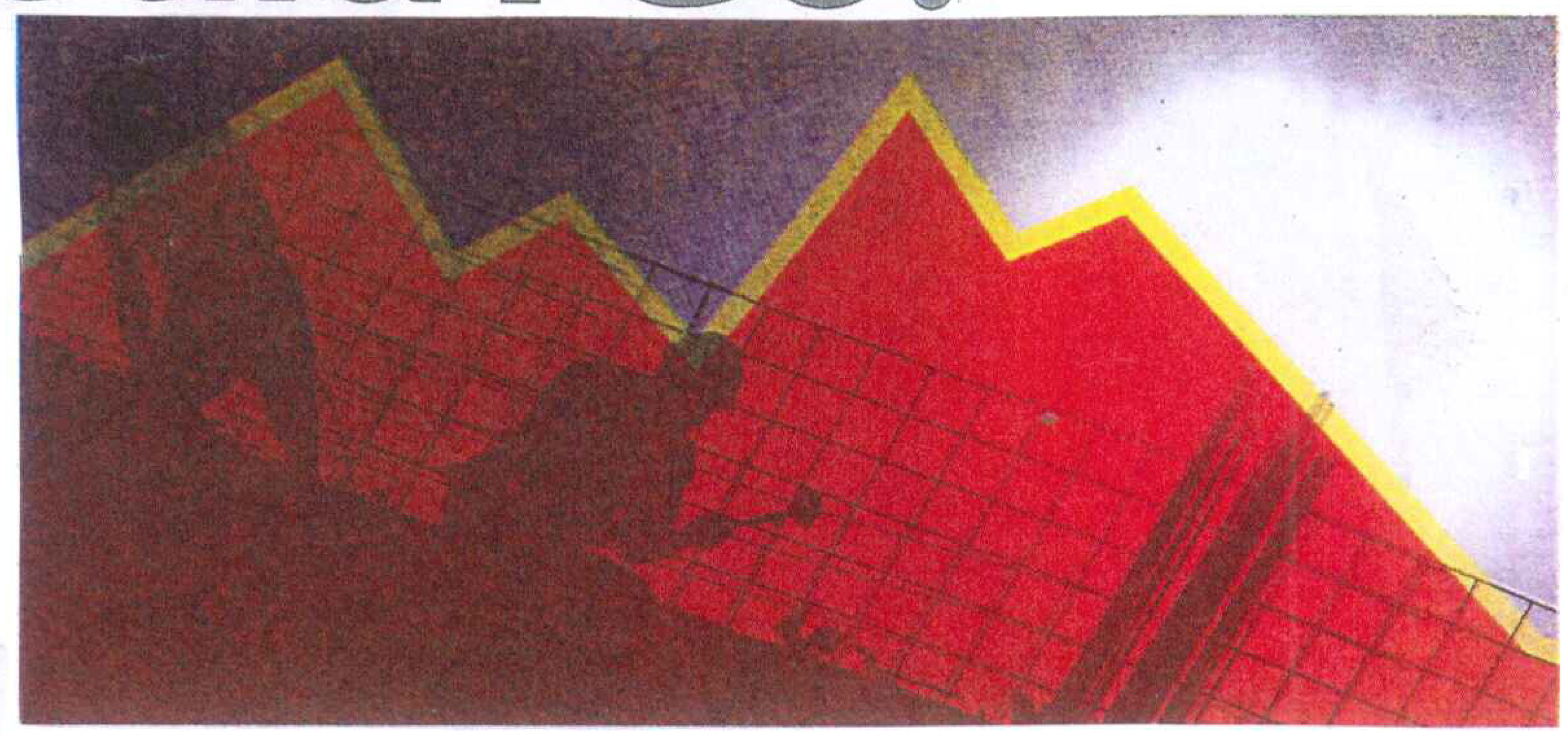
Should I Stay or Should I Go?

How should investors react in times of uncertainty? Colin Bloodworth explains the arguments to sell, hold and buy



Should you buy, sell or hold? The answer: it depends. You have three choices; what is right for you will depend on necessity, cash flow, time span of your investments, age of retirement, overall investment strategy, appetite for risk and a host of other considerations.

Let's consider the factors that could determine your action after seeing a big drop in the value of your savings, which may well be the case right now as the euro zone crisis plays out.

Reasons to sell

1. There is a strong likelihood that market conditions will get much worse. The problem is that you may be overly influenced by media reports, which tend to focus on bad news. Remember that when you hear there has been a big sell-off those who have already sold will have obtained a higher price than you are going to achieve.
2. You are in dire need of cash. This may indicate you have not maintained adequate cash reserves and should not have been investing in stocks in the first place. Many people who are tired of the poor returns on cash in the bank are tempted by the higher returns available in the capital markets, particularly when they see the markets doing well. Unfortunately, it is often the case that smaller investors move in too late and lose money. If this has happened to you, just put it down to experience. You will be in good company; even big banks ran out of cash in 2008 and the situation could be about to repeat itself in southern Europe.
3. You want peace of mind. Investors are often driven by greed or fear rather than logic. It is human nature and requires a lot of discipline to overcome. But if at the end of the day your stock market investments are causing loss of sleep it may be better to leave the playing field and seek lower returns with less risk. Not the best way to get rich but wealth-building means risk-taking and it's not everyone's cup of tea.

One point worthy of note is that stock market investments, including managed funds, are generally liquid and can be turned into cash fairly quickly. This is not the case with real estate, which could take years to turn into cash. In times of need, access to cash, even if it means taking a loss, can be more important than holding valuable but unsalable assets.

Reasons to hold

1. You see stock market investing as a long term strategy and are aware of the ups and downs that will always be a feature of the markets. You have adequate cash reserves and see no reason to cash-in long term holdings, no matter how bad the news may appear.
2. You may be thinking of buying or selling but wish to keep your options open a bit longer.
3. Under no circumstances do you wish to realize a loss, so you are determined to hang in no matter how long it takes for your investments to recover their losses.

As with property, a gain is not a gain and a loss is not a loss unless you sell.

Reasons to buy

1. You see the big dip in the markets as a buying opportunity. After a market crash, few step in, but very often the people who do turn out to be the most successful investors. If we look back to March 2009, for example, confidence in the markets was extremely low, yet a glimmer of hope that the worst was over drove the markets back up in a very short time. Few people may be aware that the S&P 500 index rose 100 percent between then and July 2010. Shrewd investors who invested in the markets in March 2009 and sold in July 2010 would have doubled their money. Of course, getting the timing right is not so easy but the above example shows what opportunities exist when markets are down. It also shows the folly of selling at the wrong time. Another point to bear in mind is that it takes a 100 percent gain to recover from a 50 percent loss!
2. You wish to rebalance your portfolio. Let's imagine you have constructed a carefully balanced portfolio consisting of cash, stocks, bonds, commodities, property and alternative investments. Let's say the stock market element represents 40 percent of the portfolio. If the market suffers a loss that percentage will be reduced, assuming other assets in the portfolio have not lost a similar or greater amount. It will therefore be necessary to sell part of the other assets and reinvest in the stock market element to bring it back to 40 percent.

> **"When you have investments in a market that is crashing and you don't bat an eyelid, the chances are you are on the right path**

Don't make emotion-charged decisions

It is easier said than done, but when it comes to investing, we are like a bunch of lemmings. How many rushed for a piece of the Facebook action with expectations of doubling their money? Remember the scramble to buy technology stocks in the late '90s? One of the world's shrewdest investors, Warren Buffett, was buying shares in paint companies at the time.

When you have investments in a market that is crashing and you don't bat an eyelid, the chances are you are on the right path.

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