

Volatility is Back

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Over the last month we have seen a return of volatility and decline in the world markets. The financial markets are complex, inter-connected, and global. We are all in this together. When financial crisis occurs in another part of the world, the markets in the US react. World leaders recognize their interdependency. They coordinate their efforts to avoid economic collapse. Looking ahead, we need to beware of simple solutions and sound bites. The financial problems of our country and others have take a lifetime to create, and will take some hard choices to correct.

How do you survive? Nothing goes up—or down—forever. Remember the roller-coaster performance of 2007 through 2009. When the next bull and bear cycle occurs remember that this too shall change.

Appropriate diversification helps minimize losses and also positions your portfolio to be ready to catch the next move up. In 2008 and early 2009, we faced an economic tsunami that affected nearly all asset classes. But people with reasonably well-constructed portfolios didn't see their accounts drop nearly as much as those with less-diversified holdings and those who had chased performance. Moreover, diversified investors enjoyed the early stages of the market recovery. A media contact asked me, “What should investors be doing now?” The simple answer is to follow their plan. If they are properly diversified, you should at most rebalance back to their recommended allocation. If you are still in the accumulating phase of life, you should also continue to invest each payday.

If you are overly concerned, maybe to the point of not being able to sleep; you aren't as risk-tolerant as you had previously believed. This is a good time to assess both your need to assume some risk and your tolerance for it. Remember to distinguish between your financial capacity to handle risk and your actual reaction to it.

You can not control the markets; therefore focus on what you can control. All of us feel helpless at times during the market volatility, but there were always things over which we did have control. The most important of those are our reaction to events. In the end, that is all that any of us really can do.

The future is uncertain, but plan for one anyway. If anything, the last few years have underscored the importance of planning. You cannot depend upon gains in your home's value or fabulous returns in your existing stock portfolio to help you easily achieve your financial goals. Your retirement, your children's education, your business, all have to be funded by your contributions, and you need to manage your various risks. The future belongs to those who plan.

Expect the unexpected. Bad—and good—surprises happen. We'll no doubt have more surprises in a choppy recovery. But be open to the possibility of some good things along the way.

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Charles Buck CFP®

“Never invest in a business you can not understand”

Warren Buffet

Ask the CFP®

Q. What is the rule of 72 I have heard used with investing?

A. The Rule of 72, discovered by Albert Einstein, is a quick way to determine how long it will take to double your money given a certain rate of return. To use the rule is to divide any percentage return into 72 to find how long it takes to double your investment. For instance, dividing by 72, by the rate of return, for example 6%, will give you a result of 12 years.

Another question is what rate do I need to earn to double my money in 10 years? To calculate the result, divide 72 by 10 and you see that it takes 7.2% rate of return to double your money in 10 years.

Another way to use this rule is for the question; with an inflation rate of 3% how long will it take to reduce my purchasing power in half? Another calculation, 72 divided by 3 equals 24 years for your purchasing power to be reduced by one half.