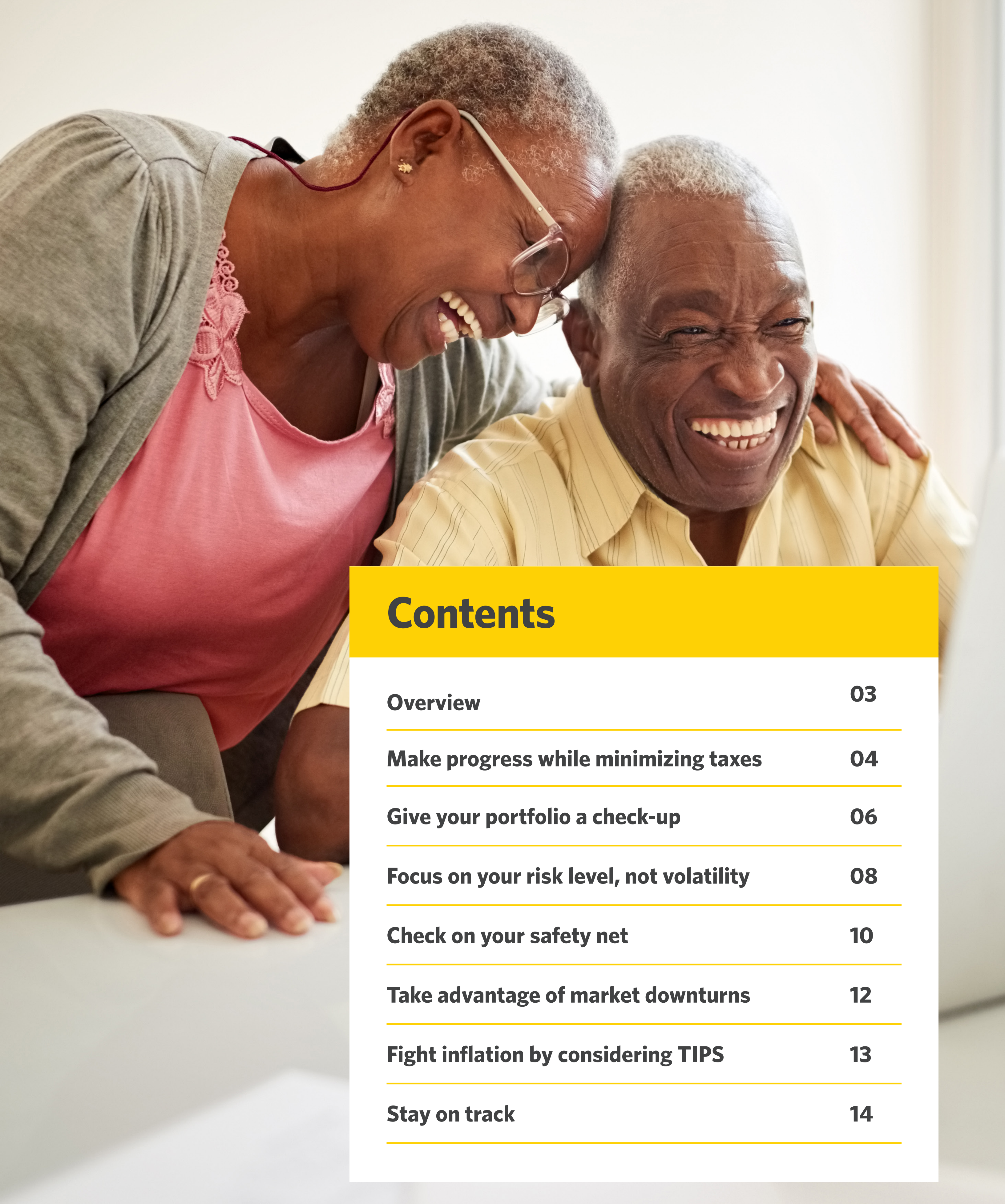
7 Actionable Strategies for Navigating Market Uncertainty

Edward Jones



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Overview

In an uncertain market, like the one we're currently experiencing, only one thing is certain, and that is market volatility. But the lesson here, as always, is to focus on what you can control. And the fact is, two of the most important variables are under your control—how you respond to market volatility and how you invest your money.

Here are seven practical strategies you and your financial advisor can use to help navigate market turbulence, keep your financial strategy on track and achieve your long-term objectives.

Your performance is your own

It's tempting to compare your portfolio's performance to a broad index such as the S&P 500. However, while indexes can provide insight into the general performance of stocks and bonds, they usually are not a relevant comparison to your own personal performance because:

1. A market index is not based on your goals or your comfort with risk.
2. Indexes are generally not diversified across different types of investments, but instead usually focus on a certain asset class, such as large company stocks or international stocks.
3. Your performance will be affected by your contributions and withdrawals, while the published market returns are not.

1.

Make progress while minimizing taxes

It's not what you earn but what you keep. The general principle: Help minimize taxes by holding tax efficient investments in taxable accounts and less tax efficient investments in tax-advantaged accounts.

Maximize retirement plan contributions, including your 401(k)

Be sure to max out contributions to your employer-sponsored retirement plan or IRA, including any catch-up provisions if you're 50 or older. These pre-tax contributions can reduce your taxable income and your earnings will grow tax deferred or tax free if you are using a Roth IRA.

Consider a health savings account (HSA)

An HSA is designed to work with a qualifying high-deductible health plan. Your money goes in tax free, grows tax free and comes out tax free when you use it for qualified medical expenses. You can carry over unused funds from year to year, and the account is yours to keep even if you change jobs, change health care plans or retire.

Seek tax-efficient mutual funds and exchange-traded funds (ETFs)

You don't have to buy and sell a lot of mutual funds to generate taxable gains, because the fund managers themselves can make trades often, and these trades can produce capital gains whose tax liability will generally be passed on to you. Also, some mutual funds pay out a lot of taxable dividends. So, a fund that does relatively little trading or pays fewer dividends could be considered tax efficient. The same is true for index funds and ETFs, which have less turnover than mutual funds and capital gains are only taxed with the ETF is sold by the investor.

Look at municipal bonds*

The interest from municipal bonds is generally exempt from federal income tax, and often from state and local income taxes, too. However, the income from some municipal bonds may be subject to the alternative minimum tax. Generally speaking, the higher your tax bracket, the more you may benefit from municipal bonds as opposed to taxable corporate bonds.

Harvest losing investments

If you have losing investments in your taxable accounts, you can sell them at a loss to help reduce your tax bill and potentially better position your portfolio going forward. Called tax-loss harvesting, this strategy may allow you to sell investments in which you have a loss, and then offset realized investment gains with those losses.

How a financial advisor can help

While minimizing taxes is important, tax savings should not undermine your investing goals. A financial advisor can help create a balanced strategy for you and reevaluate your investments periodically for tax efficiency.

* Before investing in bonds, you should understand the risks involved, including credit risk and market risk. Bond investments are also subject to interest rate risk such that when interest rates rise, the prices of bonds can decrease, and the investor can lose principal value if the investment is sold prior to maturity.

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2.

Give your portfolio a check-up

Market fluctuations can cause your portfolio to drift from your intended investment mix, leaving you over-allocated to some areas and underexposed to others. Any time is a good time to check if your portfolio is still aligned with your goals, time horizon, financial situation and comfort with risk.

Start by evaluating your investment mix and holdings

Reconsider your mix of stocks, bonds and cash. Check to see if you're diversified within each of these asset classes.

For stocks, look at:

- Size (Different-sized companies tend to lead the market at different times.)
- Style (Is it growth stock or value stock, and how does that fit your investment strategy?)
- Sector (What part of the economy does it represent? Consider different industries such as health care, real estate, energy, technology, etc.)
- Geography (This includes domestic, international and emerging markets.)

For bonds, look at:

- Sector (Options include government, corporate and municipal bonds.)
- Maturity (Bonds of different maturities provide diverse levels of yield and interest rate risk.)
- Credit quality (Bonds of different qualities may perform differently as the business and credit cycles evolve.)

Then check your individual holdings. This will help you decide whether an investment remains a good candidate for your portfolio. With stocks, you'll want to check a company's fundamentals (metrics such as earnings and sales numbers, as well as stock valuation measurements like price-to-earnings ratio) and analysts' opinions.

When it comes to bonds, be sure to review credit ratings (bonds can be upgraded or downgraded, which can affect your portfolio's risk level) and duration (a measurement of the bond's price sensitivity to interest rate changes).

Fine-tune your portfolio by rebalancing

Rebalancing is the act of adjusting your investment mix to restore your asset allocation to target levels defined by your investment strategy. Your investment strategy should consider your risk level, time horizon and long-term objectives. There are a number of ways to rebalance, including:

- If your allocation to any asset class has drifted away from your target, you may want to get it back into balance.
- If you make regular contributions to your portfolio, you may want to adjust future investments into asset classes currently underrepresented in your portfolio.
- You may want to sell some of the investments that are exceeding your target and use the proceeds to get back on track.

How a financial advisor can help

No doubt giving your portfolio a check-up is a good idea. But it can be time-consuming to do it yourself. A financial advisor has the skills to evaluate your investment mix and can stress test different scenarios to rebalance your portfolio and help you feel confident about your financial future.

3.

Focus on your risk level, not volatility

"Risk" and "volatility" are often confused because they're often used interchangeably when talking about investments. But they are different. "Volatility" usually refers to price fluctuations—up or down—in a stock, portfolio, or market segment during a short period. "Risk" refers to uncertainty and is much broader than volatility. Risk and volatility are normal when it comes to investing, and some risk can actually serve a valuable purpose. If you can't accept some risk, you may not have the potential to achieve higher returns.

Keeping a cool head

What typically prevents most investors from reaching their goals is not market volatility itself, but their reaction to this volatility. Investing based on emotions can often lead to disappointment. This is where risk comes into play. Understanding your comfort level with risk can make you a more self-aware and confident investor, and help you avoid some of these pitfalls. By knowing your risk tolerance in advance, you can better control your emotions and stick to your long-term strategy during the inevitable market corrections along the way.

Determining your own risk level

Generally, your risk level is assessed along three dimensions:

Risk tolerance

This is your willingness or comfort level with taking risk. Gauging your risk tolerance and your potential behavior when faced with risk is important because it's unlikely you'll reach your long-term goals if you abandon your strategy during inevitable short-term market declines.

Risk capacity

Risk capacity is your ability to handle investment risk. Unlike risk tolerance, which might not change over the course of your life, risk capacity is more flexible and changes depending on your personal and financial goals — and your timeline for achieving them.

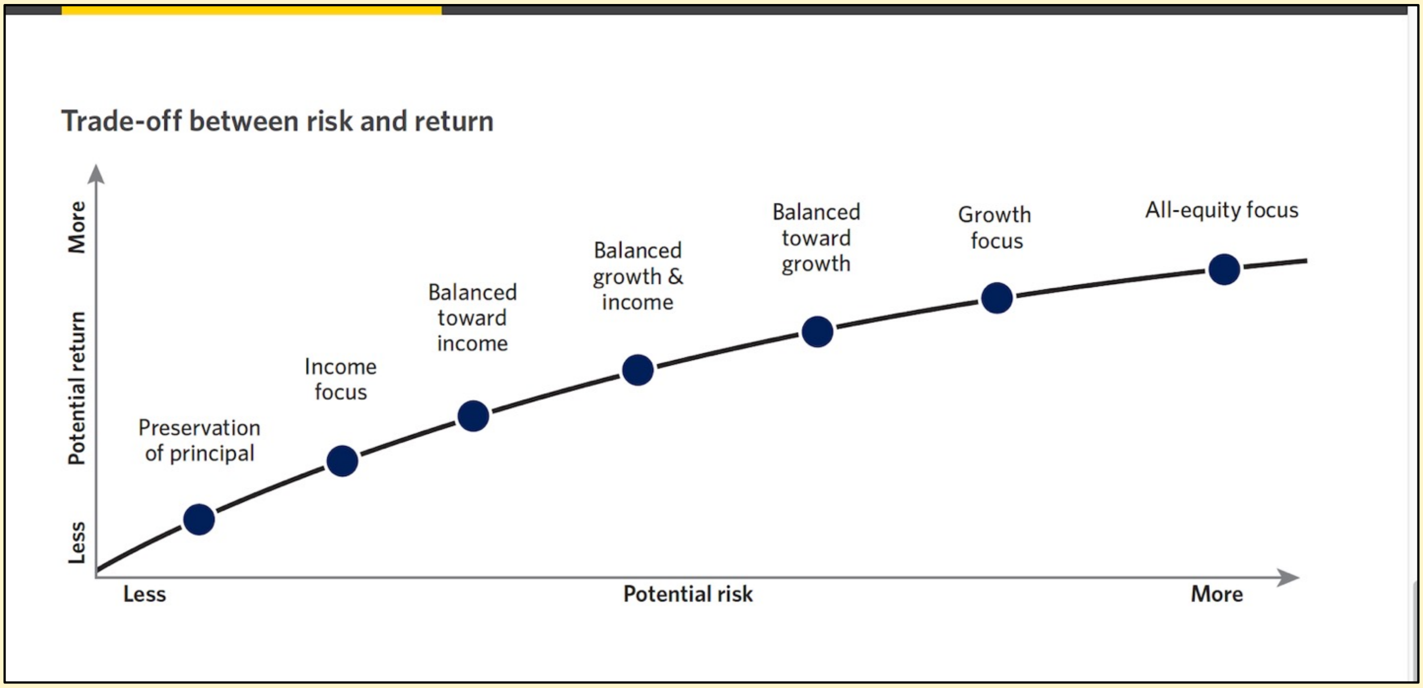
Required risk

This is the level of risk required to achieve your investment goals. Generally, the higher the return you need to reach your goals, the more potential risk you'll need to accept to achieve them.

Early retirement vs. risk: The balancing act

Suppose you want to retire at age 55 and you have a low risk tolerance. However, your financial advisor estimates that to accomplish this goal, you will need a higher return, resulting in a higher degree of portfolio volatility. In this case, you may have several choices, including working longer, saving more, reevaluating your goal or accepting a higher degree of volatility. However, it's important to ensure you're not taking on unnecessary risk. While this is a personal decision, by better understanding your goals, and the risks associated with achieving them, you can make a more informed decision.

This chart depicts the trade-offs between investment risk and return, using x- and y-axes, plotting risk from low to high on the x-axis and rate of return from low to high on the y-axis. The portfolio starts at Preservation of principal for low risk and low rate of return. Moving along, the potential risk to the portfolio increases as the focus on the potential rate of return increases, from an Income focus, to Balanced toward income, to Balanced growth and income, to Balanced toward growth, to Growth focus, and finally, to a portfolio with an All-equity focus – which represents a portfolio with the highest potential risk and return.



Source: "Understanding Risk" Edward Jones Strategy Report RES-5483O-A

How a financial advisor can help

While investing poses risks, not investing can also be a risk to your financial future. A financial advisor can help you build a portfolio that balances your risk tolerance, capacity for risk and the risk you're required to take with your financial goals so you can stay invested, no matter the market conditions.

4.

Check on your safety net

Another way to feel secure despite today's market uncertainty is knowing you have a good safety net in the form of emergency cash reserves.

Grow your safety net

If you're a salaried employee, you should keep three to six months' worth of living expenses in highly liquid accounts such as savings or money markets. Also, you'll probably need to increase your total amount to account for inflation, which has been running at some of its highest rates in decades.

What happens when your cash runs out?

It's a good idea to think through where you can go for funds if your cash accounts are depleted and you still need more funds.

Consider long-term assets in taxable accounts.
These assets will be taxed at the lowest rates.

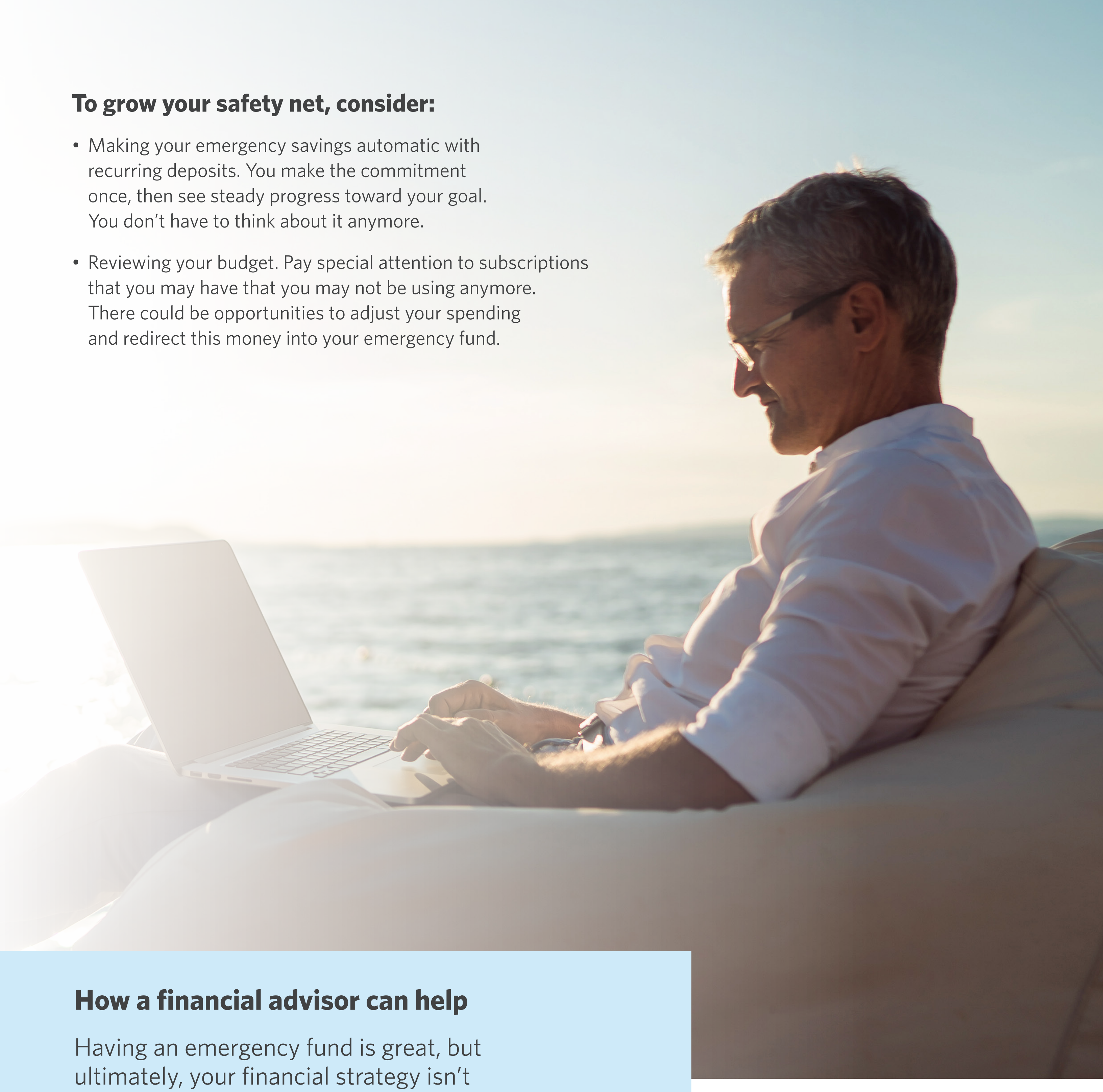
Own a home? Look into a home equity line of credit.
Rates on home equity lines of credit are still low relative to historical norms, and your interest may be tax-deductible, depending on your individual circumstances.

Turn to fixed income.
Look to the more stable and defensive parts of your portfolio. This means withdrawing money from bonds and bond funds, which tend to hold up better and have smaller price swings than stocks do during volatile market stretches.

Don't raid your 401(k) plan.
There are plenty of reasons NOT to do this, including the fact you may be subject to 10% early withdrawal tax penalties if you're not 59 1/2 or older, and you may also need to pay income tax on the amount you withdraw.

To grow your safety net, consider:

- Making your emergency savings automatic with recurring deposits. You make the commitment once, then see steady progress toward your goal. You don't have to think about it anymore.
- Reviewing your budget. Pay special attention to subscriptions that you may have that you may not be using anymore. There could be opportunities to adjust your spending and redirect this money into your emergency fund.



How a financial advisor can help

Having an emergency fund is great, but ultimately, your financial strategy isn't complete without a plan to protect it. A financial advisor can help you think through difficult topics, including how to provide for your family's future if you're no longer able and how to pass on the legacy you intend.

5.

Take advantage of market downturns

Volatile markets aren't all doom and gloom. They can present buying opportunities for investors with a long-term horizon and money to invest. But mustering the discipline to make purchases during a volatile market can be difficult—even when purchasing solid investments with strong fundamentals. Systematic investing, in the form of dollar-cost averaging, can help reduce your anxiety about the investment process—and help you stay invested in the market.

What is dollar cost averaging?

With dollar cost averaging, you steadily build your portfolio by investing a fixed dollar amount at regular intervals. By investing on a set schedule, you develop discipline that can help you be a better long-term investor. Plus, investing systematically lets you buy more shares when the price is low and fewer when the price is high. Think of it this way: It helps "average out" your share price over time.

Of course, as with all suggestions mentioned in this guide, dollar cost averaging does not guarantee a profit or eliminate risk, nor does it protect against loss in a declining market.

How a financial advisor can help

Working with a financial advisor can provide a disciplined process for your financial strategy. A financial advisor can also evolve your plan as you prioritize new goals or manage life events, and help you up seize opportunities as markets change.

6.

Fight inflation by considering TIPS

If you're concerned the rate of inflation will grow and eat away at your purchasing power, consider having some of your fixed income in the form of Treasury Inflation-Protected Securities, or TIPS.

What are TIPs and how do they work?

Like traditional Treasury bonds, Treasury Inflation-Protected Securities are backed by the full faith and credit of the U.S. government (meaning there is no credit risk involved). But, as their name implies, TIPS also offer inflation protection. While the interest rate on these securities is fixed, the par value (or face value) increases with the Consumer Price Index. So, if the rate of inflation hits 5% annually, for example, your investment grows right along with it, Remember, though, if you buy a TIPS at a premium and we enter a period of deflation, future inflation adjustments could be negative.*

How a financial advisor can help

Selecting the appropriate asset allocation—which might include TIPS—is an individual decision. A financial advisor can help you find the right balance so you can feel secure and on track to reach your financial goals.

* Yield-to-maturity cannot be predetermined because of uncertain future inflation adjustments. If TIPS are sold prior to maturity, you may receive less than your initial investment amount. If bonds are not held in a tax-advantaged account, investors will be required to pay federal taxes on the accredited value annually, although they will not receive any principal payment until maturity. When the inflation rate is high and the principal value is rising significantly, the taxes paid on TIPS may exceed interest income received. Therefore, TIPS may not be suitable for investors who depend on their investments for living expenses.

7.

Talk with us to see if your plan is on track

It's only natural to wonder if the market volatility we're experiencing is going to derail the better future you see for yourself and your family. The best way to get your arms around where you stand today, and plan for what's ahead, is to talk with a financial advisor who works with you to understand your personal goals and priorities, along with your financial picture, to help you plan holistically.

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