

Talking to Clients Suffering From High Anxiety

By: Kimberly Foss

There's no diplomatic way to say this: the global stock markets are supremely volatile right now. Going forward, it's hard not to be worried about predictions like the one from Royal Bank of Scotland analyst Andrew Roberts, who says the global markets "look similar to 2008." Roberts also predicts technology and automation are set to wipe out half of all jobs in the developed world. If you listen closely out the window, you might almost hear traders shouting "Sell! Head for the exits!"

When you're in the middle of so much panic, when people are stampeding in all directions, it's hard to realize that there is no actual fire in the theater. Yes, oil prices are down dramatically, and could go lower, which is not exactly terrific news for oil companies and oil services concerns — particularly those who have invested in fracking production.

But cheaper energy is good news for manufacturers and consumers, which is sometimes forgotten in the gloomy forecasts. Chinese stocks and the Chinese economy are showing more signs of weakness, and there are legitimate concerns about the status of junk bonds. These bonds have stabilized in the past few weeks, but another Fed rate hike could destabilize them all over again, leading to forced selling and investors taking losses in the dicier corners of the credit markets.

If you can think above the shouting and jostling toward the exits, you might take a moment to wonder about some of these panic triggers. Are oil prices going to continue going down forever, or are they near a logical bottom? Is this a time to be selling stocks or, with prices this low, a better time to be buying? Are China's recent struggles relevant to the health of your portfolio and the value of the stocks you own?

And what about Roberts, who's essentially yelling "Fire!" in the crowded theater? A closer look at his track record shows that he has been predicting disaster, with some regularity, for the past six years — rather incorrectly, as it turns out. In June 2010, when the markets were about to embark on a remarkable five-year boom, he wrote: "We cannot stress enough how strongly we believe that a cliff-edge may be around the corner, for the global banking system (particularly in Europe) and for the global

economy. Think the unthinkable," he added, ominously. ("The unthinkable," whatever that meant, never happened.)

In July 2012, Roberts wrote: "People talk about recovery, but to me we are in a much worse shape than the Great Depression." Wow! Wasn't it scary to have lived through, well, a 3.2% economic growth rate in the U.S. the following year? What Great Depression was he talking about? Taking his advice would have put you on the sidelines for some of the nicest gains in recent stock market history. It's also interesting to note that Roberts did not predict the 2008 market meltdown.

Since 1950, the U.S. markets have experienced a decline of between 5% and 10% (the territory we're in already) in 35.5% of all calendar years — which is another way of saying that this recent downturn is entirely normal. One in five years (22.6%) have experienced downturns of 10% to 15%, and nearly 18% of the last 56 years have seen downturns, at some point in the year, of more than 20%.

Stocks periodically go on sale because people panic and sell them at just about any price they can get in their rush to the exits, and we are clearly experiencing one of those periods now. Whether this will be one of those 5%-10% years or a 20% year, only time will tell. But it's worth noting that, in the past, every one of those downturns eventually ended with an even greater upturn and markets testing new record highs.

In times like these it is helpful to remember that, in order to generate the type of long-term returns that create wealth, you have to accept a certain amount of risk. With that risk comes volatility. The key is not to take steps to avoid the risk altogether, but to manage the risk where possible.

As part of that, I've developed a DARE platform for advising clients:

Diversify – Diversification is your best friend in volatile markets.

Allocation – Percentage exposed to stocks versus bonds can help reduce the volatility of the market and increase wealth over time.

Rebalance – A recent study by Vanguard notes that rebalancing at 5% thresholds is the optimum balance between risk control and cost minimization.

Evaluate – What stage in life are you in? Do you need income, growth or preservation of principal, and what is your ability to take risk in the market and stay in for the long run?

As a final note, David Booth from Dimensional Fund Advisors observed, "Where people get killed is getting in and out of investments. They get halfway into something, lose confidence and then try something else. It's important to have a philosophy."

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