Composure in the Face of Bad News

By: David Jeter, CFP® *August 2015*

I'll start by getting all of the bad stuff out of the way upfront. Global stock markets slumped last week, including the U.S. which is now negative for the year as measured by the S&P 500 and Dow Jones Indices; a continued fear of China slowing along with their move to devalue the Yuan; and oil prices dropping below $40 per barrel. Of course, we add that news to Greece, the EU, and too much debt in many places, and we get a ramp up in volatility and a selloff in the markets.

However, as I have been counseling for a long time now, volatility is natural and has been long overdue in the market. In fact, I have referred to data in the past that suggest for the S&P 500 Index, between 1980-2014,[1] the average intra-year drop from peak to trough during the year is 14.2%. We have not reached that average in over three years and as of this writing still have not hit the average. The U.S. Stock Market has risen for six years with little pull back, and to that end some amount of retreat was not unexpected. Though expected, it doesn't make it enjoyable when it's happening. So, allow me to note a few things I'd like you to keep in mind.

"Watching the news and trying to be patient is like trying to lose weight and loading up the freezer with ice cream."

First, no one is certain what will happen next. Will there be a large decline, a small decline, a large rebound, or will the markets stay flat? No one knows, nor do they know when this 'path' will occur. You will hear and read from many who say they know...but, they don't. You are diversified, and patience will be an ally.

Second, in order to be patient, it helps that you don't listen to or read the news all of the time. The hardest thing to do is to temper your emotions while firing provocative news updates at them. The appearance of volatility and the reality of it may not be equal. Remember my comment above about 'average' volatility. The media will use the word 'plunge' when I use the word 'average'. That's tough for anyone to take. Watching the news and trying to be patient is like trying to lose weight and loading up the freezer with ice cream.

Third, you may be worried that with a 6+ year upward move, stocks are as expensive as they were before the dot.com bubble and the financial crisis. They aren't. Stocks are not cheap right now, but they aren't sky high either.

What I have preached before is to not let unavoidable setbacks become unrecoverable ones. What I mean is that this would be the wrong day to let emotions seep into your financial judgment. The clearer head remembers that the market does not go up in a straight line forever. It never has, and it never will. And in that regard, when the market drops it equates to lower prices. Lower prices means things are now on sale from a short time ago. We like when things are on sale! So as long as you have the correct amount of money for you in cash and fixed income investments to cover your short and intermediate term needs, natural market drops each year have little effect on your well-being, and you have made the right decisions for your entire financial picture.

That last sentence is critical. Weathering a further decline is possible when you are extremely diversified, have the right amount of cash, hold bond investments and have a plan in place for the long term from which to make unemotional, process-based decisions. Because when emotions meet unpredictable markets, I find the result is misbehavior and regret.

[1]Source: J.P.Morgan Asset Management Guide to the Markets as of June 30, 2015.

If you would like to discuss the subject matter in this article or any question related to your financial planning, please contact David Jeter at djeter@alleghenyfinancial.com or 412.536.8012.

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