



## Living With Volatility

The current renewed volatility in financial markets is reviving unwelcome feelings among many investors—feelings of anxiety, fear, and a sense of powerlessness. These are completely natural responses. Acting on those emotions, though, can end up doing us more harm than good.

At base, the increase in market volatility is an expression of uncertainty. The sovereign debt strains in the U.S. and Europe, together with renewed worries over financial institutions and fears of another recession, are leading market participants to apply a higher discount to risky assets. It is all reminiscent of the events of 2008, when the collapse of Lehman Brothers and the sub-prime mortgage crisis triggered a global market correction. This time, however, the focus of concern has turned from private-sector to public-sector balance sheets.

As for what happens next, no one knows for sure. That is the nature of risk. But there are a few points individual investors can keep in mind to make living with this volatility more bearable.

- ❖ Markets are unpredictable and do not always react the way the experts predict they will. The recent downgrade by Standard & Poor's of the U.S. government's credit rating, following protracted and painful negotiations on extending its debt ceiling, actually led to a strengthening in Treasury bonds.
- ❖ Quitting the equity market at a time like this is like running away from a sale. While prices have been discounted to reflect higher risk, that's another way of saying expected returns are higher. And while the media headlines proclaim that "investors are dumping stocks," remember someone is buying them. Those people are often the long-term investors.
- ❖ Market recoveries can come just as quickly and just as violently as the prior correction. For instance, in March 2009—when market sentiment was last this bad—the S&P 500 turned and put in seven consecutive months of gains totaling almost 80 percent. This is not to predict that a similarly vertically shaped recovery is in the cards this time, but it is a reminder of the dangers for long-term investors of turning paper losses into real ones and paying for the risk without waiting around for the recovery.
- ❖ Never forget the power of diversification. While equity markets have had a rocky time in 2011, fixed income markets have flourished—making the overall losses to balanced fund investors a little more bearable. Although proper diversification does not always ensure a profit or protect against loss in a declining market, diversification can spread risk and lessen the bumps in the road.
- ❖ Markets and economies are different things. The world economy is forever changing, and new forces are replacing old ones. For example, the IMF noted in its April 2011 World Economic Outlook that while advanced economies seek to repair public and financial balance sheets, emerging market economies are thriving. A globally diversified portfolio takes account of these shifts.

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❖ Nothing lasts forever. Just as smart investors temper their enthusiasm in booms, they keep a reserve of optimism during busts. And just as loading up on risk when prices are high can leave you exposed to a correction, dumping risk altogether when prices are low means you can miss the turn when it comes. As always in life, moderation is a good policy.

The market volatility is worrisome, no doubt. The feelings being generated are completely understandable. But through discipline, diversification, and understanding how markets work, the ride can be made bearable. At some point, value will re-emerge, risk appetites will re-awaken, and for those who acknowledged their emotions without acting on them, relief will replace anxiety.

Source: Dimensional; Adapted from "Living with Volatility" by Jim Parker

## For More Information

For more information on the services offered by M Wealth, please contact:

JoNell Hermanson  
503.414.7310  
jonell.hermanson@mfin.com

Erik Bjorvik  
503.414.7656  
erik.bjorvik@mfin.com

Andrew Brigham  
307.733.3759  
andrew.brigham@mfin.com

Luan Dollens  
503.414.7544  
luan.dollens@mfin.com

Michael Skourtes  
503.414.7572  
michael.skourtes@mfin.com

Bryce Stadick  
503.414.7598  
bryce.stadick@mfin.com

Amy Ellingson  
503.414.7698  
amy.ellingson@mfin.com

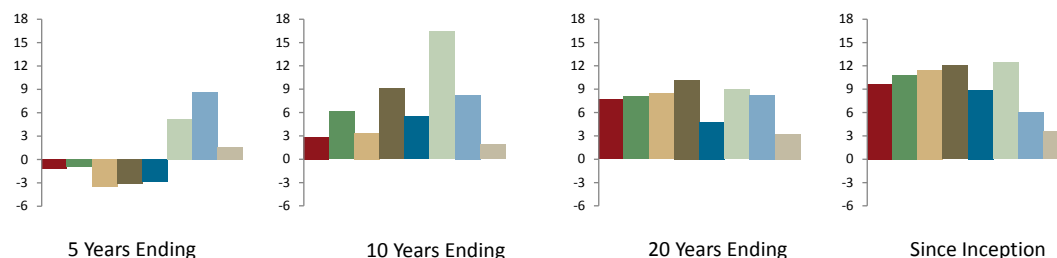
or visit the M Wealth website at:

[www.mfinwealth.com](http://www.mfinwealth.com)

M Financial Wealth Management  
1125 NW Couch Street, Suite 900  
Portland, OR 97209  
800.508.1820  
[www.mfinwealth.com](http://www.mfinwealth.com)

## Survey of Long-Term Performance

As of September 30, 2011



Index	5 Years Ending 9/30/2011	10 Years Ending 9/30/2011	20 Years Ending 9/30/2011	Since Inception (inception date)
<b>US Large Company Stocks</b>				
S&P 500 Index	-1.18	2.82	7.64	9.66 (1/1926)
<b>US Small Cap Stocks</b>				
Russell 2000 Index	-1.02	6.12	8.05	10.80 (1/1979)
<b>US Value Stocks</b>				
Russell 1000 Value Index	-3.53	3.35	8.48	11.48 (1/1979)
<b>US Real Estate Investment Trust Stocks</b>				
Dow Jones US Select REIT Index	-3.17	9.07	10.19	12.06 (1/1978)
<b>International Stocks</b>				
MSCI World ex USA Index	-2.90	5.50	4.78	8.92 (1/1970)
MSCI Emerging Markets Index (gross div.)	5.17	16.41	8.96	12.43 (1/1988)
<b>Bonds</b>				
S&BBI Long-Term Corporate Bonds	8.59	8.21	8.27	6.02 (1/1926)

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