WESTBOURNE
INVESTMENT ADVISORS

"Volatility is far from synonymous with risk. In fact, it is often the friend of the investor who is patient, disciplined, and long-term focused." – Warren Buffett, 2014 Berkshire Hathaway letter

Navigating Volatility: A Guide for Long-Term Investors

Volatility is front-and-center, driven by rising tariffs impacting imports from global trading partners, sparking fears of a trade war. Markets are on edge, with the S&P 500 swinging daily by 1% to 5% in response to escalating tensions. At the same time, proposed cuts to U.S. federal spending and EU subsidies are fueling concerns about economic growth, causing wild fluctuations in bond yields and stock prices. While we're confident that over the long-term, trading partners and companies will work through or around all this chaos through a combination of negotiation and economic dynamism, in the meantime, it feels like the stock market is caught in a storm. Though admittedly uncomfortable, volatility is a natural part of investing. Let's explore how to use this panic and sell-off to our advantage.

Understanding Volatility: A Long-Term Investor's Perspective

As long-term investors, our focus is on building and preserving wealth over time, not reacting to short-term market swings. Volatility refers to price fluctuations in investments, especially stocks, over short periods. These movements are part of the market's natural cycle. A 5% drop in a stock or a 10% dip in the S&P 500 is volatility in action. While the S&P 500 has averaged annual returns of around 10% since 1926, the path is never smooth, with yearly swings of 20% or more quite common.

Volatility and risk may feel the same, but they are not the same. Risk represents the permanent loss of capital, such as the erosion of purchasing power due to inflation or selling a stock for $80 after purchasing it at $100. Volatility, by contrast, measures the market's fluctuations, rational or otherwise, occurring over time. These shifts are temporary and not a cause for alarm for those who understand their regularity. As Warren Buffett observed, "Volatility does not define risk. Risk arises from a lack of understanding of one's actions."

Why Volatility Matters

Volatility tests our resolve as investors, an emotional challenge that tests our ability to separate short-term setbacks from long-term success. Behavioral studies show that when markets drop, fear drives many investors to sell, often locking in losses. Research indicates that investors typically underperform the market by 3-5% annually due to fear-driven behavior - volatility exposes the gap between what we *should* do (stay invested) and what we naturally *want to do* (flee/sell).

It's also important because it's essential to long-term growth and compounding. Stocks have historically outperformed inflation and bonds, averaging 6-7% *real* returns (above inflation) over decades, precisely because of their volatility. Smooth, low-risk investments like bonds or cash limit potential gains. Volatility offers opportunities for those with a long-term perspective. As financial advisor Nick Murray describes it: "v*olatility is nothing but tiny moments of opportunities for anyone focused on the long term.*"

Why Volatility *Doesn't* Matter.

If your investment horizon is long enough, volatility is irrelevant. Over any 15-year period since 1926, the S&P 500 has never posted a loss, even amidst significant crashes like 1929, 1987, 2008, and 2020. Dramatic dips in the short-term are insignificant over longer periods. Wealth is built through compounding over decades, not daily market fluctuations. Focusing on short-term volatility - what behavioral scientists call "narrow framing" - leads to unnecessary anxiety. Checking your portfolio daily can feel like a rollercoaster ride, while checking yearly typically reveals steady growth.

Our investment strategy accounts for volatility. We build balanced portfolios with diversification and a fixed-income buffer for near-term needs, so we're not forced to sell during downturns in the market and may rightly ignore daily market fluctuations. As Peter Lynch reminds us, "*the key to making money in stocks is not to get scared out of them*."

Managing Volatility: Staying Calm and Focused

A critical factor of navigating volatility is managing behavior. Trust the process - stocks grow as businesses grow, and history supports this. Since 1950, the S&P 500 has increased 100-fold, adjusted for inflation. Lean on us, your advisor, to help filter out the noise. Research shows that a steady hand can help curb impulsive decisions. When markets dip, we'll remind you that this is normal, we've planned for it, and staying invested is the best course of action.

Consider 2008: The S&P 500 fell 37%, but a $10,000 investment, if held and reinvested, grew to over $40,000 by 2023. Selling at the bottom would have eliminated those gains. Staying calm—often with guidance from an advisor—turns volatility from a threat to an opportunity. Nick Murray resonates again, "No panic, no sell. No sell, no lose."

The Path Forward

Volatility is not something to fear - it's an inherent part of the market's growth process. It's a test of investor resolve, not a threat to long-term wealth. As your *fiduciary*, we're here to help you stay grounded, manage risk, and protect your financial future.

Don't hesitate to contact us with questions or visit our Annapolis office.

Stay the Course,

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