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Business

STRATEGIES | JEFF SOMMER

Yes, Buy Stocks, but Watch Your Step

T. M. DETWILER

Though this is not the moment for quick profits, taking the long view can reap rewards.

IN THE MIDDLE of another gut-wrenching day in the financial markets, I received a startling note.

It came from FPA Crescent, a mutual fund with an excellent track record, and it said that while the market had been falling, the fund had begun buying stock. It said the managers intended to buy more if prices fell further.

This apparent courage when so many traders were panicking seemed noteworthy, so I got on the phone with Steven Romick, one of the FPA Crescent managers, who was riding out the coronavirus storm at his home in Los Angeles. He said the fund was acting rationally and not particularly bravely.

He explained his reasoning succinctly: "We're investing for five to seven years from now, and the prices of many good stocks are obviously a lot better now than they were a few weeks ago." But his fund is still buying gingerly because while the market may be cheaper, he said, it still isn't cheap. "When we think it is, we'll really jump in," he said.

The fund has been holding a lot of cash — 36 percent of its assets on Dec. 31 — reflecting a view that the market has been overpriced. But now, Mr. Romick said, it is reasonable to nibble carefully at some of the better pickings, knowing full well that doing so involves short-term risk if the markets drop more.

"You shouldn't be in the market at all if you can't handle something like this," Mr. Romick said. But if you can afford to take a long view while buying at these lower prices, he said, you can reap greater rewards.

As he talked, I realized that I — and millions of other people — are implicitly endorsing this view. We have been buying stocks and bonds in mutual funds through workplace retirement accounts, even though falling prices mean we have been losing a lot of money lately.

That's painful, whenever I think about it, so I try not to focus on the losses. If I need that money to live on before prices rebound — as I expect they eventually will — I'll regret those losses. But I'm betting that won't happen.

In fact, Mr. Romick's comments reminded me that there is a positive side to falling prices for people who continue to be regular buyers. By investing regularly with every paycheck, I'm getting better prices now than I did a couple of months ago. What's more, the average price I'm paying for long-held mutual funds is dropping. (That's what the asset management trade calls "dollar cost averaging.")

Assuming I can hang in long enough for the markets to recover, as I did during the last financial crisis more than a decade ago, my long-term returns will be better because of these lower-priced purchases.

But don't get me wrong. Buying now is not a prudent short-term bet. And Mr. Romick emphasized that it would be foolish to buy in this market with the expectation of making a quick profit. To the contrary, he said, he has no idea where the stock market is heading over, say, the next three months, except: "I expect that there will be a lot more pain, unfortunately."

With that in mind, Mr. Romick suggested a thought exercise. Imagine that the stock market, with all its lurches and false signals, won't even exist for those three months. "The question then is: When the market comes back three months from now, what should I have in my portfolio that I'll want there for the next five to seven years?" he said "We're making investments with that kind of horizon in mind."

Nibble carefully at some of the stock market's better pickings.

With its long view, the FPA Crescent fund has become more bullish now that we're in a bear market, the fund's data suggests. Its net allocation to stock on Feb. 19 — the peak for the S&P 500 — was 57 percent. By March 13, it had risen to 67 percent. In that same stretch, the S&P 500 declined 20 percent, according to FactSet. In other words, the overall market represented by that index became 20 percent cheaper. (The bad news, or the good, depending on whether you are buying or selling, is that it has become cheaper still.)

Unlike index fund investors — and I am one — Mr. Romick isn't putting money into the entire stock market. Instead, he buys individual stocks. Citing regulatory constraints, he would not disclose his most recent purchases. But he cited Alphabet, the parent of Google, and the American International Group as longtime portfolio holdings that are even more appealing now that they're being pounded.

Google relies on advertising for the bulk of its revenue, worrying some investors in this environment, and A.I.G., a global insurance group that was bailed out in the last financial crisis, will face insurance losses connected to the coronavirus, Mr. Romick said. He is confident that both stocks will continue to be profitable for his fund, however, even if their prices fall further in the next few months.

Still, he's not recommending that ordinary people jump into stocks in a big way right now.

Others are even more emphatic. For example, Richard Bernstein, a former Merrill Lynch strategist who now runs his own firm, said he thought investors were still barely coming to grips with the reality of a bear market. That's not surprising, he said, because a falling market typically has three important phases.

In the first phase, he said, people tend to say things like: "The worst is over. There are bargains out there. I've got to jump in." The second is: "No, this is worse than anybody ever imagined." Right now, he said, people are probably teetering between these two attitudes.

The last phase is: "This will never end. It's hopeless." That's when you want to be fully invested in stocks, Mr. Bernstein said, and when there are easy profits. It happened in March 2009, when the market began to take off, yet few people believed it.

"It will happen again," he said, "even with the coronavirus, but we're not there yet."

James W. Paulsen, chief investment strategist of the Leuthold Group in Minneapolis, put it this way: He's not confident about where the market will be in three months, is a bit more comfortable with a six-month horizon and is "very confident about a year from now."

With the caveat that the coronavirus adds a dimension of uncertainty that he can't really assess, he said, "I think it's highly likely that in one year, the stock market will be higher than it is today."

I'm not that confident. Still, I fully expect the market will be higher at some point. And so I expect to keep buying.

Jeff Sommer writes Strategies, a column on markets, finance and the economy. He also edits business news. Previously, he was a national editor. At Newsday, he was the foreign editor and a correspondent in Asia and Eastern Europe.