



# Don't just do something, stand there!

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**When markets are uncertain, it may be tempting to make changes even when we know that we shouldn't mess with our established strategy. What are some good ideas to "scratch the itch" of action bias?**

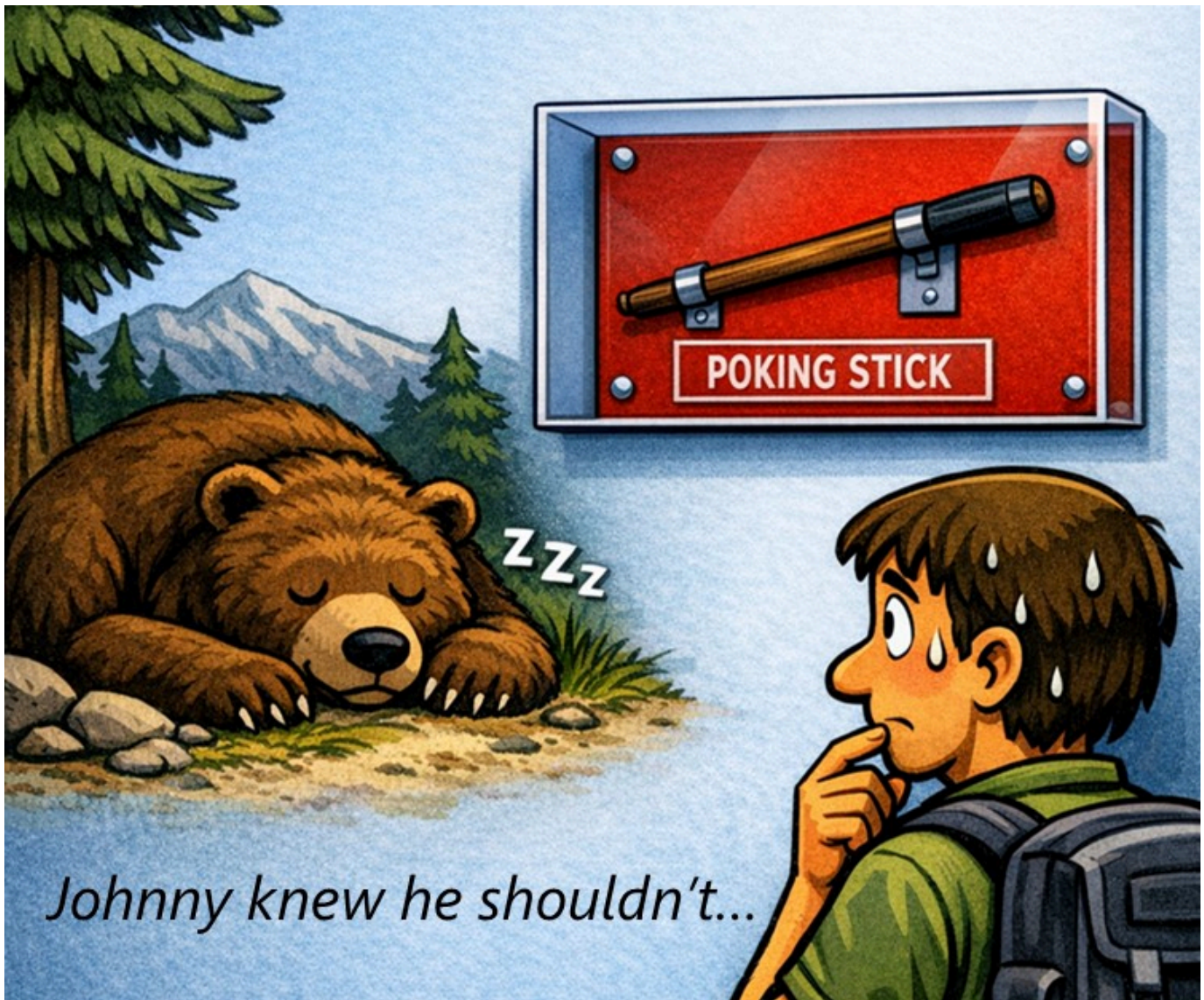
## Key points

- Periods of heightened uncertainty—driven by geopolitics, domestic politics, and technological disruption—may prompt families to reconsider their investment approach, but behavioral research suggests that frequent trading in response to market events can be counterproductive and may lead to lower net returns.
- Rather than reacting impulsively, families may benefit from disciplined strategies such as rebalancing and tax-loss harvesting, which can add value and help address the urge to take action while supporting long-term goals.
- The UBS Wealth Way approach encourages families to focus on what can be controlled, automate beneficial actions, align decisions with their goals, and proactively manage risk—helping to maintain financial stability and resilience through periods of market volatility.

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## Introduction

We live in a period of incredible uncertainty.

Geopolitical tensions abound, from the US-Iran conflict and the Ukraine-Russia war to the US-China rivalry and simmering trade tensions across the global. Domestic politics are another source of uncertainty, with US political partisanship at record highs ahead of the midterm elections.

As if these concerns weren't enough, rapid advances in artificial intelligence are also creating an undercurrent of dread amid fears of potential job disruptions.

Against this backdrop of uncertainty, many find themselves reconsidering their approach to investing.

Uncertainty often creates a strong urge to take action. In behavioral finance, this tendency is known as "action bias," a common response among investors. Sometimes, it just feels right to do something—*anything*—to help gain a sense of control.

While this tendency is natural—perhaps a part of our evolved "fight or flight" response—research suggests that it may be counterproductive. In a seminal research study, cleverly titled "Trading is Hazardous to Your Wealth," behavioral scientists

found that households with high portfolio turnover experienced 6.8% annualized underperformance compared to those with lower turnover.<sup>1</sup>

This result may be attributed to human nature, transaction costs, and tax implications, all of which tend to work against investors when trading frequently. Even when higher turnover leads to better gross returns, increased taxes and costs often result in lower net returns. With this in mind, maintaining a disciplined, long-term approach may help families avoid costly mistakes.

When markets are uncertain, it's tempting to make changes even when we *know* that we shouldn't mess with our established strategy. At the same time, complete inaction may not always be the best course. Certain portfolio management strategies—such as rebalancing and tax-loss harvesting—may help add value in a variety of market environments.

For example, if an investor's portfolio has not been rebalanced recently, it is possible that the recent equity drawdown has caused the stock allocation to drift below the portfolio's long-term target, while bond allocations have risen above the long-term target. Rebalancing may help the portfolio get back to the target allocation and thus increase the portfolio's ability to participate in a potential market rebound.

Additionally, recent market losses may present opportunities for tax-loss swaps—harvesting a capital loss in one investment while replacing that exposure with another investment. By realizing capital losses while they are available, investors can build up the ability to offset realized capital gains and thus defer capital gains taxes. When a family has a net capital loss in a given tax year, they may deduct up to \$3,000 against ordinary income and carry the remainder forward to future tax years.

Strategies such as rebalancing and tax-loss harvesting may help families address the urge to take action. By contrast, other changes—such as major portfolio or risk profile changes—may be undesirable if they are driven solely by market conditions rather than by a change in spending or retirement goals.

With this in mind, here are some approaches that may be helpful for "scratching the itch" to make changes while supporting long-term objectives.

### **1. Focus on what can be controlled**

Wisdom from the Serenity Prayer—"the serenity to accept the things we cannot change, the courage to change the things we can, and the wisdom to know the difference"—is relevant for investing. It is usually impossible to reduce portfolio risk without also reducing portfolio return potential, and markets can snap back quickly following a risk event.

Short-term volatility is unavoidable, so families may want to be wary of attempting to time markets. Instead, it may be preferable to look for opportunities to improve the risk-return dynamic by building well-balanced, diversified portfolios. Families may also want to look for opportunities to defer spending and/or boost portfolio contributions to take advantage of a market decline.

### **2. Automate beneficial actions**

Habits have a compounding effect, so families may seek out opportunities to automate portfolio management strategies, such as rebalancing when allocations drift more than 5% from targets or systematically harvesting tax losses. Automation may help capture value without increasing the number of active decisions required. Many strategies are most effective when implemented regularly, even if they feel counterintuitive or uncomfortable.

### **3. "Quarantine" major decisions.**

The term quarantine, originating from the Italian "quarantina," refers to a 40-day period of isolation used to help fight the spread of the Black Death. When considering significant changes to long-term strategy or plans, families may benefit from allowing themselves time to reconsider—perhaps not 40 days, but at least a week—before taking action.

### **4. Align decisions with goals.**

The UBS Wealth Way approach is our approach to help families organize their financial lives in to strategies based on the purpose and time horizon:

- Liquidity—to help provide cash flow for short-term expenses,
- Longevity—for longer-term needs, and
- Legacy—for needs that go beyond your own.

Segmenting wealth by purpose may help families to build portfolios that reflect their goals and values. By putting short-term market risks and potential portfolio changes into context, this framework aims to support objective decision-making, which can be especially valuable when market volatility and uncertainty are high.

When planning for the future, envisioning one's future self may help prioritize growth and long-term goals, such as retirement, family experiences, and philanthropy. Empathy for one's future self may help families look past short-term uncertainties and address the opportunity cost of investing too conservatively with long-term assets. It's also helpful to know that there is a dedicated Liquidity strategy portfolio of high-quality, lower-risk investments that are earmarked to help pay for day-to-day spending if market volatility persists.

## 5. Manage risk proactively.

Regardless of the source of concern—politics, geopolitics, or technological disruption—market volatility and bear markets are a persistent risk. Historically, most investment portfolios have recovered losses within three to five years following major disruptions. Building a Liquidity strategy that can fund spending for three to five years may help families maintain their lifestyle during periods of market stress. For additional research and strategies, see UBS Bear Market Guidebook ([www.ubs.com/bearmarketguidebook](http://www.ubs.com/bearmarketguidebook)).

Time frames may vary. Strategies are subject to individual client goals, objectives and suitability. This approach is not a promise or guarantee that wealth, or any financial results, can or will be achieved.

<sup>1</sup> Brad M. Barber, Terrance Odean, *Trading Is Hazardous to Your Wealth: The Common Stock Investment Performance of Individual Investors*, The Journal of Finance, Vol. LV, no. 2. April 2000.

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