BUSINESS

Road to Retirement: Lessons from the 10-year bull market

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April 7, 2019 at 6:00 am

The month of March marked the 10th anniversary of the bottom of the bear market that occurred during the mortgage-triggered financial crisis. In mid-March 2009, the S&P 500 hit a low of 676 points, and had
fallen about 57 percent from its previous high-water mark. That is the type of decline that makes people nauseated.

Yet despite that stomach-turning free fall, at the end of the first quarter of 2019, the S&P 500 stood at about 2,800. When you also include the dividends paid by the companies in the S&P 500, the total return for the U.S. stock market since the bottom in 2009 is about 400 percent. Given that in 2009 stock market investors were projecting the "end of the American wealth building machine," and today stock market investors are optimistically looking forward, what can you learn from this?


Photograph by Ellen Jaskol
Charlie Farrell

First, if you look at the history of financial markets, you'll see that massive swings in investor psychology are common. We go from "we'll all be rich" to "we'll all be poor" in a matter of a few short months. The reasons for the shifts are always a bit different, but what is consistent is the shift. We saw a mini-example of this last year. The S&P 500 sank 20 percent in a few weeks on a big shift in investor psychology at the end of 2018. And then it quickly pivoted again to optimism.

Now, if you are looking for a rational basis for these shifts, you won't find one. They don't make sense, but they are a reality. So instead of trying to figure out why investors do this, just accept that they do, and figure out how you are going to react to it.

No matter how many times we go through this, and how many articles are written about staying the course, many investors still sell during the downturns. That's why markets go down; investors are dumping their stocks. For those who bailed on the stock market in 2009, and there were many, they likely locked in big declines and then didn't get back into the market for many years — missing the bulk of the recovery.

For instance, if you had $100 in stocks in 2008, sold them for $50 at the bottom of the crisis in 2009, then waited until 2012 to get back in, you would only have about $130 today. If you had just left the money in the market, you would have had $245 today, or about 90 percent more money. Think about what sort of impact that could have on your retirement plans. If you simply stayed calm, you could have had a lot more money.

The main point I want to make is that while the market will continue to shift from periods of grand optimism to severe pessimism, the more accurate narrative is the “optimistic” one, not the pessimistic one. What I mean by that is the valuations we see in optimistic cycles have been more reflective of what the future holds than the pessimistic values we saw during panic phases.

Let’s go back to 2008. The S&P 500 was valued at about 1,500 points prior to the crisis, and then it fell to
675. So which one of these values was a more accurate assessment of what the future might hold, the optimistic or the pessimistic? Well, since we have 10 years of history to look at, it was the optimistic view. The market moved from 1,500 to 2,800. It didn’t move from 675 to 300. This is important to remember for the next time the market loses its footing.

Yet the fear that most investors experience during big market declines has the power to alter their commitment. Professional and lay investors alike fall victim to this all the time. So let me give you a few tips that might help the next time.

Make sure you are diversified. The easiest way to do this is to invest in something like a broad-based index fund designed to track the S&P 500.

Keep some safe money out of the stock market. Since market declines can last several years, I’d be sure to keep any money you might need in the next few years in things like savings accounts, CDs or high-quality Treasury bonds.

Don’t check your statements too often during a decline. You can get anchored on the valuation changes and then panic if you see your $100,000 fall to $60,000. If you just took a long nap of say three or four years, you’d likely miss all of it. So keep in mind that the value you see isn’t likely to be the value you have in a few years.

Have faith. At the end of the day, during a crisis, you have to have faith in America. I realize that may be difficult given our current news cycle and contentious political discourse. But instead of thinking about our politicians, think about your family members, co-workers, friends and neighbors. You probably like those folks, and they are out there working hard and trying to improve things. That’s the America you should focus on, because that’s the fundamental backbone of the economy and the markets.

You have to believe that the system bends but doesn’t break. If you don’t have this fundamental conviction about America, you probably won’t stick to the plan. Recall that the optimistic narrative has been the correct one.

Charlie Farrell is a CEO of Northstar Investment Advisors LLC, and guides the firm's investment philosophy. He is the author of "Your Money Ratios: 8 Simple Tools for Financial Security." This article is for information and education purposes only. It does not constitute investment, tax or legal advice.

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