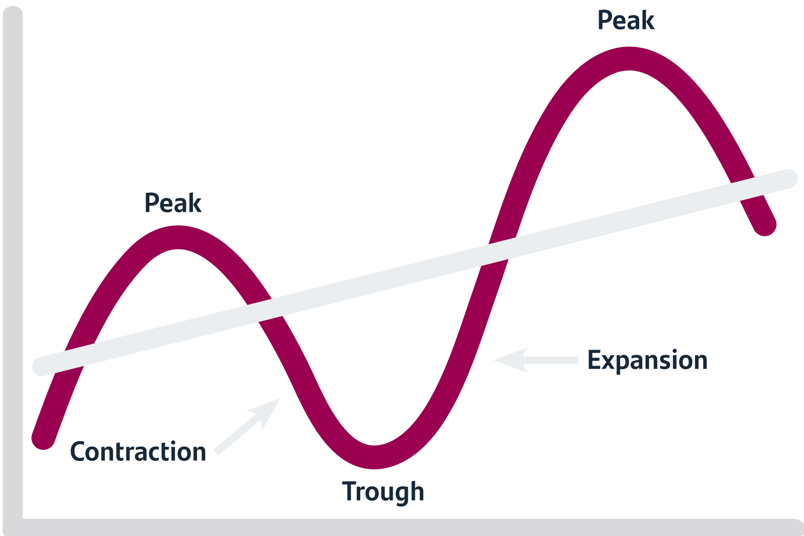
Principles of Investing

Downturns bring opportunity

The COVID-19 pandemic had serious knock-on implications for the global economy that have since been exacerbated by the war in Ukraine and the effects of inflation rising around the world.

Hearing about economic downturns, whatever triggers them, and watching investment markets go down in the process, can be unsettling for investors. But it's all part of an established cycle and can also bring opportunities.

The economic cycle



Past performance is not a guide to future performance, but this established cycle does suggest we can be confident that recovery will eventually follow any downturn, no matter how severe it may seem at the time.

Recoveries from recent history

The MSCI World Index represents shares from all over the world. It fell by more than 30% between May 2008 and February 2009, as a result of the global financial crisis, before bouncing back by more than 40% by the end of 2009.[1] This started a 'bull run' that then saw share markets on a broadly rising path until COVID-19 hit in 2020.[1] Another strong recovery for markets followed the initial, sharp COVID-19 dip until they began to fall back again in early 2022 on the back of the war in Ukraine and inflation related woes.[1]

The S&P 500 Index measures the performance of the 500 largest companies in America. It returned growth of 2.03% in 1987, the year of the Black Monday crash (19 October) compared to 14.62% in 1986.[2] After the crash it bounced back to 12.40% growth the following year and 27.25% in 1989.[2]

Understanding the downsides and upsides

We have a powerful natural instinct to protect ourselves from harm, to flee from what we see as a threat. When markets are going down your instinct may be to encash part, or all, of your investment. But here is some food for thought.

While there may be personal circumstances which mean it's the best course of action for you, selling investments when markets are low can mean you end up with less than you put in. It can also mean you miss out on recovery when it comes, making it tougher to build your funds back up. Especially when savings rates are at historic lows.

When investment prices fall, sometimes it is possible to invest and take advantage of the downturn in market values. Whilst investment prices may fall further from this point, over the longer-term, when markets eventually recover, your additional investment can add to your overall investment return. Clearly, the value of your investments will vary depending on the timing of encashment, whether this be part or all of your portfolio. You may still not get back all of your original investment if market values do not recover in time.

A benefit of regular investing

If you invest regularly you will naturally buy investments at different times and at different prices. When prices are lower your money will buy more units. When they are higher it will buy fewer. Over time this can help to smooth out the impact of market ups and downs on the returns you are able to achieve. Regular investing can benefit from the term referred to as pound cost averaging.

[1] FE Analytics, 22 July 2022
[2] Macrotrends, 22 July 2022

Do I need to take action?

It may be more a case of whether you want to take action. When markets are lower it can be a good time to review your balance of savings versus investment. But whether to invest more will depend on your personal circumstances and won't be the right thing for everyone. A financial adviser can help you to work things out.

Explore the other principles of investing

To cut through the noise and understand the principles of investing, visit our website **here** where you can watch or read about them.

Asset Management

Let's be clear!

Investment terms explained

Bull - a bull market is a positive one, with prices rising and money flowing in from investors. A 'bullish' investor is one who feels confident about markets.

Index: A way of tracking the overall performance of a basket of individual investments of a similar type. For example, the FTSE 100 index tracks the performance of shares in the 100 largest companies by market value on the London Stock Exchange.

Inflation: Measures the increase in price of selected goods and services in an economy over a period of time.

Pound cost averaging: Investing relatively small amounts regularly. By spreading out the investment, investors avoid buying at a single price meaning the level at which they invest in the market is averaged out.

Shares (often referred to as equities or stocks): In investing, this is a share of ownership in a company. Investing in a fund gives exposure to underlying share prices without investors actually owning the shares themselves.