TFSA Investors: Don’t Stop Doing This During a Market Correction

Description

Tax-Free Savings Account (TFSA) investors are getting nervous. The coronavirus is sending shocks throughout the global economy. An oil price war stands to upend Canada’s energy sector. While the ultimate impacts are still unknown, they could be larger than anyone anticipated.

More than ever, it’s important to review your investing habits. Better yet, review your *entire* financial life. Market downturns can quickly pick up steam, so acting early can pay big rewards.

There’s one thing in particular that you should *never* stop doing, especially during a bear market.

Do this first

The number one thing you should *never* stop doing in a market correction requires some initial steps. The following tips may sound boring, but they’re simply the best things you can do to improve your financial well-being.

The first step is to take a comprehensive accounting of your finances. What does that mean?

First tally up your liquid assets and debts. Don’t include illiquid assets like homes, cars, or collectibles. You can only service your debts with cash. Illiquid assets won’t be useful if you’re in a short-term bind. Understanding the disparity between your liquid assets and total debts is the first step to identifying your vulnerabilities.

The second step is to focus in on your upcoming liabilities.

When analyzing a company, many investors calculate something called a *quick ratio*, a measure of how well a firm can service its near-term financial liabilities. You should do the same for yourself. Total the next 12 months of financial obligations, including things like rent or mortgage obligations, food, and vehicle or debt payments.

After you understand how much you’ll be on the hook for over the coming year, compare this figure to your liquid assets. This is essentially your *personal* quick ratio.

Many people automatically factor in wage earnings. While that's a helpful exercise, it's a mistake to assume that your income levels will continue unimpeded. That's why it's important to compare just your liquid assets, not your liquid assets plus any expected income.

During the last bear market, millions of jobs were unexpectedly lost. Don't make the mistake of assuming you'll have an interrupted stream of cash to rely on.

Never stop saving

Boiling down your financial situation into a few key numbers is critical if you want to understand where you're financially vulnerable, and make sure to take action on your insights.

One of the best things you can do is to lower discretionary spending. Avoid making large purchases that lock you into a multi-year debt obligation. If you were thinking about upgrading your car or vehicle, for instance, it's best to delay the purchase. Take a fine-tooth comb to your budget, identifying areas in which spending can be reduced.

This brings us to the number one thing you should never stop doing: saving.

Lower discretionary spending means more saving. If you have high interest debt, pay that off as quickly as possible. If you lose an income source or your net worth plummets, these obligations can balloon quickly, damaging your financial life for years to come.

If you have no debt, redirect this money into regular stock purchases. This might sound crazy when markets are falling, but it's a proven method for accumulating wealth. Rather than trusting yourself, implement automatic contributions, which regularly invest a set amount of money into your TFSA. For example, you can have $200 pulled from your banking account every two weeks.

Investing when the market is dropping is difficult to do, but buying lower is all about assuming risk that others are unwilling or unable to take.

Cleaning up your financial life now will allow you this flexibility. Establishing automatic contributions today will ensure that you actually follow through.

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