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Don’t let emotions upset a steady savings and retirement strategy

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Emotions and retirement savings don’t mix very well. We are hardwired to flee from current danger giving little weight to the future.

In a matter of a few weeks, we’ve gone from a veritable economic nirvana and record-high stock prices to the fastest bear market in history and a U.S. economy seemingly on life support. It’s no wonder people are panicking.

Before you take any significant and potentially irreversible actions regarding your retirement savings, you should pause and ask some important questions.

Evaluate short-term need for cash

Retirement investing is by definition a long-term exercise. You accumulate assets over a roughly 45-year working career with the hope of spending it over the next 20 or 30 years in retirement. Throughout this multidecade period, you should expect numerous stock market corrections and job changes. The key to achieving retirement plan investing success is to maintain a steady savings and investing strategy.

After a market decline like this one, the only assets you should be considering moving to cash are assets you absolutely need within the next two years. If your time horizon is longer than two years, you have assets outside your plan you can use or you have access to a short-term credit facility, like a home equity line of credit, the odds are very good that waiting to sell will put you further ahead than selling now.

It’s also worth noting that in the 32 years data has been collected, March was the third-highest month on record for insider buying, according to the Washington Service, a group that tracks this activity. In the month that just ended, more than 2,800 executives and directors of public companies purchased more than $1.19 billion of their own company’s stock. Do you really want to be selling when the people with the deepest understanding of the value of company stock are feverishly buying?

Reflect on personal risk tolerance

The unforeseeable and stunningly rapid collapse of an 11-year bull market is a chilling reminder of investment risk. Now is an ideal time to reevaluate your personal risk tolerance. There’s nothing like watching one-third of your account balance evaporate in just a few weeks to test your comfort level with risk.

If the past few weeks caused you to lose sleep over your losses, which is certainly not an irrational reaction, you should consider yourself a risk-averse person. If, on the other hand, the massive sell-off has you looking for ways to invest more at these discounted prices, you have the entrepreneurial spirit of a risk-taker.

Neither approach is correct per se, they are just different. Now is an ideal point in time for self-reflection and improved understanding. When you have the opportunity, ask an investment professional if your investment strategy is properly aligned with your actual risk tolerance.

Time to rebalance

For most long-term investors, market sell-offs like this one present an excellent opportunity to rebalance your portfolio. Rebalancing is the simple act of buying more of what went down (stocks) by selling what has been outperforming (bonds). In doing so, you bring your total portfolio back into its preferred long-term allocation between stocks and bonds. This has the same effect of investing new money into the stock market at reduced prices and should accelerate your recovery.

CARES Act

On March 27, the CARES Act was signed into law. This law clears the way for millions of Americans affected by the COVID-19 outbreak to withdraw up to $100,000 from their 401(k) account, free from the normal 10 percent early withdrawal penalty and allows you to stretch the normal income taxes owed over a three-year period.

The law also increases the maximum allowed loan amount from $50,000 to $100,000 in order to help folks deal with a temporary loss of income due to the coronavirus. Thousands are likely to take advantage of the federal government’s short-term window to withdraw money from their retirement accounts.

Recognizing some may have no other choice, understand pulling this trigger could be catastrophic to your financial security at retirement. Think long and hard about other sources of short-term funds before you dig into your retirement savings. What you withdraw not only reduces your retirement balance today, it also eliminates the compound earnings these dollars will generate. For example, $100,000 withdrawn today would also cost a 45-year-old more than $286,000 in compound earnings by the time she turned 65, assuming a 7 percent average annual rate of return.

We live in a time of great uncertainty with emotions running high. Rise above your emotions and take the time to consider the long-term consequences of any action you take in the next few months. Your 65-year-old self will thank you.

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