Embracing the Chaos of Global Markets

"Chaos was the law of nature; order was the dream of man." – Henry Adams

Life is chaotic. If you have ever managed a business, renovated a kitchen, or brought a three-year-old on a family trip, you know that most events do not turn out the way they were envisioned. No matter how much planning you do, no matter how many potential problems you forecast, life can throw you a curve ball. And those unforeseen events almost always have a significant impact on the outcome of your life's projects, for better or worse.

Living in the midst of such chaos is understandably frustrating. We all have an innate desire to make sense out of the chaotic world around us, to connect the dots, to link cause and effect; the reality is that it's not always possible. This seems to be especially true in the global financial markets. Although the long-term historically positive return on stocks, driven by the global power of capitalism, is very reliable, the short-term up and down movements that interrupt this gradual rise are no more consistently, or accurately, predictable than the annual hurricane forecasts in Florida.

The good news is that global markets will prevail in allowing all of us to take advantage of the long-term wealth generating power of capitalism. However, many investors have been disappointed in their investment results in the past. The capital markets are not to be blamed; the markets have always done their part over the long-term. Where investors go wrong is in failing to recognize, or accept, that randomness is everywhere. For most individuals, investment disappointment is the result of that innate human desire for control. Multitudes of investors are constantly analyzing corporate financial reports, investor surveys and stock charts in an effort to predict the near-term future movement of financial assets. Unfortunately, this course of action often ends unpleasantly, as unforeseen events leap out to confound an investor's well-formulated plans. If you look back on history, events like the fall of the Berlin Wall, 9-11, the powerful revival of Apple Computer and the Japanese nuclear disaster in 2011, were all unpredictable. Yet each of these events had a significant impact on the short-term movements of capital markets, and they each conspired to make some strategists look like fools (through no fault of their own,) and others look like geniuses (with no effort on their part.)

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So, how can you expect to have a successful investment experience when random events get in the way? There are a few simple steps you can take that will allow you to be a successful investor in spite of the chaos around you, and which will allow you to make sense out of that chaos (at least from an investment perspective.) First, remember that diversification is your friend. Random events do have unpredictable effects on financial assets, but a given event may have a positive impact on one asset at the same time it has a negative impact on another. For example, terrorism or military activity in the Middle East is usually bad news for stocks, but it typically results in higher prices for bonds, gold and oil. By investing globally and diversifying into many different types of stocks, bonds and commodities, you can minimize the impact that any single random event can have on your portfolio.

The world is a big place and with modern economies so intertwined, diversifying through global investing is an obvious necessity. Yet, what typically derails a well-constructed, globally diversified portfolio is an investor's own emotional reaction to the random chaos described above. Chaos makes one feel uneasy, and this unease can lead to emotional investment decisions, almost always at precisely the wrong time. Adopting a disciplined, rules based approach to investing, and a process that will ensure that the rules are consistently adhered to, despite the emotional ups and downs of the markets, is the best way to avoid that pitfall.

Random chaos is an inevitable fact of life. The truth is that chaos can no more be eliminated from the stock market than it can from a vacation with a three-year-old. The best approach is to accept this fact and adopt an investment process that not only acknowledges unpredictability, but embraces it through global diversification and discipline. As Yogi Berra famously said, "It's tough to make predictions, especially about the future." Your own investment odyssey will certainly have its ups and downs, but if you embrace the chaos, take the emotion out of the process, and allow global markets to work for you, you will be glad you made the trip.

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