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How to Learn to Worry Less and Love a Market Correction

In the aftermath of the financial crisis, equities have been the go-to investment option for more than a decade now. We've been riding a high for so long, it's tough to remember the last time a market correction happened.

But now one has happened again.

We were due. Don't be alarmed. This could actually be good news for long-term investors—if everyone stays calm and has a plan.

A correction isn't a crash

A market correction is just what the name implies—a correction to a market that has shot too high. The drop may seem a bit frightening at first. With 2008 still fresh in investors' minds even after years of recovery, it's understandable why most of us would feel a tinge of apprehension. But don't panic.

A correction is a natural part of the market. It doesn't necessarily indicate that the market will nosedive into global financial crisis territory of 50% market losses. If losses begin to creep above 20%, we're no longer in a correction—we're entering a bear market.

Develop and stick to a sensible plan

Timing the market is not advisable. But that doesn't stop many investors from shifting their investments into cash in the hopes of addressing market downturns. Consequently, they miss some of the market's biggest gains while they sit on the sidelines. Rather than trying to time the market, investors should focus on time in the market, allowing investment returns to compound year after year.

Selling off stocks after they dip may leave you worse off than you would be if you remained invested. Don't sell just because others are selling. Quarterly returns may make the market appear volatile, but the market appears comparatively tranquil over a longer time period—an insight that may be forgotten amid short-term market swings. Long-term buy-and-hold investing may not be exciting, but it has historically been an effective strategy.

Key Points

- A market correction is just what the name implies—a correction to a market that has shot too high. It's a natural part of investing.
- Don't sell just because others are selling. Long-term buy-and-hold investing may not be exciting, but it has historically been an effective strategy.
- The market's cyclical nature is a fundamental truth investors need to keep in mind. A diversified portfolio consisting of a broad assortment of investments is intended for just such an occasion.

Be greedy when others are fearful

"The more [the market] goes down, the more I like to buy," investor Warren Buffett said as he bought stocks during a sell-off a few years ago.[1] Consider taking advantage of a correction and turn the risk of volatility into an opportunity to buy at a discount if this strategy fits in with your time horizon and risk profile. Picking up stocks at a lower price could be a great way for investors to gain new investment opportunities with greater growth potential.

FIGURE 1 shows the effects of two different historical approaches to volatility. Each assumes $10,000 invested on 12/31/77 into the S&P 500 Index[2] and no taxes or transaction costs. The opportunistic investor added $2,000 each time the market dropped 8% or more in a month, and the apprehensive investor shifted assets in the face of volatility. Ultimately, the opportunistic investor had a return that was significantly higher at the end of 2018.

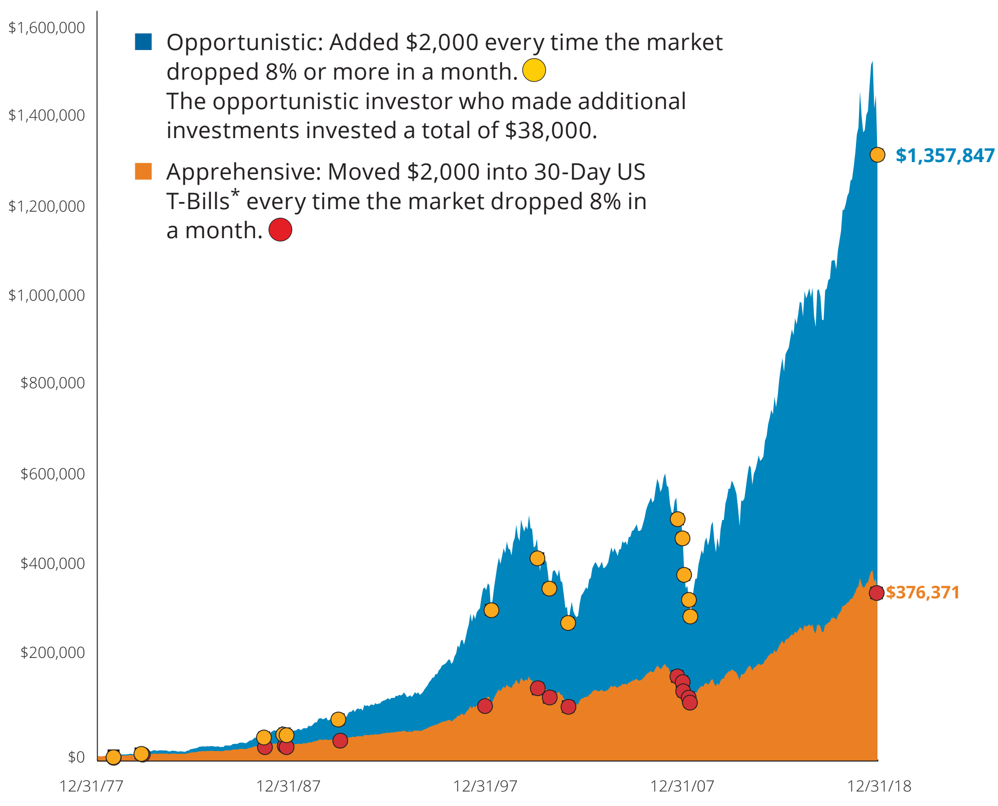
Failing to plan is planning to fail

Speak with your financial advisor to understand how you can position yourself now for a correction—and for the one after that whether it's next month, next year, or several years from now. The market's cyclical nature is a fundamental truth investors should keep in mind, and a diversified portfolio consisting of a broad assortment of investments is intended for just such an occasion.

FIGURE 1

An Opportunistic Investment Approach Has Historically Been Profitable

Hypothetical Growth of $10,000 Invested in S&P 500 Index (12/31/77-12/31/18)



Data Source: Thomson Reuters, 1/19; **INDEX PAST PERFORMANCE IS NOT A GUARANTEE OF FUTURE RESULTS.** Assumes reinvestment of capital gains and dividends and no taxes.

*T-Bills are guaranteed as to the timely payment of principal and interest by the US government and generally have lower risk-and-return than bonds and equity. Equity investments are subject to market volatility and have greater risk than T-Bills and other cash investments

[1] "Warren Buffett: I Bought Stocks in Wednesday's Big Selloff," CNBC, 10/14
[2] S&P 500 Index is a market capitalization-weighted price index composed of 500 widely held common stocks. The S&P 500 Index is unmanaged and unavailable for direct investment

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Important Risks: Investing involves risk, including the possible loss of principal. Diversification does not ensure a profit or protect against a loss in a declining market.

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