



# Perspectives on Volatility

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# Perspectives on Volatility

Happiness = Reality - Expectations

FACT INFORMATION

# Perspectives on Volatility

## The S&P 500 Index Moves into a Correction, but That isn't Always Bad

Date	Days to 10% Correction	Next Three Months	S&P 500 Index Future Returns Next Six Months	Next Twelve Months
10/11/1955	12	9.7%	17.7%	14.8%
10/27/1997	14	11.5%	24.8%	21.5%
8/14/1998	20	5.2%	16.9%	25.2%
4/14/2000	15	11.3%	1.3%	-12.1%
2/8/2018	9	5.5%	10.6%	5.0%
2/27/2020	6	1.7%	16.8%	27.9%
1/24/2022	14*	?	?	?
1/24/2022		7.5%	14.7%	13.7%
Average		7.6%	16.8%	18.1%
Median		100.0%	100.0%	83.3%
% Positive				

# Volatility Isn't Unusual

**5-10%**

**84 Declines**

1-month average recovery time

**10-20%**

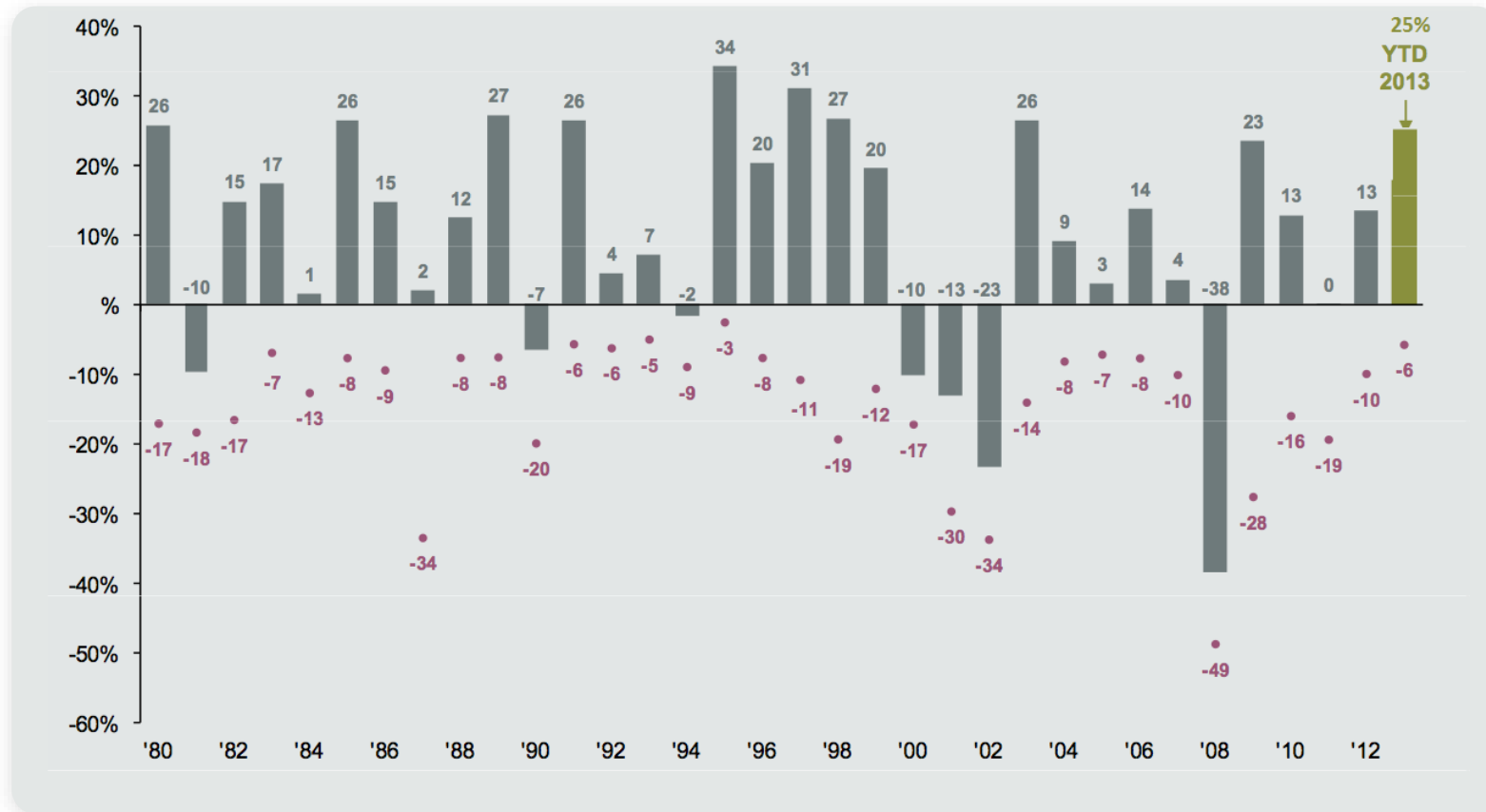
**29 Declines**

4-month average recovery time

# Volatility Isn't Unusual

## S&P 500 Intra-Year Declines vs. Calendar Year Returns

Despite Average Intra-Year Drops of 14.7% Annual Returns Positive in 25 of 33 Years



# Volatility Isn't Unusual

**22** of the **32**

corrections since 1950 never reached a 20% drawdown

**2** of the **22**

corrections took more than a year to recover from

# Corrections Can Happen in Healthy Markets

**3** of the **22**

market corrections occurred during a recession

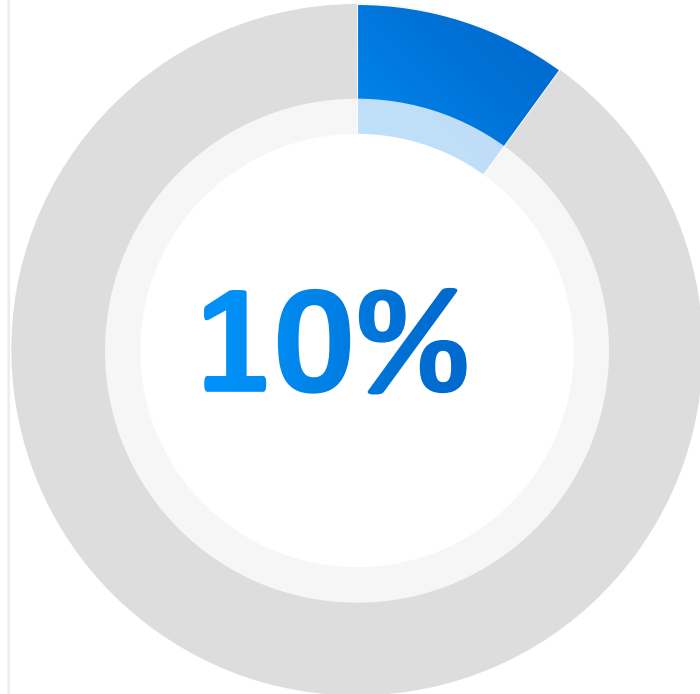
## **In a Recession**

Average 16% and 9 months

## **Not In a Recession**

Average 14% and 4 months

# Corrections Can Signal a Bull Market



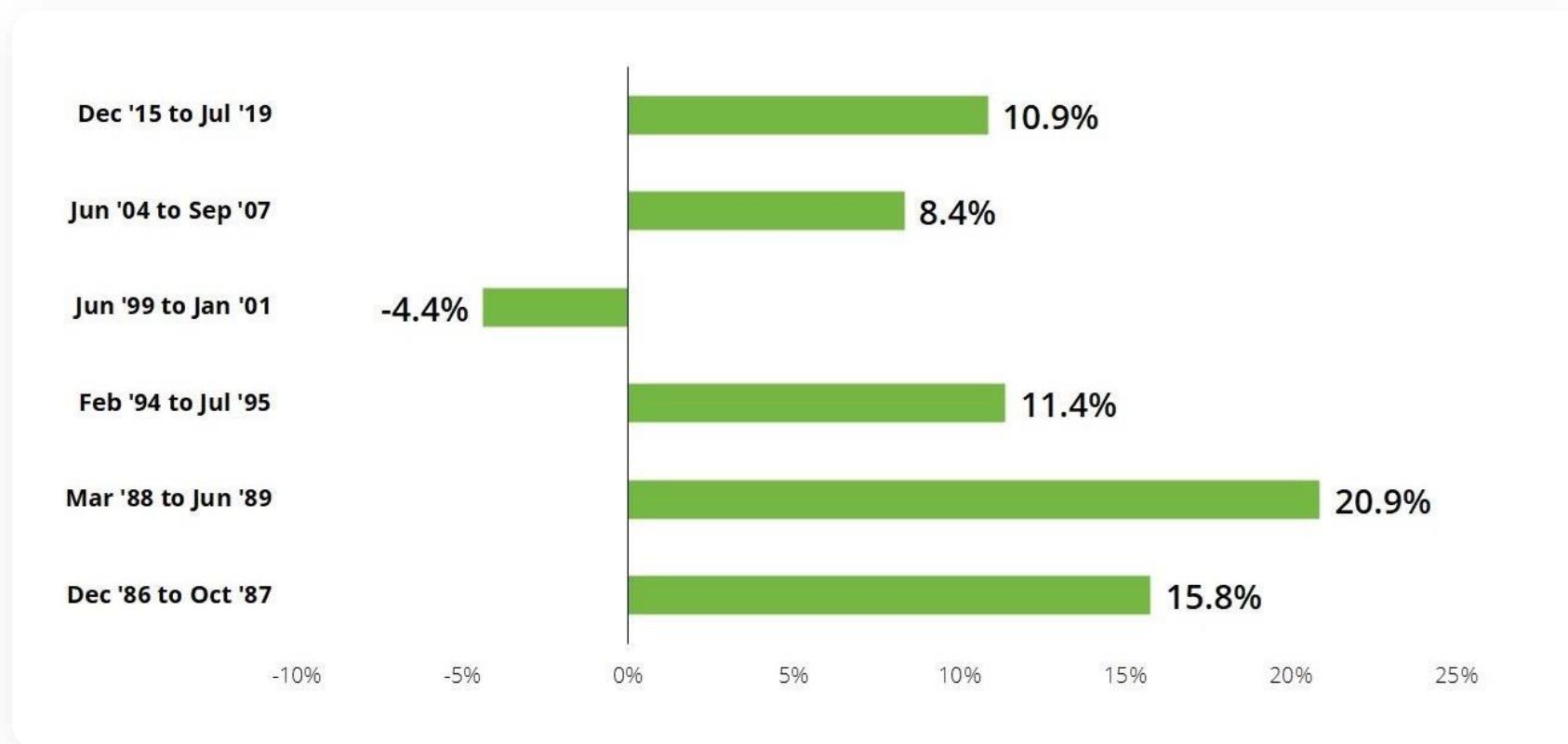
In seven of the last nine bull markets, the S&P 500 dropped **10%** or more in the first two years



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## Stock's Decent Track record with Rate Hikes

The S&P 500's Annualized Return in Recent Rate Hike Cycles



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## Stocks Usually Take Geopolitical Events in Stride

### The S&P 500 Index and Geopolitical Events

Market Shock Events	Event Date	S&P 500 Returns		Days	
		One Day	Total Drawdown	Bottom	Recovery
<b>COVID-19</b>	1/20/2020	-0.3%	-33.9%	63	148
<b>Iranian General Killed In Airstrike</b>	1/3/2020	-0.7%	-0.7%	1	5
<b>Saudi Aramco Drone Strike</b>	9/14/2019	-0.3%	-4.0%	19	41
<b>North Korea Missile Crisis</b>	7/28/2017	-0.1%	-1.5%	14	36
<b>Bombing of Syria</b>	4/7/2017	-0.1%	-1.2%	7	18
<b>Boston Marathon Bombing</b>	4/15/2013	-2.3%	-3.0%	4	15
<b>London Subway Bombing</b>	7/5/2005	0.9%	0.0%	1	4
<b>Madrid Bombing</b>	3/11/2004	-1.5%	-2.9%	14	20
<b>U.S. Terrorist Attacks</b>	9/11/2001	-4.9%	-11.6%	11	31
<b>Iraq's Invasion of Kuwait</b>	8/2/1990	-1.1%	-16.9%	71	189
<b>Reagan Shooting</b>	3/30/1981	-0.3%	-0.3%	1	2
<b>Yom Kippur War</b>	10/6/1973	0.3%	-0.6%	5	6
<b>Munich Olympics</b>	9/5/1972	-0.3%	-4.3%	42	57
<b>Tet Offensive</b>	1/30/1968	-0.5%	-6.0%	36	65
<b>Six-Day War</b>	6/5/1967	-1.5%	-1.5%	1	2
<b>Gulf of Tonkin Incident</b>	8/2/1964	-0.2%	-2.2%	25	41
<b>Kennedy Assassination</b>	11/22/1963	-2.8%	-2.8%	1	1
<b>Cuban Missile Crisis</b>	10/16/1962	-0.3%	-6.6%	8	18
<b>Suez Crisis</b>	10/29/1956	0.3%	-1.5%	3	4
<b>Hungarian Uprising</b>	10/23/1956	-0.2%	-0.8%	3	4
<b>N. Korean Invades S. Korea</b>	6/25/1950	-5.4%	-12.9%	23	82
<b>Pearl Harbor Attack</b>	12/7/1941	-3.8%	-19.8%	143	307
<b>Average</b>		<b>-1.1%</b>	<b>-6.1%</b>	<b>22.5</b>	<b>49.8</b>

Source: LPL Research, S&P Dow Jones Indices, CFRA, 01/24/2021

All indexes are unmanaged and cannot be invested into directly. Past performance is no guarantee of future results.

The modern design of the S&P 500 Index was first launched in 1957. Performance before then incorporates the performance of its predecessor index, the S&P 90.

# Volatility Mythbusting

## **“Fast Correction = Bad Market”**

Average 12-month return is 13.7%,  
positive 83%

## **“This is an unusually bad market”**

We average about one correction per  
year

## **“This is the top”**

We average about one correction per  
year

## **“There goes the bull.”**

Seven of the last nine times, an early bull  
market included a correction

## **“The Fed is going to kill the market”**

Tightening cycles have been bullish more  
often than not

## **“What if there is a war?”**

Geopolitical events tend to give short,  
shallow drawdowns

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“I just have a feeling about this market...”

FACT INFORMATION

# Noise



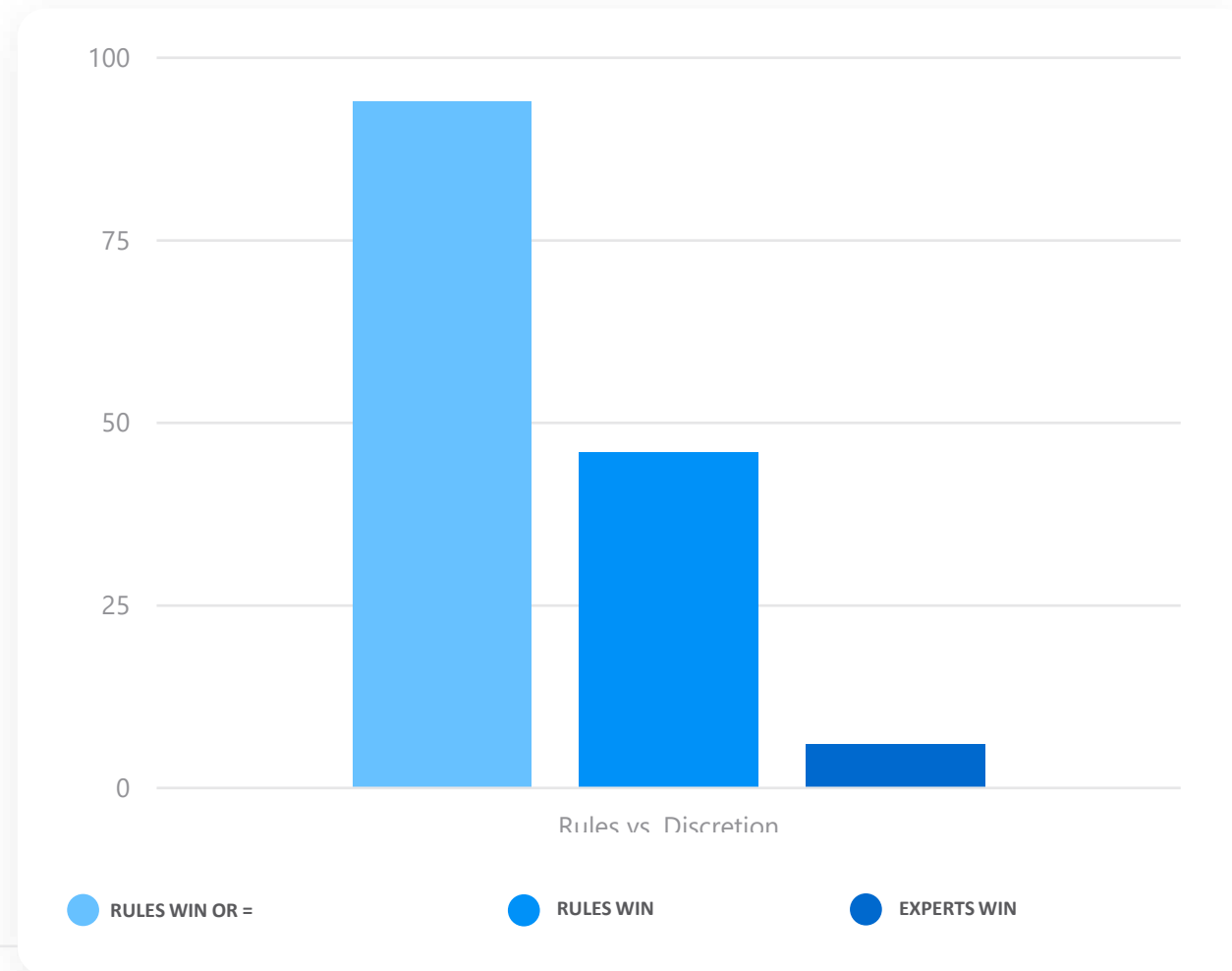
## ATTRIBUTION

“The fact that your brain becomes more risk seeking in bull markets and more conservative in bear markets means that you are neurologically predisposed to violate the first rule of investing, “buy low and sell high.” Our flawed brain leads us to subjectively experience low levels of risk when risk is actually quite high...”

The Behavioral Investor

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Rules dramatically outperform discretion and do so at a significant discount.



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“I’ll just wait until the smoke clears...”

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# Perspectives on Volatility

## Reasons to Sell



AT T R I B U T I O N

“In the 20th century, the United States endured two world wars and other traumatic and expensive military conflicts; the Depression; a dozen or so recessions and financial panics; oil shocks; a flu epidemic; and the resignation of a disgraced president. Yet the Dow rose from 66 to 11,497.”

Warren Buffett

## ATTRIBUTION

“A study performed by the Federal Reserve...looked at mutual fund inflows and outflows over nearly 30 years from 1984 to 2012. Predictably, they found most investors poured money into the markets after large gains and pulled money out after sustaining losses—a buy high, sell low debacle of a strategy.”

**Ben Carlson**

A Wealth of Common Sense

# Smoke is Opportunity

0-5% equals

**8.3%**

35-40% equals

**14%**

50%+ equals

**53%**

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“So and so expert says...”

FACT INFORMATION

# Experts of “Experts”

- The **more** famous, the **less** likely to be correct
- The **bolder** the past prediction, the **worse** the future prediction
- Wrongness **did not** shake confidence

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1 in 170 Analysis of 78,695 predictions

FACT INFORMATION

# Becoming an Informed Consumer of News

## Assessing Credibility and Authority

- ✓ Evaluate the source
- ✓ Question the melodrama
- ✓ Examine the tone
- ✓ Consider motive
- ✓ Check the facts/data

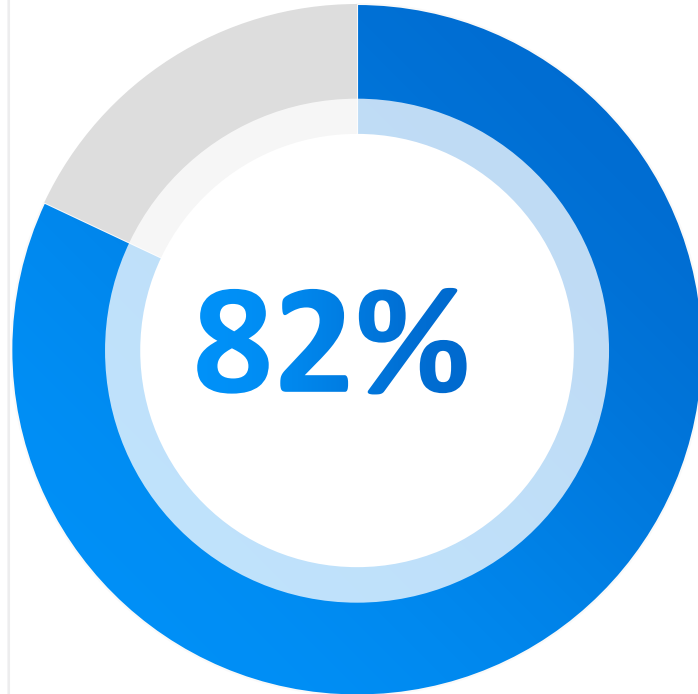


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“Time to go to cash...”

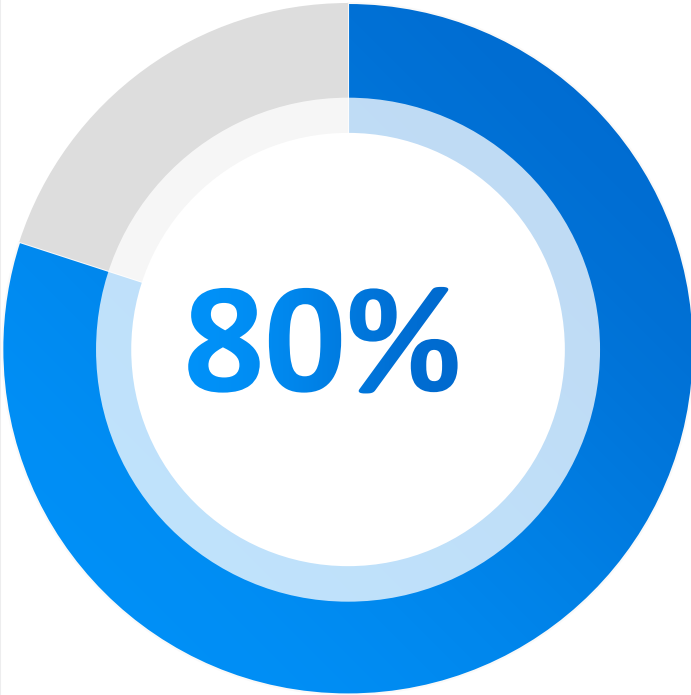
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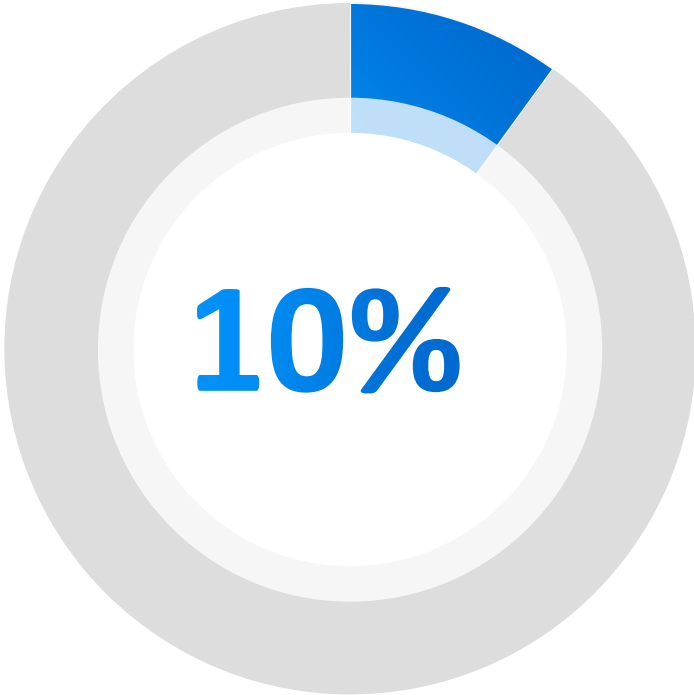


to match doing nothing.”  
– W. Sharpe

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Of the returns



Of the time

ATTRIBUTION

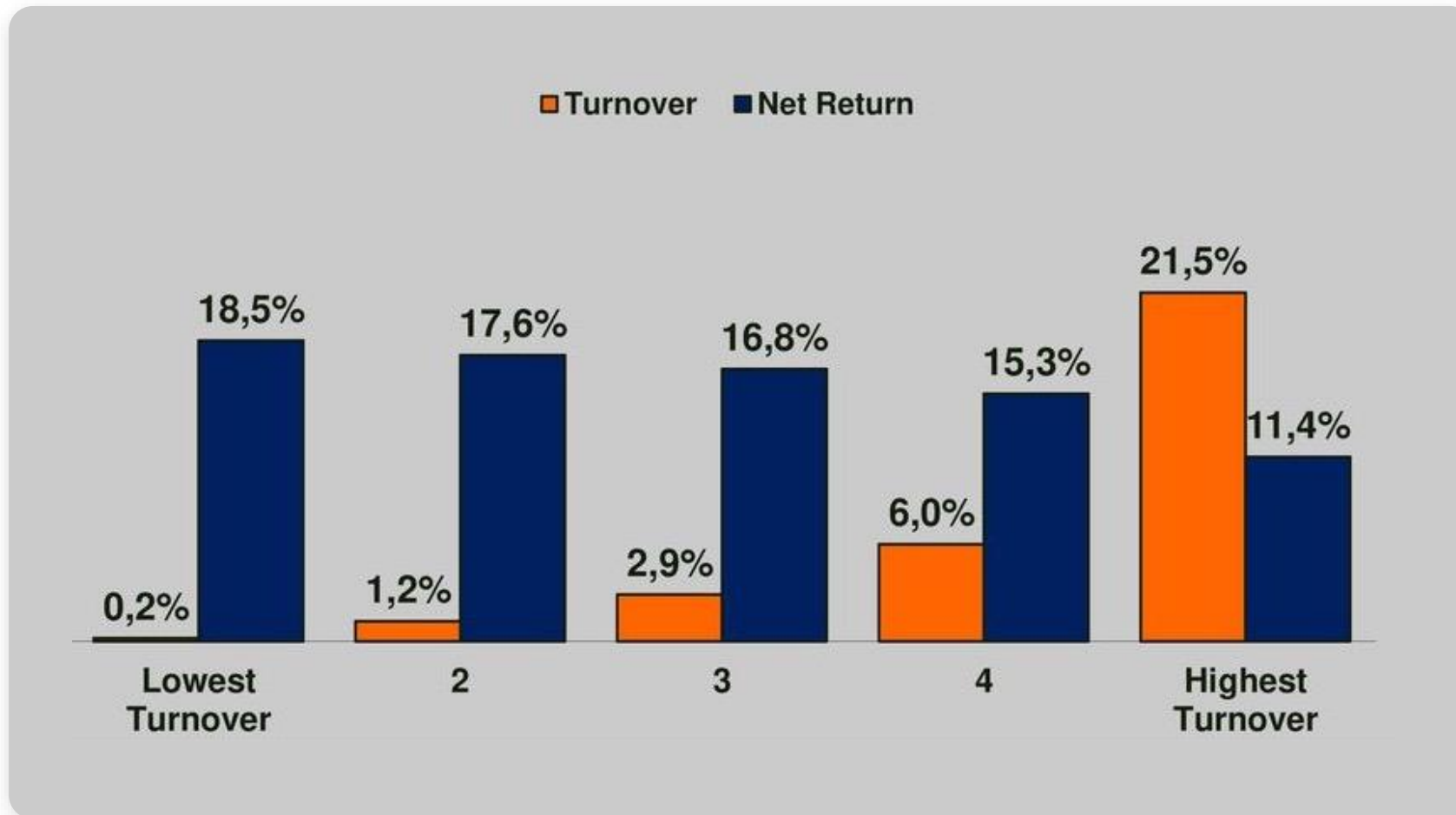
“Across 19 major stock exchanges, investors who made frequent changes trailed buy-and-hold investors by 1.5% a year.”

**Meir Statman**

What Investors Really Want

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## Monthly Turnover and Annual Performance



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“I better make some changes...”

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# A Lost Decade?

S&P 500

**\$10,361**

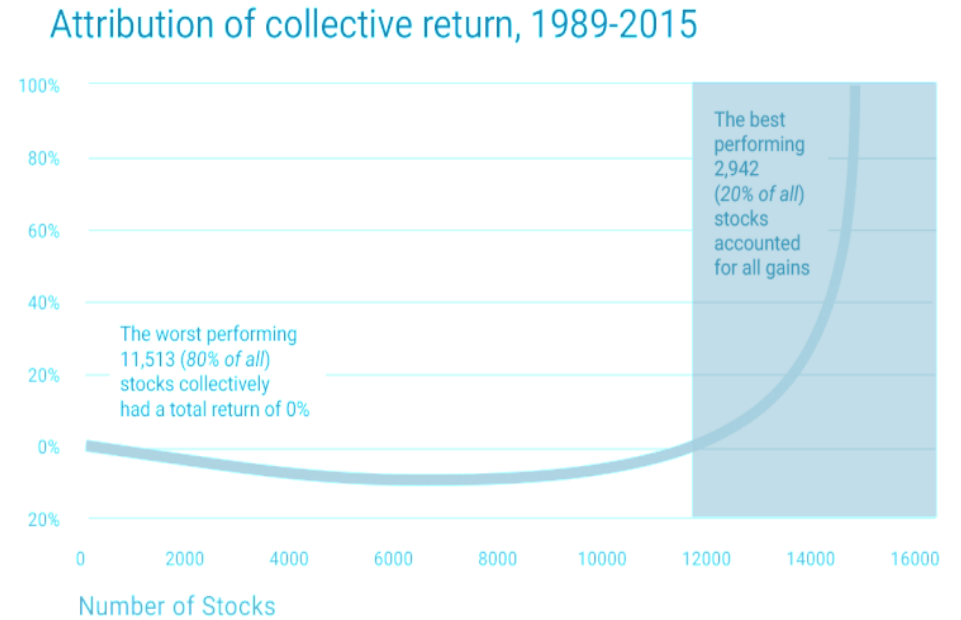
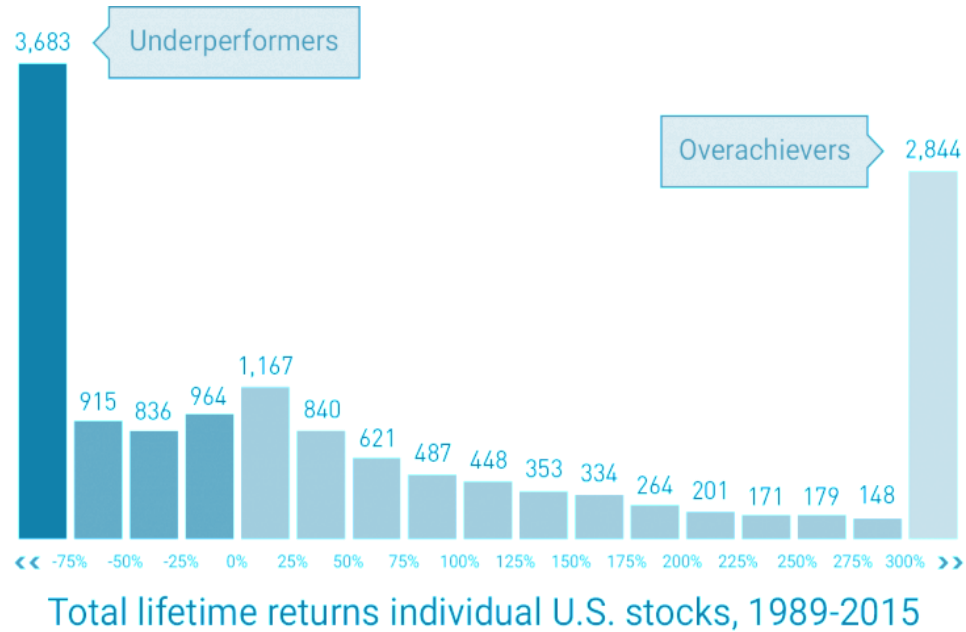
US Growth

**\$8,848**

Diversified

**\$19,746**

# Stock Returns + Base Rate Blindness





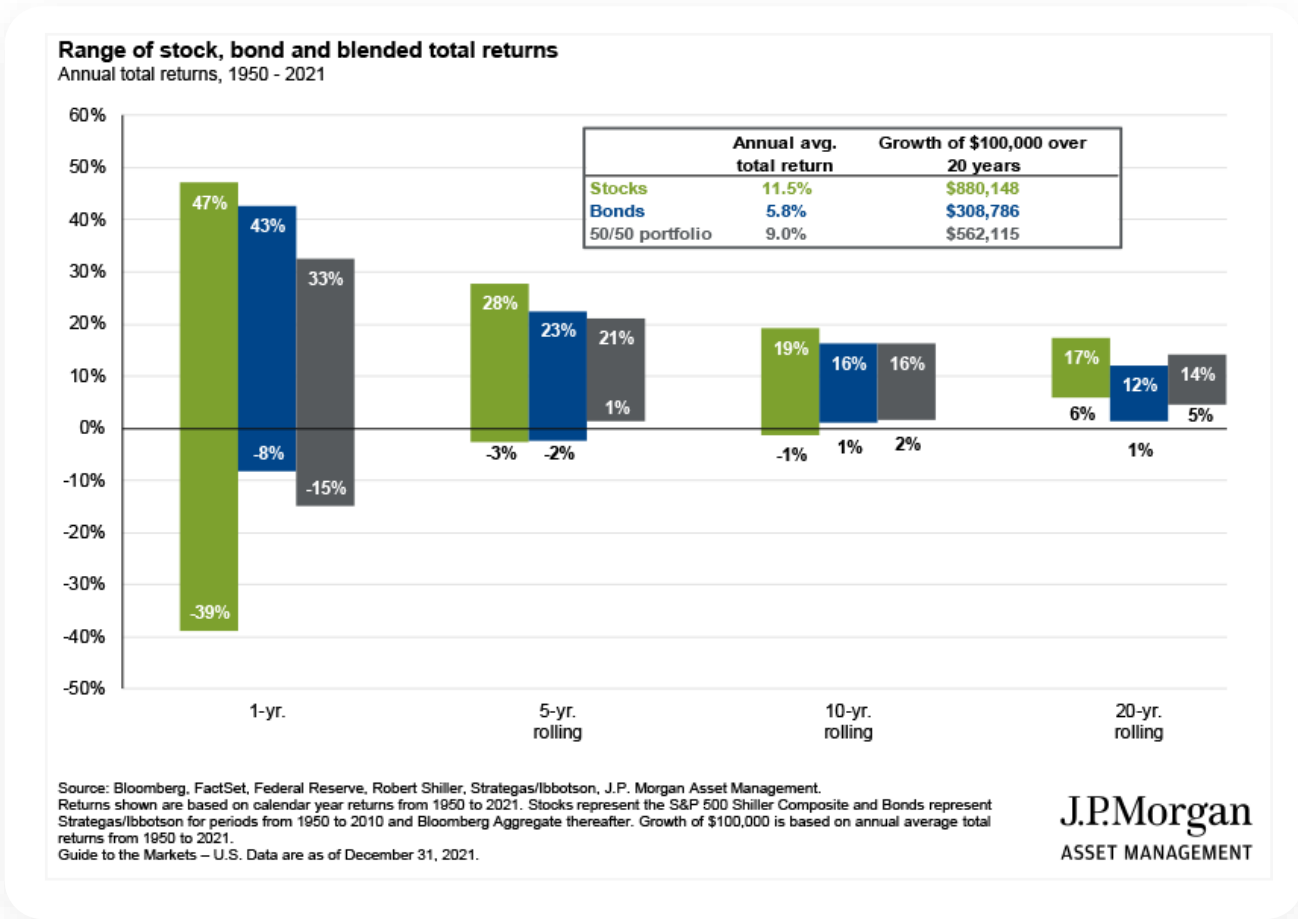
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“I’m going to keep a close eye on things...”

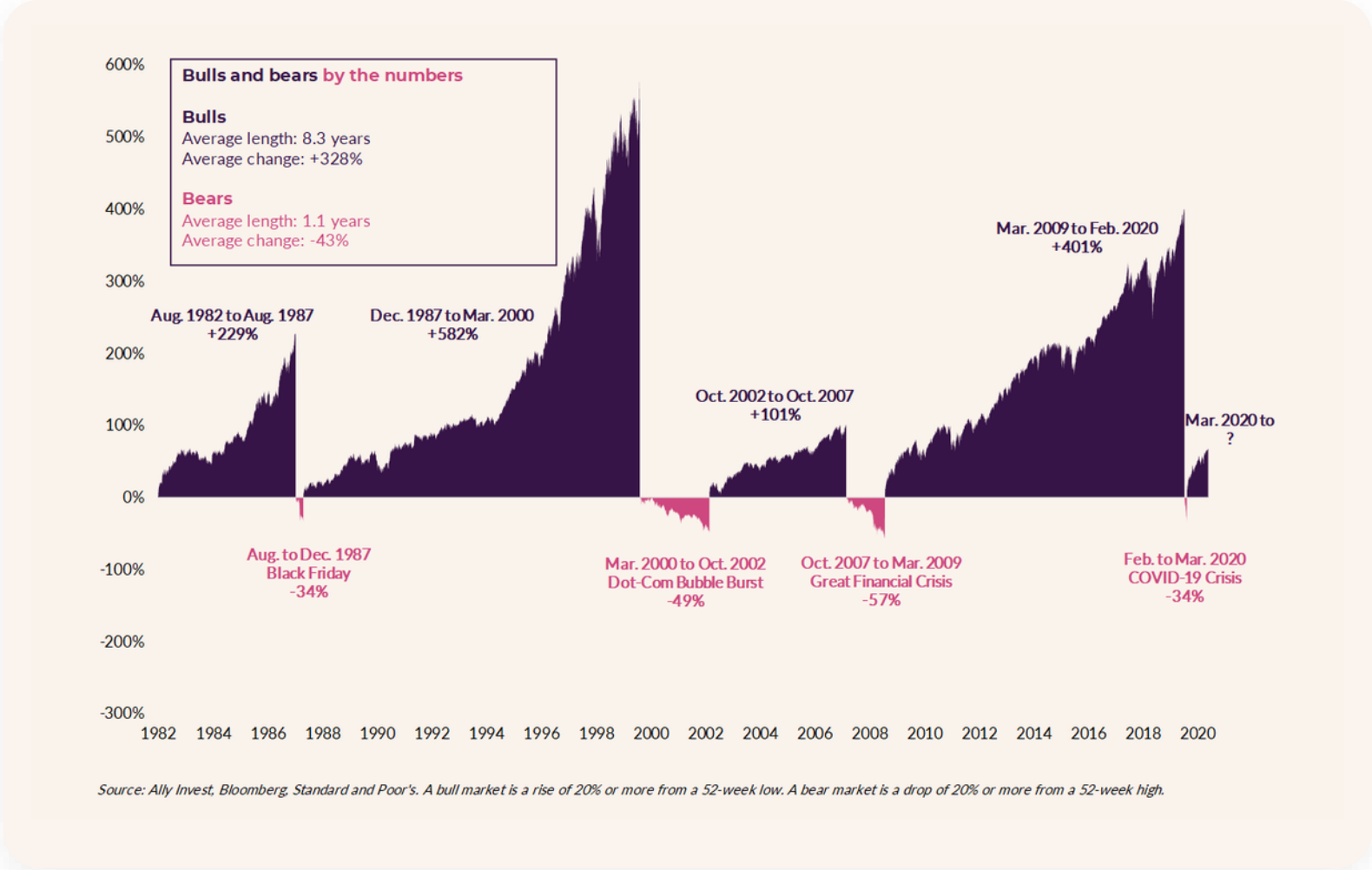
FACT INFORMATION

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## Time, Diversification and the Volatility of Returns



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“There’s nothing I can do...”

FACT INFORMATION

# Three Part Noise Test

**01**

**Is it Knowable?**

**02**

**Is it  
Controllable?**

**03**

**Is it of Enduring  
Importance?**

# Control



## Things you CAN control:

- Your savings rate
- Having a formal financial plan
- Creating realistic financial goals
- Discipline around staying the course
- The type of financial media you consume
- Your emotions
- Trading frequency (less is more)
- An awareness of your risk taking preferences
- The fees you pay for advice and financial products
- Using tax advantaged investment products
- The degree to which you are diversified
- Educating yourself about investing basics
- Continuing education to increase earning potential

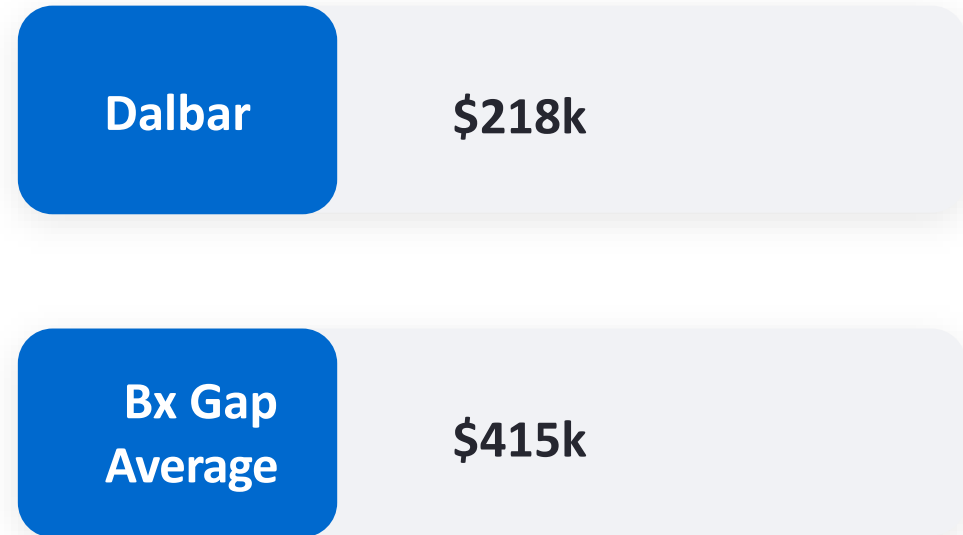
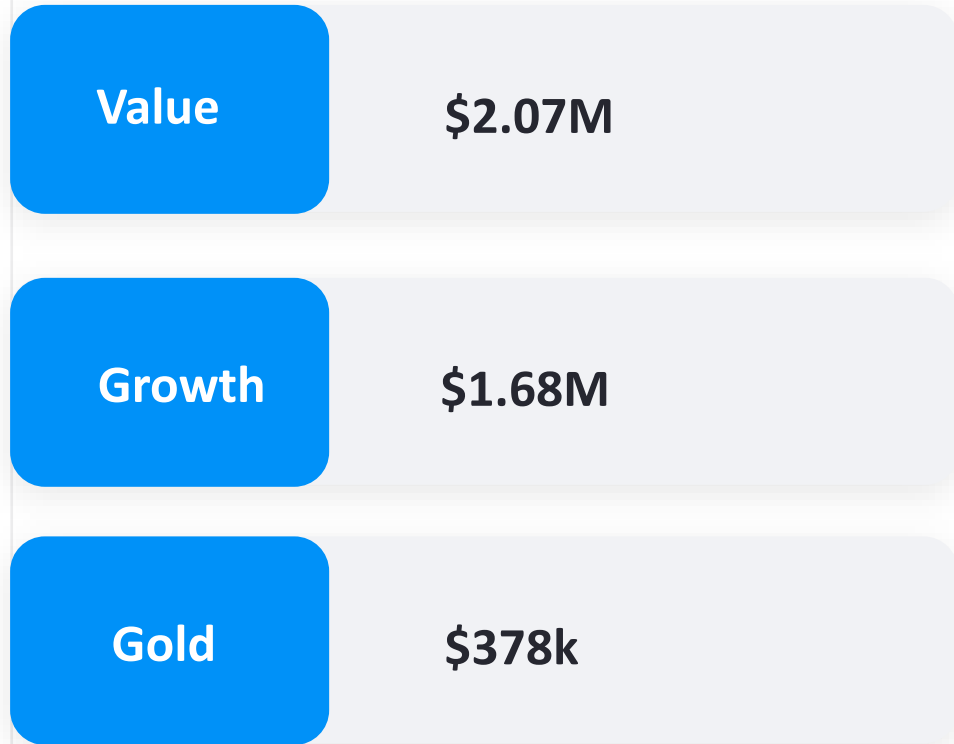


## Things you CAN'T control:

- The trajectory of the market broadly
- Acts of God
- Federal Reserve interest rate decisions
- The behavior of politicians or CEOs
- The timing of the next bear market
- Inflation
- Geopolitics; war and peace
- The housing market
- Catastrophic headlines

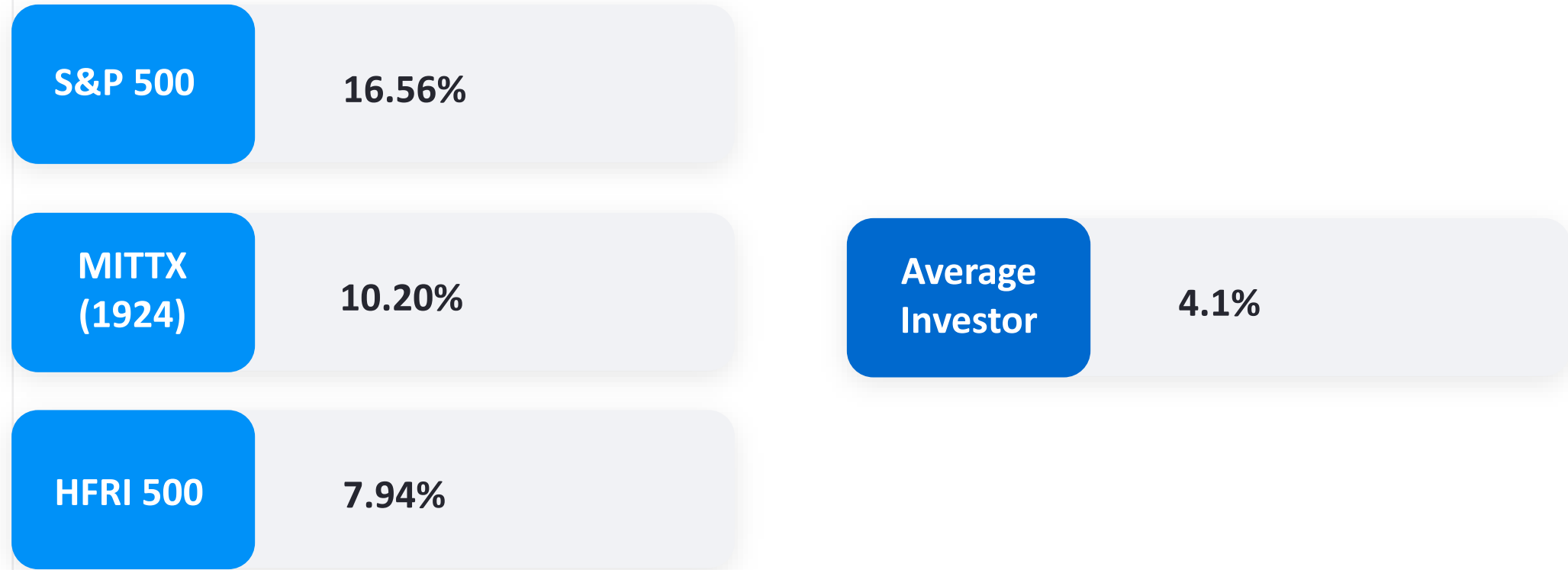
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Style vs. Behavior (1972 to Present)



# Perspectives on Volatility

Active/Passive vs. Behavior





# Old School vs. New School

## Old School

Asset Allocation	( 35bps)
Tax Management	(62 bps)
Product Allocation	(49 bps)
Rebalancing	(36 bps)

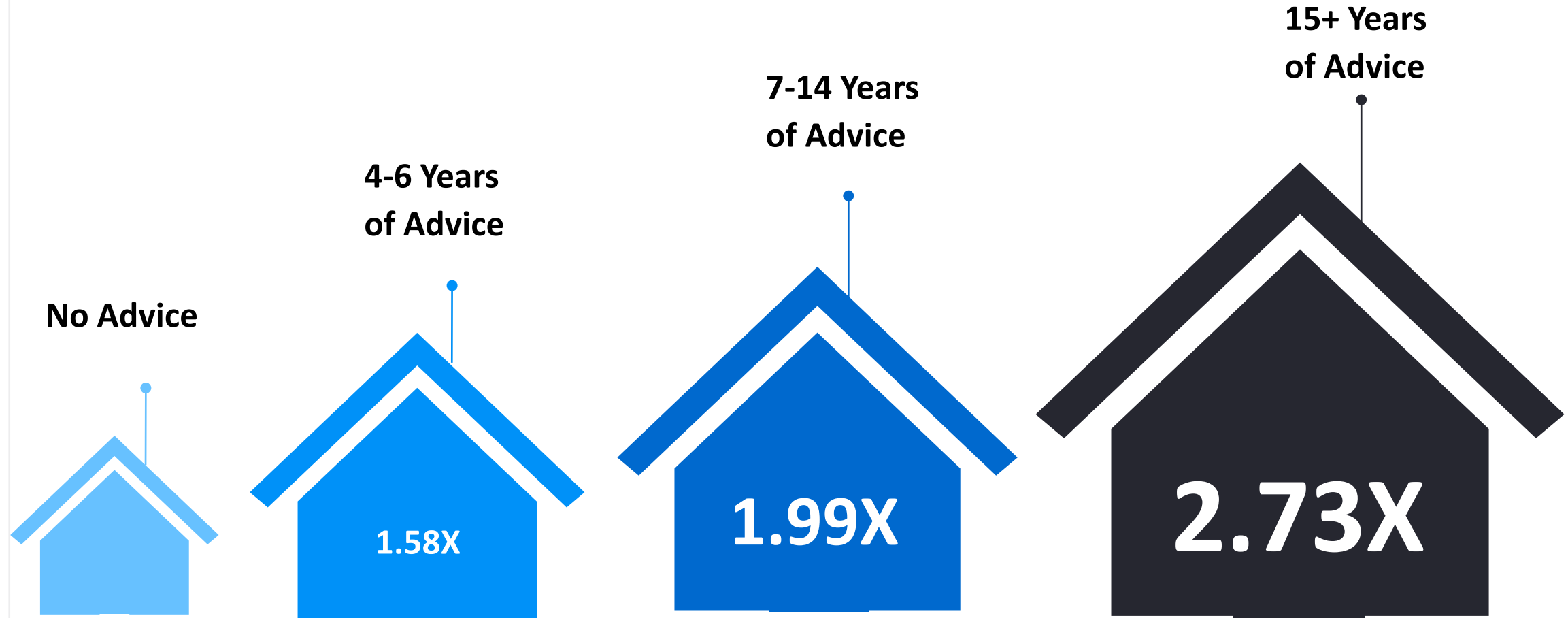
vs.

## New School

Client Assessment	(65 bps)
Behavioral Coaching	(244 bps)
Goal Optimization	(89 bps)
Saving + Withdrawal Guidance	(90 bps)

# The Value of BeFi

Difference in household financial assets attributable to financial advice



# Downmarket Checklist

This checklist can help you have more informed conversations with clients during moments of market volatility.



## Why?

Empathize with concern and pivot to goals.



## What?

Gently provide factual refutations of fear.



## Who?

Identify peers and experts who support facts.



## How?

Provide one small, concrete step for moving forward.

## ATTRIBUTION

“Think about the most meaningful thing you have ever done. I would wager it took a measure of risk, uncertainty and hard work to achieve. In this, as with all risk, comes a valuable lesson: to strive for certainty is to doom oneself to mediocrity. Nothing is less safe than playing it safe and nothing guarantees loss like trying to avoid it. Consider the person who remains unattached to avoid risking heartache and finds loneliness in the process. Or the would-be entrepreneur who never makes the leap of faith and wastes a career working at jobs they hate. Or the investor paralyzed by fear of volatility that arrives at retirement with resources inadequate to meet their needs. Indeed, the irony of obsessive loss aversion is that our worst fears become realized in our attempts to manage them.”

**Daniel Crosby**

The Behavioral Investor

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