It's Back

QAM Perspectives – March 2018

Quadrant's regular newsletter that highlights topics we believe will affect markets or are important in understanding them.

Volatility.

A topic that arises more frequently in periods of heightened levels of financial turbulence is the idea that markets are more volatile now than they used to be.

February's equity market corrections of nearly or slightly above 10% for U.S. equities (S&P 500 Index) and 8% for Canadian equities (S&P/TSX Index) has again made volatility front of mind for many investors. To many, the correction probably felt bigger than it really was, given that, from a capital markets perspective, 2017 was a year of unprecedented stability as part of an extended bull market. For all of 2017, there were only 8 trading days in which U.S. equity returns (S&P 500 Index) varied by more than +/-1% in a single day, adding to investors' complacency heading into 2018. In contrast, for the first 50 trading days of 2018, we have already seen the same equity returns vary by more than +/- 1% in a single day for 18 days.

"Volatility is basically a function of uncertainty."

John Bollinger, renowned analyst and author.

The return variation experienced so far in 2018 is actually more reflective of typical historical market fluctuations. However, it doesn't feel this way given the human tendency toward recency bias. It's like how the first 12 degree day in April feels much warmer than 12 degrees in October even though both temperatures are the same.

Despite how we may feel, volatility is not heightened this time around. The last equity market correction prior to this one was less than three years ago (third quarter of 2015), when U.S. and Canadian equity markets experienced declines in the range of 6.5% to 8.0% (local currency). In fact, since the end of World War II in 1945, there have been 27 corrections (defined as a decline of 10% or more) and 12 bear markets (defined as a loss of market value of over 20%).

Volatility affords opportunity. In looking back, most of the corrections did not become bear markets and most bear markets were not crashes. Each one of these historical instances turned out to be buying opportunities for long term investors. This can be seen plainly in long term equity market growth.

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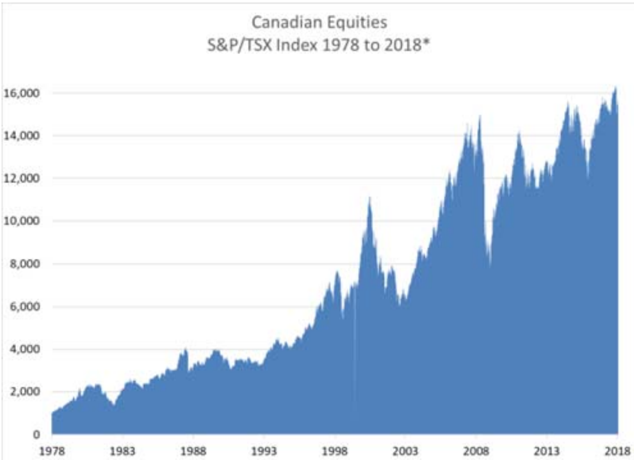

Over the past 20 years, equity market levels, while experiencing market corrections, have continued to increase over the long term.

Despite market corrections in February 2018, it should be noted that on a local currency year-to-date basis (as of March 21, 2018), returns have recovered to approximately -0.3% for U.S. equities (S&P 500 Index) and -4.1% for Canadian equities (S&P/TSX Index).

Our Thoughts

Rather than define risk as the fluctuation of returns over time (i.e. volatility), we prefer to think of investment risk as the probability of permanent loss of capital. But we are mindful that most people are anxious when volatility increases. Volatility (or uncertainty) is inherent in financial markets. As human beings, we have a natural aversion to uncertainty.

For Quadrant, successful investing means properly managing the risks and uncertainties associated with financial markets and creating investment portfolios utilizing time-tested, well-proven investment tenets that take into account each investor's specific circumstances and tolerance for risk (both financial and emotional).

Companies with strong balance sheets, competitive advantages, sound economics and reasonable valuations are inherently of higher quality and outperform the general market in more challenging times. At Quadrant we remain firm in our belief that inflation protected growth in the long-run comes from holding high quality stocks, while liquidity requirements and stability should be provided by a cautiously selected fixed income position in the portfolio. We don't ignore current market sentiment but instead are opportunistic in periods of extremes in market sentiment through a proven and diligent investment process.

If you or someone you know could benefit from our services, please have them contact our offices at 204-944-8124 or email us at inquiries@quadasset.com.