Asset Risk Consultants (ARC)

In these strange times, many of the fiduciaries who I have spoken to have noted their clients, while concerned over the significant movements in financial markets, are currently more focussed on making sure they and their families are safe and remain healthy. However, a number of trustees have enquired what we might recommend investors should do in response to current market volatility. So here are a few thoughts that may prove helpful.

<u>This Period of Uncertainty Will Pass</u>
There are a multitude of “unknowns” about the COVID-19 virus and its impact on financial markets and economies in general. It is clear that there will be significant negative consequences for economic growth and financial markets have fallen rapidly as a consequence. Investment markets are likely to remain volatile for some time. Only as a path forward becomes clearer will the volatility caused by fear subside. But eventually that will happen and financial markets are likely to stabilise and may well rise swiftly.

<u>What Should An Investor Do Now?</u>

(i) Don’t Double Guess The Professionals
Many of ARC’s clients employ discretionary managers who will be seeking to protect capital and grasp opportunities. These managers will most likely be taking appropriate actions already, so investors who take tactical actions as an overlay to manager discretion, run the risk of “doubling” or “offsetting” the actions of their managers.

(ii) Don’t sell investments unless it is essential
Now is the time to postpone selling risk assets unless absolutely unavoidable so as to avoid crystallising gains. Timing the bottom is virtually impossible. Selling now to get back in when the market has fallen further might work but more often than not history tells us that the turn is missed.

(iii) Think About Re-Balancing
For clients who have not delegated responsibility to a discretionary manager, the chances are that their risky assets (equity exposure) has materially underperformed their diversifying assets (bond exposure), resulting in an underweight equity exposure. Both theory and experience tells us that consideration should be given to re-balancing (selling some bonds to buy more equities) to return the overall portfolio risk budget to the appropriate level. When the recovery eventually arrives this will make a positive contribution to returns but the decision to do so may not be palatable to all investors. Nevertheless it is the right thing to do.

In summary, currently financial markets are reacting to fear not facts. This phase will pass and some semblance of order and rationality will return to financial markets. Now is definitely not the time to be trying to time the market, nor to second guess experienced discretionary fund managers who will be seeking to preserve capital and take advantage of opportunities. It may be sensible to re-balance asset allocation if the risk asset percentage has moved more than say 5 percentage points. But that is not the same as calling the bottom. It is merely seeking to keep the proportion of risk assets constant.

I hope this is helpful and as always we welcome your comments and questions.