Russell Investments

Investor

Helping you make informed investment decisions

UNDERSTANDING MARKET VOLATILITY

INVESTED. TOGETHER.™

Living with market volatility isn't easy. When financial markets experience an upward or downward spike, it can be difficult not to get caught up in the hype. From attention-grabbing news headlines to predictions from industry economists—it seems everyone has a different opinion on what the market will do next, and what you should do about it.

There is certainly a tendency for all of us to get excited about short-term fluctuations in the market. We should be concerned for the fortunes of the individual securities, countries and sectors we have invested in, but making decisions under stress can sometimes lead to irrational decisions.

During periods of market distress, it is important for investors to take a longer-term view of their holdings, and consult their financial advisor on the optimal positioning to help ensure they reach their desired investment outcome.

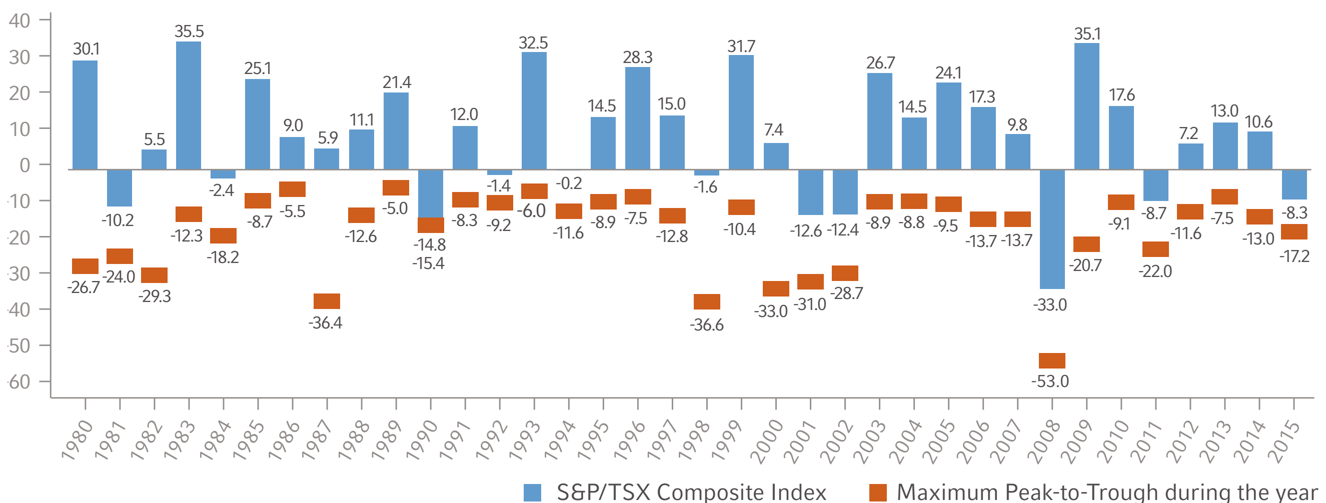
Having an agreed-upon plan and a well-diversified portfolio of stocks, bonds and alternative assets can help you look past short-term volatility. An allocation to defensively oriented stocks—such as real assets, for example—can also help you more easily weather volatile periods. Stocks with defensive characteristics may help preserve capital as they generally don't fall as far as the broader market in declining periods (and don't climb as far as the broader market in rallies). Defensive stocks are characterized by companies with stable earnings and strong balance sheets with limited leverage that can withstand shocks regardless of the state of the overall market.

Generally speaking, what occurs in the stock market in a specific year (or month, or day) is not likely to have a significant impact on your investments over the longer term. Given demographic trends in Canada, even someone on the cusp of retirement can have another 20 to 25 years to grow their portfolio. Over any 20-year time period, equities have historically outperformed bonds and cash. For the average investor, more than 50% of the money they will spend in retirement they have not yet earned the day they retire.[1]

Despite annual pullbacks, in 25 of the last 35 years, Canadian equity markets finished in positive territory.

The pullbacks are common and should not distract long-term investors

Canadian equity returns (in %) per calendar year and declines during the year



Source: Russell Investments, BNY Mellon

As of 12/31/2015. Returns calculated with dividends included. Maximum peak-to-trough represents the return difference between the largest peak-to-trough of the calendar year.

Index returns represent past performance, are not a guarantee of future performance, and are not indicative of any specific investment. Indexes are unmanaged and cannot be invested in directly.

Equity market volatility is normal: equities and other "risk" assets typically provide higher expected long-term returns than savings deposits and government bonds because they have a higher investment risk and a higher degree of short-term uncertainty. If equities were less volatile, and their returns more predictable, then the expected long-term returns would also be significantly lower.

Some level of equity risk is necessary for most investors if they want to achieve the goals they have in retirement. Over an investing lifetime, there's no way to eliminate all discomfort while retaining the exposure to risk necessary to generate meaningful returns that can outpace inflation.

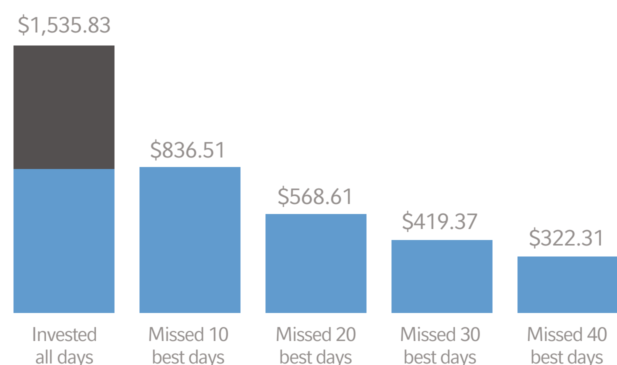
Fortunately, although they may be unsettling, moments of heightened anxiety also tend to signify points of potential opportunity. By looking at the historical performance of the equity market, we can see that despite volatility, the market has recovered over the long term.

One of the best examples of such a recovery is the period between 2009 and 2014. As the Great Recession hit in 2008, Canadian equities—as represented by the benchmark S&P/TSX Composite Index—began a rapid decline from the commodities-fueled boom of the early 2000s, and closed at a low of 7,566.94 points on March 9, 2009. The index then began to rise, reaching an all-time high of 15,657.63 points on September 3, 2014. That means it more than doubled in that five-year period. An investor who just stayed the course through the recession was most likely rewarded. Of course, the markets have continued to fluctuate since then.

Changing your investment strategy in response to short-term market conditions can be dangerous: investors reacting to market events risk selling after periods of negative returns, and chasing performance. This can lead to the worst of all worlds: "buy high, sell low". Investors should base their investment strategy on their investment goals, time horizon, financial circumstances and risk tolerance, not the behavior of markets over the most recent weeks.

Market timing is difficult

CRITERIA: Investment of $1,000 for 2,514 days in a 10–year period



Source: Russell Investments, Confluence

Based on daily returns of S&P/TSX Composite Index for 10-year period ending December 31, 2015.

For illustrative purposes only.

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It is very difficult to successfully time the market over the long run. The average investor doesn't usually have the time (or desire) to keep an eye on the market every day. Moreover, since most market rallies occur in brief spurts, there are a host of reasons to avoid timing the market. Market timers waiting for the right spot to buy, risk being out of the market during these sudden market changes. Investing for the long run, with a well-diversified portfolio, may be the best way to capture the potential upside.

It is important to accept that the value of your investments will rise and fall based on market behavior which is out of your control. Implementing a disciplined process of rebalancing can be a better process for managing your portfolio risk than reacting to volatility.

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While you would need to stay in the market to capture its potential gains, it's also important to stay in the market with the right portfolio for you, one that is aligned with your goals and long-term expectations for risk and return.

Important Information:

[1]Source: 15/35/50 Russell Investment's Retirement Lifestyle Rule

Commissions, trailing commissions, management fees and expenses all may be associated with mutual fund investments. Please read the prospectus before investing. Mutual funds are not guaranteed, their values change frequently and past performance may not be repeated.

Please remember that all investments carry some level of risk, including the potential loss of principal invested. They do not typically grow at an even rate of return and may experience negative growth. As with any type of portfolio structuring, attempting to reduce risk and increase return could, at certain times, unintentionally reduce returns.

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