Investing during a crisis: What to do when your stock investment is falling

We know how it feels to see your investment dropping in value day after day. With every drop comes a skip in your heartbeat and you begin you wonder if you made the right decision to invest in the first place. And we care – that is why we want to share with you what can help you navigate those difficult times.

Especially if you invest in stocks, you are bound to experience high and low moments with the stock. And as with many investors, you invest because you seek to make a gain on your money…. and in the shortest possible time. So, what do you do when this does not seem to be happening? Most investors will naturally sell their shares or disinvest completely. But is this really the best decision to make? In this article, we will explain why it may not be a good idea to do what feels natural in a time of crisis.

You do not actually lose money until you disinvest

In investing, two concepts are often distinguished: paper loss and actual loss. Paper loss is the fall in value that you see in your investment whenever the share price reduces. This loss is seen as "paper" and not real as the money is not actually in your hands. It only becomes an actual loss when the money now moves from the investment account into your hands.

And so what?

This difference is important because it means you won't actually lose money until you withdraw. The investment that you see dropping today could rise tomorrow if the stock picks up and your paper loss can easily turn into paper gain. In other words, if you are patient enough, you could gain back all that you have lost, and that "paper" loss never actualizes into a loss for you.

What you must never do – Time the Market

Investors in equity are known for adopting strategies for when to enter and exit a particular market or equity investment. Timing the market is an investment strategy for exiting the market when it's high and reentering when it's low. It can also refer to selling your shares when prices fall and waiting to reinvest when the market picks up. Many investors, unfortunately, adopt this as their method of making the most out of the market because it sounds very smart.

However, this move may not always be beneficial as the equity market is highly unpredictable. It is very difficult to predict when a stock will fall or rise because it depends on many factors, including investor tendencies. What many investors end up with, rather, is reentering after the stock has made its best returns. They lose all the returns they would have made if they had just left their investment lying there.

What you can do

Wait it out: According to Warren Buffet, "the stock market is a device for transferring money from the impatient to the patient." A good solution for you to consider is to hold on to the investment you have made (without necessarily adding more to it) and leave it to endure the highs and lows of the stock. Eventually, as history has proven, your money is more likely to grow over the long term than make losses. To date, every significant market fall has been followed by a rebound. We anticipate downturns; we just can't predict how low the market will go or when it will bounce back.

Diversify: Another method you could also adopt is to diversify your investment portfolio if the drop in equity persists. Instead of completely disinvesting, you could decide to now buy more fixed-income securities (bonds or bills). This allows you to still keep investing your money. You can readjust your portfolio whenever you think you are comfortable with investing in equities again.

Although this may not be possible if you are investing in a mutual fund (because you do not determine the asset allocation), you can consider now channeling new deposits into a mutual fund that has more fixed-income than equities as you leave your current investment in the equity mutual fund. (At Databank, our fixed-income funds are MFund and EdIFund Tier 1. You can switch to these funds if you are no longer comfortable with returns in Epack, ArkFund, EdIFund Tier 2 and/or BFund because of their equity component.

Buy more: It doesn't look like the logical response to such a situation, but it could actually be a good way to make more on the returns. A fall in share price means the shares are cheaper. This also means that the number of shares you can buy has also increased. And this becomes good news should the stock rise again. If the share price was GHC 2.00 and you invested GHC 200, you would own 100 shares in the investment. But if the share price reduced to GHC 1.00 and you invested the same GHC 200, you would rather own 200 shares. Now imagine the fund started picking up again and the share price moved to GHC 5, your 200 shares (GHC 200) would now be valued at GHC 1,000 compared to GHC 500 if you had been able to purchase only 100 shares.

It is for this reason in investing, you are encouraged to buy low and sell high – and not the other way around.

Keep calm

No decision should be made when you are panicking – whether it is what to say or where to invest. If need be, go back to the drawing board. Assess your investment goals, time horizon and risk tolerance. Determine what is good for you based on your assessment and advice from your licensed financial advisor. Then you can decide if you would like to wait it out, diversify or buy more.

So, in this current crisis, what will you do?