Why I Won’t Forget the 2020 Market Crash When Buying Stocks in 2021

Description

The 2020 market crash caused a wide range of shares to experience major price declines. For example, the S&P 500 declined by a third in a matter of weeks as investors began to price in a weaker economic outlook.

Even though there has been a stock market rally since then, the crash acts as a reminder that the stock market can be hugely unpredictable and very volatile.

Therefore, buying financially-sound businesses and diversifying in 2021 could be a sound move that lowers risks during what remains a very uncertain economic situation.

The ongoing potential for a market crash

Even though the 2020 market crash occurred in a shorter amount of time than previous bear markets, it was not an unprecedented event in terms of share prices falling heavily in a matter of weeks. For example, there have been previous rapid declines in the stock market, notably in the dot com bubble and the global financial crisis.

Predicting such events is almost impossible. Therefore, they could occur at any time without any prior warning. With the economic outlook being very uncertain at the present time, there may even be a higher chance of a market decline in the coming months. While this may or may not take place, being ready for it at all times could be a means of reducing risk and capitalising on a possible recovery in its wake.

Buying financially-sound businesses

Even though most shares fell heavily in the 2020 market crash, buying financially-sound businesses could be a shrewd move. The stock market declined partly because of a weaker economic outlook caused by coronavirus. As such, it could have a larger negative impact on companies with weak balance sheets that contain large amounts of debt. They may be less able to service their debt should sales fall than a company that has lower leverage.

Of course, buying even the most financially-stable business will not make any investor immune from a stock market fall. However, it can mean their holdings have a higher chance of still being in existence to benefit from a potential market recovery as the economic outlook improves and investor sentiment strengthens.

Building a portfolio for 2021

The 2020 market crash also showed that some sectors can be worse affected than others by a downturn. For example, at the present time industries such as financial services and resources are underperforming many of their index peers due to relatively weak operating conditions.

As such, owning a variety of companies that operate in a broad range of industries could be a shrewd move. This strategy will not eliminate risk entirely. However, it could reduce overall risks during the course of 2021 and in the coming years, with the economic and stock market outlook continuing to be very unpredictable because of the ongoing pandemic.

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