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He Retired the Week the Dow Slid 12%. Consider It a Wake-Up Call to Check Your Portfolio.

By Gail MarksJarvis Updated March 9, 2020 / Original March 6, 2020

Illustration by Sally Deng

Tracy Donaldson, of Orlando, Fla., had an inauspicious start to retirement. The Dow Jones Industrial Average plunged 12% in the week he retired.

"This is very disconcerting and very bad timing," says Donaldson, 66 years old, who retired on Feb. 28 after a 38-year career at Walt Disney in travel and logistics coordination. "I decided not to look at my investments so I wouldn't be depressed and upset."

Donaldson's financial advisor, Dennis Nolte of Seacoast Investment Services, says he plans to reassure the retiree during an upcoming planning lunch that he will be fine even if the coronavirus-driven market correction of the past few weeks turns into a bear market where stocks are down 20% or more. Donaldson has a guaranteed pension from Disney, along with Social Security. Even in a lengthy downturn, Donaldson will be able to cover his living expenses with that income without touching his retirement account until it recovers.

But Nolte and other financial advisors say that many retirees could be in a more fragile position in a bear market because they don't have Donaldson's guaranteed income. Companies have largely ended "defined benefit" pensions in recent years in favor of "defined-contribution" plans like 401(k)s. What's more, the market disruption comes after an 11-year bull market that has inflated Americans' retirement savings—401(k) millionaires, anyone?—and left many wrong-footed.

> "Now, people want to know if this is the next bear market. I don't think so, but you never know. Do a gut check and make sure you have a good quality portfolio now. "
>
> — Scott Bishop, financial planner at STA Wealth Management

A recent Vanguard Group survey of 44,000 do-it-yourself investors, for instance, found that many had become more exposed to risks in the stock market during the bull run than they might have intended or that were appropriate for their proximity to retirement. On average, the survey found, investors were far short of the bond allocations that usually help cushion portfolios from sharp losses. The average bond allocation was 23%.

"During the bull market, they just let money run," says Steve Utkus, director of the Vanguard Center for Investor Research.

Advisors frequently recommend that people on the verge of retiring establish portfolios that are invested 60% in stocks and 40% in bonds (or 50/50 for more-conservative investors) to help weather stock market downturns. The idea is to mitigate "sequence of return risk," or the risk that a long stock market plunge early in retirement could derail long-term income potential and exhaust savings while still needed to cover bills later in retirement.

To keep that risk from striking retirement savings, advisors typically review portfolios each year and move money from overinflated stock portfolios into bonds. But Utkus says he thinks many individuals have been inattentive while the S&P 500 index climbed about 400% during the bull market.

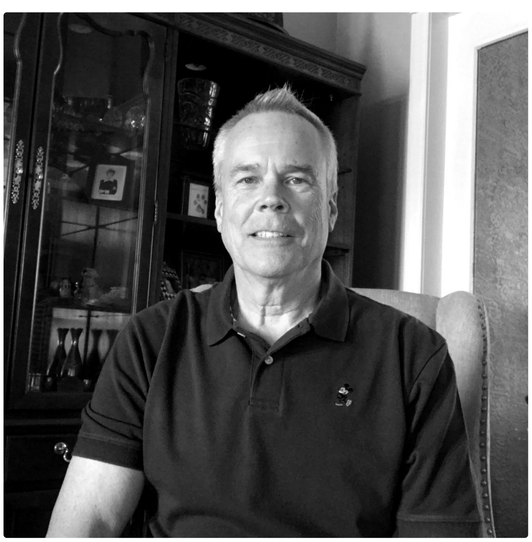
Analysts are now debating whether the recent correction will turn into a bear market. Some have emphasized that the coronavirus impact on the economy is likely to be less severe and less prolonged than the recession that left the stock market down 57% on the morning of March 9, 2009, when the bull run began. Yet the uncertainty and market volatility in recent weeks have been reminiscent of October 2008 in the financial crisis, and they are a reminder to investors that the gains they cherish in 401(k) and retirement accounts aren't necessarily for keeps.

"It's really easy to talk about the ability to take on risks when the market is up 30% like last year," says Nick Hofer of Boston Family Advisors. "But all of us lived through 2008, and that's still on people's minds."

Now that the fear of the coronavirus has delivered a fresh reminder that stocks can plunge unexpectedly, investors who have been taking excessive risks should try to use a market rebound to make adjustments, says Scott Bishop, a Houston financial planner with STA Wealth Management. "This has been a good gut check, and people should not ignore it when they are feeling better."

While it is never clear at the outset whether a correction will heal or turn into a sharper decline, bear markets occur about every five years on average, according to research by Leuthold Group. The median bear lasts 18 months and inflicts a 30% loss.

Rallies like Monday's or Wednesday's quadruple-digit run-ups in the Dow industrials are opportunities to move some money into bonds and cash. If people are in retirement and would need to sell stocks to cover living expenses during any bear market, they should be cutting back on some stock exposure so they are prepared for the next downturn—whether it comes now or at some point in the future, Bishop said.



Financial advisors emphasize that the time to whittle stock allocations is when investors are feeling good rather than when they are already suffering losses. Some advisors ask their clients each year to envision a recurrence of the 2007-09 bear market so the person can make sure that their investments aren't too aggressive for their risk tolerance.

When Tracy Donaldson of Orlando, Fla., retired on Feb. 28, he did so as the 11-year bull market entered correction territory. ‘I decided not to look at my investments so I wouldn’t be depressed and upset,’ he says.
Courtesy of Tracy Donaldson

For example, while an all-stock portfolio may have been terrifying as the last bear market turned $10,000 invested in September 2007 into less than $5,000 by March 2009, according to Morningstar, other mixtures were less alarming. In a simple 60/40 portfolio of the S&P 500 and long-term government bonds, an original $10,000 would have turned into $7,817. In a 50/50 portfolio, an original $10,000 would have turned into $8,479 at the market’s nadir.

By April 2010—only about a year after the low point in the bear market—the 50/50 portfolio would have been back to even, and the 60/40 portfolio would have recovered about four months later, according to Morningstar. For an investor who let his or her portfolio allocation move to 80/20 just before the bear market began, it wouldn’t have returned to even until November 2011. Fast forward to the end of this past January: $10,000 that was invested in a 50/50 portfolio in September 2007 was worth $25,720. The 60/40 portfolio had climbed to $26,273, and the 80/20 was at $27,380.

“Now, people want to know if this is the next bear market,” Bishop says. “I don’t think so, but you never know. Do a gut check and make sure you have a good quality portfolio now.”

Corrections & Amplifications
Steve Utkus is the director of the Vanguard Center for Investor Research. An earlier version of this article incorrectly spelled his surname.

Questions? Comments? Write to us at retirement@barrons.com