2 Ways Market Timing Could Outperform Buying and Holding in 2021

Description

We are entering a new decade with hope and trepidation. There is hope that things will finally go back to normal after a crazy 2020, but there is also a budding fear that the next year might be worse than the one we've just been through. If that's the case, then a relatively mild market crash or a correction would be the least of our problems.

The number of new cases and the death toll is steadily rising over the past few weeks. The situation is even worse across the border, where thousands of patients are passing away every other day. Even with a viable vaccine, the fear of the pandemic hasn't been culled yet. People and businesses are suffering due to this fear.

The situation has affected the market in various ways. And there is a possibility that trying to time the market might be a better approach than buying and holding the stocks, especially for the next decade.

Historical data

The decade between 2010 and 2020 has been one of the best for the stock markets. We saw 10 years of steady stock price growths, and apart from sectors, like energy, that had their fair share of problems, most stocks rewarded buy-and-hold investors. But the chances are that history isn't going to repeat itself.

According to historical patterns, a reversal tendency and correlation coefficient, there is a strong possibility that the market returns in the upcoming decade will be significantly lower than the previous decade. So, buying and holding stocks and waiting for the magic of compounding might not do you as much good as it did in the last decade.

An overpriced market

According to Warren Buffett and several other experts, the stock markets were overpriced before the crash. And then, when it started a rapid recovery, it became even more overpriced, as indicated by the

Buffett Indicator, which calculates the relationship between the stock market valuation and GDP. On the TSX, several recovery stocks are aggressively overpriced, and it might not be a perfect time to buy and hold them.

The chances are that over the next few years, once the recovery sentiment wanes off, the stocks would either normalize or stay stagnant, neither of which bodes well for your returns. Instead, if you buy some of the underpriced stocks from a sector that is still suffering (and will probably experience a late recovery) and are able to time their recovery peak, you might be able to make a lot of money in a short amount of time.

One such stock might be **Killam Apartment REIT** (TSX:KMP). The real estate market hasn't fully recovered from the pandemic yet, and Killam is still trading at a price that's 25% from its pre-pandemic peak. The stock seems stagnant, but considering its history, there is a chance that it might recover and hopefully grow past its pre-pandemic valuation.

If you can time when it has reached its peak and is stabilizing, you might consider selling it, because keeping a stagnant growth stock in the portfolio (unless its offering generous dividends) is not a profitable strategy. By creating more liquidity for yourself, you can look into some other investment opportunities.

Foolish takeaway

Experts that predicted this grim future for the next decade also suggested diversifying into different asset classes. Gold might do better if the stock market is weak, so looking into some gold stocks might also be a good idea. You can also focus on the dividend side of your investment portfolio, because it is likely to stay unaffected (especially if you have strong Dividend Aristocrats in your portfolio).

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