Vanguard

Expert perspective

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Managing market volatility for your clients and your practice

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Introduction

Over the last few months, there has been a meaningful spike in market volatility as well as negative equity and bond returns. While this environment is challenging for investors—as well as advisors—there is a silver lining. These are the "moments that matter" for advisors. Your actions in the coming days, weeks, and months will have a material impact on your client and practice outcomes.

Your clients are undoubtedly experiencing the impact, and they may feel compelled to do something as a result, such as changing their asset allocations or even changing advisors. And that emotional reaction, while understandable, is likely the wrong step.

You are undoubtedly feeling the impact too. Volatility is up; markets are down; your revenue is most likely down; while your emails, texts, and calls are blowing up. Most of these requests for your time and your engagement will be challenging and difficult, as investors have experienced a start to the year with almost all asset classes in decline and high daily volatility. What seems to be missing in all the headlines is what to do about it.

The good news? Our research on Advisor's Alpha® and behavioral coaching has consistently shown that the value of an advisor is amplified in periods of high volatility and market distress. And while your job might not be as easy or as fun today as when the markets are in the green, this is your time to shine..

Tackle volatility in the markets and your practice with the same solution

One under-appreciated consequence when returns turn negative and volatility spikes are the risks to both your clients' outcomes and to your practice's outcomes. Because those two are one and the same, the solution is as well. Simply put, improving client outcomes is the key to better practice outcomes.

Given the breadth and depth of asset-class losses, this is likely true of your colleagues and competitors as well. As a result, assets and clients may be in the "danger zone," as shown below.

Danger zone

This has been the worst start to a calendar year for bonds, the third worst for equities, and taken together, the second worst for a balanced 60/40 portfolio (left side of table below). But a small part of this is a "trick of the calendar," and if you were to look at rolling four-month periods going back in time, you can see in the right side of the chart below, the 60/40 would not rank in the bottom 5 worst drawdowns, but as the 29th worst. This perspective is a prime example of why your investors need your engagement, communication, and proactive behavioral coaching now as much as ever.

Five worst 60/40 portfolio declines since 1928

YTD through April	Percentage decline	Rolling four months	Rolling four months
04/30/1932	-14.89%	06/30/1932	-28.05%
04/30/2022	-12.12%	12/31/1931	-25.79%
04/30/1939	-9.01%	05/31/1932	-25.61%
04/30/1973	-7.29%	11/30/1937	-20.51%
04/30/1941	-6.15%	12/31/1937	-19.64%

Past performance is no guarantee of future results. The performance of an index is not an exact representation of any particular investment, as you cannot invest directly in an index.

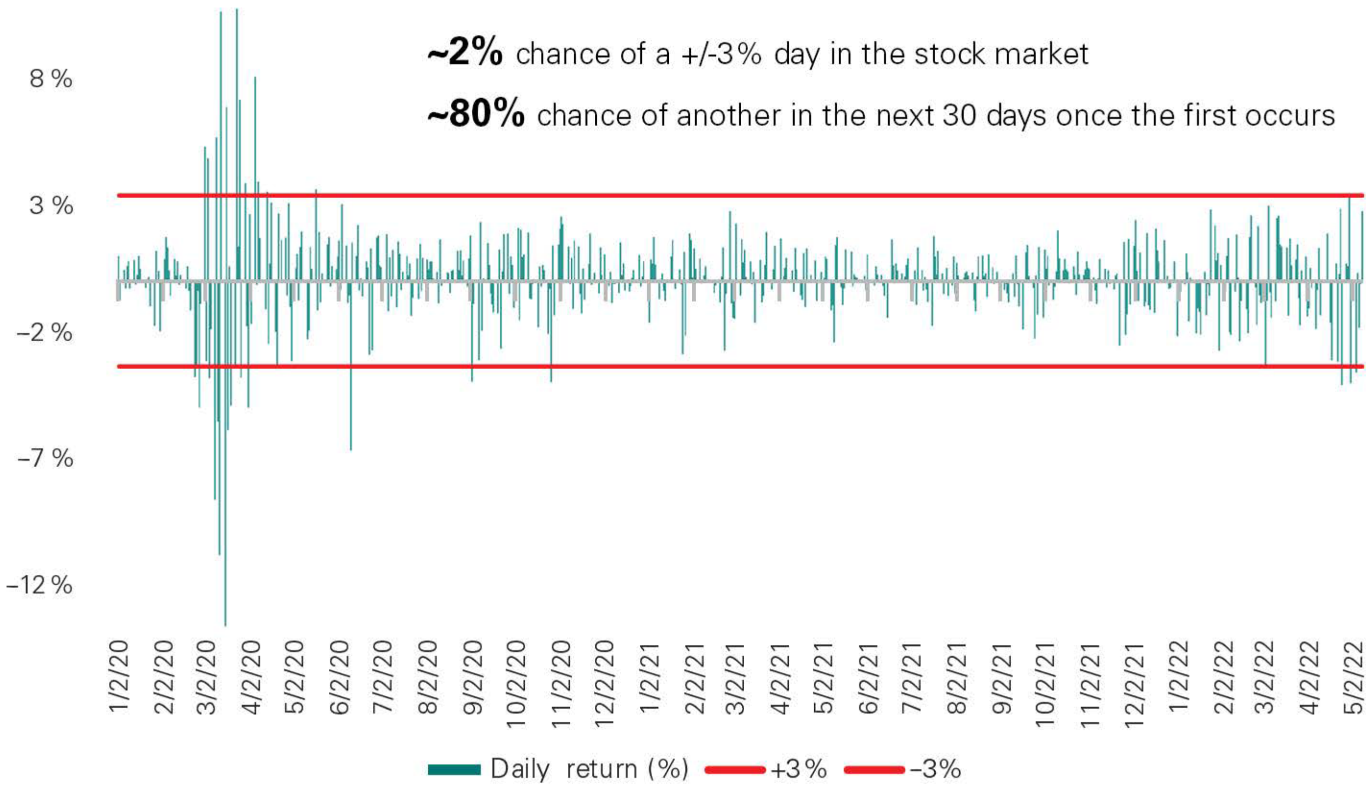
Notes: Stock allocation represented by the Dow Jones Wilshire 5000 Index through April 22, 2005; MSCI US Broad Market Index through June 2, 2013; CRSP US Total Market Index thereafter. Bond allocation represented by the Bloomberg US Aggregate Bond Index.

Sources: Vanguard calculations using data from FactSet. Data through April 30, 2022.

In addition to the drawdowns in the stock and bond markets, there has been a significant spike in daily volatility. It is critical to understand that predicting volatility spikes or declines, and the daily direction of the market within volatility regimes has not worked. However, volatility itself does have persistence and, as such, near-term future volatility is influenced by recent trailing volatility. Meaning that when the markets are in a high volatility regime, the expectation for high volatility to persist in the near term is high, with the best and worst days tending to cluster around each other. Eventually, and without a signal, volatility has been known to normalize. This can be seen in the chart below.

The best and worst trading days tend to happen together

S&P 500 Index daily price returns January 1, 2020, through May 13, 2022



Sources: Vanguard calculations using data from FactSet. Data through May 13, 2022. Data series for ~2% and ~80% statistics covers January 1, 1980, through May 13, 2022.

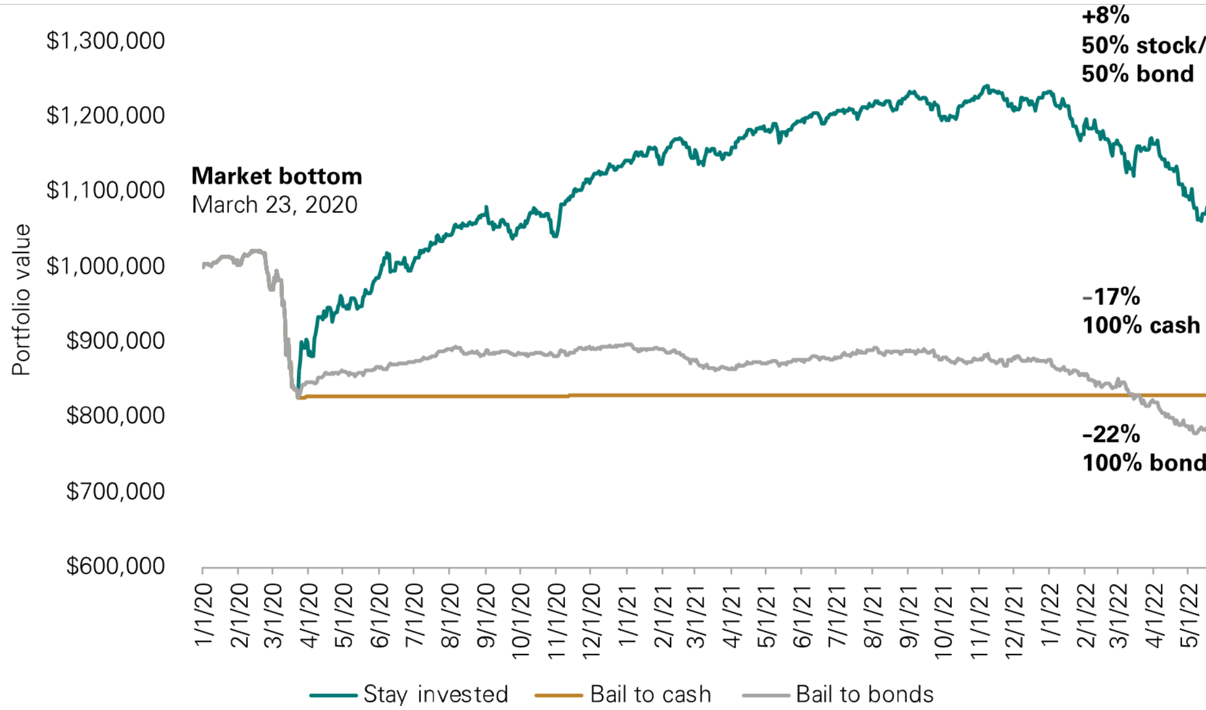
What to do? Given the declines in investor portfolios, and the expectation that volatility may continue for a while, this is an environment that is rife with opportunities to deepen your emotional connection and your relationships with your clients if you execute with care and take the time to communicate.

Bridge the communications gap

Focus not just on the markets but on proactively increasing your communications, accessibility, and empathy. It's obviously much harder to have conversations when markets are down and volatile versus up and calm. So, it's only natural that you may feel reluctant to call your clients in times like these. However, by doing so, you'll be in a better position with your client base.

Now is also a great time to step up your business development and prospecting efforts since your competitors may also be experiencing the dread of proactively reaching out in these down markets. A proactive conversation in which you convince a client to stay the course could justify many years of fees in terms of value added (see below). Look back to the most recent major market downturn from 2020. Even accounting for the current return environment, your clients would have been much better off (+8% versus –17%) by staying invested versus moving to cash, or a difference of approximately 25%, and are likely much more satisfied, loyal, and inclined to listen to you today as a result.

The COVID-19 crisis tells the stay-the-course tale



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Notes: Stock allocation consists of 60% U.S.-domiciled equites and 40% equities domiciled outside the United States. Bond allocation consists of 70% U.S.-domiciled fixed income securities and 30% fixed income securities domiciled outside the United States. U.S. stocks are represented by CRSP US Total Market Index. International stocks are represented by the FTSE Global All Cap ex US index. U.S. bonds are represented by the Bloomberg US Aggregate Float Adjusted Index. International bonds are represented by the Bloomberg Global Aggregate Float Adjusted Composite Index. Cash is represented by the FTSE 3-Month Treasury Bill Index.

Sources: Vanguard calculations using data from FactSet. Data through May 13, 2022.

Notes:

- All investing is subject to risk, including the possible loss of the money you invest.
- Diversification does not ensure a profit or protect against a loss. There is no guarantee that any particular asset allocation or mix of funds will meet your investment objectives or provide you with a given level of income.

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