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Keeping your portfolio on track through uncertainty

Veronica Willis: I'm Veronica Willis, Global Investment Strategist with the Wells Fargo Investment Institute. Joining me today on the trading floor is Darrell Cronk, Chief Investment Officer of Wealth & Investment Management at Wells Fargo.

To kick us off, Darrell, how can clients assess what is a normal versus abnormal market shift?

Darrell Cronk: Yeah, well, great to be here today, Veronica. So, it's an interesting question because I'm not sure there's always normal and abnormal market shifts. But I think when you talk about equity market volatility specifically, which is what a lot of people talk about when they talk about market volatility, there's really three kinds of corrections and pullbacks that we see.

The first is what we would call kind of a garden variety pullback, which is typically a 5 to 10% move in the market index from its peak to a lower level. Surprisingly enough, that happens on average about 2 to 3, maybe four times in a calendar year. So, it's very frequent and very normal.

The second one is a correction. A correction is probably a little more severe and a little deeper. Tends to run in excess of 10% from the peak to the downside. And somewhere between 10 and 20%. Again, not unusual for those to happen probably once every calendar year, as you think about it.

And then what's more infrequent are full bear markets, where the markets drop by 20% or more from the prior peak. Over the last 25 years, investors have experienced five bear markets. Historically, they've been anywhere from as short as 33 days out to as long as two years. And frankly, the last several bear markets have been very fast, very quick down, very quick back up. So, they're closer to that 33 days than they are the full 2 years, if you go back in history.

Veronica Willis: How should clients think about their portfolios when markets are changing every day?

Darrell Cronk: Yeah, it's a good question. And we get that question a lot, right? Investors often tend to overreact to risks that they find difficult to calibrate. So, when you think about things like geopolitical risk, even this year we've had, things like, the tariff and trade announcements, if you think back a little further, COVID was a good example of that. We've got geopolitical flashpoints that happen around the globe. Those geopolitical risks often are a source of market volatility.

I think the important thing for investors is you need to separate the signal from the noise, right. There's a lot of noise out there. And so, if you spend a lot of time focused on the headlines of the day, it often can lead you to emotional and perhaps even bad portfolio decisions. So, you've got to sit back and say, what is the source of volatility?

There's an old saying by a famous investor called Sir John Templeton, they always say this time is different. And history teaches you over and over again, actually, it's not different. Or maybe what's different is the source of market volatility is different. But the market's reaction to that volatility is not materially different.

Veronica Willis: So, thinking of tolerance for risk, how can investors or how should investors be evaluating or thinking about their appetite for risk during times of volatility and uncertainty?

Darrell Cronk: When an unforeseen event happens, like geopolitical surprises, economic uncertainty, policy uncertainty and markets react suddenly, it's a great time for investors to create a mental checklist, right? Has my time horizon changed for my goals? Has my investment objective changed? Has my appetite for risk changed? All of those can help you when you think about your long-term goals. Things like retirement, things like kids college planning, right? Most of those don't fundamentally change just because markets, you know, from this week or this month become more volatile versus less volatile.

If some event brings uncertainty to future fundamentals, earnings, typically wise investors step back and ask, are the fundamentals still in place for what I'm trying to accomplish? And if they are, then generally speaking, it's good not to overreact and do something that you'll later regret in the portfolio.

Veronica Willis: And just to wrap us up, how should investors use volatility to their advantage and create opportunities?

Darrell Cronk: Yeah, I love that question. And frankly I get it often. So, when other investors are panicking, right? And doing things emotionally and selling, you have to remember this is the reason you built a diversified portfolio, right? And that kind of an all-weather portfolio that allows you to sleep at night, right? And so that not all your investments move in unison or what we call correlate with each other in down markets.

It's really important when you experience 10% pullbacks or 10 to 20% pullbacks or even bear markets over time, smart investors will use volatility to their advantage, right? They will understand it's a normal part of economic cycles and market regimes. And as things go on sale, the stock market's one of those few things that when it actually goes on sale, people tend to move away from it instead of run towards it, right? Everything else that we know and experience in our lives when it goes on sale, people tend to run towards the sale and want to buy more. It's not intuitive and not the case for the stock market.

And so, I think, again, that professional advice, that objective advice can really help you remind ourselves that we plan for these moments. You stay disciplined when you have a well-constructed portfolio, that is diversified and can be the key to strong investment performance over time and actually hitting your goals.

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