Debunking 3 Investor Myths on Volatility

When the market has one of its sharp downturns, it's easy to think that switching to a conservative asset allocation strategy is the way to ensure your money is available when you are ready to retire. But when you think about what's important for retirement savings – inflation protection and continued growth – you may be surprised that "low-risk" strategies might put your retirement at risk.

Here are three myths about going too "low-risk" in response to volatility:

MYTH #1: "INVESTING CONSERVATIVELY PROTECTS MY SAVINGS"

It's true that conservative investments may weather the market's downside better than many aggressive strategies. But going too conservative or taking your money out of the market also comes with important risks. If conservative investments may limit the downside, they may also limit the upside. In other words, you may be limiting your growth potential, and the decades of market compounding that may benefit younger investors. Another thing to keep in mind is that if your return is less than the rate of inflation, the purchasing power of your savings may be much lower a decade or two into retirement.

MYTH #2: "VOLATILITY IS A BAD THING"

No one likes volatility, but riding out the ups and downs in the stock market is a price many investors are willing to pay for potentially higher returns – returns you may need on the path toward retirement readiness. Keep in mind that volatility often feels worse in the short-term. The further the horizon for your investment objectives, the less you need to worry about day to day, or even month to month volatility. If the market's swing really bothers you, consider picking a quality investment with an appropriate balance of growth and downside protection, then try to avoid logging into your account every day.

MYTH #3: "I'M READY TO RETIRE, SO IT'S TIME TO GO LOW RISK TO PROTECT MY ASSETS"

Certainly a 65-year-old with a lifetime of savings who's ready to start retirement should probably have less risk in their portfolio than a 25-year-old with little cash and a lifetime of earnings ahead of them. It's quite likely that you may live two or three decades after you retire. Investing too conservatively, even on Retirement Day 1, could mean giving up the growth you'll want to meet long-term goals. Retirement planning today is about boosting the odds that you can close the retirement income gap between what you have now and what you want to have later. Being too conservative can be just as significant a problem as being too aggressive.

IN SUMMARY: YOU CAN'T CONTROL THE MARKET, BUT YOU CAN CONTROL YOUR ACTIONS

Your 401(k) plan is one of the most important savings vehicles you have. Saving as much as you can manage, having a plan, and choosing an appropriate investment are all under your control. A well-diversified retirement portfolio may have stocks for growth and a fixed income position to hedge in the event of an equity market sell-off. Remember that being heavily weighted in bonds is a common strategy reserved for investors nearing or in retirement to protect their savings and generate income.

And sticking with your retirement plan is also critical. Also remember that market gains are often made and lost in just a few trading days out of the entire year. If you are transferring your assets into safe havens and miss the bounce back from a down market, your annual return may be much less than someone who stayed the course with a diversified portfolio.

More conservative assets may have a role to play in your retirement. But when you think about the decades of retirement spending ahead of you and the growth you may need, you may want to think twice about the cost of staying out of the market.

Investing involves risk, including loss of principal.

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