Coping with volatile markets: 6 tips for alleviating anxiety

Volatility, or wide, rapid swings in equity prices, is a natural part of investing. These price movements may seem more exaggerated when the media focuses on other economic issues, such as credit problems or a declining housing market. As the chart below shows, the worst 12-month stock market declines usually have been followed by periods of significant recovery. But that's not always the case; for example, a year after September 2001 the S&P 500 remained down 20.5 percent.

12 Months Ended	Trailing 12-Month Return	Next 1-Year Return	Next 5-Year Return	Next 10-Year Return
Feb. 2009	-43.3%	+53.6%		
Sept. 1974	-38.9%	+38.1%	+16.8%	+15.5%
Sept. 2001	-26.6%	-20.5%	+7.0%	+2.82%
March 2003	-24.8%	+35.1%	+11.3%	
May 1970	-23.3%	+34.8%	+7.2%	+8.2%
Aug. 1988	-17.8%	+39.0%	+15.8%	+17.0%
Oct. 1962	-14.9%	+35.3%	+14.3%	+10.6%
July 1982	-13.6%	+59.2%	+29.6%	+19.2%
Sept. 1966	-12.0%	+30.6%	+8.7%	+ 6.9%
Dec. 1957	-10.8%	+43.4%	+13.3%	+12.9%

Source: Wilshire Compass – reflects S&P 500 Index returns. The S&P 500® is an unmanaged index and investors cannot invest directly in an index.

- This table illustrates time periods in which the S&P 500 index has experienced a return of -10% or less over the span of 12 months as well as the subsequent 1-, 3-, 5-, and 10-year performance since the inception of the index in 1957.
- The trailing 12-month returns were sorted from worst to best. Adjacent 12-month periods were not considered. As a result, the 12 months ended February 2009 had the lowest return in the data set, so the 12-month periods that overlapped with February 2009 were not considered.
- The trailing 12-month returns are compounded total monthly returns for the S&P 500 as reported by Wilshire Compass. The 5- and 10-year returns are annualized total returns. Investors cannot invest directly in an index.
- This chart demonstrates historical results. There is no guarantee of future positive returns after a prolonged stock market downturn.

Investment options are subject to investment risk. Shares or unit values will fluctuate and investments, when redeemed, may be worth more or less than their original cost. It is possible for an investment option to lose value.

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Here are six tips to help cope with challenging market environments:

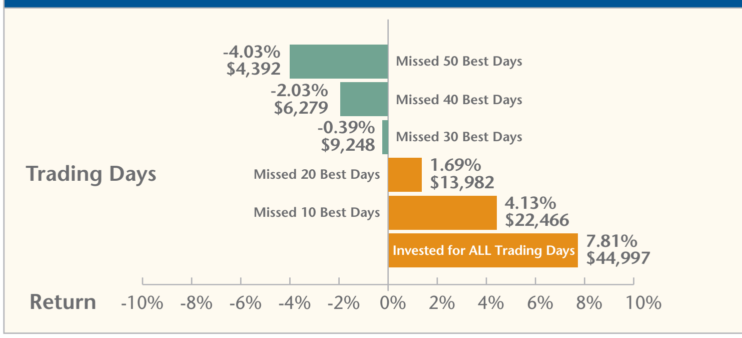
1. Stay in the market

When you sell an investment, you can increase your chances of missing the major market movements that signal the start of a longer recovery. Many of these major upside moves can happen quickly, often in just a few days. To avoid missing these key days, you may want to consider staying invested and avoid panic selling. Consider this hypothetical example as illustrated in the following chart:

An individual who was invested in the S&P 500 from January 2, 1992, until December 31, 2011, would have turned a $10,000 investment into $44,997, for an average annual return of 7.81 percent. Alternately, an investor who panicked and sold their positions during this same period and missed the 10 best trading days in this period would have seen their return fall from 7.81 percent to 4.13 percent.[1]

The simple lesson: you may want to consider staying invested, since no one can predict when the market will experience its best days.

Missing the Market | **Value of a $10,000 investment in S&P 500: 1/2/1992 – 12/31/2011**



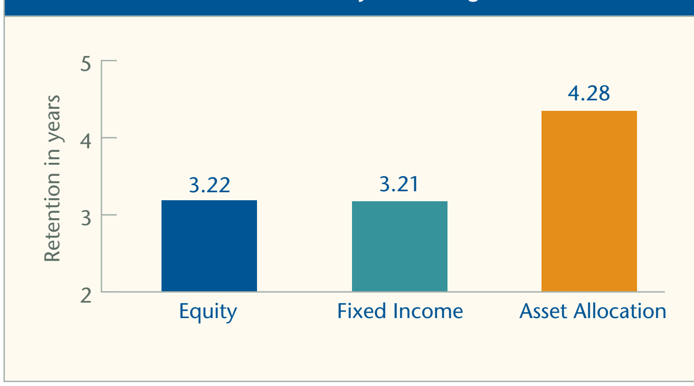
This example is hypothetical; individual results will vary. Results include reinvested dividends. Past performance is no guarantee of future results. The S&P 500® is an unmanaged index and investors cannot invest directly in an index.

Source: Ned Davis Research, Inc., as of December 31, 2011

2. Invest for the long term

Studies show the longer an investor held their investment position, the greater their returns.[2] Of the three types of investments studied (stock funds, bond funds, and asset allocation investment options), the average investor in asset allocation funds held their investment options the longest (an average of 4.30 years) over the five time periods studied (1-, 3-, 5-, 10-, and 20-years). As a result, these investors successfully weathered one of the most severe market declines in history (2000-2002).

Asset Allocation Investors Generally Have Longer Retention Periods



Since asset allocation investment options take a lot of the guesswork out of investing, investors tend to hold them for longer time periods compared to investors in equity and bond investment options. This 20-year (1989-2009) analysis shows these differences. The Dalbar study found that frequent mutual fund exchanges are tied to lower overall returns. (Note: Asset allocation/ diversification does not guarantee a profit or protect against a loss.)

Source: Dalbar March 2010 QAIB Study

The 2010 Dalbar QAIB Study analyzed a 20-year period beginning on 12/31/1989 and ending 12/31/09. The average investor refers to the universe of all mutual fund investors whose actions and financial results are restated to represent a single investor. This approach allows the entire universe of mutual fund investors to be used as the statistical sample, ensuring ultimate reliability.

3. Diversify the portfolio

Another important strategy is to diversify the portfolio. According to the Dalbar study, investors guess incorrectly about the market's direction 50 percent of the time.[2]

Diversification is the process of spreading investments across a number of different types of investment options, as well as in different styles and market capitalizations of equities and bonds. Diversification enhances the benefits of asset allocation so investment balances may be less affected by short-term market swings than they would be if you invested in a single asset class.

If you are an investor who is nearing retirement, consider consulting your financial professional or a representative of the Principal Financial Group® about changes that may help minimize losses and offer diversification for short-term investment options.

Note: Asset allocation/diversification does not guarantee a profit or protect against a loss.

4. Consider asset allocation portfolios

Historically, business cycle contractions last about one-sixth as long as expansions.[3] Now may be a good time to re-evaluate your risk tolerance.

If you want a professionally managed investment option to handle this complicated task, **consider using target-risk and target-date asset allocation portfolios.** These investment options are specifically designed to align you with a risk tolerance or projected retirement date with a diversified portfolio.

For example, a target-risk lifestyle investment option can be elected based on a person's risk tolerance preferences and can offer 12 to 16 separate asset classes in one investment. Similarly, the family of target-date lifestyle investment options offers asset allocation based on a portfolio's future target date. Typically, with a target date investment option, the allocation shifts over time to typically more conservative assets. Some target date investment options reach their most conservative allocation at the target date but others continue to shift for years beyond the target date. Both target-risk and target-date investment options are designed and managed based on the established principles of portfolio diversification and risk management.

The Principal LifeTime portfolios, which are target-date funds, invest in underlying Principal Funds, Inc. mutual funds. Each Principal LifeTime portfolio is managed toward a particular target (retirement) date, or the approximate date the participant or investor starts withdrawing money. As each Principal LifeTime portfolio approaches its target date, the investment mix becomes more conservative by increasing exposure to generally more conservative investment options and reducing exposure to typically more aggressive investment options. The asset allocation for each Principal LifeTime portfolio is regularly re-adjusted within a time frame that extends 10-15 years beyond the target date, at which point it reaches its most conservative allocation. Principal LifeTime portfolios assume the value of the investor's account will be withdrawn gradually during retirement. Neither the principal nor the underlying assets of the Principal LifeTime portfolios are guaranteed at any time, including the target date. Investment risk remains at all times

5. Remember the benefits of long-term investing

The bottom line: It takes discipline to keep today's bad news from derailing your long-term investment goals. However, when you continue to pursue your long-term investment goals, you should recognize that successful investing is a marathon, not a sprint.

Keep in mind that both separate accounts and mutual funds are subject to the typical risk of investing, including but not limited to, market risk and the risk associated with the underlying securities in the portfolio.

6. Stay in touch with your financial professional

News headlines can understandably make you nervous. However, to keep these developments in perspective while staying focused on your personal situation, **remember to stay in touch with your financial professional or a representative of The Principal® by calling 1-800-547-7754.** They are familiar with your personal situation and can provide the information you need to help you stay on track to reach your retirement savings goals.

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While these six tips can help you navigate through periods of market volatility, one thing to remember is that the stock market is a collective gauge of investor sentiments, negative and positive. It is the investor's task to not be distracted by these emotional moves. These six tips can help you stay focused.

Sources:

[1]Ned Davis Research, Inc., as of December 31, 2011.
[2]Dalbar March 2010 QAIB Study.
[3]George Hildebrand, *Business Cycle Indicators and Measures*, Probus Publishing, 1992.

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