long-Term Performance

This past month is a good reminder that volatility comes with investing in the stock market. When it strikes, it helps to remember long-term investors have historically been rewarded for taking on the additional risk. The equity market tends to be in a bull cycle nearly 80% of the time and has compounded at an annual rate of 10% (including dividends).

Plus, most corrections don't materialize into bear markets. Since 1960, there have only been 21 corrections in the S&P 500 (a decline between 10% and 20%) and 8 bear markets (a decline of more than 20%). Patience is key during market downturns. The penalty for being out of bull markets is generally more severe than the benefit one might get from occasionally being right in bear markets. A prime example is the 2008/2009 financial crisis during which the S&P 500 experienced one of the largest declines on record. Within four years of hitting bottom in March 2009, the index climbed back above its 2007 highs. Any investors who chose to move to the sidelines in 2009 would have locked in losses and potentially missed some or all of the recovery.

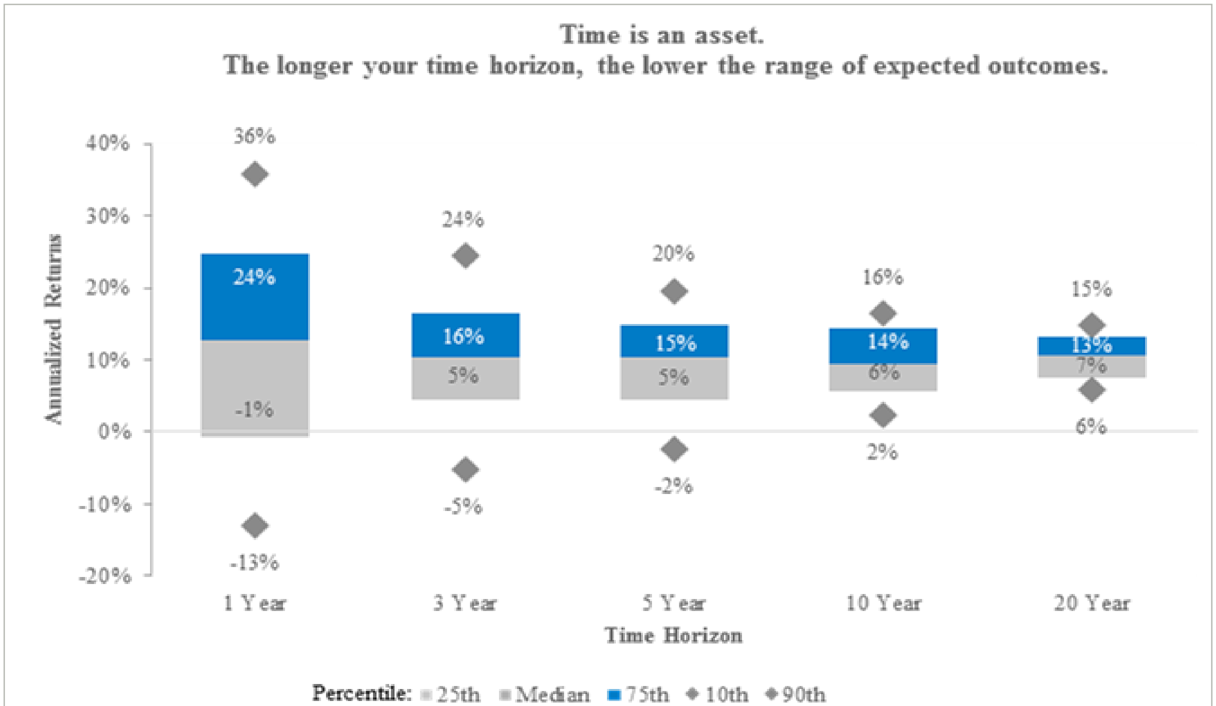


Source: Factset

Keeping Volatility in Perspective

The period between a drawdown and recovery can feel like an eternity when you're living through it. But as a long-term investor, time is on your side. We'll help you tune out the "noise" and remain focused on the asset allocation you need to achieve your goals by:

- Creating a strategic asset allocation that fits your risk preferences and objectives
- Diversifying across and within asset classes
- Making tactical changes to weather short-term market fluctuations
- Adjusting your strategic asset allocation as your needs and preferences change



Notes: Data through 6/30/18, Ibbotson SBBI US Large Stock from 12/31/1925 to 4/30/1987, S&P 500 5/29/1987 to 6/30/2018
Source: Factset, Morningstar Direct

Also, know that we're actively monitoring market events and evaluating what they mean for investors going forward. Please don't hesitate to contact us if you have any questions or concerns.