Separating Emotion from Action: Taking Advantage of the Selloff

MARCH 2020

The global stock markets have been highly volatile. With a backdrop of a continued price war on oil and uncertainty about the economic impact of the global spread of the coronavirus, stocks fell into bear market territory the week of March 9. They have since fallen further.

We recognize that all this is highly unnerving and even frightening for clients. We further acknowledge that the full economic and medical effects of the virus outbreak are unknowns. We share your and your clients' concerns about loved ones and our broader communities as we grapple with this health emergency. However, what we do know is that panicked investing is never a good strategy.

Part of Litman Gregory's investment discipline is to use our long-term orientation to clients' advantage by looking out beyond the near-term fear to rationally assess fundamentals and valuations. One of our core strategies is to take advantage of market dislocations. When there is a highly compelling case, we are prepared to act by adding back to risk assets like stocks when they are cheap and unloved. This is one of the hardest actions to take as an investor—to "be greedy when others are fearful." But by acting with informed conviction, we believe we can add long-term value to client portfolios.

As you may know, we have been conservatively positioned with lower allocations to U.S. stocks and higher allocations to fixed-income and diversifying alternative strategies. In recent weeks we've seen the benefits of these latter holdings, as they've held up compared to stock markets, or even appreciated.

Following the more than 20% selloff in U.S. stock markets, however, our five-year forward-looking return estimates improved. We took advantage of the decline to modestly increase the exposure to U.S. stocks in our balanced portfolios by 2% to 4%, depending on the portfolio. We believe this shift improves the long-term return potential of the portfolios without meaningfully impacting their risk profile. After these trades, we remain moderately underweight to U.S. stocks.

As valuation-based investors, we view large price declines as opportunities to add back to stocks at attractive prices. If the selloff continues—and clearly it could—while it may be uncomfortable, we will be assessing whether it makes sense to further increase our portfolio allocations to stocks (by another similar increment), which we believe can pay off handsomely for investors who stick to their discipline through volatile market environments.

Again, we understand that significant market volatility—in this case combined with a scary real-world health threat—naturally elicits questions and emotions. Our team is here and available to talk through any questions or concerns you have.

Best regards,

The Litman Gregory Investment Team

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