The New York Times

What Should You Do About a Falling Stock Market? Nothing

If you had a perfect ability to predict how far the market would fall and when it would bottom out, it would make sense to move money in and out. But you do not.

By Neil Irwin

Jan. 3, 2019

Millions of investors will receive year-end statements from their brokerages and retirement plan managers in the coming weeks, and the great majority of them will have unpleasant news: losses.

The S&P 500 finished the year down 6.2 percent, with the steepest declines recorded in the fourth quarter.

With Apple's announcement of disappointing sales in China on Wednesday, the bad times for stocks continued in the first week of the new year. While most economic data has remained strong, there are some rumblings that 2019 may be quite a bit rougher than 2018. Corporate executives are becoming more pessimistic, according to surveys, and Americans are conducting Google searches for the word "recession" at the highest rate since the last one just ended in 2009.

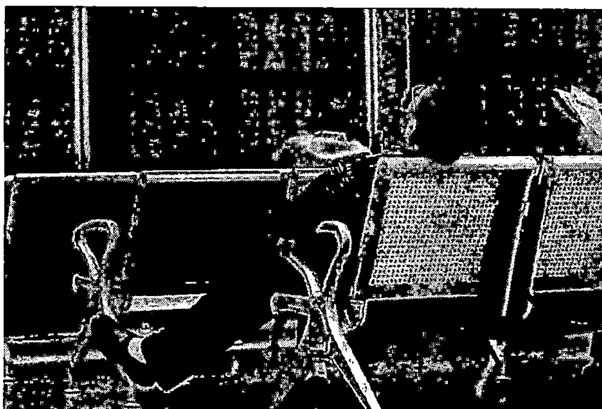
If it all makes you want to flee — or at least shift your 401(k) into cash — that's understandable. It's also a bad idea.

The sensible response to this unnerving series of developments is to do pretty much anything else. Read a book. Go for a walk. Take up knitting. Or just do nothing at all, like take a nap.

If you are a long-term investor (and any money you have tied up in the stock market should be intended for the long term to begin with), tumult like that of the last few months isn't something that should cause panic. Rather, it's the price you pay for enjoying returns that, over long time horizons, are likely to be substantially higher than those for cash or bonds.

ECONOMY *Here's a brief guide to what you should know about recessions.*

That's true if this episode turns out to be a false alarm for the overall economy, as is a distinct possibility. But it's also true even if this does turn out to be the start of a prolonged period of economic and market distress — especially if you are still in the phase of your life of contributing to a retirement plan or otherwise accumulating savings.



Napping at a brokerage office in Beijing in October.
Jason Lee/Reuters

The recent pessimistic tone in markets is getting way ahead of the evidence. Nothing so far in either the economic data or the market indicators that most reliably predict economic swings suggests there will be anything worse than a modest slowdown in economic growth in 2019.

Businesses are still expanding and adding jobs. The yield on two-year Treasury bonds has fallen in the last three months, but it would have fallen a lot more if the bond market — which tends to be closely tied to the direction of the overall economy — had been predicting an imminent recession.

Moreover, an investor who moved money into cash now would be doing so just as the valuation of stocks was becoming more favorable — buying high and selling low, not the way great fortunes are made. That's especially true when you factor in the drop in longer-term interest rates, which makes shares particularly appealing relative to bonds.

In early November, investing $100 in stocks would buy you about $4.64 worth of corporate earnings, versus the $3.21 in interest you would could receive by investing in 10-year Treasury bonds. Now, stocks offer $5.25, while bonds offer only $2.61.

But most important, even if the economic road ahead really is as bumpy as some in markets seem to fear, you're probably not going to be successful at timing those swings just right.

Of course, if you had a perfect ability to predict how far the market would fall and when it would bottom out, it would make sense to move money in and out. You do not.

There is a wide range of evidence that people are pitiful at timing the market. Even supposed investment experts lack that prescience.

Even if you turned out to be right about a continuing tumble in 2019, the great risk would be that whenever the rebound began, you would be caught out of position, unable to take advantage.

Suppose you were clever enough to recognize at the start of December 2007 that a major recession was about to take place, and you moved your money out of stocks.

Yes, you would have saved yourself from steep losses in 2008 and early 2009. But you have to ask yourself: Would I have also had the courage to put money back in while the economy was still in horrendous shape in 2009, with double-digit unemployment and a banking system in tatters?

If not then, when would you have moved money back in? People who simply left their savings fully invested in the stock market in December 2007 have now made a 134 percent return on that money. Would you have done better than that, or would you have missed out on a big chunk of those gains out of the same caution that led you to pull money out of stocks to begin with?

People who did not panic in the fall of 2008 — the most panic-worthy time in most of our lifetimes — and kept putting their retirement funds into stocks did indeed incur steep losses over the ensuing months. But their newly invested funds were being put into stocks at the most favorable valuations in a generation, and thus enjoyed the full benefit of the rebound when it eventually came.

A truism of economic and financial cycles is that by the time it feels like the coast is clear and putting money into riskier investments is completely safe, the real money has already been made. People who looked at the economic chaos of early 2009 and stuck to their guns have ended up far better off than those who, convinced that a double-dip downturn was imminent, waited for years to get in.

This equation changes, of course, if we're talking about money needed imminently as opposed to longer-term savings, such as for retirement. The economy looks stable now, but that could change — it's still possible that markets and C.E.O.s know something about the future that isn't clear in the data yet.

But that's more of a fundamental argument about how your assets should be allocated. If an 18 percent drop in stocks is enough to cause you to change your entire investment strategy, that money shouldn't have been in stocks to begin with.

The entire point of investing in stocks is that you get greater long-term expected returns in exchange for tolerating bigger ups and downs. Episodes like those of the last few weeks are, in effect, the price you pay for returns that are substantially higher than bonds or cash over longer periods.

Just as there are no free lunches, there are no excess returns without some volatility and risk.

As individual investors, we cannot control volatility. What we can control is our own mind-set and reaction, and the more level your head, the better your long-term results are likely to be.

Neil Irwin is a senior economics correspondent for The Upshot. He previously wrote for The Washington Post and is the author of "The Alchemists: Three Central Bankers and a World on Fire." @Neil_Irwin • Facebook

A version of this article appears in print on Jan. 3, 2019, on Page B1 of the New York edition with the headline: Left Agitated By Markets? Go Easy Now

READ 384 COMMENTS