INVESTMENT STRATEGIES IN A BEAR MARKET

Keep a cool head when considering how to handle retirement funds. BY JOHN SPOTO

The ongoing stream of negative economic news, including stubbornly high unemployment and low expectations for economic growth worldwide, has created gut-wrenching volatility in financial markets.

Watching your investments decline day after day can be disturbing as you contemplate the implications for your financial future. In our results-driven society, the question on many anxious investors' minds is, "What should I do?"

There's not one easy answer, but above all, there are four fundamental principles that apply to all investors regardless of your age or stage in life:

> THE TIME TO DETERMINE THE **RIGHT INVESTMENT STRATEGY** IS BEFORE, NOT DURING, FINANCIAL STRESS.

1. Sudden and prolonged declines in the stock market are inevitable: If you are unwilling or unable to tolerate these painful periods in exchange for higher potential returns, you will save yourself money, energy and heartache by avoiding the stock market.

2. The market is unpredictable: No one, including experts, can consistently predict the turns the market will take. Anyone who suggests he or she has a system or model for doing so is just not credible. Although economics propel stock prices in the long run, in the short run the market is driven up and down erratically by emotions that are affected by political and financial events around the world. These events come when least expected and change direction just as quickly.

3. Plan precedes investment: The time to determine the right investment strategy is before, not during, financial stress. What do you expect to use the money for? When will you need it? What is your emotional and financial ability to handle losses? Short-term goals dictate stable investments, so you can be confident the money will be there when you need it. Longer term goals call for a mix of stocks and bonds that offer a greater chance to grow your money, but will periodically incur losses. Will these losses cause you to lose sleep or affect your ability to reach your financial goals? The answer to these questions will determine how much of your money to allocate to stocks versus bonds.

4. Emotions should not drive decisions: During periods of extreme market volatility, investors often make rash decisions that they regret later. Step back and assess your specific situation rationally before you act. Assuming you have a well thought out plan in place and your circumstances have not changed, don't lose conviction. Stick with your plan. ➤

Changing a long-term plan by reacting to short-term conditions has not proven to be a successful investment strategy.

Once you have a grasp on the four basic principles, you can begin to consider your life stage to determine how to proceed in a long-term downturn:

1. THE YOUNG SAVER

If you're actively saving in your 20s or 30s, a prolonged bear market is a blessing in disguise. It gives you a rare opportunity to buy shares at low prices early in your career, so you can benefit later from healthy returns when the markets come back. Instead of reducing your allocation to stocks, consider increasing it.

2. THE MID-CAREER INVESTOR

Part of any good investment strategy is maintaining the asset allocation you decided was right for you. Bear markets knock that mix out of whack by reducing the value of the stocks in your portfolio. So, if you are in your 40s or 50s and 10 years or more from retirement, steel yourself and rebalance your portfolio back to your original asset allocation.

Don't underestimate the emotional difficulty of executing this approach. It means that during a time of economic crisis, you are selling the assets (cash and bonds) that held up well in order to buy more stocks after they have suffered the greatest losses. When you are ready to retire, you will be glad you chose to take advantage of this strategy.

> IF YOU UNDERSTAND THAT **DECLINES AND LOSSES ARE TO BE EXPECTED,** YOU CAN BUILD A SENSIBLE INVESTMENT PLAN.

3. THE NEAR RETIREE AND RETIREE

For those of you in your 60s and 70s who are close to or already have begun to spend down your savings, a prolonged market decline can be devastating because you are forced to sell more shares when they are cheap in order to pay for living expenses. This permanently removes those shares from the portfolio, meaning they can't increase in value when the market recovers. In other words, you are forced to cannibalize your portfolio early in retirement, increasing the likelihood that you will deplete your investments prematurely.

So what can you do? Focus on what you can control, mainly reducing expenses or increasing income by delaying retirement or working part-time. This will lower the amount you take out of your nest egg, allowing you to preserve more of your portfolio until the market recovers.

It's not easy to keep your emotions out of investing. However, if you understand that declines and losses are to be expected, you can build a sensible investment plan. For most people, such a plan not only limits the toll on their portfolio, but also offers a great opportunity to build wealth. MVB

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