OLD NORTH STATE TRUST, LLC

One Certainty About Investments: Markets Hate Uncertainty

Troubled times can lead to troubled investors. One of a good financial advisor's most important duties is to help clients avoid making rash decisions at times of great change and uncertainty, such as we are going through right now.

A major change in government, as we see coming after the 2016 elections, is one of those things that can make investors very, very nervous. But not necessarily because of the potential direction that the newly elected officials might take the nation. History shows that financial markets don't care whether we have Republican or Democrat in the White House; they just hate uncertainty.

An excellent example of this came literally during the overnight hours on election night, when the presidential result was down to the wire and could have gone either way. Those markets operating at the time plunged briefly. But when the stock exchanges opened on Wednesday morning, and it was clear who the winner would be, all the losses were made up; the markets remained stable and have risen into record territory since.

So now that we know who the president will be, we can get back to the business of business!

I have seen an interesting statistical analysis that goes back to 1933, the depth of the Great Depression. This covers the worst and the best of the twentieth and twenty-first centuries' economic booms and busts, through war and peace and widely different governmental scenarios.

The best market performance, measured in average annual price appreciation for securities, was 15.1 percent. And that very high growth rate took place under both Democratic and Republican presidents.

As it happens, those numbers also corresponded with Republican control of Congress, though of course it would be a gross oversimplification to say that was the only cause. Comparable numbers show 14.3 percent market growth under a Democratic president with a split Congress, and 9.5 percent – still robust and healthy – with Democrats controlling both the White House and Capitol Hill.

The slowest markets, with growth from 3.5 percent to 4.9 percent, were when Republican presidents served alongside a Democratic or split Congress.

I don't offer these numbers to argue for any particular strategy or theory of investing, other than to reinforce the case against panic or hasty decisions based on election results. Or based on anything else in the news, for that matter.

Let me talk about how other sorts of uncertainty can distort investors' thinking. Who can forget how worrisome things got in 2008, when the market was going to pot?

At that time, while working for a large bank's trust department, I had a client who was getting very nervous. (Did I say "A" client? Truth be told, more than one fit that description.) But I was having a lot of difficulty regularly talking this one particular client off the ledge. He kept wanting to sell off everything and go to cash. I kept trying to talk him out of it and he kept insisting that was what he wanted to do. Finally, I couldn't talk anymore and he made me sell out.

This happened to be at just that falling market's precise bottom! He couldn't have picked a worse time. Not even one of my other clients panicked in this way, or chose such a rash strategy. All the others, to my great relief, stayed the course. They kept the faith, maintained their allocations, and saw their investments rebound.

Today, those other investors' portfolios are back and beyond where they were then and they never missed a beat.

Of course, in retrospect, it's easy to see that they had reacted appropriately. But that's not to say that these clients weren't worried. Of course, they were. But through the financial crisis of 2008-09, they continued to live their lifestyles; they worried, but they trusted me and our system. Nothing changed, except the numbers on their statements.

The client who sold out, though, didn't have those numbers to work with anymore. When the market started its way back up, he had a greatly reduced amount of cash to invest. Since that time, I have seen the real-life consequences of those decisions from eight years ago, and they have been significant.

The man has bought into a retirement community and, sadly, developed Alzheimer's disease. His wife, who was never part of the decision-making process when it came to finances, had to start making investment and spending decisions, but with a much smaller pot of funds to work with.

It has not been possible for this couple to get the assisted-living services they need, and they are quickly using up what funds they have left in paying for home care. It's a truly sad story. I wish that I could have helped them better, but my hands were tied when the client insisted on disregarding my advice.

Fear drove bad decisions that are now affecting the rest of this couple's lives.

So, to use a great historical phrase, even while not giving in to the fear "fear itself," what should a wise investor do during times of uncertainty? Let me offer a few general suggestions for those who can't bear the idea of remaining entirely passive.

First, think about your investment objectives. After all, what's happening in this year's market is likely to be far less important if your time horizon is long than if you'll need a particular sum within the next year or two. Any decision influenced by current market numbers should always be weighed against your overall goals, not taken in a vacuum.

Second, when in doubt, talk with your advisor about current conditions, your specific worries, and how those fit with your financial plan. Experienced investment professionals will offer examples, data and targeted advice that's relevant to you and your objectives. That means you're not left relying on just the latest thing you read or see on TV.

Finally, remember that sharp changes in the markets, when they come, don't affect all investments equally. So, these uncertain times can be a good opportunity to re-balance your portfolio. Your advisor can offer specific suggestions about how and when to do this, if it's appropriate. This is a good idea on its own – "buying low and selling high" – but also has the psychological advantage of doing something careful and rational rather than just watching and waiting.

In any case, though, my best advice now during this time of profound political transition, is to remain calm. And if you're inclined to analyze the situation, do it in consultation with a trusted financial advisor who can help you weigh facts and data rather than fears and speculation.