Navigating Market Volatility

Over the last month, many of you may have noticed the recent ups and downs of the financial markets. Higher interest rates, rising inflation and the ongoing pandemic have all contributed to recent market volatility and that will very likely continue to be a big theme throughout 2022.

The initial economic shock of the pandemic has had knock-on effects all over the world, most notably the global supply chain crisis. At the same time, more localised events like China's property crisis and Europe's energy crisis are slowing economic activity for both them and their trading partners. Now, geopolitical tensions between China, Russia, and the West are adding further uncertainty to the mix. Investors are understandably spooked.

The question is, of course, what investors should do in a situation like this. It's easy to panic when markets go into freefall—especially for private investors who may be watching their life-savings shrink. However, history shows that the best way for investors to deal with economic turmoil is often to ignore it.

Ongoing uncertainty is slowing global economic growth
Businesses all over the world are facing higher shipping costs and longer wait times. As economies began to recover from the pandemic in 2021, the growing demand for energy resources strained supply chains, resulting in an energy crisis that has further raised shipping and production costs. Now, a political rift between Russia, a major fuel exporter, and Europe has raised fears of even higher energy prices on the continent. While most of these events may be happening far away, the impacts on global markets are felt by investors everywhere.

What's causing the supply chain crisis?
The supply chain crisis is an ongoing result of COVID. Both the virus itself and the measures that governments took to prevent its spread massively disrupted the global economy. This resulted in shortages of raw materials, labour, and energy, which slowed down production all over the world while also raising production costs.

As the first major lockdowns came, Logistics companies found themselves without anything to ship. They laid off workers and scrapped equipment to save money in 2020, only to find themselves short of both in 2021. Today, production levels remain low in many economies that continue to pursue strict COVID measures that keep workers out of factories. There aren't enough goods being produced to meet demand, and what is being produced faces longer shipping times at higher prices than before the pandemic. So, what should an investor do in this kind of situation?

How volatility has impacted investors
Right now you may be seeing a fall in the value of your investments. KiwiSaver, managed funds and shares have all dipped in the last few weeks. When markets become volatile, it's

easy to let our emotions dictate the decisions we make. For many investors, when markets fall, the sense of fear creates an urgency to act. We start to panic thinking there's no way markets can recover. In reality, drops like this have happened before, only to recover in time.

Miscalculations have already hurt KiwiSaver investors
We saw this happen at the start of the pandemic in 2020. Trustees Executors performs back-office administration for 25% of all KiwiSaver money. During the market volatility of March 2020, we saw many investors make the decision to transfer out of growth funds and into conservative funds as the share market fell, to the potential detriment of their future savings.

Where in a typical month we might process 1,000 fund switches, for the month of March 2020 this increased almost 10-fold and at its busiest day processed over 1,500 switches. Of these switches, over 89% were investors switching out of riskier profiles to more conservative ones. As a result, they suffered more from the market crash (when they invested in riskier growth funds), and then benefited less from the recovery (because the conservative investments were less affected by both the crash and the recovery).

Managing fear is key
For some, the thought of losing everything will inevitably cause them to make one of the worst decisions they could. They sell and crystallise losses, only to buy back in when markets have recovered. Essentially selling low and buying high—the opposite of the cliche "buy low, sell high". This is incredibly dangerous because it turns a temporary downturn into a permanent loss. To avoid this, investors need to remain calm and most often do the hardest thing of all—nothing.

Keep your focus on the big picture
Despite day-to-day changes, the long-term market trend is upward. Even a serious economic crisis can only bring markets into disarray temporarily. Once a crisis is resolved, markets tend to recover relatively quickly, returning to their previous growth trajectory. Investment funds are designed to take advantage of this greater upward trend to provide long term growth and financial security, and history shows that they do so very effectively.

Consider your objectives
When emotions run high, it's important to remember why you're invested. If your objective or your circumstances have not changed, your investment strategy shouldn't either. To those still considering the switch, think about the following; are my objectives the same, are my circumstances the same, and with regards to KiwiSaver, does my current fund type (be it growth or conservative) help me to achieve my objectives? If you answered yes to all of these questions, then stay the course.

So what's next for 2022?
As we enter 2022, we expect inflation will continue to be a dominant force and markets now expect central banks to raise interest rates. In line with this, the US Federal Reserve has

indicated it expects to end its asset purchase program by mid-March and is likely to raise interest rates progressively this year to counter inflationary pressures. Similarly, the European Central Bank (ECB) indicated that it would ‘take any measures’ to get back to its 2% inflation target. In December the Bank of England raised its rates, albeit modestly.

The other major issue for 2022 will be the impact of the highly infectious Omicron Covid-19 variant. This variant has been causing significant absenteeism in workplaces overseas, in turn prolonging already significant disruption to supply chains.

Some health authorities are hopeful this variant could improve immunity levels against subsequent variants. The view currently suggests Omicron is delaying rather than derailing the global economic reopening. Some countries, such as the UK, even ended their COVID restrictions during the Omicron wave. As this plays out, we believe global diversification will continue to be rewarded. As ever, if invested for the long-term it remains important for investors to stay the course.

We’re here to help

Our goal at Trustees Executors is to protect our clients’ financial security and to help you realise your financial goals. That includes helping you get through difficult economic times and making sure that your investments recover along with the economy as a whole.

If you’re feeling anxious about market volatility, talking with a financial adviser can offer you some perspective and support. As always, it’s important to check in and ensure that your current investment strategy is right for you and serves your objectives.