MURRAY JOHN
& Associates

FINANCIAL VIEWPOINT

MURRAY JOHN AND ASSOCIATES LTD

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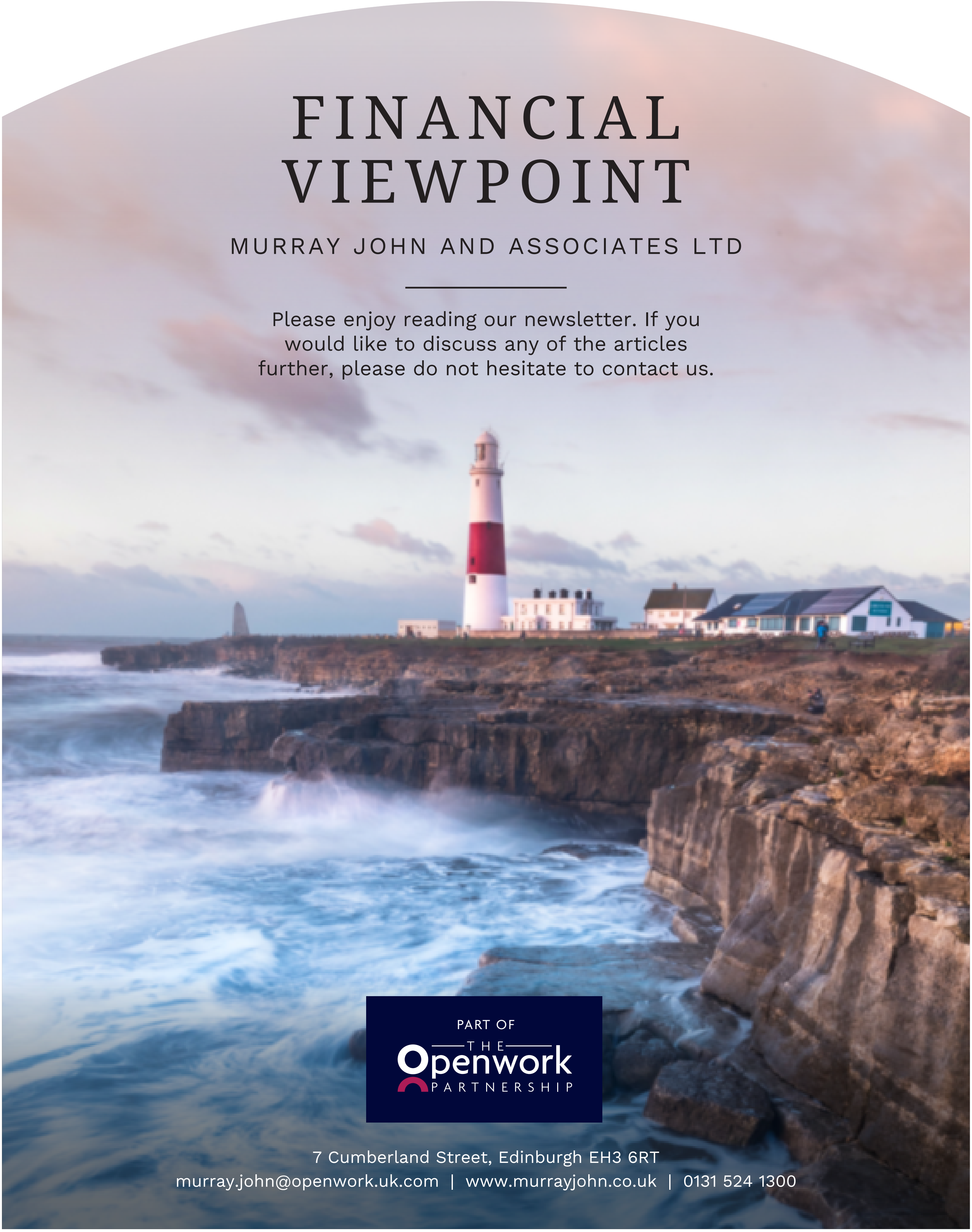

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3 important reasons for staying invested through market downturns

It's been a difficult year for investors so far. Inflation and political uncertainty have led to market volatility.

Market volatility can be scary, especially if the value of your investments drops, but it's important not to let fear guide your decision about whether to stay invested in your portfolio. Here are three reassuring reasons for staying invested in the stock market during uncertain times.

1. The best financial decisions are not based on emotion

Emotions can play a big role in your financial decision-making if you aren't vigilant. The thrill of seeing your investments increase in value can quickly be replaced with panic and fear when the value decreases during market slumps.

When you understand the cycle of emotions related to investing, you can reframe downturns as opportunities to maximise your returns in the long term. This is because when the value of investments falls, it becomes cheaper to buy more shares or fund units – providing greater opportunities to grow your wealth when conditions improve.

As Warren Buffett, one of the world's most successful investors, famously said: you should aim to be "fearful when others are greedy, and greedy only when others are fearful".

By looking at the situation objectively, without the influence of emotions, you will be able to make sensible financial decisions based on your understanding of how the markets tend to ebb and flow.

2. Bull markets tend to outlast bear markets

When markets are trending upwards and investments are generally growing in value, this is called a "bull market". This is when you will often see your investments increasing in value.

By contrast, a "bear market" describes periods when the market has dropped 20% or more from its peak. Despite rallying in October, the S&P 500 is currently down 22% since the start of the year, with many of the top-performing US stocks noting significant drops since the start of the year.

As seen in the chart below, bull markets have not only been more frequent over the past 60 years, but they have also tended to last far longer than the average bear market.

So, despite the rocky start to 2022 for investors, it makes financial sense to be optimistic about the prospect of markets recovering sooner rather than later. As the markets recover, you could see significant increases in the value of your investments.

3. Staying invested could produce better long-term gains than moving to cash

Attempting to time the market by moving your investments into cash during market downturns could lead to significantly lower long-term returns than if you had stayed invested throughout.

The chart below shows how returns on £1,000 invested can be affected by attempting to use this strategy.

The end results show that the initial investment would have created a final value of £1,993.32 if it had remained invested throughout downturns; if the same amount had been invested initially, but removed from investments during downturns, the final value would have only been £1,042.43.

The difference in returns is partly because the best days in the markets tend to occur immediately after a downturn. By attempting to time the market, you will often miss out on the significant returns generated on these important days. Compounding is the process of generating returns on the total value of your portfolio, including both your initial investment and any returns generated since then, so the impact of missing the best days in the market will be reflected in your portfolio's value for many years.

Get in touch

If you're concerned about whether the current market volatility will affect your long-term financial plans, seeking expert advice can help to reassure you and keep you on the right track.

We can help you to decide on the most appropriate next steps based on your circumstances and future goals. Please get in touch to arrange a time to chat.

Please note: *The value of investments and any income from them can fall as well as rise and you may not get back the original amount invested. Past Performance is not a guide to future performance and should not be relied upon.*

The financial assets quilt

Why diversification is key when inflation rises

To stay ahead of rising costs and maintain your assets' purchasing power, your portfolio needs to provide positive returns. Diversification can help you achieve this.

What is diversification?

Diversification is investment jargon for the well-known proverb: "don't put all of your eggs in one basket".

While a well-diversified portfolio doesn't give you guaranteed downside protection, it can help you maximise long-term growth potential. Since the values of different types of assets don't always behave the same way or move in the same direction, holding a range of different investments can help reduce your risk.

Balance between risk and reward

The balance between risk and reward should be front of mind – diversification is key to this.

The chart below breaks down historical performance and volatility of different asset classes – cash, equities, real estate and so on – over time. The balanced portfolio – represented by the white boxes – highlights how diversification can help reduce risk in the portfolio and enhance returns.

Protect your downside

When global events provoke market volatility, a well-diversified portfolio can help protect your downside.

As illustrated below, when Russia's invasion of Ukraine caused volatility, some markets were more severely affected than others.

Had you invested the majority of your money in Europe, you would have suffered far greater potential losses than if your portfolio had been invested across all regions.

4 main asset classes for a well-diversified portfolio

Spreading your wealth over different asset classes should achieve a strong, well-balanced portfolio.

1. Cash
Secure and easily accessible, cash is generally considered to be the safest asset. However, it tends to provide lower long-term returns than other asset classes and its value can be eroded by inflation.

2. Bonds
Bonds are a loan you make to a company or organisation from which you receive interest payments. While usually considered medium risk, this depends on who is issuing them.

3. Equities (or shares)
Equities are an ownership stake in an individual company listed on a stock market index – the FTSE 100 in the UK or the S&P 500 in the US, for example. Many investors hold equity assets in funds, such as pensions, ISAs, or unit trusts, which are often pooled or collective investments. Investing in individual companies tends to carry more risk, so a collective approach can be extremely beneficial, especially since funds are looked after by professional managers. Because your money is pooled with other investors, you can often access a range of investments that might otherwise be unavailable.

While history shouldn't be considered a guide to the future, over the longer term equities tend to outperform other types of investment.

Shares can be volatile. Their value can go up as well as down and you may not get back the full amount invested.

Alternative investments
Property is one alternative investment. Its returns tend not to closely correlate with those of shares or bonds, which may be useful if you want to introduce another source of potential capital growth and income into your portfolio.

While property tends to be less volatile than equity or bonds, its value can fall as well as rise and is also less liquid; it can take longer to invest into and sell when you want to access your money.

Other alternative investments include:
— Infrastructure funds (large, high cost projects, often connected to public development of core systems such as transportation or electrical supply)

— Natural resources (companies that are involved in the extraction of oil, gas, coal, metals, etc.).

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Diversification is more than just the type of asset held

You can also diversify across:

— Geographical regions – the US, UK, Europe, or Asia

— Sectors – finance, energy, or transport

— Themes – technology, healthcare, or renewable energy

— Size – smaller companies (small cap) or larger companies (large cap).

3 reasons diversification is key

A well-diversified portfolio can help you:

1. Minimise risk and increase potential returns
Diversification spreads risk and helps to limit the impact of market volatility on your investments. When one sector, asset class, or geographical area falls, a rise in another area could help to offset the loss.

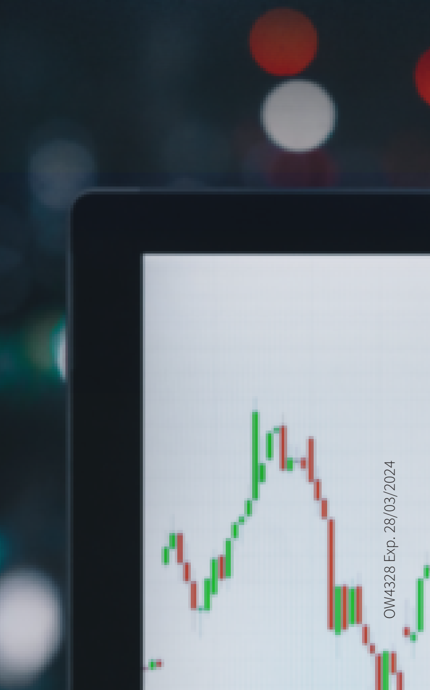
2. Provide greater opportunity for returns and eliminate investment biases
Diversification can help prevent you from falling foul of investment biases. You may be overly confident about the performance of sectors you know, or geographical regions that you're familiar with. These unconscious biases could see you miss out on potential growth, whereas a diversified portfolio won't be constrained.

3. Help you to consolidate gains
As your investment goal approaches, you might want to consolidate your gains. Diversification allows you to do this by rebalancing, increasing the number of lower-risk assets you hold.

This should help to avoid the value of your investments suddenly falling in value when you need to withdraw funds.

Get in touch

If you want to ensure that your portfolio is well-diversified and balanced according to your financial goals, we can help. Please get in touch to arrange a time to chat.



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The effect of psychology on investors

You should base financial decisions on logic and facts. But psychology can have a much larger effect than you think, and it can lead to you making decisions that aren't right for you. Read on to find out more about what behavioural finance is and how it could affect you.

"Behavioural finance" was first coined in the 1970s by economist Robert Shiller and psychologists Daniel Kahneman and Amos Tversky. They used the term to refer to how unconscious biases and previous experiences affect the way people make financial decisions.

It can be used to explain why investors can make knee-jerk decisions or invest in opportunities that aren't in their own best interest. Rather than relying purely on facts, investors often have biases that affect how they react to certain situations.

Finance bias can lead to "irrational" decisions through shortcuts

There's a reason why people often make decisions based on biases: they can make the decision-making process quicker.

If you imagine how many decisions you need to make every single day, it's easy to see why this kind of decision-making can be useful. From what to eat for breakfast to which way to travel to work, it'd take up all your time if you carefully went through the facts for each decision you make. So, you make shortcuts by using biases.

However, while it can be a useful process in your day-to-day life, bias can have a negative effect when you're making important decisions, including financial ones.

Behavioural finance covers five concepts:

1. Mental accounting
Mental accounting can be incredibly useful when you're managing a budget. However, inflexibility could mean you miss out on opportunities.

The concept refers to how people may designate money for certain purposes. So, you may have different savings accounts for various goals. It's a process that can help you manage your outgoings and work towards goals.

However, it can also lead to irrational decision making.

You may not dip into a savings account that you've allocated to buying a new car even when you face an emergency and it'd make sense logically.

How you receive the money may also affect how you use it. For instance, you may put off using money that was given as a gift in an emergency because you believe it should be used for something special.

2. Herd behaviour
Herd behaviour is something that's often seen in investing. When you hear that lots of people are selling certain stocks or buying a specific share, it can be easy to be led by this and follow suit.

It can lead to you making decisions that, while possibly right for others, don't suit you or your circumstances. It's not just investing where herd behaviour can have an effect. You may be tempted to purchase an item after a friend has or choose a savings account because someone you know has.

3. Anchoring
When you have some information, you may focus on this – anchoring your views to this data.

Setting a benchmark can be useful, but it can mean you don't take in other information, especially if it's contradictory.

So, you may hold on to investments even after the value has fallen because you've anchored its worth to a previous valuation.

4. Emotional gap
Emotions often play a role in financial decisions. You may sell a stock because you fear that the price will fall, or make an impulse purchase because you're happy.

Being comfortable with your financial plan is important, but an emotional gap can fuel irrational decisions as you're more likely to overlook data.

5. Self-attribution
This concept refers to how investors are likely to have overconfidence in their abilities.

You may believe you can reliably time the market to maximise profits when the markets are unpredictable. In this case, it's common to see "wins" as being down to your knowledge, while "losses" are attributed to things outside of your control.

Unconscious bias may affect your decisions in ways you don't expect. If you have any questions about your finances and the decisions you need to make, please contact us.

The value of your investment can go down as well as up and you may not get back the full amount you invested. Past performance is not a reliable indicator of future performance.

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