Survival Guide for Scary Financial Markets.

David Andrew

Foreword

Scary times happen! In the past 50 years we've seen the 1973/74 OPEC Oil Crisis, the '87 Stock Market Crash, two Gulf Wars, the GFC and Covid-19. It's inevitable there will be troubling events. Unfortunately, many troubling events occur with little warning or indication of how long they might last.

These events often see emotional investors panic. History repeatedly shows these investors are robbed of their wealth because of their inability to separate their emotions from investing. We don't want you to suffer the same fate!

My colleague, and friend, David Andrew, wrote this book to help investors remain calm, avoid reacting, and make wise choices during difficult times.

Follow David's thoughtful advice and you'll always navigate difficult investment markets successfully.

We hope you find his message both sensible and reassuring.

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Introduction

My motivation in writing this brief e-book is to share what I know to help you survive and thrive in scary financial markets. Having worked in markets for more than 30 years, I have seen some scary markets first-hand. Those experiences guide my thinking and perspective on decision-making.

It fascinates me that while some people are terrified when markets wobble, others remain calm and just take it in their stride.

Why is that? How can one investor calmly carry on, quietly confident that everything will be ok, while another feels deeply insecure and compelled to make decisions that could be ruinous?

There's no simple answer, but successful investors do leave subtle clues.

In this book, I have condensed as many of these clues as possible, into as few words as possible, to give you the best chance of success.

But like most things in life preparation is everything - the best possible crisis planning occurs *before* the crisis is upon you.

David Andrew
Author

This book draws on all the crises of the past to provide context for this one, (and for all the crises we are yet to experience).

These events will come and go, but markets endure and so do those investors who play by some time-tested rules.

As I write, we are in the midst of the Covid-19 pandemic, and we are all feeling a range of emotions and living new experiences each day. This event has been likened by our country's leaders to a war - a war on an unseen enemy - so I have woven a war theme into my storyline.

I hope you take something valuable from the message and find it comforting during tough times.

Introducing our Hero

At 3.10am on the morning of 4 July 1918, Australian and US troops, British tanks and planes, and Australian and French Artillery commenced one of the most important battles of WWI. While Gallipoli may be Australia's most famous battle, the battle for Le Hamel has taken its place in history as one of our most important victories.

Our hero is the Australian engineer and commander, Lieutenant General John Monash, whose meticulous planning and use of combined arms in a coordinated way completely outwitted the Germans, leading to an astonishing success.

The plan Monash prepared was different to anything attempted by Allied forces up to that point. Rather than relying on the usual tactics of the British generals, Monash tried something completely new by using every military resource available to him in a coordinated and imaginative way. He also ensured that every man in his command knew his role and responsibilities.

Nothing was left to chance.

Monash used RAF planes for aerial reconnaissance, and to drop ammunition and supplies to troops during the battle.

He used British Mark V tanks in a coordinated fashion to protect the advance of Australian and US infantry, while coordinated artillery attacks combined shrapnel, high explosives and smoke to target German troops and their ammunition dumps.

Never had such an ensemble of resources been placed under an Australian commander.

What happened next was remarkable. Over a two-kilometre stretch, the plan unfolded with orchestra-like precision.

So well planned was the attack, Monash had calculated that all Allied objectives would be accomplished in 90 minutes.

At dawn, as the smoke cleared, messengers reported back to the elegant Bertangles Chateau (the Australian command HQ) that all objectives had been met.

The entire battle plan had been won, not in 90 minutes as planned, but in 93.

So, what can we learn from Monash's meticulous planning and how might it inform the way we invest successfully?

Rule 1 - Understanding the Enemy (What are you up against?)

Monash's enemy was easily identified but not well understood. The Germans were feeling the stress of war, but so too were the Allies. Battle casualties, fatigue, the deadly Spanish flu and plummeting enlistment numbers all meant that manpower was sparse.

Monash needed a strategy that could maximise effect but use manpower sparingly.

This meant he needed to understand his enemy, their supply lines, the location of their ammunition stores, trenches and bunkers. To achieve this, he had the RAF fly hundreds of reconnaissance missions with photographers and created detailed maps of German positions, enabling the creation of an evidence-based plan.

Any gap in his understanding of the enemy was unacceptable - it created a potential weakness in his plan and exposed Monash's troops to greater risk.

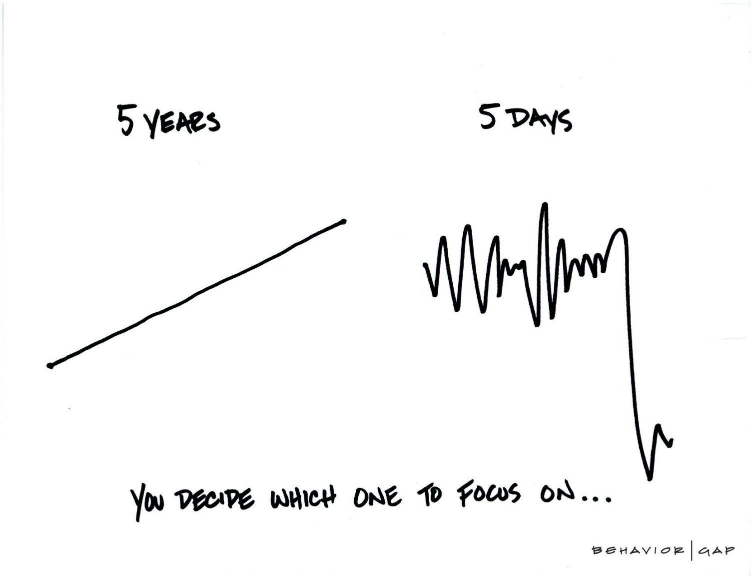
He knew he would have casualties, but it was his responsibility to minimise them.

In investing, the enemy is uncertainty. Investment success lies in understanding this uncertainty and having a plan to deal with it.

Over the past 90 years the US share market has provided an average annual return of about 10 per cent, as has the Australian share market.

During that long period, there have been very few years when the market provided that exact return - the yearly results were far more variable. In fact, over those 90 years, the S&P 500 index was either *up by more than 20 per cent, or down by more than 20 per cent* on 40 occasions. That's an extraordinary level of variability.

To be a long-term investor you need to understand and accept this uncertainty. Investors can only measure their returns in decades - not years, not months and certainly not days. **When markets go down you cannot afford to go down with them.**



Becoming fearful and depressed about the markets takes you further away from your objective and can lead to ruinous action.

There will be plenty of ‘experts’ on the news each night predicting what will happen next, but this noise just adds to the uncertainty.

Getting back to Monash, the most important element of his success was his absolute clarity about his final objective.

So too with investing. You must have an unshakeable resolve to stay the course - in good times and bad - to achieve the return you are entitled to as reward for the risks you have taken.

Anything less is an unacceptable outcome.

This commitment to your goals paves the way for you to create an effective investment battle plan.

Rule 2 - Have a Plan (Meticulous is Good)

Monash had a reputation for devising unusual tactics and for meticulous planning. This trait was a hangover from his training as a civil engineer. This enabled him to combine all the resources available to him in a formation that maximised the probability of success.

In formulating the battle plan for Le Hamel, Monash knew he needed to rethink his tactics given his constrained resources.

Leaving nothing to chance, he set about understanding every risk possible and creating a plan for it.

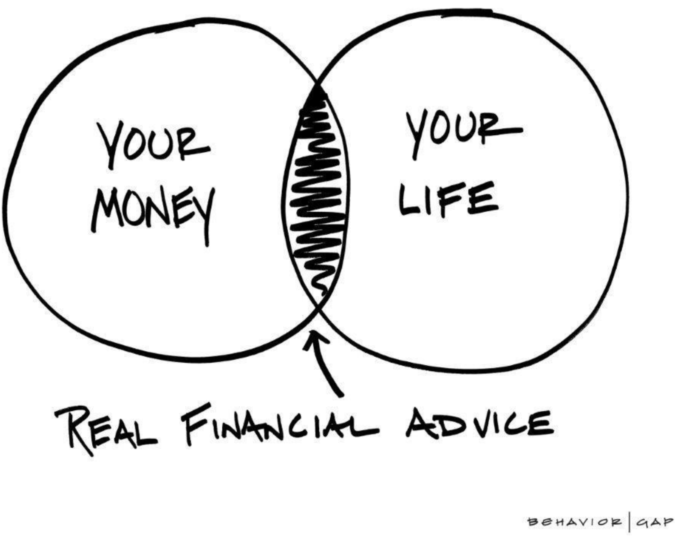
To maintain the element of surprise, he forbade all troop movements in daylight and used harassing fire and the noise of ageing aircraft to distract attention from tank and troop movements.

He considered different options, threats and contingencies, then settled on a battle plan. He knew in advance how he would react to certain risks, and this minimised the possibility of his commanders making panicked decisions in the heat of the battle.

In contrast to Monash's meticulous planning, most people spend more time planning their annual holiday than they spend mapping out their financial future.

But a detailed financial plan considers all the possible contingencies and that acknowledges scarce resources, enables an investor to come to terms with their risks and to have a ready response.

For example, a goal with inadequate savings to fund it needs to be reconsidered - the earlier the better.



Everything in life is a trade-off. Understanding this is a critical first step in achieving the financial milestones and goals that matter most.

Does the investor save more, work longer, take less income in retirement, wait for a home upgrade, take more investment risk?

These are all questions that should be considered before the investment plan is implemented.

Once the plan is in place, nobody invested in shares should be surprised when the market drops 10 per cent, or for that matter 20 or 25 percent. In fact, this has happened on so many occasions we know in advance it will happen again.

An investment in shares requires a long-term view.

It's how *you respond* to these events that determines the success of the plan - more on this in *Rule 5*.

Rule 3 - Use Every Resource You Have Available

Monash knew that he could not force the Germans back using a traditional brute-force attack of massed infantry supported by artillery bombardment. For a start, he simply didn’t have enough men, and he had been shocked by the general disregard for loss of life shown by other generals.

At a conference in Paris earlier in 1918, he had argued the case - against criticism from the establishment - for the use of new light-weight machine guns as an offensive weapon. He also pioneered the use of advancing tanks as protection for the infantry battalions who followed behind.

These two improvements changed the game as the enemy had little time to take their defensive positions. As the artillery bombardment lifted, the Allies were already upon the German trenches.

None of the resources Monash used could have won the battle in isolation. Not the infantry, nor the tanks nor the artillery, but *together* they had a chance.

Monash needed all the resources he had, working in a coordinated way, to give maximum effect to the battle plan.

In the world of investing, we call the use of the full breadth of resources, 'diversification'. The science and discipline of this strategy is one too few investors pay real attention to.

Very few people can achieve their goals simply by investing everything in a cash deposit - the returns are so low that the result would be a meagre lifestyle.

Similarly shares alone are too aggressive. Many investors consider a diversified portfolio to be one where they hold 20 different shares. Worse still is the speculator's portfolio - where the investor is in an endless search of the next big winning story.

It is precisely these portfolios that come under extreme stress during scary markets. And these are precisely the portfolios where recovery is more doubtful.

Using real diversification principles makes the investing journey so much safer and more enjoyable. Just as Monash could not eliminate the risks for his troops, the efforts he made to keep them safe paid off handsomely in the relatively low casualties.

Similarly, a portfolio can be structured so that while you may still feel anxious in scary times, you won't feel tempted to respond to your fear because you have confidence your portfolio is robust, and in return, confidence in a full recovery is well founded.

If you're retired and living off your portfolio, you'll need to ensure that you have enough cash set aside to fund at least one year of your income needs. Then you will need a store of high-quality fixed income investments to buffer the impact of a falling share market.

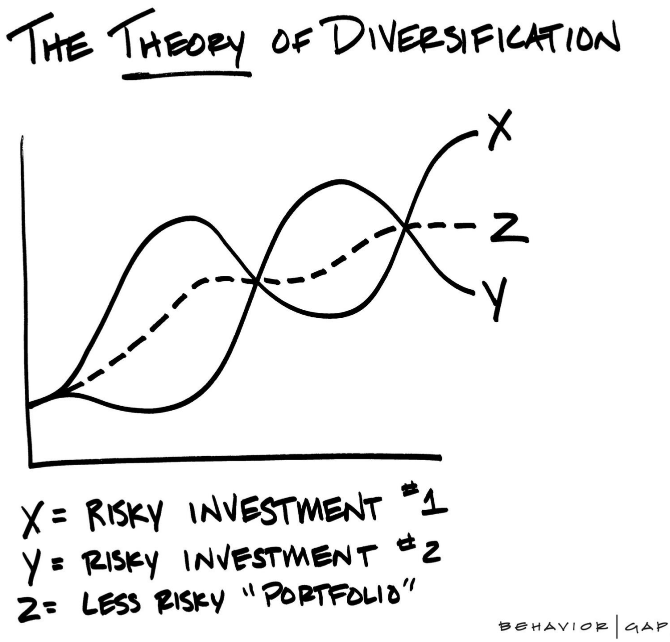
Ideally, you'll have enough defensive assets to fund at least six-years' worth of living expenses.

Only then should you consider your share market exposure.

Few investors realise that it is possible to have a portfolio of 300 stocks and achieve a similar, and often better return than the 20-stock portfolio you might choose on your own or with your broker.

Add to that the opportunity to gain a diversified exposure to international shares, value and smaller company stocks, and your portfolio is now looking robust, diversified and truly able to withstand a scary market.

True diversification isn't difficult, nor is it that common.



Rule 4 - Be Disciplined (but Flexible)

In the formulation of the battle plan, Monash considered hundreds, perhaps thousands, of contingencies, spending hours poring over the possibilities if something didn't go to plan. He spent hours considering the detail of each action and then took the time to brief his officers on the plan. Every person, no matter their seniority, knew their part.

Risk, it's said, is what's still left when you have considered every contigency.

Monash understood this better than most and did everything he could to reach his objective and keep his men safe.

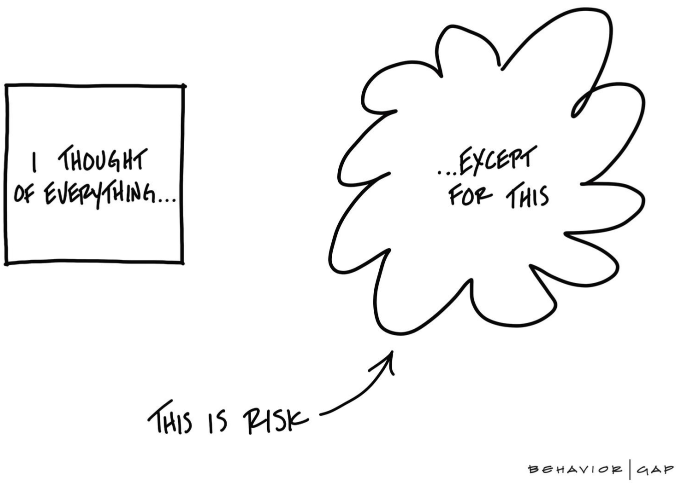
The risks he took were carefully considered and measured, but once the plan was set it was implemented with precision.

In investing, things go to plan most of the time, but every now and then events occur that rattle confidence - scary markets are an example. Having a real plan to reference back to is a great starting point. If the plan is off track, ask yourself why. What needs to happen to get you back on track?

Questions like these give rise to rational conversations. They may still make you feel uncomfortable, (they're scary times after all), but the conversation is measured and, importantly, referenced against a game plan. It is far easier to get back on track when you know your destination.

Time after time we see investors panic when markets fall. This inability to separate their emotions from their investment plan can result in staggering losses.

If there's no investment plan to begin with investors are left searching for the rule book on how to react.



Rule 5 - Focus on What You Can Control

A lesser know fact about the victory in Le Hamel was that behind the scenes there was a concerted effort underway to have Monash demoted.

A Jewish man of Prussian parents, Monash was a proud Australian, having been born in Melbourne in 1865. Others didn’t see it that way.

As Monash planned Le Hamel, the official war correspondent C.E.W. Bean and Sydney Sun correspondent Keith Murdoch (Rupert's Dad) were plotting his downfall.

As historian Roland Perry put it bluntly: “Bean didn’t like Monash because he was Jewish. Murdoch didn’t care if he was Jewish, gypsy or geranium, his motive was that he couldn’t manipulate him.”

Two days before the battle began, Bean and Monash arrived at command headquarters with the Australian Prime Minister Billy Hughes, who was unaware the battle was imminent. Bean and Murdoch had misled Hughes that Monash’s senior men were opposed to him.

Hughes was ready to demote Monash but after consulting with senior officers and seeing the superb planning in place, he couldn't find anyone with a bad word to say about him.

The battle went ahead with Monash in command.

Monash could well have been distracted by the political manoeuvring taking place, but he was clear on what he could control and stuck to his game plan. He knew that focusing on the things he could control was his best chance of success.

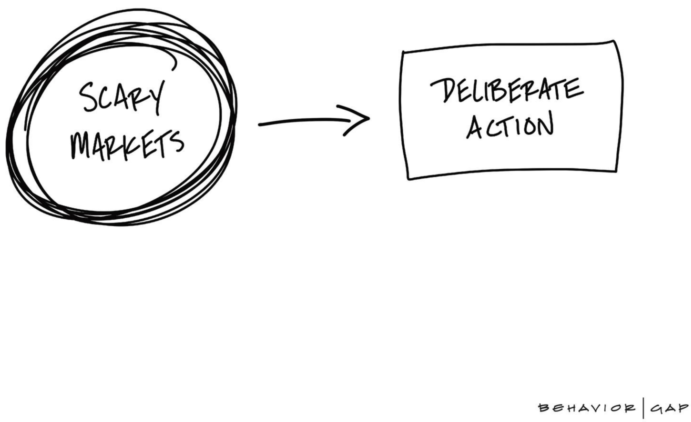
If I have convinced you that *Rule 1* is true, you now know that your mission is not to avoid scary markets, rather to deal with them in a way that serves you as an investor.

There will always be economic and market events capable of derailing your plan. When the inevitable crisis hits, the headlines will scream ***Panic! Meltdown! Billions Wiped Off Shares***!

At this point you will have a choice: *React to the news or remain resolute in your plan.*

When things get hot in investment markets it's sometimes hard not to be sucked into the feelings of uncertainty, loss and fear. But like Monash, you will know that the one thing you can control is your behaviour and your response.

When you have a plan - one built on evidence and one that is updated regularly and battle-ready, you stand a much better chance of achieving the investment outcomes you are looking for.



The markets won't change; they will continue to go up and down. Your investment experience will be shaped by whether you choose to let your emotions go up and down with them.

Epilogue

So complete was Monash's victory in Le Hamel the Germans were demoralised, and while they counter-attacked, their retreat to the Hindenburg Line and ultimate surrender began at Le Hamel. On 12 August 1918 at Chateau Bertangles, Monash was knighted as Knight Commander of the Order of Bath on the battlefield by King George V, the first time a British monarch had honoured a commander in such a way in 200 years.

Monash left us an enduring legacy through his intellect, his commitment to research and evidence-based principles and planning, his respect for the resources available to him, and his ability to execute a disciplined plan in full knowledge of the risks.

The five principles outlined in this book can serve all investors as well today as they served Monash in 1918.

As we deal with the uncertainties of achieving financial independence and freedom, scary times will come and go - intuitively we all know that.

The challenge for investors is to build a plan you can stick to. In time, the confidence you will gain from a real game plan will open the door to a much bigger future.

Afterword

For many people reading this little book the message will resonate, but it can be hard to know how to take the first step. While these principles seem logical, many investors aren't wired to think this way and so it can be daunting.

If after reading this book you would like a better investment experience, please visit www.fygplanners.com.au
for further information on evidence based investing and how to manage your wealth during Scary Times.

SIMPLE ≠ EASY

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