LGC&D Wealth Management, LLC
Educated Investor Feature Articles: 2008, Vol. 24
October 31, 2008

Bear Market Retirement Investing Survival Tips (Regardless of Your Age)

Overview: As markets continue to decline, some individuals are wondering if they should wait to begin saving for retirement, get out of the market or even stop contributing to their retirement plan entirely. Bear markets can hurt your investment portfolio, but a sudden, emotional reaction in the midst of them can hurt even worse. Instead, sticking to a strategy will allow you to stay the course no matter where you're at on your path to retirement. Following are additional survival tips.

All Investors
As touched on above, among the most important components to a successful investment experience is to have a carefully designed strategy and, like a postage stamp on an envelope, to stick to your strategy through thick and thin.

Another basic tenet of investment theory is that risk and *expected* return are related. Stocks have provided higher returns than Treasury bills because stocks are riskier. That lesson is made very clear during bear markets when the risk can display itself in the form of low or even negative returns, sometimes for extended periods. In fact, these times of stress are exactly why stocks have *generally* (but not always) provided higher returns over the long term. Similarly, stocks of stressed or small companies have historically provided higher returns than those of "blue-chip," large companies. The more perceived risk, the more investors demand a risk premium (higher *expected* return) as compensation.

Reducing investment expenses wherever possible is another important component. Whether the result of fees, taxes or your own too-frequent trading, expenses reduce your returns.

Early Career
If you're just beginning your career, don't hesitate to save for retirement, regardless of the market climate. The growth of your savings is directly related to the length of time that you save, so the longer you wait to begin, the more it is likely to cost you in the long run.

During your early saving days, to capitalize on the aforementioned risk premium, it is often prudent to tilt your investments more heavily toward stocks or stock mutual funds ("equity") versus Treasury bills and similar vehicles ("fixed income"). Moreover, buying stocks in a bear market means that you're paying less for more. You're basically buying "on sale," with plenty of time for prices to recover by the time you retire.

In fact, as a young investor, you are in an enviable position, because you have considerably more time to withstand the ups and downs of the market while benefiting from: (1) the power of compounding interest, or your money making money for you, and (2) the fact that, at least historically, despite short-term "mood swings," the stock market has trended upward.

As you enter your 30s, you can hope to see significant income growth in your career, providing you with more disposable income. While it can be easy for that extra money to slip away on extra expenses, it's vital to maintain disciplined retirement saving that increases at least in proportion with your income growth. A guiding principle is to always "pay yourself first" by seeking ways to auto-save, before the money hits your wallet. Take maximum advantage of employee-sponsored saving plans or similar opportunities and, if your employer is providing matching funds, contribute at least as much as needed to receive your full match. Don't cheat yourself out of free money.

Midlife Career

As you enter into your 40s and 50s and inch a little closer to retirement, you may wish to more heavily incorporate asset preservation. In other words, you want to include a sufficient amount of equity (riskier) investments so your portfolio at least keeps pace with inflation, but you don't want to take on more risk than you can tolerate during bear markets. Changes to the amount of risk and expected reward within your portfolio should be made in accordance with your own unique willingness, ability and need to accept risk — and not in reaction to short-term market fluctuations.

Consider the following analogy. Professional kite flyers will tell you that one of the most difficult skills to master is what to do when their kite starts to plunge downward. The natural, panicky impulse is to pull back on the line. However, this action only accelerates the kite's death spiral. The simple kite-saving technique is to calmly step forward and thrust your arms out. This causes the downward acceleration to stop, allowing regained control.

Just as yanking backward on a sinking kite line is the impulsive move, too often investors want to "pull back" (sell) when their portfolio's value takes a dive. The right strategy is the less-intuitive one of remaining calm and maintaining a steady course.

If you are questioning your mid-career retirement investments, ask yourself: "What has changed that would cause me to abandon my strategy?" More often than not, the answer is likely to be: "Nothing." The risk you previously took on by investing in equities is merely displaying itself during the bear market. Unless your own willingness, ability or need to accept risk has changed, "nothing" should also be the answer to what you might change about your investment plan.

End of Career

There is no denying, individuals near or in retirement face the biggest real challenges during a bear market. The ability to continue earning and/or to ride out the storm is more limited. And decisions made during the first few years of retirement can be crucial, in that they can affect your lifestyle throughout retirement.

However, all of the essential tenets of investing should continue to guide your course — perhaps even more so. First, it's important to recognize that your investment time horizon may not be as short as you think. People often consider their investment horizon as the number of years to retirement, instead of the rest of their lives. Couples should consider the life expectancy of the second-to-die, which is greater than that of either spouse. And life expectancy is increasing as our overall population enjoys improved health. Thus, it is as important as ever to remember that panic-selling stock in a dropping market will translate to less money invested during expected market recovery, and less ability to benefit from renewed growth.

In or near retirement, it can become even more important to consult a professional investment advisor who can offer you objective, fee-only advice. He or she can help you assess the various ways you can stretch your dollars further into retirement. For example, if a bear market hits during retirement, you and your advisor might consider ways you can reduce your spending; increase your income; or, if carefully planned, adjust your portfolio to reflect any true change in your willingness, ability or need to accept market risk. A trusted advisor also can help remove the emotion out of investing by forming a disciplined, academically based investment plan tailored to address your unique objectives.

In short, having a good investment plan in place and remaining adherent to it can help you sleep better at night, no matter where you are along your journey.