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News & Notes

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The corrective for volatility in investments? Think long-term!

by Jeff Englin

Markets have always moved up and down, with those movements measured as “volatility”. Now, most of us have heard the age-old advice for investing: “Buy low, sell high”. While that adage may be accurate in its simplicity, it’s a mistake for most of us to pursue it as our big aim.

First let’s take a look at the root of the concept – timing. “Timing” encourages the mindset of trying to guess when a particular type of investment is at a “low” when you are trying to buy-in/purchase. And then it creates a sense of alertness to watch for the “right time” to sell. While this is perfectly correct mathematically and logically, it feeds the emotional knee-jerk reactions of being confident when a market or stock has been or is doing well (when in reality it might be at a “high” point), and causes anxieties and concerns which may drive one to sell when the stock/mutual fund is doing poorly (when it is more than likely at the “low”), thinking I better get out before I lose any more! So, yes; our heart tells us exactly the opposite of what our brain knows we should do.

Another issue with the adage is that it encourages people to “watch” and analyze their investments more often than is helpful. I’m not saying that keeping in touch with what is happening in the markets is bad. But for many folks, it’s usually better to have a once or twice a year review of your plan - with a three to five-year or longer focus and then leave it alone. Go back to focusing on your daily life – the family, work, and your hobbies. Don’t worry about the day-to-day drama that goes on within the bond and (especially) the stock markets. Quite frankly, the day-to-day stuff doesn’t really matter. Whether you are retiring next year, in five years, or in 25 years, the fact is that what happened yesterday or today are merely blips on the overall screen. One dramatic example: October 19, 1987, also known as “Black Monday”. Stock markets around the globe crashed; starting in Hong Kong, spreading through Europe, then hitting the US. The Dow Jones Industrial Average (DJIA, which at the time was considered the best indicator of what was happening in the overall US economy) dropped 508 points or 22.6%! One day! …ouch.

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Corrective for volatility in investments...

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However, for those who didn't panic (or maybe weren't paying attention) and stayed in their positions (didn't sell), the crazy drop that October was pretty much completely recovered by the end of that same year, just a few months later.

Generally, those who didn't focus only on the immediate issues at hand like short-term traders, but who looked at their accounts over a longer horizon, ended up being just fine. Most of them didn't panic (sell); they maintained the shares they owned. And those shares eventually recovered their previous values. In fact, those investors were then handsomely rewarded as we slid in to the "go-go" years of the '90's, a decade of fantastic growth. But those who had let their short-term concerns and anxieties rule found themselves selling out of positions (at lows), then standing on the sidelines not only missing out on the recovery of their positions, but typically not comfortable getting back in to the markets until they had seen some significant growth, finally feeling confident enough to buy back in (after significant gains had been missed).

Focusing on short-term gain is TRADING.

Looking at long-term growth is INVESTING.

As I mentioned, that was the most dramatic market crash/correction/pull-back. Most downturns (which have cyclically occurred throughout civilized history) happen and span a timeframe of anywhere from two to five years, the longest being the Great Depression (1929-1939). Market drops occur from time to time and will continue to do so. There will be more in the future, I don't know when, or how long they'll last. Rather than concentrating on the current market value of your long-term investments, I encourage people to focus on the number of shares they own while they're investing.

Which brings me to my final point. During your working years, invest all you can (i.e. acquiring as many shares as you can). When you buy "shares" of an investment, the value of our account depends on the number of shares you own times the value of those shares …that day. If you aren't selling today, it doesn't matter what the price (or overall value) is today. I'm not referring to money needed in the short-term. But what should be in the stock market is "long-term" funds. Market history has shown us that patience in steady investing will best serve us with long-term growth.

And for the plot-twist at the end: those who are investing during a market downturn can have the satisfaction of two things:

(1) We haven't lost any of the shares we previously purchased, and

(2) the new money that's going in is buying more of those shares at a lower price!

When the price per share recovers, we'll not only have the same value as before, but we'll be money ahead for all those shares we bought "on sale".

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