Equities

Time to reflect or act

With the recent increase in stock market volatility, it is perhaps an opportunity to step back and add some perspective and context into the mix.

In order to do this we will need to make a number of assumptions based on the information to hand and these can be either right or indeed completely wrong and in themselves may drive us to make good or bad decisions about investment strategy, asset allocation and timing, all of which contribute to the performance of portfolios. We may take a short term reactive decision where fear of further market falls may be the principal driver, or we can attempt to interpret the fundamentals and take a longer more pragmatic view.

Corrections occur in every cyclical bull market. We have already seen twelve corrections of 5% or more since global stock markets bottomed in 2009. Over the longer term there have been sixteen corrections of 10% or more – about one-third were in the region of 20% - during cyclical bull markets over the past five decades.

A pullback has been somewhat overdue as the previous one of any note was in 2011, and in truth the conditions were ripe from a sentiment, technical and market positioning perspective.

However, history suggests that one will fear a dozen bear markets for everyone that actually occurs. Each time the investor who sets out to trade the cycle will be tempted to do the one thing which history shows is the most likely to lead to poor performance – sell equities.

This is contrary to the traditional 'buy and hold' investment strategy which most long term investors follow, although it has been questioned in recent years, largely because it doesn't work particularly well in bear markets.

However, the successful long-term performance record of 'buy to hold' investing generally remains intact and there are powerful reasons for believing that it remains the most sensible mainstream approach to investment.

Some investors may succeed with investment policies based on short-term timing, but since this is, in actuality, largely a 'pass the parcel' game with existing wealth, an equal number of investors will not. Some will say that real investment is about sharing in the new wealth that companies are able to create each year through the profits they earn selling their goods and services in the real world, part of which they then distribute as dividends which increase over time.

That is not to say that taking money out of the markets doesn't protect capital. However, it is all about the timing. Selling out of fear of a bear market which subsequently turns out to be a correction that reduces over-stretched valuations and increases the prospects of further price appreciation can be a costly exercise. Rarely do investors get the timing of sales and re-entry into the markets absolutely correct. Not only are there the costs of buying and selling, but the exit and entry points can be notoriously difficult to judge. Oh that it were simply the case of buying low and selling high.

by **Stuart Cowan**, Investment Director, Ramsey Crookall & Co Ltd

If there is a fundamentally sound investment strategy in place, with money allocated into areas that are seen as offering the prospect of long-term growth, and weightings are appropriate so that excessive falls in a particular sector or stock are not too damaging then thoughtful investment into good quality equities will be rewarded even if the ride is somewhat bumpy along the way.

By all means act swiftly and decisively if you have overriding concerns about macro-economic, geopolitical and market conditions, but do remember that being out of the market during the 'good' times can seriously limit performance. It is after all, mostly about the timing.

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