It's never fun to switch on your TV or computer Monday morning only to see bad news about the markets. After all, Mondays are hard enough without having to worry about the markets, right?

But chances are that's exactly the kind of news you saw this past Monday. The media pumped out headline after headline, none of them pleasant. "Stock Markets Plunge." "Dow® Drops 1,000 Points." Turmoil, upheaval, volatility, fear … you probably saw all those words and more.

But what, exactly, do we have to fear?

In my opinion—nothing. Because as the great scientist Marie Curie once said, *"Nothing in life is to be feared. It is only to be understood."* (Trust a scientist to say something smart.) And she's exactly right! Of course, there are plenty of things in life to be concerned about … including what's going on in the markets. But instead of fearing the news, let's try instead to *understand* it.

So here's what happened.

Here's a two-sentence summary. When the U.S. markets opened Monday, investors started selling right from the word go. The Dow went so far as to drop over 1,000 points in only ten minutes.1

Now for a lengthier explanation. Imagine that your favorite amusement park announced a new ride called "The Drop." It takes you up slowly, higher and higher into the air, then drops suddenly. Now imagine that over the weekend, thousands of people start waiting at the gates for when the park opens on Monday morning. Everyone wants to be first on the ride. Monday morning comes, the bell sounds, the gates open, and all those people pour in at once, each and every one anxious to ride "The Drop" first.

It seems a little silly, doesn't it? All those people, pushing and shoving, just to get on a ride. Why not hold back for a little bit, wait for the commotion to die down, and *then* decide whether to ride or not? Wouldn't that make life so much simpler, so much less hectic? But that sort of phenomenon is common. In fact, we see it every Black Friday! People tend to make decisions based on pure emotion. Either they *want* something or they *fear* something, and thus, have to act *now*.

What happened with the markets is equally silly … and equally based on emotion. In this case, the primary emotion was fear.

Too many investors were afraid of remaining in the markets, so they jumped at the first chance to board a lifeboat—before even learning whether the ship was actually sinking. The result? The single largest point-loss ever during a trading day.1 By Monday's close, the markets actually recovered somewhat, but "The Drop" might not yet be over. In fact, we are now experiencing what experts call a **market correction**—a 10% drop from a recent peak.

So why did it happen?

Here's another two-sentence summary. Some investors are afraid of how China's ongoing economic problems, coupled with a continued drop in oil prices, will affect their investments. Other investors are afraid simply because fear breeds fear.

Let's start with China. (You may have seen me explain some of the following information before, but it's worth repeating.) What we experienced on Monday is a drop in the bucket compared to what they've recently gone through. *Their* worst day was probably July 27, when the Shanghai Index fell 8.5%.2 (By point of comparison, our S&P 500® only dropped about 4% on Monday. 3) China's market crash was largely driven by emotion, too. First came greed, when government-created hype caused millions of people to pour their money into stocks. For months, state-owned media urged people to buy stocks, loudly proclaiming that the markets were the place to put their money.

As the demand for stocks increased, so too did stock prices. But that didn't deter investors, who kept buying as long as stocks looked like they were going up. To make a long story short, stock prices rose too high, too fast. Meanwhile, the overall Chinese economy had actually been slowing down, and, despite its size, was thought by some analysts to be relatively weak in terms of growth. The end result was a bubble. And as every little child knows, bubbles pop.

In June, investors finally woke to the fact that their nation's economy wasn't an effective prop for their nation's markets. Once again, investors acted emotionally—but this time, out of fear instead of greed. Their sudden loss in confidence led to a sharp sell-off in the stock market, one that has continued to this day despite the Chinese government's attempts to stop it.

So why are the goings-on in China causing such anxiety here? After all, it's estimated that only 1.5% of Chinese shares are owned by foreigners.4 The answer is something called *financial contagion*. Just as an actual disease can spread from person to person, some investors are afraid China's economic problems will spread from country to country. China's economy is the

second largest in the world, and when it struggles, it can affect all those other nations and companies that do frequent business with China.

And there's the fear. People who have invested in companies affected by China are worried that China's woes will affect their investments in turn.

Oil prices are stirring up financial heartburn, too. On Monday, prices fell below $39 a barrel, the lowest since 2009.5 And while that's good news for drivers at the pump, it can bring negative side-effects, too. Falling oil prices makes life harder for companies in the energy industry. It also hurts countries that depend heavily on exporting oil. These pains are another likely source behind Monday's sell-off.

So now that we understand the situation, what should we do with this information? Here are some ideas:

1. Remember that market corrections are normal and fairly common. In fact, many experts believe that corrections are actually healthy, because they put the brakes on the kind of overly-rapid growth that might otherwise turn into a bubble.
2. Remember that we're still in a bull market. Even Monday's plunge can't wipe out the enormous gains the markets have made over the past few years. While it's certainly possible the markets might continue to fall, we're still some distance away from "bear market" territory, which is defined as a 20% drop from a recent peak.
3. Remember that emotion makes a good servant and a bad master … and should never be used to make investment decisions. Emotion is largely responsible for China's stock market problems, and it's also responsible for Monday's panic-selling. Proper investing comes from having a sound strategy, preferably one that exists within an overall financial plan. The two Rs, ration and rules, are an investor's best tools. Unfortunately, too many investors do the opposite. They invest emotionally. When stocks go up, exuberance prevails. When stocks start going down, fear takes over. As China has recently proved, both emotions tend to be very harmful.
4. Remember not to rely on the media. You'll be seeing a lot more headlines in the coming days, so this point is key. Remember, too, that whether it's state-owned or private, the media has a vested interest in stirring up emotions. In China's case, people believed the media's hype instead of relying on critical thinking or common sense. In our case, the temptation will be to believe the media's doom-and-gloom. Never make financial decisions based solely on what you read in the newspaper.

One more thing, remember what I said about the two Rs, ration and rules? Let's focus on that for just a moment.

As you know, there's absolutely no way to predict what the markets will do tomorrow. We can make educated guesses, but we can't know for sure. But in a sense, it doesn't matter. Because whichever way the markets go, *our* course is already set. It's a course based on specific rules that we will not deviate from, since we know they'll serve us well in the long run.

Think of it like this. Imagine you're driving your car in a storm down a long, winding road—the kind of road with a lot of twists and turns. Because of the conditions, you can't tell for sure what lies ahead of you. You simply don't have that knowledge. How do you cope? How do you keep moving forward? The answer is, because you've already prepared yourself. You've buckled your seat belt. You've ensured your car and tires are well-maintained. You're paying attention to the road, and you're well-versed in defensive driving tactics. No matter what unexpected hazard comes up, you're as prepared as you possibly could be. That's what gives you the confidence to keep going.

This same principle applies to our investing strategy. It's true; we don't know what the markets will do tomorrow. But we already know what *we'll* do. We've already been analyzing market trends, so we've largely seen this coming. We already have a plan for when your portfolio should play defense as opposed to offense. We've already set rules for when we decide to buy and at what point we decide to sell and move to cash.

By continuing to follow this approach, we can eliminate emotion and guesswork. We also don't have to worry about accidentally selling low and buying high, because we've already determined our *own high* and *our own* low.

So as other investors act out of fear, here's the way *we're* going to act: with ration and rules. My team and I are always evaluating the state of your portfolio. If we feel the need to recommend any changes, we'll certainly let you know. But in the meantime, we believe in our investment strategy for a reason: because it will help you reach your long-term goals. We still think that to be the case. While a correction might be uncomfortable, it will pass … and potentially bring new opportunities with it.

In the meantime, we're here for you if you have any questions or concerns. Please feel free to give me a call at (409) 792-0179. I'm always happy to talk to you!

Sincerely,

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