If This Is Anything Like 1987, Now Is a Good Time to Buy Stocks

Description

On Friday, stocks staged a massive recovery, with the TSX rising 9.7% in the span of one trading day. Stocks remained down from their February highs, but nevertheless, the rally provided hope to many investors that markets still have some life in them. While many investors have all but resigned themselves to a protracted bear market, that needn't necessarily be the case. As you're about to see, sometimes even extreme market downturns can recover quickly. In fact, in many cases, the most extreme one-day swings are followed by the fastest recoveries. To show how that can be the case, we need look no further than the stock market crash of 1987.

It took two years for markets to recover in 1987

The stock market crash of 1987 was a legendary event. With U.S. markets crashing 22% in a single day, it was a steeper percentage decline than anything we've seen recently. Investors were spooked like never before. Yet despite how steep the crash was, stocks only took two years to recover. Looking at the S&P 500 data from 1987 to 1989, we see that the Dow peaked in August 1987 at 2700 and first topped that level in August of 1989. That's just two years for the Dow to fully recover from the worst one-day percentage drop in history!

That's not even including dividends!

Another incredible thing to note about the speedy recovery after 1987 is that the figures just mentioned don't include dividends. If you add yield into the equation, then investors recovered in much less than two years. The same is true of the crash of 1929, where dividend reinvestment shrank the time to break even from 25 years to 10 years.

Foolish takeaway

The most obvious takeaway from the stock market crash of 1987 is that a steep slide doesn't mean you shouldn't be in stocks. In fact, it could mean just the opposite. The best time to buy stocks is when they're low, and even if you don't have cash to sink into the market right now, you can profit through dividend reinvestment.

A great asset for such a strategy is the **iShares S&P/TSX 60 Index Fund** (TSX:XIU).

XIU is a relatively high-yield ETF that pays out cash income you can reinvest when markets are down.

Yielding about 3.3% right now, it pays $3,300 on every $100,000 invested. That's $3,300 you can use to accumulate more shares even if you don't have extra cash savings lying around. Over time, it can add up to a considerable return–even if stocks fall further from where they are now.

If you hold XIU now, you can rest easy knowing that you'll get dividend income through any market crash that's coming. While dividends could be reduced, you'll earn at least some income. This is in contrast to a pure capital gains fund where you can't earn any profit on long-term holdings until stock prices start to recover, which could take years.

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