Market Volatility
Facts & figures

Many investors have concerns about volatility when it comes to investing – particularly about the impact on their superannuation and other investments.
It is important to understand the causes of market movements and how to minimise your risk.

Why do markets move so much?

Markets are influenced by many things – industrial, economic, political and social factors can all have an impact. Markets rise when people are confident, and they fall in times of fear. It's the normal cycle of "fear and greed", and these cycles tend to see markets overshoot on the upside and the downside.

Consumer and business confidence affect spending and therefore company profits. Global trade and production naturally affect economic growth. Poor political and fiscal decisions in some countries may lead to a flow–on effect in other countries who are owed money. And of course, natural disasters can cause major damage to any economy with no warning.

During times of market volatility, it's important to remember one of the fundamental principles of investing – markets move in cycles. Global share markets experienced considerable volatility as a result of the global financial crisis, but overall, there have been strong returns over the 10–year period.

Current economic outlook

Uncertainty around the potential effects of war in Ukraine, supply issues, rising inflation and increasing interest rates saw equity and bond markets tumbling in the first half of 2022, with significant ups and downs each day.

Asia–Pacific markets were not immune to this downturn.

As worrisome as the rapid fall in equity prices can be, it's important to understand that changes due to the global financial crisis saw the underlying structures of the global financial system strengthened.

The global financial crisis was exacerbated by compromised underlying factors within the financial system that required a structural realignment of markets. Such a dynamic isn't as much of a concern now, it is more about uncertainty of things like company profits, and the specter of recession due to slowing consumer confidence and, therefore, spending.

This fear of the unknown has caused people to sell investments, but the problem is where else can we invest to get a decent return and some capital growth, particularly with property values also beginning to fall?

ASX IMAGE ABOVE COURTESY OF ABC NEWS.

What is the effect of market movements on investment returns?

The table below shows the effect of market volatility on different asset classes for one, five, ten and 20 year periods. We can see that over 20 years returns across all asset classes are positive.

Asset class returns as at 30 June 2022

ANNUAL PERFORMANCE	1 YEAR	5 YEARS	10 YEARS	20 YEARS
Australian shares	-7.4	7.2	9.4	8.2
International shares	-6.5	10.1	14.1	6.2
Australian Listed Property Securities	-12.3	4.4	9.2	5.4
Australian Bonds	-10.5	0.9	2.6	4.7
Cash	0.1	0.9	1.7	3.6

What is the effect of market volatility on super funds?

In times of market volatility your super balance may decline, but it is important to remember that markets move in cycles. Volatility is a natural part of the economic cycle. Markets are influenced by a range of factors and are inherently unpredictable. History demonstrates that over the long term, share markets trend upward.

It is also important to remember that although the unit prices within super may have declined the number of units you hold remains the same and as your employer continues to contribute to your super.

SOURCE: 2023 Vanguard Index Chart

TIPS FOR REVIEWING YOUR INVESTMENTS

Understanding your time horizon

It's important to know what your time horizon is when it comes to how you should invest your money. For instance, if you know you need to make a purchase in the next 12 months then you would consider investments that are less likely to be impacted by movements in financial markets. If you have a longer time horizon, consider investments such as superannuation which are aimed for retirement. You can also consider investments that have greater growth potentially to make your money work harder for you over a longer period.

Don't put all your eggs in one basket

Diversification is one of the most effective ways of managing volatility. It can help deliver smoother, more consistent returns over time. Your investment may benefit by being spread across a variety of asset classes, including shares (domestic and global), fixed income, cash, direct and listed property, and alternatives. This diversification should help soften the effects of any share market falls as some asset classes often tend to do well whilst others are struggling. Also, spreading your assets around means you are less reliant on any one asset class at any particular time.

If you hold geared investments this means the investment manager uses the assets held within the unit trust as security for borrowing, which means you are increasing your market exposure.

The main risk is that by increasing the amount you have invested you both magnify losses when markets are going down and magnify returns when markets are doing well.

Understand your risk profile

All investments carry some risk. How much risk you're willing to accept will be influenced by your financial situation, family considerations, time horizon and even your personality. If market volatility has caused you to reassess the way you feel about risk, it's important that you see your financial adviser to discuss any necessary changes to your financial plan.

Don't lose sight of the bigger picture, superannuation is a long–term investment. Shares, which usually form a large part of most people's super accounts, are a long–term investment. They are designed to provide capital growth over a period of more than five years.

Staying the course:

As ever, we hold to our Principles for Investing Success. Discipline, especially, is essential in times such as these.

Investors who abandon their long–term financial plans rather than staying the course through a recovery could cause themselves lasting harm.

Investors mostly have experienced gains for the last decade; it's important to remember that equity markets are filled with ups and downs but have rewarded investors over the long–term.

When share markets fall in value, it may be tempting to sell up, but history would show us that the smarter move is to invest more when prices are lower.

By taking a long–term view of investing, you can ride out any short–term fluctuations in the market and take advantage of growth opportunities over the long term.

Understanding the implications of withdrawing

Before you withdraw from an investment you should understand all the implications, risks and costs involved.

- Crystallising losses. If the value of your investment is falling, you are technically only making a loss on paper. A rise in prices could soon return your investment to profit without you doing anything. Selling your investment makes any losses real and irreversible.
- Incurring capital gains tax (CGT). Make sure you know what your CGT position will be before selling any asset.
- Losing the benefits of compounding. If you're thinking about making a partial withdrawal from an investment, remember that it's not just the withdrawal you lose, but all future earnings and interest on that amount.

KEY TAKEAWAYS

Keep in mind that:

- Super is a long–term investment designed to generate sufficient money so you can enjoy your retirement.
- Diversification is an important part of a long–term super investment strategy.
  To create the lifestyle you want in retirement, it may be necessary to invest in growth assets like shares so that your returns stay ahead of tax and inflation.
- It may be beneficial to ride out the bad times in order to achieve long term growth.
- It's important to stay focused on your long–term goals
- If you are unsure contact APRA's Workplace Advice Consultant:

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