20 Years After Nortel: Should You Invest When Stocks Are at an All-Time High?

### Description

Canadians remember the stunning collapse of the country’s most valuable company, Nortel Networks. In a matter of two years, the stock plummeted from a high of $125 to a low of $.70.

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Those who bought the stock near its peak watched as the company’s sudden downfall wiped out millions of dollars in investments.

Fast forward 20 years and many stocks are trading near their all-time high; it’s been over a decade since a major market correction. Nobody wants to buy a stock when it’s at its highest price, so naturally many would-be investors are waiting on the sidelines.

However, avoiding stocks altogether creates its own risks. Any returns from cash or cash equivalents can be eaten away by inflation. Also, you might miss out on massive gains while you’re playing the waiting game.

What can you do if you’re fearful of investing in this market?

## The psychology of investing

While it’s psychologically difficult to invest if you’ve been burned by losses from a single stock or to invest in the market when stock prices are reaching new highs, here are three ways to overcome the fear.

These methods include investing for the long term, using dollar cost averaging, and investing in a diversified portfolio of high-quality stocks.

## Research shows there’s no bad time to invest

Several years ago, the Vanguard research team back-tested the performance of two hypothetical portfolios against every rolling 10-year period from January 1926 through December 2011.

This period includes many recessions, most notably the Great Depression of 1929, the dot-com bust in 2001, and the Great Recession of 2007.

Both portfolios were invested in identical assets. One portfolio was invested as a lump sum and the other used dollar cost averaging to enter the market in equal installments over a three-year period.

While the initial research was performed to highlight the differences in returns from lump-sum investing versus dollar cost averaging, subsequent studies prove that there really is no bad time to invest.

The studies indicate that in only one of the past 10 recessions, starting in 1948, a lump-sum investment would have declined over the ensuing decade.

Even when the money was invested at the worst possible time — just before a market correction –90% of the time the investment grew by an average of over 8% in the following 10-year period.

## Invest for the long term

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As the studies prove, even investors who invested at a market peak just before a recession occurred came out ahead of investors who were not invested in the market whatsoever.

Although there were short-term losses, the growth over the 10-year period following the initial investment was far superior to any results that could be achieved by sitting on the sidelines.

## Don’t try to time the market

Through dollar cost averaging, you invest equal amounts of money in the same stock in regular intervals regardless of market conditions, essentially averaging costs over time. It is often psychologically easier to invest using this approach since it ensures you buy stocks during market highs and lows.

## Diversify your holdings

Another way to conquer the fear of investing is to buy stocks in a broad range of categories. This allows you to capitalize on the cyclical nature of various businesses.

A well-diversified equity portfolio spreads your risk over multiple investment sectors, which lessens the impact of downturns on your overall stock portfolio.

In the case of Nortel, those investors who had all of their eggs in one basket faced financial ruin, while those who held diversified portfolios fared far better.

# The bottom line

Don’t let the fear of investing at the wrong time keep you from investing. Remember that in most cases even those who invested at the worst possible time had significant returns 10 years after their initial investment.

By investing for the long term, dollar cost averaging, and selecting high-quality, diversified stocks, investors will not only make money but should have no fear that they are entering the market at the wrong time.

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