



When Markets Fall

An Investor's Guide to Staying Disciplined
When Everyone Else Is Panicking

Lessons from Institutional Investors
on Navigating Volatility

The Most Expensive Emotion in Investing

Over the 30 years ending in 2023, the S&P 500 returned an average of 10.15% annually. The average equity investor earned 6.81%. That gap — 3.34% per year — was not primarily caused by bad stock picking. It was caused by bad timing, driven by fear.

The research, published annually by DALBAR in their Quantitative Analysis of Investor Behavior, tells a remarkably consistent story across decades of data: individual investors systematically buy high and sell low. They pour money into the market after it has risen and pull money out after it has fallen. The pattern is so persistent, so universal, and so costly that it has earned its own name: the behavior gap.

To put this in concrete terms: on a \$1 million portfolio, a 3.34% annual gap compounds to approximately \$1.5 million in lost wealth over 20 years. Not lost to fees. Not lost to bad security selection. Lost to fear.

Fear is not free. It is the single most expensive line item in most investors' financial lives, and it never appears on a statement.

THE BEHAVIOR GAP IN NUMBERS

S&P 500 average annual return (30 years):	10.15%
Average equity investor annual return:	6.81%
Annual gap caused by behavior:	3.34%
Cost on \$1M portfolio over 20 years:	~\$1.5 million

Source: DALBAR Quantitative Analysis of Investor Behavior, 2024

Why Smart People Make Bad Decisions

The investors who sell at the bottom are not unintelligent. Many are successful professionals, business owners, and executives who make excellent decisions in every other area of their lives. The problem is not intelligence but architecture. The human brain is hardwired for an environment radically different from financial markets.

Three cognitive biases do most of the damage:

Loss Aversion

Nobel laureate Daniel Kahneman demonstrated that losses feel roughly twice as painful as equivalent gains feel good. A \$50,000 portfolio decline causes much more emotional distress than a \$50,000 gain causes satisfaction. This asymmetry means that during market downturns, the emotional pressure to “do something” — to stop the pain — becomes nearly irresistible, even when doing nothing is the optimal strategy.

Recency Bias

We overweight what just happened. After months of falling markets, it feels like markets will fall forever. After months of rising markets, it feels like they will rise forever. Neither is true, but both feel true in the moment. Recency bias causes investors to extrapolate short-term trends into permanent conditions — selling after declines and buying after rallies, which is precisely backwards.

Herding

We are social animals. When everyone around us is selling — when the news is apocalyptic, when colleagues are moving to cash, when social media is filled with panic — it feels irrational not to follow. But the crowd is almost always wrong at market extremes. The investors who profit most from market dislocations are the ones who have built processes specifically designed to override the pull of the herd.

The key insight: These are not character flaws. They are features of human cognition that served us well for 200,000 years of survival — and serve us terribly in financial markets. You cannot eliminate them. But you can build systems that override them.

What the Best Investors Actually Do

The most successful investors in history are not people who avoided fear. They are people who built frameworks that allowed them to act rationally when fear was at its peak. Two investors, in particular, offer lessons that every individual investor can apply.

Warren Buffett: The Framework Behind the Famous Quote

Everyone knows the quote: “Be fearful when others are greedy, and greedy when others are fearful.” But the quote alone is practically useless without the framework behind it.

When Buffett invested \$5 billion in Goldman Sachs preferred shares in September 2008 (while the global financial system was on the brink of collapse) he was not blindly being brave. He was being analytical. He understood Goldman’s intrinsic value. He structured the deal with a massive margin of safety (10% preferred dividend plus warrants). And he had a process, refined over decades, that allowed analysis to override emotion.

The lesson is not “close your eyes and be brave.” The lesson is: **have a process that produces clarity when the market is producing chaos.** Buffett could act in 2008 because he had already done the work. He knew what he was buying, what it was worth, and what price would give him sufficient margin of safety. When the price arrived, the decision was mechanical.

Howard Marks: Redefining Risk

Howard Marks, co-founder of Oaktree Capital and author of *The Most Important Thing*, offers a complementary framework. His central insight: **the biggest risk in investing is not volatility. It is the permanent loss of capital.**

Marks draws a sharp distinction between price fluctuation and actual loss. When the market drops 20%, you have not lost 20%. You own the same businesses, generating the same cash flows, with the same long-term prospects. The only way the decline becomes a loss is if you sell. Price is what you pay. Value is what you own. A market decline changes the first without changing the second.

This reframe is powerful because it changes the question investors ask during a downturn. Instead of “How much have I lost?” the question becomes: “Is the value of what I own impaired, or only the price?” If the answer is that value is intact, then the decline is not a risk to be feared, it is an opportunity to be evaluated.

The Playbook for Downturns

When markets fall sharply, here is what top-tier investment managers actually do: they do not sell out of panic. They revisit research. They rebalance. They deploy capital. They stress-test portfolios and look for asymmetric opportunities where the potential reward meaningfully exceeds the risk.

Again, the best investors are not immune to fear. But they have a process that takes precedence over emotion. Here is a simplified version of that process, adapted for individual investors:

1 Separate Signal from Noise

Is this decline driven by a fundamental shift in economic conditions — a major recession, a credit crisis, a structural change in the market — or is it a sentiment-driven correction? Most declines are the latter. Markets overshoot in both directions because participants are emotional, not because the underlying economy changed overnight. The discipline is to diagnose before acting.

2 Reassess the Thesis

For every position in the portfolio, ask: has anything changed about the underlying value of this business? Not the price, the value. Are the cash flows permanently impaired? Is the competitive position weakened? Is the balance sheet at risk? If the thesis is intact, a lower price means a wider margin of safety, not a reason to sell. If the thesis is genuinely broken, sell — but sell because the research and analysis demands it, not because the market is down.

3 Evaluate the Opportunity

Market declines create dislocations. Quality assets that were fully valued at higher prices may now offer compelling risk-adjusted returns. Great investors view corrections as inventory clearance events — the same goods are available at lower prices. The discipline is to have a prepared list of investments you've researched and you would buy at the right price, so that when prices arrive, the decision is execution rather than deliberation.

4 Act with Discipline

Rebalance toward your long-term targets, not away from short-term fear. If your target allocation is 70% equities and the decline has taken you to 60%, the best response is to buy equities to restore the target, not to sell more equities to reduce the pain. This is mechanically simple but emotionally difficult, which is precisely why most investors do the opposite.

Your Action Plan

Here is a practical framework you can implement now, so that when volatility spikes, you have a plan rather than a panic.

DURING THE DOWNTURN: WHAT YOU CONTROL

Reduce the noise. Stop checking your portfolio daily. Turn off financial news alerts. The signal-to-noise ratio of financial media during a market decline is approximately zero. Every minute spent consuming panic coverage strengthens the cognitive biases that cost you money.

Revisit your plan. Look at your written time horizon and allocation targets. Remind yourself why you invested the way you did. If those reasons have not changed, the plan has not changed. The price is different. The strategy is not.

Resist the urge to act. The most powerful thing you can do during a downturn is often nothing. The impulse to “do something” feels productive but is almost always destructive. Stillness, in this context, is a discipline.

DURING THE DOWNTURN: WHAT YOUR ADVISOR HANDLES

The analytical work. Reassessing every position, stress-testing the portfolio, separating signal from noise, and identifying whether the thesis on each holding is intact or impaired. This is the heavy lifting that requires a process, not a reaction.

The rebalancing. Systematically moving your portfolio back toward its long-term targets — buying what has fallen when the fundamentals remain sound, and trimming what no longer fits the thesis.

The opportunity evaluation. Identifying quality assets that the decline has made available at better prices, and deploying capital with discipline rather than emotion.

The conversation. A real, substantive discussion about what is happening in the market, what it means for your portfolio specifically, and why the plan is or is not changing. Not a scripted reassurance from a call center — a direct conversation with the person making your investment decisions.

AFTER THE DOWNTURN

Review together. Sit down with your advisor and assess what happened. Did the process hold? Did the portfolio perform as expected relative to the severity of the decline? What can be strengthened for the next time?

Use it as data. Every downturn is a rehearsal for the next one. The investors who improve after each cycle are the ones who compound wealth over decades.

You don't have to carry this alone. Institutions and ultra wealthy investors have teams, processes, and systems. You can too. A good advisor gives you access to that same infrastructure.

The Math of Missing the Recovery

The data on this point is unambiguous: the best days in the market occur in close proximity to the worst days. Selling during a decline means you almost certainly miss the snapback — and missing even a handful of the best days devastates long-term returns.

Scenario	Annualized Return	Growth of \$10,000
Stayed fully invested	10.1%	\$66,200
Missed the 5 best days	7.8%	\$44,400
Missed the 10 best days	6.1%	\$32,100
Missed the 15 best days	4.6%	\$24,200
Missed the 20 best days	3.3%	\$18,800
Missed the 30 best days	1.0%	\$11,900

Hypothetical illustration based on S&P 500 returns over 20 years. Past performance does not guarantee future results.

Consider what this means: missing just the 10 best days over two decades cut your ending wealth in half. And here is the critical detail — **seven of the 10 best days in the market occurred within two weeks of the 10 worst days**. The best days and worst days are clustered together. You cannot avoid the worst days without missing the best days. They are a package deal.

This is the mathematical case for staying invested. It is not a moral argument. It is not about courage or discipline for their own sake. It is arithmetic: the cost of being out of the market at the wrong moment is catastrophically high, and the moments that matter most are impossible to predict in advance.



Far more money has been lost by investors preparing for corrections, or trying to anticipate corrections, than has been lost in corrections themselves.

— Peter Lynch

The Role of a Disciplined Advisor

Vanguard’s research on “Advisor’s Alpha” quantifies something that most investors sense intuitively: a good financial advisor adds meaningful value. Their estimate is approximately 3% in net returns annually. But the source of that value is not what most people expect.

The largest single component of Advisor’s Alpha is not investment selection, not asset allocation, and not tax optimization — though all of these matter. It is **behavioral coaching**: the act of keeping clients invested when they want to flee, and disciplined when they want to chase.

This is counterintuitive. We hire advisors because we expect them to pick better investments or find opportunities we would miss. And good advisors do this. But the research consistently shows that the biggest value-add is not what the advisor does with the portfolio — it is what the advisor prevents the client from doing to the portfolio.

WHERE ADVISOR VALUE COMES FROM (VANGUARD ADVISOR’S ALPHA)

Behavioral coaching:	~1.5%	Keeping clients disciplined through volatility
Asset location:	~0.75%	Tax-efficient placement across account types
Rebalancing:	~0.35%	Systematic return to target allocation
Spending strategy:	~0.70%	Tax-smart withdrawal sequencing in retirement

Total estimated value: ~3.0% or more in net returns

Source: Vanguard, Putting a Value on Your Value: Quantifying Advisor’s Alpha, 2024

Think about what this means in practical terms. On a \$1 million portfolio, 3% in annual added value translates to roughly \$30,000 per year — compounding over decades. The difference between a \$2 million retirement and a \$3.5 million retirement may not be which stocks were picked. It may be whether someone was there during the downturn of 2026 or 2030 to say: “The plan is still sound. Here is why. Let’s stay the course.”

But not all advisors are equipped to provide this kind of coaching. An advisor who uses model portfolios built by someone else may not have the depth of understanding to explain *why* a position is worth holding. An advisor you can only reach through a call center cannot provide the personal relationship that builds the trust necessary to hold steady. Behavioral coaching requires competence, access, and trust — and all three must be present for it to work.

Volatility Is the Price of Admission

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The stock market is a device for transferring money from the impatient to the patient.

— Warren Buffett

Markets fall. They always have. They always will.

Since 1950, the S&P 500 has experienced a decline of 10% or more roughly once every 18 months. A decline of 20% or more occurs roughly once every six years. A decline of 30% or more has happened five times. Each time, the market recovered and went on to set new highs. Each time, investors who sold at the bottom locked in losses that patient investors recovered.

The question is not whether you will experience a downturn. You will. The question is whether you will have the framework, the process, and the support to hold steady when it arrives.

Volatility is not a defect in the market. It is the mechanism by which long-term returns are generated. Stocks earn more than bonds over time precisely because they are more volatile — and most investors cannot tolerate that volatility, so they sell at the wrong time and surrender the premium to those who stay. The return you earn over a lifetime of investing is, in large part, compensation for the discomfort of watching your portfolio decline and choosing not to act on that discomfort.

This is what Howard Marks means when he writes that risk and return are not opposites — they are companions. The willingness to endure short-term uncertainty is the price of long-term compounding. Investors who accept this — who build it into their expectations and their plans — are the ones who capture the returns that accrue to patience and discipline.

The institutional investors who manage trillions of dollars understand this deeply. They do not hope for calm markets. They prepare for turbulent ones. And when turbulence arrives, they have the process, the capital, and the temperament to act on opportunity rather than react to fear.

You can do the same.

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You don't need to predict the future. You just need to be prepared for it.

— Howard Marks

How Erenda Helps You Stay the Course

Everything in this guide points to a single conclusion: the investors who capture long-term returns are the ones who combine rigorous analysis with emotional discipline. At Erenda Capital Management, our entire approach is built around this principle.

Institutional Risk Management

We evaluate downside scenarios before investing, not after. Every position in your portfolio has been stress-tested against adverse conditions. When markets fall, we are not scrambling to understand our exposure — we have already mapped it. This preparation is what allows us to respond with analysis rather than react with anxiety.

Direct Access to Your Portfolio Manager

When markets are volatile, you can speak directly to the person making your investment decisions — not a scripted reassurance from a call center, not a relationship manager relaying messages. The person who knows your portfolio, your thesis, and your plan is the person on the other end of the phone. This is the foundation of the trust that makes behavioral coaching possible.

A Process Built on Value, Not Sentiment

Our investment decisions are driven by fundamental analysis of intrinsic value — not by market sentiment, not by headlines, and not by what the crowd is doing. When the market declines, our process asks one question: has the value of what we own changed, or only the price? If value is intact, a lower price is an opportunity. This framework, applied consistently, is what produces long-term outperformance.

Alignment Through Co-Investment

Management invests alongside every client, in the same portfolios and the same strategies. When we counsel patience during a downturn, we are counseling ourselves as well. Our capital is on the same line as yours. That alignment is not a marketing claim — it is the structural foundation of every recommendation we make.

Is Your Portfolio Prepared for the Next Downturn?

If the ideas in this guide resonate with you — if you believe that disciplined, research-driven investing with a long-term focus is the right approach — we would welcome a conversation.

We offer a complimentary portfolio review: a confidential, no-obligation discussion about your current positioning, your risk exposure, and whether your portfolio is built to weather volatility or vulnerable to it.

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