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Embrace basics in uncertain times

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Most of us are not interested in holding down a job into our 80s, and nobody wants to be a financial burden on others, yet far too many people experience one or both of these fates because they fail to properly save for retirement.

The most frequent investment question 401(k) participants are asking these days is about the upcoming U.S. presidential election and its effect on the financial markets. Fears of a prolonged vote count or a delayed decision, along with the potential significance of this election on future U.S. tax, health care, environmental policy and now the vacancy on the U.S. Supreme Court, understandably places a lot of investors on edge.

If that's you, you are not alone.

According to JPMorgan, the bond-futures market, the dominion of sophisticated institutional investors, is prepping for this election as one of the biggest risk events of the past decade.

2020 election

History provides some interesting clues about the fate of an incumbent president. Interestingly, a simple stock market return calculation has routinely coincided with the winner since 1936. According to Capital Group, one of the world's largest asset managers, if the S&P 500 Index is positive for the 90 days before the election (Aug. 3 — Nov. 3) the incumbent party has won 87% of the time. As of Oct. 14, the S&P 500 is up 5.9% since Aug. 3. Clearly, the gains of today could go negative.

You have been here before

This isn't the first time, and certainly not the last, you will be faced with the age-old dilemma about what to do when you are staring down the barrel of an event that profoundly influences your retirement savings. Your contemplation is understandable. Your mettle as an investor has been battle-tested as the S&P 500 fell 35% in less than a month this past March, and a 19% decline was endured during the fourth quarter of 2018.

Think fundamentals

When investing for your retirement, your goal is to generate the highest rate of return commensurate with the time horizon for the investment and your willingness to accept risk. If your time horizon is short, say less than five years, you should not take as much risk as a person with a 10-year horizon, and your expectations about upside return need to be reduced.

How do you know if you have taken on too much risk? Candidly, if you find yourself routinely getting angry at losses, losing sleep at night or looking back at past decisions where you sold at market lows and missed out on the upside in a market rebound, it's time to rethink your strategy. Your mind, sleep patterns and pocketbook are more likely than not to benefit from a disciplined approach.

Benefits of investment discipline

A core discipline exercised by successful investors is portfolio rebalancing. 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 discipline invests new money into the stock market at reduced prices and accelerates your recovery when prices rebound. For example, when the market surged both in early 2019 and the second quarter of 2020, a rebalanced portfolio enjoyed the ride higher.

Consider using professional management

For most 401(k) investors though, watching an investment account go up and down and taking action when the time is right, is not something they feel called to do. Therefore, your plan's target-date fund or balanced-fund alternative may be the better solution. By investing in these types of funds, you turn over the investment decisions to a professional investment manager. With target-date funds, you not only have the pros deciding when to take more or less market risk because of prevailing economic and political conditions, but also deciding when to take less risk because of your proximity to retirement.

Successful 401(k) investing is all about having a plan and sticking to it. We speak to many retirement plan participants, and it's hard to convince them to look long term regardless of current events.

The power of human nature to flee from perceived danger rears itself time and again leading some to decisions they may later regret. Our best advice is to pick a strategy, and stick with it. If you can't do that, hand the reins over to the pros, and let them make the calls for you.

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