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360 Insights

Investing Through Emotions

By Alex Kluesner

Ongoing trade wars, rising inflation expectations, interest rate movements, COVID-19 variants, bear market predictions, the Russian attack on Ukraine and heightened geopolitical uncertainty,

...that's a lot to think about.

The first quarter of 2022 reminds us all how much uncertainty can fill the world at any given moment—and how little control we have over it all. This perceived lack of control can lead to feelings of anxiety and stress in our everyday lives. One of the best coping techniques is to focus on what we can control. The key to this strategy is identifying what is actually in our control and what is not. This is especially true when it comes to your portfolio. So, let's remind ourselves of what we can and cannot control during our own investment horizons.

The Russian invasion of Ukraine has produced unimaginable tragedy and suffering on so many levels. And to see it play out daily on news broadcasts with live reports from the battlefield stirs up many emotions. The invasion has also caused dramatic price swings, which we call volatility, in global stock, bond and commodities markets. Every downturn in markets inevitably brings with it the question of "is it different this time?" This sort of market behavior is a constant recurrence throughout history but takes a wide range of forms along the way. Consider the U.S. stock market as proxied by the S&P 500 index. Since the beginning of 1980, the S&P 500 has gained 12.3% per year and finished 35 of the 42 calendar years with positive performance. But the ride has been far from smooth as shown by the average 14.5% intra-year decline during that same period.

This highlights the importance of staying the course. For example, if an investor sold at the bottom of the COVID-19 market downturn in March of 2020, they would have missed out on double-digit returns by the end of that year. Morningstar analysts point out that even a less risky 60% stock/40% bond portfolio experienced a 10% loss or greater in 22% of the rolling 12-month periods over the last 30 years.[1] We need to remind ourselves that we cannot control the exogenous forces that affect our investments; risk and price swings are the price of admission we pay as investors.

Having a historical perspective of market volatility is helpful, but those who plan ahead for what they will do when volatility shows up are often better served. First, taking action for action's sake rarely proves profitable over the long term even for professional money managers – don't feel like you need to do something just because markets are down. However, there are steps you can take to regain control and peace of mind in the face of uncertainty. For those drawing down on their portfolio, meet with your advisor and discuss how much you are withdrawing. If taking money from your portfolio during volatile markets makes you feel uneasy, remember that we account for down markets in your plan. If you still don't feel comfortable, defer some spending that might be able to wait like a vacation or a new car purchase. For those still saving toward retirement and other long-term goals, review your planned contributions and the amount of emergency funds available outside of your investments. Markets have historically recovered, even from geopolitical shocks, so investing additional money while stocks are down could provide a boost to your portfolio over the (Continued on page 4)

Geopolitical Risk and Your Portfolio

By Jonathan Scheid, CFA, AIF®

There has been no shortage of market-moving headlines over the past few years. As investors, and people, we've had to digest a lot of information, and a good deal of change, from forces that are generally beyond our control. The most recent headline-dominating, market-moving event was the Russian invasion of Ukraine.

Our hearts truly go out to everyone impacted by this conflict. This article will not end war, but it may help us worry less about one aspect of life—our financial life.

The Known Unknowns of Investing

One of my colleagues described investment markets as cold-blooded. Regardless of bloodshed and world headlines, stock and bond markets react quickly to new information and adjust to reflect the price people are willing to buy and sell at. Unfortunately, geopolitical risks, like Russia's invasion of Ukraine, are not new to investors and markets. They fall into the "known unknown" category that we have to manage.

The provided table shows how frequently we've had to manage through these known unknowns. Outside of the sheer number of geopolitical events we've encountered, the table provides several insights on how markets react to these events and what comes next.

One theme consistent with all these events is the stock market, measured here by the S&P 500 Index, which fell in value once the geopolitical event occurred. Generally, investors don't like war or conflict since they don't know how long and how large an event it will be.

Then, as more information becomes available, investors assess what is occurring and the impact to economic factors, like growth, spending and inflation, and the impact to profits of the companies they own. There is a point where investors feel the impact of the news is properly reflected in the price of stocks, or maybe when the end to the geopolitical event is in sight, and the sell-off stops. In the table, we can see that the average sell-off occurred over 12 trading days following a geopolitical event. Additionally, there was a wide range of outcomes as the longest was 27 trading days and the shortest was two trading days.

After markets sell-off, they may move sideways for a while, but they have historically returned their appreciating ways with time. In the table, we can see that stocks returned to their pre-geopolitical event level an average of 137 trading days later. The range of recovery timeframes was very wide as the longest it took to for markets to recover to prior levels was 1,475 trading days and the shortest was three days. Of course, other factors can come into play at any time which may lengthen the recovery period. The point here is that stock markets fluctuate, but they have historically trended higher even in the face of geopolitical conflict.

Managing Geopolitical Risk

As investors, we always have the choice of where we put our money and the risks that we are willing to take. Investing in stocks comes with a lot of risks—some known and some unknown. Anytime we own stocks, however, we likely have some exposure to geopolitical risk. Of course, we use broad diversification to help mitigate some of the impact of specific country volatility, but that only goes so far.

Ultimately, one of our greatest controllers of geopolitical risk is the same lever that influences our overall portfolio risk—stock exposure. Therefore, getting the right amount of stock exposure in our portfolio also helps calibrate our geopolitical risk exposure. Given this, we feel there are two insights we can provide in managing these risks.

The first is to make sure we have the proper allocation to stocks. A risk-assessment questionnaire or conversation with our advisor about market downside likely influenced the amount of stock exposure we have in our portfolios. If someone is struggling with the ups and downs in a portfolio, it may be time to have another discussion with a trusted advisor about what the overall allocation to stocks should be.

The second insight is that we should avoid our temptation to time these types of events. As we can see in the table, we don't know how long or how deep a geopolitically induced market sell-off will last. We don't want a situation where we end up selling low and then buying back in at a higher price. That is surely not a winning investment strategy. Understanding that there will be market volatility when geopolitical risks are present can help reduce the urge to go to cash and potentially ruin a well-constructed financial plan.

Geopolitical risk is one of the risks that comes with investing. One of the best ways to manage it—and the worry and concern that may come from its potential investment impact—is to make sure our investments are properly diversified and our allocation to stocks is properly sized for our risk attitudes and return needs.

Impact of Geopolitical Events on Markets is Often Short-Lived

Event	Start of sell-off	Duration of sell-off (trading days)	Duration to recover to prior level	Size of sell-off in S&P 500 (%)
Israel Arab war / oil embargo	10/29/73	27	1475	-17.1
Shah of Iran exiled	1/26/79	9	34	-4.6
Iranian hostage crisis	10/5/79	24	51	-10.2
Soviet invasion of Afghanistan	12/17/79	12	6	-3.8
Libya bombing	4/21/86	20	7	-4.9
First Gulf War	1/1/91	6	8	-5.7
Kosovo bombing	3/18/99	4	9	-4.1
9/11 attacks	9/10/01	6	15	-11.6
Iraq war	3/21/03	7	16	-5.3
Arab spring (Egypt)	1/27/11	2	3	-1.8
Ukraine conflict	3/7/14	6	13	-2.0
Intervention in Syria	9/18/14	21	12	-7.4
Average		**12**	**137**	**-6.5**

Source: JP Morgan Asset Management. Past performance is not indiciative of future results. Markets represented by S&P 500 Index, an index of U.S. large company stocks. Indexes are unmanaged baskets of securities that investors cannot directly invest in. Index performance does not reflect the fees or expenses associated with the management of an actual portfolio.

7 Tips to Control Identity Theft

Given heightened geopolitical tensions, the risk of cyber-attacks and identity theft are becoming even more pervasive. Identity theft occurs when someone steals your personal information to commit fraud, such as fraudulently opening accounts, gaining access to accounts, filing tax returns, filing for unemployment benefits, obtaining medical services, or sending fake bills to your health insurer, etc. While these are core steps to take, this is not designed to be an exhaustive list of all steps you may need to take to prevent identify theft.

1. Freeze your credit for free with all three credit bureaus. A credit freeze will prevent someone from applying for and getting approval for a credit account or utility services in your name. This is the best way to prevent identity theft.
2. Review your accounts and credit reports regularly to ensure no suspicious activity.
3. Enable two-factor authentication for any online accounts, especially for email, social media and financial accounts.
4. Use a password manager to generate, manage and store unique passwords for your accounts. Do not reuse passwords!
5. Encrypt and password protect all computers and mobile devices.
6. Sign up for banking and credit card alerts via email or text message.
7. Know the sender of email! Before clicking any link or downloading any file, be 100% certain of the sender. If in doubt, open a new browser and navigate to your account or confirm with the sender that they sent you something. One downloaded file can result in malicious software being installed on your computer.

Confused as to how to do any of these seven tips? Contact your advisor for help!
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long term. And having a fullyfunded emergency fund gives you that much needed emotional buffer for when markets go haywire or life throws the unexpected at you.

Once you've met with your advisor and considered making any warranted adjustments, performing the last step is often the most difficult for some: stop looking at your portfolio. It is certainly easier said than done, but limiting excessive looks at your portfolio will provide less temptation to act out of emotion rather than on facts. Instead, use that time to reconnect with family, friends, community and yourself.

1 **Source:** "Ukraine Invasion: Seeking (and Finding) Reassurance in Troubled Times." https://www.morningstar.com/articles/1081275/ukraine-invasion-seeking-and-finding-reassurance-in-troubled-times