KEEN ON
RETIREMENT

Market Volatility is Back: Time to Panic or Just Normal?

Welcome to Keen on Retirement
With Bill Keen and Steve Sanduski

Steve Sanduski:	Hey everybody. We are back for another episode of Keen On Retirement. I'm your co-host Steve Sanduski and with me as always is Bill Keen and Matt Wilson. Gentlemen, how are you today?
Bill Keen:	We're doing good Steve down here in Kansas City. You know the groundhog saw a shadow a couple weeks ago so I guess six more weeks of cold weather here in our area.
Steve Sanduski:	I think that's what they say and I'm looking out the window up here in the Milwaukee area and it is a gray cold day.
Bill Keen:	You know, every time I complain about the weather down in Kansas City I always think of you, it makes me feel better.
Steve Sanduski:	Appreciate that, Bill.
Bill Keen:	Yeah, yeah. Well I had some other data too that just came in that states that the groundhog only has a 39% accuracy rate.
Steve Sanduski:	You don't use that for investment strategy ideas?
Bill Keen:	Well, we have not yet.
Steve Sanduski:	Maybe as a contrarian indicator, how's that?
Bill Keen:	Yeah, exactly, exactly. Hey, Matt and I wanted to give you a hard time Steve. We still are convinced that you're a big buyer of Bitcoin and we saw that when we put our podcast out, what was it three or four episodes ago, I think we called

the, well, we didn't mean to but I think that was about the top, wasn't it? Wasn't it at 17,000 back then and hit six here just a month or so later.

Steve Sanduski: Yeah, recently it was at six. I think as we're having this conversation today it's probably closer to 8000. So yeah, it's been cut in about half which just goes to show that all this crazy investment products out there, there are some products that are good standard investments that have stood the test of time and then there's other stuff that you really shouldn't be touching with a 10 foot pole.

Matt Wilson: Yeah. That's a good point Steve because with this market volatility there's been some investment vehicles that have closed down because they can't operate in this type of volatility.

Steve Sanduski: Yeah, exactly. It's unfortunate that in our industry, one of the bad things about our business is that there are companies out there that create products essentially for what I think of the sole purpose of just trying to make money and the next thing about what you guys are doing there is you can see through that and you know the kinds of investment vehicles that are good for clients and the kind of things that are bad for people. And so obviously you guys are really focused on the stuff that has again, stood the test of time and it's just unfortunate there is that kind of junk out there and I personally know people that have been hurt significantly from these investment products. People that should have known better unfortunately and it's just sad.

Matt Wilson: Some of those things, those products, they do a tribute to some of the volatility and I wouldn't be surprised if we start to see some regulations soon to be passed about coming up with these products. They try to track volatility and they give you a way to invest in volatility. You kind of think, well, that doesn't sound, how do you invest in volatility and essentially they have these contracts that are on different sides of the market and when volatility picks up depending on what side of it you're on you can do well or lose a lot of money.

And there was one fund in particular, I just saw an article on Bloomberg, that it had 3.6 billion in assets and it basically just got wiped out just in the last couple of days. All of that just completely gone.

Bill Keen: Some somebody thinking that they could go in and have some derivatives security that they're able to leverage out against some fictitious, I don't even know what you would call that investment but I guess you don't call it anything at this point at least in that fund, do you?

Matt Wilson: And like Steve as you're saying, what's the purpose of this vehicle and really as you mentioned, the company that put it together I'm sure just, they saw some dollars to be made by selling a product to individuals and they've disclosed all the risks but of course that is not always representative of what the real risks really are and especially in this case where almost all of it's gone.

Steve Sanduski: Right. Well, and I'm sure you guys remember back about 20 years ago there was a hedge fund called Long Term Capital Management that had some of the "smartest people" that were part of it. I mean people like Nobel Prize winning economists that were part of their organization and they were investing in all kinds of esoteric investment products and of course that thing blew up and the Federal Reserve essentially had to kind of step in and they had to get a bailout and it almost tanked the markets back about 20 years ago.

So, we've seen this story before and it's just unfortunate that the same story keeps getting repeated time and time again and again it's another example, another reason why people really need to work with professionals who have a perspective, who have seen these stories happen before and are smart enough to just stay away from that stuff and just continue to work with the things that are tried and true and we don't have to get super fancy and sometimes just the simpler strategy is the better strategy.

Bill Keen: We believe in keeping things liquid, we believe in keeping things transparent, we believe in getting people in the right allocations upfront so that folks are set up to get through what what might happen if we have a downturn. Not if we have a downturn, we know there's going to be a downturn.

Up until a few weeks ago I think we had gone, how many days had we gone Matt without a three percent correction, was it like 450 days or something along those lines without even a three percent downturn from a high? Was that right?

Matt Wilson: Almost. It was like 448 days and that was the longest streak on record without a three percent correction. The previous longest streak was 370. Definitely had I think many participants in the market got kind of in lulled into this kind of false sense of stability. Us as professionals kind of know inherently that volatility will pick back up and even in our outlook piece that we put out here at the beginning of the year, that was one of the things that we said that we're going to probably see a back to normal situation in volatility for 2018. 2017 very little, 2018 expect to see not anything out of the norm but just back to the norm.

The volatility that we saw here in just the last few weeks isn't out of the ordinary. It's just we haven't had much and I think that did spook some people. actually there was, one of our research providers, they put out a note that said, there have been 144 four percent drops in the S&P 500.

Bill Keen: In a day, right?

Matt Wilson: Yeah, in a single day.

Bill Keen: In a single day, yeah.

Matt Wilson: So 144. You think about how long the S&P 500 has been around, that could be almost two a year. That's definitely more common than people think, it's just what was probably more rattling to individuals was the point to drop. So the Dow Jones on this recent pullback had the largest point drop ever. The points are less and less relevant as the index gets bigger because 1000 on the Dow when it's 10000 is a 10% move or when it's 20000 it's a 5% move. So we care about the percentage moves not about the point moves. But of course all the headlines were largest point drop in history and all that.

We will always have the largest point drop in history going forward, it's just kind of the nature of large numbers of how that works so.

We look at lot of the fundamental and economic backdrop with the economy and corporate America. When the volatility start picking up, the news that day, here's the news, the headlines were, the U.S. added 200,000 obs in the month of January.

Bill Keen: Okay.

Matt Wilson: Wages grew at the fastest pace since 2009.

Bill Keen: Okay, jobs up, wages up, okay.

Matt Wilson: The Atlanta Fed has this what they call GDPNow and it's a way for them to estimate where they expect the annual rate of G.D.P. to come in the coming quarter and they're at 5.4% on their GDPNow tracker.

Bill Keen: Annualized growth rate.

Matt Wilson: And that is the fastest pace since 2003.

Bill Keen: A recession is what we don't want and that's two negative quarters of G.D.P. and this report from one of the fed agencies is that we're going to be growing at 5.4. That might be a little high but anyway if that's the case, all right, so that's three points you've made, I'm still waiting for the negative points to correction.

Matt Wilson: The market went down that day. The fears are okay, inflation could potentially pick up because now wages are going up so interest rates should rise to reflect these inflation expectations and of course the Federal Reserve control short term interest rates and the potential for them to increase them maybe faster than what they're projecting is out there. So there's some issues with interest rates rising but rates are still historically low, they're just going to probably get back to a more normal level.

One of the things with the short-term interest rates, the Federal Reserve controls, we're still at a lower rate than where we were when Lehman went bankrupt back in 2008. And that was when the whole financial system was melting down.

Bill Keen: Right. So unprecedented low rates right now and inflation potentially picking up to some extent. But all these indicators still showing very positive economic growth. Finally in this what they call plow horse recovery from 08, 09, and that made some people anxious I guess. It gave it an excuse, didn't it, it gave the market an excuse to have a healthy correction.

Matt Wilson: Exactly. For us, all those things that we just mentioned, all those positive economic data, for us it's like, this is just a normal market event that we used to rebalance if it makes sense for certain situations and take advantage of it when it happens.

Bill Keen: So actually buy some securities within the parameters of the models that we're operating for folks.

Matt Wilson: Right, yeah.

Bill Keen: Right, right. So essentially, if we traded, if these markets, I hate even to say markets. I like to say the great companies of the U.S. and the world, if they just traded around a straight line, you would have to know how to time it right capture any profit from it. But if you go back to 1950 and look at where the market was as an example, in one 67-year-old person's lifetime the Dow was at about 200. It's up 120 times in one 67-year-old person's lifetime.

So it doesn't just trade around a straight line, it inherently goes higher as earnings go higher and this economy expands here in the U.S. and globally. So, to try and time the market proves to be a fool's game because you have to be right twice and typically it's almost impossible. I've never seen anybody do that. If they've done it it's been on accident.

I always ask, what is the purpose of the resources that we're investing for folks and in our case in almost all cases it's an asset that someone can live on for the rest of their lives. That means that their asset is a long-term investment still even if they're retired. They're going to need some money back this year to live on and next year and the third year and fourth year and fifth year out and that's why we keep that those moneys invested in something that won't fluctuate with the equity markets. But a good portion of even a retiree's asset is still 10-year money, 15 Year, 20 year, 25 years out invested.

And so my question always is what portion of this money is long term money still and what portion of it is this year's money and is our time horizon 10 minutes or is our time horizon a lifetime, the remainder of a lifetime. Granted, a retired person doesn't have 67 years still to invest but they very well may have 25 to 3 years to invest.

Matt Wilson: Yeah, and we talk about this a lot too because the markets are volatile, that is the price of the long-term return. Equities provide a significant return over the more stable assets like fixed income in cash and the cost of that return is the volatility and so it's always for us about putting it in perspective on these long-term numbers that Bill just mentioned but then also on bringing it back, expect to see some downturns on any given year. We can see those things happen and those aren't things to be scared. Of course, we don't to see it. I mean, it is unnerving when you see your account balances go down but it is part of the process.

I overheard Bill having a conversation with somebody recently too and he was talking about back when he first started, how often people got to see their account balances. Today it's instantaneously all day while the markets open, it's updating every second, people are checking their account balances.

Bill Keen: Right. I started about 26 years ago in the industry. Four times a year, quarterly statements would come out and around those four times a year people would see kind of how their investments were doing. I'll tell you, technology has been amazing, it's been wonderful, it's created so much growth and productivity for us, our economies here and globally. Long term investors being able to get on their computers, on their smartphones and hit refresh every 10 minutes to see where their account balances are, I'm telling you, it's not a healthy thing. It is not a healthy thing for people to be looking at their accounts every 10 minutes, every day, whatever it is and obsessing on, hey, when it's going up, people, I've just made another 10,000, I made another 30,000, I made a 60, and when it goes down it's oh.

Yes, does it seem like you're being a good steward because you're watching your asset every day. It could fool you into thinking that you're being responsible by watching your assets. Who could say, well, I'm just not going to look at it for quarter to quarter. Well, 26 years ago that's all that people really looked at. They could call in and ask but very few people did call in and ask their balances. They just got their quarterly statements. I do think what Matt mentioned is a detriment.

Most of our folks that we work with aren't looking at it daily. It's interesting we go through these times, people who have built their wealth long term themselves, who have had to save money and live within their means and they've been through these cycles, they have a way different perspective on how this has worked. They're retired, or they've built their wealth because of the capital markets. They've been saving money, they see the trends, they've been through things like 01, 02, 08, 09. They've stayed true to their program and they've recovered, they've been through it.

People who come into money either through inheritance or large sports contract or something of that nature who don't have any perspective tend to be the ones that panic. They want all the upside but they don't have any perspective at all about the downside and frankly probably shouldn't be in the market because they're not going to be able to understand it or comprehend it. Some can but I've just seen over time people who haven't built their wealth on their own over a lifetime have a difficult time understanding this. I think it's somewhat tragic, especially the young people that are starting these 401-k's who see their balance go down for two days and they want to stop their contributions. These are seven figure mistakes over a lifetime, Steve.

Steve Sanduski: They are, yeah. As you guys well know when the market's declining and this concept of dollar cost averaging, that if you are investing on a consistent basis like in a 401-k where you've got money coming out of your paycheck once or twice a month that is going into to make investments in your 401-k plan, as the market goes down, if you put your kind of fixed dollar amount in that means you can buy more shares. Of course that's no guarantee of profits but it's always better to buy lower and sell higher than it is to buy higher and sell lower.

Bill Keen: Truly there's two pieces to being successful in a long term financial plan and especially for people that are at or near retirement or in retirement, and that is the planning. The planning I believe that it's got to happen first. You have to have an objective for your capital and your resource. It's how much money can we spend when we do retire, when can we retire, what will the taxes look like, how will we structure our Medicare gap coverage or the policies that go along with that prescription drug coverage, when will we take Social Security, what insurances do we need, how do we have things titled if something were to happen to us, we mentioned it last podcast when we had Devin on talking about his Hawaii false missile attack experience. These are all planning issues.

The investments are simply an engine to the plan. And so, today we've started the podcast off talking about the investments because there's been some volatility and we thought it deserved some discussion, but I think we should kind of pivot here mid show and go over to some of the planning things that we're seeing that really are the kind of the longer-term things that could make a difference. So, I think we've got 2017 taxes right now needing to be prepared and then we've got the planning and thinking ahead about how 2018 and beyond can look as well.

What do you think? Are you guys with me on that or do we need to beat the market into the ground a little bit more?

Steve Sanduski: There is one more thing I want to say about the markets if I could and this ties back to what you were saying a little bit earlier, Matt, talking about this point decline and as you mentioned, the media is all over saying, well, this is the biggest decline in the market ever. Well, of course we all know it's the biggest point decline and you eloquently stated how as the averages continue to go up over time, the point decline becomes a smaller percentage. So, I have some numbers here that come from investors.com to put this in a little perspective.

The decline that we had in the Dow Jones Industrial Average on what was it about February 5th or so, the average declined by 1175 points which again is the worst one-day point decline but in terms of percentages it was the worst since August of 2011 but it was just the 25th worse since 1960. So even though it's the number one point decline, just since 1960, it's only the 25th worst percentage decline. And maybe even some more perspective, we go back to 1987 when the market dropped and that was the biggest percentage decline in October 19, 1887. But the point decline that day was 508 points. So it was less than half of today's yet that was the worst percentage decline by far in the Dow Jones Industrial Average.

These numbers get a little shaky and of course we know the media is all about trying to present things in the scariest fashion but when you really look at it, it's just par for the course.

Bill Keen: Right. And I would encourage our listeners to go back five or six episodes on the podcast and look at, we did a whole show on the 30 year anniversary of the 1987 crash and we talk about what happened during that time and what we came through and where we're at today. That would be a great episode to go back and listen to so maybe we can link to that in the show notes, Steve.

Steve Sanduski: Yeah, absolutely. Yeah, that was a great show.

Bill Keen: One more thing on the market. So, I wanted to move to planning and taxes but I think, I want to be respectful in saying that you might listen to what we're saying and as fiduciary advisors, people hire us to tell them the truth about their situation, they don't hire us to tell them what they necessarily want to hear. The people that work with us say no, we're hiring you as advisors to help us with this endeavor that we know, we're wired back to front, we're going to make an emotional decision, or an emotional mistake and we need help.

I don't want to come off as downplaying that when somebody clicks on their account and they see that it's down x percent or x number of dollars I'm not downplaying that as irrelevant. I understand that's emotional and I honor the fact that that's difficult. There's a fine line between us, I don't want to sound like I'm not understanding in the feelings. The point we're trying to make is that we're on this journey with people for a life time and helping them become successful over a lifetime of investing and meeting their objectives. We have to kind of bring the truth and the perspective into the situation and to help people get through those times which is what they've hired us to do in the first place.

And again, it does all come back to each person's risk tolerance and where they should be at any given time asset allocation wise so that they're comfortable. I would tell you that it's a calling for us to help people do what I believe most people cannot do on their own and that's navigate their investments truly long term.

Matt Wilson: We talk about it a lot. And the reason is because we know the data that tells us after the volatility starts to pick up, the percentage returns after that are much higher than they were before it. So people feel good when things aren't very volatile and then when volatility picks up we talk so much about the opportunities that arise during those volatile times. Yes, of course, we don't like seeing accounts go down and values go down but at the same time, we structure in such a way to be able to use those opportunistically.

History has told us that once the declines are over the markets will go back up again. I mean that's how it's always worked.

Bill Keen: It's how it's always worked every other time. What did we say, past performance not guaranteed future results but that's how it's worked every other time.

Matt Wilson: I just ran across some analysis here too and I've seen similar data in the past but this was just a recent article about dips in the stock market and so this was specific to four percent drops. What they looked at was over the past 30 years, following the next 12 months after a four percent drop, do you know what the average return is after that?

Bill Keen: Okay so, the 12th month period after a four percent drop in the markets.

Matt Wilson: That's right.

Bill Keen: Is it up 10 percent or so? I'm just guessing.

Matt Wilson: Average return the next 12 months is 25%. That's for all stocks. Of course isn't representative of a globally diversified portfolio but the point is, the rebounds are very significant. And so, after volatility picks up, that's not the time to be making adjustments to the portfolio where you're selling positions that are down. That's a one-month period. The following five years is a 14% average return. So, after the volatility picks up we see much better returns going forward.

Steve Sanduski: Yeah, I mean those are some great numbers to be sharing here Matt and Bill. One of the things I think it's also important to remind people and this is a simple concept and that is when the market declines you're looking at paper losses but those are just paper losses unless you sell. And then when you sell they become permanent losses. It's just important that, again, getting back to your point Bill about the emotional aspects of investing, none of us like to see a paper loss either but we don't want to compound that into a permanent loss by making an emotionally based decision at exactly the wrong time.

Bill Keen: There's two ways that can happen. One is you have money in these equity markets that you need back. So you needed the money back and you didn't have any choice, you had to sell it because you needed it back. The other way is to make that emotional decision that we talked about. So if we can help people plan around those two things, get them in a position where they're not going to panic because they're comfortable with their allocation and they understand why we're doing what we're doing and hopefully they do have perspective from their lifetime journey of investing and they've seen cycles.

And the two, any money that somebody is going to need back to either live on or have a big purchase or pay for a wedding or buy a car, you name it, it's not in the market. If they need that money back within, we typically at our firm we say five years. I know a lot of firms that say less than that but we like to have five years of someone's income needs outside of the equity markets so that it provides some insulation against having to sell at a bad time.

We talk about that all the time in our planning so that our clients and friends of the firm can understand those things so that they're pre-committed to the action they're going to take. And like Matt says again, using those things as opportunities so that you can get through those and say my goodness, wait a second, if we use those as opportunities and in the cases where we're able to rebalance portfolios where it makes sense and buy some things in the downturns within the parameters we've agreed on, you literally could look up and say I was better off that the market corrected than had it not corrected.

Now, that's hard to understand but if you've been through it over the course of a lifetime you get that and you look at those things as opportunities, not as something to run for the hills for. One last thing that I think is important, I've had several discussions lately, I would say if you're out there, if you're listening and you have an investment account or somebody is calling on you and they're telling you that they know how to, your advisor's telling you they know how to get out of the market at the highs and get back in close to the lows so that you can side step the volatility in the market, so that you can get the upside without the downside and they know how to time it right, I would turn and run away from those people as fast as possible.

I've never seen anyone that's been able to do that accurately so if someone ever has the thought that we do that. When I talk to people, I say, I want you to understand what we can do for you and I want you to understand really clearly what we cannot do for you. We do not purport to be able to know when the market is at a high so that we can sidestep it all.

Can we rebalance accounts and keep them within parameters? Absolutely. Do we know how to get it all out at the right time and then get back in at the bottom? No. We have to be very, very clear about that. And if that's what somebody is looking for we tell them that we're not the firm to execute on that strategy for them, very respectfully of course but that is something that I think it's important to table here today. And some of these annuity products we've talked about in prior episodes where they say you get all the upside with none of the downside totally plays into people's fears and produce a nice commission for the sales person as well.

Steve Sanduski: Well, Bill, there's a lot of wisdom in what you just said there so thank you for sharing that. One of the things I want to comment on what you just said there was, you talked about pre-committing to a course of action. And one of the great things that you guys do is you have a plan. You work with your clients, you put a plan together and you know what you're going to do when certain things may happen in the financial markets and I remember many years ago when I was playing baseball, what I would do before every pitch is I would ask myself okay, I'm playing in the infield. If the ball comes to me what am I going to do with it.

So before every pitch I always ask myself, when the ball comes to me what am I going to do with it. I pre-committed prior to the pitch this is exactly what I'm going to do if this ball comes to me so I didn't have to think in a split second, oh, the ball came to me, there's a runner on first and second, I'm I throwing it to third or am I trying to throw the guy out at first base. I knew what I was going to do so that's exactly what you guys are doing as financial adviser. So I think that's an important point to really get across here.

Bill Keen: Well, thank you. Thank you, that's a great example too.

Steve Sanduski: Well guys, I know we're getting ready to wrap up here and we had thought we'd talk a bit about the planning process and 2017 taxes, 2018 and what's going on there. Maybe we'll save that for the next episode.

Bill Keen: Okay. Steve, that sounds good. We'll still be right in the thick of tax season for 2017 taxes and we're still evaluating some of the strategies that folks can employ for 2018 and beyond with this new tax law. That tees up a real nice episode for next time. Sometimes these things take on a life of their own and I think it's important that we have that discussion.

Steve Sanduski: Absolutely. All right. Well hey, thanks guys. Great show, great information and we look forward to the next episode.

Bill Keen: All right, Steve, thank you.