Investing is easy! (it's staying on track that is hard)

Let's start with some cold hard facts.

1. Typically, **within every calendar year**, the FTSE All-Share will experience a peak-to-trough temporary decline of around 15%.
2. Typically, **every five years or so**, the FTSE All-Share will experience a longer-but-still-temporary decline of 30% or more.[1]

How would you react when faced with these events?

Fortunately, once we know these events are not only likely they are inevitable, we can start to accept them as a normal part of investing and plan accordingly. Indeed, we should (with time and experience) come to embrace them as evidence that the system continues to operate normally.

That doesn't mean we can all sit there with big smiles on our faces as we watch our valuations fall but it does mean we can be better prepared to control our actions in response to the falls.

Unfortunately, it is human nature to want to be proactive in these situations and somehow protect ourselves from the 'hurt' of seeing the paper value of our investments falling, however the potential impact of acting at these times can be devastating to financial outcomes.

Perhaps the most graphic representation I have ever seen of this is illustrated in the chart below which shows the annualised percentage returns in the US over varying time periods. The highlighted columns show the average investor return and the average return of the wider US market in which these same investors were investing.

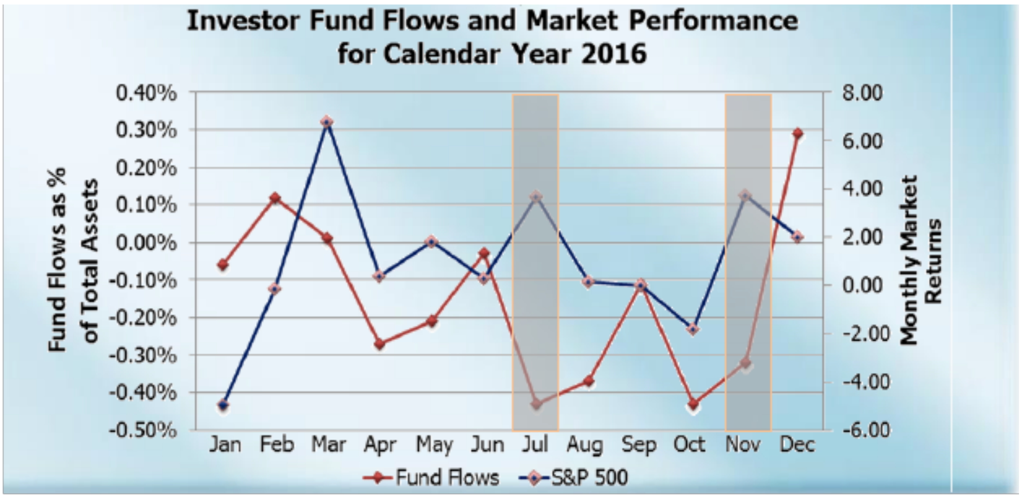
	Investor Returns					
	Equity Funds	Asset Allocation Funds	Fixed Income Funds	Inflation	S&P 500	Bloomberg Barclays Aggregate Bond Index
30 Year	3.98	1.85	0.57	2.65	10.16	6.34
20 Year	4.79	2.29	0.48	2.13	7.68	5.29
10 Year	3.64	1.78	0.40	1.83	6.95	4.34
5 Year	9.83	4.85	0.05	1.40	14.66	2.23
3 Year	3.42	1.45	-0.23	1.25	8.87	3.03
12 Months	7.26	5.48	1.23	2.07	11.96	2.65

Over each time period investors underperformed the market, often by significant amounts. On the basis that all the average investor had to do was nothing in order to obtain the market return it begs the questions – '*What exactly did they do to miss out on all those gains?*'

The answer is that it was almost certainly one of these **3 BIG mistakes**:

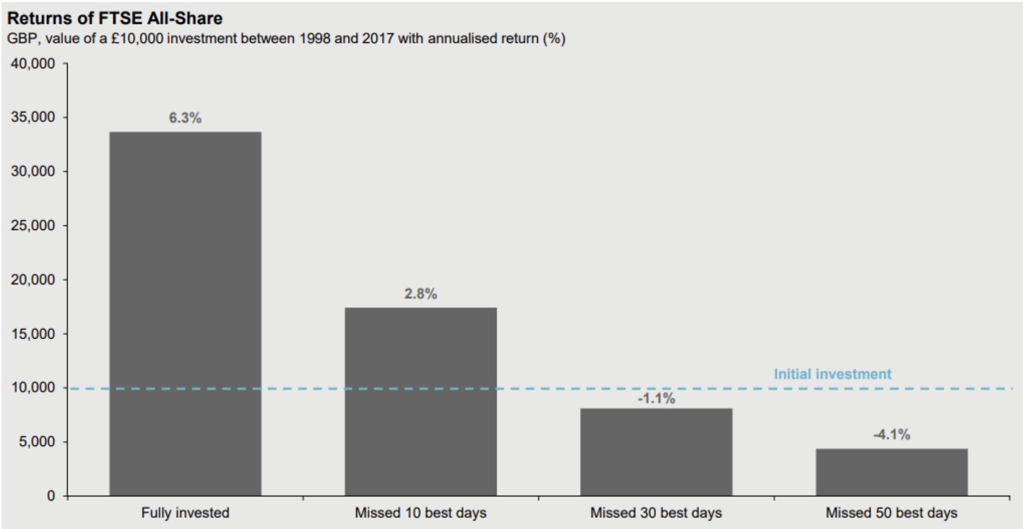
1. **They tried to time the market – the biggest BIG mistake**.

   2016 provided a great case study for this one (but you can find them every year if you look for them). There were two major geo-political events; the late June EU referendum here in the UK and the November Presidential election in the US. The chart below shows two lines indicating how investors were reacting to these events and how stock markets were reacting:



To simplify the chart the highlighted vertical bars show the red line dipping at both of these points indicating that the massive preponderance in the market was towards people selling. The blue line shows that the market actually went up at both times. The result – investors missed out on gains they will never be able to recover. Bear in mind this is just one year. If you add these mistakes over many years it is easier to see how the average investor can underperform the market to the same degree. Investing in line with your financial plan is a lifetime's work and can span decades not just years.

Without wishing to the labour the point (but I'm going to anyway) the below chart shows the annualised return of the UK stock market from 1998 to 2017 and the impact of not being invested on the best 10, 30 and 50 days.



Source: Bloomberg, FTSE, J.P. Morgan Asset Management. Investment outcomes based on price returns. For illustrative purposes only. Returns calculated daily over the time period assuming no return on each of the specified number of best days. Past performance is not a reliable indicator of current and future results.
Guide to the Markets - UK. Data as of 30 September 2018.

Until such time as we develop a crystal ball market timing the market will never be an effective strategy and will likely continue to be the most sure-fire way to derail a financial plan. If the brightest investment minds in the world, with the best research, doing it all day every day along with billions of pounds at their disposal can't do it then I think we can safely assume none of us can – and therefore shouldn't waste our time trying.

2. **Reducing the diversity of a portfolio**. Inside every tortoise there is a hare trying to get out.

   When you see markets racing higher and certain sectors in particular flying away it is oh so tempting to sell your beautifully diversified portfolio and try to hop on the bandwagon. Linked to the above issue of market timing we will not know when to get out of these stocks. I will mention two types of stock and say no more – Technology & Banking.

3. **Chasing the next hot thing.**

   If you ever read the financial press (which I hope for your sake you either keep to a minimum or better still avoid completely) you will see plenty of tips for the '*next hot thing'* in investing. Whether this is a geographical region, economic sector or investment style there will always be something touted to be the next place to be invested. This plays to the human condition of fear (of missing out) and greed. This can lead to investors chopping and changing their otherwise beautifully diversified portfolio, suffering dealing charges as they go. Even if one or two of these calls go right it is guaranteed that some will go wrong and when it does the usual response is to chase higher and higher returns with riskier and more speculative investments often with disastrous results.

You are the determining factor

All of this evidence points directly to the fact that each of us are the dominant determinant in our long-term financial success. After us the next biggest determinant is asset allocation i.e. whether you are invested in stocks, property, cash etc (but that is probably a topic for another day).

Suffice to say we, as investors, have a far greater impact on our finances than economic events or one's exposure to a particular market as long as we can continue to be disciplined when all those around us are losing their heads.

So, let's reflect again on the cold hard facts. When these events happen, and they inevitably will, our counsel as Financial Planners will always be to sit tight, not to overreact and to wait for the equally inevitable recovery because that is how you will realise the greatest real-life financial outcomes and keep your financial plan on course. Our job will continue to be to provide this counsel and guide you successfully through these times. Together we will make sure that your financial plan stays on track.

[1] courtesy of Nick Lincoln, Values to Vision Financial Planning

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